

# North American Free Trade & Investment Report

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cross-border trade in Mexico, the U.S., and Canada*

## Mexico: Private Equity

### Legal Obligations of Mexican Companies - Or How to Avoid Common Pitfalls

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**(EDITOR's NOTE: This is part one of a two-part article.  
Part two will appear in the February 15, 2007 NAFTIR.)**

#### Corporate Obligations

Foreign investors may freely establish a Mexican company or acquire stock in an already established one. The most common corporate form chosen by investors is the "Sociedad Anónima" (S.A.) or "Sociedad Anónima de Capital Variable" (S.A. de C.V.) - Variable Stock Corporation. Other forms of corporations are the "Sociedad de Responsabilidad Limitada" (S. de R.L. or S. de R.L. de C.V.) - Limited-Liability Company, the "Sociedad de Nombre Colectivo" (S. en N.C.) - General Partnership or the "Sociedad en Comandita Simple" (S. en C.S.) - Limited Partnership. Because the S.A. and S.A. de C.V. are the most common corporate forms, this article will focus on obligations related to these corporations.

#### Incorporation of an S.A. or S.A. de C.V.

##### *Corporate structure*

The capital stock of an S.A. or S.A. de C.V. is divided into shares and the shareholders are liable only to the extent of their contributions. This corporation may exist under any kind of name, followed by the words, "Sociedad Anónima (de Capital Variable)", or its abbreviation "S.A. (de C.V.)". The shareholder's obligation is limited by their amount held in stocks. At least two shareholders and a minimum capital of fifty thousand Mexican pesos are required to form the company. Each shareholder should purchase at least one share of stock. The charter for the entity ("Acta Constitutiva" or "Estatutos") is a combination of what in the U.S. is known as articles of incorpora-

tion and by-laws. This document will designate the initial shareholders, members of the board of directors or the sole administrator of the Mexican company, its principal officers and the statutory auditor ("Comisario"). The charter will also approve the issuance of powers of attorney to one or more key representatives of the Mexican company. The charter must contain a clause to the effect that foreign shareholders of the Mexican company waive any right to seek the protection of their own governments in the event of any dispute regarding the Mexican company ("Calvo Clause"). A public notary who will register the company with the Public Registry of Commerce ("Registro Público de Comercio") must ratify the charter.

The shares are divided in titles ("Títulos"), which are used to credit and transmit shareholder's rights. In general, shares have the same value and confer equal rights. Relative ownership of share value defines the distribution of profits and capital among the shareholders. Shareholders can be represented and need not take part in the shareholder meetings. However, company directors are not allowed to represent shareholders.

The main difference between the S.A. and the S.A. de C.V. is that the capital amount for an S.A. is fixed and specified in the articles of incorporation and by-laws. Any increase or decrease requires modification of the articles of incorporation and by-laws. In contrast, the capital of an S.A. de C.V. differentiates between minimum fixed capital and an unlimited variable capital. Increase and decrease of variable capital does not require a modification of the articles of incorporation and by-laws.

Either company is obliged to keep accounting books and corporate records such as (i) a Daily Book, (ii) a Led-

ger, (iii) a Book of Shareholder's Assembly Minutes, (iv) a Shareholder's Record and, in the case of an S.A. de C.V., (v) a Book of Increases and Decreases in Capital.

### **Powers of Attorney**

Special care must be given to powers of attorney granted to local directors. Shareholders who want to retain control over the company should issue specialized powers of attorney to the members of the board of directors or the sole administrator. Powers of attorney, which include authority to grant sub-powers of attorney and to sell company assets, are usually too broad. In addition, with the exception of powers for labor and judicial issues, powers of attorney should be granted as joint powers only to company directors.

The most important powers of attorney necessary to operate a company are:

a) General power of attorney for acts of administration

This power allows representation of the company in all extra-judicial actions that are necessary for the operation of the company such as hiring and firing employees.

b) General judicial power of attorney for cases and collections

This power of attorney allows the bearer to represent the company before courts and litigate for the company.

c) General power of attorney for acts of ownership

This power entitles to sell, buy, encumber, or impose ownership limitations on the assets that belong to the company.

d) General power of attorney to approve bonds and contracts of credit

This power of attorney grants representation of the company for the fulfillment or endorsement of payment of obligations as well as the signing of checks and contracts that can encumber the company.

### **Other Important Obligations**

Companies should also be aware of the following obligations:

- Registration with the National Registry of Foreign Investments ("Registro Nacional de Inversiones Extranjeras", "RNIE") of any foreign capital participating in the company;

- Application for a federal tax identification number, ("Registro Federal de Contribuyentes, R.F.C.") in order to open bank accounts, sign leases, keep records of tax-deductible expenses and write invoices;

- Registration with the Mexican Social Security Institute ("Instituto Mexicano del Seguro Social", "IMSS"). Each time the company hires or terminates an employee, it must give notice to the IMSS within 15 days;

- Registration with the National Institute for the Workers' Housing Fund ("INFONAVIT) and the Retire-

ment Savings System ("Sistema de Ahorro para el Retiro", "SAR"); and

- Application for environmental and other necessary licenses.

### **Administration of the S.A. or S.A. de C.V.**

All S.A. and S.A. de C.V. are administered by its highest corporate body, the General Shareholders Assembly ("Asamblea General de Accionistas", "Assembly"). The assembly is responsible for the ratification of all operations and for taking resolutions. Shareholders must meet at least once a year and within four months following the end of the reporting period in an ordinary assembly meeting. The shareholder's main obligation is to approve the annual financial report and the election or ratification of the administrator or board of administration. Shareholders might also conduct extraordinary assemblies in which they decide upon (i) the continuation or the dissolution of the organization, (ii) an increase or decrease of the capital, (iii) a merger or any other modification of the company's articles and by-laws

In order to constitute an ordinary assembly, half of the company's capital must be represented and any resolutions must be approved by the majority of the participants in the assembly. In general, three-quarters of the company's capital must be represented in an extraordinary assembly and resolutions have to be approved by half of the corporate capital.

The shareholders designate one or several temporary and revocable executives, who may be partners, in order to manage the company. While a sole administrator is named the General Manager, two or more administrators form an Administrative Board ("Consejo de Administradores"). All their powers and responsibilities are regulated within the articles of incorporation and by-laws. Sole administrator's meetings or members of the board of administrators' meetings may be held inside or outside of Mexico. Foreign sole administrators or directors that act in Mexico need a work visa.

The Administrators are also responsible for presenting a financial report at the annual shareholder's annual assembly that includes the following information:

- Financial statement for the past fiscal period;
- Balance sheet;
- Income statement;
- Statement of changes in financial position and equity.

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