FINANCIAL SERVICES M&A

Mexico



LEXOLOGY
Getting The Deal Through

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Quick reference guide enabling side-by-side comparison of local insights, including into the market and policy climate; key legislation; required regulatory consents and filings; ownership restrictions; directors and officers' issues; foreign investment restrictions; competition law and merger control issues; deal structures and strategic considerations; tax; ESG, public relations, political and policy risk management; shareholder activism; due diligence, including in relation to emerging technologies; pricing and financing; purchase price adjustments; deal terms (including reps and warranties, indemnities and closing conditions); dispute resolution; and current trends.

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Table of contents

MARKET AND POLICY CLIMATE

Market climate

Government policy

LEGAL AND REGULATORY FRAMEWORK

Legislation

Regulatory consents and filings

Ownership restrictions

Directors and officers – restrictions

Directors and officers – liabilities and legal duties

Foreign investment

Competition law and merger control

DEAL STRUCTURES AND STRATEGIC CONSIDERATIONS

Common structures

Time frame

Tax

ESG and public relations

Political and policy risks

Shareholder activism

Third-party consents and notifications

DUE DILIGENCE

Legal due diligence

Other due diligence

Emerging technologies

PRICING AND FINANCING

Pricing

Purchase price adjustments

Financing

DEAL TERMS

Representations and warranties

Indemnities

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Closing conditions

Interim operating covenants

DISPUTES

Common claims and remedies

Dispute resolution

UPDATE AND TRENDS

Trends, recent developments and outlook

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MARKET AND POLICY CLIMATE

Market climate

How would you describe the current market climate for M&A activity in the financial services sector in your jurisdiction?

Very active, particularly concerning fintech. The Mexican Financial Technology Institutions Law (the Fintech Law) allowed an important number of domestic and international players to start operating in Mexico. This has then generated significant M&A activity: on the one hand, consolidation of fintech companies and, on the other, fintech companies seeking further growth by acquiring other types of traditional financial services entities, such as banking institutions and securities brokerage houses. The latter case is a consequence not only of fintech companies expanding their services to traditional banking and securities clientele but also expanding their scope of operations beyond the several restrictions imposed by the Fintech Law. Recently there has been notable M&A activity in joint ventures focused on developing e-banking or international banks looking for banking licences as a quicker process than applying for a banking licence from scratch.

Law stated - 07 December 2022

Government policy

How would you describe the general government policy towards regulating M&A activity in the financial services sector? How has this policy been implemented in practice?

One of the main objectives of the government policy towards financial services M&A transactions is the proper identification of the potential shareholders of financial entities. The regulation and the regulators give special attention to the information and documentation disclosed by the acquirers during the processes held before the National Banking and Securities Commission. Shareholder information is a point of interest for the Mexican regulator, not only of who has control of the relevant financial entity, but also of the origin of the resources and to avoid those resources, if from illicit origin, ending up in the capital of financial entities.

Law stated - 07 December 2022

LEGAL AND REGULATORY FRAMEWORK

Legislation

What primary laws govern financial services M&A transactions in your jurisdiction?

The primary laws governing financial services M&A transactions in Mexico are the following:

- the Credit Institutions Law;
- the Securities Market Law;
- the Popular Savings and Credit Law;
- the Financial Technology Institutions Law;
- the Investment Funds Law;
- the Financial Groups Law;
- the General Provisions applicable to Credit Institutions;
- the General Provisions applicable to brokerage houses;
- the General Provisions applicable to Popular Savings and Credit Entities, Integration Organisms, Community

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Financial Companies, and Rural Financial Integration Organisms referred in the Popular Savings and Credit Law;
- the General Provisions applicable to Financial Technology Institutions;
- the General Provisions applicable to Investment Funds and persons who provide services to them; and
- the Rules for the establishment of Subsidiaries of Foreign Financial Entities.

Law stated - 07 December 2022

Regulatory consents and filings

What regulatory consents, notifications and filings are required for a financial services M&A transaction? Should the parties anticipate any typical financial, social or other concessions?

Depending on the type of financial entity and the percentage of the capital stock involved in the M&A transaction, a notice or an authorisation request must be filed with the National Banking and Securities Commission (CNBV).

Please note that each financial entity is regulated by specific statutory provisions, and thus, the applicable rules may vary from one another; however, generally speaking, a notice must be filed before the CNBV within a few days of the M&A transaction being executed if it represents less than 2 per cent, 5 per cent or, in certain cases, 10 per cent of the capital stock acquired, depending on the type of financial entity.

The notice must include, among others, the identification data of potential shareholders (name, nationality, address, and tax ID number), as well as a declaration of the origin of the funds that will be invested in the financial entity.

If the acquisition exceeds the percentages referred to above, the authorisation request must be filed before the CNBV prior to the execution of the M&A transaction. The authorisation request must include information regarding the financial situation of the potential shareholders (ie, financial statements, real estate, bank accounts (balances), investments, mortgages, etc) and certain personal disclosures. This information must be provided to the financial authorities with the details, and in the formats provided by the authorities for such purposes.

Additionally, if the acquisition exceeds certain thresholds set forth in the applicable laws and regulations (20 per cent of the capital stock of banking or popular companies, 30 per cent of the capital stock of brokerage houses, or 50 per cent of the capital stock of electronic payment funds institutions or crowdfunding institutions), such transactions will be considered as a change of control. Therefore, in addition to the requirements mentioned in the paragraph above, the change of control authorisation request must include, among others, a business plan that covers the organisation, administration and internal control that will be implemented by the acquirers, as well as the directors that will be appointed because of the change of control of the entity.

Law stated - 07 December 2022

Ownership restrictions

Are there any restrictions on the types of entities and individuals that can wholly or partly own financial institutions in your jurisdiction?

Foreign governments cannot participate in the capital stock of Mexican financial entities, unless their participation is: (1) a result of temporary prudential measures, such as financial support or bailouts; (2) indirect and does not involve having control of the financial entity; or (3) structured through an official entity where the government does not exercise authority functions and its corporate bodies operate independently.

In addition, legal entities and individuals that do not have an adequate financial, legal and moral capacity cannot be direct or indirect shareholders of Mexican financial entities. To evaluate these capacities, the regulation sets forth certain information that must be disclosed during the notice or authorisation request procedures held before the

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relevant financial authority, such as the financial situation of the potential shareholders (ie, real estate, balances in bank, investments, mortgages, etc), as well a statement under oath where the potential direct and indirect shareholders declare, among others, that they are in compliance with any credit or debt obligation, and that they have not been subject to or been involved in federal or local proceedings, criminal investigations or any other proceedings in Mexico or in any other country.

Law stated - 07 December 2022

Directors and officers – restrictions

Are there any restrictions on who can be a director or officer of a financial institution in your jurisdiction?

The directors of Mexican financial entities must demonstrate to the corresponding authority that they have technical skills, honourability, a satisfactory credit history, experience and extensive knowledge in financial, legal or administrative matters. The Mexican financial regulation establishes the information that must be disclosed to the authority to ascertain these criteria before directors' appointment.

As a general rule, the following persons cannot be appointed as directors of a Mexican financial entity:

1. officers of the financial entity, unless their position is general manager or is within two hierarchies immediately below the general manager;
2. the spouse or concubine of the persons mentioned in (1);
3. persons who have a pending proceeding against the financial entity;
4. those who have been sentenced for crimes against property, or disqualified from engaging in commerce or from holding a position in Mexican public service or in the Mexican financial system;
5. those who have been declared bankrupt or insolvents and have not been rehabilitated;
6. those who perform inspection or have supervisory power over the financial entity; or
7. those who participate on the boards of directors of another financial entity of the same kind.

Nonetheless, the specific legislation for each type of financial entity establishes certain restrictions for each specific case.

Additionally, Mexican financial entities must have a certain percentage of independent directors who are not part of the day-to-day administration. As a general rule, the following persons cannot be appointed as independent directors:

- officers of the financial entity;
- shareholders of the financial entity that have decision-making power;
- clients, suppliers, debtors, creditors, partners or directors of a company that is a relevant client, supplier, service providers, debtors, or creditors of the financial entity; or
- officers of a foundation, association or non-mercantile company that receives relevant donations from the financial entity.

Nevertheless, the specific legislation for each type of financial entity establishes certain restrictions for each case.

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Directors and officers – liabilities and legal duties

What are the primary liabilities, legal duties and responsibilities of directors and officers in the context of financial services M&A transactions?

There are no special liabilities, legal duties or responsibilities of directors and officers in the context of financial services M&A transactions, other than their general fiduciary duty obligations, particularly exercising their duties with proper diligence, confidentiality, transparency and avoiding conflicts of interest.

Law stated - 07 December 2022

Foreign investment

What foreign investment restrictions and other domestic regulatory issues arise for acquirers based outside your jurisdiction?

The Mexican Foreign Investment Law does not establish restrictions on foreign investors holding any interest in a Mexican financial entity. However, it does generally set forth that the approval of the Mexican National Foreign Investments Commission is required if a foreign entity intends to hold an investment of more than 49 per cent of the capital stock of a Mexican entity.

If the acquirer is a foreign financial entity, it must fulfil the requirements set forth in the Rules for the establishment of Subsidiaries of Foreign Financial Entities instead of the applicable regulation for the financial entity that will be acquired.

Law stated - 07 December 2022

Competition law and merger control

What competition law and merger control issues arise in financial services M&A transactions in your jurisdiction?

Mandatory notification

Although all concentrations that occur in Mexico or have effects in Mexico are subject to the Federal Law of Economic Competition (the Competition Law), and may therefore be investigated by the Federal Economic Competition Commission (COFECE) or the Federal Institute of Telecommunications (IFT and, jointly with COFECE, the Mexican Antitrust Authorities), the Competition Law sets forth certain monetary thresholds that trigger the obligation of economic agents to notify concentrations and obtain clearance before they are consummated. In this sense, a transaction will be subject to a mandatory pre-merger filing by reaching at least one of the thresholds, which are provided in article 86 of the Competition Law, related to: (1) the price of the transaction, (2) the size of the target, and (3) the size of the economic agents participating in the transaction (ie , sellers, purchasers and target).

Gun jumping

In Mexico, before closing a transaction parties must avoid sharing competitively sensitive information, such as current and future pricing, top customers, supply contracts, and strategic plans (among others). In addition, transacting parties must remain separate and independent before closing; that is, the acquiring entity must avoid exerting control over the assets or routine business, management or operations of the target business.

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Note that the Competition Law considers as a 'concentration' not only mergers and acquisition but 'any acquisition of control, or any other act by means of which companies, associations, stock, partnership interest, trusts or assets in general are consolidated, and which is carried out among economic agents'. Therefore, special attention should be paid to those loans, convertible or not, which establish monitoring clauses or similar that may confer control to the lender over the target. COFECE has made clear that fines will be imposed for failing to report – and obtain clearance for – the issuance of warrants that convey economic and voting rights to the acquirer of such warrants, prior to being exercised and converted into actual stocks in the target.

Law stated - 07 December 2022

DEAL STRUCTURES AND STRATEGIC CONSIDERATIONS

Common structures

What structures are commonly used for financial services M&A transactions in your jurisdiction?

Stock deals are the typical structures used in acquiring regulated financial entities. Asset deals are rarely seen given the associated regulatory complexities and actionability challenges. When only a portion of a financial entity's business is the subject matter of an M&A deal, previous spin-offs are structured for the buyer to acquire a spun-off company keeping or receiving the balance sheet of the respective separated business. This type of structures brings further regulatory complexities to the transaction. Acquisition structures and processes would also depend on whether the target is a privately owned entity or a publicly traded company, the latter cases being required to follow takeover rules.

Law stated - 07 December 2022

Time frame

What is the typical time frame for financial services M&A transactions? What factors tend to affect the timing?

The typical time frame for financial services M&A transactions is between 12 and 24 months. The timing is essentially affected by the required regulatory and antitrust approvals.

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Tax

What tax issues arise in financial services M&A transactions in your jurisdiction? To what extent do these typically drive structuring considerations?

The tax issues are not particularly different from standard M&A deals other than given the regulated nature of the targets, there may be less flexibility in terms of structuring.

Law stated - 07 December 2022

ESG and public relations

How do the parties address the wider public relations issues in financial services M&A transactions ? Is environmental, social and governance (ESG) a significant factor?

ESG has just recently become relevant, particularly for foreign financial institutions. However, we have not yet identified

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in public sources an M&A transaction cancelled due to ESG issues. Nevertheless, ESG has been taken seriously as part of internal policies of Mexican financial institutions controlled by foreign and global institutions and, therefore, will be a factor in future M&A deals.

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Political and policy risks

How do the parties address political and policy risks in financial services M&A transactions?

This is certainly one of the key elements in deciding to proceed with an M&A deal and part of the basic diligence items when analysing an acquisition. The political and policy risks matrix typically covers strategy with regulators seeking approval, transparency and certainty of the legal framework, compatibility with international standards or domestic rules of the investor, anti-bribery diligence and anti-money laundering compliance of the target, among many others.

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Shareholder activism

How prevalent is shareholder activism in financial services M&A transactions in your jurisdiction?

Shareholder activism is very rarely seen in Mexico and, consequently, is scarcely present in financial services M&A transactions.

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Third-party consents and notifications

What third-party consents and notifications are required for a financial services M&A transaction in your jurisdiction?

Non-government third-party consents and notifications required for a financial services M&A transaction are normally related to third-party lenders and special strategic partners, if any.

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DUE DILIGENCE

Legal due diligence

What legal due diligence is required for financial services M&A transactions? What specialists are typically involved?

Regulatory compliance is the main legal due diligence. This includes detailed review of a wide variety of topics, including operating manuals, general operations compliance, selection of material financial assets (eg, material loan portfolio), capitalisation requirements, regulatory inspections, audits and sanctions, litigation and tax.

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Other due diligence

What other material due diligence is required or advised for financial services M&A transactions?

Anti-money laundering, anti-terrorism, anti-bribery and antitrust compliance have recently become very important due diligence topics.

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Emerging technologies

Are there specific emerging technologies or practices that require additional diligence?

Additional diligence is required mainly to confirm that the target entity has all relevant permits and approvals to perform certain financial-technology activities, and that it is in compliance with its corresponding regulatory obligations.

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PRICING AND FINANCING

Pricing

How are targets priced in financial services M&A transactions? What factors typically affect valuation?

Valuations are normally associated to international standards, where items such as assets under management, number of clients, geographical presence, scope of financial products, loans and deposits, technology, as well as capitalisation and reserves are important factors that are taken into account.

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Purchase price adjustments

What purchase price adjustments are typical in financial services M&A transactions?

Any that are typical of ordinary M&A deals, including earn-outs and net value adjustments.

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Financing

How are acquisitions typically financed? Are there any notable regulatory issues affecting the choice of financing arrangements?

Acquisition finance structures vary depending on the type of target and the associated regulatory restrictions. The most important restrictions normally faced by certain regulated financial institutions are prohibitions on acquirors pledging purchased stock.

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DEAL TERMS

Representations and warranties

What representations and warranties are typically made by the target in financial services M&A transactions? Are any areas usually covered in greater detail than in general M&A transactions?

Those typical of M&A transactions, with greater detail on regulatory compliance, including anti-money laundering, anti-terrorism and anti-bribery compliance, and regulatory sanctions.

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Indemnities

What indemnities are typical for financial services M&A transactions? What are typical terms for indemnities?

Those typical of M&A transactions. Particular survival periods and special indemnities are commonly associated to the regulatory statute of limitations on regulatory compliance and associated regulatory sanctions. Taxes, social security and labour contingencies are also matters typically uncapped and subject to survival periods under the statute of limitations.

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Closing conditions

What closing conditions are common in financial services M&A transactions?

Regulatory and antitrust approvals and third-party consents, as well as absence of material adverse effects would be the most common closing conditions. Sometimes successful conclusion of regulatory audits or internal regulatory compliance clean-up are agreed too.

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Interim operating covenants

What sector-specific interim operating covenants and other covenants are usually included to cover the period between signing and closing of a financial services M&A transaction?

The covenants are not particularly different from standard M&A deals, with particular emphasis on regulatory compliance.

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DISPUTES

Common claims and remedies

What issues commonly give rise to disputes in the course of financial services M&A transactions? What claims and remedies are available?

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Typically, regulatory compliance, balance-sheet associated matters and taxes.

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Dispute resolution

How are disputes commonly resolved in financial services M&A transactions? Which courts are used to resolve these disputes and what procedural issues should be borne in mind? Is alternative dispute resolution (ADR) commonly used?

Dispute resolution clauses may vary depending on the type of investors. While domestic parties may normally agree on Mexican courts and a purchase agreement governed by Mexican law, foreign purchasers or sellers may prefer foreign courts (most commonly, New York courts) or arbitration and purchase agreements subject to foreign law (also typically, New York).

Law stated - 07 December 2022

UPDATE AND TRENDS

Trends, recent developments and outlook

What are the most noteworthy current trends and recent developments in financial services M&A in your jurisdiction? What developments are expected in the coming year?

There is a great interest from national and international participants in carrying out M&A operations. The Mexican Fintech Law allowed a significant number of domestic and international players to start operating in Mexico. This has then generated a large amount of M&A activity; on the one hand, consolidation of fintech companies and, on the other, fintech companies seeking further growth by acquiring other types of traditional financial services entities, such as banking institutions and securities brokerage houses. The latter case is a consequence not only of fintech companies expanding their services to traditional banking and securities clientele but also expanding their scope of operations beyond the several restrictions imposed by the Fintech Law. Recently there has been significant M&A activity in joint ventures focused on developing e-banking or international banks looking for banking licences as a quicker process than applying for a banking licence from scratch.

The main hurdle we have seen is the extensive information of direct and indirect shareholders required by the Mexican authorities. We believe that during 2022 and 2023 there will be an increase in M&A transactions from all types of entities: banks, fintech companies and brokerage firms.

The chapter was co-authored by Eduardo Flores Herrera and Carlos Cortés Justo, who have since left the firm. The authors would like to thank Eduardo Brandt López and Edgar Martín Padilla for their contributions to the chapter.

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Jurisdictions

Egypt	Soliman, Hashish & Partners
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India	Khaitan & Co
Indonesia	ABNR
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