

MEXICO

TRADE SUMMARY

The U.S. goods trade deficit with Mexico was \$50.1 billion in 2005, an increase of \$5.1 billion from \$45.1 billion in 2004. U.S. goods exports in 2005 were \$120.0 billion, up 8.3 percent from the previous year. Corresponding U.S. imports from Mexico were \$170.2 billion, up 9.2 percent. Mexico is currently the 2nd largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Mexico were \$18.0 billion in 2004 (latest data available), and U.S. imports were \$13.5 billion. Sales of services in Mexico by majority U.S.-owned affiliates were \$9.8 billion in 2003 (latest data available), while sales of services in the United States by majority Mexico-owned firms were \$1.3 billion.

The stock of U.S. foreign direct investment (FDI) in Mexico in 2004 was \$66.6 billion, up from \$59.1 billion in 2003. U.S. FDI in Mexico is concentrated largely in the manufacturing, banking, and finance sectors.

Mexico has signed a total of 11 free trade agreements with 43 countries, including the European Union, Chile, the five economies of the Central American Common Market, Israel, and Uruguay. Mexico also implemented an Economic Partnership Agreement with Japan on April 1, 2005.

North American Free Trade Agreement

The North American Free Trade Agreement (NAFTA), signed by the United States, Canada, and Mexico, entered into force on January 1, 1994. This free trade agreement progressively eliminates tariffs and non-tariff barriers to trade in goods; improves access for services trade; establishes rules on investment; strengthens protection of intellectual property rights; and creates an effective dispute settlement mechanism. The NAFTA is accompanied by supplemental agreements that provide for cooperation to enhance and enforce labor standards and to encourage environmentally friendly practices and bolster environmental protection in North America.

IMPORT POLICIES

Tariffs and Market Access

Under the terms of the NAFTA, Mexico eliminated tariffs on all remaining industrial and most agricultural products imported from the United States on January 1, 2003. In October 2005, Mexico announced a tariff-rate quota on U.S. high-fructose corn syrup (HFCS), with a duty-free in-quota rate. Mexico otherwise appears to apply its WTO-bound rate of 156 percent to 210 percent on U.S. exports of HFCS. The safeguard action for U.S. chicken leg quarters expires at the end of 2007 (see section on agriculture, below).

FOREIGN TRADE BARRIERS

Trade growth in agricultural products has been balanced since the NAFTA was implemented, with U.S. exports to Mexico increasing by \$5.7 billion from 1993 to 2005, and U.S. imports from Mexico increasing by \$5.6 billion. The numbers are less balanced, however, when considering nonagricultural trade. U.S. non-agricultural imports from Mexico grew \$125 billion compared with U.S. export growth of \$73 billion from 1993 to 2005.

A number of U.S. exports, both agricultural and non-agricultural, are subject to antidumping duties that limit access to the Mexican market. Products subject to these duties currently include beef, rice, epoxidized soy oil, apples, liquid caustic soda, ammonium sulfate, polyvinyl chloride, bond paper, industrial fatty acids, stearic acid, ethylene glycol monobutyl ether, and welded carbon steel pipe and tube. In 2005, Mexico terminated the antidumping investigations of crystal polystyrene and newsprint, and the self-initiated investigation of pork legs (hams), without imposing duties.

Agricultural Products

The United States exported \$9.3 billion in agricultural products to Mexico in 2005, setting a new record. Mexico became the United States' second largest agricultural market in 2004. Under NAFTA, Mexico has eliminated nearly all import tariffs and tariff-rate quotas on agricultural products from the United States. As of January 1, 2005, the only U.S. agricultural exports subject to tariffs or tariff-rate quotas are corn, sugar, dry beans, orange juice, chicken leg quarters, high-fructose corn syrup, and milk powder.

During the past year, Mexico's Secretariat of Economy (SECON) continued antidumping duties on beef, rice, and apples, and initiated a sunset review of existing duties on beef. In 2004, SECON terminated its antidumping investigation of U.S. pork, finding no cause for continuing the investigation. SECON subsequently self-initiated an antidumping investigation of U.S. pork legs (hams), and on December 21, 2005, Mexico announced it was terminating the investigation without imposing measures. Concerns about Mexico's methodology for determining injury to the Mexican domestic industry and for calculating dumping margins in the rice case led the United States to challenge the antidumping measure at the WTO. In June 2005, the WTO panel found in favor of the U.S. position. Mexico appealed the decision and the WTO Appellate Body subsequently agreed with nearly all of the panel's findings. SECON modified the beef dumping duties in 2004 in response to the findings of a NAFTA Chapter 19 panel, which determined that SECON did not sufficiently demonstrate that U.S. beef imports had damaged Mexico's beef industry. The panel's decision on remand, in which it must either uphold SECON's remand determination or issue additional remand instructions to SECON, is still pending. Mexican policies in this area have reduced the number of U.S. suppliers and altered product trading patterns. Industry representatives assert that \$100 to \$500 million in revenue is lost each year due to antidumping duties in the beef sector.

On December 29, 2004, SECON suspended the application of the 46.58 percent antidumping duty on U.S. red and golden delicious apples exported by members of the Northwest Fruit Exporters (NFE) and established a reference price system for NFE members. In February 2005, a Mexican court nullified the reference price system and on May 26, 2005, in response to an order from a Mexican court, SECON announced the elimination the 46.58 percent antidumping

FOREIGN TRADE BARRIERS

duty for NFE members and the beginning of a new antidumping investigation on U.S. red and golden delicious apples for those members. On September 29, 2005, SECON announced the preliminary results of its investigation and imposed a preliminary antidumping duty of 44.67 percent on red and golden delicious varieties for all but three members of the NFE, who received lower or no duties. The original antidumping duty of 46.58 percent still applies to red and golden delicious apples by exporters who are not members of the NFE. When it announced the preliminary results of its investigation, SECON requested additional information from NFE exporters as well as exporters who had not yet participated in the investigation but wished to do so. That information was due in November 2005.

In July 2003, Mexico imposed a NAFTA safeguard on U.S. chicken leg quarters that will remain in effect until December 31, 2007. The safeguard takes the form of a tariff-rate quota (TRQ) on chicken leg quarters. The TRQ preserves market access for U.S. exporters at levels achieved in recent years. Pursuant to the NAFTA, Mexico agreed to provide compensation to the United States, including a commitment not to impose any additional import restrictions on U.S. poultry products and to eliminate certain sanitary restrictions on U.S. poultry products. U.S. poultry product exports were up 74.7 percent from October 2003 to October 2005.

On December 31, 2001, the Mexican Congress approved a 20 percent tax on certain beverages made with sweeteners other than cane sugar, including HFCS. HFCS sales fell dramatically below prior volumes, as bottling companies in Mexico switched to cane sugar to avoid the paying the tax. Industry estimates that the annual cost of this trade barrier to the United States is roughly \$944 million in U.S. HFCS sales losses and sizeable investment losses. Industry analyst's estimate that full restoration of the Mexican market for HFCS sales would increase the price per bushel for corn \$0.06 nationally, or \$0.10 in key corn states. Although temporarily suspended by the Fox Administration, the Mexican Supreme Court ruled this action unconstitutional and reinstated the tax on July 12, 2002. The tax has been renewed each year by the Mexican Congress, including for 2006. On March 16, 2004, the United States requested consultations under the dispute settlement procedures of the WTO, and on July 6, 2004, a WTO panel was established to review the dispute. The panel announced its findings on October 7, 2005, which supported the U.S. position that the tax is inconsistent with Mexico's WTO obligations. Mexico appealed the panel's report to the WTO Appellate Body on December 6, 2005. The Appellate Body circulated its report upholding the panel's finding on March 6, 2006.

On September 30, 2005, SECON established a tariff-rate quota of 250,000 metric tons for imports of U.S. HFCS, which will be in place until September 30, 2006. Imports will be managed through a permit system, but will not be exempt from the 20 percent domestic tax applied to certain beverages. Several HFCS consuming firms in Mexico have obtained injunctive relief (amparos) exempting them from the tax. The TRQ action mirrored a U.S. decision to establish under NAFTA a FY 2006 duty free tariff-rate quota for imports of 250,000 metric tons of Mexican sugar.

On August 18, 2005, Mexico placed additional duties on imports of several products from the United States. Tariffs ranging from nine to 30 percent were imposed on chewing gum, other confectionaries, certain fortified milk products, and certain wines. Mexico took this action after the United States failed to comply with a WTO recommendation that the Continued Dumping

FOREIGN TRADE BARRIERS

and Subsidy Offset Act (CDSOA), known as the “Byrd Amendment”) be brought into conformity with U.S. WTO obligations. The U.S. Congress repealed the CDSOA in December 2005.

Sanitary and Phytosanitary Issues

In recent years, Mexican sanitary and phytosanitary standards have created barriers to exports of certain U.S. agricultural goods, including grains, seed products, apples, stone fruit, pork, beef, poultry, citrus, wood and wood products, dry beans, avocados, potatoes, and eggs. In addition, procedural requirements regarding sanitary and phytosanitary inspections at port of entry do not always reflect agreements reached between U.S. Department of Agriculture officials and the Mexican Secretariat of Agriculture, resulting in unnecessary delays at border points of entry, seaports, and airports. While the situation improved during 2005, significant quantities of imports were still rejected or delayed at the border.

Mexico banned imports of U.S. beef in December 2003, following the detection of a positive case of Bovine Spongiform Encephalopathy (BSE) in the State of Washington. In March 2004, Mexico announced that it would accept U.S. boneless beef from cattle less than 30 months of age, and it subsequently lifted restrictions on a number of offals and processed boneless beef products. Currently, bans or restrictions remain on bone-in beef, live cattle, certain offals and pet food. The United States is working intensively to fully re-open the market as quickly as possible.

The application of a zero tolerance for the presence of small amounts of bone in boneless beef led to the rejection of numerous U.S. beef shipments and the prohibition of exports from certain U.S. beef plants during 2005. An agreement to apply existing tolerances for bone as established in Mexican regulations has since greatly reduced the number of rejections.

In September 2005, Mexico’s Secretariat of Health implemented a rule regulating the meat sector that established a tolerance of zero for the presence of salmonella in raw meat. This scientifically unjustifiable standard could lead to unnecessary product recalls and export restrictions for U.S. meat exporters.

Despite the lack of a protocol for returning live animals and adequate inspection facilities in Mexico, in June 2004, the Mexican Congress approved a measure requiring that the inspection of imported live animals take place in Mexico. The lack of adequate inspection facilities has hampered the importation of live animals. While Mexico’s Congress appears to agree that the law should be changed, the provision remains in place pending agreement upon other modifications to the Animal Health Law.

In October 2005, Mexico lifted its Low Pathogenic Avian Influenza restrictions on poultry imports from nine U.S. states, but restrictions on 11 counties in Texas remain in place following a 2004 detection of High Pathogenic Avian Influenza.

Administrative Procedures and Customs Practices

U.S. exporters continue to be concerned about Mexican customs administrative procedures, including insufficient prior notification of procedural changes; inconsistent interpretation of regulatory requirements at different border posts; and uneven enforcement of Mexican standards and labeling rules. There have been relatively few specific complaints, however, and Mexican customs has been putting procedures in place to address issues of non-uniformity at border ports of entry. Agricultural exporters note that Mexican inspection and clearance procedures for some agricultural goods are long, burdensome, non-transparent, and unreliable. Customs procedures for express packages continue to be burdensome, although Mexico has raised the *de minimis* level from \$1 to \$50. However, Mexican regulations still hold the courier 100 percent liable for the contents of shipments.

To be eligible to import well over 400 different items, including agricultural products, textiles, chemicals, electronics and auto parts, Mexican importers must apply to the Secretariat of Finance and Public Credit (SHCP) and be listed on a special industry sector registry. U.S. exporters complain that the registry requirement sometimes causes costly customs clearance delays when new products are added to the list of subject items with immediate effect, thereby denying importers sufficient notice to apply. They also report that certain importers have been summarily dropped from the registry without prior notice or subsequent explanation, effectively preventing U.S. exporters from shipping goods to Mexico.

Mexico requires import licenses for a number of commercially sensitive products. It also uses estimated prices for customs valuation of a wide range of products imported from the United States and other countries, including apples, milled rice, beer, distilled spirits, chemicals, wood, paper and paperboard products, textiles, apparel, toys, tools, and appliances.

Since October 2000, the Mexican government has imposed a burdensome guarantee system for goods subject to estimated prices. Importers cannot post bonds to guarantee the difference in duties and taxes if the declared value of an entering good is less than the official estimated price. Instead they must deposit the difference in cash at a designated Mexican financial institution or arrange one of two alternative sureties (a trust or line of credit). The cash deposit is not returned for three months and then only if the Mexican government has not initiated an investigation and if the supplier in the country of exportation has provided an invoice certified by its local chamber of commerce. Mexican banks charge as much as \$500 to open an account for this purpose and \$50 for each transaction, making this a burdensome and costly regulation for businesses on both sides of the border. The governments of the United States and Mexico are discussing an exchange of customs data that would result in the elimination of the estimated pricing regime.

In addition, U.S. exporters have expressed concerns regarding post-importation verification practices implemented by Mexican Customs and administered by private entities. Mexico has indicated that all information will remain confidential and that verifications are intended to validate the accuracy of all information presented to Mexican Customs. However, U.S. firms remain apprehensive about sharing business confidential information with a third-party. The U.S. government continues to monitor the situation.

U.S. firms also have raised concerns with a Mexican regulation (Annex 18) that requires additional documentation for imports of certain textile products. In particular, the regulation asks for detailed specification information, which certain exporters claim is proprietary and results in increased paperwork for the importer. Although the U.S. Government has confirmed with Mexican customs officials that the additional information is necessary for Mexican customs enforcement efforts, we continue to explore less burdensome alternatives.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Under NAFTA, Mexico was required, starting January 1, 1998, to recognize conformity assessment bodies in the United States and Canada on terms no less favorable than those applied in Mexico. The United States is still awaiting action on a 2003 request by a U.S. certification body to be recognized in Mexico. On January 21, 2005, Mexico published the *convocatoria* (formal announcement, or “call”) in the *Diario Oficial* stating that one or more government agencies are requesting certification organizations for the standards involved. While the publication of the *convocatoria* has been considered a positive step, Mexican interests in the conformity assessment sector have vehemently resisted entry by non-Mexican entities, both before and after the publication of the *convocatoria*. To date, no U.S. certification bodies have been recognized by Mexico. In the telecommunications sector, Mexico has agreed to implement a Mutual Recognition Agreement to accept the results of testing to Mexican telecommunications regulatory requirements, by June 2006. If implemented, this will allow U.S. accreditors to accredit U.S. labs to test to Mexico’s requirements.

U.S. exporters have alleged that certain regulations are enforced more strictly for imports than for domestically-produced products, and that there has been inconsistent treatment for the same goods at various ports of entry. Mexico has over 700 technical regulations called “Normas Oficiales Mexicanas” (NOMs) issued by a number of different agencies, each with its own conformity assessment procedures. Only the Secretariat of Economy, the Secretariat of Agriculture (for a limited sub-set of its NOMs), the Secretariat of Communications and Transport (for one of its NOMs), and the Secretariat of Environment and Natural Resources have published some conformity assessment procedures. Key Mexican ministries such as Health, Energy and Labor have yet to publish their respective procedures.

The United States is Mexico’s largest export market for tequila, accounting for 50 percent of Mexican production. In 2003, the United States imported over \$402 million of tequila. Approximately 77 percent of the total volume was tequila in bulk form. In August 2003, the Mexican government, citing the need to ensure the quality of Mexican tequila, considered amending the official standard for tequila to require that tequila be “bottled at the source” in Mexico. The existing Mexican standard had required that only 100 percent agave tequila be bottled at the source. (Tequila made from less than 100 agave tequila could be sold and exported in bulk form under the prior official standard.) On January 6, 2006, Mexico published a final revised tequila standard that establishes new requirements for bulk exports. This does not include a requirement that all tequila be bottled in Mexico, but does contain onerous administration and inspection requirements for all bottlers. On January 17, 2006, the United States and Mexico signed an agreement which will ensure that Mexican exports of bulk tequila to the United States continue without interruption. Mexico will be prohibited from regulating the

FOREIGN TRADE BARRIERS

marketing of tequila in the United States as well as the labeling, formulation, and marketing of distilled spirits specialty products (i.e., products that contain tequila, such as tequila-based liqueurs) outside of Mexico.

Mexico standards for all distilled spirits continue to include “analytical parameters” not based on science that could bar U.S. distilled spirits exports. Similarly, Mexico's alcohol content levels are inconsistent with international standards.

U.S. exporters of vitamins, nutritional supplements, and herbal remedies have reported that Mexico’s health law regulations are discriminatory and arbitrarily impede access to the Mexican market. While Mexico has stated that it is looking at ways to address these concerns, the U.S. Government has thus far seen no progress. According to industry’s estimates, the cost of this alleged trade barrier to the United States is over \$500 million annually.

GOVERNMENT PROCUREMENT

Mexico’s efforts to make its government procurement regime more transparent through policies and technologies have resulted in increased competition as well as savings for the government. The Mexican government has established several “e-government” Internet sites to increase transparency of government processes and establish guidelines for the conduct of government officials. “Compranet” allows on-line processing of government procurement and contracting. Implementation, while successful, still needs further regulatory and technological advances throughout the Mexican government.

The NAFTA Government Procurement Chapter allowed Mexico to cover only a temporary narrow list of services, based on the requirement that it would develop a permanent list of excluded services by July 1, 1995. After several years of discussion, the United States, Mexico, and Canada reached agreement in 2004 on a list of excluded services. The agreement means that Mexico will allow suppliers from its NAFTA partners to participate in the procurement of all of its services (by the entities covered under NAFTA and above specified contract values), except for the services that it expressly excludes. This means increased access for U.S. suppliers to Mexico’s purchases of services. The expanded access became effective in June 2005 when Mexico published its list of excluded services.

As of January 1, 2003, NAFTA limits the total value of contracts that Mexico’s parastatal petroleum and electricity monopolies, PEMEX and the Federal Electricity Commission (CFE), respectively, may remove from coverage under NAFTA to \$352 million per year. The United States has not been able to confirm whether this commitment has been properly implemented, as Mexico has not provided the statistics called for under NAFTA. Mexico has indicated it will send to the United States and Canada notice of the set-aside calculation, along with the methodology used in the calculation.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Under NAFTA and the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), Mexico is obligated to implement certain standards for the protection of intellectual property and procedures to address infringement, including copyright piracy and trademark counterfeiting. Despite a fairly comprehensive set of IPR laws and an increase in the number of seizures and arrests during 2004 and 2005, the extent of IPR violations in Mexico remains dramatic. Monetary sanctions and other penalties, when imposed, are minimal and largely targeted at the bottom-tier of the piracy chain, i.e. the small scale sellers of pirated materials, who are numerous and easily replaced. A concerted effort to target the highest levels of organized crime, which is increasingly behind piracy in Mexico, is necessary to make a real impact and deter piracy. The United States remains concerned about the continuing high levels of piracy and counterfeiting in Mexico and closely monitors how the Mexican government is addressing these problems. Mexico was taken off the Special 301 “Watch List” in 2000, but returned to the list in 2003 and remained on the “Watch List” in 2004 due to enforcement deficiencies.

Copyright Protection

Copyright piracy remains a major problem in Mexico, with U.S. industry loss estimates growing each year. Although enforcement efforts by the Mexican government seem to be improving, piracy levels continue to rise, resulting in closures of legitimate copyright-related businesses, according to industry sources. Pirated and counterfeit sound and motion picture recordings are widely available throughout Mexico, where piracy has shifted from traditional formats to optical discs (CD, DVD, CD-ROM). The International Intellectual Property Alliance (IIPA) estimates that trade losses due to copyright piracy in Mexico totaled \$1,253.4 million in 2005. That year, music piracy represented 65 percent of the total market; business software piracy, 64 percent; motion picture piracy, 62 percent; and entertainment software piracy, 75 percent. In July 2003, the Mexican Congress amended the Mexican copyright law, and finally in September 2005 published the law, thereby bringing it into effect. Industry associations and Indautor, the Mexican government agency that regulates copyrights, claim the new legislation brings Mexico in compliance with its obligations under the NAFTA IPR Chapter and the WTO TRIPS Agreement.

Mexican law enforcement agencies have conducted thousands of piracy raids and the U.S. copyright industries report good cooperation with the police in various jurisdictions around Mexico. In 2003, the Attorney General's Office created an IPR enforcement unit, which combines federal prosecutors and police to make the enforcement regime more effective and efficient. In 2004, the Attorney General's Office authorized its Organized Crime Division to investigate piracy. Very few IPR violations result in prison terms. As a result, pirates and counterfeiters are often released and return to their illegal activities. Well-known markets selling pirated and counterfeit goods, such as Tepito in Mexico City, remain ubiquitous.

FOREIGN TRADE BARRIERS

Patent, Trademark, Pharmaceutical and Agricultural Chemical Protection

Patents and trademarks are under the jurisdiction of the Mexican Institute of Industrial Property (IMPI), an independent agency that operates under the auspices of the Secretariat of the Economy.

U.S. pharmaceutical and agricultural/chemical companies are concerned about the lack of coordination between IMPI and other Mexican agencies with regard to government procurement of copies of patented pharmaceuticals. In 2003, the Mexican Ministry of Health agreed that starting with purchases scheduled for delivery on January 1, 2003, IMSS (Mexican Social Security Institute) and possibly ISSSTE (Social Security Institute for Government Workers) would purchase only legitimate versions of products patented in Mexico. Unfortunately, it appears this agreement is not being fully implemented due to alleged financial shortcomings at the agencies.

In September 2003, the Ministries of Health and Economy implemented a Presidential decree that requires applicants for safety and health registrations to show proof of patent and proof that test data was obtained in a legitimate matter. According to the regulation, failure to present proof of patent and test data will result in denial of the registration. Also, if a company is caught providing false information, it can now be subject to both civil and criminal proceedings. While this measure is a positive development, the regulation limits linkage to product patents only, excluding process patents. Moreover, U.S. industry reports that enforcement of the regulation is weak, as the Ministry of Health (MOH) continues to provide local companies authorization to market unauthorized copies of patented pharmaceutical products. It is hoped that compliance with this decree will help to eliminate copies of patented pharmaceuticals from the supply chain for IMSS and ISSSTE.

U.S. companies holding trademarks in Mexico have cited problems with trademark enforcement and administration. When counterfeit items are discovered, injunctions against trademark violators are often unenforceable and are consistently challenged before the courts. Although federal administrative actions are supposed to be completed within four months, actions related to trademark enforcement often take as long as 18 months. The time can be lengthened by jurisdictional and procedural disputes within the Mexican government, as well as by internal coordination problems within IMPI and between IMPI and the Attorney General's office. Trademark applications in Mexico are not subject to opposition.

Registrations are issued and can only be canceled after registration. On average, it takes two and a half years to cancel a trademark registration, and the registrant is allowed to continue using the mark for one year following cancellation.

Border Enforcement of IPR

NAFTA Article 1718 and Article 51 of the TRIPS Agreement obligate Mexico to allow U.S. intellectual property rights holders to apply to Mexican authorities for suspension of release of counterfeit trademark or pirated copyright goods. Intellectual property rights owners seeking to use the procedure must obtain an order from IMPI that directs customs officials to detain the

FOREIGN TRADE BARRIERS

merchandise. Companies requesting such actions generally report positive outcomes. However, U.S. industry has sought increased cooperation and communication between IMPI and Mexican customs in order to prevent the release of counterfeit goods into the Mexican market.

SERVICES BARRIERS

Telecommunications

The 2004-2005 Global Information Technology Report's Networked Readiness Index (NRI) of 104 nations's ranked Mexico number 60, down from 44, on a scale measuring the degree of Information and Communication Technology development. The outcome of this year's report reflects Mexico's struggle with constructing regulations to promote interconnection and technology convergence and improve competitiveness.

Among Mexico's greatest challenges, is promoting telecommunications competitiveness. Telmex continues to dominate the market and retain influence over the Secretariat of Communications and Transport (SCT) and the Federal Communications Committee (COFETEL). Both agencies have failed to adequately resolve disputes and act upon competitors' claims of market discrimination. The few times the government has attempted to take action to improve competitiveness, Telmex has successfully blocked enforcement by using court-ordered injunctions and other legal maneuvers.

This behavior is exemplified by the current debate over so-called Triple-Play services (voice, data, and video). Previously, Cable TV operators were given the legal capacity to offer telephony services through their networks only if they partnered with a licensed telecom carrier. This requirement limited the spread of VoIP services by restricting Cable TV operators. Due to the intervention of the Federal Competition Commission (COFECO), however, the ruling was recently over-turned and the partnering requirement abolished, enabling Cable TV operators to offer triple-play services. The ability of cable companies to provide triple-play services is expected to trigger regional consolidation among the approximately 200 cable companies as they attempt to successfully compete with Telmex. Industry sources suggest that COFETEL is considering granting Telmex the immediate ability to provide video or broadcasting services to placate Telmex for the perceived loss of market share. COFECO, among other agencies, has suggested that Telmex not be given the ability to provide the services for at least two years. However, Telmex has insisted that it will release video phone services in the near future and is prepared to legally fight such a ruling.

COFETEL and SCT have been hesitant to increase foreign direct investment in the sector. In accordance with the WTO dispute, Mexico – Measures Affecting Telecommunications Services, in August 2004, Mexico removed the provisions of Mexican law that created a uniform tariff and proportional return system for international traffic and the requirement that the carrier with the greatest proportion of outgoing traffic to a country negotiate the settlement rate on behalf of all Mexican carriers. In August 2005, COFETEL published a new set of regulations for resale-based telecommunications services in Mexico. Such services would be open to one-hundred percent foreign owned companies. However, these regulations and the resale rules constructed

FOREIGN TRADE BARRIERS

by SCT continue to prevent foreign carriers from using leased lines to bring calls directly into the domestic network.

A troubling development is COFETEL and SCT's desire to implement a long distance "calling party pays" system for wireless services that will shift all interconnection charges to the company (and ultimately customer) where the calls originate. If implemented, interconnection rates and tariffs could cost U.S. industry and consumers hundreds of millions of dollars annually, depending on the rate set. Acting on the advice of COFECO and Mexico's Federal Regulatory Commission (COFEMER), COFETEL and SCT have refrained from publishing their calling party pays regulations until they are able to provide a more favorable playing field for interconnecting companies and consumers. COFETEL has also pledged to ensure that any new rate imposed for terminating calls on wireless networks would be cost-oriented, consistent with Mexico's WTO obligations.

Many telecom experts believe that granting COFETEL further authority and independence would improve the Mexican government's ability to promote the convergence and interconnection of technology systems while avoiding conflicts of interest with SCT and Telmex. However, recent legislative efforts to increase COFETEL's transparency and allot it the power to apply sanctions, establish official standards, adopt OECD quality standards, and increase transparency in the contract/concessions process have not passed. The SCT, which has been criticized as unduly partial to Telmex's interests, continues to have the last word on regulatory decisions and enforcement. Legislation to strengthen COFETEL and grant it independence from SCT remains key to improving Mexico's competitiveness in the telecommunications sector.

INVESTMENT BARRIERS

Ownership Reservations

Mexico's oil and gas policy is highly restrictive when it comes to private equity investment. The sector remains closed to foreign investment other than in the Liquefied Natural Gas (LNG) sector and in the marketing of petroleum products. Only Mexican nationals may own gas stations.

The Mexican constitution mandates state ownership of hydrocarbons and provides that no concessions or other types of production-sharing agreements or risk contracts shall be granted in regard to hydrocarbon exploitation.

Mexico was able to meet its energy needs for many years under this restriction. Recently, the Mexican government has explored ways of allowing additional foreign investment in the energy sector consistent with its constitution, hoping to attract capital that will strengthen the highly leveraged national oil company, Pemex. So far the reform efforts have had little success.

Other laws limit certain sectors or activities (e.g., forestry exploitation) to Mexican nationals. Investment restrictions prohibit foreign ownership of residential real property within 50 kilometers of the nation's coasts and 100 kilometers of its land borders. However, foreigners may acquire the effective use of residential property in the restricted zones through trusts administered by Mexican banks. A national foreign investment commission reviews foreign

FOREIGN TRADE BARRIERS

investment in Mexico's restricted sectors, as well as investments in non-restricted sectors that exceed a 49 percent share of an investment with a value greater than \$150 million (as adjusted each year for growth in Mexico's nominal GDP). These restrictions are incorporated into the NAFTA.