



Basic Guide for Foreign Investors



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INTRODUCTION

As a result of years of hard work and efforts, Mexico has become one of the leading players in the current world economy. Today, our country is the seventh trading power in the world.

Among its various assets and riches, which include a stable economy, and a real democracy, Mexico has now nine free trade agreements, which have turned the country into a natural platform for trade and investment. Strengthened by its strategic geographic position, which creates the ideal circumstances, Mexico has a pivotal role in international trade.

World wide investors have and, in fact, are already taking advantage of the great potential that Mexico offers for accessing the worldwide market.

This guide provides a general overview of Mexico's legal framework, and its investment opportunities, for foreign companies.

Addressing the initial frequently asked questions by any potential investor, this basic outline will prove useful in dealing with the main concerns and offering a general idea of the country's advantages for foreign investment.





INVESTMENT FRAMEWORK

Over the last several years, Mexico has removed significant foreign investment barriers as part of an ambitious economic development plan that aims to achieve, and sustain, industrial development and expansion.

The government has recognized that substantial private capital is needed to create additional employment and to increase industrial output, which also results in attracting an influx of modern technology, management techniques and financing.

A. FOREIGN INVESTMENT LAW

The Foreign Investment Law establishes, as a general rule, that foreign investors may hold 100 percent of the capital stock of any Mexican corporation or partnership, except in those few areas expressly subject to limitations under the same. All investors from NAFTA and non-NAFTA countries are granted the same investment treatment in Mexico. To attract further flows of capital, changes have been accelerating to allow even greater foreign capital participation, for example, in railroad services, ports, airports, telecommunications, and certain financial services.

The following are the categories of limitations on foreign investment contained in the Foreign Investment Law.

1. Activities reserved for the State.

The constitutionally-defined “strategic activities” continuing to be reserved exclusively for the State are the following:

- a) oil production and oil refining;
- b) basic petrochemical production;
- c) sale of electricity to the public;
- d) nuclear power;
- e) telegraph and radiotelegraph services;
- f) local postal service;
- g) bill issuance and coin minting; and
- h) control, supervision and surveillance of ports, airports and heliports.

2. Activities reserved for Mexican investors.

The following activities of the Mexican economy are reserved for national investors:

- a) domestic land transportation of passengers, tourists and cargo not including passenger, or package delivery services;
- b) retail gasoline sale, and distribution of liquefied petroleum gas.
- c) radio broadcasting and television services (except cable television, where foreign participation may reach up to 49 percent);
- d) credit unions;
- e) development banks;
- f) professional and technical services expressly defined by the applicable legal provisions;
- g) international land transportation of passengers, tourists and cargo between points in Mexican territory, and services of administration of central stations for passenger and auxiliary automotive service vehicles.

Foreign investment may participate up to 51 percent in the capital stock of Mexican companies operating in these areas. Beginning January 1, 2004 foreign investment may reach up to 100 percent.

3. Activities subject to specific participation percentage.

In the following three categories, foreign investment is authorized up to 10 percent, 25 percent, and 49 percent:

- a) 10 percent in cooperative production companies;
- b) 25 percent in domestic and specialized air transportation and air shuttle services;
- c) 49 percent, which includes the following activities:
 - i) insurance and bonding institutions, currency exchange houses, general deposit warehouses, financial leasing and factoring companies, special purpose financial companies (non-bank banks), companies mentioned in Article 12-Bis of the Securities Market Law which handle security portfolios in the name of third parties, investment companies' fixed capital and companies operating investment companies;
 - ii) manufacture and commercialization of explosives, firearms, cartridges, munitions and fireworks, excluding their acquisition and use for industrial or extractive activities, or the production of explosive mixtures for use in these activities;
 - iii) printing and publication of newspapers for circulation exclusively in Mexico;
 - iv) ownership of series "T" shares of companies that own agricultural, cattle-raising or timber land;

v) cable television, basic telephone services;

vi) fishing in fresh water, along the coast and in the exclusive economic zone, except aquaculture;

vii) integral port administration, piloting port services for interior navigation operations, shipping companies commercially using vessels for interior and coastal navigation, except for tourist cruise ships and for use of dredges and naval devices for port construction, conservation and operation;

viii) supply of fuel and lubricants for ships, aircraft and railway equipment; and

4. Majority interest upon approval.

Subject to approval of the Foreign Investment Commission, foreign investors may hold greater than a 49 percent interest in the following activities:

a) port services such as piloting, dock services, mooring and lighterage;

b) naval companies using vessels exclusively for high-seas traffic;

c) administration of air terminals;

d) private educational services;

e) legal services;

f) credit information companies;

g) institutions for categorization of securities;

h) insurance agencies;

i) cellular telephone services;

j) oil and gas well drilling;

5. Acquisition of existing Mexican companies.

Foreign investors may acquire up to 100 percent of the shares of any company unless one of the limitations previously mentioned applies to such company, requiring only registration with the Foreign Investment Commission. However, a resolution from the Foreign Investment Commission is required when foreign investors wish to acquire more than 49 percent of the capital stock of existing Mexican companies when the total value of the assets of the Mexican company is greater than \$712 million pesos (approximately US\$75 million).

6. Real estate.

Foreign participation in a Mexican company owning real estate within the restricted zone (100 kilometers wide from the borders and 50 kilometers wide from the coastal shores) for non-residential purposes is permitted, requiring only a notification to the Ministry of Foreign Affairs. If for residential purposes, title of the real estate must be held through a trust by a trustee which must be a Mexican bank. Approval of the Ministry of Foreign Affairs is required.

7. Neutral investment.

Neutral investment is a mechanism that allows foreigners to hold greater percentages of the capital of Mexican companies in restricted areas. Such investment may be done either through Mexican companies or in authorized trusts.

- a) The Ministry of Economy may authorize companies to issue special series of shares with limited or no voting rights.
- b) Banks acting as trustees may be authorized by the Ministry of Economy to issue instruments of neutral investment granting holders economic and limited voting rights, with the restriction that no voting rights may be granted for ordinary shareholders or partners meetings.
- c) The Foreign Investment Commission may authorize neutral investment in the capital stock of Mexican companies by international development financial companies.

B. PRIVATIZATION

Since 1982, the Mexican government started a privatization process of government-owned enterprises, as part of the policy to liberalize the economy. More than 1,150 government-owned enterprises - of what once were approximately 1,400 - have been privatized, contributing more than US\$24 billion to the federal treasury.

Many government-owned enterprises have been privatized, including hotels, airlines, all of the banks, the telephone company (TELMEX), mining (Minera Cananea), TV channels (TV Azteca), theaters, sugar mills, fishing companies, automobile assembly, steel companies, and other companies covering a wide range of activities.

Depending on the specific characteristics of the government-owned company in process of being privatized, special rules in the bidding process are applied. Each privatization requires the approval of the Intersecretarial Committee on Privatization, with the participation of the president of the Competition Commission.

Additional areas for privatization are ports, petrochemical plants, highways, airports, telecommunication services, railroads, among others.

Outsourcing part or all of the activities of the entity without changing its ownership is another form of privatization (sometimes referred to as "indirect privatization"), without the necessity of direct ownership of the outsourcing company.

Privatization in this form opens a whole new vast area of business opportunities to national and foreign enterprises. Such contracting may be for operations to be performed separately from the facilities of the government-owned entity or actually within the facility, i.e., maintenance contracts, statistical processing, management of production, and operating computer systems.



II INVESTMENT OPPORTUNITIES

As previously mentioned, Mexico's government has entered into a process of economic modernization by adopting unprecedented actions to reduce governmental intervention in the economy and open the country to international competition, even in previously sensitive areas.

These objectives have been pursued through an intensive deregulation program directed towards promoting legal and administrative procedures favorable to private investment, national or foreign.

New dispositions have been issued in the following areas:

A. ENERGY

1. Petrochemicals and natural gas.

On December 31, 1995, the Energy Regulatory Commission Law was enacted and provides for the creation of the Energy Regulatory Commission (CRE) which has acquired the authority to act on behalf of the Ministry of Energy with regard to electric power and natural gas services.

The Law Regulating Article 27 of the Mexican Constitution referring to petroleum, reserves to the Mexican State the investment and rendering of services related to the "oil industry".

Since 1995, the transportation, storage and distribution of natural gas was opened to the private sector, including foreign participation, subject to prior authorization of the CRE. Foreign investors are entitled to construct, operate and own pipelines, installations and equipment for such purpose. Authorizations can be assigned upon prior approval from the CRE.

First-hand sales, as well as activities that do not form part of the petroleum industry regarding natural gas, are regulated. Additionally, they establish the terms and conditions of the permits granted for transportation, storage and distribution of natural gas. Since 1997, several permits for distribution of natural gas in different geographic zones have been granted through public bids, conferring an exclusivity period of 12 years for the construction of the distribution system and the receipt, transmission and wholesale delivery of gas within the zone.

As per the Foreign Investment Law, the drilling of oil and natural gas wells is still subject to the 49 percent limitation on foreign ownership, unless authorization is obtained to exceed such limit.

Regarding the petrochemical industry, foreign participation may own up to 100 percent of a company engaged in secondary petrochemical activities, requiring Mexican control and a permit from the Petrochemical Commission. The list of secondary petrochemical products includes production of the following: acetylene, ammonia, benzene, butadiene, butylene, ethylene, methanol, n-paraffins, orto-xylene, para-xylene, propylene, and toluene.

2. The electric power sector.

Articles 27 and 28 of the Mexican Constitution contain provisions reserving to the Mexican State the supply of electricity as a “public service,” which is considered a strategic activity. However, in 1992, the term “public service” was redefined to open the following areas for private investment up to 100 percent.

- a) self generation; when companies acquire, establish or operate an electricity generating facility to satisfy their own needs. Any excess production must be sold to the Federal Electricity Commission (CFE);
- b) co-generation; electricity generated associated with industrial processes using heat, steam or other energy sources. Owners of the industrial facility need not be the owners of the co-generating facility. Once again, any excess production must be sold to the CFE;

- c) independent power production is an enterprise that generates over 30 megawatts for sale to the CFE;
- d) export of electric power, derived from co-generation, independent production or small production (note that the CFE must be part of the contract negotiations);
- e) importation of electric power, by individuals or companies, exclusively to supply their own needs;
- f) production of electric power for emergency use arising from the interruption of the public service of electric power as required by the CFE; and
- g) small production; generation of electricity of less than 30 megawatts.

All of the above activities require a permit issued by the CRE based on prior opinion of CFE. The permits run for an indefinite period, except those for independent production, which run for 30 years, with a possibility of multiple extensions.

At the end of 1996, the CFE announced that it would not participate in the construction of electricity generating plants, thus opening the door for foreign and national investment in this area. In fact, some electric plants of the CFE have already been privatized.

3. Water resources.

Private parties are entitled to obtain a concession for the utilization of national water. The National Water Commission (CNA) is empowered under the Law to grant concessions for a period no less than five years and no more than 50 years. Concessions may

be renewed for the same period that the concession was granted. The renewal must be filed with the CNA within the last five years of the concession.

B. TRANSPORTATION

1. Maritime activities.

Since 1994, navigation operations are considerably open to foreign companies. Mexican shipping companies may be 100 percent foreign owned, and may register in the National Maritime Public Registry and flag as Mexican, vessels owned by them or in their legal possession under any bare boat charter agreement with option to purchase. Foreigners may flag, record and register tourist or sport vessels for private use under Mexican nationality.

However, masters, pilots, engine room and deck hands and all personnel on board on any Mexican flag vessel must be Mexican by birth. Fishing vessel personnel who carry out the following duties may be Mexican or foreign: instruction, training and supervision of activities related to the capture, handling or processing of game fish, and tourist cruise ship personnel who carry out the duties of attending to tourists.

The general shipping agent is the person or company acting on behalf of shipping companies or operators as agent or business representative to represent his principal in the bills of lading, and to perform other business his principal may request. A shipping agent company may be 100 percent foreign owned.

a. Navigation regime.

Operation on inland waterways is

reserved to Mexican shipping companies with Mexican vessels. However, Mexican shipping companies may obtain a temporary permit from the Ministry of Communications to operate or manage foreign vessels on inland waterways, or in case no Mexican shipping companies are interested, foreign shipping companies may obtain such a permit.

Either Mexican or foreign shipping companies may navigate in coastal waters provided a permit from the Mexican Ministry of Transportation is obtained. The permit is subject to reciprocity and equal conditions with the country in which the vessel is registered and with the country where the shipping company has its corporate domicile.

Also, the operation and management in Mexican territorial inland and coastal waters of tourist cruise ships as well as dredges and naval equipment for port construction, conservation and operation may be carried out by foreign or Mexican shipping companies with foreign or Mexican vessels or naval equipment.

C. INFRASTRUCTURE

1. Railroads.

Foreign investment may participate in up to 49 percent of the capital of Mexican companies engaged in the following railroad activities, with the possibility of 100 percent foreign participation subject to approval from the Foreign Investment Commission.

The Ministry of Communications may grant concessions for the following activities:

- i) construction, management and operation of railways that are considered common thoroughfares;
- ii) the providing of public rail service, which encompasses both passenger and freight traffic; Permits may be granted for the rendering of auxiliary services, which are defined as passenger or freight terminals, the transshipment or transfer of liquids, repair shops for railroad equipment and the supply centers for the operation of the equipment.

2. Airports

Foreign investment up to 49% is permitted in the capital stock of Mexican companies involved in the administration, operation, exploitation and construction of air terminals; however, the Foreign Investment Commission may authorize foreign ownership in excess of this amount.

Concessions for airports are generally granted by the Ministry of Communications, through public bid, while permits for the supply of general services to air terminals can be requested by a Mexican company through direct application to the Ministry of Communications.

3. Ports.

The Ministry of Communications is empowered under the Law to grant concessions or permits for the exploitation, use and beneficial utilization of property within the federal public domain, defined as the lands and water which are part of the harbor enclosure and the works and facilities acquired or constructed by the Federal government when located within harbor enclosures.

Concessions are granted for integral port administration and the construction, operation and exploitation of terminals, marinas and port facilities. Permits are granted for the rendering of port services which are defined as those services rendered at ports, terminals, marinas and port facilities to serve vessels, as well as those rendered in the transfer of people and goods between ships, to land, or to other means of transportation.

In addition, a permit is also required to build piers, wharves, launching docks and other similar facilities on the general waterways outside of ports, terminals and marinas.

Foreign investment is restricted to 49% regarding integral port administration and piloting services related to internal navigation.

In companies providing port services such as piloting, dock services, mooring and lighterage, foreign participation may obtain more than 49 percent ownership in Mexican companies, prior authorization from the Foreign Investment Commission. Several bids have already been published and concessions and permits granted, among others, Manzanillo, Altamira, Tampico and Veracruz.

4. Tourism.

a) Tourism Law.

In 1993, a new federal Tourism Law was enacted to define a legal framework for providers of tourism services, providing for the coordination of activities of the federal government, state governments and municipalities to avoid duplication of procedures.

The new law repealed existing regulations and focuses mainly on guaranteeing the physical security of tourists, respecting terms of reservations and of contracts

executed between the provider of tourism services and the client.

Foreign investment may participate without limits or restrictions in the following tourism services: hotels, motels, parks for camping and recreational vehicles, travel agencies, tour operators, tourist guides, restaurants, cafeterias, bars, tourism exchange service companies, scuba organizers, car rental, ports and marinas.

b) Casino gaming.

On June 19, 2002, a bill to authorize the construction and operation of Casinos in Mexico was concluded. After years of unsuccessful attempts to pass legislation to allow casinos, this new bill, which is being debated in Congress, is very likely to become the long awaited law. There are estimates that just one casino permitted to operate in Mexico could generate more than 35 million dollars annually in salaries, while 10 casinos could generate 800 million dollars in taxes, per year, for the Federal Government. Consequently, the idea is very attractive to many people.

In order to guarantee the legality of the casinos, as well as of the owners of the same, the current bill before Congress provides for five requirements to be met, in order to be able to get a permit to construct and operate a casino:

1. Only Mexican companies may request the permit. (Foreign investment is permitted).
2. All the required state and local authorizations must be obtained.
3. The origin of the money to be invested must be specified.

4. Economic solvency must be accredited, through a report issued by a qualified auditor, expressly authorized for this purpose.

5. Title of ownership or possession of the property where the casino will be built must be presented. Some areas considered likely for casino development would include Mexico City, Guadalajara, Acapulco, Cancún, Puerto Vallarta, Mazatlán, Manzanillo, and the Cabos region of Southern Baja California.

5. Construction.

a) Social interest housing.

Government-backed credits are available for the purchase of low-income housing. Both Mexican and foreign construction firms may apply to government agencies for approval of their housing construction projects for the credit. The credit does not finance the construction, but rather covers the resale of individual low-income residential units to the public, helping the developers sell the completed project more quickly.

b) Public works.

The Mexican government is focusing on promoting extensive participation of foreign and domestic private investment in infrastructure because of the limited resources of the public sector.

Public works projects are awarded through a public bid process, which may be national or international. The law regulating the bid process is the Law of Acquisitions and Public Works, which guarantees the transparency of the same. Calls for bids for different projects can be obtained on the internet through the Compranet system at <http://www.compranet.gob.mx>.

c) Industrial facilities.

There are investment opportunities in both building industrial development parks and in locating plants within them. Industrial parks, usually oriented toward small and medium-size industry, have optimal conditions of location, infrastructure and services and, therefore, are considered the best option for establishing an industrial plant.

D. NATURAL RESOURCES

1. Mining.

Concessions for the exploration and/or exploitation of minerals and substances listed in the Mexican Mining Law, may be granted by the Ministry of Commerce to Mexican individuals, Mexican companies and agrarian communities. Foreign investment may now participate up to 100 percent in the capital stock of mining companies.

2. Fisheries.

Foreign investment may participate up to 49 percent in Mexican companies engaged in fishing activities, which may apply for a concession or a permit in this area.

Foreigners may invest in Mexican companies engaged in aquaculture, up to 100 percent. Aquaculture consists of the cultivation of water species by using methods and techniques for their controlled development.

Foreigners may request permits to conduct scientific expeditions and explorations.

3. Agriculture and Agribusiness.

Since 1992, a new Agrarian Law enables domestic companies and peasants to buy, sell or rent land, to hire labor or to associate with

other producers and with third parties, including joint-venture schemes, with domestic or foreign private investors.

Any Mexican company may own land for agrarian, livestock or forestry purposes with a maximum extension of land equivalent to 25 times the limits of the individual landholdings.

Companies investing in land for agrarian, livestock or forestry purposes must issue a special series of shares or partnership interests, identified with letter "T" which represent the capital invested in the acquisition of land or the value of the land contributed. Foreign individuals or companies may not acquire more than 49 percent of series "T" shares or partnership interests.

Projects to raise animals, or for the production of cereals, fruits, vegetables and other agricultural products have been successful, with growing export opportunities.

E. TELECOMMUNICATIONS

The use of radio frequencies and the installation, operation or exploitation of public telecommunication networks may be carried out through concessions, which will be granted by a public call for bids for radio frequencies, and through direct application to the Ministry of Communication, for public telecommunication networks.

The aforesaid concessions shall be granted to Mexican individuals or corporations, which may have up to 49 percent of foreign investment.

Prior authorization from the Foreign Investment Commission, foreign ownership in excess of 49 percent is permitted for cellular telephone services.

The operation as a "reseller" of telecommunication services, without being a public telecommunication network, and the rendering of value-added services allow foreign investment up to 100 percent.

F. AUTOMOTIVE INDUSTRY

The Mexican automotive industry is comprised of final assembly plants and auto parts manufacturers, neither of which has any restriction regarding foreign investment.

Final assembly plants are defined as companies that manufacture vehicles or carry out the final assembly thereof, subject to compliance with certain national value-added content requirements, which are gradually reduced down to 29 percent in the year 2003.

Auto parts manufacturers are companies with sales to final assembly plants of components and parts for use as original equipment in excess of 60 percent of their total sales, which must include at least 20 percent of national value-added content.

Auto parts manufacturers with sales to final assembly plants, lower than 60 percent of their total sales, have no requirement for national content.

G. ENVIRONMENTAL EQUIPMENT AND SERVICES

With the current environmental legal framework, in most cases comparable with those of the developed countries, Mexico is increasing enforcement of the laws. Under this scenario, environmental compliance has become an important issue for industries searching for improved and expanded environmental services and equipment.

Major priorities for investment in environmental equipment and services are hazardous and non-hazardous waste collection and disposal, and water treatment and supply activities, in which foreign investment is permitted. The Law requiring adequate disposal and treatment of hazardous waste creates opportunities for companies investing in commercial recycling plants, confinement facilities, waste stabilization and treatment facilities and incinerators.

Another important area for development of environmental services are the needs of large

government-owned companies, such as PEMEX, the Mexican National Railway and power generating plants, where opportunities will be increased with the current privatization process.

Increasingly stronger regulation and enforcement require companies to update their pollution control procedures, in turn increasing the demand for products and services, such as equipment designed to reduce human error with the accompanying technical support, equipment designed to reduce the production of sludge, advanced monitors and instruments to measure pollution output, service programs developed to provide companies with waste management plans and engineering services to assist in the construction of waste treatment plants.

Important opportunities also for environmental services are the performance of environmental impact studies, equipment for air pollution control, disposal of state and municipal solid waste, and finally in alternative energy sources such as geothermic, solar and wind power.

H. ELECTRONIC COMMERCE

1. General.

One of the most dynamic areas in business today involves the use of computers and the internet for conducting commercial transactions. The growth in electronic commerce, or e-commerce, has been astounding over the past few years. Technological advances, development of more user-friendly applications and the ever-increasing popularity of this means of communication make the idea of an almost-paperless future more plausible all the time. Opportunities for using electronic means to facilitate communication and business transactions in Mexico are immense.

In Mexico, as in the rest of the world, the number of computers connected to the Internet and the number of internet service providers

have grown very fast, and the demand is expected to continue to grow at a rapid rate for the foreseeable future.

Opportunities abound in the areas of telecommunications, internet access and related areas, as well as in the use of electronic commerce as a marketing and sales tool for other types of businesses.

Multinational companies, as well as many of Mexico's largest companies, are energetically positioning themselves in the Mexican e-commerce market. In general, however, most Mexican companies have been slow to appreciate the importance of electronic commerce and somewhat reticent to embrace new business strategies necessary for success in an electronic era.

The direct sale of products from the web is done through local, national and international delivery services, which operate throughout the country.

Electronic commerce and advances in computer technology promise to change the way business is done throughout the world. As a natural consequence, legal concepts worldwide also must adapt to the needs of societies in the midst of an electronic revolution.

2. Intellectual property.

The use of trademarks on websites creates other issues that the Mexican Patent and Trademark Office (known by its Spanish acronym, IMPI) is grappling with. Under Mexican law, trademark protection can be cancelled if the trademark is not used.

Because webpages are not currently contemplated in law or regulations, the IMPI is using internal criteria on a case-by-case basis to determine whether website use of a trademark constitutes sufficient use of the mark under the law.

Similarly, the IMPI is using internal criteria also to determine trademark infringement in cases

of unauthorized use of a trademark on a webpage.

Copyright protection for electronic documents is covered by the Mexican Copyright Law.

In addition, the internet is creating new opportunities for the unauthorized use or pirating of software, music and other products dependent intellectual property rights.

Addressing this issue will require both technological and legal advances.

I. INSURANCE

Under the terms of NAFTA, barriers to ownership of Mexican insurance companies by NAFTA investors have been lifted. Now U.S. and Canadian investors may own 100 percent of a Mexican insurance company. Some of the world's largest insurance companies are entering the Mexican market, both by forming their own Mexican insurance company as well as through significant acquisitions and joint ventures with Mexican insurers. Setting up a subsidiary of a foreign insurance company, however, is still subject to foreign ownership restrictions, unless Treaty's provisions provide otherwise.

J. MEDICAL SERVICES

At present, Mexico City has two hospitals of first world caliber, which are operating at or near capacity. This might indicate that there are now opportunities for foreign investment in the full service hospital and medical center field. In addition, clinics in the respiratory disease field, are needed.

In the rest of the country, hospital services vary greatly. Guadalajara, Monterrey and Cuernavaca have fairly good facilities, but many other cities need good medium-sized hospitals and clinics.

J. OUTSOURCING

Outsourcing has become a dynamic business opportunity around the world. The concept is growing in Mexico for various types of services.



GOVERNMENT SALES AND CONTRACTING

Mexico has implanted strong legislation regarding the acquisitions and public works, by governmental entities, as well as the purchase or lease of personal property and the rendering of services by the same. Several laws specify the internal procedure that must be followed in the planning and programming of the corresponding purchase or work, contracting procedures, information and verification requirements, violations and penalties and dispute resolution procedures.

Government entities and dependencies may make acquisitions, enter into lease agreements, contract for services and carry out public works by virtue of: (i) public bidding, (ii) limited invitation, or (iii) direct awarding of such contracts.

A. GRANTING OF CONTRACTS

As a general rule contracts are awarded after a public bidding process. The invitation to bid is published in the Official Daily Gazette, among other publications.

Simultaneously, the bids can be acquired through the Compranet system at <http://www.compranet.gob.mx>. The bid contains the specifics of the purchase or project and the related requirements.

The laws also permit government dependencies and entities, at their discretion, to conduct restricted bidding, in which case invitations must be extended to at least three prospective suppliers or contractors.

If the entity or dependency concludes that restricted bidding is not suitable, it may opt to award the contract directly.

B. FOREIGN PARTICIPATION

The laws also distinguish between national and international bidding. An international bidding process may be carried out only in the following cases:

1. when required by treaty;
2. when the relevant entity or dependency determines, after a market investigation, that the quantity or quality of national suppliers is not adequate or that national contractors do not have the capacity to perform the work contemplated;
3. when national bidding fails to award a contract because no bids were tendered or the bids did not meet minimum requirements; or
4. when required as a condition for the granting of foreign credits to the federal government or its guarantor.

C. CHALLENGING PROCEDURES

Any interested party may present a claim before the Controller's Department for acts contrary to the laws committed by a public entity in the process of acquiring a public contract or granting a bid. Most often, claims are presented against the decision regarding the winner of a bid. At its discretion, the Comptroller's Department may begin an investigation even if there have been no claims regarding a particular bid or contract.

It must be noted that severe penalties may be imposed to government officials and private parties who participate in acts contrary to the applicable laws.



IV REPRESENTATIVES, DISTRIBUTORS, FRANCHISEES

A. REPRESENTATIVES

A foreign vendor can sell goods or services in Mexico directly through its own employees. In other cases, a vendor may decide for various reasons to use other methods to dispose of his merchandise, either through representatives or intermediaries, who may be commission agents, distributors or franchisees.

When dealing through a commission agent, the vendor should be careful to have the agent considered an independent contractor, and not an employee.

Mexican laws do not regulate the amount to be paid as commission. For tax purposes the agent's commission will be considered as his normal income. The sale by the foreign vendor could be subject to Mexican taxes.

B. DISTRIBUTORS

Distributors are independent vendors who purchase on their own and resell products, also for their own account.

Distributors, unlike commission agents, derive their income from the difference in the wholesale price at which they purchase, and the retail price at which they sell.

Income of commission agents is the commission received, which usually is fixed as a percentage of sales.

C. FRANCHISEES

Franchise agreements imply the licensing of a trademark, and as such, must be recorded before the Mexican Institute of Industrial Property to gain protection of the trademarks against third parties.

The parties to a franchise agreement enjoy full contractual freedom. Their respective obligations include, among others, the granting of a trademark license and technical assistance, protection of confidential information, compliance with quality and operational standards, payment of royalties, and access to the franchisor's system of operations.

Franchise agreements are not subject to governmental approval. In accordance with the Intellectual Property Law, franchisors must deliver to potential franchisees before execution of the franchise agreement, the technical, economic and financial information regarding the franchise and its system.

D. CONSIDERATIONS

Representatives, distributors and franchisees are subject to the Competition Law.

It is important to avoid agreements to unfairly eliminate competitors from the market.

The agreements governing the above relationships may be terminated by either party, in accordance with their terms. Mexican law does not contain specific provisions for the payment of damages or remuneration upon termination of the agreement except as may be provided in the agreement.



DIRECT INVESTMENT

Mexican and foreign investors, both private and public, may invest in Mexico through different vehicles. Tax advantages, relationships with the parent company, need of technical assistance and technology, availability of deductions, projected business and financial plan including growth expectations, as well as limitation of liability and other similar factors, must be taken into consideration, before choosing an appropriate vehicle or structure.

1. Purchase of stock or assets. The purchase stock or assets of an existing company, enables the entry into the Mexican market immediately, taking advantage of the existing operation and its infrastructure.
2. Registration of a branch. The opening of a branch of the parent company to simplify communication and accounting and consolidate advantages between the branch and the parent company.
3. Registration of a representative office. When acting as intermediaries or engaging in promotion or similar activities in Mexico, from which no income is obtained, foreign investors may may decide to register a representative office without income.
4. Creation of a subsidiary. Due to multiple commercial and legal reasons and advantages, foreign investors may prefer to incorporate a new company in Mexico, enabling them to limit their liability, as the activities of the subsidiary are legally independent from those of the parent company.
5. Joint venture companies and agreements. Foreign investors may enter into a business together with other persons or companies, through a joint venture company or a joint venture agreement.

a) “Joint venture company.”

The incorporation of a joint venture company basically takes advantage of the partners' knowledge of the Mexican business and industrial sectors, and joins efforts by bringing capital, technical assistance and technology together.

b) “Joint venture agreement” (Asociación en Participación).

The parties to a project may prefer to execute an agreement of “Asociación en Participación” by which they agree to join efforts for a specific purpose, which agreement terminates upon completion of the work or the desired objective. A new entity is not created and each of the parties is liable to the other, without liability limits, as per undertakings in the contract.



SETTING UP A COMPANY IN MEXICO

A. TYPES OF MEXICAN COMPANIES.

The vehicles for foreign and national investments in Mexico are stock corporations, of which the most common is the Sociedad Anónima (S.A.). The S.A. may have fixed or variable capital, in which case the acronym “S.A.” becomes “S.A. de C.V.”

Any legal entity may adopt the variable capital form, and may increase and decrease its capital after incorporation pursuant to the conditions provided for in the charter and the law.

In most companies the minimum capital is fixed by law, and generally, the variable capital is unlimited. Companies may increase the capital to be subscribed by the shareholders or partners, which shall be paid in the time periods provided for in the charter or in the law.

The Companies Law provides for several types of corporations. However, this Guide refers only to the two most common companies, which are used for doing business in Mexico. These are the “sociedad anónima” and the “sociedad de responsabilidad limitada”, which is now used mostly by some US investors, as explained below.

1. “Sociedad anónima.”

The minimum number of shareholders required is two, with no maximum limit.

The S.A. provides limited liability to its shareholders. A sole administrator or board of directors may manage the corporation.

The shareholders are the ultimate decision-making body of the corporation. Shareholders may call ordinary or extraordinary meetings, in certain cases under the law or as provided in the charter.

Foreigners, residents or non-residents, may be members of the board of directors.

The minimum capitalization for the S.A. is \$50,000 pesos (approximately US\$5,000 at \$10 pesos per dollar). The initial capital must be at least 20 percent subscribed and paid-in, the remainder to be paid as provided by the shareholders or decided by the board of directors.

All shares must be registered since bearer shares are no longer permitted.

2. “Sociedad de responsabilidad limitada.”

A “Sociedad de responsabilidad limitada” (S.R.L.) is similar to a limited liability company. This company may be incorporated with a minimum capital of \$3,000 pesos, and is limited to a number of fifty partners.

The partners’ liability is limited to the amount of their contribution. This type of company is oriented toward the personal capacities of its partners. Therefore, to assign or transfer partnership interests as well as to admit new partners, the consent of partners representing the majority of the capital is necessary, except when the charter provides for a higher percentage.

Since the S.R.L. appears to be similar to limited liability partnerships in the United States (L.L.C.); some observers comment that they may be considered partnerships for U.S. tax purposes.

B. INCORPORATION AND REGISTRATION REQUIREMENTS.

To incorporate a company, the shareholders have to agree on a proposed charter and by-laws and must request prior authorization from the Ministry of Foreign Affairs for the use of the proposed corporate name. These documents must be notarized by a Public Notary.

The public instrument issued by the Notary shall be registered at the Public Registry of Commerce of the domicile of the company.

A company with any percentage of foreign stock ownership must be registered before the National Registry of Foreign Investment.

Registration before the Taxpayers’ Registry, in order to obtain a taxpayer’s number is imperative. The company may not carry out any operations before this.

Other registrations with federal or local agencies is required, in accordance with the activities that will be carried out by the company.

VII LABOR

The Federal Labor Law of 1970 governs all aspects of the employer-employee relationship, including collective bargaining, the right to strike, minimum wage rates, work hours, compensation, and occupational health and safety.

Any person rendering services to another individual or entity is considered an employee if that person works under the supervision of, or is subordinate to, the contracting individual or entity. Care must be exercised in drafting service agreements in which the intent is not to form an employment relationship.

In the acquisition of an on-going business, the purchaser becomes a substitute employer for the seller, and acquires all the seller's labor obligations. The purchaser and seller remain jointly liable for labor obligations for six months after acknowledgment by employees of the notice of the transfer.

A. UNIONS

The Law provides that groups of 20 or more employees, irrespective of whether or not they are employees of the same company, may form a labor union. If a company has fewer than 20 employees, its employees may affiliate with another union and request that the company enter into collective bargaining. The largest and most influential labor union in Mexico is the Confederation of Mexican Workers (CTM).

Strikes are recognized and protected by law as a tool available to workers for obtaining improved benefits and working conditions.

Although the labor authorities may only resolve the legality of a strike once started, as a matter of practice, they may intervene in labor disputes in order to avoid work stoppages.

B. GENERAL LABOR REGULATIONS

1. Individual employment contracts

It is mandatory for employers to execute individual employment agreements in writing. Contracts are usually entered into for an indefinite term; hiring for a definite term for a specific project is permitted provided that the nature of the job is truly temporary.

2. Wages.

The government is not empowered to mandate salary increases, with the exception of the minimum wage.

3. Working hours.

Under the Federal Labor Law, the working hours per week range from forty-two to forty-eight, depending on the type of work shift: day, night or mixed. Overtime is permitted by the law.

4. Rest days.

Workers shall enjoy one fully paid day of rest for each six days of work.

Saturday working hours may be spread on the other weekly working days.

5. Termination of employment contracts.

Employees may only be dismissed, without liability for the employer, for a number of limited justifiable causes provided for in the Law.

In cases of unjustified dismissal employees are entitled to demand either reinstatement or payment of an indemnity equal to three months' salary plus 20 days' salary per year of service, seniority premium, back pay and the outstanding balance of any earned and unpaid benefits.

In the case of employees with less than one year's seniority; confidential employees, temporary employees, and employees having direct and permanent contact with the employer, prior approval of the Labor Board, the employer may refuse reinstatement, by paying to the employee an indemnity equal to twenty days' salary per year of services, in addition to the three months' salary severance indemnity.

Employees may voluntarily resign their job at any time without any liability on their part and without any obligation to give prior notice to the employer. In such case, the employee is entitled only to payment of the outstanding balance of any earned and unpaid benefits. Exclusively in the case of employment for more than 15 years, the employee must receive payment of a seniority premium,

6. Benefits.

Fringe benefits are high in relation to total payroll costs. Employee benefits are compulsory under the Labor Law. The most significant fringe benefits are the following:

- a) Paid vacations. After one year of employment, an employee is entitled to a paid vacation of six working days, increasing by two days

for each of the next three years of service. Thereafter, the vacation period increases by two days for every additional five years of service. Workers are entitled to a vacation premium in addition to their vacation days' salaries in an amount equal to 25 percent of their daily wages.

- b) Christmas bonus. Employees are entitled to an annual bonus of not less than 15 days' salary payable on or before December 20.
- c) Housing fund. Employers must contribute 5 percent of payroll to the National Workers' Housing Fund Institute. The housing contribution and the social security payments into pension and retirement funds are part of the Retirement Savings Plan, as mentioned below.
- d) Profit sharing. Profit sharing is compulsory for all businesses, regardless of size or organizational structure. Employees are entitled to receive an amount equal to 10 percent of the taxable income as calculated for income tax purposes under the terms of the Income Tax Law. In businesses whose income is derived exclusively from personal services, the amount of profit share is capped at one month's salary. Distribution of profit-sharing must be made no later than May 30 of the following year.

7. Social Security.

All employers must register, together with their employees, before Social Security agency known as IMSS (its acronym in Spanish).

Social Security dues are paid by both the employer and the employee (via withholding) every month, based on the daily salary of the employees. Social Security benefits cover job-related risks; general illnesses and maternity; disability and life; retirement, old age and unemployment at an advanced age; children's nurseries and social benefits, like the retirement savings fund. Overall, the social security costs that the employer must pay for each employee, ranges from 17 to 21 percent of the salary. The cost for the employee ranges from 3 to 4 percent.



VIII THE TAX SYSTEM

A. INCOME TAX

The Income Tax Law is amended annually, during the month of January. As such, this guide intends to provide only a general overview of the Mexican fiscal system.

1. Residency.

The federal income tax is the most important tax in Mexico as it still produces the highest portion of the total tax collected.

The two criteria crucial to the imposition of the tax to individuals and corporations are residency and source of income.

- a) Mexican residents are taxed on all income, from whatever source.
- b) Foreign residents, with a permanent establishment in Mexico, are taxed on the income attributable to such permanent establishment.
- c) Foreign residents with no permanent establishment are taxed on income attributable to Mexican sources.

For tax purposes, the Law defines “resident” as follows:

- a) Individuals are considered to be residents of Mexico when establishing their dwelling place therein, except if they are in another country for more than 183 days during the calendar year, consecutive or non-consecutive, and demonstrate acquiring residence for tax purposes in that country.
- b) Companies are considered to be residents of Mexico when the place of incorporation of the company is in Mexico or when they have in Mexico their main management or business decisions center.

2. Resident Mexican Companies.

a) Object of taxation.

Mexican resident companies are subject to tax on all income received in cash, in kind, in services, in credit or in any other form obtained during the fiscal year

b) Taxable base.

The amount subject to tax, the “taxable result,” is determined by subtracting the legally-authorized deductions and losses carried over from prior fiscal years, from income for the given fiscal year.

c) Fiscal year.

The federal income tax must be calculated and paid each fiscal year, which must coincide with the calendar year. However, taxpayers must still make provisional monthly payments.

d) Rate of tax.

During 2002, the applicable tax rate, on all taxable income of Mexican corporations, is 35 percent. Such rate will be annually reduced by one percentage point, from 2003, until 2005, when the same will be fixed at 32 percent.

The Law provides that certain Mexican companies will pay a reduced rate of tax if engaged in activities in specific sectors. There is a 50 percent reduction of the tax if the taxpayer exclusively engages in farming, ranching, fishing or forestry activities.

e) Authorized deductions.

Provided the fulfillment of all the legal requirements, all expenses and investments that are indispensable for the development of the business activity of the taxpayer are deductible. Deductions include the purchase of inventory.

f) Dividends.

The Law establishes that companies distributing dividends or profits must calculate and pay a tax of 35 percent on the result derived from multiplying said dividends by a factor of 1.5385. Such rate and factor will be annually reduced from 2003, until 2005.

Not all dividend payments trigger a corporate tax. Any distribution made from the net tax profit account is exempt from the above-stated tax liability unless such distribution is made from the net tax reinvested profit account, in which case the deferred corporate tax must be paid applying the 5 percent on the distributed profit.

g) Investments in low-tax jurisdictions.

The list of low-tax jurisdictions under the Law includes more than 90 low-tax offshore jurisdictions. Investments by Mexican taxpayers in these jurisdictions are those made directly or indirectly in branches, legal entities, real estate, shares, bank or investment accounts, and any form of participation in trusts, partnerships, investment funds, as well as any similar legal structure created or constituted pursuant to foreign law located in said jurisdictions, including those made through third parties.

Amounts received from an investment located in a tax haven are deemed to be income, profits or dividends, unless proved otherwise, and shall be deemed to be received at the time the same are accrued.

h) Transfer Pricing.

Tax authorities have the power to impose transfer pricing rules on parties the Law defines as “related.” Parties are considered to be related in the following two general cases: if one party participates, either directly or indirectly, in the management or administration of another party or if the former holds capital stock in or controls in any way the latter, and if one party or a group of parties participates, either directly or indirectly, in the management,

administration or capital of the other parties.

There is a rebuttable presumption that operations carried out between Mexican residents and companies or other entities that are residents of or located in low-tax jurisdictions are operations carried out between related parties and that the agreed upon consideration is an amount not in line with the consideration that would have been agreed upon by independent parties.

Tax authorities may consider interest payments to be a dividend if they are paid from one related party to another and if they represent payments for interest that exceeds the market rate. Interest payments related to back to back loans among related parties also may be considered dividends.

3. Taxation of foreign companies and individuals.

Non-resident companies or individuals, without a permanent establishment or fixed base in Mexico, are liable for tax on any income that falls within the definition of Mexican-source income.

The tax liability of the foreign resident is generally satisfied through a withholding by the Mexican party making the payment to the foreign resident who will be liable for the tax if not withheld.

a) Salaries and fees.

When a service is provided in Mexico, the source of income is considered to be Mexico. In the case of salaries, the tax rate is progressive, in accordance with the amount paid.

The tax rate for payment of fees for independent services is 21 percent.

b) Leasing of real estate and property.

The source of income is considered to be Mexico when the real estate or chattel is located within Mexico or when capital goods are used therein. The income derived from the use of these assets is subject to a withholding tax and no deductions are permitted.

c) Sale of real estate.

The proceeds from the sale of real estate in Mexico is considered to be Mexican-source income. There are two methods by which to pay the tax on the transaction. The first is through a withholding by the purchaser on the amount obtained without deductions. In the second scenario, the foreign seller must appoint a representative resident in Mexico, who shall give notice of any deductions to which the taxpayer is entitled, and pay the tax within the following 15 days.

d) Sale of shares.

The proceeds from the sale of shares are considered to be Mexican-source income when the company issuing the shares is resident in Mexico or when more than 50 percent of the accounting value of the shares transferred represents real estate located in Mexico.

e) Dividends.

The distribution of a dividend of a company resident in Mexico is considered to be Mexican-source income. At the time of edition of this Guide, such dividends are not subject to tax.

f) Interest.

When capital is invested or placed in Mexico, or when interest is paid by a Mexican resident or a non-resident with a permanent establishment in Mexico, the interest income derived therefrom is considered to be Mexican-source income. There are four applicable withholding rates depending on the to which the interest is paid to.

g) Financial leases.

When the property leased under a financial lease is located in Mexico, the amount considered to be interest payments is subject to a withholding tax.

h) Royalty payments.

The definition of royalty includes payments for the use or exploitation of intangible goods as well as the payments for information relative to industrial, commercial or scientific know-how, and in general, for payments made for technical assistance or transfers of technology. The source of income is considered to be in Mexico when the property or rights for which royalty payments are made are utilized in Mexico, or when the payments are made by a resident in Mexico or by a non-resident with a permanent establishment in Mexico. Payments of royalties are subject to a withholding tax.

i) Construction services.

When the services of construction, maintenance, installation, inspection or related supervisory services are provided inside Mexico, the total revenues obtained are subject to a withholding tax, without the benefit of deductions.

j) Payment of commissions.

Payment of commissions to foreign residents is exempt but if paid to residents in tax haven countries, a withholding tax applies.

B. PERMANENT ESTABLISHMENT.

Non-residents with a permanent establishment in Mexico are taxed on income attributable to such permanent establishment.

Non-residents without a permanent establishment in Mexico are taxed on Mexican-source income only.

1. Definition of permanent establishment.

For income tax purposes the term “permanent establishment” means any place in which business activities are wholly or partially carried on, including branches, agencies, offices, factories, workshops, installations, mines, quarries and any other place of exploration for or extraction of natural resources. The federal tax law provides a limited list of activities that will not be deemed to constitute a permanent establishment.

2. Agency relationship.

The activities of an individual or legal entity acting on behalf of a non-resident in Mexico may be considered a permanent establishment with respect to all the activities performed on behalf of the non-resident.

C. OTHER TAXES ON CAPITAL AND TRANSACTIONS

1. Asset Tax.

A tax on assets attributable to a business must be paid, at the rate of 1.8% on the net worth of the assets. It is not levied for the first four years of operations. Corporate and individual income tax actually paid on business income during the same period may be credited against this tax.

2. Value-Added Tax.

Mexico has a value-added tax (VAT) which is levied on the transfer of goods, rendering of independent services, granting of temporary right to use goods, and import of goods and services. Exports and some other specified items are subject to the zero-rate, such as basic foodstuffs (meat, milk, corn, wheat), medicine and agricultural services related to the production of basic foodstuffs. The general VAT rate is 15 percent, except in the border area where the general rate is 10 percent.

The computation of VAT is based on the value of the goods or services. The amount to be paid will be the difference between the tax which corresponds to the total of activities carried on in the period for which payment is made and the amounts for which accreditation is due.

Creditable tax is understood to be an amount equivalent to VAT which has been transferred to the taxpayer, plus the VAT that he has paid for the importation of goods or services in the corresponding period. If the creditable tax is greater than the VAT due for the period, resulting from the taxpayer's income from transfers, services or use, the difference will be considered a tax credit. The taxpayer may apply this credit to VAT due in subsequent provisional payments or may apply for a refund.

D. MEXICO'S TAX TREATIES

Mexico has treaties in effect to avoid double taxation and prevent tax evasion with Belgium, Canada, Chile, Denmark, Ecuador, Finland, France, Germany, Ireland, Israel, Italy, Japan, Korea, Luxembourg, Netherlands, Norway, Portugal, Romania, Singapore, Spain, Sweden, Switzerland, United Kingdom, and the United States.

Tax treaties, among other things, reduce withholding taxes on dividends, interest, royalties and capital gains.

The Mexican government has also concluded tax treaty negotiations with the Czech Republic, Greece, India, Indonesia, Poland and Venezuela.



IX INTELLECTUAL PROPERTY. LICENSING

The Mexican Institute of Industrial Property is an independent entity dedicated to the enforcement of intellectual property rights, under the Industrial Property Law, and in accordance with international standards.

A. PATENTS

A patent is a right granted to an individual or to an assignee to exclusively exploit an invention for a twenty-year, non-renewable period beginning from the date of filing the related application. To be patentable, an invention, must meet certain requirements.

Patent Law incorporates the first-to-file principle. Mexico is a party of, among others, the Paris Convention, the Patent Cooperation Treaty, UPOV and others, thus the date of filing a patent application in another member country is treated as the date of filing in Mexico.

B. UTILITY MODELS

Utility models may be registered with the Institute of Industrial Property if they are absolutely new and capable of industrial application. Protection is granted for a non-renewable term of 10 years from the date of filing.

C. INDUSTRIAL DESIGNS

Industrial designs include industrial drawings and industrial models. Industrial designs may be registered with the Institute if they are new and are used as a type or mold to make industrial products and are granted protection for a non-renewable term of 15 years.

D. INDUSTRIAL SECRETS

Industrial secrets are defined as any information capable of industrial application maintained in confidence which may be useful to obtain or to maintain a competitive advantage in the performance of economic activities, the confidentiality of which the owner has taken measures to preserve by labeling information as “confidential,” “secret,” or in another similar manner. Information in the public domain, information which may be obvious to an expert, or information which must be disclosed by law or by court order, is not considered an industrial secret.

E. INTEGRATED CIRCUITS

Integrated Circuits are protected for a 10-year term from the date of filing. The owner of a Certificate of the Topography of an Integrated Circuit has the right to stop others from reproducing the circuit in whole or in part, and to stop the importation, sale, or distribution without authorization. A protected topography of integrated circuits must bear the legend “(M)” or “(T)” plus the name of the owner.

F. TRADEMARKS AND SERVICE MARKS

A trademark is defined as a visible sign or symbol that distinguishes products or services from others of the same species or class in the marketplace. Trademarks and service marks must be registered in order to obtain exclusive right of use.

As a general rule, registration is granted to the first applicant; however, the first user in Mexico or abroad has a preferential right to register. Trademarks may be registered for up to 10 renewable years from the date of filing of the registration application with the Institute. Use of a trademark may not be discontinued for more than three consecutive years without justification, otherwise the registration could expire.

Trade or service marks cover only specific goods or services within a single class of products. There are no multiple class registrations.

G. COLLECTIVE TRADEMARKS

Collective trademarks may be registered by legally incorporated associations of producers, manufacturers, business-people or service providers in order to distinguish their products or services from those of non-members.

H. COMMERCIAL SLOGANS

Commercial slogans are phrases or legends that have the purpose of announcing businesses, commercial, industrial or service establishments to the public, to easily distinguish them from others of their kind. Commercial slogans must be registered in order to obtain exclusive right of use.

I. TRADE NAMES

Commercial names of companies and trade names of commercial, service or industrial establishments are protected without need for registration. The protection is granted in the geographic zone of the effective clientele of the company, or establishment, using the trade name and may be extended throughout the country if there is massive and constant diffusion of the name on a national level.

J. APPELLATIONS OF ORIGIN

Appellations of origin are names of geographic regions used to designate a product that originates from said region, and whose qualities or characteristics stem exclusively from the region.

K. ROYALTY PAYMENTS

Mexican law does not provide any specific rules governing minimum or maximum royalties. Tax authorities, however, have the right to adjust the taxable profit of the payer if such royalties are excessive and do not reflect “market value.”

L. COMPARATIVE ADVERTISING

Comparative advertising is permitted in Mexico if the comparison of products or services covered by a trademark is done for information purposes. The Institute may impose fines, close the business, or place

under temporary arrest those individuals who use comparative advertising and publicity that is misleading, false, or exaggerated, with the purpose of discrediting products, services or a competitor.

M. PARALLEL IMPORTS

Any person may legally import into Mexico products covered by a registered trademark, for their use, distribution or commercialization.

N. COPYRIGHTS INCLUDING SOFTWARE

Copyright is protected for original intellectual creations without need for registration.

There are two types of rights granted to authors:

1. patrimonial rights to use or reproduce the work of the author for profit, which are effective during the author's lifetime and 75 years after his death; and
2. moral rights, which include recognition of authorship and opposition to any modification made of the copyrighted work without authorization.

Such rights are perpetual, non-transferable, and non-waivable.

The protection of the author's right is granted on the following types of works: literary, scientific, technical,

legal, pedagogic, didactic, musical, pictorial, design, engraving, lithographic, sculptural, plastic, architectural, photographic, cinematic, audiovisual, radio and television, titles of periodicals, computer software and on any other work which could be considered comprised within the generic types of artistic or intellectual works mentioned above.

Copyright infringement is punishable by fine, and if done on a commercial scale, criminal penalties may also apply.

Preliminary measures, such as the seizure of infringing material, orders to cease and desist, and orders to suspend an infringement may be issued by the Institute.

Mexico is a party to the Universal Copyright Convention, the Interamerican Copyright Convention and the Berne Convention.

O. PROTECTION OF NEW VARIETIES OF PLANTS

New varieties of plants are protected under a separate law, the Vegetal Variety Law, which came in effect in 1996.

Protection is granted for a 25 year term for perennial, forestry, fruit, ornamental plants and grafts, and 20 years for other species.

The owner has the right to the exclusive use of the breeding material for commercial production, marketing and sale.



IMMIGRATION

The General Law of Population establishes three general groups for the treatment of foreigners entering into Mexico: non-immigrant, immigrant, and permanent resident.

A. NON-IMMIGRANT

Foreigners may enter the country, on a temporary basis, under various categories, such as tourists, visitors, students, religious ministers, and travelers in transit, among others.

The visitor category is the most common one for foreigners entering the country for business meetings, market studies, to carry out any technical or management activities for Mexican companies, or to attend corporate shareholders or board of directors meetings. Such visitors will be granted a permit (FM3) for up to one year, renewable four times, for a total period of five years.

The permit shall specify the place and activities to be carried out by the foreigner. When a remunerated activity is performed for a Mexican entity, the Mexican entity will be jointly responsible for any sanctions imposed for violations of the terms of the permit.

B. IMMIGRANT

Immigrants are foreigners authorized to enter the country with the purpose of establishing permanent residency. Immigrants will be allowed to remain in the country upon satisfying various requisites and will be granted an immigrant (“inmigrante”) permit (FM2) for up to one year annually renewable for up to five years. Upon completion of the five-year period, the foreigner will be granted permanent resident (“inmigrado”) status. Immigrants staying out of the country more than 18 months in a continuous or non-continuous manner during the five year annually renewable period will not be granted the permanent resident status until a new five-year period has elapsed thereafter. When such absences total more than 2 years, foreigners will lose their immigrant status.

Immigrant categories include retirees, investors, professionals, scientists, technicians, relatives, artist and sportsmen, among others.

C. PERMANENT RESIDENT

Immigrants residing in the country for five years may acquire permanent resident status (“inmigrado”). Under such classification, the foreigner’s periods of permitted absences

from Mexico become more liberal, and may freely carry out any activity without permit from the Ministry of Interior. However, if the permanent resident foreigner remains outside Mexico for more than three consecutive years or for more than five years in a 10-year period, the foreigner will lose permanent residency status.

D. GENERAL COMMENTS

Foreigners entering the country as non-immigrants may import a vehicle during the term of their status complying with certain requisites, such as periodic renewals and posting bonds. Immigrants may not import a vehicle, except for immigrants in the retiree (“rentista”) classification. Non-immigrants and immigrants may import household belongings with certain restrictions.

E. TEMPORARY ENTRY OF VISITORS AND MEMBERS OF A BOARD THROUGH THE “FMVC”

The FMVC immigration form facilitates the entry into Mexico of foreigners, as visitors, including the following categories: business visitors, members of the Board, technicians, and transfer of staff.

For these purposes, the term business visitor includes foreigners who intend to realize any business activity related with trading or signing of commercial agreements, the search for alternatives to invest in

the country, or attending board of directors meetings of enterprises, legally established in Mexico.

The form is available at the consular offices of Mexico, airlines, travel agencies and immigration staff at the ports and the points of entry to the country and are valid for a maximum period of time of thirty (30) days.

F. TEMPORARY ENTRY OF BUSINESS PERSONS UNDER NAFTA

Chapter XVI of NAFTA states the general principles under which a NAFTA Party may authorize temporary entrance of businesspersons of another NAFTA Party, without the need for an employment permit.

The term businessperson under NAFTA includes the following categories: business visitor, traders-investors, intra-company transferees, and professionals, all of which may not receive income for their activities in Mexico.

All the above authorizations shall be temporary, and thus visitors shall be classified as non-immigrants. NAFTA creates the “FMN”, a special immigration document, currently included in a combined immigration form covering tourists, and the FMVC category mentioned in E. above, issued by the consular offices or at the airlines, to businesspersons crossing the border to develop a non-Mexican remunerative activity for a maximum of 30 days.



EXPORTS FROM MEXICO

One of the priority objectives of Mexican foreign trade policy is to promote exports, especially non-petroleum exports. This has been made possible through the adoption of several programs which grant additional advantages to exporting industries.

A. FOREIGN TRADE COMPANIES (ECEX)

This program may be adopted by entities whose corporate purpose is the promotion and commercialization of exports.

B. HIGH-EXPORT COMPANIES (ALTEX)

To be eligible for this program, applicants must demonstrate direct exports of at least US\$2,000,000 or 40 percent of the company's total annual sales, or indirect exports of at least 50 percent of their total annual sales.

C. IMPORT TAXES DRAWBACK PROGRAM

This program may be entered into persons or entities performing direct or indirect exports. Companies within this program are eligible for a refund of import taxes paid for imported parts incorporated into the exported goods and for those returned in the same condition as imported.

D. MAQUILADORA PROGRAM (IN-BOND PROGRAM)

Maquiladora plants are assembly plants - often referred to as in-bond plants - in which raw materials or component parts are temporarily imported for assembly in Mexico and the assembled product is exported. The temporary import of the foreign materials is free of general import tax and value-added tax, subject to their final exportation within the finished product.

Maquiladoras are allowed to sell in the domestic market. The products to be sold are subject to the general import duty and counter-vailing duties, if any, and value-added tax on the foreign parts and components originally imported duty free.

E. TEMPORARY IMPORT PROGRAM FOR EXPORT (PITEX)

This program may be entered into by individuals or entities directly or indirectly exporting goods. In order to be eligible, annual exports represent at least 10 percent of total annual sales of products registered in the Pitex program.

Exporters who adopt this program may be authorized to temporarily import duty free:

- 1) raw materials, parts and components destined to be incorporated into export goods;
- 2) containers and packaging and bottling materials, trailer containers; and
- 3) fuel, lubricants, spare parts and consumable goods used in the manufacturing process.

F. SECTOR PROMOTION PROGRAMS

Under NAFTA, all finished products that comply with the NAFTA rules of origin are not subject to US or Canadian import duties on their export from Mexico.

However, as provided for by NAFTA, since January 2001, all non-originating NAFTA components, incorporated into finished products to be exported to the US and Canada, are subject to Mexican import duties and the corresponding 15% Value Added Tax.

The Mexican government is aware that, for certain companies, components from outside North America are very important. To minimize the impact of this NAFTA provision, Mexico has implemented Sector Promotion Programs, which objective is to eliminate import duties on some of the non-NAFTA originating components, or to reduce the same to a duty no higher than 5%. To date, there are various programs covering the most important areas, such as the electronic, electric, automotive, furniture, toys, capital assets, and clothing sectors.

The coming into effect of the Free Trade Agreement with the European Union, further minimizes the consequences of this rule. If the EU components of the finished products are free of duties, under such EU Treaty, then the Mexican duty to be paid will be zero. Consequently, the export of the finished product to the US or Canada will be totally free of duties.



INTERNATIONAL FREE TRADE AGREEMENTS

A. INTERNATIONAL AGREEMENTS

In a more interrelated and competitive world, Mexico has adopted several measures to assure its participation. Mexico has developed a network of free trade agreements, which in addition to our country's strategic geographic position, have given it a pivotal role in international trade.

The nine free trade agreements to which Mexico is, currently, a party to, have stimulated the trade expansion of the country, placing Mexico as the world's seventh trading power, and turning it into one of the most dynamic markets.

Since 1986, Mexico is part of the GATT (now the World Trade Organization), with the goal of participating in the consolidation of a system allowing for a more equitable distribution of international commercial benefits and the furthering of multilateral policies.

In addition, since 1994, Mexico has been part of the Organization for Economic Cooperation and Development (OECD). As a member of the same, some of the implications related to investment in Mexico are non-discriminatory treatment to investors, further liberalization of investment regulations and increased accountability of the legal system.

In November 1993, Mexico became a member of the Asia-Pacific Economic Cooperation Mechanism (APEC), and now has the opportunity to conduct trade in one of the most promising areas of the world.

Although Mexico is not a member of MERCOSUR (Common Market of the Southern Hemisphere) formed by Argentina, Brazil, Chile, Paraguay and Uruguay, it does have strong commercial ties with its member states, and has signed a number of bilateral trade agreements of limited scope with its members.

B. FREE TRADE AGREEMENTS IN EFFECT

As of June 2002, the following free trade agreements entered into by Mexico are in effect:

- | | |
|-------------------------------------|---|
| a) NAFTA (United States and Canada) | f) Colombia and Venezuela |
| b) European Union | g) Nicaragua and Honduras |
| c) Bolivia | h) Israel |
| d) Chile | i) Iceland, Liechtenstein, Norway and Switzerland |
| e) Costa Rica | |

2. North American Free Trade Agreement (NAFTA)

The North American Free Trade Agreement came into effect on January 1, 1994, committing the United States, Canada and Mexico to a process of phasing out trade barriers completely by January 1, 2009. NAFTA was by far the largest free trade area in the world. The subsequent lowering of trade tariffs in the European Union now makes NAFTA one of the two largest free trade areas.

Under NAFTA, U.S. and Canadian companies enjoy tariff-free treatment on all NAFTA-made goods that enter Mexico on a phase-in schedule.

Fifty percent of all tariffs on U.S. and Canadian exports to Mexico were eliminated as of January 1, 1994, the day NAFTA entered into force. By January 1999, Mexico discontinued tariffs on 65 percent of all U.S. and Canadian goods entering the country, and by January 2009, all tariffs on NAFTA imports shall disappear.

3. Mexico - European Union Free Trade Agreement

The European Union (EU) is Mexico's second largest commercial partner in the areas of foreign investment and international trade of goods and services, and is the world's largest market.

The free trade agreement with the EU came into effect on July 2000.

The Treaty's general aims comprise progressive, preferential and reciprocal trade liberalization, liberalization of current payments, capital movement and invisible transactions and investment promotion, in accordance with WTO's rules.

As of the year 2003, 100 percent of industrialized Mexican products will have access to the common market duty free. Approximately 95 percent of Mexican exports will obtain a rule of origin from the EU, among the most important are textiles, transport and auto parts

sector, household electrical appliances, electronics, shoes, chemicals and plastics.

On July 2000, 47 percent of the EU industrialized products obtained duty free access to the Mexican market. By January 2003, this number will increase to 52 percent, and on January 2007, all tariffs will be eliminated. Moreover, the maximum duty on those industrial products to be phased out after January 2003, will be 5 percent.

The commercial liberalization will allow Mexico to increase foreign investments. It will likewise create improved access to the European market for Mexican companies which wish to invest or export.

C. PROFITING FROM CURRENT FREE TRADE AGREEMENTS

One of the least analyzed aspects of Mexico's privileged position as a free trade partner is the benefits it offers for world wide investors to access other markets, free of duties.

For instance, with the entry into effect of the Mexico - EU Free Trade Agreement, companies from the United States and Canada, as NAFTA members, may access the EU market, free of duties. Likewise, countries, members of the EU, may access the USA and Canada markets, under the same conditions.

With the simultaneous application of NAFTA and the Mexico - EU Agreement, international companies may export their products to such markets, free of any import duties, or at very reduced ones.

However, this can only be achieved if the following two conditions are met: (1) the processing or final assembly in Mexico of the products to be exported, and (2) due compliance with the rules of origin provided for by NAFTA or the Mexico - EU Agreement, respectively, in order to qualify as an originating product.

This outstanding advantage should be subject to serious consideration by all international companies, which intend to expand their world-wide market access of their products.



OVERSEAS TRADE COMMISSIONS

NORTHAMERICA

UNITED STATES

ATLANTA

229 Peachtree St., N.E. Suite 1100,
International Tower, Atlanta, Georgia 30303,
U.S.A.

Tel: (404) 5-22-27-40 / 5-22-53-73 /
5-22-53-74 / 5-22-08-57

Fax: (404) 6-81-33-61

Virginia Arteaga Sáenz

E-mail: carteaga@bancomext.gob.mx
cc-atlanta@bancomext.gob.mx

CHICAGO

225 North Michigan Av., Suite 1800
Chicago, Illinois 60601, U.S.A.

Tel: (312) 8-56-03-16

Fax: (312) 8-56-18-34

Miguel Angel Leaman Rivas

E-mail: mleaman@bancomext.gob.mx
cc-chicago@bancomext.gob.mx

DALLAS

2777 Stemmons Freeway, Suite 1622
Dallas, Texas 75207, U.S.A.

Tel: (214) 6-88-40-96, 6-88-40-97,
6-37-02-33

Fax: (214) 9-05-38-31

Carlos Bello Roch

E-mail: cbello@bancomext.gob.mx
cc-dallas@bancomext.gob.mx

DETROIT (Trade Unit)

2000 Town Center, Suite 1900
Southfield, Michigan 48075, U.S.A.

Tel: (248) 3-51-62-84

Fax: (248) 3-51-26-99

Luis Carlos Salazar

E-mail: lsalazar@bancomext.gob.mx
cc-detroit@bancomext.gob.mx

HOUSTON (Trade Unit)

5065 Westheimer Road Suite 707
East Houston, Texas 77056, U.S.A.

Tel: (713) 965-07-67

Fax: (713) 965-07-31

Armando Camarena Aranda

E-mail: acamaren@bancomext.gob.mx

LOS ANGELES

350 South Figueroa St.
World Trade Center Suite 296,
Los Angeles, California 90071, U.S.A.

Tel: (213) 6-28-12-20

Fax: (213) 6-28-84-66

Herminio Hernández Ramírez

E-mail: hhernanr@bancomext.gob.mx
cc-los.angeles@bancomext.gob.mx

MIAMI

220 Alhambra Circle, Suite 210,
Coral Gables, Florida 33134, U.S.A.

Tel: (305) 4-42-73-74

Fax: (305) 4-42-41-47

José Antonio Rivas Hurtado

E-mail: jrivash@bancomext.gob.mx
cc-miami@bancomext.gob.mx

NEW YORK

Trade Commission of Mexico

375 Park Avenue 19th Floor
New York, N. Y. 10152, U.S.A.

Tel: (212) 8-26-29-78, 8-26-29-39

Fax: (212) 826-29-79

Edmundo González Herrera

E-mail: egonzalh@bancomext.gob.mx
cc-nueva.york@bancomext.gob.mx

SAN ANTONIO (Trade Unit)

203 S. St. Mary's St. Suite 350
San Antonio, Texas 78205, U.S.A.

Tel: (210) 2-81-97-48

Fax: (210) 2-81-97-49

Lauro Andrés Jauregui Araiza

E-mail: ljauregu@bancomext.gob.mx
cc-san.antonio@bancomext.gob.mx

SEATTLE (Trade Unit)

2132 Third Avenue,
Seattle, Washington 98121, U.S.A.

Tel: (206) 4-48-89-42

Fax: (206) 4-43-04-52

María Guadalupe Aceves

E-mail: trademexwa@qwest.net
cc-seattle@bancomext.gob.mx

CANADA

MONTREAL

1501 McGill College, Suite 1540
Montreal, Quebec H3A 3M8, Canadá

Tel: (514) 2-87-08-99, 2-87-16-69

Fax: (514) 2-87-18-44

Arturo Hauser Veytia

E-mail: ahauser@bancomext.gob.mx
cc-montreal@bancomext.gob.mx

TORONTO

66 Wellington St. West,

P.O. Box 32, Suite 2712

Toronto Dominion Bank Tower;

Toronto, Ontario M5K 1A1, Canadá

Tel: (416) 8-67-92-92, 8-67-93-25

Fax: (416) 8-67-18-47

Rafael José Cortés Gómez

E-mail: rcortes@bancomext.gob.mx
cc-toronto@bancomext.gob.mx

VANCOUVER

200 Granville Street, 1365-200.

Vancouver, B.C. V6C 1S4, Canadá

Tel: (604) 6-82-36-48 6-82-24-70

Fax: (604) 6-82-13-55 844-78-66

Sergio Javier Rios Martínez

E-mail: srios@trademexbc.com
bancomext@trademexbc.com

WESTERN EUROPE

GERMANY

Rüsterstrasse 1, D-60395

Frankfurt Main, Germany

Tel: (69) 9-72-69-80

Fax: (69) 9-72-69-811

Francisco González Díaz

E-mail: fgonzalez@bancomext.gob.mx
frankfurt@bancomext.de

BRUSSELS (Trade Unit)

Av. Franklin Roosevelt No. 94

C.P.1050, Brussels, Belgium

Tel. (2) 6-29-07-87

Fax: (2) 6-44-04-45

Graciela Baez Ricardez

E-mail: bxtbruselas@starmedia.com

SPAIN

Carrera San Jerónimo 46-2º piso
Madrid, Spain 28014
Tel: (1) 4-20-20-17
Fax: (1) 4-20-27-36
Carlos Ceceña Cervantes
E-mail: ccecena@bancomext.gob.mx
cc-espana@bancomext.gob.mx

FRANCE

4 Rue Notre Dame Des Victoires
Paris, France 75002
Tel: (33) 142-86-60-00 al 08,
142-86-60-12
Fax: (33) 142-61-52-95
José Manuel Rodríguez Chauviere
E-mail: jorodcha@bancomext.net
francia@bancomext.net

HOLLAND

Kneuterdijk 2, 1st Floor
2514 The Hague, Netherlands
Tel: (70) 3-63-16-40
Fax: (70) 3-46-69-92
Raúl Alfaro Ugalde
E-mail: ralfaro@bancomext-nl.com
cc-holanda@bancomext.gob.mx

ITALY

Foro Buonaparte 12
Milán 20121, Italy
Tel: (2) 879-08-61
Fax: (2) 72-00-40-00
José L. Fernández Santisteban
E-mail: jfernans@bancomext.gob.mx
milan@bancomext.it

UNITED KINGDOM

5th. Floor Rear
33 St. James Square
First floor, London SW1Y4JU
Tel: (207) 726-44-42
Fax: (207) 726-60-04
Elena Espinosa de los Reyes
E-mail: mespinod@bancomext.gob.mx
cc-ingles@bancomext.gob.mx

ASIA

KOREA

The Korea Chamber of Commerce &
Industry Bldg.No. 642-6F 145, 4-KA
Namdaemun-Ro, Chung-Ku
Seul, Korea
Tel: (2) 7-75-56-13
Fax: (2) 7-75-56-15
José Antonio Peral Vallejo
E-mail: jperal@bancomext.gob.mx
cc-bancomxt@bora.dacom.co.kr

HONG KONG

Trade Commission of Mexico
Suite 3203 A, Central Plaza 18,
Harbour Road,
Wanchai, Hong Kong
Tel: (852) 28-77-34-34
Fax: (852) 28-77-66-07
Norma Beatriz García Gordillo
E-mail: ngarciag@bancomext.gob.mx
cc-hongkong@bancomext.gob.mx

JAPAN

Osaka (Trade Unit)
Osaka Chamber of Commerce and Industry
Bldg. 5F 2-8 Honmachi-bashi
Chuo-ku Osaka 540-0029 Japan
Osaka 559-0034, Japan
Tel: (6) 6920-92-45
Fax: (6) 6920-92-46
E-mail: cc-osaka@bancomext.gob.mx

Tokyo

2-15-2 Nagata-Cho,
Chiyoda-Ku, Tokio, Japan 100
Tel: (3) 35-80-08-11, 35-80-08-12
Fax: (3) 35-80-92-04
Sergio A. Inclán Gallardo
E-mail: sinclan@bancomext.gob.mx
cc-japon@bancomext.gob.mx

MALAYSIA (Trade Unit)

Suite 22-05, 22nd Floor Menara Tan&Tan,
207 Jalan Tun Razak
50400 Kuala Lumpur, Malaysia
Tel: (3) 2164-58-35
Fax: (3) 2164-36-98
Cecilia Alonso Segura
E-mail: klnce@po.jaring.my
cc-malasia@bancomext.gob.mx

SINGAPORE

150 Beach Road No.14-01
The Gateway West Tower
189720, Singapore
Tel: (65) 62-97-20-52
Fax: (65) 62-97-17-21
Carlos Edgardo Ríos Reyes
E-mail: crios@bancomext.gob.mx
bnncesin@singnet.com.sg

TAIWAN

Mexican Trade Services
International Trade Building Suite
2905, 29th Floor.
333 Keelung Road. Sec. 1 P.O. Box 109-0994
Taipei, Taiwan,
Tel: (2) 757-6526, 757-6527, 757-6528
Fax: (2) 7-57-61-80
Marco Antonio Barragán Fernández
E-mail: mextramb@ms64.hinet.net
mextrade@ms64.hinet.net

LATIN AMERICA AND THE CARIBBEAN

ARGENTINA

Av. Alicia Moreau de Justo 1150,
Oficina 305-B, Puerto Madero
1107, Buenos Aires, Argentina
Tel: (1) 43-31-51-69, 43-31-53-45
Fax: (1) 43-31-50-84
Samuel Lara Sánchez
E-mail: slara@bancomext.gob.mx
cc-argentina@bancomext.gob.mx

BOLIVIA (Trade Unit)

Avenida Sánchez Bustamante No.509
Zona Calacoto, La Paz, Bolivia
Tel: (2) 78-52-24
Fax: (2) 78-52-24
Andrea Corina Sosa Pérez
E-mail: modcombancomext@kolla.net

BRAZIL

Rua Holanda 14,
Jardim Europa CEP. 01446-030
Sao Paulo, Brazil
Tel: (11) 30 88 48 11, 30 88 47 25
Fax: (11) 30 88 39 41
Roberto Díaz Martínez
E-mail: rdiazm@terra.com.br
cc-brasil@bancomext.gob.mx

CHILE

Felix de Amesti 128, 2° piso.
Las Condes, Santiago de Chile
Tel: (2) 20-65-147, 20-65-181,
20-67-024, 24-60-942
Fax: (2) 20-66-285
Carlos Fuentes Arriaga
E-mail: cfuentes@bancomext.gob.mx
cc-chile@bancomext.gob.mx

COLOMBIA

Edificio Teleport Business Park
Calle 114 No 9-45 Torre B. Of. 907, 908,
909
Santa Fé de Bogotá, Colombia.
Tel: (1) 62-92-972, 62-92-961
Fax: (1) 62-92-727
Rigoberto Flores Bustamante
E-mail: rfloresb@bancomext.gob.mx
cc-colombia@bancomext.gob.mx

COSTA RICA

Edificio "C", Piso 3, Ofi plaza del Este
de la Rotonda de la Bandera, 100 mts. al
Oeste. Frente al Colegio Anastasio Alfaro
Barrio Dent, San José, Costa Rica
Tel: (506) 23-49-601, 28-38-652,
28-38-653, 28-38-672
Fax: (506) 23-49-613
Fernando Torres Parraud
E-mail: ftorresp@bancomext.gob.mx
cc-costa.rica@bancomext.gob.mx

CUBA

Miramar Trade Center, 3ª. Av. Entre
78 y 80, 4° piso, Desp. 408. Miramar, Cd. De
La Habana, Cuba
Tel: (7) 2-04-22-15, 2-04-28-87,
2-04-27-62
Fax: (7) 2-04-26-66
Manuel Orella Arechandieta
E-mail: morella@bancomext.gob.mx
bancomextcuba@hotmail.com

ECUADOR (Trade Unit)

Av. 6 de Diciembre 4843 y Naciones Unidas,
Quito, Ecuador
Tel: (2) 43-08-21
Fax: (2) 43-10-05
Susana Peñaherrera Toledo
E-mail: cc-ecuador@bancomext.gob.mx

GUATEMALA

Edificio Géminis 10, Torre Sur
12 Calle 1-25 Zona 10, Piso No.11
Ofic.1111 - 1112 Guatemala, C.A.01010
Tel: (502) 33-53-205, 33-52-863,
33-82-866
Fax: (502) 33-52-724
Rafael de la Cruz Laso
E-mail: rdela@bancomext.gob.mx
bancomext@intelnet.net.gt

HONDURAS (Trade Unit)

Av. República de México Casa 2402, Col.
Palmera
Entre Parque Benito Juárez y Av. Juan Lindo
Tegucigalpa, Honduras
Tel: (504) 2-21-17-10, 2-32-01-38,
2-32-01-41, 2-32-40-39
Fax: (504) 2-21-17-12, 2-32-47-19
Galo Espinoza Fernández
E-mail: gespinoz@bancomext.gob.mx
modulocomercial@cablecolor.hn

NICARAGUA (Trade Unit)

Km. 4.5 Carretera a Masaya, 25 varas arriba
Altamira, Nicaragua
Tel. (505) 27-81-859, 27-84-921
Fax. (505) 27-82-886
Johanna Reyes Meléndez
E-mail: modulonic@ccmexico.co.cr

PERU (Trade Unit)

Jorge Basadre 710
Col. San Isidro, Lima 27, Peru
Tel: (1) 44-05-205
Fax: (1) 42-19-918
Miguel Angel Godinez Villegas
E-mail: mgodinez@bancomext.gob.mx
bnceper@tsi.com.pe
cc-peru @bancomext.gob.mx

DOMINICAN REPUBLIC (Trade Unit)

Arzobispo Meriño 265 Esq. Las Mercedes
Santo Domingo, República Dominicana.
Tel. (809) 6-87-64-44
Fax: (809) 6-87-78-72, 333-50-31
Juan Francisco Colón Presbot
E-mail: tracomex@tricom.net

EL SALVADOR (Trade Unit)

Calle Circunvalación y Pasaje No. 12,
Colonia San Benito,
San Salvador, El Salvador
Tel: (503) 2-43-20-37, 2-43-31-90,
2-43-04-45
Fax: (503) 2-43-77-30
Octavio Lozano García
E-mail: olozano@bancomext.gob.mx
modulocomercial@telesal.net

VENEZUELA

Asociación Bancaria de Venezuela 4° piso
Oficina 44, Av. Venezuela, El Rosal
A.P.61181, Caracas1060-A, Venezuela
Tel: (2) 95-16-078, 95-12-962,
95-51-47
Fax: (2) 95-12-494
César Eduardo De la Peña Domínguez
E-mail: cdelad@bancomext.gob.mx
ca-venezuela@cantv.net



OFFICES IN MEXICO

HEADQUARTERS

MEXICO CITY

Camino a Sta. Teresa 1679,
Col. Jardines del Pedregal
Delegación Alvaro Obregón
01900 México D.F.
Tel: (55) 5481 60-00
Fax: (55) 5652-94-08
E-mail: www.bancomext.gob.mx

BANCOMEXT CENTERS

METROPOLITAN AREA

METROPOLITAN AREA

Periférico Sur No. 4333, 3er. Piso Ote.
Col. Jardines en la Montaña,
14210 México D.F.
Gabriel Leyva Reyes
E-mail: aleyva@bancomext.gob.mx
Tel: (55) 5449-9000, 5449-9424
Fax: (55) 5449-9223, 5449-9443

TAXCO

Av. de los Plateros No. 208 Locales A y B
Col. Centro 40200 Taxco, Guerrero
Hesiquio Hernández Uribe
E-mail: hhernanu@bancomext.gob.mx
Tel: (762) 622-49-23; 622-79-26,
622-02-81, 622-06-72
Fax: (762) 622-40-11

CUERNAVACA

Blvd. Alta Tensión 580
Esq. Av. Cuauhtémoc,
Col. Cantarranas
62448 Cuernavaca, Morelos
Lorenia Orantes Bazán
E-mail: aorantes@bancomext.gob.mx
Tel: (777) 318-07-83, 318-07-93,
318-08-12, 312-15-07,
312-15-08, 312-15-03
Fax: (777) 318-88-77

MEXICO CITY (WTC)

Filadelfia esq. Dakota s/n P.B.
Col. Nápoles
03810 México, D.F.
Carlos Arellano
Tel: (55) 5488-2893, 2895 al 98
Fax: (55) 5488-2891
E-mail: pdiaz@bancomext.gob.mx
fherrera@bancomext.gob.mx

TOLUCA

Vialidad Metepec No. 284
Edificio Plaza San Juan 2º Piso
Col. Residencial Las Américas
52150 Metepec, Edo. de México
Lajos Szendro Kassa
E-mail: szendro@bancomext.gob.mx
Tel: (722) 212-24-10, 212-24-48,
212-25-63, 219-37-18
Fax: (722) 212-23-99, 212-25-82

NORTH

MONTERREY

Av. Fundidora No. 501 Col. Obrera,
CINTERMEX
64010 Monterrey, N.L.
Alejandro R. Blasco Ruíz
Santiago Rodríguez Macías
E-mail: ablasco@bancomext.gob.mx
sarodmac@bancomext.gob.mx
Tel: (81) 83-69-21-00
Fax: (81) 83-69-21-50, 55

CHIHUAHUA

Antonio de Montes No. 1103
Col. San Felipe
31240 Chihuahua, Chih.
Ricardo Armienta Trejo
E-mail: rarmient@bancomext.gob.mx
Tel: (614) 439-24-30, 439-24-19,
439-24-10, 413-96-01
Fax: (614) 413-95-22, 439-24-41

CD. JUAREZ

Blvd. Tomás Fernández No. 7930 P.B.
Fracc. Campestre Juárez,
32470 Cd. Juárez, Chihuahua
Luz Ma. Silva Gallegos
E-mail: lsilva@bancomext.gob.mx
Tel: (656) 629-00-23, 29-06-46-49
Fax: (656) 629-00-25, 626-00-24

GOMEZ PALACIO

Calzada Lázaro Cárdenas No. 180,
Parque Industrial Lagunero
35070 Gómez Palacio, Durango
José Castañeda Hernández
E-mail: jcastanh@bancomext.gob.mx
Tel: (871) 750-05-13, 750-06-21,
750-20-18, 750-13-23
Fax: (871) 750-13-23

SALTILLO

Periférico Luis Echeverría No. 1560
Edificio Torre Saltillo 3er. Piso
Col. Guanajuato
25280 Saltillo, Coahuila
Sotero González Montijo
E-mail: sogonmon@bancomext.gob.mx
Tel: (844) 416-40-25, 415-13-58
Fax: (844) 415-06-71

TAMPICO

Av. Hidalgo No. 4503,
1er. Piso Desp. 102
Edificio Chairel, Fracc. Lomas del Naranjal
89349 Tampico, Tamaulipas
Jorge A. Martínez Gómez
E-mail: jmarting@bancomext.gob.mx
Tel: (833) 217-17-84, 217-15-84,
217- 18- 35
Fax: (833) 217-25-59

WEST

GUADALAJARA

Boulevard Puerta de Hierro No. 5090-5
Fraccionamiento Puerta de Hierro
45110 Zapopan, Jal.
Roberto Ureña Rangel
José Armando Salmón Muñoz
E-mail: rurena@bancomext.gob.mx
jsalmon@bancomext.gob.mx
Tel: (33) 36-48 27 00
Fax: (33) 36-48 27 22

COLIMA

Aldama No. 552 Desp. 202
Edificio "Centro Ejecutivo" Col. Centro
28000 Colima, Col.
Bernardo Montiel Hernández
E-mail: bmonriel@bancomext.gob.mx
Tel: (312) 314-83-73, 314-83-75
Fax: (312) 314-83-85

CULIACAN

Av. Independencia No. 2165
Esq. Andador Leandro Valle
Col. Centro Sinaloa
80200 Culiacán, Sinaloa
Carlos Gabriel Lerma Cotera
E-mail: clerma@bancomext.gob.mx
Tel: (667) 717-17-26, 17-16-78,
Fax: (667) 717-02-52

HERMOSILLO

Periférico Poniente y Blvd. Luis Donaldo
Colosio
Negoplaza-Edif. "C" Locales 3 y 4
Col. Raquet Club 83200 Hermosillo, Sonora
Jesús Miguel Padrés Durán
E-mail: jpadres@bancomext.gob.mx
Tel: (662) 260-71-24 al 27, 260-70-00
y 77
Fax: (662) 260-71-28

LA PAZ

Km. 5 + 290, Carretera Benito Juárez
Fraccionamiento Fidepaz
23090 La Paz, B.C.S.
Edwing José Flores Quintana
E-mail: efloresq@bancomext.gob.mx
Tel: (612) 124-09-09, 124-09-10
Fax: (612) 124-09-19

MEXICALI

Calzada Justo Sierra 505
esq. Zaragoza, Col. Nueva Baja California
Gabriel E. Suárez López
E-mail: gsuarezl@bancomext.gob.mx
Tel: (686) 554-88-00, 554-81-00,
Fax: (686) 554-81-00

MORELIA

Av. Camelinas No. 2695
Col. 5 de Diciembre
58280 Morelia, Michoacán.
Luis Gabriel Martínez Márquez
E-mail: lmartinm@bancomext.gob.mx
Tel: (433) 314-82-29, 315-46-25,
315-51-28, 315-79-37 y 90
Fax: (433) 315-47-31, 315-55-70

TEPIC

Av. Insurgentes No.1044 Ote. Locales B y C
Fracc. Insurgentes, Col Menchaca
63156 Tepic, Nayarit
Rogelio Lara Ruíz
E-mail: glara@bancomext.gob.mx
Tel: (311) 214-54-66, 214-54-81,
214-55-64
Fax: (311) 214-55-00

TIJUANA

Blvd. Gral. Abelardo L. Rodríguez No.1405
Esq. con Frida Kahlo, Zona del Río
22320 Tijuana, B. C.
Gustavo Ramírez Piñón
E-mail: gramirez@bancomext.gob.mx
Tel: (664) 634-26-42, 635-76-00
Fax: (664) 635-76-94, 635-76-92

CENTER

LEON

Blvd. Mariano Escobedo No.2305 Oriente
Esq. Beethoven
Col. León Moderno 37480 León, Guanajuato
José Manuel Hoyos Salas
E-mail: jhoyo@bancomext.gob.mx
Tel: (477) 712-91-36, 712-91-48,
712-95-24 y 65, 712-96-10,
712-98-72
Fax: (477) 712-92-19

AGUASCALIENTES

Av. De las Américas No. 1604
Fracc. Santa Elena
20230 Aguascalientes, Ags.
Guillermo del Bosque Macías
E-mail: gdelbos@bancomext.gob.mx
Tel: (449) 917-19-01 al 06
Fax: (449) 917-19-19

QUERETARO

Prol. Pasteur Sur No.263 Col. Mercurio
76040 Querétaro, Qro.
Horacio Reyes Hernández
E-mail: hreyes@bancomext.gob.mx
Tel: (442) 238-22-10, 238-22-14
Fax: (442) 238-22-19, 238-22-59

SAN LUIS POTOSI

Av. Real de Lomas No. 1005, P.B.
Lomas 4ª Sección
78216 San Luis Potosí, S.L.P.
Javier Orduña González
E-mail: jorduna@bancomext.gob.mx
Tel: (444) 825-12-89, 825-13-45,
825-11-76
Fax: (444) 825-12-07, 825-12-13

ZACATECAS

Av. Ramón López Velarde No.302
Zona Centro
98000 Zacatecas, Zac.
Luis Fernando Cervantes Montoya
E-mail: lcervant@bancomext.gob.mx
Tel: (492) 924-00-51, 924-00-54
Fax: (492) 924-00-52

SOUTH

PUEBLA

Teziutlán Sur No.5, Col. La Paz
72160 Puebla, Pue.
Alfredo Arruti Bustos
E-mail: aarruti@bancomext.gob.mx
Tel: (222) 249-53-89, 249-53-90
Fax: (222) 249-95-26, 249-93-27

OAXACA

Calle de Murguía No.107
Esq. con 5 de Mayo
Col. Centro 68000 Oaxaca, Oax.
Eliseo R. Fuentes Solís
E-mail: efuentes@bancomext.gob.mx
Tel: (951) 514-71-11, 514-71-40
Fax: (951) 514-70-07 y 514-80-52

PACHUCA

Blvd. Felipe Angeles #605 esq. Constructores
Hidalguenses Col. Presa Jales Norte
José Manuel Pliego Domínguez
E-mail: jpliego@bancomext.gob.mx
Tel: (771) 718-58-07, 718-54-97
Fax: (771) 718-57-01

TAPACHULA

Av. Rialfer y Blvd. Gustavo Díaz Ordaz
30700 Tapachula, Chiapas
Leonardo Fernández Gudiño
E-mail: lfernang@bancomext.gob.mx
Tel: (962) 625-34-90, 625-31-74,
625-58-85, 625-32-92
Fax: (962) 625-34-09, 625-58-86

TLAXCALA

Av. Juárez No.53
Col. Centro
90000 Tlaxcala, Tlax.
Beatriz Sánchez Santiago
E-mail: bsanchez@bancomext.gob.mx
Tel: (246) 462-67-78, 462-68-08
Fax: (246) 462-68-38

VERACRUZ

Blvd. Adolfo Ruíz Cortínez Num. 1519
Fraccionamiento Costa de Oro
94299 Boca del Río, Veracruz
Claudia Esteves Cano
E-mail: cesteves@bancomext.gob.mx
Tel: (229) 921-04-00
Fax: (229) 922-90-51 and 922-90-53

SOUTHEAST

MERIDA

Calle 27 No.500, Col. Itzimmá
97100 Mérida, Yucatán
Adalberto Zúñiga Gómez
E-mail: azuniga@bancomext.gob.mx
Tel: (999) 927-62-65, 927-63-09 y 90,
927-68-18
Fax: (999) 927-69-55, 927-69-07

CAMPECHE

Av. Adolfo Ruíz Cortínez No.112
Edificio Torres de Cristal
Torre "A" Local 101 "A" Planta Baja
Col. San Román
24040 Campeche, Camp.
Arturo Romero Cárdenas
E-mail: aromeroc@bancomext.gob.mx
Tel: (981) 811-35-74, 811-35-98,
Fax: (981) 811-11-65

CANCUN

Av. Nader No.28
Super Manzana 2, Manzana 13
77500 Cancún, Quintana Roo
Irma Hassey Pérezcano
E-mail: ihasseey@bancomext.gob.mx
Tel: (998) 887-11-32, 887-32-32,
887-33-32
Fax: (998) 887-33-32

VILLAHERMOSA

Paseo Tabasco No.1203
11° Piso Torre Empresarial
Col. Lindavista
86050 Villahermosa, Tabasco
Luis A. Corvera Valenzuela
E-mail: lcorvera@bancomext.gob.mx
Tel: (993) 352-07-20 al 23
Fax: (993) 352-07-32