

REGULATION

Price Controls. At present, there are no price controls on our products in any of our segments. In Mexico, prior to 1992, prices of carbonated soft drinks were regulated by the Mexican government. From 1992 to 1995, the industry was subject to voluntary price restraints. In response to the devaluation of the Mexican peso relative to the U.S. dollar in 1994 and 1995, however, the Mexican government adopted an economic recovery plan to control inflationary pressures in 1995. As part of this plan, the Mexican government encouraged the *Asociación Nacional de Productores de Refrescos y Aguas Carbonatadas, A.C.* (the National Association of Bottlers) to engage in voluntary consultations with the Mexican government with respect to price increases for returnable presentations. These voluntary consultations were terminated in 1996. Formal price controls have been imposed historically in several of the countries in which we operate, including Colombia, Brazil and Venezuela, and could be imposed in the future. The imposition of price controls in the future may limit our ability to set prices and adversely affect our results of operations.

Taxation of Soft Drinks. All the countries in which we operate, except for Panama, impose a value-added tax on the sale of soft drinks, with a rate of 15% in Mexico, 12% in Guatemala, 15% in Nicaragua, 13% in Costa Rica, 16% in Colombia, 14% in Venezuela, 21% in Argentina and 18% (São Paulo) and 17% (Mato Grosso do Sul) in Brazil. In addition, several of the countries in which we operate impose the following excise or other taxes:

- Guatemala imposes an excise tax of 0.18 cents in local currency (Ps. 0.26 as of December 31, 2006) per liter of soft drink.
- Costa Rica imposes a specific tax on non-alcoholic bottled beverages based on the combination of packaging and flavor, a 5% excise tax on local brands, a 10% tax on foreign brands and a 14% tax on mixers.
- Nicaragua imposes a 9% tax on consumption.
- Panama imposes a 5% tax based on the cost of goods produced.
- Argentina imposes an excise tax on colas and on flavored soft drinks containing less than 5% lemon juice or less than 10% fruit juice of 8.7%, and an excise tax on flavored soft drinks with 10% or more fruit juice and on mineral water of 4.2%.
- Brazil imposes an average production tax of 16.5% and an average sales tax of 4.6% in the territories where we operate.

Water Supply Law. In Mexico, we purchase water directly from municipal water companies and pump water from our own wells pursuant to concessions obtained from the Mexican government on a plant-by-plant basis. Water use in Mexico is regulated primarily by the *Ley de Aguas Nacionales de 1992* (the 1992 Water Law), and regulations issued thereunder, which created the *Comisión Nacional del Agua* (the National Water Commission). The National Water Commission is charged with overseeing the national system of water use. Under the 1992 Water Law, concessions for the use of a specific volume of ground or surface water generally run for five-, ten- or fifteen-year terms, depending on the supply of groundwater in each region as projected by the National Water Commission. Concessionaires may request concession terms to be extended upon termination. The Mexican government is authorized to reduce the volume of ground or surface water granted for use by a concession by whatever volume of water is not used by the concessionaire for three consecutive years. However, because the current concessions for each of our plants in Mexico do not match each plant's projected needs for water in future years, we successfully negotiated with the Mexican government the right to transfer the unused volume under concessions from certain plants to other plants anticipating greater water usage in the future. Our concessions may be terminated if, among other things, we use more water than permitted or we fail to pay required concession-related fees and do not cure such situations on a timely manner. We believe that we are in compliance with the terms of our existing concessions.

Although we have not undertaken independent studies to confirm the sufficiency of the existing or future groundwater supply, we believe that our existing concessions satisfy our current water requirements in Mexico. We can give no assurances, however, that groundwater will be available in sufficient quantities to meet our future production needs or that we will be able to maintain our current concessions.

We do not currently require a permit to obtain water in our other territories. In Nicaragua, Costa Rica and some plants in Colombia, we own private water wells. In the remainder of our territories, we obtain water from governmental agencies or municipalities. We can give no assurances that water will be available in sufficient quantities to meet our future production needs or that additional regulations relating to water use will not be adopted in the future.

Environmental Matters. In all of the countries where we operate, our businesses are subject to federal and state laws and regulations relating to the protection of the environment. In Mexico, the principal legislation is the *Ley General de Equilibrio Ecológico y Protección al Ambiente* (the Federal General Law for Ecological Equilibrium and Environmental Protection) or the Mexican Environmental Law and the *Ley General para la Prevención y Gestión Integral de los Residuos* (the General Law for the Prevention and Integral Management of Waste) which are enforced by the *Secretaría del Medio Ambiente, Recursos Naturales y Pesca* (the Ministry of the Environment, Natural Resources and Fisheries) or SEMARNAP. SEMARNAP can bring administrative and criminal proceedings against companies that violate environmental laws, and it also has the power to close non-complying facilities. Under the Mexican Environmental Law, rules have been promulgated concerning water, air and noise pollution and hazardous substances. In particular, Mexican environmental laws and regulations require that we file periodic reports with respect to air and water emissions and hazardous wastes and set forth standards for waste water discharge that apply to our operations. We are also subject to certain minimal restrictions on the operation of delivery trucks in Mexico City. We have implemented several programs designed to facilitate compliance with air, waste, noise and energy standards established by current Mexican federal and state environmental laws, including a program that installs catalytic converters and liquid petroleum gas in delivery trucks for our operations in Mexico City. See “—The Company—Product Distribution.”

In addition, we are subject to the *Ley Federal de Derechos* (the Federal Law of Governmental Fees), also enforced by SEMARNAP. Adopted in January 1993, the law provides that plants located in Mexico City that use deep water wells to supply their water requirements must pay a fee to the city for the discharge of residual waste water to drainage. In 1995, certain municipal authorities began to test the quality of the waste water discharge and charge plants an additional fee for measurements that exceed certain standards published by SEMARNAP. All of our bottler plants located in Mexico City, as well as the Toluca plant, met these new standards as of 2001. See “—Description of Property, Plant and Equipment.”

In our Mexican operations, we built a PET recycling plant in 2004 in partnership with The Coca-Cola Company and ALPLA, which manufactures plastic bottles for us in Mexico. This plant, located in Toluca, Mexico, started operations in 2005 and has a recycling capacity of 25,000 metric tons per year from which 15,000 metric tons can be reuse in PET bottles for food packaging purposes. We have also continued contributing funds to a nationwide recycling company ECOCE or *Ecología y compromiso empresarial* (Environmentally committed companies)

Our Central American operations are subject to several federal and state laws and regulations relating to the protection of the environment, which have been enacted in the last ten years, as awareness has increased in this region about the protection of the environment and the disposal of dangerous and toxic materials. In some countries in Central America, we are in the process of bringing our operations into compliance with new environmental laws. Also, our Costa Rica operations have participated in a joint effort along with the local division of The Coca-Cola Company called *Proyecto Planeta* (Project Planet) for the collection and recycling of non-returnable plastic bottles.

Our Colombian operations are subject to several Colombian federal, state and municipal laws and regulations related to the protection of the environment and the disposal of toxic and dangerous materials. These laws include the control of atmospheric emissions and strict limitations on the use of chlorofluorocarbons. We are also engaged in nationwide campaigns for the collection and recycling of glass and plastic bottles.

Our Venezuelan operations are subject to several Venezuelan federal, state and municipal laws and regulations related to the protection of the environment. The most relevant of these laws are the *Ley Orgánica del Ambiente* (the Organic Environmental Law), the *Ley Sobre Sustancias, Materiales y Desechos Peligrosos* (the Substance, Material and Dangerous Waste Law), and the *Ley Penal del Ambiente* (the Criminal Environment Law). Since the enactment of the Organic Environmental Law in 1995, our Venezuelan subsidiary has presented the proper authorities with plans to bring our production facilities and distribution centers into compliance with the law. While the laws provide certain grace periods for compliance with the new environmental standards, we have had to adjust some of the originally proposed timelines presented to the authorities because of delays in the completion of some of these projects.

Our Argentine operations are subject to federal and provincial laws and regulations relating to the protection of the environment. The most significant of these are regulations concerning waste water discharge, which are enforced by the *Secretaría de Recursos Naturales y Ambiente Humano* (the Ministry of Natural Resources and Human Environment) and the *Secretaría de Política Ambiental* (the Ministry of Environmental Policy) for the province of Buenos Aires. Our Alcorta plant is in compliance with waste water discharge standards.

Our Brazilian operations are subject to several federal, state and municipal laws and regulations related to the protection of the environment. Among the most relevant laws and regulations are those dealing with the emission of toxic and dangerous gases and disposal of waste water, which impose penalties, such as fines, facility closures or criminal charges depending upon the level of non-compliance. Our production plant located in Jundiai has been recognized by the Brazilian authorities for its compliance with environmental regulations and for having standards well above those imposed by the law. The plant has been certified for the ISO 9000 since March 1995 and the ISO 14001 since March 1997.

We have expended, and may be required to expend in the future, funds for compliance with and remediation under local environmental laws and regulations. Currently, we do not believe that such costs will have a material adverse effect on our results of operations or financial condition. However, since environmental laws and regulations and their enforcement are becoming increasingly more stringent in our territories, and there is increased awareness by local authorities of higher environmental standards in the countries where we operate, changes in current regulations may result in an increase in costs, which may have an adverse effect on our future results of operations or financial condition. Management is not aware of any pending regulatory changes that would require a significant amount of additional remedial capital expenditures.

BOTTLER AGREEMENTS**Coca-Cola Bottler Agreements**

Bottler agreements are the standard agreements for each territory that The Coca-Cola Company enters into with bottlers outside the United States for the sale of concentrates for certain *Coca-Cola* trademark beverages. We manufacture, package, distribute and sell soft drink beverages and bottled water under a separate bottler agreement for each of our territories.

These bottler agreements provide that we will purchase our entire requirement of concentrates for *Coca-Cola* trademark beverages from The Coca-Cola Company and other authorized suppliers at prices, terms of payment and on other terms and conditions of supply as determined from time to time by The Coca-Cola Company at its sole discretion. Concentrate prices are determined as a percentage of the weighted average retail price in local currency, net of applicable taxes. Although the price multipliers used to calculate the cost of concentrate and the currency of payment, among other terms, are set by The Coca-Cola Company at its sole discretion, we set the price of products sold to retailers at our discretion, subject to the applicability of price restraints. We have the exclusive right to distribute *Coca-Cola* trademark beverages for sale in our territories in authorized containers of the nature prescribed by the bottler agreements and currently used by our company. These containers include various configurations of cans and returnable and non-returnable bottles made of glass and plastic and fountain containers.

The bottler agreements include an acknowledgment by us that The Coca-Cola Company is the sole owner of the trademarks that identify the *Coca-Cola* trademark beverages and of the secret formulas with which The Coca-Cola Company's concentrates are made. Subject to our exclusive right to distribute *Coca-Cola* trademark beverages in our territories, The Coca-Cola Company reserves the right to import and export *Coca-Cola* trademark beverages to and from each of our territories. Our bottler agreements do not contain restrictions on The Coca-Cola Company's ability to set the price of concentrates charged to our subsidiaries and do not impose minimum marketing obligations on The Coca-Cola Company. The prices at which we purchase concentrates under the bottler agreements may vary materially from the prices we have historically paid. However, under our bylaws and the shareholders agreement among The Coca-Cola Company and certain of its subsidiaries and certain subsidiaries of FEMSA, an adverse action by The Coca-Cola Company under any of the bottler agreements may result in a suspension of certain veto rights of the directors appointed by The Coca-Cola Company. This provides us with limited protection against The Coca-Cola Company's ability to raise concentrate prices to the extent that such increase is deemed detrimental to us pursuant to the shareholder agreement and the bylaws. See "Item 7. Major Shareholders and Related Party Transactions—Major Shareholders—The Shareholders Agreement."

The Coca-Cola Company has the ability, at its sole discretion, to reformulate any of the *Coca-Cola* trademark beverages and to discontinue any of the *Coca-Cola* trademark beverages, subject to certain limitations, so long as all *Coca-Cola* trademark beverages are not discontinued. The Coca-Cola Company may also introduce new beverages in our territories in which case we have a right of first refusal with respect to the manufacturing, packaging, distribution and sale of such new beverages subject to the same obligations as then exist with respect to the *Coca-Cola* trademark beverages under the bottler agreements. The bottler agreements prohibit us from producing or handling cola products other than those of The Coca-Cola Company, or other products or packages that would imitate, infringe upon, or cause confusion with the products, trade dress, containers or trademarks of The Coca-Cola Company, or from acquiring or holding an interest in a party that engages in such activities. The bottler agreements also prohibit us from bottling any soft drink product except under the authority of, or with the consent of, The Coca-Cola Company. The bottler agreements impose restrictions concerning the use of certain trademarks, authorized containers, packaging and labeling of The Coca-Cola Company so as to conform to policies prescribed by The Coca-Cola Company. In particular, we are obligated to:

- maintain plant and equipment, staff and distribution facilities capable of manufacturing, packaging and distributing the Coca-Cola trademark beverages in authorized containers in accordance with our bottler agreements and in sufficient quantities to satisfy fully the demand in our territories;
- undertake adequate quality control measures prescribed by The Coca-Cola Company;

- develop, stimulate and satisfy fully the demand for Coca-Cola trademark beverages using all approved means, which includes the investment in advertising and marketing plans;
- maintain a sound financial capacity as may be reasonably necessary to assure performance by us and our affiliates of our obligations to The Coca-Cola Company; and
- submit annually to The Coca-Cola Company our marketing, management, promotional and advertising plans for the ensuing year.

The Coca-Cola Company contributed a significant portion of our total marketing expenses in our territories during 2006, a period in which we also contributed to The Coca-Cola Company's marketing expenses and has reiterated its intention to continue providing such support as part of our new cooperation framework. Although we believe that The Coca-Cola Company will continue to provide funds for advertising and marketing, it is not obligated to do so. Consequently, future levels of advertising and marketing support provided by The Coca-Cola Company may vary materially from the levels historically provided. See "Item 7. Major Shareholders and Related Party Transactions—Major Shareholders —The Shareholders Agreement" and "Item 7. Major Shareholders and Related Party Transactions—Major Shareholders —New Cooperation Framework with The Coca-Cola Company."

We have separate bottler agreements with The Coca-Cola Company for each of the territories in which we operate. Some of these bottler agreements renew automatically unless one of the parties gives prior notice that it does not wish to renew the agreement, while others require an agreement between the parties or require us to give notice electing to renew the agreement. The following table summarizes by segment the expiration dates and renewal provisions of our bottler agreements:

Segment	Expiration Date	Renewal/Termination Provision
Mexico	For two territories – June 2013	10 years, renewable automatically.
	For two territories – May 2015	10 years, renewable automatically.
Central America	Guatemala – June 2007	Renewable as agreed between the parties.
	Nicaragua – June 2007	Five years, requires notice at least six but not more than 12 months before expiration date.
	Costa Rica – September 2007	Five years, requires notice at least six but not more than 12 months before expiration date.
	Panama – For <i>Coca-Cola</i> trademark beverages – Indefinite.	May be terminated by either party with six months prior written notice.
	Panama – For other beverages – June 2007	Five years, requires notice at least six but not more than 12 months before expiration date.
Colombia	June 2007	Five years, requires notice at least six but not more than 12 months before expiration date.
Venezuela	For <i>Coca-Cola</i> trademark beverages – August 2006 ⁽¹⁾	Five years, requires notice at least six but not more than 12 months before expiration date.
	For other beverages – August 2006 ⁽¹⁾	Renewable as agreed between the parties.
Argentina	September 2014	10 years, renewable automatically.
Brazil	December 2004 ⁽¹⁾	Five years, requires notice at least six but not more than 12 months before expiration date.

(1) We are still in the process of negotiating renewals for these territories.

The bottler agreements are subject to termination by The Coca-Cola Company in the event of default by us. The default provisions include limitations on the change in ownership or control of our company and the assignment or transfer of the bottler agreements and are designed to preclude any person not acceptable to The Coca-Cola Company

from obtaining an assignment of a bottler agreement or from acquiring our company independently of similar rights set forth in the shareholders agreement. These provisions may prevent changes in our principal shareholders, including mergers or acquisitions involving sales or dispositions of our capital stock, which will involve an effective change of control, without the consent of The Coca-Cola Company. See “Item 7. Major Shareholders and Related Party Transactions–Major Shareholders –The Shareholders Agreement.”

We have also entered into tradename licensing agreements with The Coca-Cola Company pursuant to which we are authorized to use certain trademark names of The Coca-Cola Company. These agreements have an indefinite term, but are terminated if we cease to manufacture, market, sell and distribute *Coca-Cola* trademark products pursuant to the bottler agreements or if the shareholders agreement is terminated. The Coca-Cola Company also has the right to terminate the license agreement if we use its trademark names in a manner not authorized by the bottler agreements.

DESCRIPTION OF PROPERTY, PLANT AND EQUIPMENT

Over the past several years, we made significant capital improvements to modernize our facilities and improve operating efficiency and productivity, including:

- increasing the annual capacity of our bottler plants;
- installing clarification facilities to process different types of sweeteners;
- installing plastic bottle-blowing equipment and can presentation capacity;
- modifying equipment to increase flexibility to produce different presentations, including swing lines that can bottle both non-returnable and returnable presentations; and
- closing obsolete production facilities.

See “Item 5. Operating and Financial Review and Prospects–Capital Expenditures.”

As of December 31, 2006, we owned 31 bottler plants company wide. By country, we have twelve bottler facilities in Mexico, five in Central America, six in Colombia, four in Venezuela, three in Brazil and one in Argentina.

Since the Panamco acquisition in May 2003, we consolidated 22 of our plants into existing facilities including four plants in Mexico, one in Central America, eleven in Colombia, five in Venezuela and one in Brazil. During the same period, we have increased our productivity measured in unit cases sold by our remaining plants by more than 80% company wide as of December 31, 2006.

As of December 31, 2006 we operated 206 distribution centers, almost 45% of which were in our Mexican territories. We own more than 80% of these distribution centers and lease the remainder. See “–The Company–Product Distribution.”

We maintain an “all risk” insurance policy covering our properties (owned and leased), machinery and equipment and inventories as well as losses due to business interruptions. The policy covers damages caused by natural disaster, including hurricane, hail, earthquake and damages caused by human acts, including explosion, fire, vandalism, riot and losses incurred in connection with goods in transit. In addition, we maintain an “all risk” liability insurance policy that covers product liability. We purchase our insurance coverage through an insurance broker. In most cases the policies are issued by Allianz México, S.A., Compañía de Seguros, and the coverage is partially reinsured in the international reinsurance market.

The table below summarizes by country principal use, installed capacity and percentage utilization of our production facilities:

Production Facility Summary
As of December 31, 2006

Country	Principal Use	Installed Capacity (thousands of unit cases)	% Utilization⁽¹⁾
Mexico	Bottler Facility	1,565,921	68%
Guatemala	Bottler Facility	30,770	77%
Nicaragua	Bottler Facility	66,705	44%
Costa Rica	Bottler Facility	58,877	56%
Panama	Bottler Facility	52,559	39%
Colombia	Bottler Facility	265,123	72%
Venezuela	Bottler Facility	276,534	64%
Argentina	Bottler Facility	194,548	78%
Brazil	Bottler Facility	447,922	69%

(1) Annualized rate.

The table below summarizes by country plant location and facility area of our production facilities:

Production Facility by Location As of December 31, 2006		
Country	Plant	Facility Area (thousands of sq. meters)
Mexico	San Cristóbal de las Casas, Chiapas	45
	Cedro, Distrito Federal	18
	Cuautitlán, Estado de México	35
	Los Reyes la Paz, Estado de México	50
	Toluca, Estado de México	242
	Celaya, Guanajuato	87
	León, Guanajuato	38
	Morelia, Michoacán	50
	Juchitán, Oaxaca	27
	Ixtacomitán, Tabasco	90
	Apizaco, Tlaxcala	80
	Coatepec, Veracruz	142
Guatemala	Guatemala City	46
Nicaragua	Managua	60
Costa Rica	San José	52
Panama	Panama City	29
Colombia	Barranquilla	27
	Bogotá	84
	Bucaramanga	26
	Cali	87
	Manantial	67
	Medellín	45
Venezuela	Antimano	14
	Barcelona	141
	Maracaibo	68
	Valencia	100
Argentina	Alcorta	73
Brazil	Campo Grande	36
	Jundiai	191
	Moji das Cruzes	95

SIGNIFICANT SUBSIDIARIES

The table below sets forth all of our direct and indirect significant subsidiaries and the percentage of equity of each subsidiary we owned directly or indirectly as of December 31, 2006:

Name of Company	Jurisdiction of Incorporation	Percentage Owned
Propimex, S.A. de C.V	Mexico	100.00%
Corporación Interamericana de Bebidas, S.A. de C.V	Mexico	100.00%
Panamco México, S.A. de C.V	Mexico	99.24%
Kristine Oversease, S.A. de C.V. (holding company of Brazilian operations)	Mexico	83.11%
Industria Nacional de Gaseosas, S.A. (holding company of our Colombian operations)	Colombia	97.66%