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## Mexico's Border Industrial Program: Legal Guidelines for the Foreign Investor

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## Mexico's Border Industrial Program: Legal Guidelines for the Foreign Investor

### Keywords

Collective Bargaining, Comparative Law, Human Rights Law, Labor, Women, Economic Development, International Trade

## MEXICO'S BORDER INDUSTRIAL PROGRAM: LEGAL GUIDELINES FOR THE FOREIGN INVESTOR

The border between the United States and Mexico stretches approximately 2600 kilometers.<sup>1</sup> It includes the boundaries of four states on the U.S. side and six on the Mexican side. Several large cities are located on the border with a total population reaching far into the millions.<sup>2</sup> To most Americans, the border area has been simply a tantalizing taste of tequila, trinkets, and honky-tonks. For the American businessman, however, the area has come to represent more than this, for along the border an important economic phenomenon has quietly been developing. This phenomenon, known as the *Programa Fronteriza de Industria* (hereinafter referred to as PFI),<sup>3</sup> allows for a unique combination of factors of production between the two countries. Essentially, it permits the duty-free importation of component parts into Mexico, where they can be assembled by the plentiful labor supply of Mexico and then exported back to the U.S. with a duty charged on the value added in Mexico.

### I. BACKGROUND OF THE PROGRAM

The impetus behind the PFI stems from the dismal economic situation that prevailed in the border towns during the sixties. Some figures estimated unemployment as high as fifty percent.<sup>4</sup> On the U.S. side, unemployment has also been a traditional problem, with one study placing unemployment rates as high as fifteen percent in some areas.<sup>5</sup>

The high unemployment rates on the Mexican side were directly related to the large influx of people that had migrated from the interior. The reasons for this migration were twofold. First, the migration to the border towns was a result of the transition of the Mexican

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1. Mexico's Border Program, no date, at 10 (unpublished material provided by the Mexican Chamber of Commerce of the United States).

2. Some of the Mexican border towns involved and their U.S. counterparts include: Tijuana—San Diego, Mexicali—El Centro, Nogales—Nogales, Palomas—Deming, Ciudad Juarez—El Paso, Piedras Negras—Eagle Pass, Nuevo Laredo—Laredo, Reynosa—McAllen, Matamoros—Brownsville. Hunt, *Industrial Development on the Mexican Border*, BUS. REV., February 1970, at 9 [hereinafter cited as Hunt].

3. A number of names are used to refer to the border program including "Programa de Industrializacion Fronteriza" and simply the "Border Program."

4. Hunt states that in 1968 of the 126,000 man work force in Ciudad Juarez, 15 percent were unemployed; in Nogales it was estimated that 50 percent were unemployed. Hunt, *supra* note 2, at 5.

5. Robert R. Nathan Associates, Inc., *Industrial and Employment Potential of the U.S. Mexico Border*, Dec. 1968 (prepared for the Economic Development Administration, U.S. Dept. of Commerce) at 76, 218, 222, 240.

economy from a predominantly agrarian to an industrialized economy. "This transition has generated an increase in the actual as well as potentially available industrial labor force."<sup>6</sup> Secondly, many Mexicans were attracted to the area by the hope of obtaining permits to work in the U.S. Bracero Program, which allowed Mexican farm labor to enter the U.S. temporarily to help with the harvest.<sup>7</sup> This program, formalized by a 1951 bilateral agreement between the U.S. and Mexico, attracted a great number of Mexicans.<sup>8</sup> In 1965 the Bracero Program was terminated<sup>9</sup> and the waves of Mexican workers washed against the legal dam which had been erected.<sup>10</sup> In 1968, hundreds of peasants from the interior were still arriving, enticed by the prospect of jobs in the U.S.<sup>11</sup> Some did not know the Bracero program had been terminated.<sup>12</sup>

The first attempt by the Mexican government to do something about the depressed economy of the North was Programa Nacional Fronteriza in 1962.<sup>13</sup> PRONAF, as it was commonly known, "was directed toward the tourist dollar, [but] its underlying objective was to enhance the general economic condition of the border area."<sup>14</sup> Unlike the later PFI, it was not designed to encourage foreign investment but was aimed at Mexican national development.<sup>15</sup> The threefold objectives of PRONAF were:

1. to encourage Mexican industrialization on the border;
2. to subsidize the transportation of Mexican manufactured goods to the northern areas by providing tax credits and freight rebates; and
3. to fund commercial and tourist centers in the border area.<sup>16</sup>

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6. Taylor & Bond, *Mexican Border Industrialization*, 16 MSU BUS. TOPICS 34 (1968) [hereinafter cited as Taylor & Bond].

7. *Id.* at 34. For a general discussion of the Bracero program, see Walker, *Border Industries with a Mexican Accent*, 4 COLUM. J. WORLD BUS. 25 (1969) [hereinafter cited as Walker].

8. Estimates differ as to the maximum number of Mexicans that participated at one time. One source puts the figure at 185,000. BAERRESEN, *THE BORDER INDUSTRIALIZATION PROGRAM OF MEXICO* 3 (1971) [hereinafter cited as BAERRESEN]. Another source estimates the total as high as 450,000. WRIGHT, *FOREIGN ENTERPRISE IN MEXICO—LAWS AND POLICIES* 192 (1971) [hereinafter cited as WRIGHT].

9. Act of Dec. 13, 1963, Pub. L. No. 88-203, 77 Stat. 363.

10. Mexico's Border Program, *supra* note 1, at 1.

11. U.S. NEWS AND WORLD REPORT, July 1, 1968, at 79.

12. See Jackson, *The Border Industrialization Program of Northern Mexico, Fall 1968*, at 18 (found in Selected Reprints of Academic Papers on Mexico's Border Industrialization Program, collected by the McAllen Chamber of Commerce, McAllen, Texas) [hereinafter cited as Jackson].

13. BAERRESEN, *supra* note 8, at 2.

14. Jackson, *supra* note 12, at 2.

15. See Cowan, *Mexican Border Industrialization Program*, 8 COMP. J. REV. 17, 18 (1971).

16. *Id.* at 18.

Although a number of civic improvements<sup>17</sup> and increased tourist traffic<sup>18</sup> and expenditures<sup>19</sup> are attributed to PRONAF, the program did not succeed in solving the serious unemployment problem. Therefore, the Mexican government, encouraged by the success of other countries in attracting "factories specializing in assembling and processing U.S. products for the U.S. market,"<sup>20</sup> began studying the possibility of allowing American manufacturers to operate on the Mexican side of the border. Finally, in May 1965, the President of Mexico in his Report to the Nation announced the *Programa de Industrialización Fronteriza* — the border industrial program.<sup>21</sup>

## II. FRAMEWORK OF PFI

### A. *The Legal Provisions*

The legal basis for the PFI is relatively simple. It allows foreign firms to import component parts duty-free to be assembled or finished by cheap labor in the foreign country.<sup>22</sup> These finished products can then be shipped back to the U.S., or to any other foreign country, with a duty only on the value added in Mexico. The main concern by the Mexican government is keeping these products from finding their way into the Mexican economy where they will compete with domestically produced goods.<sup>23</sup>

The legal provisions which established PFI remained sketchy for a number of years.<sup>24</sup> Although the procedures for the processing of applications from companies wanting to participate in the border

17. Baerresen lists such things as the improved appearance of border cities, modern entry gates, shopping centers and additional schools. BAERRESEN, *supra* note 8, at 2.

18. Between 1965 and 1967 tourist traffic into Mexico increased 11 percent. In 1968, the year of the Olympics in Mexico, tourism increased 18 percent. Hunt, *supra* note 2, at 4.

19. From 1961 to the end of 1966 tourist expenditures rose 48 percent to \$540 million. WRIGHT, *supra* note 8, at 192.

20. BAERRESEN, *supra* note 8, at 3.

21. Hunt, *supra* note 2, at 5.

22. Taylor & Bond, *supra* note 6, at 35.

23. Trevino, Border Assembly Operations, April 1969, at 31 (found in Selected Reprints of Articles on Mexico's Border Industrial Program, collected by the McAllen Chamber of Commerce, McAllen, Texas) [hereinafter cited as Trevino].

24. Probably the reason for the uncertain state of the law has been the desire by the government to handle each application individually. Such a procedure allows the government to evaluate each application on the basis of the "product to be assembled, the proportion of imported raw materials and component parts to be imported into Mexico, and the estimated number of Mexican laborers to be employed." Taylor & Bond, *supra* note 6, at 36. Another source suggests that the criteria considered by the Mexican officials includes: 1) the export industry may not manufacture goods already exported by Mexico; 2) the plant established must be labor-intensive; 3) the wages paid to workers must be in accordance with minimum wages in force; and 4) the factory must be built on an adequate site. *The Mexican Export Industries*, 3 BANK OF LONDON AND SOUTH AMERICAN REV. 624 (1969).

program were established in two inter-secretarial agreements in June 1966,<sup>25</sup> it was not until March 17, 1971, that the PFI was codified as a specific Mexican law.<sup>26</sup> Even this official document, which sets forth "the program's function, rules and the method of administration,"<sup>27</sup> does not include all the Mexican regulations relating to PFI. Many of the regulations are found in other sections of the Mexican code.<sup>28</sup> The following is a summary of the basic Mexican regulations relating to PFI:

1. Parties must be registered with the Ministries of Finance and Public Credit and Industry and Commerce.<sup>29</sup>
2. Companies who have obtained the proper authorization may temporarily import raw materials, machinery, parts, containers, etc., provided that 100 percent of all imports are eventually returned to their place of origin.<sup>30</sup>
3. An assembly operation does not require the assembling company established at the border or elsewhere to acquire title to the foreign source raw materials in order to import, process and re-export the same.<sup>31</sup>
4. The Department of Industry and Commerce will set up controls in the identification of raw materials and the finished materials.<sup>32</sup>
5. A twelve-month time limit, which may be renewed, is placed on imports of foreign products.<sup>33</sup>
6. Article 325 of the Customs Code provides for the posting of bonds to guarantee customs duties in the case of temporary importations.<sup>34</sup>
7. Assembled products will be permitted to be re-exported free of duties, provided that the imported articles have never been removed from the fiscal enclave. Raw materials and articles of a national or nationalized nature which are added are subject to duties.<sup>35</sup>
8. Customs clearance may take place at the border, at the company's plant or at an industrial park.<sup>36</sup>
9. Industries which apply for permission to establish themselves in bor-

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25. No. 164 Hacienda (June 1, 1966) and No. 4132 Industria y Comercio (June 20, 1966). Cited in Hunt, *supra* note 2, at 4.

26. Art. 321, para. 3, Customs Code, as cited in Mexican Border Industrialization Program, 1971 (available from the Secretaria de Industria y Comercio); also cited in Trevino, *supra* note 23, at 32; and Cowan, *supra* note 15, at 25.

27. BAERRESEN, *supra* note 8, at xv.

28. Although there has been some suggestion that the lack of a clear legal basis may cause concern to investors, the latest figures do not bear this out. In 1973, with 350 companies participating, \$600 million worth of products were exported from the border area. Bolin, *Border Industry Facts for 1973*, MEXICAN AM. REV., Sept. 1973, at 14.

29. Art. 321, para. 3, sub art. 5, Customs Code, *supra* note 26.

30. *Id.* at art. 321, para. 3, sub art. 7.

31. *Id.* at art. 324.

32. *Id.* at art. 322.

33. *Id.* at art. 321, para. 3, sub art. 7.

34. Trevino, *supra* note 23, at 32.

35. Arts. 393, 334, Customs Code, *supra* note 26.

36. *Id.* at art. 321, para. 3, sub art. 12.

der towns shall ipso facto be considered as being subject to the tax system for all purposes connected with their operation.<sup>37</sup>

10. Since it is impossible to fix general rules for all industries participating, each case will receive individual evaluation and specific control regulations.<sup>38</sup>

No change in U.S. laws was necessary, as the legal basis was found in Section 807 of the U.S. Tariff Schedules, which states:

Articles assembled abroad in whole or in part of fabricated components, the products of the United States which (a) were exported in condition ready for assembly without further fabrication . . . . (c) have not been advanced in value or improved in condition abroad except by being assembled and except by operations incidental to the assembly process such as cleaning, lubricating, and painting . . . . A duty upon the full value of the imported article, less the cost on value of such products of the United States.<sup>39</sup>

A similar section allows for the same treatment of metal component parts to be assembled outside the United States.<sup>40</sup> Together, these sections make possible the re-importation of American made products with a duty only on the value added. It should be noted, however, that value added does not necessarily mean only the cost of Mexican labor. H. E. Outlaw, U.S. district director for customs at Laredo, points out: "Value is added whenever the nature of the product is altered. When a Mexican worker adds a buttonhole, for example, the whole value of the article changes, and it becomes subject to higher duties."<sup>41</sup> This misunderstanding caused a Dallas firm to assemble television cabinets which were later faced with prohibitive duties at the border.<sup>42</sup> Similar difficulties can probably be avoided by obtaining advance clearance from the particular customs district involved.<sup>43</sup>

#### B. *Establishing a Company Under the PFI*

Assuming that the American businessman has decided to establish an assembly or finishing plant in one of the border towns under the PFI, the following discussion will focus on the procedures which should be followed in receiving preliminary approval, establishing the corporation and obtaining final approval.

The potential investor must first obtain the preliminary ap-

37. *Id.* at arts. 22, 47, 471-81.

38. *Id.* at arts. 350(1), 352, 353, 356.

39. 19 U.S.C. 807 (1963).

40. 19 U.S.C. 806.30 (1963). The latest statistics indicate that "imports from Mexico under Section 806.30 are fairly negligible, about \$10 million in 1971," (unpublished material furnished by the U.S. Embassy in Mexico, June 30, 1972).

41. *BUSINESS WEEK*, Dec. 2, 1967, at 122.

42. *Id.*

43. See Walker, *supra* note 7, at 30.

proval of the Mexican government for the establishment of the plant. This prior approval is obtained by completing form EF-14, and submitting it to the Ministry of Industry and Commerce with a duplicate copy sent to the Finance and Public Credit Department.<sup>44</sup> In general, the data required in this form includes the name of the corporation and its location and address, the corporate capital structure and investment program, the product or products to be processed, the processes to be carried out with the products and the probable labor to be employed.<sup>45</sup> Once this application has been approved, operation of the plant should begin within 120 days, as delay will necessitate an application for extension.<sup>46</sup>

Once preliminary approval is obtained, temporary importation may begin upon completion of forms EF-16 and EF-17.<sup>47</sup> The first form makes possible the temporary importation of raw materials and component parts, while the latter allows for the temporary importation of machinery and equipment.<sup>48</sup> Both forms must be filled out in six copies and should be submitted to the same address as form EF-14.<sup>49</sup>

Preliminary approval also means that another important step, the establishment of the business organization, may be taken. The organization may take the form of either a branch or subsidiary. The subsidiary is generally favored because of several disadvantages common to branches under Mexican law. For example, branches cannot own real estate, take longer to form and are not well regarded by Mexican authorities.<sup>50</sup> Conversely, subsidiaries take less time to form, receive tax advantages and are regarded as nationals under Mexican law.<sup>51</sup> Throughout the remaining discussion, the assumption is that the form of association will be a subsidiary formed according to Mexican law.

Mexican law provides for five forms of association:

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44. Form EF-14 is available from the Ministry of Industry & Commerce, General Bureau of Industry, Avenida Cuauhtemoc No. 80, Mexico 7, D.F.

45. Mexican Border Industrialization Program, *supra* note 26, at 17.

46. See Procedures for Starting an Assembly Plant Along the Northern Border of Mexico, June 14, 1972 (unpublished material available from the San Diego Chamber of Commerce) [hereinafter cited as Procedures].

47. Both these forms are available from the same address as given for form EF-14, *supra* note 44.

48. Mexican Border Industrialization Program, *supra* note 26, at 22, 23.

49. *Id.*

50. BUSINESS INTERNATIONAL CORP., INVESTING, LICENSING AND TRADING CONDITIONS ABROAD—MEXICO, 1973, at 7 [hereinafter cited as INVESTING—MEXICO].

51. U.S. DEPT. OF COMMERCE, OVERSEAS BUSINESS REPORT 72-027: ESTABLISHING A BUSINESS IN MEXICO 9 (July 1972) [hereinafter cited as OVERSEAS BUSINESS REPORT].



1. *Sociedad en nombre colectivo*;
2. *Sociedad en comandita simple*;
3. *Sociedad en comandita por acciones*;
4. *Sociedad anonima*; and
5. *Sociedad de responsabilidad limitada*.<sup>52</sup>

Of these five, the one most recommended for border industry purposes is the *Sociedad anonima*, or corporation. The corporation offers the advantages of limited liability and relative freedom of transfer of ownership interests, and is the only form allowing a large number of persons to participate.<sup>53</sup> The corporation must consist of at least five shareholders and, once established, becomes a legal entity with juridical personality.<sup>54</sup> Although the law establishes minimum requirements, a certain amount of flexibility exists so that the parties may structure the corporation to meet their needs.<sup>55</sup>

If the decision is made to form a corporation, the articles of association must be drafted. This instrument must contain basically the same information as is required by U.S. law for incorporation.<sup>56</sup> The next step is to apply to the Ministry of Foreign Relations for a permit to form a Mexican company. This is required by the emergency decree of 1944, and must be inserted in the articles of association by the notary.<sup>57</sup> It is recommended that this procedure be handled by a lawyer in Mexico City within ten to fifteen days after incorporation.<sup>58</sup> The articles of association must also contain the Calvo Clause, which requires that "any foreigner who acquires shares

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52. For a good discussion of the forms of association see *id.*

53. WRIGHT, *supra* note 8, at 219.

54. *Id.* at 220.

55. *Id.*

56. *Id.* at 221. Specifically, it must include:

1. Name of the company;
2. Operation period;
3. Address;
4. Purpose;
5. Stocks value;
6. Board of Directors;
7. Name, address, place and date of birth, and occupation of the stockholders;
8. Manner in which the stockholders' capital is to be subscribed;
9. Company's vigilance;
10. Date for stockholders' general meeting;
11. Corporate year;
12. Inventories and balances;
13. Legal reserves, profits and losses;
14. Plans for dissolution and liquidation of the company;
15. Transitory clauses.

See Procedures, *supra* note 46, at 1.

57. WRIGHT, *supra* note 8, at 221.

58. Procedures, *supra* note 46, at 1.

in the corporation agrees that he will be considered as a Mexican with respect to his shares and that he will not invoke the diplomatic protection of his home government."<sup>59</sup> Next, the articles of association should be presented to a notary, who will keep the original in the bound books of the notary and will issue certified copies to the corporation.<sup>60</sup>

After being constituted with the notary, a petition together with the articles of association should be filed with the Department of Public Property Registry.<sup>61</sup> A hearing will be held, although in many cases it will be waived, and "the judicial order . . . issued and the recordation effected as a matter of routine."<sup>62</sup>

After the corporation has been established and the necessary registrations made, final approval should be secured by filing form EF-15<sup>63</sup> with the Ministry of Industry and Commerce. This form, though similar to EF-14, requires more data, including the amount of investment, a charter of the corporation (if possible), copies of registration with various agencies and information relating to raw materials and labor, processing costs and productive capacity.<sup>64</sup>

A final form, EF-18, must be filed quarterly with the Ministry of Industry and Commerce.<sup>65</sup> This form, requesting information on lists of imports and exports, cost of processing, bonds, shrinkage and waste, customs control and taxes, is to fulfill the interest of the Mexican government in the development of assembly plants under PFI.

The procedure is finally completed by registration with several agencies, including:

1. The Federal Tax Collector's Office;
2. Social Security;
3. Health Department;<sup>66</sup>
4. State Commercial Tax Department;
5. Municipal Treasury Department;
6. Public Department of Labor;
7. National Importers and Exporters of the Mexican Republic at the Mexican Institute of Foreign Trade;
8. General Statistics Division of the Directory of Industry and Commerce Department; and
9. National Chamber of Industry and the Chamber of Commerce.<sup>67</sup>

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59. WRIGHT, *supra* note 8, at 221.

60. *Id.* at 220.

61. Procedures, *supra* note 46, at 1.

62. WRIGHT, *supra* note 8, at 222.

63. This form is available from the same address as form EF-14, *supra* note 44.

See Mexican Border Industrialization Program, *supra* note 26, at 3.

64. *Id.* at 19.

65. *Id.* at 24.

66. One source indicates that a permit must be obtained from the Ministry of Public Health approving the company's premises. Cowan, *supra* note 15, at 23.

67. Procedures, *supra* note 46, at 2.

To the American businessman, the procedure which has just been described may seem a bit confusing. Therefore, to help the prospective investor, the Mexican government has established quasi-official committees which are located in certain border towns.<sup>68</sup> These committees, known as *Comites Consultivos de Formento Industrial Para la Zona Fronteriza Norte*, have as their stated purpose the responsibility "to assist the potential investor, to forward the proper applications for permits, and to submit along with the firm's papers an opinion, based on the information rendered by the applying firm, as to the firm's suitability in regard to the purposes of the program."<sup>69</sup> Specifically, the *Comites* will:

1. Forward for approval studies based on data supplied by the applicant;
2. Forward similar studies for the importation of raw materials, machinery, etc.;
3. Forward special applications for extraordinary imports;
4. Submit applications when immigration factors are involved; and
5. Submit subsequent applications for additional raw materials and machinery.<sup>70</sup>

In addition to the *Comites*, Chambers of Commerce on both sides of the border can be extremely helpful in "moving to Mexico."<sup>71</sup> Several of the U.S. border towns have formed industrial teams which, in conjunction with similar organizations on the Mexican side, provide the potential investor with guidance on such subjects as electricity, legal assistance, housing, and taxes.<sup>72</sup>

### C. *Acquiring Land and Buildings*

Upon the decision to move to Mexico, the investor's consideration must turn to obtaining suitable land and building facilities for the assembly plant. In this regard it would seem that a major obstacle exists, because Article 27 of the Mexican Constitution prohibits:

The acquisition by foreigners, including foreign companies, of title to land or bodies of water within the so-called prohibited zone—that is, within 100 kilometers [about 62 miles] of the land borders or 50 kilometers [about 31 miles] of the seacoast. . . .<sup>73</sup>

Furthermore, laws and regulations, drafted from a concern for self-defense, make foreign ownership of interest in any companies, that

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68. One source says these *Comites* are located in Ciudad Juarez, Mexico and in Mexicali, Mexico.

69. Jackson, *supra* note 12, at 8.

70. Cowan, *supra* note 15, at 27.

71. Jackson, *supra* note 15, at 10.

72. See generally The El Paso—Juarez Twin Plant Concept Handbook—1973-1974 (available from the El Paso Industrial Development Corp. and the El Paso Chamber of Commerce) [hereinafter cited as El Paso—Juarez Handbook].

73. WRIGHT, *supra* note 8, at 115.

own land in the prohibited zone, impossible.<sup>74</sup> The drafters of the 1917 Constitution, who had just freed themselves from Spanish domination, took steps to prevent any future creeping domination. The prohibition, though openly evaded during much of Mexican history, continues on the books to our time.

The American businessman would be well advised not to violate this prohibition, as the penalties can be severe. For example, any acts or contracts can be held void, and certificates or interests can be declared "without any value."<sup>75</sup> In addition, the emergency decree of 1944 sanctions the seizure of property by the government for a violation.<sup>76</sup> Penalties of imprisonment, fines (up to 10,000 pesos) and penalties against consuls, notaries and other officials for authorizing a prohibited instrument may be imposed.<sup>77</sup>

The Mexican government, realizing the need for foreign industries to acquire land in order to operate, has made several methods of acquisition possible. The most common way of holding land is by a lease.<sup>78</sup> Because this lease is usually for ten years or less, it does not violate the emergency decree of 1944, which requires a permit for land holdings longer than ten years.<sup>79</sup>

An alternative means of acquiring land is by placing it in trust. This was made possible by a Presidential Decree of April 30, 1971, which allows a foreign company to acquire the property which is then placed in trust in a Mexican bank.<sup>80</sup> Applications for such a trust must be made to the Mexican Department of Foreign Relations, and the Mexican Inter-Secretarial Commission.<sup>81</sup> Under a trust plan, land may be held up to thirty years and must be sold to a Mexican entity at the end of the trust period.<sup>82</sup>

Some confusion exists regarding the ownership of buildings. The implementing law of Article 17 seems to extend the prohibition to "lands and their accessions," but since "accession" is not clearly defined in Mexican law, the Ministry of Foreign Relations has permitted foreign-owned companies to acquire buildings in the prohibited zone.<sup>83</sup> As is the case with land, the most popular means of

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74. *Id.*

75. *Id.* at 116.

76. *Id.*

77. *Id.*

78. Quick Facts About the El Paso — Juarez International Twin Plant Program, March 1973 (unpublished material furnished by the El Paso Industrial Development Corporation) [hereinafter cited as Quick Facts].

79. See WRIGHT, *supra* note 8, at 117.

80. See OVERSEAS BUSINESS REPORT, *supra* note 51, at 7.

81. El Paso—Juarez Handbook, *supra* note 72, sec. 4:40, at 1.

82. OVERSEAS BUSINESS REPORT, *supra* note 51, at 7.

83. WRIGHT, *supra* note 8, at 118.

acquiring buildings is by lease. One of the significant developments in this regard has been the growth of industrial parks in participating Mexican towns.<sup>84</sup> Developers will build "shell or turn-key facilities to the tenants' specifications."<sup>85</sup> The cost of leasing these facilities ranges from \$.10 to \$1.50 per square foot, depending on such factors as age of the building, type of construction and interior finishing.<sup>86</sup> A further advantage of industrial parks is that they are located within the bonded manufacturing zone, thus making the resolution of bonding problems somewhat easier.<sup>87</sup>

The businessman will welcome the fact that expropriation is low on the list of investment hazards in Mexico.<sup>88</sup> In fact, the alien in Mexico is protected by Article 27 of the constitution which provides:

private property shall not be expropriated except for reasons of public utility and by means of indemnification. . . .<sup>89</sup>

### III. OTHER FACTORS TO CONSIDER

#### A. Labor

The major factor making PFI attractive to the foreign investor is the availability of productive labor at a comparatively low cost. This section focuses on this factor, and deals specifically with minimum wages, fringe benefits, labor contracts and dismissal of workers.

Mexican minimum wages, which are established biennially in all regions or zones,<sup>90</sup> are determined by a tripartite group consisting of a chairman and six representatives from labor and six from business.<sup>91</sup> These determinations can, however, be reviewed or revised by a federal commission in Mexico City.<sup>92</sup> The rates for both skilled and unskilled labor are determined by the cost of living, the general economic conditions and the needs of companies.<sup>93</sup> It should be noted that these minimum requirements can often be increased by as much as 25 percent by negotiated collective labor contracts.<sup>94</sup>

During the past few years, minimum wages have tended to rise sharply all over Mexico. For the period 1970-71, minimum wages were

84. Steiner, *The Mexican Border Industrialization Program*, TEXAS BUS. REV., July 1971, at 147 [hereinafter cited as Steiner].

85. Quick Facts, *supra* note 78, at 1.

86. El Paso—Juarez Handbook, *supra* note 72, sec. 3.00, at 1.

87. See Steiner, *supra* note 84, at 147.

88. OVERSEAS BUSINESS REPORT, *supra* note 51, at 7.

89. *Id.*

90. BAERRESEN, *supra* note 8, at 23. Another source says there are 109 zones; INVESTING—MEXICO, *supra* note 50, at 18. Still another source states that the rates are determined by the states; Taylor & Bond, *supra* note 6, at 38.

91. OVERSEAS BUSINESS REPORT, *supra* note 51, at 13.

92. BAERRESEN, *supra* note 8, at 23.

93. *Id.*

94. See INVESTING—MEXICO, *supra* note 50, at 18.

increased 15.5 percent, while in 1972-73 they were upped an average of 16-20 percent.<sup>95</sup> In the border area, the average increase from 1968-69 to 1970-71 was 13.7 percent.<sup>96</sup> For 1974-75, the projected increase for all of Mexico is 15-20 percent.<sup>97</sup> There is, of course, political pressure by local communities to keep minimum wages low, and thus gain an advantage, but the local commissions are aware of this and strive to prevent "adjustments that significantly alter the present pattern of wage levels among competing areas."<sup>98</sup> Some comparative minimum wages which an investor presently faces are:

1. Ciudad-Juarez—42.30 pesos per day;<sup>99</sup>
2. Reynosa—33.75 pesos per day;<sup>100</sup>
3. Tijuana—62.30 pesos per day;<sup>101</sup> and
4. Nuevo Laredo—39.85 pesos per day.<sup>102</sup>

Compared with other countries where programs similar to PFI operate, Mexico pays relatively high minimum wages. For example, Mexico pays an average of 28 cents to 46 cents (U.S.) per hour, whereas Hong Kong pays 30 cents, Japan 54 cents, Korea 13 cents and Taiwan 14 cents.<sup>103</sup>

The foreign investor should also consider that the Mexican worker must be paid overtime for any work done beyond the legal requirement. Male workers receive double pay for overtime beyond eight hours per day, and female workers receive triple pay.<sup>104</sup> A new law, passed in 1970, obligates employers to pay triple time for work beyond nine hours of overtime.<sup>105</sup> Any work done on Sundays must be compensated at 25 percent above the daily wage.<sup>106</sup>

95. *Id.*

96. BAERRESEN, *supra* note 8, at 24.

97. INVESTING—MEXICO, *supra* note 50, at 18.

98. BAERRESEN, *supra* note 8, at 26.

99. El Paso—Juarez Handbook, *supra* note 72, sec. 4:10, at 1. These minimum wages do not include fringe benefits. One dollar = 12.49 pesos.

100. Mexico's Border Industrialization Program for U.S. Manufacturers at Reynosa, Tamps., Mexico, no date, at 2 (unpublished material furnished by the McAllen Chamber of Commerce) [hereinafter cited as Reynosa].

101. Procedures, *supra* note 46, at 4.

102. Covarrubias, Memorandum Regarding Mexican Border Assembly Operations, March 25, 1972, at 1 (unpublished material available from the Laredo Chamber of Commerce) [hereinafter cited as Covarrubias].

103. BAERRESEN, *supra* note 8, at 24. It should be noted that all of these minimum wages are before fringe benefits.

104. Steiner, *supra* note 84, at 146. One source, however, states that women cannot work overtime and "if this prohibition is violated, overtime should be paid two hundred per cent more than salary payable for the hours of the working shift." Procedures, *supra* note 46, at 5.

105. Steiner, *supra* note 84, at 146.

106. INVESTING—MEXICO, *supra* note 50, at 18.

In estimating costs of labor, the border investor should take into consideration not only minimum wage, but also fringe benefits which may amount to as much as 50-60 percent of the minimum wage.<sup>107</sup> Bonuses are one of the major fringe benefits accruing to the Mexican worker. For example, a worker on vacation must be paid his daily salary plus a 25 percent bonus.<sup>108</sup> At Christmas, a bonus of fifteen days salary must be paid before December 20th.<sup>109</sup>

Besides bonuses, Mexican law guarantees the worker a certain amount of time off from work with pay. The Mexican laborer is given every seventh day off with pay.<sup>110</sup> After a year's work, he is guaranteed six days of paid vacation, which must be increased by two days for each additional year of employment up to a total of twelve days.<sup>111</sup> Finally, the Mexican laborer is entitled to five paid holidays every year, and a sixth every six years on Inauguration Day.<sup>112</sup>

Social security is another fringe benefit which must be included in the total cost. The Mexican social security system covers such items as:

accidents and illnesses (10% salary up to seventy-two weeks), non-occupational diseases and paid maternity leave, day-time nurseries, disability, old age and various death benefits; and unemployment insurance.<sup>113</sup>

The cost of social benefits "is shared among employers (62.5 percent), employees (25 percent), and the government (12.5 percent)."<sup>114</sup> The rates paid by employers range from 11.75 to 13.4 percent of the payroll, and are paid every two months.<sup>115</sup> Mexican law, also, requires companies, with more than 100 employees, to maintain a doctor and infirmary, while companies with more than 300 employees must es-

107. *Id.* at 26. Another source estimates the rates as high as 60 percent. *Id.* at 18. Some confusion exists in regard to minimum wage. One source says that American companies must pay 50 percent higher minimum wages. Taylor & Bond, *supra* note 6, at 38. This is not mentioned by any other source. The conclusion of this author is that the 50 percent additional pay is probably confused with the 50-60 percent cost of fringe benefits.

108. El Paso—Juarez Handbook, *supra* note 72, sec. 4:10, at 2.

109. *Id.* at 1.

110. *Id.*

111. INVESTING—MEXICO, *supra* note 50, at 19. Generally employers grant 15 days total and some pay an additional 15-day bonus.

112. *Id.* Some sources say there are seven legal holidays each year. El Paso—Juarez Handbook, *supra* note 72, sec. 4:10, at 1; also Steiner, *supra* note 84, at 146. Some labor contracts also call for 9-10 additional paid holidays.

113. INVESTING—MEXICO, *supra* note 50, at 20.

114. *Id.*

115. Covarrubias, *supra* note 102, at 2. Another source puts the rate between 8.3 and 11.7 percent. Steiner, *supra* note 84, at 146.

establish hospital facilities.<sup>116</sup> Many companies have voluntarily established savings plans, life insurance, sports facilities and lunches.<sup>117</sup>

Potentially, one of the most beneficial fringe benefits to the Mexican worker may be profit sharing. This benefit, established under a 1964 law, requires all firms to distribute 20 percent of "net distributable profits" to their employees, excluding managers, directors, apprentices and those who have worked less than sixty days during the fiscal year.<sup>118</sup> The determination of "net distributable profits" is a complicated procedure, that can probably be best accomplished by a Mexican accountant, attorney or management consultant. Basically, it involves deducting a fixed deduction of 30 percent and a variable deduction of 10-80 percent from the base, which includes net pre-tax earnings and profits set aside for capital reserves, bad debts and other contingency reserves minus corporate taxes.<sup>119</sup>

Some border cities claim that profit sharing does not affect industry under PFI,<sup>120</sup> but companies should be prepared to pay "an increased wage bill as a result of the profit-sharing requirement."<sup>121</sup> One source states:

On the average, the profit to be shared amounts to about 8% to 12% of net (income). A survey of firms with a total of 33,000 employees showed that profit sharing equaled 0.8% of gross income of the companies. For the individual, his share was about 60% of his monthly take home pay, or less than 5% of his annual wages.<sup>122</sup>

Another source says the amount actually distributed to employees after deduction of income tax ranges from 2.8 percent to 12.6 percent with the average being about 12 percent.<sup>123</sup> However, relief is available as newly created firms are exempt during the first two years of operation.<sup>124</sup> Although employees have a right to share in profits, this does not allow them to interfere in the administration of the firm.<sup>125</sup>

Some additional fringe benefits which the investor must consider include sick pay, an education tax for which American companies pay 1 percent of payroll to support Mexican education and a new housing support tax of 5 percent of the payroll to fund the National Housing Program.<sup>126</sup>

116. INVESTING—MEXICO, *supra* note 50, at 20.

117. *Id.*

118. *Id.* at 18.

119. *Id.* at 19.

120. Steiner, *supra* note 84, at 147.

121. Taylor & Bond, *supra* note 6, at 39.

122. Walker, *supra* note 7, at 29.

123. OVERSEAS BUSINESS REPORT, *supra* note 51, at 14.

124. See Taylor & Bond, *supra* note 6, at 39.

125. OVERSEAS BUSINESS REPORT, *supra* note 51, at 14.

126. See El Paso—Juarez Handbook, *supra* note 72, sec. 4:10, at 2.



The foreign investor must also consider the labor contract or contracts which he will be negotiating. There are, basically, two types of labor contracts—individual worker contracts and collective work contracts.<sup>127</sup> Both types contain basically the same information, but the difference is that a collective work contract is negotiated with a union and applies to all workers in the union.<sup>128</sup>

There are nine national unions in Mexico, with the strongest being the *Confederacion de Trabajadores de Mexico* (CTM), which is closely allied with the PRI party of Mexico and has spearheaded most movements for change in labor.<sup>129</sup> Labor strikes do not appear to have been a great problem to industry in Mexico, as 98 percent of strikes called in 1972 did not materialize.<sup>130</sup> The grounds upon which a legal strike can be called are:

1. Refusal by the employer to comply with contractual obligations;
2. Refusal to accept an arbitration award; and
3. To support another legal strike provided a majority of workers agree.<sup>131</sup>

Generally, strikes can be minimized if companies employ a labor supervisor and avoid aggressive negotiating.<sup>132</sup>

Should the businessman decide to dismiss an employee, several additional considerations are necessary. If an employee is dismissed for cause, the firm has no responsibility, although the case may be investigated.<sup>133</sup> However, upon dismissal not for cause, the employee must be given severance pay amounting to:

three months' pay, twelve days' additional pay for every year employed, and full pay from the time of dismissal until a final decision on the merits of the case is reached in court, should he appeal his dismissal.<sup>134</sup>

A worker unjustifiably dismissed may choose between reinstatement and indemnification.<sup>135</sup>

#### B. *Immigration*

Mexican law also contains certain provisions relating to U.S. employees employed by the firm established in Mexico. The main provision which will concern the firm is Section I of the Federal Labor Law requiring "that at least 90% of a firm's skilled and unskilled

127. *Id.* at 3.

128. *Id.*

129. INVESTING—MEXICO, *supra* note 50, at 17.

130. *Id.* at 18.

131. *Id.*

132. *Id.*

133. Covarrubias, *supra* note 102, at 2.

134. INVESTING—MEXICO, *supra* note 50, at 20.

135. *Id.*

workers must be Mexican nationals."<sup>136</sup> Because of the lack of suitable Mexican workers in certain skilled areas, the Mexican government does allow the employment of alien technicians, supervisors and management personnel.<sup>137</sup> Although the Mexican government allows the entrance of such worker, it also requires a special permit and that Mexican workers be trained to take their places.<sup>138</sup>

In regard to the entrance of U.S. citizens to be employed in the Mexican plant, some considerations on the status of the alien are important. Aliens may enter Mexico under three statutes:

1. immigrant;
2. non-immigrant;
3. *inversionista* (investor).<sup>139</sup>

The immigrant status is usually applied to aliens who intend to establish residence in Mexico. For PFI purposes, the last two statutes are probably most important. The non-immigrant enters on a Visitor's Card and may stay for six months.<sup>140</sup> If the entrance is for business purposes, the card is renewable once; and if the entrance is for scientific, technical, or artistic purposes, the card may be renewed three times.<sup>141</sup> The status of investor is given to an alien who guarantees he "will assume an active role in any livestock, agriculture, industrial or export business," and an investment of 200,000 pesos, which may be lowered by the Ministry of Interior.<sup>142</sup>

### C. Customs

Since the businessman operating a plant under PFI is going to be continually involved in moving component parts and finished products back and forth across the border, he will be interested in knowing the legal requirements which must be met in order to carry out the transfers as smoothly as possible. As mentioned earlier, one of the concerns of the Mexican government is that the temporary imports do not enter the Mexican economy, but do in fact return to the U.S. To insure their return, the Mexican government requires that foreign companies post a bond guaranteeing that all raw materials, machinery and equipment, parts, tools, and containers are returned.<sup>143</sup> This requirement "has caused plants established under the program to be called 'in bond' plants."<sup>144</sup> The two major types of

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136. *Id.*

137. WRIGHT, *supra* note 8, at 197.

138. OVERSEAS BUSINESS REPORTS, *supra* note 51, at 19.

139. *Id.*

140. *Id.*

141. *Id.*

142. *Id.* at 19, 20.

143. Procedures, *supra* note 46, at 3.

144. Hunt, *supra* note 2, at 5.

bonds in use are the revolving bond and the single entry bond. The revolving bond is used mainly for the importation of raw materials for assembling or processing, while the single entry bond, on the other hand, is usually employed as a guarantee for the entry of machinery and other capital goods.<sup>145</sup> Both bonds are usually written for one year and are renewable. The size of either bond depends on "production rates, the number of shipments in process and Mexican duties (plus 10% for fines) on the materials being imported."<sup>146</sup> Because of the difficulties involved in increasing the size of the bond, a company would probably be well advised to overbond "in order to accommodate unexpected import requirements."<sup>147</sup> The cost of the bond will usually vary between one and two percent of its value,<sup>148</sup> and is "based on the Mexican customs duty on the materials if they were conventionally imported into the Republic."<sup>149</sup> The Mexican government has indicated that the bonds may be posted in the following ways:

- a. with a pledge;
- b. by an authorized bonding company, paying the percentage commission;
- c. by making a cash deposit; or
- d. with an authorized customs area.<sup>150</sup>

Of course, in this procedure, a Mexican customs official would be invaluable.

The Mexican-established business will also face U.S. customs duties on products returning to this country. The duty is determined according to "the extent that the Mexican wholesale value of the finished product exceeds the cost of the U.S. components."<sup>151</sup> The actual rates vary greatly. It is important to determine, beforehand, the custom duties in order to avoid prohibitive rates.<sup>152</sup>

One of the problems faced by industries in the past has been the time factor in getting through customs. Delays have ranged from twenty-four hours to three days.<sup>153</sup> Such delays can be costly. One large firm reported paying \$2,261.00 in yearly costs as a result of

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145. BAERRESEN, *supra* note 8, at 70, 71.

146. *Id.*

147. *Id.*

148. *Id.* A businessman must also consider an unofficial cost commonly known as "*mordida*." *Mordida* may be thought of as a gratuity or tip and usually must be paid if cooperation by Mexican officials is needed.

149. Reynosa, *supra* note 100, at 2.

150. Mexican Border Industrialization Program, *supra* note 26, at 4.

151. El Paso—Juarez Handbook, *supra* note 72, sec. 5:00, at 2.

152. BUS. WEEK, Dec. 2, 1967, at 122.

153. INVESTING—MEXICO, *supra* note 50, at 23.

delays.<sup>154</sup> Some suggested ways of reducing time lost in clearing customs are:

1. paying overtime to customs officials;
2. preparing all paperwork in advance;
3. the use of special one-day services at Mexican customs; and
4. substituting company employees for customs officials.<sup>155</sup>

Another time-saving device used by some companies is the kit system. Under this system, a company employs a warehouse on the U.S. side of the border where all raw materials are assembled in kits and then sent to Mexico for assembly. A number system maintains the identity of all materials, thus facilitating identification at customs.<sup>156</sup> Finally, there is some movement toward considering industrial parks as bonded areas, where all customs determinations may take place.<sup>157</sup>

#### D. Taxation

The Mexican Income Tax Law establishes two classifications of taxpayers:

1. Business entities, which are subject to a single corporate income tax; and
2. Individuals, who are taxed on personal income whether from personal services or from capital.<sup>158</sup>

The corporate income tax rate can vary from 0-42 percent,<sup>159</sup> depending on the income involved, and is applied against taxable income. Taxable income is defined as "gross income less costs and expenses related to producing that income, with exceptions."<sup>160</sup> Some examples of deductions include bad debts, cost of goods sold, social welfare payments and employee retirement plan payments.<sup>161</sup> Additionally, any income tax paid in Mexico is deductible from U.S. federal income tax liability.<sup>162</sup> Tax rates for individual income vary from 0-35 percent.<sup>163</sup> Theoretically, aliens residing in Mexico must pay income tax regardless of the source of their income, but this provision is not enforced.<sup>164</sup>

Mexican law also requires that a tax varying from 0-2 percent be paid on dividends. A tax on distributable profits has been repealed,

154. BAERRESEN, *supra* note 8, at 72.

155. *Id.* at 74.

156. *Id.* at 75.

157. *Id.* at 72.

158. OVERSEAS BUSINESS REPORT, *supra* note 51, at 21.

159. Covarrubias, *supra* note 102, at 4.

160. INVESTING—MEXICO, *supra* note 50, at 11.

161. OVERSEAS BUSINESS REPORTS, *supra* note 51, at 22.

162. El Paso—Juarez Handbook, *supra* note 72, sec. 4:70, at 1.

163. Covarrubias, *supra* note 102, at 4, 5.

164. INVESTING—MEXICO, *supra* note 50, at 12.

so now profits are only taxed when dividends are paid.<sup>165</sup> Another tax which must be paid is the Commercial Revenue Tax (sales tax), which is based on the gross receipts of the company at a rate of about 1.8 percent.<sup>166</sup>

State taxes are generally lower, and in addition to the education and housing tax mentioned earlier, can include:

1. Public Investment Tax;
2. Recording fees;
3. Commercial Revenues Tax-Rate: 1.2 percent;
4. Transfer Tax on Real Estate-Rate: 1 percent; and
5. Real Estate Tax.<sup>167</sup>

Besides federal and state taxes, local municipalities may also levy taxes. An example of municipal rates is provided by Tijuana, which is approximately .05 percent of all assets.<sup>168</sup> Some taxes which are not levied in Mexico are excess profits tax and capital taxes.<sup>169</sup>

Although some firms operating in Mexico report a tax burden of in excess of 50 percent,<sup>170</sup> taxes do not seem to have inhibited investment under PFI. Besides the incentives inherent in PFI, some additional tax concessions are available on the state level. The state of Texas reportedly grants "ten years property tax and part of the .09% sales tax exemptions to industries considered as new and necessary."<sup>171</sup>

#### IV. CONCLUSION

Since its inception, PFI has grown at a remarkable pace. Starting with only a few companies in 1965, the program now involves approximately 350 firms<sup>172</sup> and employs close to 65,000<sup>173</sup> members of the Mexican workforce. Although the number of companies has not expanded as fast as it did in the early seventies, there appears to be a sustained growth in the number of persons employed. For example, in the past few years employment has increased at a rate of about 15 percent, or approximately 1,000 new jobs per month.<sup>174</sup>

The future of PFI appears to be bright. Although the U.S. gov-

165. OVERSEAS BUSINESS REPORTS, *supra* note 51, at 21.

166. El Paso—Juarez Handbook, *supra* note 72, sec 4:70, at 2.

167. *Id.* Although these particular taxes are for Chihuahua, it is believed that they are a typical sample of taxes which may be encountered.

168. Procedures, *supra* note 46, at 6.

169. INVESTING—MEXICO, *supra* note 50, at 11.

170. *Id.*

171. Covarrubias, *supra* note 102, at 1.

172. Border Industry Program, June 30, 1972, at 1 (unpublished material available from the U.S. Embassy in Mexico).

173. Bolin, *Border Industry Facts for 1973*, MEXICAN-AMERICAN REV., Sept. 1973, at 1.

174. Border Industry Program, *supra* note 172, at 6.

ernment maintains a position of neutrality on the program, it is believed that privately the Department of Commerce is very much interested in its progress.<sup>175</sup> The Mexican government is, of course, greatly in support of the program. The government is doing everything possible to encourage investment, including tax concessions, elimination of red tape, and the allowance of 100 percent foreign ownership of corporations established under PFI.<sup>176</sup>

The expansion of the program is also being urged by the Mexican government. In 1967, provisions were established that would allow the border program to be extended to the interior of Mexico.<sup>177</sup> Such extensions must have approval from the Department of Industry and Commerce, and probably would not be allowed if the industry would compete with an already established Mexican industry.<sup>178</sup> Further expansion has been made possible by the Presidential Decree of March 17, 1971, which among other things allows for the establishment of plants in the coastal area.<sup>179</sup> Although no plants have moved to the coast yet, it is expected that some will do so in the near future.<sup>180</sup>

Further expansion of the program is possible through the entrance of Mexican manufacturers into the border program. Reportedly, many Mexican manufacturers are seriously considering opening plants under PFI.<sup>181</sup> Another indication of expansion is the report by several officials that the Mexican government is studying "a measure to permit the sale in Mexico of those border industry products which are not competitive with domestic industry."<sup>182</sup> Such a measure would, undoubtedly, add new incentives to industry operating under the program.

Ironically, the greatest threat posed to the future of the program may be rising wages. As pointed out earlier, minimum wage rates have increased at a steady rate during the past few years.<sup>183</sup> In the state of Tamulipas, facing Brownsville and McAllen, Texas, minimum wages have increased 300 percent from 1962 to 1970, an increase

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175. See Mexico's Border Program, no date, at 6 (unpublished material available from the Mexican Chamber of Commerce of the U.S.).

176. BUS. ABROAD, Dec. 11, 1967, at 21. Bolin reports the fact that PFI is unaffected by the new foreign investment law which in other industry limits the proportion of foreign participation in many cases to 49 percent. Bolin, *supra* note 173, at 14.

177. Trevino, *Border Assembly Operations*, MEXICAN-AMERICAN REV., April 1969, at 33.

178. *Id.*

179. Border Industry Program, *supra* note 172, at 4.

180. *Id.*

181. Mexico's Border Program, *supra* note 175, at 7.

182. Border Industry Program, *supra* note 172, at 6.

183. See INVESTING—MEXICO, *supra* note 50, at 17.

of about 35 percent per year.<sup>184</sup> Although rates have leveled off some in the past three years, the level of minimum wage rates is crucial to the future of the program.

For the foreign businessman, the prospect of doing business in Mexico under PFI will undoubtedly grow in attractiveness in the coming years. With a stable political situation<sup>185</sup> and with an estimated growth rate for 1973 in excess of 7 percent, such investment will be welcome and profitable. However, as with any investment, close attention to the pertinent legal guidelines involved is necessary if a successful business venture is to be accomplished. Familiarity with the pertinent laws and cooperation with Mexican officials and institutions will make possible a rewarding investment in the *Programa Fronteriza de Industria*.

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184. Steiner, *supra* note 184, at 149.

185. INVESTING—MEXICO, *supra* note 50, at 1.

