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Fox Tracks across the Mexican Maquiladora Industry

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Fox Tracks Across the Mexican Maquiladora Industry

Heidi M. Timmons*

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I. INTRODUCTION

“¡México es nuestro!”¹ “¡Ganamos!”² On July 2, 2000, Mexican voters shouted their exuberance for President Vicente Fox’s³ victory over the Institutional Revolutionary Party (“PRI”),⁴ finally dethroned after a seventy-one

* J.D., University of the Pacific, McGeorge School of Law, to be conferred 2005; B.A., Spanish, California State University, Sacramento, 2002. I want to thank my parents, Jan and Oscar Timmons, my grandmother, Hilda Benvenuto, and my sister, Holly Timmons, and my best friend, Kevin Macklin, for their love and support. Licensed Mexican attorney Virginia Lizeth Blackman reviewed this article for accuracy.

1. “Mexico is ours!” *Mexico Embraces Change*, S.F. CHRON., July 4, 2000, at A18.

2. “We won!” *Id.*

3. Vicente Fox Quesada is the 15th President of Mexico. Mention of Fox, the Fox Administration, the Administration, or the President in this Comment is in reference to Vicente Fox unless otherwise noted.

4. See Carol Wise, *Mexico's Democratic Transition: The Search for New Reform Coalitions*, 9 NAFTA L. & BUS. REV. AM. 283, 285-305 (detailing the inception and development of the PRI political party). Mexican revolutionaries formed the PRI in 1929 and later it emerged as a semi-authoritarian party. *Id.* at 285-86. Despite growing corruption, the PRI remained popular until the late 1990s when Mexico's gross domestic product (“GDP”) plummeted and inflation approached three digits. *Id.* at 286-88. At that time, the PRI's traditional left wing constituency criticized the more conservative decisions of the PRI. *Id.* at 290. The remaining PRI loyalists came from the less industrialized parts of the country, with high illiteracy rates, and limited access to educational media channels. *Id.* at 288. The PRI's defeat in 2000, by President Fox, showed that PRI followers consisted of the less-educated population who prefer higher spending on government assistance programs. *Id.* at

year reign.⁵ While the United States rarely sees one political party control the presidency for more than two consecutive terms,⁶ the PRI dominated the executive branch since the birth of Mexico's democracy because of low inflation, generous state assistance, and high growth rates.⁷ Foreign investors are concerned about this drastic change in government and its effect on foreign investment in Mexico.⁸

Apart from the influence of President Fox, several changes within the maquiladora industry alarmed investors. Tax changes, such as the permanent establishment tax and Article 303, dramatically altered maquiladoras in Mexico.⁹ The appreciating peso and the competition from China further affected investment in Mexico.¹⁰ These substantial changes, all within the last four years, transformed maquiladora investment in Mexico from a standard business to a fluctuating market on the verge of complete elimination.¹¹ Consequently, Fox's response to this period of change in the maquiladora industry is vital to investors.

This comment explores the impact of the Fox presidency on the maquiladora industry. Part II provides a background of maquiladora¹² foreign investment in

304. In addition, the PRI's fall from executive power further engrained the party's traditional nature, with authoritarian and populist tendencies that are out of touch with a more democratically minded electorate. *Id.* at 305; see also *Mexican Political Parties*, DALLAS MORNING NEWS, July 1, 2003, at 12A (noting that PRI presidents have been leftist, centrist, and recently pro-business).

5. *Mexico Embraces Change*, *supra* note 1, at A18; *Mexican Presidents and Heads of State*, Mexico Connect, (2003), at http://www.mexconnect.com/mex_/history/presidents.html (last visited Mar. 3, 2004) (copy on file with *The Transnational Lawyer*); see also *Fox Wins Mexican Presidency, Ending 71-Year PRI Dynasty*, CNN, (2000), available at <http://www.cnn.com/2000/WORLD/americas/07/03/mexico.elections/> (last visited Mar. 3, 2004) [hereinafter *Fox Wins*] (copy on file with *The Transnational Lawyer*) (showing Vicente Fox as the 15th President of Mexico since the office's creation in 1929). President Fox is a member of the National Action Party ("PAN"). *Id.*; see also *infra* note 44 (explaining the background of the PAN political party); Jennifer E. Harman, Comment, *Mexican President Vicente Fox's Proposal for NAFTA into a European Union-Style Common Market—Obstacles and Outlook*, 7 L. & BUS. REV. AM. 207, 210 (2001) (noting that Mexican citizens elected President Fox on July 2, 2000, but he did not take office until December 1, 2000).

6. See *The Presidents of the United States of America from George Washington to George W. Bush*, Enchanted Learning, at <http://www.enchantedlearning.com/history/us/pres/list.shtml> (last visited Oct. 6, 2003) (copy on file with *The Transnational Lawyer*) (stating that over the last fifty years the United States has elected six Republican and four Democratic Presidents).

7. Wise, *supra* note 4, at 286. See *Fox Wins*, *supra* note 5 (acknowledging that the PRI controlled the presidency since the office's inception seventy-one years prior).

8. See also Tim Weiner & Graham Gori, *Can Mexico's New Leader Really Work Wonders?*, N.Y. TIMES, Oct. 29, 2000, § 3 (Money and Business), at 1 (acknowledging the profound expectations of Mexicans and foreign investors placed on Fox's election); Shannon Buggs, *Investors Should Consider Mexico*, HOUSTON CHRON., July 17, 2000, (Business), at 1 (relating that the Bolsa Mexicana de Valores, Mexico's stock exchange, increased more than six percent the day after the election). Investors maintain that significant positive changes in the Mexican economy after the election are still in the future. *Id.*

9. See *infra* notes 60-89 and accompanying text (reviewing the effects of the permanent establishment tax and Article 303 provisions).

10. See *infra* notes 130-75 and accompanying text (exploring the effects of the appreciated peso and the competition from China).

11. See Susan Ferriss, *Mexico's Broken Dream: After Surge, Manufacturing Jobs Move to China*, ATLANTA J.-CONST., Nov. 16, 2003, (Business), at 4H [hereinafter *Mexico's Broken Dream*] (stating that Mexicans doubt the future of manufacturing in Mexico as a result of the maquiladora crisis).

12. See Random House Unabridged Dictionary 1173 (2nd Ed. 1982 (explaining how to pronounce the word maquiladora). Maquiladora (ma·qui·la·do·ra) is pronounced (mə kē'īə dōr 'ə). *Id.* The dictionary's concise

Mexico prior to the Fox presidency. Part III discusses the complex challenges in foreign investment resulting from decisions made by the Fox Administration, as well as other far-reaching problems facing foreign investment in Mexico. Part IV provides an overview of President Fox's accomplishments in foreign investment in Mexico. Finally, Part V of this comment informs investors regarding the future of maquiladora foreign investment in Mexico. This comment concludes that Mexico remains an attractive location to U.S. investors engaged in manufacturing but it is not as attractive for investors from other countries. In addition, the Fox Administration will need to strengthen Mexico's infrastructure and energy supply in order to remain competitive with other desirable manufacturing locations, particularly China.

II. BACKGROUND

A. *Overview of Foreign Investment in Mexico and the Maquiladora Industry*

Mexico is an advantageous destination for foreign investment because of its low labor costs and proximity to the United States.¹³ In 2003, A.T. Kearney, a consulting firm, ranked Mexico as the world's third most desirable country for foreign investment after the United States and China.¹⁴ A major sector of foreign investment in Mexico is the maquiladora industry.¹⁵ Mexico established maquiladoras in 1965 to encourage foreign corporations to operate businesses along the northern border of Mexico.¹⁶ Since the late 1990s, maquiladoras have primarily focused on assembling,

pronunciation key explains the phonetics: ð = a as in alone, ē as in ēqual, and ô as in order. *Id.*; U.S. GEN. ACCT. OFF., INTERNATIONAL TRADE: MEXICO'S MAQUILADORA DECLINE AFFECTS U.S.-MEXICO BORDER COMMUNITIES AND TRADE; RECOVERY DEPENDS IN PART ON MEXICO'S ACTIONS, GAO Report No. 03-891, 5 n.1, 6 (2003) [hereinafter GAO Report No. 03-891] (noting that the term "maquiladora" is derived from the Spanish word *maquilar*, which is a service that a miller provides when he or she grinds wheat into flour). Similarly, a maquiladora provides assembly services without necessarily taking ownership of the goods being assembled. *Id.* at 5 n.1. The term maquiladora has expanded to include all subsidiary plants in Mexico owned by foreign investors. *Id.* at 6. However, official maquiladoras register with the Mexican government to receive preferential tariffs on inputs and machinery and simplified customs procedures. *Id.* at 6.

13. *See id.* at 5, 37 (2003) (noting reasons foreign investors have invested and continue to invest in Mexico). In the 1960s, low labor costs originally enticed investors to Mexico. *Id.* at 5. Despite competition from other countries, Mexico remains an important site for investors because of its proximity to the United States. *Id.* at 37; *see also* Paulo Monteiro, *Mexico Still Considered Good Market for Carmakers Despite Economic Woes and Weak Auto Sector Outlook*, WORLD MARKETS RES. CENTRE DAILY ANALYSIS, Oct. 14, 2003 (stating that even though Mexico ranks high for foreign investment, the outlook remains mixed for future investment in Mexico).

14. *See* Ricardo Sandoval, *Mexican Economy Sees a Bit of Hope, Despite Slump, Nation Ranks High on List of Best Places to Expand*, DALLAS MORNING NEWS, Oct. 10, 2003, (Business), at 1D (quoting Carlos Niezen, a principal in A.T. Kearney's Mexico City office, who stated that Mexico enjoys the perception of a stable economy). This third place ranking is a notable improvement from Mexico's ninth place ranking in 2002. *Id.*

15. *See* GAO Report No. 03-891, *supra* note 12, at 1 (acknowledging that Mexico's maquiladora program is the largest and most dynamic factor in U.S.-Mexico trade).

16. *See id.* at 5 (explaining that the maquiladora program was established as a part of the Border Industrialization Program to develop the U.S.-Mexico border).

manufacturing, and exporting finished products.¹⁷ Maquiladoras currently account for one-half of Mexico's total exports.¹⁸ Maquiladoras offered foreign investors the ability to take advantage of temporary importation of inputs¹⁹ from foreign sources without payment of import duties.²⁰

To take full advantage of the maquiladora program and achieve recognition as an "official" maquiladora, firms must register with the Mexican government.²¹ Foreign investors need to maintain a corporate presence in order to register as a maquiladora.²² After registration, the maquiladora firms are eligible for preferential tariffs on inputs and machinery and simplified customs procedures.²³ The maquiladora industry reached its peak in October of 2000.²⁴

17. Carlos Angulo-Parra & Edmundo Elfas-Fernández Juárez, *Mexico: Maquiladoras and NAFTA Beyond Year 2000*, The National Law Center, (July 1996), available at <http://www.natlaw.com/pubs/spmxcu4.htm> (last visited Mar. 3, 2004) (copy on file with *The Transnational Lawyer*) (relating the background of the maquiladora industry). In the initial stages of the maquiladora program the Mexican government only waived import duties on materials imported for incorporation into finished products for export. *Id.* Subsequently, maquiladoras' primary focus became assembly and manufacture. *Id.*

18. See Jesus Cañas & Roberto Coronado, *Maquiladora Industry: Past, Present and Future* BUS. FRONTIER (Fed. Res. Bank Dallas, El Paso Branch), Issue 2 (2002) (noting the accomplishments of the maquiladora industry).

19. See Lucinda Varga, *NAFTA, The U.S. Economy and Maquiladoras*, BUS. FRONTIER (Fed. Res. Bank Dallas, El Paso Branch) Issue 1 (2001) (listing inputs as materials, parts, and machinery imported by maquiladoras). Maquiladoras incorporate inputs into the finished products that maquiladoras subsequently export. *Id.* [Note by comment author use the terms "inputs" and "components" interchangeably, but primarily, authors use the term "inputs.;" see also Neville, Peterson & Williams, *Mexico Facing New Era in 2001*, J. COM., Feb. 9, 2000, (Global Commerce), at 12 (defining inputs as parts, components, packaging, or machinery used to produce goods for export); GAO Report No. 03-891, *supra* note 12, at 33, 39 (itemizing duty-free treatment to include import on parts, components, and other inputs). The Mexican government removed tariffs from inputs, parts, and components. *Id.* at 39; David W. Eaton, *Transformation of the Mexican Maquiladora Industry: The Driving Force Behind the Creation of a NAFTA Regional Economy*, 14 ARIZ. J. INT'L & COMP. L. 747, 747 (1997) (explaining that manufacturing firms import raw materials, parts, and components (inputs) duty free).

20. See Eaton, *supra* note 19, at 748 (identifying temporary importation of inputs, without taxes, as the most important benefit for manufacturers).

21. See GAO Report No. 03-891, *supra* note 12, at 6 (explaining that the term maquiladora loosely refers to any subsidiary plant of a foreign company involved in export from Mexico). The GAO report uses the term to define those maquiladoras that officially register with the Mexican government. *Id.*

22. See Chiang-feng Lin, *Investment in Mexico: A Springboard Toward the NAFTA Market—An Asian Perspective*, 22 N.C. J. INT'L L. & COM. REG., 73, 109-10 (1996) (stipulating that investors must obtain a permit from the Mexican Ministry of Commerce and Industrial Development ("SECOFI")). To qualify for registration maquiladoras must generate employment, contribute foreign currency, foster the integration of Mexican industry, and facilitate technology transfers. *Id.* at 110. After registration, the maquiladora can proceed with temporary, duty-free importation of inputs for production. *Id.* Registration permits qualified maquiladoras to import inputs temporarily, for manufacturing, without paying customs duties. *Id.* at 110-11. Mexican Customs requires maquiladoras to post a bond, and the government can use the bond money if the maquiladoras fail to re-export the goods, as required by the law. *Id.* at 111; see also Sandra L. Shippey & Patrick W. Martin, *Legal and Practical Issues Involved with Maquiladora Financing*, 8 NAFTA L. & BUS. REV. AM. 253, 263 (itemizing additional requirements for registering a maquiladora with the Mexican government).

23. See GAO Report No. 03-891, *supra* note 12, at 6 (enumerating the various key benefits maquiladoras receive after registration with the Mexican government).

24. See *id.* at 14 (detailing the history of production for maquiladoras). The maquiladora industry increased production by 197 percent from January 1993 until its peak in October 2000. *Id.*

Throughout the 1980s and 1990s, several countries in Europe, as well as the United States, Japan, Korea, and Taiwan, all established maquiladoras in Mexico.²⁵ There are several reasons why foreign investors locate maquiladoras in Mexico. First, Mexico's proximity to the United States makes it a primary target for foreign investors who wish to take advantage of the U.S. market.²⁶ Mexico's proximity to the United States attracts investors that rely on "just-in-time" shipping,²⁷ a process that quickly moves the input from the maquiladora to a company's assembly plant in the United States.²⁸ The just-in-time system reduces inventory to a minimal level by producing and delivering goods on an as-needed basis.²⁹ For example, manufacturers such as Sanyo make 5.5 million televisions a year primarily for Wal-Mart stores located inside the United States.³⁰ Sanyo's production system utilizes just-in-time shipping to divide production between Tijuana and Arkansas.³¹ Accordingly, other countries that are more remote, such as those located in Asia, find it impossible to compete with Mexico's expedited system.³²

Second, Mexico's North American location enabled inclusion in the North American Free Trade Agreement ("NAFTA"),³³ which removed many of the trade barriers to investment and trade between Mexico, the United States, and Canada.³⁴ The implementation of NAFTA created the world's largest single market for goods and capital.³⁵ Since NAFTA's implementation, Mexican exports to Canada and the United States have increased by 225 percent.³⁶ NAFTA

25. See *id.* at 5 (explaining that in the 1980s Europe and Japan joined the United States in establishing maquiladoras in Mexico). Japanese, Korean, and Taiwanese maquiladoras first began leaving Mexico after the implementation of Article 303. *Id.* at 36; see also *infra* notes 74-89 and accompanying text (discussing Article 303).

26. See GAO Report No. 03-891, *supra* note 12, at 37 (noting Mexico's unique competitive advantage because of its location bordering the United States); see also Sandoval, *supra* note 14, at 1D (indicating that economic analysts cite Mexico's proximity to the United States as the most important reason for locating businesses in Mexico).

27. See *Mexico: Maquila Doors Closing*, ECONOMIST INTELLIGENCE UNIT—BUS. LATIN AM., Feb. 24, 2003 (stating that just-in-time shipping is an important factor for many manufacturers and their suppliers).

28. *Id.*; Elisabeth Malkin, *Manufacturing Jobs are Exiting Mexico*, N.Y. TIMES, Nov. 5, 2002, at 1.

29. See Lin, *supra* note 22, at 114 n.248 (indicating that low quantities of inventory reduce maquiladora production costs and make the manufactured products more competitive in the market).

30. Malkin, *supra* note 28, at 1.

31. See *id.* at 1 (explaining how Mexico benefits from its ability to offer just-in-time shipping).

32. See *Mexico: Maquila Doors Closing*, *supra* note 27 (providing that Toyota Motors will soon start producing truck beds in Tijuana that will be shipped just-in-time to the company's assembly plant in California, a distance short enough to make production in Asia impractical); see also Lin, *supra* note 22, at 114 n.248 (noting that suppliers must locate near manufacturing plants to take advantage of just-in-time shipping).

33. North American Free Trade Agreement, Can.-Mex.-U.S., reprinted in 32 I.L.M. 289 (1993) [hereinafter NAFTA] (entered into force Jan. 1, 1994).

34. Harman, *supra* note 5, at 210-11; see Lin, *supra* note 22, at 116, 128 (stating NAFTA removed tariff, quota, license, ground transportation, and technical barriers to trade). Mexico will benefit from a free flow of products through the North American market. *Id.* at 116.

35. Harman, *supra* note 5, at 211.

36. See Antonio O. Garza, Jr., *A Letter from the Ambassador*, Export America, Nov. 2003, available at

outlines trade rules between various industries, including transportation, auto parts, textiles, apparel, energy, and environmental protections.³⁷ In addition, NAFTA defines customs procedures, barriers to trade, and competition policy investment.³⁸ Furthermore, by 2009, NAFTA requires the elimination of all tariffs on goods traded among NAFTA partners and prohibits the parties from increasing or adopting additional tariffs on NAFTA goods.³⁹ In addition, ten years of NAFTA created a familiar environment for investors to conduct business.⁴⁰ Even with Mexico's many desirable attributes, investors are beginning to relocate their manufacturing facilities to other countries. Maquiladoras began to decline due to increased labor costs, fiscal uncertainty, and competition from other countries.⁴¹ In 2000, President Fox confronted these challenges upon his election.

B. Background of the Vicente Fox Presidency

The election of President Fox was a landmark in the history of Mexican government.⁴² For the first time in Mexico's history a political party other than the PRI gained control of the presidency.⁴³ Vicente Fox is the first elected Mexican president from the PAN,⁴⁴ an organization that has a conservative, pro-business platform.⁴⁵ The PRI monopolized the preceding seventy-years of the Mexican presidency while focusing on developing a corporate economy with limited involvement in the global world.⁴⁶ This change in government signals a

http://www.export.gov/exportamerica/NewOpportunities/no_mexico_1103.html (last visited Mar. 3, 2004) (copy on file with *The Transnational Lawyer*) (highlighting the effects of NAFTA between the United States, Mexico, and Canada).

37. See Harman, *supra* note 5, at 211 (listing specific provisions included in the NAFTA agreement).

38. *Id.* at 211.

39. See Lin, *supra* note 22, at 74, 119 (adding that by 2009, fifteen years after NAFTA's 1994 effective date, all products traded within the NAFTA market will receive duty-free entry if the products have a NAFTA origin). NAFTA will phase out tariffs over a fifteen-year period between 1994 and 2008. *Id.*

40. See Alan M. Field, *Headed South; The Economy and China's Emergence as a Low-Cost Manufacturing Center are Taking Toll on U.S.-Mexico Trade*, J. COM., Apr. 14, 2003, at 19 (commenting that NAFTA has educated Mexico on trade and fostered investor familiarity with Mexico).

41. See GAO Report No. 03-891, *supra* note 12, at 14; see also Cañas & Coronado, *supra* note 18 (noting the underlying challenges for maquiladoras in Mexico); Paul Day, *Mexico Struggles With Declining Industrial Competitiveness*, MARKET NEWS INT'L, May 13, 2003 (stating that the number of maquiladora plants has dropped 6.4 percent a year since 1999).

42. See *Fox Wins*, *supra* note 5 (elaborating on the end of the PRI's seventy-one year dynasty).

43. See *id.* (explaining Fox's victory was historical and the cleanest election in Mexico's history). Previous elections have exhibited fraudulent results. *Id.*

44. See Guy Poitras, *The Rise of the PAN*, 9 NAFTA L. & BUS. REV. AM. 271, 272 (providing a background on the formation of the PAN in 1939); see also Wise, *supra* note 4, at 284 (defining the PAN as a center-right political party). The PAN is conservative and entertains a business-oriented constituency. *Id.* at 292. The 2002 PAN candidate, President Fox, attracted younger, largely urban, better-educated, middle-class voters. *Id.* at 303; see also *Mexican Political Parties*, *supra* note 4, at 12A (classifying the PAN as pro-Catholic).

45. See Harman, *supra* note 5, at 208 (summarizing Vicente Fox's political career).

46. See David Hale, *Mexico Needs a Chinese Shock*, FIN. TIMES (London), July 9, 2003, at 13 (identifying the PRI's focus during its domination of the government).

shift in the focus of Mexico's economic policy.⁴⁷ Investors need to be aware of the implications of this shift and the impact on the future of foreign investment in Mexico.⁴⁸ President Fox pledged to "jump-start the economy" by increasing foreign investment from \$11 billion⁴⁹ to \$20 billion a year.⁵⁰ Because of Mexico's favorable location for investment, potential and current investors are closely monitoring how Fox intends to develop and nurture foreign investment in Mexico.⁵¹

III. PROBLEMS FACED BY PRESIDENT VICENTE FOX THAT AFFECT FOREIGN INVESTMENT IN MEXICO

Although Mexico is attractive to investors, President Fox faced complex foreign investment issues. First, the maquiladoras' minimalist taxation regime, which controlled for thirty years, began to change in the 1990s.⁵² Several laws spurred this change, including the permanent establishment tax⁵³ and Article 303.⁵⁴ Second, the political climate in Mexico, which includes a history of corruption and present day extreme political party conflict, influences the government's approach towards maquiladoras.⁵⁵ Finally, Mexico's relationship with the United States, and competition within the global economy to remain a choice manufacturing location, affects the maquiladora industry.⁵⁶

47. See James Pinkerton & John W. Gonzalez, *Decision in Mexico; Texas Optimistic of 'New' Neighbor*, HOUSTON CHRON., July 4, 2000, at A25 (reporting that business leaders are encouraged by Fox's campaign pledge to further open Mexico's economy to free trade and foreign investment). However, another commentator said that the presidential change would not change Mexico's economic policy. *Id.*

48. Cf. Day, *supra* note 41 (implying that Fox's promise of a seven percent increase in foreign investment seems unlikely because of a weak global economy and Mexico's lack of reform).

49. All references to currency in this comment are in U.S. dollars unless otherwise noted.

50. See Fox Wins, *supra* note 5 (reviewing the promises made by Fox during his presidential campaign); Brendan M. Case, *Fox Challenges 'Maverick' CEOs; President-elect of Mexico Seeks Economic Partners*, DALLAS MORNING NEWS, Oct. 13, 2000, at 1D (explaining that in addition to increasing foreign investment, Fox wants to deepen trade relations).

51. See David Adams, *Fox's Vision: Purer Mexico, A Unified North America*, ST. PETERSBURG TIMES, Nov. 24, 2000, (National), at 1A (commenting that foreign investors expressed concern regarding Fox's confusing signals on economic policy). In addition, after the election analysts advised investors to reduce investment in Mexico. *Id.*; see also Anthony DePalma, *International Business; Mexico Victor Faces Choices on Economy*, N.Y. TIMES, July 7, 2000, § C, at 1 (relating that investors, analysts, and business leaders are adjusting to the end of the PRI's seventy-one year one-party rule and questioning how Fox intends to handle the complex economic issues facing Mexico).

52. See GAO Report No. 03-891, *supra* note 12, at 33 (highlighting the rapid evolution of maquiladora tax law that took place in the 1990s).

53. See *id.* (noting that "permanent establishment" is a concept found in virtually all double taxation treaties).

54. See *infra* notes 60-89 and accompanying text (reviewing the effects of the permanent establishment and Article 303 provisions).

55. See *infra* notes 93-119 and accompanying text (outlining the corrupt past in Mexico's government and law enforcement and describing the legislative gridlock in Mexico's Congress).

56. See *infra* notes 120-75 and accompanying text (expanding on the relationship between the U.S. economy and Mexico and Mexico's growing competition with other countries as a location for manufacturing).

A. Foreign Investors Leery of Uncertain Tax Policies

Prior to the Fox presidency, foreign corporations realized major benefits by establishing maquiladora operations in Mexico.⁵⁷ Two such benefits were duty-free imports and minimal taxation.⁵⁸ However, eroding tax benefits affected the establishment of new companies within the maquiladora industry in Mexico.⁵⁹

Since the 1960s, Mexico taxed maquiladoras on a low percentage of the maquiladora's fixed assets located in Mexico.⁶⁰ In 1998, Mexico changed the tax laws to label maquiladoras as permanent establishments⁶¹ in Mexico.⁶² By repealing the coveted "temporary" status of maquiladoras, this new identification removed a key incentive for foreign investors to conduct maquiladora operations in Mexico.⁶³ If Mexico begins taxing maquiladoras as permanent establishments, it would make countries, such as China, more appealing because permanent establishment tax laws would require companies to pay higher taxes.⁶⁴ Characterization as a permanent establishment and the accompanying threat of the permanent establishment tax particularly concerned the United States since ninety-five percent of maquiladoras are U.S. owned.⁶⁵ In addition, U.S. owned maquiladoras face double taxation by the

57. See GAO Report No. 03-891, *supra* note 12, at 33 (explaining that low taxes were the primary benefit for maquiladoras).

58. See *id.* (noting that until the mid-1990s maquiladoras enjoyed virtual freedom from taxation).

59. See *id.* at 28 (explaining that International Trade Commission research shows a growing number of textile and apparel products being produced in China instead of Mexico).

60. Michael C. McClintock, *Sunrise Mexico; Sunset NAFTA-Centric FTAA—What Next and Why?*, 7 SW. J. L. & TRADE AM. 1, 81 (2000); James F. Smith & Chris Kraul, *U.S., Mexico Reach Deal on Factory Tax; Business: Accord Boosts Latin Nation's Revenue while Temporarily Heading off Double Levies Against American-Owned Firms*, L.A. TIMES, Oct. 30, 1999, at A1; see GAO Report No. 03-891, *supra* note 12, at 33 (stating that the maquiladora tax regime remained constant for thirty years until the 1990s); see also Kevin G. Hall, *Maquiladoras Seek Tax Rule Relief*, J. COM., Jan. 25, 1996, at 3A (describing asset taxes as taxes on plants and equipment used in Mexico).

61. See GAO Report No. 03-891, *supra* note 12, at 33 (noting that permanent establishment companies may be taxed in the host country). A permanent establishment is typically a branch of a parent company from one country doing business in another "host" country, and is subject to taxes in both countries. *Id.*; see also Mauricio Monroy, *Harmonizing the Mexican Tax System with the Goals of the North American Free Trade Agreement (NAFTA)*, 35 SAN DIEGO L. REV. 739, 746 (1998) (explaining the elements that create classification as a permanent establishment). Acting through dependent agents in Mexico who have power to conduct business also creates a permanent establishment. *Id.* Mexican tax law defines a permanent establishment as an entity that partly or entirely conducts business in Mexico. *Id.*

62. See GAO Report No. 03-891, *supra* note 12, at 33 (indicating that Mexico adopted the permanent establishment concept as a part of its income tax law in 1981 but exempted maquiladoras from the tax until 1998). Mexico affirmed the permanent establishment tax in the U.S.-Mexico tax treaty of 1992. *Id.*

63. See McClintock, *supra* note 60, at 81 (noting that the permanent establishment tax means maquiladora plants could face the average corporate rate taxes of thirty-four percent).

64. See also GAO Report No. 03-891, *supra* note 12, at 28 (examining the differences between Mexico and China in the manufacturing industry). Corporate income taxes for Mexican-based maquiladoras are higher than China. *Id.*; see also Cañas & Coronado, *supra* note 18 (relating that the permanent establishment change to the Mexican tax code propelled the maquiladora industry into fiscal confusion with regard to income and customs taxation).

65. John Moody, *Maquiladoras' Tax Status Extended*, SAN DIEGO TRIB., Aug. 11, 2000, at C1; see Daniel McCosh, *Confusion Greeted New Tax Rules for Maquilas*, J. COM., Feb. 14, 2000, (World Trade), at 3

United States and Mexican government.⁶⁶ For that reason, the United States lobbied the Mexican government to delay the treatment of maquiladoras as permanent establishments.⁶⁷ In 2000, Mexico conceded to the United States and provided maquiladoras with two taxing options to avoid the permanent establishment tax.⁶⁸ Subsequently, in 2002, Mexico renewed this taxing option and the United States agreed to provide a foreign tax credit to U.S. firms that paid maquiladora income taxes to Mexico.⁶⁹

However, investors complain that the application process for the tax exemption is time consuming.⁷⁰ Despite the complaints, Mexico refuses to change the permanent establishment treatment referenced in Mexico's tax law until at least 2007.⁷¹ Ultimately, investors frequently cite the permanent establishment tax as a cause for uncertainty regarding investment in the maquiladora industry because it makes long-term financial planning impossible.⁷² This continuing uncertainty is a significant deterrent to further maquiladora investment in Mexico.⁷³

In addition to the permanent establishment tax, another tax law that affects foreign investment in Mexico is Article 303 of NAFTA.⁷⁴ This provision affects maquiladoras that rely on non-North American inputs because Article 303

(arguing that taxing maquiladoras as permanent establishments would prevent the industry from thriving and generating significant trade between the United States and Mexico).

66. See Cañas & Coronado, *supra* note 18 (illustrating the double taxation facing maquiladora corporations which maintain parent companies in the United States and a subsidiary maquiladora in Mexico).

67. See Andrea Mandel-Campbell, *Worries Persist After Tax Decision on Maquiladoras*, FIN. TIMES (London), Nov. 1, 1999, (World News), at 4 (revealing that negotiations between the United States and Mexico regarding the permanent establishment tax spanned six months).

68. See McClintock, *supra* note 60, at 81 (reporting that Mexico and the United States had to compromise on tax issues in order to preserve the maquiladora industry). Mexico assented to continue taxing maquiladoras on a percentage of their fixed asset value but raised this percentage to increase tax revenue. *Id.*; see also Shippey & Martin, *supra* note 22 (referring to the requirements maquiladoras need to comply with in order to circumvent the permanent establishment tax). Instead of the permanent establishment tax, the maquiladora must pay the greater of 6.9 percent of its assets or 6.5 percent of its costs; or, the maquiladora must secure an advanced pricing agreement from the Mexican government. *Id.*

69. See Shippey & Martin, *supra* note 22 at 276 (explaining that the agreement between Mexico and the United States extended beyond 2002); see also GAO Report No. 03-891, *supra* note 12, at 40 (stating the foreign tax credit was the result of a Second Additional Protocol to the United States-Mexico tax treaty).

70. See Cañas & Coronado, *supra* note 18 (noting that some maquiladoras have waited as long as three years to know their tax liability). Increased tax uncertainty existed because the exemptions for United States maquiladoras were set to expire in December 2002. *Id.*

71. See GAO Report No. 03-891, *supra* note 12, at 40 (summarizing the agreements reached between the United States and Mexico regarding the permanent establishment tax).

72. Cañas & Coronado, *supra* note 18. See GAO Report No. 03-891, *supra* note 12, at 33 (identifying the change in the permanent establishment provision as the most significant tax change in thirty years).

73. GAO Report No. 03-891, *supra* note 12, at 33; see Cañas & Coronado, *supra* note 18 at 5-7 (arguing that prolonging the fiscal uncertainty until 2007, in essence, passes the predicament onto the next administration).

74. See NAFTA, art. 303, 32 I.L.M. 289 (1993) (listing the specific statutory requirements for compliance); see also GAO Report No. 03-891, *supra* note 12, at 34 (detailing the background of Article 303 of NAFTA).

eliminates duties for imported inputs from a non-NAFTA country.⁷⁵ NAFTA envisioned a significant change in the maquiladora model.⁷⁶ Originally, maquiladoras provided duty drawbacks⁷⁷ for inputs imported to Mexico from any source, including non-NAFTA countries, but Article 303 repealed the maquiladora benefit that permitted choosing inputs from any country.⁷⁸ NAFTA scheduled the law for implementation seven years after signing the treaty.⁷⁹ Article 303 mandated that by the end of 2000, manufacturers could only exempt North American inputs from taxes.⁸⁰ However, compliance with Article 303 was impossible for all maquiladoras because at the outset, not every maquiladora in Mexico is North American.⁸¹ Furthermore, this provision essentially eliminated duty-free imports from non-NAFTA treaty countries.⁸² As a result, this NAFTA provision impairs maquiladoras that rely on non-NAFTA suppliers for inputs.⁸³

To complicate the situation, Mexico did not sufficiently prepare for future reliance on domestic suppliers during the seven-year grace period, as intended by Article 303.⁸⁴ The phasing out of this NAFTA benefit negatively affects Mexico's competitive edge over other leading countries of export.⁸⁵ However, in response to Article 303, the Mexican Economic Ministry instituted a promotional program, exempting maquiladoras from paying taxes on inputs generated in North America.⁸⁶ The Economic Ministry designed these exemptions to encourage maquiladoras to comply with Article 303.⁸⁷ The network of North American suppliers and inputs, contemplated by Article 303, requires significant changes in maquiladora input sources, particularly for Asian maquiladoras.⁸⁸ Despite the promotions put in place by Mexico, Article 303 eroded the competition among maquiladoras that depend on inputs from outside North America.⁸⁹

75. See GAO Report No. 03-891, *supra* note 12, at 34 (citing NAFTA as a major factor in the decrease in maquiladora production and employment).

76. *Id.*

77. *See id.* (defining "duty drawback" as the refund, waiver, or reduction of customs on imported goods).

78. *See id.* (contrasting the maquiladora duty drawback system with NAFTA's duty drawback system).

79. *See id.* (acknowledging that duty drawbacks for inputs of non-NAFTA origin ended January 1, 2001).

80. See Miguel Jauregui Rojas, *Review of Legal Developments in Mexico: 2000-2001*, 10 U.S.-MEX. L.J. 3, 12 (2002) (referring to the implications of Article 303).

81. *See id.* at 12 (relating that non-North American investors continue to rely on inputs from non-North American countries that do not receive the tax exemption).

82. *See* Cañas & Coronado, *supra* note 18, at 7 (discussing the effects of Article 303).

83. *See* GAO Report No. 03-891, *supra* note 12, at 34 (drawing attention to the closure of some maquiladora firms).

84. *See id.* at 34 (explaining that inputs from a non-NAFTA country are now taxed).

85. *See id.* (acknowledging that Article 303 affects maquiladoras that rely on non-NAFTA suppliers).

86. *See* Rojas, *supra* note 80, at 12 (illustrating that the Mexican government issued promotional programs to avoid financially destroying maquiladoras that rely on non-North American inputs).

87. *See id.* at 12 (explaining that the tax benefits will encourage maquiladoras to use North American inputs).

88. *See* GAO Report No. 03-891, *supra* note 12, at 35 (reporting that Japanese and other Asian-owned maquiladoras rely on inputs from Asia); *see also id.* at 36 (listing Asian companies that have left Mexico).

89. *See* GAO Report No. 03-891, *supra* note 12, at 35-36 (citing some maquiladoras as having cost increases in production of up to twenty percent).

B. Issues in Mexico's Political Climate

While the problems brought by Article 303 loomed in the background for seven years, Mexico's government did not respond swiftly to this or other problems that arose in the maquiladora industry.⁹⁰ Mexican business executives accuse the Fox Administration of lacking vigor in pursuing more foreign investing in Mexico.⁹¹ Consequently, maquiladora investment declined and immediate government action is necessary in order for the industry to regain its competitive edge.⁹²

The history of corruption in the police force as well as the government makes foreign investment difficult to address.⁹³ Mexican business representatives argue that in order to remain competitive, Fox needs to stop corruption.⁹⁴ The vice-president of Latin American operations for a Chicago-based industrial and chemical company doing extensive business in Mexico, recently stated, "Fox will have to address the crime situation, which has an impact on attracting foreign investment."⁹⁵ Corruption also affects spending because the World Bank⁹⁶ estimates that corruption costs Mexico nine percent of its Gross Domestic Product ("GDP").⁹⁷ In addition to the waste of capital, corruption results in unsafe streets, which discourage potential investors.⁹⁸

90. See *id.* at 40 (noting that the Mexican government was slow to respond to the maquiladora challenges). The Mexican government initially took a "wait and see" approach to the maquiladoras decline, in belief that they would be replaced by higher paying and more profitable industries. *Id.* In 2002, maquiladora representatives finally pressured the government to implement changes. *Id.*; see also Malkin, *supra* note 28, at 1 (acknowledging the Mexican government was slow to resolve the confusion over the new duties assessed on Asian components because of Article 303 and the tax status of maquiladora plants).

91. See Juan Forero, *Mexico Manufacturers Lose Business to China, A New King of Low-Cost Plants Emerges*, INT'L HERALD TRIB., Sept. 4, 2003, (Finance), at 14 (criticizing the government's failure to respond to the lower labor costs in China, which have surmounted Mexico's competitiveness).

92. See GAO Report No. 03-891, *supra* note 12, at 40 (indicating that the Mexican government needs to reform energy, infrastructure, and labor for the success of maquiladoras).

93. See Paulette L. Stenzel, *The U.S. and Mexico Sin Fronteras-Without Borders: Sustainable Development from a Local Perspective*, 27 WM. & MARY ENVTL. L. & POL'Y REV. 441, 478 & n.266, 490 (2002) (noting the corruption that endured for seventy-one years within the PRI, the Mexican government, and the police force).

94. See Forero, *supra* note 91, at 14 (stating that corruption needs to be addressed in order to remain competitive, since Chinese labor costs are about one-fourth lower than Mexican labor costs).

95. Weiner & Gori, *supra* note 8.

96. See The World Bank, *What is the World Bank*, (2004), at <http://web.worldbank.org/WBSITE/EXTERNAL/EXTABOUTUS/contentMDK:20040558~menuPK:34559~pagePK:34542~piPK:36600~theSitePK:29708,00.html> (last visited Mar. 3, 2004) (copy on file with *The Transnational Lawyer*) (explaining the function of the World Bank). The World Bank includes 184 countries that provide low-interest loans, interest-free credit, and grants to developing countries. *Id.*

97. *Opening Mexico; Don't Overlook Legacy of Transparency*, DALLAS MORNING NEWS, July 22, 2003, at 16A (reporting that the cost of corruption is more than the cost of education in Mexico) *Id.*

98. See Stenzel, *supra* note 93, at 493 (reporting that in 2002, private Mexican corporate executives hired former New York City Mayor Rudolph Giuliani to advise Mexico City on reducing crime). The executives are paying Giuliani and his associates 4.3 million U.S. dollars to make Mexico City a safe place to do business. *Id.*

Along with the history of corruption, President Fox also faces the challenge of a gridlocked and hostile Congress⁹⁹ that refuses to pass his legislation.¹⁰⁰ The PRI members in Congress consistently rally against Fox's plans and thwart his agenda.¹⁰¹ Furthermore, the Democratic Revolutionary Party ("PRD")¹⁰² is a left wing, liberal party that conflicts with Fox's party, the PAN, and its right wing, conservative philosophy.¹⁰³ For instance, the PRD's animosity toward Fox culminated in a 2003 incident where the PRD refused to pass the national budget.¹⁰⁴ Even the PAN, Fox's own political party, expressed dissatisfaction with several of Fox's policy decisions.¹⁰⁵ In addition, the PRI, PAN, and PRD are struggling with intra-party conflict.¹⁰⁶ Moreover, the Green Ecologist Party of Mexico ("PVEM")'s¹⁰⁷ formal withdrawal of support for President Fox further compounded the political tension in Mexico.¹⁰⁸

99. Mention of Congress, congressional, or legislature in this Comment is in reference to the Mexican Congress unless otherwise noted.

100. See Hale, *supra* note 46, at 13 (noting that Congress and Fox have reached an impasse concerning proposals to broaden the tax base, open the energy industry to foreign investment, and to liberalize the labor market). *But see infra* notes 180-219 and accompanying text (outlining the bills passed or amended by Congress which greatly affect the maquiladora industry).

101. Cf. Tim Weiner, *Corruption and Waste Bleed Mexico's Oil Lifeline*, N.Y. TIMES, Jan. 21, 2003, at A1 (providing a background to the corruption associated with the PRI and Mexico's oil company, Pemex). To defend the PRI's remaining control over Pemex, the PRI resists every effort to reform Pemex. *Id.* The PRI refuses to cooperate with Fox and change the Mexican Constitution to permit foreign investment in Pemex. *Id.*

102. See Wise, *supra* note 4, at 288 (commenting that in 1982, disaffected PRI party members formed the PRD political party). In 1988, the reigning PRI faced its first credible challenge by the PRD party for the presidency. *Id.* at 288-89. At that time, the middle class and educated urban voters voted for the PRD candidate. *Id.* at 292. The former PRI members, who launched the PRD party, originated primarily from the disgruntled left wing ranks of the PRI. *Id.* at 292. The 1994 presidential elections revealed that the PRD party declined in popularity because PRI political decisions had won back the vote of the poor. *Id.* at 296. However, in 1997, the voters changed again, and the southern, poor, and agricultural-producing states sided with the PRD. *Id.* at 303; see also *Mexican Political Parties*, *supra* note 4, at 12A (labeling the PRD as center-left on economic and social issues); cf. M. Delal Baer, *Fox Faces Thunder on the Left*, L.A. TIMES, Nov. 26, 2000, at M1 (asserting the PRI has an ally with the left wing PRD).

103. See Michael Stott, *Mexico Celebrates 'People's Victory'*, HERALD (Glasgow), July 8, 1997, at 10 (stating that in Mexico's July 1997 election, the right wing PAN received twenty-seven percent of the votes, and the left wing PRD collected twenty-six percent of the votes).

104. See David Gaddis Smith, *Mexico City Mayor Looking Like Successor to Fox; Lopez Obrador Very Popular in Nation*, SAN DIEGO UNION-TRIB., Feb. 16, 2003, at A19 (recounting that the PRD believes that it works to its electoral advantage to remain in extreme opposition to the PAN and Fox); see also Rojas, *supra* note 80, at 6 (asserting that the PRD criticizes the President's policies and decisions). For example, the PRD rejected an airport in Mexico City that would have been a principal source of growth. *Id.*; *Dismal Year Ends with Sensible Budget*, LATIN AM. ECON. & BUS., Dec. 2003 (observing that Congress finally passed the 2004 budget on December 31, 2003).

105. See Wise, *supra* note 4, at 305 (indicating the primary complaints of the PAN party against President Fox). The PAN party objects to President Fox's desire to deal directly with the public, that he appointed a diverse cabinet, and his independent stance on policy issues) *Id.*

106. See *id.* at 305 (outlining the tensions within the PRI, PAN, and PRD parties since the 2000 elections).

107. See *Mexican Political Parties*, *supra* note 4, at 12A (stating that the PVEM formed in 1991 and promotes environmental and youth issues).

108. See Rojas, *supra* note 80, at 6 (explaining that the PVEM dissolved its union between the PAN and President Fox).

In 2000, the PRI opposition only held a slight majority in the Mexican Congress.¹⁰⁹ After the recent congressional elections in July 2003, the PRI strengthened its position in Congress.¹¹⁰ Presently, 282 members of Congress belong to the PRI, and the PAN holds 197 members.¹¹¹ Even though the PRI has the most members, it lacks a sufficient number to control the Congress.¹¹² Since the PRD and the PVEM also now hold a significant number of representatives, enacting legislation is challenging at best.¹¹³ For example, the recent proposed energy and labor reform bills were unsuccessful in legislature.¹¹⁴ The Fox Administration introduced an energy reform bill in August 2002, but it stalled in Congress.¹¹⁵ Legislators opposed aspects of the bill dealing with privatization because it would require amending the Mexican constitution.¹¹⁶ President Fox also introduced a labor reform package to Congress, representing a compromise between labor groups, business, and government, but Congress refused to pass the bill.¹¹⁷ As of January 2004, Mexico's sharply divided Congress persists in refusing to enact fiscal, energy, and labor reforms and permits Fox to only pass a limited number of laws regarding foreign investment.¹¹⁸ Thus, Congress prevents Fox from passing much-needed reforms and causes foreign investors to invest in other countries.¹¹⁹

109. See *A New Sun; Overview*, HOUS. CHRON., Nov. 26, 2000, (Special), at 2 (listing the breakdown of representatives in the 628 member Congress). The PRI, PAN, PRD, and PVEM hold 271, 252, 66, and 22 seats, respectively. *Id.* The bicameral Mexican Congress includes 500 seats for the Chamber of Deputies and 128 seats for the Senate. *Id.*

110. See John Authers, *PRI's Gains in Mexico Poll Herald Horsetrading with Fox Former Ruling Party*, FIN. TIMES (London), July 15, 2003, (The Americas), at 3 [hereinafter *PRI's Gains in Mexico*] (reporting that the Federal Electoral Institute announced that Fox's party, the PAN, has a minority in Congress).

111. See *Composición de la Cámara por Partido [Composition of the Chamber by Party]*, available at <http://www.cddhcu.gob.mx/> (last visited Feb. 9, 2004) (copy on file with *The Transnational Lawyer*) [hereinafter *Composition of the Chamber by Party*] (listing the current number of members of the Mexican Chamber of Deputies); see also *Grupos Parlamentarios [Parliamentary Groups]*, available at <http://www.senado.gob.mx/legislatura.php?ver=grupos&lng=es> (last visited Feb. 9, 2004) (copy on file with *The Transnational Lawyer*) [hereinafter *Parliamentary Groups*] (portraying the current makeup of the Mexican Senate).

112. See *PRI's Gains in Mexico*, *supra* note 110, at 3.

113. See *Composition of the Chamber by Party*, *supra* note 111 (stating that in the Chamber of Deputies the PRD holds 95 seats and the PVEM holds 17 seats); see also *Parliamentary Groups*, *supra* note 111 (acknowledging that in the Mexican Senate the PRD holds 16 seats and the PVEM holds 5 seats).

114. See GAO Report No. 03-891, *supra* note 12, at 40-41 (highlighting examples of conflict in the Mexican Congress).

115. See *id.* at 40 (stating that Congress refused to pass the bill even though government officials and industry representatives stress that Mexico has an urgent need for energy reform).

116. *Id.*

117. *Id.* at 41.

118. See Jason Lange, *Analysts: Mexn [sic] CenBank's Dollar Sales to Boost Peso*, MARKET NEWS INT'L, Jan. 21, 2004 (noting that since 2000, Congress has prevented President Fox from passing fiscal, energy, and labor reforms); see also *infra* notes 180-219 and accompanying text (outlining the bills passed or amended by Congress and Fox that greatly affect the maquiladora industry).

119. See Lange, *supra* note 118 (noting that economists say reforms would reduce labor and energy costs and spur economic growth).

C. Mexico and the Global Economy

The Fox Administration and the Mexican Congress are aware that the United States economy directly affects the Mexican economy.¹²⁰ From 1994 through 2001, the United States accounted for sixty-seven percent of the total foreign investment in Mexico.¹²¹ The maquiladora industry is especially sensitive to the economic situation of the United States.¹²² First, ownership and production directly connect U.S. owned maquiladoras with U.S. companies.¹²³ Second, in 2001 alone, maquiladoras exported ninety-eight percent of their products to the United States.¹²⁴ Third, maquiladoras import seventy-nine percent of inputs from the United States.¹²⁵ Accordingly, a slowdown or improvement of the United States economy significantly affects the maquiladora industry.¹²⁶ To illustrate, the 2001 recession in the United States caused a 400,000-job loss in the maquiladora industry.¹²⁷ In addition, 420 maquiladora plants closed between 2001 and 2002.¹²⁸ Furthermore, the recession in the United States decreased maquiladora imports of U.S. inputs.¹²⁹ However, the U.S. economy is not the only global influence on the maquiladora industry.

Investors are also concerned with the appreciation of the Mexican peso.¹³⁰ Since 1998 and continuing after President Fox's election, the Mexican peso has steadily increased in value.¹³¹ However, a stronger currency translates to higher

120. GAO Report No. 03-891, *supra* note 12, at 26; see Brendan M. Case, *Moves by Telmex, TV Azteca boost Mexico's Bolsa*, DALLAS MORNING NEWS, Sept. 8, 2000, at 11D (asserting that the U.S. economy has a "profound influence on Mexico").

121. See Robert Donnelly, *Dealing with the Rising Sun*, BUS. MEXICO, May 1, 2003, available at 2003 WL 6179595 (copy on file with *The Transnational Lawyer*) (noting that Mexico received \$91 billion in foreign direct investment from 1994 to 2001).

122. GAO Report No. 03-891, *supra* note 12, at 26.

123. *Id.* at 9 (listing top U.S. firms that maintain maquiladoras in Mexico). Delphi, RCA, Ford Motor Company, Tyco, General Electric, General Instruments, Johnson & Johnson, and ITT all are maquiladora employers. *Id.* Seventy-nine of the top one-hundred maquiladora employers are from the United States. *Id.*

124. *Id.* at 8.

125. *Id.*

126. *Id.* at 26, 57 (citing the U.S. economic slowdown as a significant determinant of a decline in maquiladora employment).

127. See David Bacon, *Maquiladora Bosses Play the China Card: Companies in Mexico Threaten to Relocate to China*, DOLLARS & SENSE, Sept. 1, 2003, at 20 (providing the decreased employment statistics according to Marco Antonio Tomas of Mexico City's Center for Labor research).

128. Cañas & Coronado, *supra* note 18, at 5.

129. See John D. Breidenstine, *Best Prospect Sectors in Mexico*, U.S. COMMERCIAL SERVICE (Nov. 2003), at http://www.export.gov/exportamerica/NewOpportunities/no_mexico_1103.html (last visited Mar. 3, 2004) (copy on file with *The Transnational Lawyer*) (mentioning that in 2002, the slowdown of the U.S. consumer electronics market caused a decrease in Mexican assembly). Maquiladoras import U.S. inputs to use for assembly into finished products to export. *Id.*

130. See GAO Report No. 03-891, *supra* note 12, at 3 (explaining Mexico's appreciated peso has eroded its competitiveness in the maquiladora industry).

131. See *id.* at 31-32 (graphing the real dollar exchange rate of the Mexican Peso from 1995 through 2002); see also John Authers, *Investors Ride the Mexican Trade Wave: Foreign Money is Flooding into a Booming Economy*, FIN. TIMES (London), Apr. 15, 2002, (Survey-FTFM), at 7 (observing that in late 1998, the

operating costs for maquiladora owners.¹³² Historically, growth periods for maquiladoras revolved around a depreciated peso because a devalued peso helped maquiladoras control costs.¹³³ Thus, maquiladora owners relied on peso devaluations to absorb higher labor costs.¹³⁴ Prior to the Fox presidency, the government steadily devalued the peso to make Mexican exports more competitive and enhance the country's position as a low-cost manufacturing location.¹³⁵ With the now higher peso, maquiladoras are sensitive to the peso exchange rate because they incur production costs in pesos.¹³⁶ An appreciation of the real exchange rate of the peso makes goods exported from Mexico more expensive.¹³⁷ This results in investors choosing to invest elsewhere after comparing Mexico's currency with other countries like China, whose currency has decreased in value within the past five years.¹³⁸ This decrease allows China to compete more effectively for foreign investors in contrast with Mexico.¹³⁹

To offset the rising peso Mexico needs to update its infrastructure,¹⁴⁰ energy, and water supply to remain competitive for foreign investment.¹⁴¹ Mexican business representatives urge Fox to cut taxes, lower electricity costs, and improve roads.¹⁴² However, energy and infrastructure issues are difficult to address when Mexican taxpayers are accustomed to paying little or no taxes to

Mexican peso measured 10.8 pesos to the U.S. dollar). In April 2002, the peso valued nine pesos to the dollar. *Id.*; GAO Report No. 03-891, *supra* note 12, at 31 (stipulating that the peso has consistently appreciated against the dollar in real terms since 1998). This trend of a strong peso has continued, even through the maquiladora decline. *Id.*

132. GAO Report No. 03-891, *supra* note 12, at 31.

133. *See id.* at 30-31 (noting that in 1984, a devalued peso prompted a three-year surge in U.S. automotive industry investments in maquiladora plants). In addition, the peso devaluation in 1994 spurred the expansion of Mexico's maquiladoras until 1999. *Id.*; *see also* Cañas & Coronado, *supra* note 18 (stating that Mexico's recent macroeconomic stability has kept the peso strong).

134. *See* Cañas & Coronado, *supra* note 18, at 5 (stipulating maquiladoras can no longer expect a depressed peso to offset increasing labor costs); *see also* Rojas, *supra* note 80, at 11 (addressing the issue that companies need to control labor and management in order to keep up with an increased peso).

135. *See* Martyn Warwick, *Mexico is Poised for Revolution; Telecommunications*, INFO. ACCESS COMPANY, May 1995, at 38 (relating that International Technology Consultants predict that devaluation of the peso will make Mexican exports more competitive); *see also* Wise, *supra* note 4, at 288 (stipulating that the Mexican government devalued the peso to expand exports).

136. *See* GAO Report No. 03-891, *supra* note 12, at 58 & n.4 (discussing maquiladoras with products destined for the United States). Goods exported to the United States generate revenue in dollars. *Id.*

137. *See id.* at 58 (articulating that goods made in the United States are less expensive as compared to Mexico when the peso is elevated).

138. *Id.* at 31.

139. *See id.* (comparing the depreciation of the Chinese currency, the yuan, with the Mexican peso).

140. Roads, ports, and airports need to be modernized.

141. GAO Report No. 03-891, *supra* note 12, at 40; Robin Emmott, *Potent Peso is Put through its Paces*, EUROMONEY, Feb. 1, 2002; *see* Lin, *supra* note 22, at 93 n.110 (explaining that a decreased water supply especially constrains the textile industry, which requires sufficient water for the dyeing, printing, and finishing process).

142. *See* Forero, *supra* note 91, at 14 (identifying taxes, electricity, and roads as problems to address to remain competitive with China).

support their government.¹⁴³ In addition, funding for infrastructure and energy reform has encountered stiff resistance in Congress.¹⁴⁴ Currently, middle class professionals shoulder the majority of the tax burden of Mexico, while the industries pay virtually no taxes.¹⁴⁵ As a result of the low taxes, Mexico's inadequate infrastructure pales in comparison with China's coastal ports, which appeal to manufacturers.¹⁴⁶ Poor infrastructure is particularly harmful for the maquiladora industry.¹⁴⁷ Investors have elected to locate operations near Mexico's major cities or the United States-Mexico border, which avails maquiladoras of improved infrastructure.¹⁴⁸ With respect to electricity, Mexico's state-run company charges more for electricity than the United States and substantially more than China.¹⁴⁹

Competition with other countries has increased as many nations around the world have adopted export-oriented manufacturing plants similar to Mexico's maquiladoras.¹⁵⁰ For example, India and Pakistan offer export industries fiscal and institutional incentives, as well as fully developed infrastructure in the form of industrial parks.¹⁵¹ In addition, El Salvador has cheaper labor costs and less-stringent regulations than Mexico,¹⁵² while both the Dominican Republic and Honduras have lower manufacturing wages than Mexico.¹⁵³ However, out of all the country-competitors, China is the most worrisome for Mexico in the area of manufacturing.¹⁵⁴ The maquiladora industry's decline in employment is due

143. See Day, *supra* note 41 (quoting Finance Ministry Spokesman, Raul Ostos-Martínez, who urges that the government needs to create a new tax culture to accustom Mexicans to paying more taxes); see also Wise, *supra* note 4, at 305 (indicating that in 2000, Mexico needed tax reform because public revenues stagnated at fifteen to eighteen percent of GDP).

144. See Day, *supra* note 41 (providing a background of Mexico's political climate). After seventy years of the same political party in power, Congress is unaccustomed to negotiating to pass legislation. *Id.*

145. See Rojas, *supra* note 80, at 13 (demanding that industries contribute to Mexico's tax burden).

146. See Field, *supra* note 40, at 19 (comparing China's infrastructure to Mexico's remote locations, which have poor access to major land routes, railroads, and seaports). Although major routes have improved, secondary roads remain very slow for truckers to traverse. *Id.*

147. See Lin, *supra* note 22, at 93 (stating that maquiladora investors find it easier and less expensive to truck or ship materials across the border than to transport goods inside Mexico).

148. *Id.* at 94.

149. Ferris, *supra* note 11, at 4H.

150. See Cañas & Coronado, *supra* note 18, at 8 (articulating the challenge of global competition for the Mexican maquiladora industry).

151. See *id.* (analyzing the benefits of manufacturing plants located in other countries besides Mexico).

152. See Forero, *supra* note 91, at 14 (reporting that Gicsa Corporation, a blue jeans manufacturer for Target and American Eagle Outfitters, is considering moving to El Salvador where labor is twenty-two percent less expensive).

153. See GAO Report No. 03-891, *supra* note 12, at 28 & n.21 (enumerating 2002 statistics, which show Mexican workers earning \$2.50 an hour, Dominican workers earning \$1.50 an hour, and Honduran workers earning \$1.30 an hour). Mexican wages are almost sixty-seven percent higher than the Dominican Republic and ninety-two percent higher than Honduras. *Id.*

154. See *id.* at 26 (discussing the majority of industry association representatives who referred to the role of China in the decline of maquiladoras); see also Cañas & Coronado, *supra* note 18, at 8 (listing the different plants that have transferred from Mexico to China). In 2002, Royal Philips Electronics moved its plant and 900 jobs to China, and Ameses de Juárez, an automobile parts maquiladora, transferred to China and laid off 800

partially to investors transferring production to Asia.¹⁵⁵ In particular, China boasts many benefits for foreign investors that are lacking in Mexico, including lower labor, electricity, and water costs.¹⁵⁶ China also offers investors lower, more competitive corporate income tax rates.¹⁵⁷ In 2001, China joined the World Trade Organization (“WTO”).¹⁵⁸ This made China more attractive for foreign investment because China now has lower tariffs on exported goods by virtue of the Most Favored Nation status.¹⁵⁹

In addition to lower tax rates and WTO membership, the non-democratic Chinese government is easily able to govern globalization.¹⁶⁰ In Mexico, democracy and multi-party conflicts make it more difficult for the President and Congress to agree on efforts to globalize.¹⁶¹ Previously, the one-party PRI control made the Mexican Congress the equivalent of a rubber stamp on any legislation the PRI wanted to enact.¹⁶² Currently, the tri-party control in Congress creates a legislative gridlock because three strong parties make it difficult to obtain a majority and pass needed legislation.¹⁶³ On the other hand, investors are mindful of consumers who look down upon manufacturing performed in non-democratic countries.¹⁶⁴ In 2003, the economy minister of Mexico, Fernando Canales, stated

Mexican workers. *Id.* Sanyo Electric Company also laid off 1,884 employees and relocated to China and Indonesia. *Id.*

155. Hale, *supra* note 46, at 13.

156. See GAO Report No. 03-891, *supra* note 12, at 28 (discussing the advantages China has over Mexico); see also Malkin, *supra* note 28, at 1 (detailing China’s benefits over Mexico, including a sophisticated base of manufacturing suppliers, tax breaks, well-trained engineers, and efficient ports).

157. GAO Report No. 03-891, *supra* note 12, at 28.

158. *Id.* at 26 & n.18.

159. See Raj Bhala, *Conference: Interfaces: From International Trade to International Economic Law: Enter the Dragon: An Essay on China’s WTO Accession Saga*, 15 AM. U. INT’L L. REV. 1469, 1479-80 (reviewing the benefits of WTO membership). Most Favored Nation status removes the high tariffs China previously faced when exporting goods. *Id.* at 1479. For example, in 1994, China produced one-seventh of the world’s clothing and shoes. *Id.* Until China entered the WTO, those goods would face tariffs as high as twenty-three percent in the European Union. *Id.* WTO membership makes tariffs on those same shoes and clothes only 4.8 percent. *Id.* In 1994, the World Bank estimated that if China joined the WTO, it would obtain greater access to foreign markets and would increase exports by thirty-eight percent. *Id.* at 1480.

160. See Hale, *supra* note 46, at 13 (relating that communism in China assists the country’s global expansion as a trading nation). Mexico can only meet China’s challenge to foreign investment if the various political parties in Mexico come to agreement. *Id.*

161. See *id.* (summarizing the major incidents in Mexico’s political history). The Mexican Revolution from 1910 to 1916 led to the one-party PRI government. *Id.* Now that a different political party controls the presidency, Congress resists accepting the PAN and President Fox. *Id.* This could make President Fox unproductive and unable to pass his legislation. *Id.*

162. See Wise, *supra* note 4, at 290-306 (contrasting Mexico’s current gridlocked Congress with the PRI era, where the Mexican Congress used its two-thirds majority to approve all of the PRI’s proposed constitutional amendments).

163. See *id.* at 306 (noting that the Mexican Congress closely scrutinizes and modifies all of the presidential bills proposed by Fox). President Fox must fiercely negotiate to pass legislation. *Id.*

164. See Sandoval, *supra* note 14, at 1D (quoting a U.S. official who recently told a group of U.S. and Mexican business leaders that, “Mexico has two things China does not, the United States right next door and a democracy.”).

that China does not respect human rights and is not a country with a solid political and economic institution.¹⁶⁵ Nevertheless, despite the economy minister's opinion of consumers, a Japanese electronics firm, TDK, transferred its plants to China because Chinese laborers will work for one-third the cost of Mexican wages, which translates to less-expensive products for consumers.¹⁶⁶ Cheap labor is also eclipsing the advantage of Mexico's close-proximity to the United States because savings in labor expenses offset shipping costs from China.¹⁶⁷ However, larger products still cost more to ship from China.¹⁶⁸ Consequently, for larger products, Mexico becomes more cost-efficient, notwithstanding higher labor expenses.¹⁶⁹

In contrast with labor groups in other countries, especially China, Mexico's labor unions are demanding more benefits and higher wages.¹⁷⁰ Various collective bargaining agreements negotiated by labor unions are disastrous for Mexico's ability to compete with other countries.¹⁷¹ The high wage and benefit increases associated with collective bargaining agreements are problematic for Mexico's economy because manufactures will choose to locate in countries without labor unions.¹⁷² Mexican workers are in jeopardy of losing their jobs to foreign competition if they do not change their tactics towards employers.¹⁷³ However, the Mexican government disagrees on how to balance labor rights against retaining employers.¹⁷⁴ For instance, in 2001, Sony lowered wages and benefits to

165. Forero, *supra* note 91, at 14.

166. See *Mexico: Maquila Doors Closing*, *supra* note 27 (stating Mexican workers earn \$1.47 per hour, but Chinese workers will work for one-third of that wage). TDK transferred its plants to China in January 2003. *Id.*; see also *Mexico's Broken Dream*, *supra* note 11, at 4H (noting that Chinese workers earn sixty-one cents per hour, and Mexican manufacturing workers earn \$2.08 per hour).

167. See *Mexico: Maquila Doors Closing*, *supra* note 27 (finding that China's less expensive operating conditions more than compensate for the trans-Pacific shipping costs). Shipping in large volumes makes it more economical. *Id.*

168. *Id.*

169. See *id.* (relating that Pioneer, a Japanese electronics firm, produced its smaller car speakers in Shanghai but kept its large, customized car speakers in Mexico). The cost of shipping the large speakers from China was too expensive. *Id.*

170. See Toh Han Shih, *Low Wages Help Region Maintain its Edge*, S. CHINA MORNING POST, Dec. 8, 2003, (Business Post), at 2 (asserting that China has no independent labor unions to struggle for higher wages).

171. See Rojas, *supra* note 80, at 3 (illustrating an example of the recent Volkswagen bargaining agreement, which increased wages by fourteen percent, including benefits).

172. See *id.* at 3 (arguing that Mexican workers need to stop demanding salary increases in order to preserve their employment).

173. See *id.* at 8 (stating that "Mexican workers are not productive in real terms or when compared to labor in other countries."). In addition, aggressive labor unions threaten maquiladora existence in Mexico. *Id.*

174. See Bacon, *supra* note 127, at 20 (relating that the Coalition for Justice in the maquiladoras agrees that lower wages are preferable to no employment). Workers face maquiladora neighborhoods with dilapidated schools, hospitals, refuse collection, and sewer systems. *Id.* However, since companies threatened to take investments to China, Fox proposed to amend the labor law to eliminate traditional worker protections. *Id.*; see also Talli Nauman, *Development in Mexico: As Established Policies Are Nurtured, the Hopes of Many Mexicans Wither on the Vine*, BORDERLINES, Oct. 1, 2001, at 1 (stating that analysts express serious concerns about wages, working conditions, and training opportunities).

workers under the threat of moving the entire manufacturing plant to China altogether.¹⁷⁵ Mexicans conclude that employment in poor working conditions is better than no employment.¹⁷⁶ Therefore, to prevent maquiladoras from closing their plants in Mexico, President Fox has responded with several important laws.

IV. THE FOX ADMINISTRATION'S RESPONSE TO FOREIGN INVESTMENT PROBLEMS IN MEXICO

President Fox has struggled to strengthen foreign investment in Mexico and address the problems of the maquiladora industry since taking office in 2000.¹⁷⁷ Although reforms are slow and laws are difficult to enact amidst Mexico's splintered Congress,¹⁷⁸ President Fox has managed to approve a number of laws, which positively affected foreign investment in Mexico, particularly in the maquiladora industry.¹⁷⁹ Specifically, President Fox addressed changes to tax policies, Mexico's political climate, and Mexico's relationship with the global economy.

A. *Changes to Tax Policies*

President Fox has successfully lowered taxes for maquiladoras by establishing the Sectoral Promotion Program ("PROSEC"), the Information Technology Agreement ("ITA Plus"), and the Temporary Importation Program for the Production of Articles for Export or ("PITEX"). Fox has also passed laws that combat the uncertainty surrounding the permanent establishment tax and provide additional tax exemptions for maquiladoras.

First, in 2000, the Mexican legislature enacted PROSEC, which both reduces tariffs for non-North American maquiladoras¹⁸⁰ and offsets the negative effects brought on by the changes in NAFTA.¹⁸¹ PROSEC enables tariff-free entry of non-

175. See Bacon, *supra* note 127, at 20.

176. See Nauman, *supra* note 174, at 1 (acknowledging that companies make Mexicans fearful of losing their jobs so they accept lower wages).

177. See Susan Ferriss, *Mexican President Ends U.S. Trip*, Cox News Service, Nov. 6, 2003, (Business), at 4H (reporting Fox discussing Mexico's problems with attracting foreign investment to Mexico, specifically the maquiladora industry).

178. See generally *supra* notes 99-119 and accompanying text (reviewing the gridlock in Mexico's Congress).

179. See *infra* notes 180-219 and accompanying text (outlining the bills passed or amended by Congress and Fox that greatly affect the maquiladora industry).

180. See GAO Report No. 03-891, *supra* note 12, at 35 & n.25 (reporting that to comply with Article 303 of NAFTA, Canada chose to eliminate hundreds of its most favored nation duties on inputs).

181. See *id.* at 39 (noting that in response to the crisis in the maquiladora industry, Mexico enacted PROSEC to reduce the impact of Article 303); GAO Report No. 03-891, *supra* note 12, at 34; Rojas, *supra* note 80, at 12 (articulating the requirements of Article 303); see also *supra* notes 74-89 and accompanying text (explaining the implications of Article 303). The provision eliminated the tax waivers for non-North American maquiladoras.

NAFTA inputs not readily available through a NAFTA partner.¹⁸² However, the application process that requires tracking the origin of thousands of production parts is extensive.¹⁸³ Additionally, the Mexican government damaged investor confidence in the PROSEC program by revoking many tax exemptions that maquiladoras were relying on under PROSEC.¹⁸⁴ Maquiladora representatives complained that PROSEC did not provide enough assistance to compensate for the effects of Article 303 of NAFTA.¹⁸⁵ Further, U.S. foreign investment declined because of PROSEC.¹⁸⁶ The program decreased the value of NAFTA's duty-free exports for U.S. suppliers.¹⁸⁷ Consequently, to enhance PROSEC for foreign investors, Mexico expanded the list of products eligible for tariff reduction under PROSEC throughout 2001 and 2002 enabling investors to obtain more exemptions.¹⁸⁸

Second, in April 2002, Fox amended the maquiladora and PITEX decrees to eliminate the tedious tracking formerly required for tax reasons.¹⁸⁹ This amendment reduces the administrative burden for maquiladora and PITEX companies.¹⁹⁰ Mexico originally established PITEX in 1990 as a viable foreign investment alternative to maquiladoras¹⁹¹ to permit companies to import inputs

182. See Cañas & Coronado, *supra* note 18 (relating that the Mexican government passed PROSEC in response to industry appeals over rising tariffs). The program permits maquiladoras to apply for reduced tariffs of up to five percent. *Id.*

183. See *id.* (portraying the PROSEC process as tedious).

184. See Steven B. Zisser, *Rules Still Unclear for Mexican Maquiladora Program*, Danzas AEI, Issue 298 (Apr. 2001), available at <http://www.ca.danzas.com/frameset.cgi?winLocation=http://www.ca.danzas.com/worldwide/northamerica/resource/298.html> (last visited Mar. 4, 2004) (copy on file with *The Transnational Lawyer*) (reporting that the Mexican government removed hundreds of Harmonized Tariff Schedule numbers that were previously covered under PROSEC). "Unlike the United States, Mexican Decrees are subject to immediate modifications or revocations without any opportunity for a challenge or comment". *Id.* For an explanation of the term "HTS numbers" see Donald L. Fischer, *Import ABCs—Knowledge of Classification Rules Helps Importers Determine Duties*, J. COM., Nov. 6, 1996, (Global Commerce), at 2C (explaining that the HTS numbers resulted from an agreement of nations belonging to the WTO). The HTS number describes the commodity and its appropriate duty rate. *Id.* Under NAFTA, items with certain HTS numbers are imported duty free. *Id.*

185. See GAO Report No. 03-891, *supra* note 12, at 39 (stating "PROSEC was too restrictive because it applied to very few imported inputs").

186. See Breidenstine, *supra* note 129 (explaining that the PROSEC program has lessened the value of the duty exemption enjoyed by the United States for products made in Mexico). Since duty-free entry for U.S. suppliers of electrical components is less competitive, foreign investment originating from the United States decreased. *Id.*

187. See *id.* (noting that PROSEC established most-favored nation tariffs of five percent for many categories of industrial inputs, which positively affected some foreign investors, but negatively affected U.S. investors).

188. See GAO Report No. 03-891, *supra* note 12, at 39 (noting that the list of products eligible for tariff reduction "expanded to include more than 16,000 products from twenty-two industry sectors, including electronics, textiles, and apparel").

189. See Edmundo Elías-Fernández, *How Latest Changes to Mexican Customs and Laws Impact Exporters*, MANAGING EXPORTS, Mar. 2003, at 1 (arguing that the new decree is a major breakthrough for maquiladora and PITEX owners).

190. See *id.* at 1 (noting that investors previously tracked the machinery and equipment for five years).

191. See Justin Gazer Rice, Comment, *PITEX and Maquiladora Import Programs: A Working Guide and Comparative Evaluation*, 33 TEX. INT'L L.J. 365, 368-69 (1998) (comparing the differences between the PITEX and maquiladora programs).

duty-free.¹⁹² While maquiladoras are usually located in northern Mexico along the U.S.-Mexico border, PITEX companies more often locate in the interior of Mexico.¹⁹³ As a result, PITEX companies typically use more Mexican inputs than maquiladoras.¹⁹⁴

Third, in September 2002, Mexico and fifty-eight other countries signed ITA Plus, which removes tariffs from electronic and high technology inputs, regardless of the country of origin.¹⁹⁵ ITA Plus will gradually remove tariffs from semi-finished and finished products in electronic and high technology sectors.¹⁹⁶ ITA Plus will eliminate most of the costs in the domestic productive chain and allow the domestic market to grow and allow the administration to save on imports and exports.¹⁹⁷

Fourth, in October 2002, Fox and the Mexican Congress signed several tax laws to benefit maquiladoras. The new rules provide a basis for companies to establish, expand, or maintain export-oriented manufacturing operations in Mexico with a high level of certainty regarding taxes.¹⁹⁸ Chiefly, the government passed a law lowering the corporate income tax rate, which includes maquiladoras, one percent each year until 2005.¹⁹⁹ In addition to lower corporate taxes, the legislature devised a simpler formula for maquiladoras to avoid the permanent establishment tax.²⁰⁰ Maquiladoras no longer need to apply for an "advance-pricing agreement" to avoid the permanent establishment tax.²⁰¹ The legislature also devised a simpler formula for calculating the transfer price that

192. See GAO Report No. 03-891, *supra* note 12, at 6 & n.4 (explaining that Mexico "PITEX requires companies to export a minimum of thirty percent [30%] of their total annual sales").

193. See *id.* at 6 n.4 (contrasting maquiladoras with PITEX companies).

194. *Id.*

195. See *id.* at 39 (stating that Mexican officials believe that ITA Plus may help reduce the administrative burden on maquiladoras).

196. See *id.* at 39 & n.28 (mentioning that Mexico did not formally commit to these tariff reductions under the WTO, which can be removed at any time).

197. *Electronics Industry to Reduce Prices on 3,200 Products with ITA Plus*, CORP. MEX., Sept. 11, 2002 (illustrating that ITA Plus reduces taxes on 209 products beginning September 2002, twenty-two products beginning January 2003, and sixty-one products beginning January 2004).

198. John A. McLees, Jaime Gonzalez-Bendiksen, & Carlos Angulo, *Mexico Enacts Major Improvements to its Maquiladora Tax Regime*, TAX ANALYSTS WORLDWIDE TAX DAILY, Jan. 27, 2003 (advising that the previous uncertainty surrounding Mexico's tax laws undermined its ability to compete for new foreign investment).

199. See Manuel Solano, *Spate [sic] of Recent Tax Developments in Mexico Offers Glimpse of Changes in Store for 2004*, TAX ANALYSTS WORLDWIDE TAX DAILY, Nov. 19, 2003 (stating that the corporate income tax rate will fall from thirty-five percent in 2002 to thirty-four percent in 2003 and so forth until 2005); see also *Mexico: Maquila Doors Closing*, *supra* note 27 (noting that legislation lowered the corporate income tax rate).

200. See *supra* notes 60-73 and accompanying text (defining and reviewing the effects of the permanent establishment tax); see also McLees et al., *supra* note 198 (identifying the new amendment to the Income Tax Law as Article 216-Bis).

201. *Mexico: Maquila Doors Closing*, *supra* note 27; see McLees et al., *supra* note 198 (explaining that maquiladoras with capital-intensive operations with substantial foreign-owned assets will usually elect an advance pricing agreement). Even with the high administrative costs and uncertainties associated with APAs, the agreements are still lower than the other options under the permanent establishment tax exemption. *Id.*

foreign firms must pay in order to maintain the exemption from the permanent establishment tax.²⁰²

Finally, in October 2003, Fox and the legislature agreed to provide maquiladoras with an additional tax exemption.²⁰³ The new law recognizes that maquiladoras constitute an important source of employment for Mexico and the Fox Administration has a policy of establishing mechanisms to promote maquiladoras.²⁰⁴ The income tax exemption amends the prior 2002 income tax law.²⁰⁵ The tax exemption seeks to make Mexico more competitive for low-cost manufacturing, in comparison with other countries, primarily China.²⁰⁶

In conclusion, the changes in PROSEC and PITEX, the new ITA Plus law, and the new tax exemptions have provided maquiladoras with more incentives to invest in Mexico. However, further changes in the political climate and the global economy are also necessary to entice foreign investment to Mexico.

B. Changes in Mexico's Political Climate

In addition to changes in taxes, Fox has also changed the political environment in Mexico. Pressure from the maquiladora industry caused the Mexican government to create the Presidential Council for Competitiveness, to approve the Decree for the Development and Operation of the Maquiladora Export Industry ("Maquiladora Decree"), and to pass the Freedom of Information Law.

In July 2002, the Mexican government, along with private business, created the Presidential Council for Competitiveness.²⁰⁷ "It promotes investment, increases employment, and accelerates Mexico's economic growth."²⁰⁸ The program is a cooperative effort between government and business with the Mexico Ministry of Economy ("SECON")²⁰⁹ overseeing the council.²¹⁰ SECON's

202. See *Mexico: Maquila Doors Closing*, *supra* note 27 (noting that the government needs to approve more changes to keep maquiladoras healthy in the long term).

203. See *New Tax Incentives*, No. 7, Baker & McKenzie, (Nov. 2003), available at <http://bakernet.com/BakerNet/default.htm> (last visited Mar. 3, 2004) [hereinafter *New Tax Incentives*] (indicating that the Fox Administration implemented the income tax exemption to promote maquiladora growth).

204. *Id.*

205. *Cf. id.* (stating that the taxpayer must comply with Article 216-Bis of the Income Tax Law).

206. *Cf. Michael Becka et al., Latin American Tax Review: Update on Mexico's Maquiladora Tax Benefits*, TAX ANALYSTS WORLDWIDE TAX DAILY, Jan. 16, 2004 (identifying China as a low-cost manufacturing jurisdiction in competition with Mexico).

207. GAO Report No. 03-891, *supra* note 12, at 39.

208. *Id.*

209. See Mary Beth Sheridan, *Mexico's New Cabinet Hailed as Business-Savvy; Politics: President-Elect Fox Taps U.S.-Trained Experts*, L.A. TIMES, Nov. 23, 2000, at C1 (announcing that World Bank economist Luis Ernesto Derbez will head the new SECON). SECON handles trade and promotes small and mid-size businesses. *Id.*; see also *Managing Exports Miscellany*, MANAGING EXPORTS, (June 2003), at 8 (explaining that the acronym "SECON" signifies the Mexico Ministry of Economy).

210. GAO Report No. 03-891, *supra* note 12, at 39.

activities include creating a fiscal stimulus package for export factories, including maquiladoras.²¹¹

In May 2003, Mexico published the Maquiladora Decree, which modifies certain aspects of the maquiladora industry.²¹² The Maquiladora Decree simplifies regulations for companies that provide support and logistic services to maquiladoras.²¹³ The Maquiladora Decree streamlines customs requirements for companies with several subsidiaries operating under one maquiladora program.²¹⁴ In addition to these changes, the Maquiladora Decree also reduces administrative costs and procedures related to annual reporting functions.²¹⁵

In June 2003, Fox's Administration advanced efforts to eliminate corruption in the bureaucracy and police by passing the Freedom of Information Law.²¹⁶ This law sheds light on all aspects of government because it requires all branches of government to provide copies of government documents for public inspection.²¹⁷ In addition to the Freedom of Information Law, Fox has also publicized information about his personal income and investments and his administration's expenditures.²¹⁸ President Fox's gestures have translated to improved police professionalism.²¹⁹

C. Changes Between Mexico and the Global Economy

Given the increased competition for maquiladoras, Fox is working to face the challenges of a growing global economy. Two major components affect Mexico's competitiveness: the U.S. economy and the value of the peso. These components have recently changed in Mexico's favor. Primarily, President Fox is

211. See *id.* (noting that the Secretary of the Economy has agreed to fund a comprehensive study on the maquiladora industry). The funding will come from the National Council of the Maquiladora Export Industry ("CNIME"). *Id.*

212. See *id.* at 38 & n.27 (stating that the Maquiladora Decree will enhance legal certainty for maquiladoras). The Mexican government aimed reforms at simplifying regulations for companies that provide support and logistic services to maquiladoras. *Id.*

213. See *id.* at 38 (reporting that "it remains unclear whether the Maquiladora decree will satisfy maquiladora critics who seek greater legal certainty and improved incentives for maquiladoras").

214. See *id.* (noting that this streamlined customs system will allow companies with several subsidiaries to transfer finished or semi-finished products from one subsidiary to another).

215. See *id.* (providing an example of an administrative cost-saving feature that maquiladoras will only have to submit one annual report, which maquiladoras can now submit electronically).

216. Geri Smith, *Mexico: Vibrant Democracy is Still a Long Way Off*, BUS. WK., July 14, 2003 (Bus. Wk. Int'l Edition), at 24 [hereinafter *Democracy Long Way Off*]; E. Eduardo Castillo, *Mexico Starts Freedom of Information Act*, ASSOCIATED PRESS ONLINE, June 11, 2003 available at 2003 WL58611421.

217. *Democracy Long Way Off*, *supra* note 216, at 24; see Castillo, *supra* note 216 (noting that the law permits Mexican citizens to obtain government documents within twenty days of request). Examples of government documents include employee wage statements, details regarding public programs, and government contracts. *Id.*

218. See Castillo, *supra* note 216 (indicating that Fox revealed his personal and presidential expenditures to make the Mexican government more responsible).

219. See *Opening Mexico; Don't Overlook Legacy of Transparency*, *supra* note 97, at 16A (arguing Mexican citizens have not given President Fox enough credit for improving law enforcement).

attempting to alter Mexico's dependence on the United States by encouraging more foreign investment from other countries.²²⁰ However, since Mexico currently still depends on the U.S. economy, the improvement of the U.S. economy during 2003²²¹ should make investment in Mexico more lucrative.²²² In addition, since 2002, the peso has depreciated twenty percent against the U.S. dollar, and this has helped Mexico regain its competitiveness.²²³

Mexico's poor infrastructure affects competition with other countries,²²⁴ but one goal of the United States-Mexico Partnership for Prosperity plan ("Partnership") includes updating the economic infrastructure.²²⁵ In February 2001, Presidents Fox and Bush²²⁶ signed the Partnership, which contemplates projects to facilitate investment in small business, infrastructure, and technology.²²⁷ The Partnership prompted a successful meeting among 800 U.S. and Mexican businesses to discuss housing, infrastructure, and information technology.²²⁸ New business ventures will develop as a result of the Partnership.²²⁹ Presidents Fox and Bush also pledged to work together regarding North American energy resources.²³⁰

220. See Donnelly, *supra* note 121 (announcing that President Fox would like to make a trade agreement with Japan to diversify foreign investment in Mexico).

221. See U.S. DEP'T. OF COM., BEA Report No. 03-11, GROSS DOMESTIC PRODUCT (GDP) BY INDUSTRY FOR 2002: SERVICES-PRODUCING SECTOR LEADS ECONOMIC REBOUND; MANUFACTURING BEGINS RECOVERY (2003) (reporting "a broad-based economic rebound in 2002" for the United States). The real gross national product increased from 0.3 percent in 2001 to 2.4 percent in 2002. *Id.*

222. See John Authers & Sara Silver, *Free trade with the US and Canada did not Spur Wider Economic Reform, and Limited Progress Towards Creating Prosperity is in Danger of Stalling*, FIN. TIMES, (London), July 1, 2003, (Comment & Analysis), at 19 (indicating that Mexico's foreign investment leveled off but the upturn in the U.S. economy may reverse the trend).

223. Geri Smith, *Solid Growth, Sluggish Government*, BUS. WK., Feb. 16, 2004, at 30 [hereinafter *Solid Growth, Sluggish Government*].

224. See *supra* notes 140-49 and accompanying text (comparing Mexico's infrastructure to other countries in competition with Mexico).

225. See Jerry K. Mitchell, *The Partnership for Prosperity, Spreading the Benefits of NAFTA*, U.S. Commercial Service, Mexico (Nov. 2003), available at http://www.export.gov/exportamerica/NewOpportunities/no_mexico_1103.html (last visited Mar. 3, 2004) (copy on file with *The Transnational Lawyer*) (summarizing the Partnership for Prosperity initiative).

226. George W. Bush is the 43rd President of the United States. Mention of Bush, the Bush Administration, or President Bush in this Comment is in reference to George W. Bush unless otherwise noted.

227. See Hale E. Sheppard, *Revamping the Export-Import Bank in 2002: The Impact of this Interim Solution on the United States and Latin America*, 6 N.Y.U. J. LEGIS. & PUB. POL'Y 89, 124 (2003) (describing the private-public alliance designed to foster an environment where Mexican citizens are not compelled to abandon their country due to a scarcity of jobs).

228. See Mitchell, *supra* note 225 (asserting that a similar conference is expected in 2004 to highlight other key industry and service sectors).

229. *Id.* (stating that the United States Trade and Development Agency is "funding feasibility studies in the transportation, energy, and infrastructure sectors, which will increase United States exports").

230. See Press Release, Joint Statement by President George Bush and President Vicente Fox Towards a Partnership for Prosperity, The Guanajuato Proposal, (Feb. 16, 2001), available at <http://www.whitehouse.gov/news/releases/2001/02/20010220-2.html> (last visited Mar. 3, 2004) (copy on file with *The Transnational Lawyer*) (stating that the United States and Mexico will consult with Canada regarding energy resources).

The various changes in the global economy, such as a stronger U.S. economy and weaker peso, should initiate more foreign investment in Mexico. In addition, the Partnership between the two presidents should create better infrastructure and energy use in Mexico, which is vital to the maquiladora industry.

V. CONCLUSION

Fox's presidency shows limited success for the maquiladora industry. President Fox needs to convince Congress to pass tax and electricity reforms that will permit Mexico to remain competitive in the maquiladora industry.²³¹ The multi-party gridlock in Congress prevents the President from addressing the country's problems.²³² Only fierce negotiations and flexibility within the reigning PRI will keep investment pouring into Mexico. If Fox can implement changes, foreign investment in Mexico will improve.²³³ However, if Fox continues the trend of taxing foreign companies, particularly those not from the United States, foreign investors will likely look elsewhere for better investment opportunities.²³⁴ Indeed, Japan already announced that it will move its manufacturing out of Mexico if changes to security, labor, tax structure, and infrastructure are not implemented.²³⁵

In January 2004, Presidents Fox and Bush met in Mexico for the Special Summit of the Americas, in which the two presidents renewed their commitment to the Partnership between the two countries.²³⁶ This meeting was a positive sign for the future of U.S. investment in Mexico and it showed that President Fox will continue in his attempt to improve foreign investment in Mexico.²³⁷ For example, in October 2003, President Fox praised Ford Motor Company's long presence in

231. See *Mexico's Broken Dream*, *supra* note 11, at 4H (stating that all analysts agree that Mexico's government must act swiftly to enact reforms to attract investment); see also Cañas & Coronado, *supra* note 18 (acknowledging Mexico needs tax reform, specifically, clear and definite tax rules for maquiladoras).

232. See Wise, *supra* note 4, at 306 (noting that the three main political parties, PRI, PAN, and PRD are feuding amongst themselves in Congress).

233. See Garza, *supra* note 36 (noting that leaders in Mexico need to implement a range of reforms in order for the country to experience strong economic growth and job creation).

234. See Cañas & Coronado, *supra* note 18 (arguing that changes are needed in order for Mexico to remain competitive).

235. See *Japan Threatens to Withdraw Investments*, DIARO CIUDAD JUAREZ, Dec. 12, 2003, available at <http://www.maquilaportal.com/cgi-bin/public/hist/hist.pl?Klein=2003-12-16&Klein2=5878&Klein3=DECEMBER> (last visited Mar. 3, 2004) (copy on file with *The Transnational Lawyer*) (reporting that the Japanese Ambassador to Mexico, Mutsuyoshi Nishimura, warned Mexico that countries, such as China, are offering more favorable investment conditions).

236. See Garza, *supra* note 36 (asserting that the meeting will precipitate the goals of economic growth and job creation in both countries); see also *Media Availability with U.S. President George W. Bush and Mexican President Vicente Fox Quesada Following their Meeting*, FED. NEWS SERVICE, Jan. 12, 2004 (relating that the two presidents will work towards developing their economies and achieving competitiveness and productivity).

237. See Garza, *supra* note 36 (stating that the presidents will join with other leaders in the Western Hemisphere to promote open economies).

Mexico and Ford's intent to invest \$1.6 billion to build a new factory in Mexico.²³⁸ Ford's investment is evidence that Fox continues to make Mexico a competitive market to attract U.S. investors. However, Article 303 still inhibits investment from other countries, with the exception of companies whose manufacturing requires just-in-time shipping. In October 2003, industry production began growing in Mexico. It has displayed its best performance in four years.²³⁹ Accordingly, maquiladora investment should increase in 2004, even if Congress does not pass Fox's fiscal, labor, and energy reforms.²⁴⁰ Yet, it appears that Fox's tax and energy reform bills may pass by the end of 2004.²⁴¹ Therefore, even with the tumultuous political environment, potential investors should take into account that Mexico remains the closest country to the United States that a manufacturer can produce a product at a minimal price.

238. See *Mexico's Broken Dream*, *supra* note 11, at 4H (acknowledging that finished-auto-for export assembly is growing in Mexico).

239. See *Solid Growth, Sluggish Government*, *supra* note 223, at 30 (adding that Mexico's economy is expected to expand from 3 to 3.5 percent in 2004).

240. See *id.* (explaining that Mexico needs reforms to generate vigorous growth); see also *New Increase in Maquiladora Investment?*, GLOBAL INSIGHT, Dec. 22, 2003, available at <http://www.maquilaportal.com> (last visited Mar. 3, 2004) (copy on file with *The Transnational Lawyer*) (reporting that SECON predicts an overall growth of 6 to 10 percent in the maquiladora industry in 2004). In addition, CNIME and President Fox predict foreign investment will increase \$800 million dollars from 2003. *Id.*

241. See Solano, *supra* note 199 (noting that Fox's proposal to amend Mexico's Federal Tax Code may be implemented in 2004); see also *Solid Growth, Sluggish Government*, *supra* note 223, at 30 (noting that a limited number of energy reforms may pass in 2004). But see Jorge Castañeda, *It's Not Too Late for President Fox to Shake Up Gridlocked Mexico*, BALTIMORE SUN, Jan. 21, 2004, (Editorial), at 17A (arguing that the Mexican Congress will definitely not pass Fox's tax, energy, labor, or political reforms).