

Mexican Reform Bill Threatens Private Sector Investments

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On March 24, President Andres Manuel Lopez Obrador presented an extensive reform bill to the Mexican Chamber of Deputies, targeting 23 laws, which could considerably affect the private sector.

Businesses and investors in Mexico — particularly in the mining, energy, rail and construction industries — are likely to experience the most significant impact.

In this article, we aim to provide you with a comprehensive explanation of the potential repercussions of this bill and its implications for your business interests.

What's Being Proposed

The reform bill has three main sections:

- Rectification of Corruption Acts;
- Protection of Public Finances and Deterrence of Actions Detrimental to the Public Interest; and
- Reinforcement of the Federal Public Administration.

Rectification of Corruption Acts

Based on the premise of challenging corruption acts, the reform bill proposes changes to existing laws in order to establish a "more precise and comprehensive" definition of "juicio de lesividad." The executive branch would have broader authority to initiate actions to nullify or amend administrative acts it considers to be contrary to the public interest or harmful to the financial interests of the state.

These adjustments also seek to amend the nullity trial, or "juicio de nulidao," for addressing administrative acts that fail to satisfy legal prerequisites. Administrative acts that do not adhere to the validity criteria set forth in paragraphs one to 10 of Article 3 of the Federal Law of Administrative Procedure could no longer be cured as previously allowed.



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Additionally, declarations and registrations containing regulatory irregularities made by individuals will become the responsibility of those individuals.

Protection of Public Finances and Deterrence of Actions Detrimental to the Public Interest

This section introduces measures to:

1. Revoke Administrative Acts Influenced by Subsequent Events That Compromise Public, General or Social Interest

This would signify a substantial shift in the legal framework governing administrative acts, as it would allow the revocation of concessions or permits based on events that transpire after they are issued. Businesses operating in Mexico would face a new level of uncertainty concerning the stability and certainty of their concessions and permits.

The proposal broadens the basis upon which the federal government can revoke administrative acts, extending it to instances where subsequent events — including changes in public policy, social or economic circumstances, or other factors affecting public, general or social interest — warrant revocation.

This increased discretion afforded to the government raises concerns about the potential for arbitrary decisions and the overall predictability of the legal environment for businesses in Mexico.

These changes could have significant consequences for industries such as mining, energy, rail and construction, which rely heavily on concessions and permits for their operations.

For example, domestic and foreign businesses and investors may be reluctant to invest in projects without assurance that their concessions or permits will remain valid or unchanged over the long term.

Furthermore, disputes may increase between the private sector and the Mexican government. Affected parties may challenge the legality and constitutionality of these revocations and foreign investors may bring arbitration claims under investment protection treaties, putting further strain on the judicial system and potentially damaging Mexico's reputation as a stable and attractive investment destination.

2. Mandatory Inclusion of Exorbitant Clauses in Acquisition and Public Works Contracts

Exorbitant clauses grant public administration unique powers, which are absent in private contracts, enabling the government to unilaterally terminate a contract without the contractor's consent.

The proposed bill requires the inclusion of these provisions in all procurement and public works contracts, thereby authorizing the state to prematurely terminate contracts for reasons pertaining to public interest, potentially without providing adequate compensation.

Furthermore, the bill proposes penalizing public officials who neglect to incorporate these clauses in these agreements.

3. State Compensation

The bill stipulates that the government will not be obligated to pay compensation when (1) individuals

fail to fulfill their obligations under administrative acts, (2) the revocation or early termination is based on public, general or social interests or the integrity of national persons or institutions, and (3) the individual's investment has been recovered.

Additionally, the proposed changes would remove the second paragraph of Article 21 of the Expropriations Law that asserted that the application of laws regarding state compensation would occur without prejudice to the provisions of international treaties to which Mexico is a party and of the effect of arbitration agreements.

While the bill attempts to subject compensation obtained in arbitration proceedings to the Federal Government Liability Law and the Expropriation Law, it is unlikely that the derogation of this provision succeeds in avoiding Mexico's liability, as will be explained below.

4. International Public Biddings

The bill would permit the state to acquire goods through international public bidding without first exhausting national public bidding under specific conditions.

5. Employment of Former Public Servants by Private Parties

The bill proposes that public servants, upon leaving their positions, may not work for or provide services to private parties they previously supervised or regulated or with whom they entered into contracts or administrative acts until a specified period of time has passed. This waiting period is determined by the position held while in public service.

According to this proposal, private parties would be liable for hiring former public servants in violation of these stipulations.

Reinforcement of the Federal Public Administration

This section of the bill strives to streamline the consolidation of public entities, reabsorb their assets into federal agencies and expedite the execution of public works and services.

Notable proposals in this section include:

1. Public Entities Sectorization

The bill suggests broadening the opportunities for consolidating public entities based on public, general or social interests, national security and economic activities.

2. Integration and Reintegration

Suggested amendments to Article 16 of the Federal Law of Public Entities would permit the Ministry of Finance and Public Credit to propose the transfer of personnel and resources to federal agencies with the aim of enhancing their effectiveness and efficiency.

3. Allocation

The bill seeks to modify several laws to grant indefinite allocations for the provision of public services to

public entities.

4. Recovery of Real Estate Through Administrative Means

The proposed bill includes changes to the National Property Law that would establish a streamlined procedure for the administrative recovery of assets within the federation's public domain regime.

This new process could potentially compromise the rights of businesses and private property owners in Mexico, as it aims to expedite the government's ability to reclaim real estate and other assets it deems necessary for public, general or social interests, national security or the protection of fundamental human rights.

Under the proposed amendments, the government would be granted broader authority to recover real estate assets more rapidly and with fewer procedural obstacles. This expedited process could adversely affect businesses and private property owners in Mexico, as the government would have a more efficient mechanism for expropriating assets it considers necessary for public use or in the public interest.

While the government may argue that the intent behind this proposal is to enable the effective use of public assets and foster public welfare, the proposal raises concerns about the protection of private property rights.

The streamlined process might not offer ample opportunities for affected parties to challenge the government's actions or seek appropriate compensation for the loss of their assets, potentially undermining the legal safeguards for businesses and property owners in Mexico. This again may provide grounds for foreign investors to bring arbitration against Mexico under applicable investment protection treaties.

5. Administrative Trust

The bill proposes incorporating the principle of trust in the public sector for executing works and services, asserting that the government should not be subject to the same formalities as private parties.

To this end, the bill proposes amending Article 19 of the Public Works and Related Services Law to allow for public infrastructure projects to begin before the completion of required procedures and permits when circumstances are extremely urgent or involve the country's economic development, defense of sovereignty or national security.

6. Advance Payments

The bill recommends broadening the possibility of granting higher advance payments for acquisitions of specific types of equipment, such as medical and security equipment, as well as machinery for infrastructure development and maintenance. This measure aims to expedite these acquisitions in exceptional cases provided they are justified by immediate delivery or lower prices.

The bill would also include differentiated treatment for micro, small and medium-sized national enterprises, increasing the advance payment range from 10% to 15%.

What Might Happen Next

To pass, the bill only requires a simple majority in the Chamber of Deputies and the Senate, as it involves modifications to 23 laws and not the federal constitution. The Morena political party and its allies currently hold a sufficient majority to approve this potentially problematic bill. However, if enacted, it is likely to face multiple constitutional challenges.

In addition, the implementation of the provisions in this bill, if passed, may lead to claims against Mexico under investment protection treaties that safeguard foreign investors and their investments.

These treaties afford various protections against actions of the host state, including one that provides that expropriation must not only serve a public purpose or interest and be carried out in a nondiscriminatory manner but also adhere to due process and be accompanied by prompt, adequate and effective compensation.

Several provisions in the bill designed to facilitate and expedite expropriation proceedings, as well as reduce or even eliminate compensation in certain cases, appear to contradict these investment protection treaties and international law.

Consequently, Mexico's application of these provisions may entitle foreign investors to initiate arbitration against the country under the relevant bilateral investment treaties.

Even U.S. investors, who under the new United States-Mexico-Canada Agreement that replaced the North American Free Trade Agreement have more limited protections than other investors, might also resort to arbitration under certain conditions. This is because expropriation is one of the few standards that, if breached, still allows U.S. investors to initiate arbitration against Mexico under the USMCA.

U.S. investors may also resort to arbitration when their investment is structured through a government contract in sectors such as oil and gas, power generation, telecommunications, transportation services and ownership or management of roads, railways, bridges or canal.

On the other hand, the bill's attempt to subject compensation obtained in international proceedings or in arbitration to domestic law by removing a paragraph from the Expropriation Law is unlikely to be effective. Mexico's international commitments are recognized at a constitutional level, and the derogation of such paragraph does not have any impact on these commitments nor on Mexico's existing agreements to arbitrate.

Additionally, the removal of such paragraph is completely irrelevant at an international law level and any investor will be entitled to effectively pursue remedies under international law and enforce arbitration agreements.

If anything, the derogation of this paragraph may bring uncertainty in respect of arbitrations sitting in Mexico, reviving the ghost of the infamous *Commisa v. Pemex* case and discouraging foreign investors from accepting Mexico as a seat of arbitration in the future.

What Businesses and Investors Should Do Now

Since this reform bill would change Mexico's legal landscape and could increase litigation and arbitration proceedings, it's crucial that businesses, foreign and domestic investors and private property owners in

Mexico stay informed about the bill's progress and engage with industry associations to discuss the potential implications of its provisions on their operations.

Building a robust compliance program and maintaining a thorough understanding of the evolving legal environment can help businesses mitigate risks and adapt to any potential changes in the regulatory framework.

Investors should also analyze whether they are sufficiently protected under international treaties and consider modifying the structure of their investments to maximize this protection.

They should also keep this bill in mind when setting up new investments and signing new contracts with Mexico or Mexican authorities.

Also, considering the possible challenges to the constitutionality of the bill, businesses and investors must keep an eye on the outcomes of any such legal actions. These outcomes may provide valuable insights into the future direction of Mexico's legal environment and its impact on private sector activities.

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