Panel Discussion Part 1: Establishing an Agency or Distributorship in Mexico

Boris Kozolchyk
Ignacio Gomez-Palacio
Juan Manuel Trujillo

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PART ONE: ESTABLISHING AN AGENCY OR DISTRIBUTORSHIP IN MEXICO

MODERATOR: MICHAEL W. GORDON,*
PANEL MEMBERS: BORIS KOZOLCHYK,**
IGNACIO GÓMEZ-PALACIO,***
JUAN MANUEL TRUJILLO****

THE PROBLEM

GROWFAST CHEMICALS, INC., AND DISTRIBUIDORAS AGRÍCOLAS, S.A. GROWFAST CHEMICALS, INC., (GROWFAST) is a Delaware chartered corporation with principal administrative offices in Topeka, Kansas. It has manufacturing facilities in several states. GROWFAST manufactures many different trademarked pesticides and fungicides used by commercial growers of ornamental plants. One of the fungicides is Sollate™, which for nearly two decades has been used extensively by commercial and home growers of many tropical plants, including orchids. It has long been considered the only successful fungicide to control several serious fungi. GROWFAST has no significant competitors in the United States for Sollate™, having nearly the entire market. It has competition for many other of its products, however.

Intellectual property protection

Patent. The formula for Sollate™ is patented in the United States. Due to patentable improvements in Sollate™, it has a dozen more years of patent protection.

Trademark. The name Sollate™ is part of a commonly recognized logo which is a protected trademark registered in the United States and several European nations.

Copyright. The detailed instruction manual for the use of Sollate™ has a copyright in the United States, granted nearly twenty years ago.

Establishing an Agency or Distributorship in Mexico. GROWFAST decided during the tripartite negotiations which led to the creation of NAFTA to enter the Mexican market after NAFTA was implemented. Because GROWFAST has little experience marketing its products in Latin America, it has chosen to find either an agent or distributor to handle Sollate™ sales in Mexico. Through the assistance of the Commercial Officer at the United States embassy in Mexico City, GROWFAST contacted officers of a Mexican owned distributorship of a wide variety of

* Chesterfield Smith Professor of Law, University of Florida College of Law.
** Director and President, National Law Center for Inter-American Free Trade, Tucson, Arizona.
*** Of Counsel, Jáuregui, Navarrete, Nader y Rojas, S.C., Mexico D.F.
**** National Law Center for Inter-American Free Trade, Tucson, Arizona.
agricultural products, including tools, fertilizers, fungicides and pesticides. The Mexican distributorship, DISTRIBUIDORAS AGRICOLAS, S.A. (AGRICOLAS) is a family owned enterprise located in Monterrey. It distributes agricultural products throughout Mexico. None of its products conflicts with Sollate™, and AGRICOLAS is delighted to be able to add Sollate™ to its list of products.

The president of GROWFAST has asked you to assist in the preparation of the legal documents establishing the chosen form of distributorship. It seems quite obvious that a written agreement will be necessary.

THE DISCUSSION

Michael W. Gordon: We have moved from an era where we questioned whether we ought to do business in Mexico to an era where doing business in Mexico is simply something we do. Now, we want to learn how to do business more effectively. In many ways, I look upon Mexico in the same way I might look on France or Spain or other countries which no longer are in that terribly restrictive phase of their legislation which Mexico went through in the 1970s and well into the 1980s. I have long thought that one thing that was being overlooked: with the enactment of North American Free Trade Agreement ¹ there would follow a great deal more common trade. We need to look more at the problems of the people in the trenches, the problems of blockage at the border, bills of lading and similar subjects. On the other hand, the area that I've been particularly interested in is the area of litigation. With more trade comes more commercial litigation, more product liability litigation. We have two very different systems in which that litigation may take place. So we will try to explore some of those issues.

Should GROWFAST establish an independent foreign agent where title would remain with GROWFAST until products are sold, or have an independent foreign distributor, a more formal relationship, where title would pass to the distributor who would then resell those products? We are concerned with whether or not that choice would exist in Mexico and whether Mexico recognizes a distinction between agents and distributors.

Ignacio Gómez-Palacio: I think it is important to focus first on the terminology and different kinds of contracts that there are in Mexico. We loosely talk about an independent foreign agent and an independent foreign distributor and I'm not sure we're talking about the same things. When U.S. lawyers talk about an agent, Mexican lawyers talk about a commisionista. Is it the same thing? In Mexico, there are three ways to approach the matter based upon law and upon practice. Parties are free to negotiate and enter into appropriate obligations between them. Article 78 of our Código de Comercio² establishes that the parties are free to

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² Código de Comercio [Cód. Com.], art. 78 (Mex.).
enter into obligations since the validity of commercial acts is generally not subject to formalities or predetermined requirements. This is rather aggressive. You must remember that Mexico’s commercial code comes from the last century. There are a number of things we have to confront with this code and our company law. But in this area, there is not too much of a problem because it’s left to the will of parties.

I will review the three different ways in which the relationship between the parties, the principal and agent, may be approached. The first is the practice recognized as the mediation contract, or contrato de mediación. This has nothing to do with arbitration or mediation as commonly used in the United States; here we talking about something else. There is no representation of the principal. This is a contract that is very relevant because there is no representation of the principal and therefore, generally, no tax impact in Mexico. We’ll be talking about the tax matters because when you have a relationship of agent-principal, and the agent in fact represents the principal, and the principal is doing business in Mexico, there is a tax impact. But when you mediate, you don’t have this relationship. For example, this is the kind of contract that is used frequently in the sale of machinery. In Puebla, there are many textile plants. Mediators go around with catalogs, talking to managers, saying, “Look this is a beautiful piece of machinery, worth two million dollars, you’ll do your textiles better. If you want to buy this, this is the name of the seller, the address of the seller, you may contact him.” When you do this, you don’t want to talk about a commission as a payment for the mediator, but a fee, because if you start talking about a commission, you start getting into a different kind of a contract.

I’m going to call the next kind a commission agreement. U.S. lawyers might like to call it an agency agreement, but I’m going to call it a commission because our law refers to a contrato de comisión. Here, note that we have the same word applied to two distinct matters. One meaning is the commission which is the mandate, what one is being asked to do. The same word, comisión may also be applied to the money to be paid for the service. This is important to understand.

Sometimes I find a U.S. lawyer who tries to treat Mexico as a Texas branch. He or she has problems because we are a civil law country and therefore we think differently. We have behind us Justinian, the Roman law and the Napoleonic Code. That means that, generally speaking, when we talk about a particular contract, it is as if we are talking about a box or a particular door. If you say “contrato de comisión” or if you say “contrato de compraventa” that means that under the civil code you go to a building, you go up four stories to the floor called “contracts”, you go down the corridor and open the door which is called “purchase and sale” and there are the rules. It is simply a different way of thinking. It’s not only important that we lawyers in the practice think that way, but the courts think that way too. This means, for example, courts are going to apply the rules that they consider applicable to the nature of that contract, regardless of the name of the contract. Therefore, you may call a contract a “purchase agreement” or “agency agreement” or
"comisión" but, upon analysis, it may be found to be another kind of contract, for example, a mediation contract. You may call it a "mediation contract" but it could turn out to be a commission contract. It is accepted jurisprudence in Mexico, that is, five decisions in the same way, that the court should analyze the nature of the contract, regardless of the name of the contract.

So, talking about the comisión mercantile or the commission agent, we are talking about a contract regulated by the commercial code. You must understand that this contract is a power of attorney. The law says it is a "mandato" applicable to commercial acts. A mandate is contrato de mandato or a mandate contract based on the Civil Code. So this is really a power of attorney for commercial acts, a contrato de comisión. That is close to your agency agreement.

The contrato de comisión is regulated under an old commercial code. It is generally treated as a non-permanent relationship. The code states something to the effect that the commission agent who performs any act in discharge of the commission of his principal must continue it until its conclusion. The understanding is that the agent tacitly accepts the commission. It's so odd. You get the feeling that somebody is getting some kind of an order. Some characteristics of the commission agent are, first, he receives two commissions - the commission which is the mandate, "Sell such goods" (Sollate™ fungicide in the hypothetical problem). Second, he also may be receiving a commission which is the payment of a given fee. This commission can be open or secret. We accept a secret commission, and this is done in many instances. This means that the agent can act in behalf of the principal or in his own name. If acting in his own name, he need not disclose the name of the principal. Therefore, you have a secret agency. However, this agency can be revoked. As civil lawyers, we are very careful of the words we use. We don't say "terminated" or "rescinded." In Mexico, we say "revoked." It is revoked because it is a power of attorney; a mandato, and therefore you can revoke it. Generally speaking, Mexico has no protection for agents or distributors the way other countries have. The relationship can be revoked at any time. It is extinguishable by the agent's death, if the agent is a physical person.

Distribution agreements are not recognized by the laws of Mexico because there is no door, no definition in the civil law. Therefore, this is really left to the free understanding and agreement between the parties. It's what we call contrato innominado or non-named contracts. Why? Because they are not named, or defined, in the Código de Comercio. As a matter of fact, mediation is a non-named contract and innominado also is. The characteristics here are different from the commission contract where the title does not pass to the agent. Here the title to the goods generally passes to the distributor who may or may not hold a mandate. Generally speaking, there is a mandate which can also be revoked at the will of the parties. Other matters such as territory, quotas, inventory, price controls, profits and the like are left to the will of the parties.
Thus, there are three types of contracts: mediation, commission and distribution.

The choice of the type of contract to use may be influenced by the Mexican income tax law or the Mexican labor law. The general rule is that the principal is considered to be doing business in Mexico when he is represented in Mexico. He is acting through his appointee with a certain power of attorney or representation. The income tax law is going to apply to the income, not just his profits. In Mexico, income rather than profits, is going to be subject to tax.

One other issue to be concerned about is the labor law. The principal may find himself sued in Mexico by his agent’s employees under the concept that the agent is in fact a substitute employer and that the true employer is the principal. This is what we call the patron substituto. In practice, a businessperson may use shell companies which are put between two parties in order to protect the true employer. How can this be avoided? In your contract, provide evidence that the agent has means and intends to act as an employer. The agent is a going concern with all the elements of a going concern. Therefore the agent stands as a true employer and not a shell between the two parties.

Gordon: Ignacio has referred to civil law, commercial law, and labor law. Boris, would you explain the Mexican framework, including the different sources of law and the fact that two of those are national and one is state? What kind of laws might apply in this instance?

Boris Kozolchyk: First, a point of terminology. The hypothetical assumes that there is a distinction between a distribution agreement and other title or non-title passing agreements such as regular or consignment sales, franchises, and commission agency agreements. This is not the case. A distributorship agreement under both U.S. and Mexican law may adopt the format of a consignment sale, a commission agency, or a franchise agreement. Legally speaking, a buyer as well as an agent or a franchisee can be a distributor. Now, I turn to salient aspects of the distinctive legal “framework” that Professor Gordon asked me to address. These are: sources of applicable law, method of reasoning and key principles of the law of agency and of contractual remedies.

(a.) Sources of applicable law. Mexico’s private law, i.e., the law that governs lawful transactions between private parties, is found either in the state civil codes or in the civil code for the federal district as well as in the federal commercial code. This civil-commercial dichotomy is not universal throughout the civil law world. Some European countries such as Italy and Switzerland have given it up in favor of a unitary (civil and commercial) code. This is a model that is still being considered by some Latin American countries. Yet, the majority of Latin American jurisdictions (Mexico included) continue to be influenced by the dual code model set forth in early 19th century European codification.

The two most influential approaches were the German or subjective approach and the French, objective or “acts of commerce” approach.¹

¹ For a more detailed description of the two approaches, see Boris Kozolchyk, The Commercialization of Civil Law and the Civilization of Commercial Law, 40 La. L. Rev. 3 (1979).
The German approach specified who had the status of a merchant and enacted a code that governed the rights and duties of both large and small merchants. The French or objective approach provided rules that governed acts of commerce, regardless of who engaged in such acts. Not much analysis is required to discover that these seemingly opposite approaches actually overlap; you can hardly describe who is a merchant without stating what they do, and you cannot list acts of commerce without describing the merchants who ordinarily engage in these acts. With some notable exceptions, Mexico's Código de Comercio chose the objective approach. Accordingly, this code lists the acts of commerce to which it applies. Unlike the state civil codes, the Código de Comercio is a federal enactment. Yet, this dichotomy is also somewhat misleading because most Mexican state civil codes repeat or transcribe many if not most of the provisions of the Civil Code for the Federal District.

From a commercial law standpoint, civil codes have a distinctive scope because they apply to non-profit making transactions of individuals or civil associations. Among these, are family and other non-profit associations, including law firms set up as asociaciones civiles. State civil codes could apply to some of the same transactions as the commercial code as long as these transactions lack the element of intermediation with intent to profit, which is the common denominator of commercial acts under Article 75 of the Código de Comercio. In the hypothetical problem before us, we need to determine if at least one of the parties entered into or performed one of the acts of commerce listed, expressly or analogically, by the commercial code. If so, the commercial code will apply to the controversy. This does not mean that the state civil code or the civil code for the federal district will not be applied. It can still be applied as a supplement or default provision if the federal civil code does not cover the subject or does not provide a useful principle of interpretation. As a provider of supplementary substantive provisions and of general principles of interpretation for the entire spectrum of private law, the civil code functions as the "constitution" of Mexico's private law.

(b.) Method of legal reasoning. Lic. Gómez-Palacio referred to civil law categories as boxes. This is an important datum when attempting to understand key differences between the methods of reasoning of U.S. and Mexican lawyers. What do these boxes mean to a Mexican lawyer? To begin with, they are the result of definitions and classifications. Contracts as well as any other "juristic" acts (i.e., acts by public or private parties to which the legal system attributes legal consequences) are painstakingly defined and classified. Thus, a Mexican law student is taught to distinguish between juristic acts and facts. Juristic acts, in turn, could be a person's legally binding declaration of intent, such as a firm offer or a will, or two or more parties' contracts. Contracts, in turn,
could be *nominados o innominados*. They could also be *unilaterales* or *bilaterales*, real formal or consensual, of *ejecución deferida* or *sinalág-maticos* and so on. Less elaborate classifications are also taught to some U.S. law students (depending upon how "traditional" or "demanding" the law teacher may be) but the normative significance of classifications is totally different in the two legal systems. For a U.S. lawyer, judge or law professor, these classifications are theoretical tools, useful only to the extent that they reflect transactional reality or help to explain statutory or judicial language. For a Mexican lawyer, classifications have substantive value; they are capable of creating, extinguishing or modifying rights and duties. Accordingly, Mexican classifications have a life of their own. If a given transaction does not fit within them it will live a highly uncertain, *sui generis*, legal life.

Definitions and classifications are the logical devices with which Mexican lawyers, jurists and law professors establish the essence (referred to as the *naturaleza jurídica* or legal nature) of legal institutions. A legal institution devoid of an essence, or violative of an established essence, may well lose its right to legal existence. Let me illustrate the impact of "essential" legal reasoning with a set of questions asked of me during a lecture on the law of conditional sales delivered at a Spanish law school approximately twenty years ago. After I described conditional sales law and practice in some civil and common law countries, I was asked, "Isn't it true that sales are, by essence, bilateral, sinallagmatic and consensual contracts? If so, does not title to the property sold automatically pass to the buyer once he and the seller agree on subject matter and price? And, if so, how could there be such a thing as a conditional sale? Isn't it clear that conditional sales simply cannot exist?" Significantly, my questioner was impervious to the fact that, while he questioned the existence of such sales, millions of them were taking place in Spain and throughout the commercial world. What truly mattered to my questioner was not the empirical existence of the described transaction but the transaction's inconsistency with a three century old definition. According

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7. Significantly, the same reasoning apparent in the questions in the principal text was apparent in Latin American doctrinal opposition to conditional sales legislation. For a more detailed discussion, see Boris Kozolchyk, Towards Seamless Borders, Vol. 1: Making Free Trade Work in the Americas (1993).

8. One of the most influential definitions of the contract of sale in the civil law world is found in the work of a great French jurist. See R. J. Pothis, Treatise on Obligations, Vol. 1, published circa 1764 (Chez Debure) and translated into Spanish shortly thereafter. The 3rd edition of the Spanish translation of Pothis's *Tratado de las Obligaciones* (trans. by S.M.S. (Barcelona, Biblioteca Científica y Literaria, undated)) first establishes the essence of obligations (at p. 3 et seq.) and then proceeds to classify contracts into, among others, "consensual" and "real" (at p. 15). Consensual contracts are those that are binding "by the mere consent of the parties such as sales, rental of property, agency, etc.. Real contracts require more than the mere consent, such as does the loan of money..." And, at p. 14, sales are classified as synallagmatic and bilateral contracts: "Contracts that are perfectly bilateral and synallagmatic are those in which the obligation assumed by each party corresponds to an equally principal obligation of the other, such as with sales agreements. ...where the seller's obligation to sell is equal in importance to the buyer's obligation to pay the purchase price. ..." (author's translation). Pothis's influence extended not only to civil law countries but also to England where "his lucidity and mastery of the law" was compared by
to this definition, sales of goods were essentially both consensual and synallagmatic agreements. As such, they transferred title to goods upon payment of an agreed purchase price. My questioner assumed that this definition of a sale agreement had earned its eternal place in history and ruled all contemporary (cash as well as credit) sales of goods. He did not realize that his definition and the syllogistic set of questions it spawned reflected an 18th century cash sale practice and failed to reflect one of the most widespread 20th century sales credit practices.

Contrary to the popular misconception that traces Latin America's legal reasoning to that of the Romans, it was not the pragmatic, problem oriented Romans who influenced Latin America's legal conceptualization. This conceptualization was influenced more by Aristotle and his medieval scholastic disciples. Unfortunately, this method of legal reasoning continues to ignore the role that Aristotle and some of his scholastic disciples themselves ascribed to observation whenever they attempted to distill the essence of discernible reality. Thus, while Latin America's and Mexico's scholastic method of reasoning confers symmetry and certainty upon definitions, classifications and interpretations, these are at the expense of flexibility and fairness. For once legal essences are codified, they remain frozen in time until recodified. Thus, regardless of changing commercial practices, and even of changing terminology, definitions and classifications based upon essences continue to rule from their graves.

An example of the foregoing approach is found in a case before the Supreme Court of Costa Rica. The issue was the liability of a broker for the forgery of bonds purchased from him by a sophisticated client. The client had previously satisfied himself of the bonds' genuineness. This issue was decided by the Costa Rican Supreme Court after establishing the essence of the commercial code contracts of "commission agency" and "brokerage." If the defendant was deemed a "broker" he would not be liable because, essentially, as a broker he was an intermediary. In contrast, if he was deemed a "commission agent" he would be liable because, essentially, as a commission agent he was doing business on his own behalf. It was of no consequence to the Supreme Court of Costa Rica that in the Costa Rican marketplace the terms broker and commission agent were often used interchangeably. It similarly made no difference that the foreign legal experts who testified on the essential meaning of those terms were unaware of the Costa Rican marketplace usage and were not asked to familiarize themselves with local practices. Nor was it deemed important that the defendant (commission agent or broker)
had relied on his client’s assertion that he himself had ascertained the genuineness of the bonds. What mattered was the essential and abstract definition of “commission agency” and “brokerage.”

Using a similar approach, the Mexican Supreme Court decided that the descendants of a joint venturer were not entitled to the royalties produced by their deceased father’s contribution to a joint venture. In doing so, the Mexican Supreme Court was not interested either in the parties’ actual or implied intent or in the significance of the deceased’s contribution to the continuing profits of the surviving joint venturer. The decision was based upon a determination of the “legal nature” of an asociación en participación or joint venture under Mexican law. Since the asociación en participación was classified as a highly personal (intuito personae) type of business association, it ceased to exist upon the death of a joint venturer, regardless of the lasting value of that joint venturer’s contribution and the appropriation of this value by the surviving joint venturer. Once the joint venture terminated, so did the rights to royalties made possible by the efforts of the deceased. One is left to wonder why would an association’s “highly personal” legal nature prevent a fair distribution of earnings made possible by the contributions of the deceased joint venturer? The answer is that legal classifications, (the boxes to which Lic. Gómez-Palacio was referring) often have greater significance in Mexico’s commercial legal reasoning than do the parties’ contractual intent, and commercial usage and custom.

(c.) A key principle of the law of agency and representation. Agency in Mexico, unlike agency in the United States and in other civil law countries such as Germany, is still “causal” in nature. This means that equities or defenses lurking in the relationship between the principal and the agent can be raised by the principal against the innocent third party who dealt with his agent. Thus, the defense of insufficiency of the powers of representation, whether in entering into a sale or commission agency agreement or in representing a principal in a court proceeding, is commonplace in Mexican commercial litigation. It is not unusual for the president of a large company to sign an agreement only to subsequently deny his power to bind his company based upon an insufficient grant of authority in the company’s charter, bylaws or power of attorney. Similarly, it is not unusual for an attorney to claim that opposing counsel also lacks the power to represent his client. Because these defenses are quite common in Mexican and Latin American commercial litigation, the recent Organization of American States’ Convention on The Law Applicable to International Contracts emphasized the need to apply principles and rules on international agency consistent with the needs of

international trade. One such principle requires that an agent clothed with ostensible authority be able to bind his principal regardless of defenses or equities that may arise from the principal-agent relationship.

(d.) Remedies for breach of contract. In common law countries, we take it for granted that the parties to a contract can rescind their agreement by themselves, based upon one party's determination of the other party's breach, actual or anticipatory. This is an important right and remedy in distribution agreements. Unless the franchisor or seller can replace his defaulting distributor quickly and extra-judicially, the damage caused to a product's reputation could be permanent. Although some Mexican courts have begun to move in this direction, the majority of Mexican courts in my experience still treat rescission as a judicial remedy, not one which a private party may initiate and execute. The theory behind the courts' reluctance to allow private parties to rescind contracts is that a rescission managed by the parties transforms the parties into judges of their own performance. This is a function which, allegedly, belongs exclusively to courts of law. As a rule, then, extra-judicial rescission will only be allowed by Mexican courts sparingly and when the distributorship agreements contain highly ritual clauses stating the parties' agreement to permit termination of the contract upon the occurrence of certain specified acts and expressly conveying the right of termination to the aggrieved party. Accordingly, it is much safer in Mexico to rescind judicially than extra-judicially. This remedial constraint makes the rescission of a distributorship agreement in the manner contemplated in the hypothetical problem quite costly.

To summarize, it is important to keep in mind that, in dealing with Mexican commercial law, an American lawyer and businessman will encounter a foreign legal system. The foreignness of this system is a product of different legal and cultural assumptions. Aside from the above described fundamental differences in legal reasoning, Mexico's commercial law, culturally, is still influenced by the values of an agricultural survival society. Such a society regards real property as the most valuable form of property and the real property mortgage as the queen of security devices. Personal or moveable property is still regarded as the lowest in value (res movilis, res vilis). In an agricultural survival society, family and friendship ties often count more heavily than do the "objective" merits of a third party claim. This is so because property that belongs to the family or friends must be protected at the expense of the rights of unknown third parties, such as the bona fide purchasers and creditors.

15. Articles 10 and 15 of the Convention state the following:

(1) Article 10. In addition to the provisions in the foregoing articles, the guidelines, customs and principles of international commercial law as well as commercial usage and practices generally accepted shall apply in order to discharge the requirements of justice and equity in the particular case.

(2) Article 15. The provisions of Article 10 shall be taken into account when deciding whether an agent can obligate its principal or an agency, a company or a juridical person.
Third parties may attempt to purchase friendly treatment by the family by means of bribes, but this method of doing business is costly and uncertain. I am confident that the implementation of NAFTA’s principles of national (and equal) treatment as well as of administrative transparency will, in due course, help to correct these problems. But we must be patient; it will take considerable time and tri-national cooperation before the commercial playing field, including dispute resolution, is sufficiently leveled throughout the NAFTA region.

Gordon: In looking at the provisions dealing with commission agents in Articles 273 to 308 of the Código de Comercio, you see how very different the approach in Mexico is from the relative freedom to modify the relationship by contract in the common law system. I think it is also important to note that when we use the commercial law in Mexico, we are dealing with a single federal commercial law. There are no individual state commercial laws. But, if we have to fall back, it will be to the state civil code. In this case involving a party from Monterrey, the state civil code would be that of Nuevo Leon. The state civil codes tend to follow the federal district civil code. When one presents you with provisions of the “civil code of Mexico” it is usually the federal district civil code.

Gómez-Palacio: There is no “civil code” of the country of Mexico. But note that the Civil Code, so-called, of the Federal District of Mexico, is also applicable in matters of a federal nature. This would include cases involving the Código de Comercio which is federal. It does not necessarily follow that a transaction in Monterrey would be governed by the Nuevo Leon code if the matter were of a commercial nature. The Civil Code of Federal District would supplement matters of a federal nature, including commercial transactions governed by the Código de Comercio.

Gordon: Difficult questions may arise as to whether a conflict is really a question of a commercial nature or a question of a civil contract.

Gómez-Palacio: Can you use all these three contracts at the same time or not? What is the nature of the contrato de mediación - comisión? We really don’t know because we don’t have it defined in the laws. What is the legal nature of the distribution contract? Again, we don’t know. The only one we sort of know for a fact is the comisión, which is a mandate applicable to commercial acts, like a power of attorney for commercial acts. If there is a contrato de comisión, you cannot have an agency and a mediación at the same time. The point is mediation, no representation. Then you can’t have an agency, or commission.

On the use of the word “brokers”, generally speaking we don’t use the word ‘brokers’ or corredores for this kind of relationship except for certain special sales. We have corredores used like notary publics for mercantile acts. They are given public faith in those kinds of relationships. It’s really not a very defined matter but this is not the kind of words

16. See KOZOLCHYK, TOWARD SEAMLESS BORDERS, Chapter 1: The Continuing Commercial Legal Highway.
we use for that area, which is what we're talking here, a really permanent relationship between the principal and agent to sell pesticides.

Kozolchyk: My point was not that you could use a corredores to sell the pesticides, my point was that the terms that are usually used are those which are taken out of the code which may very frequently not really mirror what is happening. I'm convinced that the commission agents that the legislators had in mind when they adopted the statute are not the commission agents that you see today. Who knows what the legal nature is of the contrato de mediación? One must try to define the legal nature of the relationship in terms of pre-existing institutions. The assumption of commercial law is that there is a binding act as long as the merchants do it repeatedly and in a form which is customary. Whereas the assumption of this 19th Century codification is that the act must conform to the terms of a label in order to be valid. If the act does not conform to that label, who knows what you have. It's a totally different approach to the growth of commercial law. This creates an enormous gap between practice and what is in the law.

Gordon: However, we do not have time now to talk about how the conflict is resolved in Mexico.

Gómez-Palacio: Basically there is a commercial transaction if there is a merchant or an act of commerce. There is a list of acts of commerce in Article 1049 and 1050 of the Código de Comercio.

Gordon: One of the possibilities for GROWFAST to do business in Mexico would be to go a step further than establishing one of these contractual relationships by creating a subsidiary in Mexico.

Juan Manuel Trujillo: I have been asked to give a brief overview of the company law in Mexico because the question is whether to incorporate a subsidiary in Mexico. First of all, the main consequence of incorporating a subsidiary in Mexico is creating a new legal entity, which is going to have Mexican nationality under the law of Mexico. One purpose in creating a subsidiary would be to isolate the subsidiary in relation to the parent company in the United States. Other considerations that should be considered are tax issues, operational costs, marketing, market presence in Mexico, and the feasibility of financing in Mexico through means in Mexico.

What is the corporate structure in Mexico? In Mexico the company law is a federal law. Companies are not regulated by states as in the United States. The tax regime is also important. We do not distinguish as in the United States between partnership and corporations in regard to the tax regimes. Generally speaking, all commercial legal entities are taxed at the same rate, 34%.

The process of incorporation also is different from the United States. In Mexico all companies follow almost the same procedure and formalities for incorporation of the company whether it is a corporation or a partnership. We do not recognize the one member company in Mexico. Therefore, we should think about having at least two members. Two members may come from the United States if the foreign investment law allows.
What are the business forms recognized in Mexico? There are six business forms recognized in Mexico: Sociedad Nombre Colectivo, Sociedad en Comandita Simple, Sociedad Coopertiva, Sociedad de Responsabilidad Limitada, sociedad anónima and Sociedad Coopertiva. This last one, the comparative form, is regulated by an independent law which is not part of the company law. The limited partnership and the sociedad de responsabilidad limitada could be compared to what is now emerging in the United States as the limited liability company. Nevertheless, there are many differences. The sociedad anónima is much like the corporation in the United States. Also we recognize what we call the asociación de participation which doesn’t have a legal personality and is not recognized as a business organization itself. It would be roughly comparable to the joint venture of the United States. All of them except for the comparative form may have a fixed or variable capital.

What is the corporate reality in Mexico? In practice, it is rare to find a partnership. The main reason for the preponderance of the sociedad anónima is because it offers limited liability to the members of the company. However, there is no tax advantage with the other forms of business. The concept of public-held corporations is not well developed in Mexico. We have a very small stock market compared to the United States. Furthermore, the corporate form used in Mexico hasn’t changed since 1934 and is responding to the needs of an agriculture-based economy. It is highly formalistic and the process of incorporation takes at least 30 days instead of a phone call as in the United States. Also, you have to call a lot of shareholders meetings and board of directors meetings in order to run the company.

All these formalities bring with them costs and small business companies cannot afford all these costs and formalities. Therefore, they don’t register. This creates a lot of problems involving liability of the members of the unregistered company.

QUESTIONS AND COMMENTS

Gordon: In beginning to do business in Mexico we indicated that GROWFAST went to the commercial officer of the U.S. Embassy, who can be very helpful. Another organization that may be helpful in beginning business and may also be helpful in continuing business by becoming a member is the American Chamber of Commerce in Mexico. John Rogers and Miquel Jáuregui Rogas have agreed to describe the role of the Chamber of Commerce.

John Rogers: The American Chamber of Commerce in Mexico is the largest chamber of commerce in the world, I believe. It has over 2,000 members. Virtually every U.S. company doing business in Mexico is a member. It is an organization that clients of U.S. attorneys may be interested in joining if they begin to do business in Mexico. In addition, for lawyers who are involved in U.S.-Mexico trade, there are two committees of the Chamber which may be of interest. One is the committee on Mexican legislation which Miguel Jáuregui Rojas chairs. The other
is the Committee on U.S. and Cross-Border Legal Matters, which I chair. This used to be called the Committee on U.S. Legislation, but we decided that it didn’t express the focus on cross-border legal matters that the committee has. We have had programs recently on issues like the operation of the NAFTA dispute settlement panels, the World Bank’s legal reform programs, and most recently the NAFTA superhighway. We meet every month on the second Tuesday of the month, at the University Club in Mexico City. If you are in Mexico City at that time, please give me a call. You would be welcome to attend the meetings of the Committee and to become active in the projects of the Committee.

**Miguel Jáuregui Rojas:** Thank you for the opportunity to advertise for the American Chamber of Commerce in Mexico. I am Chair of the Mexican Legislation Committee. The reason it is a useful tool to Chamber members and the business community at large is that we have performed a function which is similar to a lobbying function. I will give you an example. We embarked, together with about four trans-national companies, in doing away with the tax on profits, on dividends. We started this when Mr. Sera was undersecretary of the Treasury Department and we were able to persuade them that Mexico was not competitive when it had an income tax plus a dividend tax of 55% even though dividends were deductible. It was not competitive and it was very cumbersome. We meet on the last Friday of every month. We always meet for one hour; we never exceed the time; and we have very interesting programs. We go from specific legal topics affecting commerce and trade in general to specific speakers on topics that are interesting to us. So if you are in Mexico City on the last Friday of the month, call the American Chamber of Commerce in Mexico or come to the University Club, and we’ll be there.

**Kozolchyk:** The chambers of commerce could be playing an absolutely significant if not the most important role in the process of trying to make the law reflect commercial reality. It is no coincidence that in international sales what is used is the so-called INCOTERMS of the International Chamber of Commerce. In fact, the provisions of Article 2 are totally out of whack with what is done internationally. A shipment versus destination contract is not used in international trade. Regarding choice of law, one of the key provisions of the Convention says that courts in the respective countries have to apply commercial custom as one of the primary sources of law, not a secondary source. The chambers of commerce in Mexico, Canada and the United States could be playing a more important role. At the National Law Center, we have been trying to get them together to avoid the uncertainties in distribution agreements and franchising agreements and so on which we have been discussing.

**Gómez-Palacio:** Note that, although the Código de Comercio establishes freedom of the parties to enter into commercial transactions, the trans-

action may not be recognized by the code. Parties are free to enter into obligations and the validity of commercial acts is not subject to formalities in general. For example, the agency contract is subject to the fact that it must be written, but that’s about it. I want this to be very clear, you are free to enter into whatever, a contract in the United States or abroad that has not been recognized in Mexico and is not in the law, you can apply it for a given transaction. But you probably don’t have a legal nature or a box that is going to be applying certain rules, so you have to go through the general rules of the code.

Kozolchyk: You are free to enter almost any kind of commercial contract but the consequences of what you are doing are judged by existing categories, that’s where the problem lies.

Allan Van Fleet: To what extent can I go part-way down a recognized box, an agency contract, and decide there’s a third of the contents of this box that I don’t like? We want to redefine part of the relationship, yet a good lawyer would say the essence of the contract fits it within a particular box. To what extent are the parties free to augment, modify that relationship under the commercial code?

Gómez-Palacio: Let me try to answer in the clearest possible way. If the essence of a contract is that of the box, all of the rules of that box are going to be applied to your case. That’s it. Except that, of course, you may have rules in that box that allow you to do certain things that the parties are free to negotiate at their will or to waive. It depends on the particular rules. And you can use sometimes two boxes and make a purchase and lease agreement, or a lease-financing with a right to acquire.

Kozolchyk: The best illustration that I have is the following. I was giving a talk a few years ago at the University of Madrid and the talk was on conditional sales. At the end of the talk, a professor of commercial law got up and said to me, "Professor Kozolchyk, isn’t it true that sales are consensual contracts?" I said, "Yes, under 19th century codes they are regarded as consensual contracts meaning there is a binding agreement at the moment there is agreement on the subject matter and price." "Now," he says, "if sales are by nature and by essence consensual, how could conditional sales exist?" I said, "Well, it depends on what you mean by existence. If what you mean by existence is physical existence, I can assure you that as we are talking right now, probably 5,000,000 of them are existing right now in Spain. But if what you mean is do they comport with the legal definition and the essence of a sale agreement in the civil code of Spain, I have to say that they do not exist legally." But that code was written prior to the full development of commercial and consumer credit. Those transactions referred to in the 19th Century Spanish Code were basically face to face, 19th and 18th century transactions. Those sales were consensual by essence. But it is the essence not of our sales or the sales in Mexico but the original sale where title actually passed the moment there was the payment of a purchase price. There was not an executory contract with credit.
Harvey Applebaum: Under NAFTA, the panelists, who are drawn from three separate lists from the three countries, are supposed to review anti-dumping and countervailing duty administrative decisions as the national courts of that country would have done. Tell us a little about how the judicial system in Mexico would operate ordinarily. Do you see any difficulty in Canadian and U.S. panelists coming in and being under an obligation with their common law background to try to apply a judicial review as the Mexican courts would have done?

Kozolchyk: The question you ask couldn’t be more appropriate to what we have been discussing. One of the first panelists was David Ganz of the National Law Center. In the first anti-dumping case on which he was a panelist, what was the central issue? The central issue was the power of attorney. Did the Secretaria de Comercio y Fomento Industrial act with enough powers to do what they were doing? A power of attorney issue. It was not at that point a substantive issue; it was a power of attorney issue. Professor Ganz couldn’t understand why this should be an issue; this is part of that civil law tradition. When you’re dealing with powers of attorney, they have a much greater role to play. This is incidentally one of the reasons why the very first thing that the National Law Center did was try to arrive at six or eight uniform forms for powers of attorney so that people from the United States and Canada could understand the meaning that powers of attorney have under Mexican law.

Gómez-Palacio: With regard to NAFTA panels acting in place of a civil law judge, note that our concept of the function of a judge is very different. The idea that judges make law is quite difficult for us. Even after 20 or 30 years of exposure to the idea, I find it hard to believe. We treat judges like mechanics. In other words, here is the law; here is the case; here is the lever. There’s no big thing about being a judge because you study the legal nature of the problem; the rule is there; you pull down the lever; and here comes the result. That’s justice.

When U.S. lawyers ask has the law been tested? What do you mean? Has it been tested? The law is the law. Take the UCC and there is a transfer of property and you call it a sale even if it is a donation. We don’t; it’s a donation.

Jáuregui: The answer to NAFTA Chapter 19 really is that during the scenario or the venue of an arbitration, I was a proponent of Article 19. Do we not need one? Mexico can accede to Chapter 19-like arbitration and has changed its laws to do so. The reason that we did this is to do away with the formalities that Lic. Gómez-Palacio and Dr. Kozolchyk are talking about. If we don’t do that, we’re not going to modernize the Mexican system. I don’t know if going the Anglo way is making our law more modern or not, but it is making it more practical to deal with our trading partners. And the changes and the venue for arbitration were of the utmost importance to do that. They are working because we don’t want to go back into the mentality of a Mexican judge reading an article and then applying the article or the mentality of a U.S. or Canadian judge that would base himself on other precedents and do
other things that we don’t do, and avoid that kind of issue. I was surprised in my own practice of law how much pretrial discovery we are doing in Mexico now, in the scenario of arbitration. I’m going through two very complicated breakups of joint ventures, and basically what the Mexican lawyers are doing is pretrial work. This is really unprecedented, unheard of five or ten years ago. The manner in which we’re going to communicate among the three nationalities is through arbitration and applying some of our theories with the theories of Anglo-Saxon law which is very expedient and very good. I think that is why it will work. We don’t have any problem with NAFTA that way.

Keith Harvey: I wanted to ask Lic. Trujillo a question. Prof. Gordon asked about the subsidiary question. You said that if a subsidiary is formed it will become a completely new entity, governed by Mexican law. In our hypothetical we are dealing with a multi-national situation. In multi-national litigation there are some theories which are arising with multi-national enterprise liability theory, and also single entity theories. If a multi-national corporation outside of Mexico sets up a corporation in Mexico, a subsidiary, is that multi-national corporation able to do the usual things that multi-national corporations do without jeopardizing the separate status of its Mexican subsidiary and becoming liable for the subsidiary’s transactions in Mexico? Multi-national corporations usually have cash management systems; they take all the money out of the entity every night; they sweep all the accounts and take all the money out; they enter into loan agreements where various parties guarantee each other; they enter into inter-company transactions; and they freely transfer money back and forth and don’t say if it’s a loan or if it’s a capital contribution. Should a foreign multi-national parent operate differently in Mexico on a day-to-day basis?

Trujillo: Unfortunately, it is not clear today under Mexican law whether the multi-national parent will be permitted to conduct its business in the manner to which it is accustomed without risking becoming subject to being treated as if it is doing business in Mexico.