

MEXICO

Investment rules of the world

About

At DLA Piper, we have one of the largest finance and projects teams in the world with more than 600 dedicated lawyers and an established local law firm network. We share knowledge and skills in debt instruments, debt securities, funds, derivatives and portfolios, as well as energy, infrastructure and other projects, across Europe, the Middle East, Africa, Asia Pacific and the Americas.

When and wherever we work for you on finance and investment deals and projects, you can rely on our international platform; we are backed by the network and resources of one the largest and most-connected business law firms in the world.

We enjoy being part of your team, bringing experience across sectors, borders and financial products, supporting you on first-of-a-kind deals, in new markets and to grow.

With global perspective, we can help you to realize your financial strategy in whichever markets you do business.

Investment Rules of the World

With input from across our global network, this guide covers key legal topics for different financial activities and projects and gives you an overview of the points you may consider when initially looking at financing or investing in particular jurisdictions. Please [contact us](#) if you would like to discuss any legal issues or solutions for your business. We also welcome your feedback about this guide via investmentrules@dlapiper.com.



Mexico

Last modified 05 December 2019

Capital markets and structured investments

Issuing and investing in debt securities

Are there any restrictions on issuing debt securities?

There are restrictions on offering and selling debt securities under Mexican law.

Unless certain exclusions or exemptions apply, it is unlawful to offer debt securities to the public in Mexico or to request that they are admitted to trading on a regulated market operating in Mexico unless a prospectus approved by CNVB has been made available to the public.

Last modified 5 Dec 2019

What are common issuing methods and types of debt securities?

The main types of debt securities depend on the type of issuer. Typically, banks and other financial institutions issue short-term notes and commercial paper while private companies and local governments issue long-term structured notes under programs.

Debt can be issued under a short (less than a year) or a long (more than a year) term. It can be issued directly as corporate debt (*certificados bursátiles, pagarés, obligaciones*) (eg a bond issuance) or structured debt through a trust (*certificados bursátiles fiduciarios*).

Debt can be issued in a single series or under a program.

Last modified 5 Dec 2019

What are the differences between offering debt securities to institutional / professional or other investors?

Institutional investors are heavily regulated and subject to the supervision of regulatory authorities including the National Banking and Securities Commission (CNBV), National Retirement Savings System Commission (CONSAR) and *Banco de México* (BANXICO). Generally, institutional investors can only invest in those assets that applicable regulations explicitly permit.

The Securities Market Law defines institutional investors as any entity which, under federal law, is deemed as such or is a financial entity (that is, Mexican and foreign banks, broker-dealers, insurance companies, AFORES, investment funds, private pension funds, among others), including fiduciary divisions.

Last modified 5 Dec 2019

When is it necessary to prepare a prospectus?

Generally, all debt public offerings require registration with the CNBV and filing a prospectus for approval, except for:

- short-term offerings that require issuers to file only an offering statement (aviso de oferta); and
- issuances under programs, which only require an information memorandum (suplemento) because the prospectus was filed when the relevant program was authorized.

Last modified 5 Dec 2019

What are the main exchanges available?

Currently, the regulated exchanges in Mexico are Bolsa Mexicana de Valores (Mexican Stock Exchange) and Bolsa Institucional de Valores (BIVA).

Since 2014, the Mexican Stock Exchange has been part of the Mercado Integrado Latinoamericano (MILA), an agreement that integrates the stock exchange markets of Chile, Colombia, Mexico, and Peru, as part of economic integration efforts among the Pacific Alliance member countries. MILA is not a regulated stock exchange but an agreement between regulated stock exchanges establishing a regional market to trade equities from the four countries.

In October 2015, BIVA formally applied for a concession to organize and operate a new stock exchange in Mexico, which was granted by the Mexican financial authorities in August 2017.

Last modified 5 Dec 2019

Is there a private placement market?

Mexico has an active private placement market.

Last modified 5 Dec 2019

Are there any other notable risks or issues around issuing or investing in debt securities?

Issuing debt securities

Issuers are required to take responsibility for prospectuses for debt securities. Misleading statements in, or omissions from, any applicable offering document can give rise to both civil and criminal liability under Mexican law. Mexico has various investor protection statutory provisions relevant to liability for an inaccurate offering memorandum. There are also general fraud statutes and liability may also arise under Mexican law through a civil action for deceit, negligent misstatement or misrepresentation.

Investing in debt securities

Debt security terms and conditions typically contain provisions which may permit their modification without the consent of all investors and confer significant discretions on the common representative, which may be exercised without the consent of investors and without regard to the individual interests of particular investors. The conditions also provide for meetings of investors to consider matters affecting the investors' interests. These provisions typically permit defined majorities to bind all investors including investors who did not attend and vote at the relevant meeting and investors who voted against the majority.

Last modified 5 Dec 2019

Establishing and investing in debt / hedge funds

Are there any restrictions on establishing a fund?

The establishing of an investment fund requires authorization from the National Banking and Securities Commission (CNBV). The authorization request is required to include, among other information, a draft copy of the by-laws, the names of the founding shareholders and the members of the board of directors of the management company and a draft copy of the prospectus.

All regulated funds are treated the same way and are referred to as mutual funds in Mexico. Mexican law does not generally distinguish between open-ended and closed-ended funds or retail and hedge funds. They are defined differently under the Investment Funds Law (*Ley de Fondos de Inversión*): the defining characteristic of an open-ended retail fund is that it has the legal obligation to repurchase or redeem its own shares while it is expressly forbidden for a closed-ended retail fund to repurchase its own shares from its investors if they are not listed on any stock exchange. In practice, closed-ended retail funds are rare in Mexico.

Last modified 5 Dec 2019

What are common fund structures?

The most popular types of investment funds in Mexico are:

- the variable yield mutual fund or equity mutual fund (*Fondo de Inversión de Renta Variable*); and
- the mutual fund for investment in debt securities or fixed fund (*Fondo de Inversión en Instrumentos de Deuda*).

Last modified 5 Dec 2019

What are the differences between offering fund securities to professional / institutional or other investors?

Generally, Mexican law does not distinguish between the regulation of open-ended and closed-ended funds or retail and institutional /professional funds. Mutual funds can be marketed to both persons and corporations and to the public in general.

Last modified 5 Dec 2019

Are there any other notable risks or issues around establishing and investing in funds?

Establishing funds

The only legal structure used in Mexico to set up a fund is a stock corporation (*Sociedad Anónima* or SA). The Investment Funds Law was amended in 2014 to permit the establishment of a special type of SA for mutual funds, so that mutual funds are now required to comply with fewer regulatory requirements.

Last modified 5 Dec 2019

Managing and marketing debt / hedge funds

Are there any restrictions on marketing a fund?

Investment funds can be marketed by management companies, insurance companies, brokers, brokers' dealers and distributors. These entities must be authorized to market the funds.

The marketing of the investment fund management companies must be clear to avoid confusion and allow for simple interpretation. The broadcasting of announcements with ambiguous information is forbidden. The advertising material must not contain any false information, omission, ambiguity, hyperbole or deception, which might induce the public to make wrong or inaccurate conclusions about the products and services offered by the mutual fund managers.

Although its approval is not required, marketing material must be sent to the National Banking and Securities Commission (CNBV). The Association of Securities Intermediaries (*Asociación Mexicana de Intermediarios Bursátiles*) (AMIB) can also comment on marketing material.

Last modified 5 Dec 2019

Are there any restrictions on managing a fund?

Managers of investment funds must be authorized by the National Banking and Securities Commission (CNBV). The portfolio of assets must be deposited in institutions for deposits of securities, which institutions must be licensed.

Last modified 5 Dec 2019

Entering into derivatives contracts

Are there any restrictions on entering into derivatives contracts?

In Mexico, entering into derivatives contracts can be carried out in the following markets.

Organized market

In the organized markets, the derivatives contracts are governed pursuant to standardized terms and conditions (active type, underlying, quantity or size of the agreement, expiration of the agreement, price quotations and liquidation procedure). The main feature of these markets is that the seller and the purchaser never trade directly, but through a central counterparty clearing house specialized in derivatives, in order to eliminate the exchange and insolvency risks.

The only institutional, regulated and organized market existing for the trading of derivatives contracts in Mexico is the Mercado Mexicano de Derivados, S.A. de C.V. (*MexDer*), an affiliate of the Mexican Stock Exchange (*Bolsa Mexicana de Valores*). MexDer along with Asigna, its triple-A rated clearinghouse (Asigna), offers liquid, transparent Mexican benchmark products based on interest rates, foreign exchange and stock indexes. Asigna acts as a counterparty for all transactions performed on MexDer.

In principle, to trade directly in MexDer, it is required to be:

- a Clearing Member (*Socio Liquidador*), which is a trust that is a member of MexDer and owns a share in the equity of Asigna, and whose purpose is to settle and, in some cases, enter into exchange-listed futures and option contracts on behalf of clients; or
- a Trader, which is a bank, brokerage firm or any other entity, that may or may not be a member of MexDer, whose purpose is to act as a broker for one or more clearing members in entering into futures and option contracts, and which may access MexDer's electronic trading system to enter into such contracts.

Over the counter (OTC)

In the non-organized markets, the parties set out the relevant terms and conditions in accordance with their particular needs; the derivatives contracts are designed by institutions pursuant to the particular needs of their clients. In these markets, there is no clearing house and thus each party takes default risk. In the OTC, there are absolutely no limitations regarding the type of derivatives products to be commercialized, as long as there are assets, trade flows or goods that may allow the documentation of such transactions.

Last modified 5 Dec 2019

What are common types of derivatives?

In MexDer, only future, options and interest rate swap agreements are listed. Only futures and options with the following underlying assets are eligible:

- **futures** – foreign currency, indexes, debt, shares and commodities; and
- **options** – foreign currency, indexes, and shares.

All other types of derivatives contracts (including forwards and currency swaps) are privately negotiated in non-exchange-traded market transactions (OTC or Over the Counter).

Last modified 5 Dec 2019

Are there any other notable risks or issues around entering into derivatives contracts?

The derivatives market regulation relies on general provisions encompassing the Ministry of Finance and Public Credit (SHCP), *Banco de México* (BANXICO) and the National Banking and Securities Commission (CNBV). There is no regulation for OTC derivatives, which impairs enforcement and supervisory efforts by CNBV in this area, however, the CNBV aims at maintaining oversight of OTC derivatives transactions to ensure that participants do not engage in regulated activities, such as trading with securities.

Last modified 5 Dec 2019

Debt finance

Lending and borrowing

Are there any restrictions on lending and borrowing?

Lending

Lending is only a regulated activity in relation to mortgages and consumer lending. In these circumstances, and assuming none of the available exemptions apply, a lender will need to be authorized by the National Banking and Securities Commission to conduct such business. The main provisions regulating these activities aim at protecting financial services users, strengthening competition in banking services, and giving the National Commission for the Protection and Defense of Users of Financial Services (CONDUSEF) powers to supervise and impose sanctions.

There are no additional restrictions that apply to foreign lenders making loans to Mexican borrowers.

Borrowing

While borrowers are generally not regulated, it is advisable for borrowers to consider whether either the mortgage or consumer lending regimes apply to their activities, in which case they will benefit from the protections mentioned above.

Last modified 5 Dec 2019

What are common lending structures?

Lending in Mexico can be structured in a number of different ways to include a variety of features depending on the commercial needs of the parties.

A loan can either be provided on a bilateral basis (a single lender providing the entire facility) or syndicated basis (multiple lenders each providing parts of the overall facility).

Syndicated facilities by their nature involve more parties (such as agents and trustees which fulfil certain roles for the finance parties), are more highly structured and involve more complex documentation. Larger financings will typically be done on a syndicated basis with one of the syndicate taking the lead in coordinating and arranging the financing.

Loans will be structured to achieve specific objectives, eg term loans, working capital loans, equity bridge facilities and project or letter of credit facilities.

Loan durations

The duration of a loan can vary between:

- a term loan, provided for an agreed final period of time but with a short availability period;

- a revolving loan, provided for an agreed period of time with an availability period that extends nearer to maturity of the loan and which may be redrawn if repaid;
- an overdraft, provided on a short-term basis to solve short-term cash flow issues; or
- a standby or a bridging loan, intended to be used in exceptional circumstances when other forms of finance are unavailable and often attracting a higher margin.

Loan security

A loan can either be secured, unsecured or guaranteed. For more information, see [Giving and taking guarantees and security](#).

Loan commitment

A loan can be:

- committed, meaning that the lender is obliged to provide the loan if certain conditions are fulfilled; or
- uncommitted, meaning that the lender has discretion whether or not to provide the loan.

Loan repayment

A loan can be repayable on demand, on an amortizing basis (in instalments over the life of the loan) or scheduled (usually meaning the loan is repayable in full at maturity).

Last modified 5 Dec 2019

What are the differences between lending to institutional / professional or other borrowers?

Lending to institutional/professional borrowers is subject to less regulatory oversight and so less burdensome from a compliance perspective.

By contrast, lending in the context of mortgages and to consumers is a regulated activity supervised by the National Banking and Securities Commission (CNBV) and the National Commission for the Protection and Defense of Users of Financial Services (CONDUSEF).

For more information, see [Lending and borrowing – restrictions](#).

Last modified 5 Dec 2019

Do the laws recognize the principles of agency and trusts?

It is common to appoint an agent to act on behalf of other parties (as in syndicated loan transactions) and a trustee to hold rights and other assets on trust for the lenders or secured parties. Thus, the common-law principles of agency and trust are recognized in the Mexican legal framework.

Last modified 5 Dec 2019

Are there any other notable risks or issues around lending?

Generally

Loan agreements and other finance documents are subject to general contractual principles. There are no specific limitations on interest rates or the ability of lenders to charge default interest under loan agreements, however, there may be general or practical limitations stemming from usury statutes, judicial precedents and market conditions that may limit the amount of the rate as well as from tax considerations, particularly in the case of transactions among related parties.

In the event of proceedings in Mexico seeking performance of obligations of a Mexican borrower, pursuant to Mexican Monetary Law, the borrower may discharge its respective obligations by paying any sums due in a currency other than Mexican currency, in Mexican currency at the rate of exchange prevailing in Mexico and fixed and published by *Banco de México* (BANXICO) in the Official Gazette of the Federation of Mexico on the date preceding the date of payment.

Specific types of lending

In mortgage and consumer lending, the National Commission for the Protection and Defense of Users of Financial Services (CONDUSEF) is granted authority to provide for a list of 'abusive clauses' which institutions will not be able to include in their adhesion contracts, as well as the regime for its supervision and removal. Financial adhesion contracts are non-negotiable financial contracts which are offered by financial institutions and accepted 'as is' by financial services users seeking the corresponding financial service.

Standard form documentation

There are no recommended forms of lending documentation provided by market participants or regulators. Most finance transactions are documented on bank standard form documentation prepared in-house or by external legal counsel.

Last modified 5 Dec 2019

Are there any other notable risks or issues around borrowing?

In cross-border lending, borrowers are required to consider the identity of the beneficial owner of interest payments, given that tax gross-up clauses are a common feature in loan agreements and withholding tax rates range from 4.9% to 40%, depending on the beneficial owner of the interest. Lower withholding tax rates may be available to tax residents in countries with which Mexico has entered into a tax treaty to avoid double taxation. Interest payments carried out to export-import banks may not be subject to any withholding, provided that the conditions set out by the relevant tax treaty are complied with.

Last modified 5 Dec 2019

Giving and taking guarantees and security

Are there any restrictions on giving and taking guarantees and security?

Some of the key areas affecting the giving of guarantees and security are as follows.

Capacity

It is important to check the constitutional documents of a company giving a guarantee or security to ensure it has an express or ancillary power to do so and there are no restrictions on the signatories' powers that would prevent them from executing such documents.

Insolvency

Guarantees and security may be at risk of being set aside under Mexican insolvency laws if the guarantee or security was granted by a company with a certain period of time prior to the onset of insolvency (fraudulent conveyance). This would be the case if the company giving the guarantee or security received considerably less consideration, and as such, the transaction was at an undervalue. For such a transaction to be set aside, certain statutory criteria would have to be met, including that the guarantee or security was given within 270 calendar days prior to the declaration of insolvency of the affected party (or 540 calendar days for inter-company claims). Guarantees and security may also be challenged on other grounds relating to insolvency.

Financial assistance

The concept of unlawful financial assistance is not recognized in Mexico. However, fair consideration, corporate benefit, arms-length transactions and related concepts are relevant, particularly in insolvency situations.

Corporate benefit rules

The granting of downstream guarantees and security interests by a parent company to secure a loan to its subsidiary would generally be valid.

Last modified 5 Dec 2019

What are common types of guarantees and security?

Common forms of guarantees

Guarantees to secure compliance with obligations are commonly used in Mexico in all types of transactions. The most common types of guarantees are as follows.

CIVIL GUARANTEE (*FIANZA CIVIL*)

The Federal Civil Code establishes that the civil guarantee is an agreement by means of which a third party undertakes to pay the creditor if the debtor does not meet its obligations.

SURETY BOND (*FIANZA MERCANTIL*)

Under Mexican law, a bond is a guarantee issued by an authorized entity which grants bonds on a customary basis. The bond is an agreement between a guarantor and the creditor of the original debtor under which the guarantor undertakes to pay or otherwise comply with the debtor's obligations in case the debtor defaults. The bond can be granted only if a valid underlying obligation exists. A guarantor may validly agree to pay a certain amount of money which is owed and not paid by the debtor, or if the debtor does not comply with a payment obligation.

Surety bonds can be of various types, including administrative, judicial, credit and fidelity bonds.

UNCONDITIONAL ENDORSEMENT (*AVAL*)

According to the General Law of Negotiable Instruments and Credit Operations, a person may guarantee total or partial payment of amounts described in a negotiable instrument (eg promissory note) by means of an unconditional endorsement. The guarantor is jointly liable with the principal obligor and its obligations are valid notwithstanding that the principal obligation is null for any reason whatsoever.

Common forms of security

The most common forms of security are as follows.

MORTGAGE

A mortgage is a security interest granted over real estate assets that are not delivered to the creditor, and that give the creditor the right (in case of default of the secured obligation) to be paid from the value of the asset.

GUARANTEE TRUST

This is a contract under which a person transfers to a trustee the ownership or title of one or more tangible and/or intangible assets in order to secure the obligations of a settlor in favor of a third party.

TRADITIONAL PLEDGE (*PRENDA MERCANTIL*)

The pledgor (a debtor or a third party) transfers possession of the movable asset to the lender (or a third party for the benefit of the lender) to hold as security for compliance with an obligation. This pledge is commonly used to pledge stock of a private company, for instance, where the lender takes actual possession of endorsed stock certificates.

NON-POSSESSORY PLEDGE (*PRENDA SIN TRANSMISIÓN DE POSESIÓN*)

Possession and operation of the assets remain with the pledgor. This type of pledge includes the possibility of creating a floating or generic pledge over all present and future movable assets of a business.

SECURITIES PLEDGE (*PRENDA BURSÁTIL*)

This is a pledge over securities traded in the Mexican stock exchange. Securities are deposited in an account at the *S.D. Indeval, S.A. de C. V., Institución para el Depósito de Valores* (clearing agency).

Last modified 5 Dec 2019

Are there any other notable risks or issues around giving and taking guarantees and security?

Giving or taking guarantees

A civil guarantee cannot exist without a valid principal obligation. Guarantors are granted certain benefits under Mexican law, known as the benefits of *orden*, *división* and *excusión*. The benefit of *orden* requires the creditor to proceed against the debtor before proceeding against the guarantor. The benefit of *excusión* requires the creditor to ensure the assets of the debtor are first exhausted in payment of its obligations before any amounts are claimed from or paid by the guarantor. The benefit of *división* exists when there are multiple guarantors: it allows one of the guarantors which has been called to trial to have the other guarantors appear at the same trial in order to defend themselves jointly, with each guarantor being liable for its proportionate share of the principal obligation. These benefits may be waived by the guarantor.

Giving or taking security

A mortgage securing a debt above a minimum threshold value (which is determined by local law and varies from state to state) must be in writing and executed before a Mexican notary public. The mortgage instrument, which should precisely describe the property being encumbered and the term of the mortgage, must be registered in the appropriate real property public registry office to be effective against third parties. Other registrations are required depending on the type of property being encumbered. For example, registration in the aircraft registry, the maritime registry and the railroad registry.

Guarantee trusts must be executed in writing. A guarantee trust over immovable property must be executed before a Mexican notary public and the trust instrument must be registered in the appropriate real property public registry office to be effective against third parties. Guarantee trusts over movable property securing a debt above a minimum threshold value must also be executed before a Mexican notary public and the trust instrument should be registered in the federal personal property collateral registry (*Registro Único de Garantías Mobiliarias*). Other registrations, authorizations and additional actions can also be required depending on the assets being placed in trust.

A traditional pledge must be executed in writing. Special perfection requirements apply depending on the type of asset, such as delivery of bearer instruments to the lender or a third party, delivery and endorsement of registered instruments and registration in the special registry ledger (for example, in the case of shares of a private stock corporation), and delivery of non-negotiable instruments and notices to the underlying debtor, if applicable.

A non-possessory pledge must be executed in writing. A non-possessory pledge securing a debt above a minimum threshold value must be ratified before a Mexican notary public and the resulting instrument registered in the the federal personal property collateral registry (*Registro Único de Garantías Mobiliarias*) to be effective against third parties.

A securities pledge must be executed in writing and involves a foreclosure agent (*ejecutor*) and the transfer of the securities to an account at the clearing agency. A Mexican bank or brokerage firm (other than the lender) may be appointed as foreclosure agent and is responsible for selling the securities at market value if a default occurs.

Last modified 5 Dec 2019

Financial regulation

Law and regulation

What are the main laws and regulations that apply to entities that are involved in finance and investments generally?

Generally

Bank of Mexico Law (*Ley del Banco de México*)

Credit Institutions Law (*Ley de Instituciones de Crédito*)

Securities Market Law (*Ley del Mercado de Valores*)

Financial Groups Law (*Ley para Regular las Agrupaciones Financieras*)

Credit Organizations and Auxiliary Activities General Law (*Ley General de Organizaciones y Actividades Auxiliares del Crédito*)

General Law of Negotiable Instruments and Credit Transactions (*Ley General de Títulos y Operaciones de Crédito*)

Consumer credit

Law for the Protection and Defense of the User of Financial Services (*Ley de Protección y Defensa al Usuario de Servicios Financieros*)

Financial Services Transparency and Regulation Law (*Ley para la Transparencia y Ordenamiento de los Servicios Financieros*)

Mortgages

State Civil Codes (*Códigos Civiles Estatales*)

Special types of mortgages regulated in the following laws:

- Credit Institutions Law (*Ley de Instituciones de Crédito*) (Industrial Mortgage);
- Civil Aviation Law (*Ley de Aviación Civil*) (Aircraft Mortgage);
- Maritime Navigation and Commerce Law (*Ley de Navegación y Comercio Marítimos*) (Maritime Mortgage); and
- General Communications Law (*Ley de Vías Generales de Comunicación*) (Communications Assets Mortgage)

Corporations

General Law of Commercial Companies (*Ley General de Sociedades Mercantiles*)

Securities Market Law (*Ley del Mercado de Valores*)

Funds and platforms

Investment Funds Law (*Ley de Fondos de Inversión*)

Other key market legislation

Monetary Law of the United Mexican States (*Ley Monetaria de los Estados Unidos Mexicanos*)

Financial Technology Institutions Law (*Ley para Regular las Instituciones de Tecnología Financiera*)

Payments Systems Law (*Ley de Sistemas de Pagos*)

Bankruptcy Law (*Ley de Concursos Mercantiles*)

Bank Savings Protection Law (*Ley de Protección al Ahorro Bancario*)

Law to Regulate Credit Information Corporations (*Ley para Regular las Sociedades de Información Crediticia*)

Guaranteed Credit Transparency Law (*Ley de Transparencia y de Fomento a la Competencia en el Crédito Garantizado*)

Anti-Money Laundering Law (*Ley Federal para la Prevención e Identificación de Operaciones con Recursos de Procedencia Ilícita*)

Several regulations (*circulares*) issued by Banco de México, the National Banking and Securities Commission and other regulatory bodies

Last modified 5 Dec 2019

Regulatory authorization

Who are the regulators?

The Ministry of Finance and Public Credit (*Secretaría de Hacienda y Crédito Público*) (SHCP) plans and directs the Federal Government's economic policy in Mexico, as regards to finance, tax, spending, income and public debt. It supervises the Mexican banking system.

Mexico's central bank, *Banco de México* (BANXICO), promotes the sound development of the Mexican financial system and the optimal functioning of the payment systems. BANXICO ensures the stability of the domestic currency's purchasing power.

The National Banking and Securities Commission (*Comisión Nacional Bancaria y de Valores*) (CNBV), supervises and regulates all entities of the Mexican financial system (including banks, non-bank finance companies, stockbrokerage houses, financial technology institutions and mutual funds) in order to ensure its stability and proper operation and to protect the interests of the general public.

The National Commission for the Protection and Defense of Users of Financial Services (*Comisión Nacional para la Protección y Defensa de los Usuarios de Servicios Financieros*) (Condusef), promotes financial education and transparency and protects financial services users before entities of the Mexican financial system.

The National Retirement Savings System Commission (*Comisión Nacional de Sistemas de Ahorro para el Retiro*) (CONSAR), supervises and regulates AFORES, companies that administer the employees retirement savings.

The Bank Savings Protection Institute (*Instituto para la Protección al Ahorro Bancario*) has the authority to provide depositary insured institutions with limited deposit insurance in favor of banking depositors and suggest and oversee capital restoration plans to financially assist banks for the benefit of depositors.

The National Insurance and Bonding Commission (*Comisión Nacional de Seguros y Fianzas*), supervises and regulates insurance and bonding companies.

Last modified 5 Dec 2019

What are the authorization requirements and process?

Most financial entities require authorization for incorporation from CNBV (in some cases with an opinion from BANXICO confirming such entity's suitability for authorization).

The authorization process includes identifying equity holders, board members and main officers, presenting a business plan and a draft copy of by-laws, describing the proposed capital structure, describing technological infrastructure and identifying the origin of resources used as capital contributions. In most cases the regulator will have three to six months from receipt of a completed application to grant or deny authorization.

Most institutions are required to make a security deposit in favor of the Federal Treasury, representing a percentage of the corresponding institution's minimum capital requirement.

Most authorized financial institutions are listed in the Supervised Entities Registry (*Padrón de Entidades Supervisadas*).

Last modified 5 Dec 2019

What are the main ongoing compliance requirements?

Financial institutions are subject to prudential supervision (eg capital adequacy, liquidity, operational and technological risk) and requirements on Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT), protection of users of financial services and efficiency of operation and competition in financial services.

Last modified 5 Dec 2019

What are the penalties for failure to be authorized?

A person undertaking a regulated activity without being authorized commits a criminal offence and is liable to imprisonment.

Last modified 5 Dec 2019

Regulated activities

What finance and investment activities require authorization?

Generally

Main regulated activities include:

- retail banking activities (operation of deposit accounts);
- consumer lending;
- public offering of securities;
- crowdfunding and electronic wallets;
- securities brokerage (trading in securities and other investments);
- investment and asset management (managing investment funds, including distribution and appraisal entities);
- insurance and bonding issuance and brokerage;
- establishment of representative office of foreign financial institutions; and
- investment advisory services (rendering portfolio management and investment advisory services in a regular and professional manner).

Consumer credit

Consumer lending is also a regulated activity that requires governmental authorization.

Last modified 5 Dec 2019

Are there any possible exemptions?

Mexican Non-Bank Financial Entities (*Sociedades Financieras de Objeto Múltiple* or SOFOMs) are allowed to provide financing through direct loans, financial leasing and factoring without needing to obtain authorization from Mexican regulators, however, these entities are not allowed to obtain deposits from the general public. There are two types of SOFOMs:

- regulated SOFOMs which are entities with a capital link to a banking or other regulated institution; and
- non-regulated SOFOMs which lack such a capital link.

For each type of regulated activity there are a number of specific exemptions that could also apply, including for activities carried out by family offices, private equity entities and other private wealth management entities.

Last modified 5 Dec 2019

Do any exchange controls or other restrictions on payments apply?

The Mexican peso is freely convertible into all other currencies and there are no restrictions on the remittance of profits abroad or the repatriation of capital.

Last modified 5 Dec 2019

What are the rules around financial promotions?

Rules

Mexican legislation regulates investment advisors as individual or entities that without being stock exchange brokers, provide portfolio management and investment advisory services in an habitual and professional manner. Investment advisors are subject to the surveillance of the National Banking and Securities Commission (CNBV) and subject to AML/CFT regulations.

All advertising or promotion by investment advisors to the general public is subject to CNBV's approval, including advertising in connection with securities offers, which is made through prospectuses, informative brochures or other offering materials authorized by CNBV.

Exemptions

Exemptions include communications to relatives or employees, foreign investment advisors not having physical presence or agents in Mexico, or the rendering of asset management services to trusts issuing securities to the general public through the stock exchange, as long as there is no services advertisement to an indeterminate number of persons or through mass media.

Last modified 5 Dec 2019

Entity establishment

What types of legal entity are generally used to undertake financial or investment activity?

Generally

The most common type of legal entity is the stock corporation or *Sociedad Anonima*, which can adopt the variable capital form in order to be a *Sociedad Anonima de Capital Variable*, the only difference being the flexibility in the latter to increase or decrease its capital stock without having to amend formally its corporate charter.

The *Sociedad Anonima* are required to adopt the *Sociedad Anonima Bursatil* or *Sociedad Anonima Promotora de Inversión Bursátil* forms form when performing an initial public offer of their shares through the Mexican Stock Exchange.

Funds

Investment funds are required to adopt the *Sociedad Anonima de Capital Variable* form of entity.

Last modified 5 Dec 2019

Is it possible to conduct lending or investment business through a branch or establishment?

Foreign lenders are able to conduct lending activities in Mexico through a branch or office outside of Mexico.

Foreign financial institutions may conduct lending or investment business by establishing in Mexico affiliates of foreign financial institutions.

Foreign financial institutions may also establish a representative office in Mexico through which they may perform a limited list of activities, including informing and negotiating the terms and conditions of loans and investments to be made by foreign financial institutions. Specific prohibitions are applicable to representative offices such as undertaking any financial intermediation that would require authorization from the Mexican government or acting in transactions that imply the receipt of funds or investments from the public.

Last modified 5 Dec 2019

FinTech

FinTech products and uses

What are the most common technology products and FinTech applications used or being developed in the finance and investment marketplace?

Peer-to-peer funding platforms and marketplace lending

There is no strict definition for marketplace lending given the wide variety of entrants and financing techniques involved. The principal characteristics of new marketplace lenders, however, would include:

- operating from or through a non-bank lending platform established as a specialist corporate or special purpose vehicle (SPV) based structure;
- applying technology to leverage and optimize the lending platform and user experience; and
- connecting borrowers and lenders through the platform rather than applying funding arising from a wider deposit-based relationship.

Marketplace lending in Mexico is at an initial stage but has made available most forms of traditional bank funding products. Most common products include:

- debt consolidation;
- consumer loans;
- student lending products;
- small and medium-sized enterprises (SME) lending; and
- factoring.

It is likely that the volume of lending in these product areas as well as further and additional product areas will significantly increase over the coming years, as financing becomes more readily available to support the marketplace lending sector.

HOW ARE MARKETPLACE LENDING PLATFORMS FUNDING THEMSELVES?

Marketplace lending includes peer-to-peer (P2P) type structures, often operated through an electronic platform provider as well as crowdfunding and also direct-to-retail financing mechanisms. The increase in demand for credit through these marketplace platforms has also been appealing to larger pools of available capital, such as private equity and venture capital funds as well as institutional sponsors. Funding platforms will now often be backed by institutional finance in addition to, or rather than, individual investors on a traditional P2P basis.

ISSUES FOR STARTUP MARKETPLACE LENDERS

Marketplace lending businesses can be incorporated under various corporate forms, often as stock corporations (*sociedad anónima* or SA) – or one of its variations, the investment promotion corporation (*sociedad anónima promotora de inversión* or SAPI) – which provide flexibility and corporate governance features that facilitate joint venture arrangements and private equity investments. There is also an example of a marketplace lender incorporated as a Popular Finance Company (*sociedad financiera popular* or SOFIPO), a microcredit financial institution authorized and supervised by Mexico's National Banking and Securities Commission (*Comisión Nacional Bancaria y de Valores* or CNBV).

Most marketplace lenders operate as agents of investors to make loans on their behalf to third parties interested in obtaining financing. The loan funds are provided by the investors; the marketplace lender then distributes the funds on behalf of investors to various pre-qualified borrowers and also acts as agent of the investors for administrative and collection purposes.

Blockchain, smart contracts and cryptocurrencies

WHAT IS BLOCKCHAIN?

Blockchain provides a new approach to holding and authenticating data. It is a database operating through distributed ledger technology in which data is recorded on computers, by way of a P2P mechanism, based on pre-agreed consensus algorithms in the applicable

participating network. It is a form of database where data is stored in the chain in either fixed structures called 'blocks' or algorithm functions called 'hashes'.

Each block includes unique features such as its unique block reference number, the time the block was created and a link back to the previous block. Each block is reviewed by a number of nodes and the block is only added to the database if the node reaches consensus that the block only contains valid transactions. Content includes digital assets and instructions which reflect the transactions and parties to those transactions. The ability to track previous blocks in the chain makes it possible to identify transactions back to the first ever transaction completed, enabling parties to verify and establish the authenticity of the assets in the latest block. This makes blockchain exceptionally accurate and secure.

Specialist users on the system apply advanced computing software to identify time stamped blocks, verify the accuracy of the block using sophisticated algorithms and add the verified block to the chain. As the number of participants increases, the replication of the data over a wider base makes it harder for any person to alter the data in the chain. Any attempted addition or modification to the information on a block needs to be approved by all users in the network and verification of any block can only happen through a 'proof of work' process.

As a result, the data is identified and authenticated in near real-time, providing a permanent and incorruptible database sufficiently robust to operate as a store of value (eg in the case of cryptocurrencies such as bitcoin) or providing an indisputable record, for example, relating to securities transfer.

Blockchain is a decentralized system, created and maintained by users of the network rather than being dependent on any central or third-party intermediary. It may be public and open ('permissionless' or 'unpermissioned') or structured within a private group ('permissioned').

Permissionless blockchains include bitcoin and ethereum, in which anyone can set up a node that once authorized can validate, observe and submit transactions. The identities of the participants are not known (other than the unique and random identities known as an 'address'). Permissioned ledgers restrict participation in the network and only the specific participants are given access and are known within the network. The network is private, and only organizations that have been authorized can participate and view transactions.

WHAT ARE SMART CONTRACTS AND DECENTRALIZED AUTONOMOUS ORGANIZATIONS (DAOS)?

Developments in blockchain are also providing an ability to transfer and rely on instructions verified within the electronic system in the form of so called 'smart contracts'. These contracts have been converted into code and are then executed and enforced by the blockchain network on the occurrence of an event. This reduces the need for intermediaries to collect, store and act on communicated information.

Smart contracts are essentially pre-written computer codes which are stored and replicated on distributed ledger platforms such as blockchain. Execution takes place over the network, eliminating the need for intermediary parties to confirm the transaction, leading to self-executing contractual provisions. These contracts can be as simple as moving a balance from one account to another or advanced more-complex interactions with the outside world using so called 'Oracles'. With Oracles, the contract code consults with a service outside of the blockchain network to make a decision. This may entail receiving a confirmation that an event has occurred, such as payment, which automatically executes a further step in the contract, such as the transfer of an asset, which might be in digital form or by delivering instructions to a person or warehouse to release the asset for delivery.

DAOs are essentially online, digital entities that operate through the implementation of pre-coded rules. These entities often need minimal to zero input into their operation and they are used to execute smart contracts, recording activity on the blockchain. DAOs can be particularly challenging to regulate, depending on their software engine, the nature of transactions they are completing or other unique features. Questions of ownership and responsibility for resulting acts of DAOs can also be brought to question if any technical issues arise with their operation.

WHAT IS A CRYPTOCURRENCY?

The Financial Technology Law bill (*Ley de Tecnología Financiera* or LTF) that regulates the FinTech industry in Mexico, indicates that virtual assets, including cryptocurrency, will be defined by Mexico's Central Bank. However it is understood that these virtual assets will be a representation of verifiable digital value that is neither issued nor backed by a central bank or financial entity; that is, they are not legal tender, however they generate units for exchange, given its acceptance by the general public. The oldest and best-known cryptocurrency is bitcoin (itself based on the bitcoin platform) although many other cryptocurrencies now exist. For example, the most widely-known alternatives to bitcoin include ether based on the ethereum platform and litecoin (these cryptocurrencies are now actively traded with a large developing infrastructure for holding, pricing and exchanging currency).

Initial coin offerings and token-based products

WHAT IS AN INITIAL COIN OFFERING (ICO)?

ICOs are a form of digital currency or token using blockchain technology. ICOs are often a means by which funds are raised for a new blockchain or cryptocurrency venture (the market for ICOs is currently booming). ICOs come in a wide variety of forms and may be used for a wide range of purposes. Some forms of ICOs may be directed at customers or suppliers as a form of loyalty program or a form of access or purchasing power (preferential or otherwise) in respect of assets of the issuer's business. Other forms may be more focused on raising initial funding. It is essential to examine the legal and regulatory basis for any ICO, as an unauthorized offering of securities is illegal and may result in criminal sanctions in a number of jurisdictions. Legal analysis of the underlying token will determine if it should be treated as a specified investment or form of regulated security or is more appropriately a form of asset that is not itself subject to the regulatory regime.

Typical attributes provided by tokens will include:

- access to the assets or features of a particular project;
- the ability to earn rewards for various forms of participation on the platform; and
- prospective return on the investment.

Key aspects to consider will include the:

- availability and limitations on the total amount of the tokens;
- decision-making process in relation to the rules or ability to change the rules of the scheme;
- nature of the project to which the tokens relate;
- technical milestones applicable to the project;
- basis and security of underlying technology;
- amount of coin or token that is reserved or available to the issuer and its sponsors and the basis of existing rights;
- quality and experience of management; and
- compliance with law and all regulatory requirements.

The nature of the business and the purpose and structure of the token offering will typically be set out in a white paper available to potential purchasers.

Artificial intelligence and robo advisory systems

Automated financial advice tools, also known as 'robo advisors' are software tools driven by artificial intelligence (AI) that provide a variety of investment advice services, from portfolio selection to personal finance planning. The systems are generally operated on a platform /personal dashboard basis; a user can input a set of personalized data to be processed by the AI algorithms which produce optimized outcomes around specified parameters. Although generally of application in the asset management sector, AI and automated advice tools also impact in the banking and private wealth advisor sectors; the implications include decreased human involvement, although recent trends have included a growth in popularity of hybrid structures which combine AI and human inputs.

Data analysis and cloud computing

Cloud computing enables delivery of IT services through internet-based tools and applications, rather than direct connection to a physical server. Cloud-based storage makes it possible to save masses of data to remote servers, accessible through the internet rather than by way of a physical connection. With the vast data processing and storage capabilities offered by cloud computing technology and virtually no infrastructure barriers to entry, there are a number of applications in building and running FinTech businesses and the technology has had a significant impact in recent years.

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Are there any restrictions, specific laws, regulations or procedures that apply to FinTech products?

General financial regulatory regime

Financial Technology Institutions Law (*Ley de Tecnología Financiera* or LTF) was published on March 9, 2018, in the Official Gazette of the Federation.

GENERAL

FinTech companies in Mexico will need to be analyzed carefully to verify whether it falls under the scope of financial regulations requiring such activities to be carried on by authorized and supervised entities. Relevant regulations include those relating to banking, securities brokerage, insurance, and fund formation, among other services.

The *Comisión Nacional Bancaria y de Valores* (CNBV) supervises and regulates all entities in the Mexican financial system –including banks, non-bank finance companies, stockbrokerage houses, and mutual funds – in order to ensure its stability and proper operation as well as to protect the interests of the general public. Most financial entities require authorization for incorporation from CNBV (in some cases with an opinion from Mexico's Central Bank – *Banco de México* or BANXICO).

REGULATORY DEVELOPMENTS

The main elements of the Financial Technology Institutions Law (*Ley de Tecnología Financiera* or LTF) are:

- **principles** – financial inclusion, consumer protection, financial stability, promotion of competition and prevention of money laundering and financing of terrorism;
- **regulated Financial Technology Institutions (FTIs)** –
 - crowdfunding institutions (*instituciones de financiamiento colectivo*);
 - electronic payment institutions (*instituciones de fondos de pagos electrónicos*); and
 - regulatory sandboxes/innovative companies (*empresas innovadoras*);
- **authorization of FTIs** – to be granted discretionally by the CNBV, with prior approval by the Financial Technology Committee which will be formed by officers of BANXICO, CNBV and the Ministry of Finance;
- **corporate governance** – FTIs will have to be incorporated as Mexican stock corporations (*sociedad anónima* or SA) or limited liability companies (*sociedad de responsabilidad limitada* or Sde RL) in order to provide services in Mexico (CNBV will issue regulations on board of directors, officers and committee requirements for FTIs);
- **regulatory sandbox** – innovative companies that obtain a temporary authorization (up to two years) to provide services to a reduced number of clients to test innovative products, services, business models and delivery mechanisms; and
- **a Fintech Council** – the draft bill provides for the creation of a FinTech Council to act as a means of consultation, advice and coordination between public and private sectors.

Crowdfunding institutions

The LTF defines crowdfunding institutions as those that regularly and professionally carry out activities with the purpose of connecting an investor (funds provider) and an applicant (funds requester), through interfaces, websites or any other digital or electronic means of communication.

Crowdfunding institutions may perform the following activities:

- **debt-based crowdfunding** – loans or any other type of financing by investors resulting in a direct or contingent liability of applicants;
- **equity-based crowdfunding** – acquisition on instruments by investors representing the capital stock of applicants; or

- **royalty-based crowdfunding** – acquisition by investors of a portion or share of a present or future asset, or the income, profits, royalties or losses resulting from projects developed by applicants.

Electronic payment institutions

The LTF defines electronic payment institutions as those institutions which regularly and professionally carry out activities through interfaces, websites or any other digital or electronic means of communication, consisting in the issuance, management, redemption and transfer of electronic payment funds, by opening accounts for their clients to make deposits in exchange of electronic payment funds, making transfers to different accounts, and delivering money in amounts equivalent to the electronic payment funds withdrawn from the relevant account.

Electronic payment funds will be those funds that:

- are linked to monetary value equivalent to an amount in Mexican pesos or virtual assets;
- result in a payment obligation against the electronic payment institution;
- are issued against receipt of an amount of money or virtual assets; and
- are accepted by a third party as money or virtual assets.

Application of data protection and consumer laws

Pursuant to the Federal Law on Protection of Personal Data Held by Private Parties (*Ley Federal de Protección de Datos Personales en Posesión de los Particulares* or Privacy Law), in the processing of personal data, the person or entity collecting personal data (data controller) must provide a privacy notice (*Aviso de Privacidad* or the Privacy Notice), which must be made available to the data owner prior to the processing of his or her personal data.

The term 'processing' is broadly defined in the Privacy Law to include the collection, use, communication, or storage of personal data by any means. Use includes all access, management, procurement, transfer and disposal of personal data.

Consent is required for all processing of personal data, except as otherwise provided by the Privacy Law. Implicit consent (notice and opt out) applies to the processing of personal data; express consent (notice and opt in) applies to the processing of financial or asset data; and express and written consent applies to the processing of sensitive personal data. Consent may be communicated verbally, in writing, by electronic or optical means, via any other technology, or by any other unmistakable indications. Express written consent may be obtained through the data owner's written signature, electronic signature, or any other authentication mechanism set up for such purpose.

The Financial Services Consumer Protection Law (*Ley de Protección y Defensa al Usuario de Servicios Financieros*) and the Federal Law on Consumer Protection (*Ley Federal de Protección al Consumidor*) provide that product information and fees must be available to consumers.

Money laundering regulations

The Mexican anti-money laundering law (*Ley Federal para la Prevención e Identificación de Operaciones con Recursos de Procedencia Ilícita*) and its regulations apply to FinTech entities performing activities listed in such law as vulnerable activities. FinTech entities which fall within the scope of the regulations are required to verify the client's identity, any beneficiaries of transactions, register with the regulators and file monthly reports, among other requirements.

The LTF proposes that full identification of investors and applicants will be required and will further require FTIs to only use banks accounts with authorized financial institutions to receive and transfer funds to their clients and the use of cash would be limited to specific situations authorized by CNBV, taking into account the particular business model of the FinTech entity and the establishing of appropriate limits.

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What type of funding arrangements and incentives are available to FinTech businesses?

Early stage

SEED INVESTMENT

Initial investment in FinTech businesses may be provided by family and friends of the founders and other high-net-worth individuals (often known as angel investors) in return for an equity stake. Such seed investment is often used to fund the establishment and early growth of the business before larger investment is available. The investing individuals may also provide know-how and expertise to assist in the company's development. The seed investors would typically not require the same controls over the business as, for example, venture capital providers.

CROWDFUNDING

The crowdfunding sector may be appropriate for a FinTech business in the early stages. It involves members of the public investing in a business by pooling their resources through an intermediary platform, such as Crowdfunder.mx and Play Business.

There are two main types of crowdfunding: equity and reward-based.

- Equity crowdfunding involves company shares being given in exchange for investment in the business.
- Reward-based crowdfunding provides investors with a tangible benefit, such as early access to a platform or application that the business is developing.

Crowdfunding offers a large number of private investors an opportunity to make small-scale investments in early-stage businesses to which they may otherwise not have had access.

ACCELERATORS

There are various incubators or accelerators in the Mexican market which offer support, facilities and funding for startups, often in return for an equity stake. For example, the Startup Bootcamp Fintech has an accelerator program which offers entrepreneurs free office space, mentorship, global network access, and funding. It is a joint venture between Startupbootcamp and Finnovista (another leading platform for accelerating FinTech innovation in Latin America); and they are supported by leading institutions such as Visa, BanRegio, Gentera and EY.

In early 2013, the Mexican Government created the National Entrepreneur Institute (*Instituto Nacional del Emprendedor* or INADEM), an administrative body within the Ministry of Economy specifically aimed at developing a stronger entrepreneurial ecosystem. INADEM administers the National Entrepreneur Fund (*Fondo Nacional Emprendedor*) which is open to support FinTech companies. Some states in Mexico also provide certain incentives and have their own entrepreneurship institutes providing different types of support to the FinTech sector.

Venture capital and debt

Venture capital funding is a type of equity investment usually targeted at early stage FinTech companies with an established business and some trading history. Venture capital provides a viable alternative to traditional lending given that the business is unlikely to have the tangible asset base or long track record needed to attract traditional debt funding from financial institutions. There are various examples of Mexican FinTech companies receiving venture capital, such as Kueski (lending platform), Konfio (lending platform), Clip (payment processor platform) and Kubo Financiero (peer-to-peer (P2P) lending platform).

Corporate venture capital (CVC) is a type of venture capital and involves an equity investment by a corporate fund. The benefit of having a CVC as an investor for a FinTech startup is that the fund is able to share its knowledge and expertise of the FinTech sector with the company and act as an advisor. Some of the big corporates in Mexico have started to follow this global practice, albeit through accelerators. Companies such as Telefónica, Cinépolis, Volaris, Axtel, Coca-Cola, Grupo Expansión, Hoteles City Express, Ternium, and Banregio have established initiatives to interact with startups. An active player in Mexico is Telefonica's Wayra.

An additional funding option is venture debt, which is secured against a company's assets and includes an equity element allowing the debt provider to purchase shares in the company. However, venture debt providers will usually only invest into companies that have already received investment through venture capital. This alternative is still not common in the FinTech sector in Mexico.

Warehouse and platform funding

Warehouse financing may be suitable for FinTech companies which own a portfolio of assets. Funding is often provided by way of a loan from a small number of lenders to a special purpose vehicle (SPV). The loan is secured on the assets acquired by the SPV from the originator. The lenders will only fund a portion of the assets, with the remainder being financed by way of subordinated lending from the originator. Some FinTech companies may see warehouse funding as a temporary form of financing to be followed by a larger capital markets transaction at a later date. This alternative is still not common in the FinTech sector in Mexico.

Another alternative form of funding is by way of P2P lending platforms such as Kubo Financiero, Prestadero and Doopla, which bring individual borrowers and lenders together without the involvement of traditional banks. P2P lending does not involve equity investments; interest is paid on the money borrowed instead.

Senior bank debt and capital markets funding

SENIOR BANK DEBT

Once a FinTech company is established and has a track record, bank debt becomes a more viable source of funding, either on a secured or unsecured basis depending on the creditworthiness and asset base of the business. In contrast to capital markets funding which is often covenant-lite, bank funding will generally involve the imposition of financial covenants and controls that will apply over the life of the facility. Bank finance may be particularly important for working capital, overdraft, accounts management and general liquidity purposes.

CAPITAL MARKETS FUNDING

Mexico has both debt and equity capital markets which are accessible to businesses (usually of a certain size).

Raising finance by way of an Initial Public Offering (IPO) has not been a funding option for FinTech companies in Mexico given that they have not reached the size required for an IPO to become available. An IPO is the initial sale of company shares on a public exchange, such as the Mexican Stock Exchange (MSE), currently the only stock exchange operating in Mexico. On 29 August 2017, the Mexican Ministry of Finance and Public Credit (*Secretaría de Hacienda y Crédito Público*) granted *Central de Corretajes* (CENCOR) a new concession to operate a new stock exchange in Mexico, which will operate under the name of *Bolsa Institucional de Valores* (BIVA) and will be supported technologically by NASDAQ. It is anticipated that BIVA will initiate operations in early 2018. It is expected that BIVA will be targeting smaller companies than those listed in the MSE, providing better chances for IPO funding to FinTech companies in Mexico.

FinTech companies in Mexico have not explored funding alternatives through debt capital markets, although there are various alternatives available, such as bonds and securitizations.

CONVERTIBLE BONDS/LOAN NOTES

A funding tool for fast-growing FinTech businesses is to issue convertible bonds or loan notes, which are essentially a hybrid between debt and equity. Convertible instruments begin as a loan accruing interest and are convertible into shares in the issuing company at prescribed prices in certain circumstances. Mexican FinTech companies have started to explore this funding alternative, such as Kueski, a leading online lending platform in Mexico.

Incentives and reliefs

The Mexican Income Tax Law provides a 30% tax credit for research and development (R&D) expenses, including investments in R&D. The tax credit will be equal to current-year R&D expenses in excess of the average R&D expenses incurred in the previous three years. This incentive cannot be combined with other tax incentives.

There is a wide variety of targeted incentives that encourage specific types of economic development, however, FinTech-specific incentive programs are scarce. Prosoft is an initiative aimed at developing a strong, competitive, and global IT sector in Mexico, by supporting companies from strategic sectors to develop innovation ecosystems through collaborations among private sector, government, and the academic sector. The initiative is managed by the Ministry of Economy and provides cash grants for up to 70% of eligible expenses.

Local governments also provide certain incentives that are available to FinTech companies in Mexico.

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Portfolio sales

Loan transfers and portfolio sales

What are common ways of buying and selling loans?

Buying and selling loans is very common. A loan can be sold on an individual basis or packaged up with other loans and sold as a portfolio pursuant to overarching terms.

The most common way of selling loans is through an assignment of all of the assignor's rights and obligations under the corresponding loans, including any promissory notes documenting disbursements (or its substitution).

Participations in loans are also common as a way of lenders transferring an economic interest in a loan but not changing the legal relationship between the existing lender and borrower under a loan agreement.

The form and content of the transfer documentation will depend on the nature of the loans being sold. It is customary for the parties to include a template of assignment agreement as an exhibit to the loan agreement.

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What are the main considerations when transferring a loan and related security?

There are a number of issues to consider before transferring a loan or portfolio of loans. These issues are often covered as part of a due diligence exercise by the seller's legal advisors. Some of the key considerations include:

- **confidentiality** – whether the seller of the loan is allowed to disclose information relating to the loan to a potential purchaser;
- **data protection** – whether there is any personal data or other restricted information in the loan that should not be disclosed to a potential purchaser;
- **lender eligibility** – whether there are any restrictions around the type of entity to which the loan can be transferred;
- **undrawn commitments** – whether there are any continuing obligations for further funding or other material obligations on the part of the lender that may fall on the transferee or reduce claims made by the transferee;
- **transfer mechanics** – whether there are any steps that need to be taken to transfer the loan in accordance with its terms; and
- **consent** – whether a transfer requires the consent or notification of any other parties.

Last modified 5 Dec 2019

Projects

Financing / investing in energy / infrastructure

To what extent are energy and infrastructure assets publicly or privately owned?

Generally

The ownership of energy and infrastructure assets in Mexico varies according to the asset class. Subsurface rights belong to the Mexican state and the Mexican government may grant concessions to use subsurface land for mining, oil and gas drilling and production or for geothermal exploration and production, among others.

Energy

Deriving from a comprehensive Energy Reform in 2013, which involved changes at both constitutional and secondary legislation levels, a new legal framework was put in place for the energy sector.

Underground hydrocarbons, including oil and gas, are government-owned property and no private property in hydrocarbons is allowed. However, deriving from the Energy Reform, oil and gas activities such as exploration, production, treatment, refining, processing, storage, transportation and commercialization, were opened to the private sector. Private sector companies are now allowed to participate in exploration and extraction activities and ownership of extracted hydrocarbons is permitted in production sharing and license contracts, in which part of the production is given to the contractor. Owners of land where underground hydrocarbons are discovered are entitled to remuneration from commercial production of the discovered wells. The Hydrocarbons Law provides that landowners may receive a percentage of the contractor's profit. *Petroleos Mexicanos* (Pemex), the state-owned petroleum company, continues to participate in the sector but as an additional player within the blocks awarded to Pemex through entitlements, which provide Pemex the right to explore and/or produce hydrocarbons directly, or through farm-outs or PPPs.

The Electric Industry Law allows the private sector to participate freely in the generation and sale of electricity and the construction of transmission and distribution infrastructure, while maintaining the electricity grid under the operational control of the Federal Electricity Commission (CFE), the state-owned public utility. The new legal framework has created a wholesale electricity market operated by the National Centre for Energy Control (CENACE) as a single independent system operator for the entire grid. Market participants are now able to sell and purchase power directly in the market or through bilateral PPAs, including those awarded through auctions. Operational control of the national grid and the transmission and distribution of electricity are considered strategic areas that remain in the hands of the Mexican government. However, the private sector is able to participate in the transmission and distribution of electricity through agreements and joint ventures with state-owned enterprises. CFE is permitted to participate, through separate subsidiaries, in the different market activities, and is the supplier of basic retail services to residential customers and small and medium-sized commercial customers under regulated tariffs. Nuclear power generation remains under the control of the Mexican government.

Telecoms infrastructure

The legal framework for the telecoms and broadcasting sectors is set out in the in the new Federal Law of Telecommunications and Broadcasting (*Ley Federal de Telecomunicaciones y Radiodifusión*) (FLTB), which came into force on August 2014. The FLTB states that telecommunications and broadcasting activities are a 'public service of general interest', and that the government will at all times maintain the ownership of the radio spectrum. The Federal Government may grant two types of concessions to private sector companies:

- 'all-inclusive concessions', which authorize concessionaires to provide all sorts of telecommunication or broadcasting services through their network and that according to their use may be classified as commercial, public, social or private; and
- concessions to use radio-electric spectrum or orbital resources.

Transport infrastructure

RAIL

Mexican railway lines are owned by the government, which means that only the state can build new railway links. However, the rail service was privatized about 20 years ago dividing the country's railways into different regions and putting them under private management through concessions for up to 50 years.

URBAN RAIL TRANSIT

- **Mexico City Metro System** – owned and operated by the Mexico City Government
- **Monterrey Metro System** – owned and operated by the Government of the State of Nuevo León
- **Xochimilco Light Rail** – owned and operated by the Mexico City Government
- **Guadalajara Light Rail** – owned and operated by the Government of the State of Jalisco
- **Suburban Railway of the Valley of Mexico Metropolitan Area** – owned by the Federal Government, built and operated by private sector company under a 30-year concession, and required the collaboration of the Federal, Mexico City, State of Mexico and municipal governments
- **Interurban Train Mexico City–Toluca (under construction)** – owned by the Federal Government, in collaboration with the Mexico City Government, its construction is by private sector companies through public works contracts

ROADS, BRIDGES AND TUNNELS

The highway system of Mexico is made up of federal highways, state highways, and rural roads. Federal highways are those that connect with roads from foreign countries, link two or more states of the Federation, and are wholly or mostly built by the Federation with federal funds or through federal concessions by individuals, states, or municipalities. State highways and rural roads are the responsibility of state governments.

Caminos y Puentes Federales de Ingresos y Servicios Conexos (CAPUFE), a government agency under the Ministry of Communications and Transportation (SCT), is in charge of the operation and maintenance of federal roads and bridges, including those under concessions granted to third parties that engage CAPUFE for such services.

AVIATION

Aviation for the most part is privatized in Mexico. However, the administration, control and surveillance of airports is restricted to the federal government. There are certain public bodies (such as *Aeropuertos y Servicios Auxiliares* – ASA) that participate either with another authority (ie state government) or with the private sector to build, maintain and operate airports across Mexico. Other airport facilities are operated by the Ministry of Defense, the Navy and municipal authorities.

PORTS

Mexican port privatization started in 1993 with a new Ports Law which dismantled the public port agency (*Puertos Mexicanos*) and created Independent Port Administrations (*Administraciones Portuarias Integrales* – APIs) at each port or group of small ports. APIs are commercial entities controlled by the federal government, the state governments, the National Tourism Fund, and in one case by private capital. Every activity related to port administration, operation and services is under supervision of the federal government, however, APIs are granted concessions for the use and management of ports and can themselves transfer rights or grant specific services contracts to private sector terminal operators in order to supply port services. The *Coordinación General de Puertos y Marina Mercante*, under the authority and supervision of the Ministry of Communications and Transportation, has the authority on regulation and administration of ports in Mexico.

Other infrastructure

SOCIAL INFRASTRUCTURE

Most of the social infrastructure is financed by federal or state governments. In particular, public hospitals, prisons and schools are managed by the Ministry of Health, Ministry of Interior, and the Ministry of Education, respectively. However, for the design, construction and maintenance, the relevant authority will enter into an agreement with the private sector through a bidding process or a public-private partnership. For social housing, in broad terms, the private sector develops the real estate projects for social housing (either by private or public funding), then employees obtain a mortgage from the National Workers' Housing Fund Institute (*Instituto del Fondo Nacional de la Vivienda para los Trabajadores*) (INFONAVIT) to be repaid with payroll deductions that employers make and forward to INFONAVIT, as well as mandated contributions that employers make to INFONAVIT as a percentage of each worker's salary.

DEFENSE

Generally, defense assets are owned by the federal government.

WASTE

The waste management is the responsibility of each local government. The municipal authorities grant concessions to private companies for waste management. The private sector is responsible for the collection, management, transportation and disposal of the waste once it has obtained the concession.

WATER

The main infrastructure projects such as water dams, river diversions, wastewater and waterways are controlled by the *Comisión Nacional del Agua* (CONAGUA), a federal body under the supervision of the Ministry of Environment and Natural Resources (SEMARNAT). The construction and maintenance of such assets can be given to the private sector through concessions. For city distribution of water and waste-water (sewerage), each city has its own government body that is in charge of the administration, maintenance and distribution to the end-user. However, there are few cities where water supply and sanitation services are provided by private companies through concessions.

Last modified 5 Dec 2019

Are there special rules for investing in energy and infrastructure?

Generally

There is no specific regime governing or restricting investment in energy or infrastructure projects in Mexico over and above existing regulation for investors and lenders more generally but a particular proposed investment may be subject to legislative or regulatory control (eg merger control rules) and/or foreign investment restrictions. As regards the planning and implementation of the underlying energy or infrastructure project (in which the investment is to be made), the legal/regulatory position relevant to that project must be considered, including environmental authorizations/permits and/or sector specific regulatory consents or licenses. If a public body is procuring a project using private finance, and the public body is to benefit from central government funding towards the cost, the project will be subject to central government approval. Key sector-specific issues are flagged in the sections below.

Whether an investor can invest will depend on the terms of the procurement of that project if it is a public sector project and, in respect of an existing/operational project, that will depend on whether there are any contractual restrictions on 'change of control'. This is less of a concern with private sector infrastructure although investors would need to consider whether any licenses/consents/permits would be affected by their acquisition of an interest.

Energy

Private investors can participate, alongside PEMEX and CFE, the two large state-owned enterprises, in a wide range of the energy industry value chain, attracting capital and technology to areas that are in need of renewal. A cornerstone of the energy reform is the objective to open the energy sector to private and international investment by ending the monopolies of state-affiliated enterprises.

The energy reform has opened five ways in which private investors can take part in the development of Mexico's oil and gas resources, in all cases after pre-qualification and taking part in a bidding process conducted by the *Comisión Nacional de Hidrocarburos* (CNH), except that service contracts can be agreed directly with PEMEX:

- License contracts allow a company to book ownership of oil or gas assets (for financial purposes) at the wellhead after it has paid its tax dues, with the company paying a signing bonus, payments during exploration and royalties on production.
- Production-sharing contracts allow a company to recover costs and a share of the operating profit, received as a portion of the oil or gas extracted.
- Profit-sharing contracts allow a company to recover costs and a share of the profit, after it has marketed and sold the resource.
- Under service contracts a company is paid for specified project activities on behalf of PEMEX or the state.
- Farm-outs/migrations allow a company to enter into a joint venture agreement with PEMEX in a project that has already seen exploration and production efforts.

The public transmission and distribution of electric energy is still reserved to the state, provided by CFE and overseen by the new regulatory body, the National Energy Control Centre (*Centro Nacional de Control de Energía*) (CENACE). CENACE is the operator of the national electric system and wholesale market operator, however, CENACE can authorize private parties to participate in energy distribution. To incentivize investment in renewables, the government has introduced clean energy certificates, a market instrument that is part of broader power sector reform designed to support the share of electricity consumption to be generated from clean energy sources. The revenue from the sale of certificates, which are purchased by producers and large electricity consumers, is intended to be invested in other renewable energy projects.

Telecoms infrastructure

Foreign investment is authorized with no restriction for telecommunications and satellite communications and up to 49% for radio broadcasting services.

The Federal Institute of Telecommunications (IFETEL) was created by virtue of the Telecommunications Reform as an independent regulator with the authority, among other matters, to award and revoke concessions, guarantee economic competition in the

telecommunications and broadcasting markets, and determine the existence of 'dominant carriers' (participants with market participation above 50% in both the broadcasting and telecommunications sector) to whom asymmetric regulation is to be applied (currently, America Móvil in telecommunications and Televisa in broadcasting, have been deemed 'dominant carriers' by IFETEL).

Transport infrastructure

DOMESTIC PASSENGER, TOURISM AND FREIGHT TRANSPORTATION

Pursuant to the Foreign Investment Law, activities such as domestic passenger, tourism and freight transportation (except for messenger or package delivery services) is restricted to Mexican individuals or Mexican companies without allowing foreign investment (a neutral investment mechanism may be implemented to allow foreign investment where limited voting shares are issued to foreign investors).

AVIATION

Pursuant to the Foreign Investment Law, domestic air transportation services are subject to a foreign investment limit of 25%. The concessions and permits are granted pursuant to the Civil Aviation Law. Other foreign investment limitations apply.

SHIPPING

Pursuant to the Foreign Investment Law, national commercial freight shipping lines and port administration are activities subject to a foreign investment limit of 49% (a neutral investment mechanism may be implemented to allow foreign investment where limited voting shares are issued to foreign investors). Other foreign investment limitations apply.

RAIL

The Mexican government allows foreign investors to participate with up to 49% of the capital stock in companies providing railway service. Railroad activity with more than 49% foreign participation requires prior authorization from the Foreign Investment Commission.

Other infrastructure

On publicly procured infrastructure, it is quite common for long-term projects to have a 'change of control' clause which restricts change in ownership structures of the private sector. For example, in most sectors there is a restriction on change in control during the construction period but this is often relaxed post construction provided any change in control is not to an 'unsuitable third party'. How strict these restrictions are will often depend on the sector.

Last modified 5 Dec 2019

What is the applicable procurement process?

Public procurement in Mexico is governed at a federal level by the Federal Law for Acquisitions, Leasing and Services for the Public Sector (*Ley de Adquisiciones, Arrendamientos y Servicios del Sector Público*) and their corresponding laws in the different states and municipalities.

As part of the Energy Reform, CFE and Pemex have their own procurement regulations and the general law mentioned above does not apply to such governmental entities. The *Ley de Petroleos Mexicanos* and the corresponding procurement regulations issued by its Board of Directors are applicable to Pemex, and the *Ley de la Comisión Federal de Electricidad* and the corresponding procurement regulations issued by its Board of Directors are applicable to CFE.

Investing in energy and infrastructure

Public procurement is relevant where the Mexican government, or a branch of it, seeks to outsource delivery of a new project. On an infrastructure project, a potential investor would have to bid in its own capacity or as part of a consortium to deliver the overall deal which could include design, build, operation, maintenance and financing of the relevant energy or infrastructure asset. The relevant procurement legislation (as indicated above) applies to certain public bodies, such as federal government departments, and state and municipal authorities.

Public contracting may be carried out by any of the following:

- open bidding procedure (*Licitación Pública*);

- invitation to at least three participants; and
- direct adjudication.

The general rule for public contracting is to perform an open bidding procedure; however, applicable regulations expressly provide for exceptional cases under which the corresponding government bodies may observe a different procedure. There are three types of tender processes under federal regulations:

- National (reserved for Mexicans and Mexican products that contain at least 50% of its parts made in Mexico);
- International under international treaties (reserved for Mexicans and foreigners that are nationals from a country with which Mexico has a Free Trade Agreement and contains provisions for public procurement); and
- Open Internationally (open to Mexicans and foreigners irrespective of the origin of goods).

An investor may choose to seek to invest in a project (by acquiring an interest in a private sector partner) that has already been procured and is operational. However, such investments are controlled by contractual mechanisms within the original awarded contract rather than procurement regulations themselves and the parties are required to confirm whether legal thresholds under the Mexican Antitrust Law (*Ley Federal de Competencia Económica*) are exceeded, in which case the transaction would have to be notified to the Mexican Antitrust Commission (*Comisión Federal de Competencia Económica*) and obtain clearance before closing.

Financing energy and infrastructure

On a publicly procured contract, the public sector may have prescribed requirements on the funding arrangements. Following entry into the contract, the main tool for controlling the financing is that, typically, on project finance deals, a refinancing of the senior debt will require the consent of the public sector.

In the case of public contracts financed from externally sourced credit granted to the federal government or guaranteed by regional or multilateral financial organizations, the procedures, requirements and other provisions for their contracting are established by the Ministry of the Civil Service (*Secretaría de la Función Pública*), with the opinion of the Ministry of Finance and Public Credit (*Secretaría de Hacienda y Crédito Público*).

Last modified 5 Dec 2019

What are the most common forms of funding / investing in energy and infrastructure?

The principal forms of private sector funding/investment in energy and infrastructure in Mexico (including in relation to Public-Private Partnerships) include the following.

Funding

- Loans made on a corporate finance basis (balance sheet debt)
- Loans made on a project-finance basis (to a special purpose project company) on medium- to long-term bases – such loans may later be syndicated to other funders
- Bond finance
- Fibra E public offering (equity)
- Mezzanine debt (in some sectors)
- Refinancing of the debt in operational projects

Mexico's National Infrastructure Fund (*Fondo Nacional de Infraestructura* – FONADIN) has been a dynamic Mexican government tool to manage the development of national infrastructure in Mexico via public-private partnerships (PPPs), focusing on the highways, ports, airports, environment, urban mass transportation, water and tourism. FONADIN is one of the most important conduits for PPPs in Mexico by providing support – financing and know-how – for the planning, design, construction and final transfer of projects developed by the private sector. To be eligible for FONADIN support, projects must offer the country significant positive social impact and the prospect of major economic gain.

Investing

- 'Equity' investment in special purpose vehicles or entities that may have a portfolio of interests, ie share capital and subordinated sponsor loans
- Secondary market investment in operational projects (acquisition of 'equity')

Last modified 5 Dec 2019

Restructuring

Enforcement and sanctions

When can there be regulatory investigations?

When the National Banking and Securities Commission (CNBV) or the National Commission for the Protection and Defense of Users of Financial Services (CONDUSEF), considers that an authorized firm or regulated individual may have breached ongoing compliance requirements, it will launch a formal investigation. This may result in regulatory sanctions.

Last modified 5 Dec 2019

What regulatory penalties may apply?

When a rule breach has taken place, the National Banking and Securities Commission (CNBV) or the National Commission for the Protection and Defense of Users of Financial Services (CONDUSEF) may impose a financial penalty or censure, or withdraw regulated status against the firm and/or regulated individuals. The regulator will publicize these penalties.

Last modified 5 Dec 2019

What criminal penalties may apply?

Following formal investigation, the regulators have powers to impose criminal penalties in certain cases, including:

- insider dealing and misleading statements and practices;
- breaches of Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT) Regulations; and
- conducting regulated activities when not authorized.

Last modified 5 Dec 2019

Tax

Tax issues

Are stamp, registration, transfer or other similar taxes applicable?

Are there stamp, registration, transfer or other similar taxes payable on the advance, transfer or assignment of a loan?

There are no stamp, registration, transfer or other similar taxes payable on the advance, transfer or assignment of a loan.

Are there stamp, registration, transfer or other similar taxes payable on the taking, transfer or assignment of a mortgage, debenture or other security?

Most security interests must be registered at the Public Registry of Property and Commerce to ensure its validity against third parties. The fees payable for such registrations are generally not material in amount.

Are there stamp, registration, transfer or other similar taxes payable on the issue, transfer or assignment of a debt security (eg a bond)?

There are no stamp, registration, transfer or other similar taxes payable on the issue, transfer or assignment of a debt security.

Last modified 5 Dec 2019

Do tax authorities take priority on enforcement?

On the enforcement of security, do tax authorities take priority over secured lenders or secured debt security holders (eg secured bond holders)?

Secured lenders and secured debt security holders take priority over the Mexican Tax Authorities on enforcement of security.

Last modified 5 Dec 2019

Is withholding tax on interest payments applicable?

Is there withholding tax on interest payments under a loan?

Yes, to the extent the interest is paid to a person who is not resident in Mexico. An expanded definition of interest applies for these purposes, which includes yields from all forms of credit, public debt, bonds or debentures. Interest payments between persons resident in Mexico are not subject to withholding taxes.

In addition, income deriving from the sale of a right to a receivable of any nature, whether present, future or contingent, by a person who is resident in Mexico to a person who is not resident in Mexico, is also taxed as interest. The amount of deemed interest income in the hands of the non-resident acquirer is determined as the difference between the nominal value of the receivable plus unpaid interest or returns that have not been subject to withholding tax, less the price paid on the sale. As such, the purchase of bad loans by a non-resident could be subject to withholding tax on the difference between the face value and the fair market value of the loans.

If so:

What is the rate of withholding?

The general Mexican withholding tax rate on interest paid to persons not resident in Mexico is 35% (with effect from 2014), unless an exception applies.

What are the key exemptions?

The following types of interest payments are exempt from Mexican withholding tax:

- interest paid on loans to the Mexican Federal Government;
- interest paid on loans with a term of three or more years granted by financial entities resident outside of Mexico and registered with the Mexican tax authorities that are dedicated to the promotion of exports by the provision of special-term loans (thus, for example, to the extent assets and equipment produced outside of Mexico can be financed by way of an export credit loan, Mexican withholding tax may be avoided on the interest payable on the loans);
- interest derived from certain financial debt derivative transactions involving the sale of federal government securities; and
- interest derived from the sale of monetary regulation bonds issued by the Bank of Mexico.

The withholding tax rate is reduced to the following percentages in the following cases:

- 4.9% – interest paid to a financial entity resident outside of Mexico in which the Mexican Federal Government has an equity participation through the Ministry of Finance (SHCP) or the Mexican Central Bank (Banco de Mexico), provided that the financial entity is the effective beneficiary of the payment and meets certain registration requirements;
- 10% – interest paid to an entity that invests or places capital in Mexico that is derived from securities that are issued outside of Mexico to, and placed outside of Mexico with, the general public;
- 10% – interest paid to a person not resident in Mexico that derives from the sale of a right to a receivable, or that is paid to a person not resident in Mexico on certain types of securities, provided specific requirements are met;
- 10% – interest paid to banks, investment banks and certain limited purpose financial companies, in each case, resident outside of Mexico, that are the effective beneficiaries of the interest (To qualify for the reduced rate, the institution concerned must provide information to the borrower to document its status as a qualified institution. It should be noted that the use of back-to-back loan arrangements as a means of obtaining reduced withholding tax rates is not allowed under Mexican domestic law. The rate is reduced to 4.9% in the case of interest on loans paid to financial institutions resident in double tax treaty partner countries. The reduced rate of 4.9% is provided for through general regulations on an annual basis.);
- 4.9% – interest paid on publicly traded securities or securities issued through a recognized stock exchange in a country with which Mexico has entered into a double tax treaty, where the securities are registered with the National Registry of Securities and Intermediaries, and certain information requirements are met (if the information requirements are not met or the securities are issued through an exchange in a country with which Mexico does not have a double tax treaty, the rate is 10%);
- 15% – interest paid to a lessor not resident in Mexico with respect to a finance lease (In this case, the interest is considered to be Mexican-source when the leased asset is used in Mexico, or when the payments made to the non-resident lessor are deductible in whole or in part by a permanent establishment in Mexico, even when the payments are made through an establishment located outside of Mexico.); and
- 21%
 - interest payments made by credit institutions to persons not resident in Mexico, other than registered banks;
 - interest related to the sale on credit of machinery and equipment; and
 - interest in connection with loans to finance the acquisition, installation and commercialization of fixed assets, provided the loan terms are documented in the contract and payment is made to an entity registered with the tax authorities for this purpose.

Furthermore, there could be reduced withholding tax rates available on interest payments to persons not resident in Mexico who are entitled to apply a double tax treaty concluded by Mexico.

Would the same analysis apply to interest payments under a debt security (eg a bond)?

Yes.

Last modified 5 Dec 2019

Are foreign lenders and debt security holders subject to tax on interest payments?

Will the lender be taxed on interest payments under a loan in the jurisdiction of the borrower (other than by way of the application of withholding taxes), assuming the lender is not otherwise resident in that jurisdiction for tax purposes (eg by virtue of incorporation, residence or local branch)?

No.

Would the same analysis apply to interest payments under a debt security (eg a bond)?

Yes.

Last modified 5 Dec 2019

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