

## THE LAW ON FOREIGN INVESTMENT

*Adolfo Arrijo Vizcaino\**

The Law to Promote Mexican Investment and Regulate Foreign Investment,<sup>1</sup> enacted on May 9, 1973, by the Mexican Congress, is of major importance and is closely linked to the measures that have been adopted to regulate the transfer of technology. Both laws form part of the economic policy followed by President Echeverria aimed at obtaining a more balanced and independent development. The purpose of increasing Mexican enterprise without cutting off the flow of technology and capital from abroad is reflected in the objectives and policies of this development.

As its title indicates, the Law seeks to stimulate Mexican investment while also specifying the conditions under which foreign investment may participate in the national economy. The Law confirms the official policy followed up to now which, in brief, establishes that foreign investment will be well received when it helps to achieve the country's objectives, when it acts to complement national investment and when it does not displace existing business operated by Mexicans.

The Law retains the different dispositions previously established for foreign investment and specifies the economic activities that are reserved exclusively for the state and for Mexicans or Mexican companies by an exclusion-of-foreigners clause. As a general rule, foreign investment may not control more than 49 percent of the capital of Mexican corporations in all areas not otherwise specifically regulated. However, the Law accepts the need for a flexible policy on this matter and accordingly has created the National Commission on Foreign Investment, empowered to decide on the increase or reduction of this percentage in geographic areas, branches of economic activity, or in special cases, when it considers it beneficial to the country's economy. The National Commission on Foreign Investment is constituted of seven Ministries and is entitled to decide on the exceptions to the 49 percent maximum in accordance with the economic policy criteria established in the Law itself.

It will also be a general rule that the participation of foreign

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\* Partner, Bufete, Rubio and Billegas, Mexico City; Professor of Administrative and Tax Law, National University of Mexico and Universidad Ibero-Americana, Mexico City.

<sup>1</sup> Law to Promote Mexican Investment and to Regulate Foreign Investment, *Diario Oficial*, Mar. 9, 1973 [hereinafter cited as Foreign Investment Law].

investment in the management of a Mexican corporation may not exceed its capital participation. Foreign investment is defined as that undertaken by foreign individuals, foreign corporations and Mexican corporations with major foreign participation in their capital stock, or that controlled by foreigners. The Law includes provisions whereby credit institutions are authorized to acquire as fiduciaries the domain of real estate with the purpose of developing industrial and tourist activities within a strip 100 kilometers wide along the borders and 50 kilometers wide inland from the coasts, thereby enabling foreigners to invest in these areas.

An important innovation of the Law is that it regulates the purchase of existing Mexican corporations and provides that foreigners may not acquire or control a Mexican company without prior authorization of the National Commission on Foreign Investment. This is considered an important instrument for the protection of Mexican investors, as takeovers neither generate employment nor provide investment or technology, but rather displace Mexican business and nullify efforts already made. For the purpose of authorization, it is understood that a Mexican corporation is "acquired" through the purchase by foreigners of over 25 percent of its capital stock, or of more than 49 percent of its fixed assets. Leasing of the enterprise or of the assets essential to its operation shall be considered equivalent to the acquisition of the fixed assets. The National Commission on Foreign Investment may grant this authorization when it is in the country's interest.

The Law provides that shares representing foreign capital in Mexican corporations shall be nominative in every case, as this is the only legal way to identify foreign investment and to have a reasonable warranty for the effectiveness of its provisions. The Law also provides for the establishment of a National Registry of Foreign Investment as a department of the Ministry of Industry and Commerce, in which the foreign investors, the Mexican corporations controlled by foreigners, the titles of shares issued by Mexican corporations but owned by foreigners, trust agreements to acquire real estate within the borders and coasts, and the decisions adopted by the Commission, among other operations, shall be registered to legalize foreign investment in Mexico.

The Law seeks to foster and protect Mexican investment in terms of a healthy nationalism. It incorporates the industrial and trade incentives established by the present Administration and clearly defines the requirements that foreign investors must fulfill in order

to participate in the country's economy in accordance with the law. Although this Law may be considered a progressive one according to trends presently prevailing in Latin American countries and those revealed during the last few years, it in no way can be considered as excessively nationalistic, chauvinistic or anti-foreign. In fact, this Law is merely a modernized legal instrument through which our country is trying to promote its independent economic development as an emerging nation.

Government officials have repeatedly stated that Mexico does not have an isolationist attitude regarding foreign capital or technology, nor does it deny to the foreign investor the right to obtain a profit. What is proposed is that the benefit be mutual and that foreign investment shall conform to the country's laws and policies. The Mexican President has declared that in our country foreign capital will not enjoy special privileges, but neither will it be the object of discriminatory treatment. Rather, foreign investment will find in Mexico the protection of our laws, the security of our political stability, a wide range of public services, a policy of unlimited currency exchange, and solid public and private financing. Further, there exists the will of progress of all Mexicans, which ensures a constant improvement in the standards of living and a dynamic policy of social democracy which represents our best security for continued development.

Having summarized the general basis of this Law, I will proceed to analyze its principal aspects. Article 2 defines those who are considered foreign investors: foreign individuals or companies, foreign economic units without legal status (for instance, joint ventures, trusts, pledges of shares), and Mexican enterprises, the majority of whose capital is in the hands of foreigners or whose administration is controlled by foreigners. The Law reaches investment in Mexico in the capital of companies, in the acquisition of capital assets, and in other transactions, such as the leasing of commercial enterprises, acquisition of real estate, etc.

Individuals who reside in Mexico under the status of *inmigrado* (permanent residents who receive that status after residing in the country for at least five years) will not be considered as foreign investors, unless due to their activities they are connected with entities that have the capacity of making decisions of an economic nature from abroad. However, these *inmigrantes* will not be able to participate in investments made in geographic areas or activities which, in accordance with the related laws, are exclusively reserved

for Mexican citizens or Mexican companies whose charters have a clause excluding foreign investors.<sup>2</sup>

At this point, the reasons for which the Law considers as a foreign investor the Mexican corporation with major foreign participation in its capital stock, or whose administration is controlled by foreigners should be outlined. As provided by the Mexican Law on Business Corporations,<sup>3</sup> a company is granted Mexican nationality upon fulfillment of only two requirements: incorporation under Mexican laws, and establishment of a corporate domicile within Mexican territory. Before the enactment of the Foreign Investment Law it was perfectly legal for a Mexican corporation to have its entire capital structure and its administration totally controlled by foreigners. Until May 9, 1973, when this Law became effective, a number of Mexican corporations were really formal and legal structures disguising foreign investments.

Likewise, article 2 makes reference to foreign economic units without legal status. In Mexico this concept is used to define some particular operations which allow foreigners to control Mexican corporations without appearing as nominal shareholders. For instance, when a Mexican company obtains a loan from a foreign bank, it is very common for such a company to create a pledge or a trust over its shares as a guarantee. Then, as the foreign bank reserves the voting rights of those shares, we are really talking of a foreign investment, since the main decisions of the Mexican corporation may be adopted by foreigners.

Articles 4 and 5 of the Law classify the various activities in which foreign investment is either totally prohibited,<sup>4</sup> or limited to certain

<sup>2</sup> *Id.* art. 6.

<sup>3</sup> General Law on Business Corporations, Diario Oficial, Aug. 4, 1934.

<sup>4</sup> Certain activities are reserved exclusively for the State: (a) Petroleum and other hydrocarbons;

- (b) Basic petrochemicals;
- (c) Exploitation of radioactive minerals and the generation of nuclear energy;
- (d) Mining in cases to which the relative law refers;
- (e) Electricity;
- (f) Railroads;
- (g) Telegraphic and wireless communications; and
- (h) Other activities established in specific laws.

The following activities are reserved exclusively for Mexicans or for Mexican companies with an exclusion-of-foreigners clause in their corporate by-laws:

- (a) Radio and television;
- (b) Urban and interurban automotive transportation and federal highways transport;
- (c) Domestic air and maritime transportation;
- (d) Exploitation of forestry resources;

capital proportions.<sup>5</sup> The general principle established in the Law is that foreign investment should limit its participation in the capital of Mexican business enterprises to 49 percent. However, the Law authorizes the National Commission of Foreign Investment to grant, in exceptional cases and taking into consideration the changing conditions of the economy and the needs of the country, greater participation percentages in certain geographic areas or in certain economic activities, provided that the various laws or regulations have not previously established a participation percentage.

There will be sufficient flexibility so that, in certain cases, foreign investment may be allowed on a majority or total basis. An example of these special cases could be those companies engaged in bond operations in the country, which in accordance with a general resolution made by the Commission, may have up to 100 percent foreign capital. Another example in which foreign investment would be allowed on a majority basis, in accordance with official declarations, would be those companies established in certain specific geographic areas which are engaged principally in export activities. Important to such determinations are the provisions of article 13 of the Law which expressly contains the requirements that the National Commission on Foreign Investments shall take into account in approving foreign investment and in establishing the percentages and conditions that will apply.<sup>6</sup>

(e) Gas distribution; and

(f) Others established in specific laws, or regulations issued by the Federal Executive.

Foreign Investment Law, *supra* note 1, art. 4.

<sup>5</sup> Foreign investors may participate in the capital of enterprises engaged in the following activities, in the indicated maximum capital proportions:

Exploitation of national reserves of mineral substances subject to special concessions—34%;

Secondary products of the petrochemical industry—40%;

Manufacturers of parts for automotive vehicles—40%;

Exploitation of utilization of mineral substances subject to regular concessions—49%;

All other activities unless the National Commission for Foreign Investment establishes a different percentage—49%.

*Id.* art. 5.

<sup>6</sup> The Commission shall take into consideration the following criteria and characteristics of the proposed foreign investment:

I. To complement local investment;

II. Not to displace Mexican enterprises which are operating satisfactorily nor to invest in activities adequately covered by those enterprises;

III. Its positive effect on the balance of payment and, particularly, on the increase in exports;

IV. Its effect on employment, taking into consideration the occupational level that

On the other hand, article 8 requires that foreigners, as well as Mexican enterprises whose capital or administration is controlled by foreigners wishing to acquire more than 25 percent of the capital stock or more than 49 percent of the fixed assets of already established business enterprises, must obtain an authorization from the Ministry of Industry and Commerce. The leasing of a business enterprise or of the principal assets used in carrying out its activities will be treated as though it were a purchase of assets. Authorization from the Ministry will also be required when the administration of an already established business enterprise is transferred to foreign investors or when such investors under any circumstances obtain the right to determine the management of the enterprise. The authorizations shall be granted when the National Commission for Foreign Investments deems it advisable for reasons of national interest. Any actions carried out without the aforementioned authorization shall be null and void.

The Commission may, in those cases in which it deems it advisable, grant a preferential right for Mexican investors to acquire already existing business enterprises. This right shall be granted for a term not to exceed 90 days starting from the date on which the terms of the offer are made known. The period may be extended for another 90 days at the request of any interested party.<sup>7</sup>

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it generates and the remuneration of labor;

V. The employment and training of technicians and administrative personnel of Mexican nationality;

VI. The incorporation of national goods and components in the manufacture of its products;

VII. The extent to which it finances its operations with resources from abroad;

VIII. The diversification of the investment sources and the necessity of promoting regional and sub-regional integration in the Latin American area;

IX. Its contribution to the development of zones or areas of relatively lower economic development;

X. Not to take monopolistic positions in the national market;

XI. The capital structure of the economic activity;

XII. The technological contribution and assistance in research and development of the technology of the country;

XIII. Its effect on price levels and the quality of production;

XIV. To preserve the social and cultural values of the country;

XV. The importance of the activity within the national economy;

XVI. The identification of the foreign investor with the interests of the country and his connection with centers of economic decision abroad;

XVII. In general, the extent to which it collaborates in the achievement of the goals and policies of national development.

*Id.* art. 13.

<sup>7</sup> *Id.* art. 9.

Article 25 requires that the shares or any other instruments representing the capital of business enterprises must be nominative when such are owned by foreign investors. Instruments representing shares in the capital of Mexican business enterprises which are owned by Mexican investors must also be nominative when so required by specific laws or regulations or by the resolutions of the Commission. Bearer securities may not be acquired by foreign investors without prior approval of the Commission and, in such cases, the securities shall be converted into nominative shares.

Articles 18 through 22 establish a procedure by which foreign individuals or companies and Mexican companies whose charters do not exclude foreign investors may acquire the right to use and enjoy real estate located within 100 kilometers of international borders and 50 kilometers of the seacoast, where such use involves industrial or tourism activities. The Ministry of Foreign Relations, when it deems it advisable and in accordance with criteria established by the Commission, may authorize banking institutions to acquire as trustees the domain of such real estate, with the purpose of permitting the use and exploitation of the property by foreign beneficiaries of the trust or by Mexican companies whose charters do not exclude foreigners. The banking institutions acting as trustees may issue nominative and nonamortizable real estate participation certificates for the purposes of such trusts.<sup>8</sup> The foreign beneficiaries of the trust or holders of participation certificates will have the right to use the real estate and to receive any income realized by the trustee from its use or exploitation as well as the net proceeds from the sale of the property by the trustee to persons legally entitled to acquire it.<sup>9</sup> While the duration of the trusts may not exceed 30 years, lease contracts entered into by the trustee are limited to terms of 10 years or less.<sup>10</sup>

Also incorporated in this Law are the articles of the Constitution and other regulations which prohibit foreign companies from acquiring ownership of land and water in any part of the country or from obtaining concessions for the exploitation of water resources. Foreign individuals may acquire such property when authorized by the Ministry of Foreign Relations, provided that the individual agrees to consider himself as a Mexican citizen with respect to the prop-

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<sup>8</sup> *Id.* arts. 18, 19.

<sup>9</sup> *Id.* art. 21.

<sup>10</sup> *Id.* art. 20.

erty, agreeing not to invoke the protection of his government with respect to his investment under penalty in case of noncompliance of forfeiting for the benefit of the nation the properties which he may have acquired.<sup>11</sup>

On November 5, 1975, the National Commission on Foreign Investment issued eight general resolutions which contained criteria regarding the construction and application of the Law. One such resolution refers to increases in the capital of a corporation which existed before the Law was enacted. Such a corporation is authorized to increase its capital stock provided that the same proportions between Mexican and foreign capital are maintained. Again, in the case of capital increases, foreign investors must maintain individually at least the same proportion between the par value of their investment and the authorized capital of the issuing company.

The foregoing constitutes a brief summary of the Mexican Law on Foreign Investments. This Law is closely linked to the most important aims of our country, as it is based on expectations of growth and progress in the development of a national and independent economy. We do not wish to be the employees or the agents of foreign investors because that would be contrary to our economic and political sovereignty. We desire and need foreign investments under the terms of equality and justice. We desire and need foreign investments to contribute to the solution of our big national problems. Mexico has inherited from the civil wars of the last century a system of liberal democracy which dignifies individual freedom. But now, due to the demographic explosion and to the incorporation of great masses of the population formerly excluded from the benefit of civilization and progress, we are obliged to find adequate instruments to continue to maintain the principles and freedoms of our liberal democracy as we move into the wider context of a social democracy. It is my belief that under the above mentioned rules foreign investment can continue to contribute to our mutual benefit.

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<sup>11</sup> *Id.* art. 7.