Private Placements and Other Exempt Offerings in Mexico: Overview

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A Practice Note providing an overview of private placements and other securities offerings that are exempt from the registration requirement under the securities laws of Mexico. This Note explains what a private placement is and why companies, fund managers, and other players conduct private placements in Mexico. It also examines registration exemptions commonly used by issuers and investors who wish to sell equity or debt securities in exempt offerings.

An offering of securities in Mexico generally requires prior approval by the Mexican National Banking and Securities Commission (CNBV) and the registration of the securities in the National Securities Registry (RNV) maintained by the CNBV, unless one or more exemptions are available under the applicable securities laws. This Note provides an overview of securities offerings that are exempt from this registration requirement and qualify as private placements.

Merits of Exempt Offerings

Exempt offerings of securities in Mexico have three significant advantages compared with public offerings:

- They are significantly faster to implement.
- They are less exposed to market volatility.
- They have a reduced set of requirements with the corresponding reduction in expenses.

Private offerings are faster to execute since they do not require:

- Registration of the securities with the RNV.
- Review and approval by the CNBV.

Depending on the complexity of the offering, these processes can take several months. This impacts the timeline for execution of a transaction and makes it more challenging to navigate market windows to carry out the offering.

Private offerings do not require periodic disclosure of information by the issuer. In contrast, public offerings require the issuer to disclose annual and quarterly reports, and material events, which can increase expenses for the issuer, as it needs to develop its reporting function and engage legal and financial advisors.

However, private placements may not be appropriate for all offerings and issuers for the following reasons:

- Since the securities offered are not registered in the RNV, their trading is limited, which can impact liquidity.

- The securities cannot be offered to retail investors, and cannot be offered through indiscriminate solicitations or intermediation of securities by an authorized broker dealer, which can also impact both the valuation and the publicity of the offering, and ultimately, the size of the offering.

Registration Requirement for Public Offerings

Public offerings of securities require the prior approval of the CNBV, and the securities issued must be registered with the RNV (Articles 7 and 83, Securities Market Law (*Ley del Mercado de Valores*) (LMV)).

Article 2 paragraph XVIII of the LMV defines a public offering as the offering of securities, with or without a price, in Mexico, using mass means of communication and to indeterminate people. This means that if an issuer is seeking to offer its securities to retail investors, in addition to qualified and institutional investors, or through general solicitation and advertising, they must conduct a public offering and obtain the CNBV's prior approval.

Articles 85 to 89 of the LMV set out a series of requirements that must be met for the CNBV to approve the offering. A prospectus must be prepared, containing information including:

- The characteristics of the offering and the securities issued.
- A description of the business of the issuer (business section).
- A discussion of the financial condition of the issuer (MD&A section).
- A description of related party transactions.
- The capitalization of the issuer.
- A description of the issuer's corporate structure.

This prospectus must be signed by the chief executive officer, the chief financial officer and the general counsel of the issuer, as well as by the underwriters, the auditors and the external legal advisor of the issuer, which makes them potentially liable for the content and information included in the prospectus.

In addition to the prospectus, the issuer must include audited financial statements prepared according to International Financial Reporting Standards, for the previous three years, and an opinion from independent counsel as to the validity of the securities being offered, among other documents, which can increase the cost and timing of an offering.

Once a public offering is complete and the securities are registered with the RNV, the issuer becomes subject to disclosure obligations under Articles 104 and 105 of the LMV. Accordingly, the issuer must file annual and quarterly reports (including the corresponding financial statements), and periodic reports of material information concerning the issuer or the securities.

Registration Exemptions

Although the general rule is that securities must be registered to conduct an offering in Mexico, Article 8 of the LMV sets out a series of exemptions under which a private offering of securities can be conducted without registration:

- Offerings directed exclusively to institutional and qualified investors.
- Equity offerings to fewer than 100 people.

- Offerings to employees under employee stock option plans or similar plans (ESOPs).
- Offerings made to shareholders or partners of clubs or civil associations.
- Other offerings approved on an ad hoc basis by the CNBV.

Offerings to Institutional and Qualified Investors

Institutional investors include Mexican and foreign banks, broker dealers, insurance and bond companies, bonded warehouses, financial leasing companies, factoring companies and investment funds, private pension and annuities funds, and foreign pension and investment funds (Article 2 paragraph XVII, LMV).

Qualified investors are those that have a certain level of income, assets or qualitative traits that enable them to operate under a reduced level of regulatory scrutiny (Article 2 paragraph XVI, LMV). Article I, paragraph XV of the General Provisions Applicable to Issuers of Securities and Other Participants of the Securities Market (*Disposiciones de carácter general para las emisoras de valores y otros participantes del Mercado de valores)* further states that there are two types of qualified investors:

- **Basic qualified investors.** These are investors that:
  - in the last year held on average investments in securities amounting to at least 1.5 million Mexican investment units (the Mexican investment unit is a monetary unit designed to eliminate the effect of inflation; its value is published regularly by Mexico's Central Bank and is indexed to the value of the Mexican peso in 1995); or
  - in each of the last two years had gross income of at least 500,000 Mexican investment units.
- **Sophisticated qualified investors.** These are investors that:
  - in the last year held investments in securities amounting to at least 3 million Mexican investment units; or
  - in each of the last two years had gross income of at least 1 million Mexican investment units.

In addition, sophisticated qualified investors must fill out a form and deliver it to their financial advisors, in which they provide certain representations as to their compliance with the requirements to be considered as a sophisticated qualified investor. When pursuing a private offering under the qualified and institutional investors offering exemption, it is always advisable to obtain a certification from the potential investors, stating that they comply with the requirements to be considered institutional or qualified investors, regardless of whether or not this is required (as in the case of sophisticated qualified investors) to reduce potential exposure for the issuer and its advisors. There is no limit as to the number of institutional or qualified investors to which a private offering of securities can be marketed.

Offerings to Fewer than 100 People

A private offering can be made to any investors without registration if both:

- The offering is made to fewer than 100 potential investors.
- The securities being offered represent the equity or capital stock equivalent of the issuer.

Two important aspects must be considered when conducting an offering using this private placement exemption:

- The LMV refers not to the total number of investors that actually acquire the securities, but rather the number of potential investors to which the securities are marketed.
- The exemption relates exclusively to equity offerings, and is not available if a debt offering is being pursued.

While the CNBV has not adopted integration rules concerning a series of offerings that would in the aggregate exceed the 100-investor threshold, the CNBV could potentially still pursue enforcement action if it considers that a series of subsequent offerings were undertaken to circumvent this limitation.

Offerings Under ESOPs

Private offerings of securities can be made under ESOPs to employees of a company irrespective of the number of employees involved or their status as investors (whether retail, qualified, or institutional). The LMV allows for these plans to be offered to all employees or just a subset of them, and they can be implemented with securities issued by the direct employer or by entities of the same business group.

This exemption allows the offering of any type of securities. Therefore, while generally companies issue equity securities with specific vesting conditions under their ESOPs, there is no regulatory restriction on them issuing debt securities to their employees.

Offerings to Shareholders or Partners of Clubs or Civil Associations

The LMV exempts from registration offerings to shareholders and partners of issuers whose main corporate purpose is to provide services to or transact with their shareholders and partners. This exemption is targeted at members of clubs or civil associations and its application for commercial transactions of securities is limited.

Offerings Under Ad Hoc CNBV Approvals

In addition to the four exemptions specifically provided by the LMV (as discussed above) it also grants wide powers to the CNBV to approve additional exemptions on a case-by-case basis. For that purpose, the CNBV considers the distribution method, the targeted investors, the means of solicitation and other conditions that the CNBV deems appropriate. Therefore, potential issuers can seek the approval of private offerings that might not clearly fit the specific exemptions.

Summary of Requirements for Registration Exemptions

The following table summarizes the requirements and how frequently they are relied upon for commercial purposes in the Mexican market for each type of registration exemption:

Practical Law
Requirements for registration exemptions

	Qualified and Institutional Investors	100 Investors	ESOPs	Clubs and Civil Associations	Ad Hoc Approvals
Number of Investors	No	Yes, fewer than 100	No	No	No
Investor Limitations	Yes, only qualified and institutional investors	No	Yes, only to employees	Yes, only to its shareholders or members	No
Security Limitations	No	Yes, only equity	No	No	No
Frequently Used	Yes	Yes	No	No	No

Certain Requirements for Private Offerings

If an offering qualifies as private under one of the registration exemptions (see Registration Exemptions), no further approval from, or submission to, the CNBV is required before conducting the offering. However, if a Mexican issuer conducts a private placement abroad, under Article 7 of the LMV, it must notify the CNBV of the offering within one business day after the settlement date. The notification must include:

- The type of security offered and its characteristics.
- The identity of the issuer.
- The underwriters involved in the offering.
- The total issuance amount.
- The exchange in which the securities have been or will be listed.
- The use of proceeds.
- The legislation under which the securities were issued and offered.

Although there is no regulatory requirement to prepare a prospectus or similar disclosure document for a private offering, the issuer and its advisors generally prepare an offering document in the form of an offering memorandum or a private placement memorandum to distribute to potential investors. These contain the most important information regarding the issuer and the securities being offered, and in general terms contain very similar information to what is included in a prospectus filed before the CNBV.

If an issuer is relying on the exemption relating to institutional and qualified investors, the distribution of the offering documents must be directed only to these institutional or qualified investors to avoid being potentially subject to enforcement action from the CNBV. Appropriate disclaimer language must be included in the disclosure documents, expressly stating that the securities being offered are not registered with the RNV, and the documents have not been reviewed or approved by the CNBV. It is also important to state that the securities are being offered using a private placement exemption under Article 8 of the LMV, and that potential investors interested in participating in the offering must make their own analysis of the risks associated with an investment in the securities.

Since private offerings do not permit general solicitation, public promotion or indiscriminate solicitations, any communications concerning the offering must only be addressed to potential investors with whom the issuer or its advisors have a prior relationship. The issuer must refrain from general selling using any means of mass communication.

The intermediation of stock or capital stock equivalents, even if not registered with the RNV, does not have to be conducted using authorized broker dealers established in Mexico (as required by Article 9 of the LMV for public offerings), but can be placed directly by the issuer or by any advisor, without having to comply with any specific regulatory requirements.

Sanctions

It is a criminal offense to either:

- Conduct a private offering of securities, when no registration exemption is available under Article 8 of the LMV.
- Conduct a public offering of securities without the prior approval of the CNBV and registration with the RNV.

(Article 374, LMV.)

This crime is punishable with a prison sentence of between 3 and 15 years. It can only be prosecuted by the Mexican Attorney General's office with the CNBV's approval, and a formal request by the Mexican Ministry of Public Credit.

However, if an offering is conducted in breach of Articles 7 and 8 of the LMV, the affected parties may only seek damages, but may not seek that the offering be declared void (Article 4, LMV).

Current Trends in Private Offerings

In recent years, the Mexican market has experienced a significant increase in offerings of securities using the available private placement safe harbors, due to:

- Increased volatility in the global markets, caused by the COVID pandemic.
- The Russia-Ukraine conflict and the commercial dispute between the US and China.
- Significant delays in the review and approval process of registered offerings by the Mexican authorities.

This trend is expected to continue in the near future.

A bill has been recently approved by the Mexican Senate, which modifies the LMV to include a new type of offering: an *oferta pública simplificada* (a simplified public offering). Although this offering will still be technically a public offering, and the securities offered will be subject to registration with the RNV, it shares some key traits with private offerings, making it a hybrid figure. The offering will not require prior approval by the CNBV, and although a prospectus must be prepared, it will only have to be reviewed by the underwriters and the stock exchange in which the securities are intended to be listed. The distribution of the securities will be limited to institutional and qualified investors. This could make simplified public offerings an attractive alternative to traditional private offerings for certain investors, assuming that the bill is enacted and the regulations implementing the reform are adopted, which is expected to happen during 2024.

The surge in private offerings of securities has raised the attention of Mexican regulators, particularly the CNBV, which has increased the number of audits and inspections of participants involved in these transactions (such as broker dealers and financial institutions acting as trustees), to monitor that the private placement exemptions available are being met and complied with.

These inspections by the Mexican regulators (such as the CNBV, the Insurance Commission and the Central Bank) have resulted in the detection of multiple violations of the safe harbor exceptions provided under the LMV, which has resulted in numerous economic sanctions and fines being imposed. It is therefore advisable for parties interested in issuing securities under a private placement exemption in Mexico to consult with legal advisors to ensure that the proposed structure and marketing of a private offering are in strict compliance with applicable laws, and to avoid sanctions.

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