Financial Reporting and the Business Environment: A Comparison of the United States and Mexico

by

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Multinational corporations must be aware of the business and financial reporting issues that await them abroad. Investors also must have this knowledge in order to adequately interpret the financial information they receive from these companies. This study compares and contrasts the business environments in the US and Mexico, with a focus on financial reporting. The first section of this paper addresses cultural differences and their impact on the business environment as well as business laws and practices specific to each country. The second looks at the accounting standards of each country, as well as international standards. Finally, a Mexican cement company, CEMEX, is used to show how the accounting issues manifest themselves in practice.

Key Words: accounting, Mexico, international, standards
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When someone in the United States thinks of Mexico in relation to business, chances are the issue of immigrant workers is the first idea that comes to mind. However, perhaps to the surprise of many, our neighbor to the south is becoming a good place to do business due to its relatively low corporate tax rates and inexpensive labor. When looking at a foreign country as a potential place to do business, it is important to consider many factors, one of which is accounting. The reason it is important to be knowledgeable about the accounting practices in the two countries is that, due to globalization, and more specifically to the North American Free Trade Agreement (NAFTA), capital is flowing across the border in both directions.

Even though some consider it not far past the stage of developing country, Mexico does have a sophisticated accounting system of its own and a national accountant society not unlike our own AICPA. The country has its own thick books of accounting regulations and pronouncements–called bulletins–just like our FASB pronouncements. However, it does seem that Mexico's accounting is not entirely independent of U.S. GAAP. The Advanced Accounting course I took at the Technological Institute for Superior Studies at Monterrey (ITESM) used the same textbook used in many universities around the United States for the majority of its material. Because of the differences in the legal code, it was also necessary to supplement the book with material specific to Mexico.

Before addressing the similarities and differences between the two countries with regard to accounting, I would like to observe some key cultural and business differences because of their importance to anyone doing business or investing in Mexico. I will do this by using cultural dimensions from Hofstede and GLOBE, as well as looking at factors such as government, demographics, and business practices.

In order to compare the accounting practices in both countries, I will talk about the governing bodies in each nation and their responsibilities, as well as the Board responsible for setting standards on an international level. My most critical source of information will be a study done in 1994 and updated in 1998 by the accounting standards boards in the U.S., Canada, and Mexico. I will also discuss taxation of businesses because of its importance related to these issues.

After discussing the business environment and the accounting practices, I will use a large Mexican cement company, CEMEX, as an example of the accounting practices for the same company in two different countries. I first profile the company and discuss how some of the issues from my first two sections relate to the company. My main sources of information are annual reports and other forms filed with the U.S. Securities and Exchange Commission.

Chapter 1: Business and Culture

When comparing the business environments of two countries, it is necessary to look at the similarities and differences between the two cultures. This is because the business environments in the two countries are heavily influenced by cultural norms. A country's culture shapes people's actions, and these actions influence business practices and decisions.

Mexico's culture differs from that of the United States in many ways. Perhaps one of the best ways to evaluate a nation's culture for business purposes is to use Hofstede's five cultural dimensions (Hofstede 2003) or the nine GLOBE dimensions (Kinicki and Kreitner 2006), which have been developed more recently. Two of the dimensions—power distance and uncertainty avoidance—are common to both models, so I will look at twelve dimensions altogether. It is important to remember, however, that while these dimensions may characterize the country as a whole, they by no means characterize every individual in the society described.

Hofstede's Dimensions

Power Distance

Hofstede's first dimension concerns unequal distribution of power within an organization, which he calls "power distance." An organization with high power distance is characterized by those in higher positions having a disproportionate amount of power compared to those below them. Mexican corporations are generally more hierarchical, and subordinates are expected to act as such. In the U.S. there is more tolerance of feedback and help with decision-making from lower-level employees.

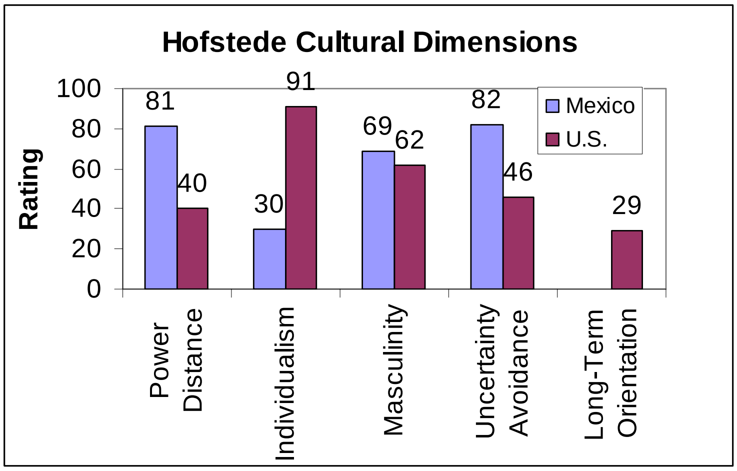

Figure 1: Hofstede's Cultural Dimensions
Source: Hofstede 2003

Individualism

The United States is a very individualistic society in which it is very common for one person to want to be the star. This is evidenced by the high CEO compensation in the U.S. compared to Mexico and most other nations. (Business Week 2000). Many U.S. firms make their CEO the star by paying him or her tens of millions of dollars while all others receive significantly less. The American dream and picture of success in our society is to get a high-paying job and be able to support an immediate family. As put by historian James Truslow Adams, the society for this dream is one in which "each man and each woman shall be able to attain the fullest stature of which they are innately capable, and be recognized by others for what they are" (Jischke 2007). Many people here also desire to attain a lot of power. In Mexico, by contrast, people are much more concerned with being good family members, and this spills over into their business practices. Success for one individual at the expense of the rest of the company is seen as a failure. This is one reason why Mexican CEOs were paid 45 times the salary of their employees on average (Wahlgren 2001) compared to 475 times in the U.S. (Business Week 2000).

Masculinity

Mexico is known for its highly masculine culture, and for many, the term “Machismo” comes to mind when this topic is brought up. One reason for this reputation is that Mexican society is seen as one dominated by men–an issue I will discuss briefly later on–and this is definitely true in the business world. However, this is not exactly the definition of masculinity relating to Hofstede’s dimensions. He defines masculinity as a culture displaying masculine values such as assertiveness, materialism, individual achievements, and power. According to the scores given—see figure 1—Mexican culture displays slightly more masculine characteristics than that of the United States. Because the U.S. generally displays materialistic tendencies and has an individualistic or assertive culture, the difference must be attributable to Mexican values relating to power.

Uncertainty Avoidance

As shown in figure 1, Mexican businesspeople are much more likely to avoid uncertainty in business situations. This means they are less likely to take risks and are more uncomfortable in uncertain circumstances. In the U.S., risk-taking is often applauded and because of the size and complexity of our economy, we are forced to get used to dealing with uncertainty on a regular basis. Mexican business culture demonstrates uncertainty avoidance in numerous ways, as Schuler et al (1996) have observed in their article in *Business Horizons*. One is that workers are generally closely supervised by their superiors. Another is that their compensation methods tend to promote "consistency and certainty," meaning that workers are rewarded for staying with a company and for doing a consistently good job. This contrasts with many jobs in the U.S., where managers and directors use bonuses and incentives for employees that are more specifically focused on financial targets.

Long-term Orientation

This dimension is the newest addition to Hofstede's model, and it is also referred to as Confucian Dynamism. Its main purpose is to account for ideological differences between eastern and western cultures. Long-term orientation is often displayed by characteristics such as persistence, a sense of shame, and having an order of relationships. By contrast, short-term orientation is displayed by actions such as protecting one's appearance and reciprocating gifts. These are characteristic of U.S. culture, evidenced by many Americans' high level of concern regarding their image and the sense many in our culture have that if one receives a gift, it should be reciprocated. Mexico has not yet been given an index in this area; however, Mexico would most likely rate slightly higher regarding long-term orientation because of its culture's value placed on family and relationships. My conjecture is that it would not be much higher because Mexican culture does show some short-term characteristics such as that of reciprocating favors.

The GLOBE Dimensions

In 1994, a group of professors led by Robert House began a study into leadership theories around the world. Their project was called the Global Leadership and Organizational Behavior Effectiveness (GLOBE) project. While studying culture and leadership in 61 nations, the group developed a set of nine dimensions, some based on those of Hofstede and some on the ideas of other researchers (House et al 2002). It could be argued that these dimensions do a better job of comparing cultures than Hofstede's model because they build upon and add to it. The nine GLOBE dimensions are uncertainty avoidance, power distance, societal collectivism, in-group collectivism, gender egalitarianism, assertiveness, future orientation, performance orientation, and humane orientation. The first two having been discussed above, I discuss the remaining seven below.

Societal Collectivism

This is the first of the GLOBE dimensions and relates very closely to the Hofstede's individualism dimension. Societal collectivism refers to how much loyalty to a social unit is rewarded in the business environment. The characteristics of this dimension are much more prevalent in Mexico than they are in the U.S. Here individuals are rewarded for their personal performance, whereas in Mexico people are rewarded when the group does well. This is also displayed in Mexico by family lifestyles. Families in the U.S. are not nearly as close as they are in Mexico. Here, most people are expected to move out of their parents' homes as soon as they can afford it, and sometimes even sooner. This is usually between the ages of 18 and 23. In Mexico, it is not uncommon for people to remain living with their parents until they are 30 years old. Extended families are also much more tightly knit in Mexico. My observation from staying in Mexico for four months and visiting various areas of the country, such as Baja California and Mexico City, is that it is more normal for someone to live with his or her parents until age thirty than it is here. My host family had two children around the age of thirty that still lived in the house. The family also had a daughter who had two children who came over almost every day for a few hours.

In-group Collectivism

In-group collectivism relates to an individual's expected loyalty to and pride in a certain group, such as the family or organization. Due to its collectivist culture, Mexico strongly displays this characteristic as well. This was something I was able to witness first-hand in Mexico on its independence day when people from all over the nation joined to yell, "Viva México!" Mexicans also display this characteristic at a much smaller level, such as with a company. Ned Crouch (2004) describes a situation in which he gave hats with a company logo to a group of employees at a certain business in Mexico and they reacted with glee. He said even the gardener was delighted to receive the hat because it made him feel like he was part of the group.

Gender Egalitarianism

Gender egalitarianism has become a significant issue in recent years. In the U.S., many women's rights activists address a phenomenon known as the "Glass Ceiling." This theory essentially says that although there are no rules related to which jobs each gender may hold, women are almost universally excluded from top management positions. While this has been an issue that must be addressed in the U.S., it is more of an issue in Mexico. The percent of top management positions occupied by women in Mexico is 24.6%, though a study based on the salaries of these managers indicates the number is actually closer to 17.3%. This is to say, some of these managers have salaries that strongly indicate that they are not near the top of their companies (Davidson and Burke 2004). In the U.S., this gap has been significantly narrowed, with women occupying 45% of top management positions (Davidson and Burke 2004). There is certainly a much stronger egalitarian movement in the U.S. than there is in Mexico, and Mexico is still perceived as a highly masculine and paternalistic society.

Assertiveness

Assertiveness relates to how willing an individual is to take charge or engage in confrontation. Mexico's culture tends to be more focused on harmony and its citizens are not nearly as forward as people in the U.S. Americans are often seen as overly dominant when they do business abroad, and despite the proximity of the two countries, this problem exists in Mexico. While the "let's get down to business" attitude is the modus operandi in the U.S., it will not get an expatriate in Mexico very far. In Mexico it is important to develop a trusting relationship with a business associate before any deals are made. If a businessperson fails to do this, they will be seen as a poor business partner. Many people from the U.S. have a difficult time understanding this emphasis on relationships in business because though relationships do play a role in the U.S. business environment this role is not as extensive as it is in other nations. Some Americans may resist the idea of the necessity to be friends with someone before doing business with him or her, or may consider it unprofessional. When visiting a foreign country, Americans must be aware of how they are perceived by their counterparts.

Future Orientation

Future orientation is the degree to which people in a certain culture tend to plan for the future. Because of the differences in how the two cultures view time, their attitudes toward the future is very different. Companies in the U.S. have more future-oriented mission and vision statements, whereas those in Mexico tend to view time as fluid and do not plan as much. Many businesspeople in the U.S. focus on innovation and future planning, some of which includes taking risks. Numerous Mexicans, on the other hand, will do what is best for today and worry about tomorrow when it comes (Crouch 2004).

Performance Orientation

The performance orientation dimension considers how much individuals are rewarded for their performance. Again, due to the collectivist culture, Mexicans usually focus on the performance of the group as a whole, and thus individuals are not rewarded as much for their personal performance. In the U.S., there is more room for reward for personal performance, evidenced by the abundance of bonuses and high CEO compensation. Also, many American firms reward only certain individuals for the performance of a group. This usually means giving top management the credit for a business's short-term success by offering stock options and performance bonuses. In Mexico, stock options and bonuses are becoming increasingly more popular, however (IUS Laboris 2006). For example, CEMEX uses an employee stock option program, though it is intended for managers and senior executives. This is included in its reconciliation of accounting standards, discussed in the third chapter. This seems to indicate a shift in business values towards those held in the U.S.

Humane Orientation

A culture is considered to have a high degree of humane orientation if it places a high value on treating people well. Businesses in the United States, although they do not always do it well, are discovering that this is an important aspect of success because happier employees are generally more productive. Many Mexican companies do a good job with regard to their employees. In fact, they do such a good job that workers in Mexico often are stereotyped as being lazy because they combine work and leisure. However, they often accomplish just as much as workers in the U.S. do. The amount of work done is comparable because, as I was taught in my business class at ITESM, the Mexican business environment often combines work and leisure. As a result, Mexicans work longer hours, but are much less likely to get burnt out because the work is less intensive.

The Ugly American Syndrome

People from the U.S. make various mistakes when doing business abroad that damage their rapport with their counterparts and decrease their chances of success. These mistakes, whether in business or travel in general, cause what is known as the "Ugly American Syndrome." Many Americans have little or no idea about the differences between our culture and others, and thus are unaware when they are doing something that is perceived as offensive in other cultures.

There are a number precautions to take and practices to avoid when traveling or doing business in Mexico. One of the first things one will be told when visiting Mexico is that many Mexicans have a different concept of time than do people in the U.S. While showing up late to a meeting in the U.S. is offensive or seen as a sign of laziness or an inability to meet obligations, in Mexico it is seen as normal. What Mexicans would find offensive is reacting harshly towards someone for showing up late. It is also considered rude in Mexico to leave a meeting early. Mexicans tend to put people and relationships ahead of projects and deadlines, and thus, failing to spend enough time with them is likely to be taken as an insult.

Another significant problem Americans run into when visiting Mexico is that they expect deadlines to be firm like many are in their home country. Many Americans see Mexicans as procrastinators because they have no problem doing whatever it is they have to do "tomorrow." Americans visiting Mexico must be patient and understand that different cultures do not have the same time priorities as their home country.

It may be difficult to understand how something done with good intentions can, through the filter of culture, be taken the wrong way. One would ask, “Don’t they understand where I’m coming from?” The answer is probably “no.” However the expatriate asking this question does not understand where the Mexican is coming from either. Cross-cultural barriers can often be as confusing as and more dangerous than language barriers. One area in which this is especially true is the idea of being a high-context versus a low-context culture, an idea popularized by anthropologist Edward T. Hall (1976).

In the U.S., we have a low-context culture, meaning that we convey how we feel by our words. Obviously, there are times when we use body language and certain actions to convey how we feel, but dependence primarily on body language is far less prevalent in the U.S. than in a country with a high-context culture. Mexico’s culture could be labeled as high-context. It relies much more on situational cues, body language, and tone of voice than American culture. One example of a situational cue that may not be understood by a foreigner is that if someone puts his hands in his pockets during a conversation, it conveys that he is bored with his conversation partner. Another common mistake Americans make in Latin America is trying to keep a personal space bubble, usually requiring a minimum distance from another person while holding a conversation. This concept is not nearly as common south of our border, and hence leaning away from someone will send a negative message. Either one of these mistakes could be fatal to a business deal, especially in a country where personal relationships are paramount in business.

Demographics

It is important for a business to understand the demographics of an area in which it is doing business, because in order to succeed, it must be able to market to, and meet the needs of, the people in the area. Depending on the area in Mexico, one can expect to find very different markets. The three big cities are Mexico City, Guadalajara, and Monterrey. These cities and the tourist areas, such as costal cities with numerous resorts, are the only places in the country with markets for expensive goods. The rest of the country is, for the most part, rural, without a high concentration of high-income residents.

According to Mexico's national population council (CONAPO 2006), Mexico's population as of 2006 was 104,860,000, approximately one-third of which lived in rural areas. Nearly 51% were women and 64% were between the ages of 15 and 64. In 2005, 6% spoke an indigenous language, and the country's official language is Spanish. According to the other population agency (INEGI 2007), 92% of the population was Catholic in 2000, and the rest was either nonreligious or of a different religion. Also from the INEGI website are the statistics on the education level of the population 15 years and older. According to the statistics, 22.7% either have no education or have less than elementary school completed. Slightly over half the population has completed high school, and 13.6 percent have completed "superior" education. These statistics can be important for businesses looking to hire skilled employees, and knowing that over half the population is high-school educated is reassuring.

The gap between the rich and the poor in Mexico is immense. Having visited numerous Mexican cities, I observed the economic situation of many of the locals. However, this gap seemed to me to be most evident in Monterrey, where I was staying. In some areas of the city, residents lived in houses that would be considered shacks by American standards. Other areas showed evidence that there were numerous millionaires living in the city. There were as many BMWs as one would expect to find in any large city in the U.S. The prices also reflected this stark contrast. Necessities such as food were very cheap, but luxury items were just as expensive as, or even more so, than in the U.S. Retailers understand that poor people need food but can not pay high prices. They also understand that luxury items are not necessary, and that the wealthy are the primary market for these items, so they can charge high prices for them.

Government

Mexico's government is structurally very similar to that of the United States. It has executive, legislative, and judicial branches of power. From living in Mexico in the months succeeding the 2006 election, I was able to gather a significant amount of information on the attitudes of the Mexican people regarding the political situation. The current president, Felipe Calderón, a Harvard graduate, is known as friendly to business. He comes from the right-leaning National Action Party (PAN) and his opponent in the razor-thin 2006 election, Andres Manuel López Obrador, was strongly associated with former prominent communist leaders from around the world. Many businesspeople throughout the nation feared that López Obrador would win the election and implement policies that would significantly damage their businesses.

López Obrador, the former mayor of Mexico City, and his party were highly popular with poor people throughout the country because of his populist policies. The immense gap between the rich and the poor is widely viewed as unjust, and many people believed that Calderón and his party would implement policies that would only benefit the rich and thus, further widen the gap. The vast majority of Mexico's poor viewed López Obrador as having the potential to be their savior.

On the other side of the spectrum, many businesspeople and investors feared that López Obrador's populist policies would stifle Mexico's economic growth and that the still developing economy would not be able to afford the damage his plans were bound to cause.

Another cause for concern in Mexico is corruption in the government. While corruption is present in the United States, the country achieved some level of success keeping it to a minimum, due in part to the system of checks and balances in the government. In Mexico it is more widespread at many levels of government. Many people see corruption firsthand in their encounters with the police. For example, when stopped for a traffic violation, many people are able to "take care of it on the spot," as I was told by more than one local citizen in Monterrey. They take care of it by giving the officer a relatively small bribe, around $10 or $20 U.S., instead of receiving a citation and going to court. Also, when crossing the border into Mexico at night, it is not uncommon for customs agents to ask everyone in the vehicle, even on a commercial bus, for a dollar or two instead of checking their luggage for contraband. Among other reasons, this corruption exists because the workers are paid small salaries and feel that their low pay justifies pocketing some of the revenues from their work.

Seeing this corruption as a common practice at the lower levels of government, it is not very hard for citizens to believe that corruption exists at higher levels when they see accusations of such on the news or in political attack ads. I was able to observe this attitude with some of the citizens during my stay in Monterrey. Some even view programs the government has in place, such as the President's pension system that López Obrador promised to eliminate, as corrupt. This pension gives the president roughly $30,000 U.S. per month for the rest of his life. Another law which many feel unjustly protects politicians is what is called *el fuero*. This law is meant to protect government officials from prosecution for their opinions by giving them immunity (Anguiano 2004). However, many Mexicans feel that this law gives elected officials a license to commit crimes. Anguiano's article cites the situations of various senators, such as Senator Ricardo Aldana, who was formally accused of participating in a scandal involving the theft of over $100,000,000 from the Mexican gasoline company PEMEX. Because of "el fuero," he was not held responsible for his part in the scandal.

However, the *fuero* law does not guarantee complete immunity for elected officials. They can be stripped of this privilege by a process called *el desafuero*. This process requires a two-thirds vote of Mexico's Legislative Assembly to revoke immunity from an official who has abused it (Anguiano 2004). At the beginning of López Obrador's campaign for the 2006 presidential election, the legislature voted to carry out the *desafuero* process in his case related to some minor contempt of court charges from 2001. This was widely viewed as a way for the opposing political parties, the National Action Party (PAN) and the Institutional Revolutionary Party (PRI), to keep him out of the presidential race (The Economist, 2005a).

Business Laws

Much like the United States, Mexico has different legal structures for business entities. Each country must make its laws appropriate to its unique business environment in order for companies to operate with high levels of success.

In the United States larger sized, public companies operate as C corporations and have many stockholders. Smaller corporations that meet certain requirements can be classified as small business, or S corporations. They benefit from certain tax advantages, such as being taxed as a partnership instead of as a corporation. Companies can also operate as a limited liability company (LLC), limited partnership (LP), limited liability partnership (LLP), or a general partnership.

Mexico has some similar options for businesses. The *sociedad anónima* (SA) is Mexico's version of a corporation. The *sociedad anónima de capital variable* (SA de CV) is a variable capital corporation. This differs from an SA in that an SA has a fixed maximum capital amount specified in the articles of incorporation, whereas the SA de CV allows the capital to vary depending on the wishes of the stockholders. The *sociedad* *de responsabilidad limitada* (S de RL) is the equivalent of an LLP. It is considered such for U.S. taxation purposes, which is why a number of foreign investors select this type of entity. It is also easier to manage bylaws using this type of entity.

Business Practices

Power Structure

Businesses also differ in practices and structure across cultures. One of the most prominent differences relates to the structure of power. While companies in the U.S. allow many people to make business decisions on a daily basis, hierarchy is much more important in Mexican businesses (Mini Career Guides 2002). Asking someone with little authority to make a decision will usually lead nowhere. Rank and status are usually very important in Mexican companies (Mini Career Guides 2002), which is why it is also important to use titles. Most Mexicans with college degrees wish to be distinguished accordingly, usually with the term “Licenciado” or “Ingeniero,” translated as “Licensed” and “Engineer.” One can observe this emphasis on distinction by looking at Mexican business cards or profiles on company websites. The Mexican practice of distinction based on college education contrasts from the U.S., where usually only people with doctorate degrees are referred to by their educational status.

Making a Deal

As mentioned above, Mexicans do not tend to be as aggressive as Americans. One of the ways in which this manifests itself in practice is that many Mexicans will avoid saying "no" directly (Executive Planet 2003). Because of this tendency, a Mexican businessperson may agree to a deal just to be courteous, and not follow through on it. This even happens with making plans. For example two people may agree to go to coffee, but one may not show up because he just accepted to be polite. Therefore, it is important to get any important business agreement in writing. Of course, the businessperson asking for the written agreement must do so very tactfully so as to not damage the relationship between the business associates.

Also, while making a deal, one thing both cultures have in common is that businesspeople wish to be respected. One area in which respect should be shown is the choice of language. One frequent problem in both countries is that people expect to travel and always speak their own language. Many Americans are upset that people come from Mexico and demand that they be spoken to in Spanish and have documents written in Spanish. However, these same Americans do not make the effort to learn Spanish when they travel to Mexico. While it is possible to get by in the larger cities in Mexico with English, English alone will not get someone very far in business. An important part of building the trusting relationship necessary to successfully do business in Mexico is showing the locals respect by using their own language.

Employee Relations & Authority

Another area in which business practices differ between the two countries is how they manage their employees. Many of the differences can be explained by the cultural dimensions discussed earlier. For instance, Mexico's high level of power distance (Rao and Teegen 2001) is manifested in that employees always consult their superiors when a decision is to be made. Because of Mexico's paternalistic culture, a person's boss is often seen as a paternal figure. Many children are taught to consult their fathers before making decisions. By contrast, in the U.S., children consult both their parents and have a greater level of independence than do Mexican children (Morris and Pavett 1992). This phenomenon holds true in business practices as many employees in the U.S. have a greater degree of independence and decision-making power than their Mexican counterparts.

In an article from the 2005 edition of *Business Mexico* some differences between U.S. and Mexican management styles were illustrated in the following story:

> "Bob came to Mexico feeling confident the management style that brought him so much success in the United States would propel him to similar success here. He reasoned that by involving all Mexican staff in the process of selling cars, they could easily attain double digit growth…So rather than telling them what he thought needed to be done, he put the question on the table and sat back to listen. Only then did Bob realize how quiet Mexico City could be." (Rutherford 2005)

The above quote is an example of how American style management does not work in Mexico. Mexican employees expect their managers to be strong and are not used to "participative management."(Rao and Teegen 2001) Because managers are expected to make decisions, it is viewed as a sign of weakness if they ask their employees to do so. While Bob thought he was empowering his employees, he was actually asking them to do something they considered stepping out of line. Mexico's culture is not geared to accept this type of participative management, so its implementation is likely to cause the employees to lose confidence in their manager rather than respect him more (Rutherford 2005).

Employment

There also exist differences in hiring practices between the two countries. Noting Mexico’s higher level of uncertainty avoidance, Mexican managers are likely to hire friends or family rather than strangers. In many circumstances in the U.S., this would be considered bad business because many people here believe that the most qualified applicant for a job should be hired and that a manager should not let his or her personal agendas interfere with that (Rao and Teegen 2001).

Promotion and Rewards

Everyone likes to be rewarded for performance, but different cultures do so in different ways. While the individualistic culture of the U.S. allows rewarding people for individual performance, Mexico’s collectivist culture is less welcoming of this practice. Pay and bonuses based on performance are less common in Mexico than in the U.S. The different pay structure is due in part to the value Mexican culture places on uncertainty avoidance, which includes more consistent compensation practices rather than incentives that fluctuate with performance (Schuler et al 1996). Rewarding an individual for his or her performance could likely have the opposite effect of what is intended by ostracizing him or her from coworkers.

Similarly, failing to reward individuals in a U.S. business is likely to be seen as bad management. Americans often feel the need to have their accomplishments recognized and feel that if they contribute something extra they should receive something extra in return. This attitude is displayed very prominently in CEO pay, in which base salary is a fairly small percentage of their compensation relative to their incentives (Leder 2007).

Retention

However, just because the Mexican culture is not welcoming of rewards for performance does not mean that Mexicans do not like extra benefits. Because of the high turnover rate in the Maquiladora industry, employers use benefits to try to retain their workers. These benefits include “day-care centers, dental services, educational programmes, scholarships, parties and picnics, psychiatry, counseling, organized sports, social activities where the families can participate intensively” (King, et al 2006). These benefits work very well in Mexico because they are geared towards family values, which are very strong in the Mexican culture. Some specific advice offered by leaders that have experience with Mexican workers is included in the following table:

Table 1: Employee Retention

RECOMMENDATIONS:
Satisfy particular employee needs
Encourage the development and practice of interpersonal skills
Have a good cafeteria service offered on site
Experience Mexican culture first hand
Offer incentives or bonuses for loyalty
Offer additional complementary incentives for family members
Remember that family is most important
Treat workers well, develop relationships.
Organize sports and other recreational events for workers
Treat all workers equally
Improve communication throughout company
Provide education assistance
Be flexible

Source: King et al 2006

The Stock Market and *La Bolsa Mexicana de Valores*

Much like the United States has the New York Stock Exchange and other markets for publicly traded securities, Mexico has the Bolsa Méxicana de Valores. La Bolsa, which is located in a very modern looking building in Mexico City, is privately owned by authorized brokerage firms. It operates under a concession granted by the Ministry of Finance (SHCP), observing Mexican Securities Law (*Bolsa Mexicana de Valores* 2006).

Chapter 2: Accounting Standards

Many of Mexico's accounting standards are similar to those used in the United States, however there are some significant differences. Businesses need to be aware of these differences and how they affect their company. Without this knowledge, a multinational organization will not be able to be listed on a foreign stock exchange. Companies also must consider whether they are willing to follow the accounting regulations of the country in which they are doing business. For instance, many companies have found compliance with the Sarbanes-Oxley Act of 2002 (SOX) to be burdensome. Companies could choose to avoid listing in the U.S. if they believe that compliance is too costly. One organization that is addressing many issues of companies issuing financial reports in foreign countries is the International Accounting Standards Board (IASB).

Current Issues

International Accounting

The bodies in charge of setting accounting standards around the world ultimately hope to achieve international uniformity among their standards. However, there exist a number of roadblocks to reaching this goal. One problem that has been identified by the IASB is that local circumstances in one country may mandate a particular treatment of an issue while another treatment is appropriate in a different country (CICA 1998).

Another issue is that, because of the numerous differences that exist, they cannot all be changed at once. In order for financial statements to be useful, users must be able to understand them. If numerous changes were implemented in a short period of time, it would be nearly impossible for most financial statement users to fully understand all the new standards used in the reports they are reading. Also slowing the process is the fact that the different countries must come to an accord on which standard is the most appropriate for each topic.

Financial Accounting Standards Board

The board that is in charge of setting Generally Accepted Accounting Principles (GAAP) in the United States is the Financial Accounting Standards Board (FASB). The FASB publishes standards, such as FAS 141, which addresses reporting issues related to consolidated financial statements. The Board is currently working with IASB to harmonize accounting principles worldwide (CICA 1998).

According to an article in the Journal of Accountancy (Gill 2007), harmonization between U.S. GAAP and International Financial Reporting Standards (IFRS) may be realized much sooner than once expected. Currently, there are over 100 countries that have adopted or are in the process of adopting IFRS. Some countries use it as their only standard, while other countries make it an option. In 2002, the FASB signed the "Norwalk Agreement" with the IASB, which states that the FASB will work to make "existing financial reporting standards fully compatible as soon as it is practicable."

Then, in February of 2006, it signed a "Memorandum of Understanding" with the IASB outlining what the two organizations plan to achieve by 2008.

Any company that trades in the U.S. and prepares its financial statements under a set of standards other than U.S. GAAP must prepare a form 20-F to reconcile the two sets of standards. However, the U.S. Securities and Exchange Commission (SEC) has stated that it is committed to eliminating this requirement for financial statements prepared under IFRS (Gill 2007). This step would be very significant because of the burden this requirement imposes on foreign companies listed in the U.S. In fact, if harmonization between GAAP and IFRS is not realized and the SEC decides as a result to not remove the reconciliation requirement, IASB chair Sir David Tweedie speculates that "there will be political pressure elsewhere to say, 'Well, let's stick it to the Americans. We'll make them reconcile elsewhere'" (Gill 2007).

Instituto Mexicano de Contadores Públicos

In Mexico, the Mexican Institute of Public Accountants (IMCP) is in charge of setting the nation's GAAP. More specifically, Mexico's Accounting Principles Commission, translated *Comisión de Principos Contables* (CPC), has historically written the standards on behalf of the IMCP. Recently, the Commission has developed a new organization, called the Mexican Counsel on the Investigation and Development of the Norms of Financial Information, translated *Consejo Mexicao de Investigación y Desarrollo de Normas de Información Financiera* (CINIF). In 2004, the IMCP decided that the CINIF would be in charge of setting financial reporting standards henceforth. According to the

IMCP (2005), the reason for this change was that the accounting profession in Mexico believed that, especially in light of globalization and all that has been happening around the world, it was time for an independent organization to be in charge of the country's financial reporting standards.

The new standards, called the Mexican Financial Reporting Standards (MFRS), were enacted beginning 2006 (CEMEX 2006a). According to the 2006 CEMEX annual report, CINIF decided to adopt the Mexican GAAP that had been in place the previous two years for 2006. The new responsibility of the CPC is to represent the accounting profession before the new organization and make recommendations about issues to be addressed.

In order to give some background on the current standards, it is necessary to discuss the framework upon which they are based. The CPC has published five series' of bulletins, lettered A-E, stating Mexico's standards. Series A covers basic accounting principles, Series B covers principles related to financial statements, Series C covers principles related to specific parties and concepts, Series D addresses special problems related to the determination of income, and Series E covers specific regulations for specialized industries (IMCP 2005). For example, the IMCP Bulletin B-8 deals with some of the same financial statement consolidation issues that FAS 141 addresses. It also publishes other declarations, such as circulars, similar to the practice of the FASB.

Similar to the conclusion of the IASB, the IMCP has recognized that some circumstances are unique to Mexico. Its declaration in December 2005 conveyed this point: "The differences that exist between the CPC Bulletins and those of IASB were identified and justified at the appropriate time" (IMCP 2005 – Translated from Spanish). One of the steps Mexico has taken to harmonize its standards to IFRS was publishing Bulletin A-8, and later Circular 49. These state that in the absence of a Mexican accounting standard to address a particular issue, the applicable international standard is to be used (CICA 1998). One example is that Mexican standards do not address the accounting for joint ventures, so IAS 31 applies to financial reporting for joint ventures in Mexico.

Significant Similarities and Differences

A study done in 1994 by the respective accounting standards boards of the U.S., Canada, and Mexico identified several key areas in which significant differences in accounting regulations exist among the three countries. This study was updated in 1998, and I have done further research to take into account changes since 1998. Here I focus on the similarities and differences between the standards of the U.S. and those of Mexico. The topics include inflation accounting, exchange rate accounting, business combinations, consolidation accounting, deferred taxes, recent progress, and parent-company reporting.

Similarities

Although Mexico and the U.S. have different standards-setting commissions, there are many similarities that exist in their sets of standards. In the IMCP's 2005 declaration regarding the new CINIF, the first subject it mentioned for the organization to evaluate related to the recognition of revenue. It stated that the goal of current standards was that revenue be recognized when the critical event in the generation of that revenue takes place. This is exactly the same as how it is treated by American standards under the Realization Principle. The most significant similarity currently, in my opinion, is that both standards boards are working to achieve convergence with international accounting standards. As I examine the differences below, I discuss some differences that have been reconciled in recent years.

Inflation Accounting

Perhaps the most significant difference between the two sets of accounting standards is how they address inflation. Elizabeth Gordon (2001) notes that the respective standards setters of the U.S., Canada, and Mexico have identified inflation accounting as one of the most significant issues in the way of harmonization. Because of Mexico's hyperinflationary economy in prior decades, the Mexican government, along with other governments such as Chile (CICA 1998), found it necessary to include standards to reflect the effects of inflation on corporations' books. Mexico's regulation that addresses this issue is Bulletin B-10 and it has been modified five times, most recently in 1997, and integrated in 2001(Vallado Fernández 2003). The CPC has found that inflation has a profound impact on the informative content of financial statements, and therefore that statements must be changed so that the statements accurately reflect the financial position of the company (Vallado Fernández 2003). In the U.S., for example, inventory and assets are held at lower of cost or market as per ARB 43.

The U.S. did at one time did adopt a form of inflation accounting. SEC Accounting Series Release 190, released in 1976, required large firms to disclose certain replacement cost estimates—such as those of inventories—in their Forms 10-K. The FASB issued SFAS 33 in 1979—and the SEC updated its release accordingly—requiring companies with inventories and plant assets of greater than $125 million, or total assets of greater than $1 billion, to include current cost and current dollar estimates in their footnotes (Journal of Accounting, Auditing, and Finance 1987). The FASB subsequently issued SFAS 82 in 1984 removing the constant dollar estimate requirement.

Perhaps the FASB did not see inflation accounting for the U.S. as appropriate because it was not—and still is not—a hyperinflationary economy. The FASB defines a hyperinflationary economy as one which experiences 100% inflation over three years (IASO 1999). Inflation accounting is a good example of an area in which the circumstances of the countries differ because Mexico's inflation rate has historically been much higher than that of the U.S. Mexico's inflation rate peaked at 159% in 1987 (Vallado Fernández 2003), while the U.S. inflation rate has stayed around 2-5% annually during the past 25 years and although unstable before 1982, it was much more controlled than Mexico's rate. Figure 2 on the next page shows the fluctuation of the inflation rates of the U.S. and Mexico's between 1975 and 2002. However, Mexico's inflation rate has been more stable since 2001, ranging from 3.1% to 5.2% from 2003-2006 (Barrientos 2007) and was 3.98% from June 2006 to June 2007 (Banco de Mexico 2007).

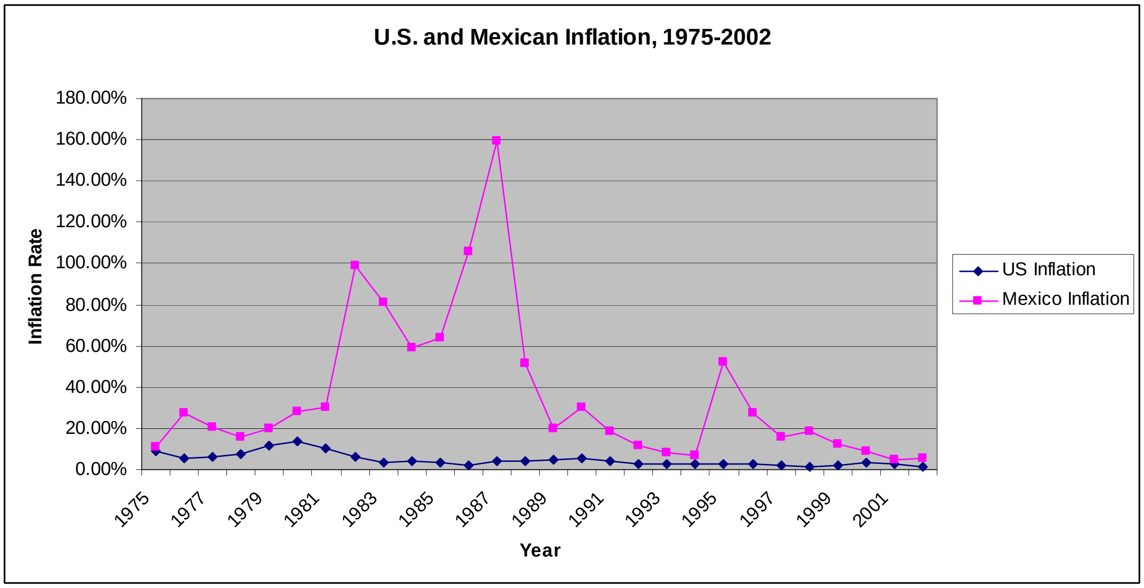

Figure 2: U.S. and Mexican Inflation rates from 1975-2002
Source: Hoffarth 2006 and Vallado Fernández 2003

Mexico's rate of inflation is most accurately reflected by their Consumer Price Index, translated *Índice de Precios al Consumidor* (INPC), which is much like the Consumer Price Index in the U.S. The INPC measures the rate of change in prices of consumer goods, and is calculated by the Bank of Mexico (Vallado Fernández 2003). Currently, some standards setters in Mexico are saying that since inflation has been controlled and relatively low in recent years, it may be time to revise Mexico's standards on inflation accounting (Davis-Friday and Rivera 2000). However, the CPC has chosen to be cautious about abandoning a standard simply because of a few good years. It recommended that the CINIF maintain the use of the standard and wait until a consistent inflation rate is firmly established (IMCP 2005).

One effect inflation has on business practices in Mexico is that it creates a situation in which it is favorable to have more monetary liabilities than monetary assets. Inflation renders monetary assets less valuable and monetary liabilities less costly. The effect of inflation on monetary assets and liabilities is referred to monetary position *larga* (long) and *corta* (short), respectively (Vallado Fernández 2003). If a company has a relatively equal amount of monetary assets and liabilities, its position is called *nivelada* (balanced).

Exchange Rate Accounting

The accounting standards for foreign currency translation are very similar in the two countries, according to the study published by CICA. For presentation on the financial statements, Mexico divides international operations into two categories. For a "foreign operation," monetary assets and liabilities are translated into pesos using the exchange rate at the end of the period and non-monetary assets are translated using the exchange rate at the date of the transaction. Items on the income statement can be translated using either the exchange rate at the transaction date or an average for the period. The effects of translation on the income statement are recorded as financing costs. For a foreign entity, the statements must be altered to reflect the purchasing power of the currency where the entity is located. All items are translated using the end-of-period exchange rate, and all translation adjustments go to an equity account.

For translating to U.S. currency for SEC financial reports, there are also two different methods. If a company uses dollars as its primary—or functional–currency, the nonmonetary assets and liabilities are translated using historical exchange rates, while monetary assets and liabilities are translated using current exchange rates. If the "functional" currency is a foreign currency, balance sheet items are translated at current exchange rates, and income statement items are translated at weighted-average rates.

Like in Mexico, the translation adjustments are taken to an equity account and not included in net income (CICA 1998).

Business Combinations

The topic of business combinations is one which has seen recent revisions in both the U.S. and Mexico. However, according to Bulletin B-7, the only method to be used to account for combinations is the purchase method. In the U.S., the pooling-of-interests method used to be the method of choice, but it has recently been prohibited. The FASB published FAS 141 in 2001, stating that all business combinations are to be accounted for under the purchase method. Another difference that has been reconciled recently is the treatment of goodwill. In both countries, goodwill is not amortized, but tested at least once per year for impairment. This became the rule in Mexico with the implementation of Bulletin B-7 effective January 1, 2005. Treatment of business combinations is a good example of the process of harmonizing accounting standards.

Consolidation and Equity Accounting

Consolidation accounting was the primary area of study in my Advanced Accounting class at Monterrey Tech. As I mentioned in my introduction, the professor chose to use the same textbook used at many universities in the U.S., and had to make a few modifications for Mexican accounting principles that differed from those presented in the textbook. According to CICA (1998), the primary difference between U.S. and Mexican standards for consolidation accounting is that the Mexican standards focus on the concept of control, while U.S. standards focus on majority ownership. The 50% ownership principle still generally applies in Mexico, but there exist numerous exceptions to it. In the U.S., the 50% rule applies unless there is strong evidence that the parent company does not have control.

Another issue is how to account for significant influence. In Mexico, a company is said to have significant influence if it owns at least 10% of the stock of another company unless circumstances show otherwise. In the U.S., an investor is presumed to have significant influence at 20% ownership. In both situations, the equity method, also called one-line consolidation, applies. Another issue that Mexico addresses is parent-company-only statements, in which the equity method is required; this issue has not been addressed by the SEC (CICA 1998).

Deferred Taxes/Accounting for Income Taxes

The U.S. uses the asset and liability method to account for income taxes as per SFAS 109, and Mexico's method is very similar, as per Bulletin D-4. Mexico used to require that a benefit be realized before any asset was recognized, but with the adoption of the asset and liability method, the standard is very similar to the method used in the U.S., in which a benefit can be recorded if it is likely to be realized.

Recent Progress Towards Harmonization

There are a number of issues that were discussed in the 1998 study of the accounting differences between the two countries. Mexico used to not have an accounting for earnings per share, but it has since implemented a standard that covers the issue. As I discussed earlier, Mexico implemented a standard for accounting for goodwill in a manner similar to that in the United States. Both countries have expressed the desire to harmonize their accounting standards with the IFRS standards, and the progress they make in this area will close the gap between the standards of the two countries.

Parent Company Financial Reporting

In addition to accounting differences related to financial reports, there are also differences in requirements for the presentation of financial reports. One such difference is that Mexican Securities laws require that companies with subsidiaries file not only reports detailing the financial position of the company and its subsidiaries, but also parent-company-only financial statements (CEMEX 2006a).

Reconciliation of Accounting Principles

The U.S. Securities and Exchange Commission (SEC) requires that foreign firms being traded on U.S. stock exchanges, usually registered as American Depositary Shares (ADSs), file form 20-F, which includes a reconciliation of the company's home country's accounting principles to U.S. GAAP. Perhaps the most interesting thing to note about the reconciliation between MFRS and U.S. GAAP is that the SEC does not require that

Mexican firms adjust their assets and liabilities recorded at inflationary costs to be adjusted to their historical costs for reporting in the U.S. According to the 2006 Form 20-F filed by CEMEX, the figures recorded at inflationary costs are considered to be a more meaningful presentation of the actual cost to the company.

Taxation

One aspect from a U.S. perspective that makes Mexico an attractive place to do business is its relatively low corporate tax rates. All entities are taxed at the corporate level, though some can receive passthrough treatment for U.S. income tax purposes if taxed in the U.S. Mexico's corporate income tax rate is 28% (Kaywood and Silva 2007). There is also a real estate transfer tax and some state taxes. Mexico also has a "business assets tax," which is currently set at 1.25% of total assets. Previously, the rate was 1.8%, but assets could be netted against liabilities (Kaywood and Silva 2007). This tax is not in addition to the income tax, but if the business asset tax is greater than the income tax for a certain year, then the excess is due. This issue is currently in the courts due to a challenge by CEMEX, which I will discuss below. Kaywood and Silva also discuss Mexico's statutory profit-sharing system, in which 10% of a company's taxable income must be placed in a profit-sharing plan for employees.

Aside from the low corporate income tax rate, another advantage of the Mexican tax system is that up to a certain amount, dividends are not taxable to shareholders. The dividend becomes taxable when it exceeds the amount in an account called "CUFIN," which includes the company’s after-tax profits. Mexican companies can also return paid-in capital to investors without taxes if they follow the CUFIN requirements. There are also a number of exemptions of certain types of income, such as the exemption for non-residents selling shares of Mexican companies on public stock exchanges (Kaywood and Silva 2007).

Another significant tax for those doing business in Mexico is the value-added tax, which is referred to in many essays as the VAT. In Mexico, it is called the IVA, which is the acronym for the Spanish translation of “value-added tax.” The VAT is a 15% tax “on the transfer of goods and services, the lease of tangible property, and the importation of goods and services” (Kaywood and Silva 2007). This may seem to add up to a lot of taxes, but Mexico’s tax system appears to be more favorable overall to taxpayers. An article from the website of the Organisation for Economic Co-operation and Development supports this statement. The article stated that “the Mexican tax system encompasses a number of commendable features, and disincentives to work, save and invest appear less severe than in most other OECD countries” (OECD 2000).

Chapter 3: The Cement Industry

This section provides an illustrative example of the comparison of the standards and practices between the two countries. Because of the size of the United States economy and the level of information available, there are many industries that could be analyzed. However, Mexico's economy is less developed and there are fewer industries in Mexico that are not dominated by foreign investors. The two most prominent of these industries are the petroleum industry and the cement industry. In this paper, I use the cement industry as my example.

This section uses Mexican cement giant CEMEX to show how the similarities and differences discussed in the previous two sections manifest themselves in the cement industry. The intent of the first two sections was to present what the business and accounting similarities and differences are, while the intent of this section is to show how they work in practice and their importance to the industry.

CEMEX Company Profile

One of Mexico's claims to fame is Monterrey-based global cement giant Cementos Mexicanos (CEMEX). According to the Engineering News Record, CEMEX has become the world's largest aggregate producer after its hostile takeover of Australian construction group Rinker, which cost them nearly $15 billion (ENR 2006). In 2004, CEMEX also took over British cement maker RMC for $5.8 billion (The Economist 2005b). Its top competitors worldwide are Lafarge from France, Holcim from

Switzerland, Heidelberg Cement from Germany, and CRH from Ireland. In terms of market capitalization, CEMEX is the second largest of the group at $25 billion, while Lafarge has a market capitalization of $28.4 billion (Yahoo! 2007).

Many attribute the company's success and growth to its management. CEMEX has been led by Lorenzo Zambrano, who, along with many of the company's managers, graduated from Monterrey Tech. He also earned an MBA from Stanford University. Another interesting fact to note is that although it is headquartered in Monterrey, the company's official language is English (The Economist 2005b).

Just one example of the phenomenal management at CEMEX is something that took place at its center of operations in Guadalajara. With all the obstacles posed by Mexico's infrastructure, CEMEX was having a difficult time delivering cement in a timely fashion. In order to address this problem, management nominated one of its computer staff, Homero Resendez, to bring together the accounting and information systems. While doing this, Resendez sought advice from Federal Express, which is an industry leader at reliable, on-time delivery. This visit, combined with a trip to the Houston Fire Department's 911 call center helped reshape how CEMEX dispatched its trucks to deliver cement and drastically improved the timeliness of its deliveries. (Petzinger 1996).

Although the company is based in Mexico, the majority of the company's income is generated outside the country. According to the Form 20-F from 2006, Mexican operations only represented 18% of net sales, while operations in the United States represented 21% of net sales. The remaining 61% came from other regions, including the United Kingdom, Spain, the Rest of Europe region (including Germany and France), South America, Central America, and the Caribbean (including Venezuela and Colombia), Africa, the Middle East, and Asia.

Dealings with the Government

Much like corporations in the U.S., CEMEX must follow U.S. regulations when doing business here. Two issues that currently involve the U.S. government in its business are taxes and trusts. Because of the recent acquisition of Rinker, the U.S. Department of Justice has said that because of antitrust regulations, according to CEMEX (2006b), the company has been required to divest certain parts of its operations in the U.S. If the company fails to do so by October 17, 2007, the U.S. District Court will have the right to appoint a trustee to take over the divestitures. A major problem with this timeline, as CEMEX noted in its disclosures, is that this may not be sufficient time to find a buyer willing to pay a reasonable price. This decision by the court could adversely affect the company's bottom line for 2007 because it does not have a choice about selling those assets and must sell to the best bidder before the deadline. Furthermore, potential buyers know that CEMEX must sell the assets and will be inclined to make low offers.

Because CEMEX does business in many nations, it must pay taxes and duties to many governments. According to the 2006 annual report, the average of the tax rates of the other nations where the company does business is higher than that of Mexico. This comparison is shown in the calculation of the effective tax rate for financial reporting purposes, and included under the adjustment titled “other,” which includes the effects of income tax rates in countries where the company does business. The increase to the effective tax rate is 2.8% of net income, bringing the effective tax rate to approximately 17% of net income.

Since 1990, the company has been in a regulatory dispute with the Commerce Department in the U.S. because it is being required to pay anti-dumping duties on its U.S. sales. Until August 2003, it was required to pay duties between 37.49% and 80.75% over the transaction amount. Since then, the duty has been set at a flat rate which has decreased and is now at $3.00 per ton. Authorities from the Mexican and U.S. governments reached an agreement in January 2006 to completely eliminate these duties over a 3 year period, and according to the agreement, there should be no duties or restrictions on cement imports from Mexico into the U.S. by sometime in early 2009. As a result, CEMEX has received over $100 million in refunds from the U.S. Commerce Department (CEMEX 2006b).

The company’s legal disputes, however, are not only with governments of foreign nations. Recently, it has had a number of disagreements with the Mexican taxing authority. In Mexico, corporations are required to pay income taxes based on the statutory tax rates or a tax on the value of their assets, adjusted for inflation, whichever is greater. However, beginning in the tax year 2007, the tax rate on business assets decreased, but corporations are no longer allowed to deduct their liabilities from their assets in calculation of the tax. This effectively increases the tax rate for all corporations that have significant amounts of debt they formerly were able to offset against their assets. CEMEX has said that it believes that the change to the law is unconstitutional "because it contravenes the required equilibrium between the tax burden and the entities' payment capacity" (CEMEX 2006a). The company has stated that it plans to challenge the amendment to the tax in the courts.

The company has also challenged the constitutionality of another amendment to the country's tax law, which requires companies who have investments in foreign countries for which the income tax burden is less than 75% of what it would be in Mexico to pay Mexican income tax on any income generated from those investments. The company filed two motions and obtained favorable rulings on both in 2005 and 2006. However, as of the date of the financial statements, the Mexican tax authority has appealed the rulings and they have yet to be resolved.

CEMEX and Financial Reporting

CEMEX and the SEC

One of the requirements of a foreign company listed on stock exchanges in the U.S., as discussed earlier, is that it files a Form 20-F, which is a foreign company's version of a 10-K. The company is also required to file numerous other forms with the SEC. One required form is a 6-K, which is an update on the company's activities. It also must file an 11-K, which is an annual report on employee stock purchase plans. In connection with its acquisition of Rinker, it has filed numerous Forms SC TO T/A, which are forms detailing and updating the status of a tender offer by a third party.

All of the company's financial statements were audited by KMPG Cárdenas Dosal, S.C., Mexico's member of KPMG International. Hence, its U.S. users can be reasonably assured that the reconciled financial statements are prepared according to the same professional standards as any domestic public company. The one discrepancy that users should note, however, is that the reconciliation does not reverse the effect of inflation accounting for assets not of foreign origin because this reversal is not required, as discussed earlier.

CEMEX is listed on the New York Stock Exchange with two types of stock. Investors can buy a CEMEX American Depositary Share (ADS), or a *Certificado de Participación Ordinario* (CPO). Each ADS represents ten CPOs, and each CPO represents two Series A shares and one Series B share. Citibank, N.A. is the depositary for the ADSs.

Sarbanes-Oxley Compliance

Another aspect of being a publicly traded company in the U.S. is that CEMEX must follow the requirements of SOX. This can be quite burdensome, as many domestic companies have complained of the costs of compliance with the far-reaching act regulating corporate governance and transparency. CEMEX has taken steps to ensure that it complies with SOX. The CEO and CFO certify the annual reports, management provides a report on internal controls over financial reporting, and the company has an independent audit committee and a code of ethics. In order to achieve further assurance that top management's certification of the annual reports is valid, the company has an internal certification process in which the senior executives below the CEO and CFO must certify that the information is accurate. It is interesting to note that CEMEX worked to ensure compliance with SOX in 2002 and subsequent years (CEMEX 2007), even though the SEC did not require complete compliance for foreign private issuers until fiscal years ending on or after July 15, 2005 (Inside Sarbanes-Oxley 2005).

Accounting Policies

The Form 20-F, which is my primary source of financial information for CEMEX, includes a reconciliation of the company's financial statements to U.S. GAAP. With regard to this reconciliation, I will discuss the differences in the balances in the stockholders' equity accounts as well as the reconciliation's effect on the income statement. In addition to the issues I address, there are also a number of smaller reconciliation items affecting equity and income, many of which are considered immaterial.

Stockholders' Equity

One significant issue is that under U.S. GAAP, stockholders' equity is slightly over $1.3 billion lower than it is under MFRS. This constitutes a difference of about 7% of total stockholders' equity. Under U.S. GAAP, shareholders' equity increased due to adjustments for goodwill, deferred income taxes, inflation for machinery and equipment, and capitalized interest. There were decreases to shareholders' equity due to adjustments to deferred employees' statutory profit sharing (ESPS), employee benefits, minority interest (financing transactions and U.S. GAAP presentation), depreciation, investment in net assets of affiliated companies, deferred charges, and the cumulative effect of an accounting change. All of these adjustments are shown in Table 2 below.

The most significant decreases to stockholders' equity from the GAAP reconciliation were due to adjustments to minority interest. The largest part of this was related to perpetual debentures, which under MFRS can be classified in stockholders' equity under "minority interest." Per the statement's summary of SFAS 150, GAAP requires that "instruments having characteristics of both liability and equity instruments that are mandatorily redeemable should be classified as debt." The other part of the reconciliation related to minority interest deals with the fact that U.S. GAAP requires that minority interest be presented separately from equity, whereas under MFRS, it is a component of equity.

The two other significant decreases to stockholders' equity were related to ESPS and the cumulative effect of the accounting change. The ESPS adjustment is related to deferred tax liabilities because the company records temporary differences between net income and taxable income for ESPS. The cumulative effect of the accounting change was related to severance payments to employees. When CEMEX purchased RMC in 2005, it charged the severance costs against goodwill. SFAS 141, however, does not allow for severance payments to be included as part of the purchase price of another business.

Therefore, the reconciliation to GAAP required that these costs be removed from goodwill and charged against earnings.

The largest increase to stockholders' equity from the reconciliation was attributable to adjustments to goodwill. Some of this was because of U.S. GAAP adjustments as of the acquisition dates of certain businesses. Another part is because up until December 31, 2004, goodwill was amortized under MFRS. U.S. GAAP required then, as it does now, testing for impairment at least once a year. The FASB discussed in FAS 142 the need for international convergence and referenced International Accounting Standard 38, which treats intangible assets in this way. Starting on January 1, 2005, MFRS began treating goodwill in a similar manner. Another 2004 adjustment related to goodwill resulted from the purchase of shares of CAH. The excess of the price paid over the fair value of the assets received was included in stockholders' equity under MFRS. Under U.S. GAAP, this excess was charged against earnings because it did not qualify as goodwill.

Carrying amounts for goodwill under MFRS and U.S. GAAP are also different because of inflation and foreign currency translation issues. Under GAAP, goodwill amounts are "carried in the reporting unit's functional currency, are restated by the inflation factor of the reporting unit's country, and are translated into Mexican pesos at the exchange rates prevailing at the reporting date" (CEMEX 2006b). MFRS requires goodwill to be "carried in the functional currencies of the holding companies for the reporting units, translated into pesos, and then restated using the Mexican inflation index" (CEMEX 2006b).

Table 2: Changes to CEMEX stockholders' equity in reconciliation to U.S. GAAP
Millions of constant Mexican pesos as of December 31, 2006

December 31	**2005**	**2006**
Stockholders' equity under MFRS	$ 119,876	159,609
Inflation adjustment	(5,433)	-
Stockholders' equity under MFRS after inflation adjustment	114,433	159,609
U.S. GAAP Adjustments:		
Goodwill, net	4,961	8,183
Deferred income taxes	592	1,691
Deferred employees' statutory profit-sharing	(3,026)	(3,012)
Employee benefits	(362)	(191)
Minority interest – financing transactions	-	(13,500)
Minority interest – U.S. GAAP Presentation	(5,963)	(7,291)
Investment in net assets of affiliates	(247)	(125)
Inflation adjustment – machinery & equipment	4,734	3,397
Employee stock option programs	1,032	-
Other adjustments – Deferred charges	(234)	(132)
U.S. GAAP adjustments before cumulative effect of accounting change	1,482*	(10,928)*
Cumulative effect of accounting change	-	(1,307)
Stockholders' equity under U.S. GAAP after cumulative effect of accounting change	$ 115,925	147,374

*Minor adjustments not shown
Source: CEMEX 2006b

The other two most significant increases to stockholders' equity came from inflation adjustments to machinery and equipment and from deferred tax assets. The inflation adjustment results because MFRS requires assets to be restated at the inflation rate of the asset's country of origin and translated for the exchange rate of the functional currency of the asset's current country, while the U.S. GAAP reconciliation requires the inflation to be recognized at the rate of the asset's current country. To account for its income taxes for U.S. GAAP purposes, CEMEX follows SFAS 109, which requires use of the asset and liability method. Under this method, assets or liabilities are recorded due to temporary differences between taxable income and book income, as I described earlier related to ESPS. The MFRS requirement is very similar, but there are still some differences in stockholders' equity due to deferred tax assets and liabilities before the implementation of this method under MFRS, and also to the fact that MFRS requires these assets and liabilities to be classified as long-term, whereas U.S. GAAP allows them to be either short-term or long-term.

The Income Statement

Many of the issues that brought about changes to stockholders' equity also affect the income statement. These changes are shown in Table 3 below. This year, the net effect was smaller on the income statement than in equity, as it was in the prior year. The primary reason that this year's effect on equity is so much greater than the effect on income is the classification of the perpetual debentures. The net effect of the reconciliation to GAAP in the Income Statement was only 308 million pesos, while the effect on equity was about 12.2 billion pesos. In recent years, it is also noticeable that as the principles become more similar, the adjustments become fewer and smaller. For instance, in 2004, the reconciliation from MFFRS to U.S. GAAP included 16 adjustments increasing net income by approximately 3.6 billion pesos. In 2006, there were 13 adjustments, decreasing net income by 308 million pesos. Of these adjustments, the most significant increase resulted from deferred taxes, and the largest decrease was due to the cumulative effect of the accounting change. Hedge accounting and inflation accounting also caused significant decreases in net income under U.S. GAAP.

Table 3: Adjustments to CEMEX net income to reconcile to U.S. GAAP
Millions of constant Mexican pesos as of December 31, 2006

Year ended December 31	**2004**	**2005**	**2006**
Net income under MFRS	$ 15,224	24,450	25,862
Inflation adjustment	387	(1,110)	-
Net income under MFRS after inflation adjustment	15,611	23,340	25,682
U.S. GAAP Adjustments:			
Goodwill	947	-	-
Deferred income taxes	410	(208)	967
Employee benefits	29	(826)	131
Hedge accounting	198	1,119	(437)
Inflation adjustment on fixed assets	(257)	(318)	(295)
Derivative adjustments	1,577	(1,531)	-
Equity forward contracts in CEMEX stock	462	-	-
Employee stock option programs	-	895	-
Monetary position result	320	181	163
U.S. GAAP adjustments before cumulative effect of accounting change	3,649	(323)	587
Cumulative effect of accounting change	-	-	895
Net Income under U.S. GAAP after cumulative Effect of accounting change	$ 19,260*	23,017*	25,374*

*Minor adjustments not shown
Source: CEMEX 2006b

U.S. based concrete producer Florida Rock Industries provides a contrast to the method CEMEX uses for inventory accounting. Though much smaller than CEMEX, it makes many of the same products, and is the largest U.S. firm in the industry, with a market capitalization of $4.6 billion. Florida Rock primarily uses the last-in, first-out (LIFO) method to account for its inventory. The exception is that it uses first-in, first-out (FIFO) for its parts and supplies inventory. Because of this method, it has to disclose the excess of "current cost" over "LIFO stated values," as well as the amount of the increase to cost of goods sold due to the use of LIFO. Using this method is, in a way, similar to the inflation adjustment that CEMEX uses in that it uses more recent prices to determine the cost of sales. The major difference is that while companies that use inflation accounting write their inventories up to fair value, companies that use LIFO maintain their inventory values, but use the more recent costs. Both methods take into account the effects of changing prices. Florida Rock also adjusts its inventory to the lower of cost or market, so if there is any deflation of prices, it will be recorded.

The Corporate Practices and Audit Committee

Much like firms in the U.S., CEMEX is required by SOX to have an audit committee. According to the 2006 Form 20-F, a new securities market law in Mexico required it to create a "Corporate Practices Committee." It elected to give its current audit committee the required responsibilities of the new committee and change its name to meet the new requirements. The responsibilities of this new committee include evaluating and enforcing internal controls, ensuring the financial statements are accurate and the auditors do good work, and overseeing all the accounting policies, officer compensation, and related-party transactions (CEMEX 2006b). The laws also require all members of this committee to be "independent directors." Some may have doubts that each person is independent because two of the members of this committee are second cousins of the

CEO. Section 301 of the Act states that to be independent, a director cannot receive any compensation from the company other than for their board service, and can not be an "affiliated person." The only mention made of relationship to executives relates to immediate family, and thus second cousins appear to qualify as independent if they meet all the other requirements.

Implications and Conclusions

As we have seen, doing business abroad is complex. There exist numerous cultural differences, which influence business practices, and must be reconciled in order to succeed. Mexico has a different corporate structure than the U.S., and companies need to know how to appropriately organize and conduct their business. They also need to know how the laws and treaties between the U.S. and Mexico, such as NAFTA, affect their company specifically.

There are also significant financial reporting differences of which companies must be aware in order to plan and report correctly. The understanding of these differences could mean the difference between choosing to be listed on a public exchange in one country and choosing not to. Investors also need to be aware of these differences in order to effectively use the information presented to them. It is also important to consider the role that IFRS will have because both Mexico and the U.S. are working towards international harmonization of standards, and to ignore this aspect of financial reporting would be a failure to plan for the future.

The example from CEMEX illustrates how some of these accounting differences affect companies listed on foreign stock exchanges. CEMEX has numerous items every year that are included in their reconciliation from MFRS to U.S. GAAP. It has also taken numerous steps to comply with SOX. Florida Rock provides a good contrast to CEMEX because it is based in the U.S. and already must follow U.S. accounting standards and regulations.

This essay is by no means an exhaustive description of all the issues that companies face doing business in another country. Rather, it is meant to provide an overview of the kind of issues that multinationals and investors face when doing business across the U.S.-Mexico border.

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APPENDIX

CEMEX Financial Statements under MFRS
From the 2006 CEMEX Annual Report

Consolidated Balance Sheeets
CEMEX S.A.B. de C.V. and Subsidiaries
Millions of constant Mexican Pesos as of December 31, 2006
US Translation: Millions of US Dollars at 10.80 pesos per US Dollar

	2006 US Dollar Translation	**2006**	**2005**
ASSSETS			
CURRENT ASSETS			
Cash and investments	US $ 1,579	$17,051	6,963
Trade receivables less allowance for doubtful accounts	1,411	15,236	18,440
Other accounts receivable	786	8,488	8,979
Inventories	1,193	12,884	12,009
Other current assets	192	2,079	1,850
Total current assets	5,161	55,738	48,241
NON-CURRENT ASSETS			
Investments in associates	709	7,654	9,728
Other investments and non-current accounts receivable	886	9,567	8,324
Properties, machinery and equipment, net	17,196	185,714	179,942
Goodwill, intangible assets and deferred charges	6,020	65,025	63,631
Total non-current assets	24,811	267,960	261,625
TOTAL ASSETS	**US $ 29,972**	**323,698**	**309,866**
LIABILITIES AND STOCKHOLDERS' EQUITY			
CURRENT LIABILITIES			
Short-term debt including current maturities of long-term debt	US $ 1,252	$ 13,514	13,788
Trade payables	1,717	18,541	15,771
Other accounts payable and accrued expenses	1,468	15,861	18,070
Total current liabilities	4,437	47,916	47,629
NON-CURRENT LIABILITIES			
Long-term debt	6,290	67,927	95,944
Pensions and other postretirement benefits	639	6,900	6,966
Deferred income taxes	2,571	27,770	28,224
Other non-current liabilities	1,256	13,576	11,227
Total non-current liabilities	10,756	116,173	142,361
TOTAL LIABILITIES	15,193	164,089	189,990

STOCKHOLDERS' EQUITY			
Majority interest:			
Common stock	366	3,956	3,954
Additional paid-in capital	5,074	54,801	49,056
Other equity reserves	(8,014)	(86,554)	(85,986)
Retained earnings	13,055	140,993	122,283
Net income	2,378	25,682	24,450
Total majority interest	12,859	138,878	113,757
Minority interest	1,920	20,731	6,119
TOTAL STOCKHOLDERS' EQUITY	14,779	159,609	119,876
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	**US $ 29,972**	**$ 323,698**	**309,866**

Consolidated Statements of Income
CEMEX S.A.B. de C.V. and Subsidiaries
Millions of constant Mexican Pesos as of December 31, 2006
US Translation: Millions of US Dollars at 10.80 pesos per US Dollar

	2006 US Dollar Translation	**2006**	**2005**	**2004**
Net sales	US $ 18,249	$ 197,093	177,385	94,915
Cost of sales	(11,649)	(125,804)	(107,341)	(53,417)
Gross profit	6,600	71,289	70,044	41,498
Administrative, selling and general expenses	(3,655)	(39,475)	(41,253)	(19,931)
Operating income	2,945	31,814	28,791	21,567
Comprehensive financing result:				
Financial expense	(494)	(5,334)	(6,092)	(4,336)
Financial income	46	494	455	273
Results from valuation and liquidation of financial instruments	(14)	(148)	4,471	1,395
Foreign exchange result	20	219	(912)	(275)
Monetary position result	398	4,303	4,914	4,495
Net comprehensive financing result	(44)	(466)	2,836	1,552
Other expenses, net	(34)	(369)	(3,676)	(5,635)
Income before income taxes, employees' statutory profit sharing and equity in income of associates	2,867	30,979	27,951	17,484
Income taxes, net	(486)	(5,254)	(3,885)	(2,137)
Employees' statutory profit sharing	(15)	(166)	10	(346)
Total income taxes and employees' statutory profit sharing	(501)	(5,420)	(3,875)	(2,483)
Income before equity in income associates	2,366	25,559	24,076	15,001
Equity in income of associates	122	1,314	1,012	467
Consolidated net income	2,488	26,873	25,088	15,468
Minority interest net income	110	1,191	638	244
Majority interest net income	**US $ 2,378**	**$ 25,682**	**24,450**	**15,224**

Consolidated Statements of Changes in Financial Position
CEMEX S.A.B. de C.V. and Subsidiaries
Millions of constant Mexican Pesos as of December 31, 2006
US Translation: Millions of US Dollars at 10.80 pesos per US Dollar

	2006 US Dollar Translation	**2006**	**2005**	**2004**
OPERATING ACTIVITIES				
Majority interest net income	US $ 2,378	$ 25,682	24,450	15,224
Adjustments to reconcile majority interest net income to resources provided by operating activities:				
Depreciation of properties, machinery and equipment	1,055	11,393	10,887	6,985
Amortization of intangible assets and deferred charges	137	1,479	1,750	3,000
Impairment of assets	60	649	181	1,641
Pension and other postretirement benefits	78	844	2,181	492
Deferred income taxes charged to results	107	1,160	1,225	1,097
Equity in income of associates	(122)	(1,314)	(1,012)	(467)
Minority interest	110	1,191	638	244
Resources provided by operating activities	3,803	41,084	40,300	28,216
Changes in working capital, excluding acquisition effects:				
Trade receivables, net	298	3,222	(504)	770
Other accounts receivable and other assets	25	266	(1,496)	(348)
Inventories	(89)	(962)	1,718	(158)
Trade payables	256	2,761	1,990	164
Other accounts payable and accrued expenses	(209)	(2,260)	(2,094)	(2,906)
Net change in working capital	281	3,027	(386)	(2,478)
Net resources provided by operating activities	4,084	44,111	39,914	25,738
FINANCING ACTIVITIES				
Proceeds from debt (repayments), net, excluding	(2,667)	(28,799)	14,618	(4,254)

the effect of business acquisitions				
Decrease of treasury shares owned by subsidiaries	165	1,781	-	-
Liquidation of optional instruments	-	-	-	(1,129)
Dividends paid	(531)	(5,740)	(5,302)	(4,516)
Issuance of common stock from stock dividend elections	532	5,742	4,722	4,456
Issuance of common stock under stock option programs	-	5	19	72
Issuance (repurchase) of equity instruments by subsidiaries	1,250	13,500	-	(827)
Other financing activities, net	148	1,594	(6,413)	(1,686)
Resources (used in) provided by financing activities	(1,103)	(11,917)	7,644	(7,884)
INVESTING ACTIVITIES				
Properties, machinery and equipment, net	(1,372)	(14,814)	(9,093)	(5,055)
Disposal (acquisition) of subsidiaries and associates	253	2,727	(44,928)	(8,608)
Minority interest	(7)	(79)	(169)	(1,528)
Goodwill, intangible assets and other deferred charges	(224)	(2,424)	11,205	1,622
Other investments and monetary foreign currency effect	(697)	(7,516)	(1,597)	(3,936)
Resources used in investing activities	(2,047)	(22,106)	(44,582)	(17,505)
Increase in cash and investments	**934**	**10,088**	**2,976**	**349**
Cash and investments at beginning of year	645	6,963	3,987	3,638
Cash and investments at end of year	**US $ 1,579**	**17,051**	**6,963**	**3,987**