

Due Diligence for Private Acquisitions in Mexico

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A Practice Note considering the purpose, scope, and practical aspects of a legal due diligence investigation for the purchase of a private company or business in Mexico. It outlines the process for legal due diligence in Mexico, including organizing the investigation and various sources of information. It also considers issues of confidentiality and data protection during due diligence in Mexico.

Due diligence is the investigation of a person or business. In the context of business acquisitions, the parties use the due diligence process to gather information about each other and about the target business or assets that are for sale. Although the seller occasionally conducts due diligence on the buyer (see Box, Seller Due Diligence), the due diligence process is usually more significant for the buyer.

Completing a due diligence investigation of a business can be more challenging and complex for a buyer in cross-border transactions. Due diligence practices can vary significantly between countries because of different:

- Legal and regulatory practices.
- Financial reporting systems.
- Business practices, expectations, and customs.

If different jurisdictions are involved, it is important for the buyer to understand the local legal and financial systems, operations, and culture.

This Note considers, from the buyer's perspective, the purpose, scope, and practical aspects of a due diligence investigation for a private share or asset purchase in Mexico. It outlines the process for legal due diligence, including:

- How to organize the due diligence process.
- The various sources of information in a typical due diligence investigation.
- The information to request and review depending on the type of transaction.
- How the information gathered should be reviewed and presented.

It also considers issues of confidentiality and data protection in Mexico.

Unless otherwise stated, a reference in this Note to:

- Civil Code means the [Mexican Federal Civil Code \(Código Civil Federal\)](#) and its correlative provisions for the Civil Codes for the States of Mexico.
- COFECE means the Mexican Federal Economic Competition Commission (*Comisión Federal de Competencia Económica*), Mexico's primary antitrust agency.
- Foreign Investment Law means the [Mexican Foreign Investment Law \(Ley de Inversión Extranjera\)](#).
- GLBO means the [Mexican General Law of Business Organizations \(Ley General de Sociedades Mercantiles\)](#).
- Income Tax Law means the [Mexican Income Tax Law \(Ley del Impuesto sobre la Renta\)](#).
- Mexican Anti-bribery Law means the [General Law of Administrative Responsibilities \(Ley General de Responsabilidades Administrativas\)](#).
- Mexican Antitrust Law means the [Federal Law of Economic Competition \(Ley Federal de Competencia Económica\)](#).
- Mexican Privacy Law means the [Federal Law of Data Protection for Data in Possession of Private Individuals \(Ley Federal de Protección de Datos Personales en Posesión de Particulares\)](#).
- Ministry of Foreign Affairs means the Mexican Ministry of Foreign Affairs (*Secretaría de Relaciones Exteriores*).
- Tax Code means the Federal Tax Code (*Código Fiscal de la Federación*).
- VAT means value-added tax.

Purpose of Due Diligence in Mexico

Globalization, the development of new technologies and means of communication, the execution of the United States-Mexico-Canada Agreement (USMCA), the emergence of new markets, debt restructuring, and the intent to recover the economy and productive activities following the impact of the COVID-19 pandemic together allowed the increase of domestic and foreign investment in Mexico and the participation of Mexican companies in the international economy. Moreover, following the 2021 reforms of tax and labor laws in Mexico which prohibited labor outsourcing schemes, Mexican entities were obliged to undergo certain corporate restructures (including mergers) to consolidate their personnel and operations in a single entity.

Because of these changing legal and economic conditions, and although there are no specific legal provisions regulating due diligence processes in Mexico, Mexican firms and entrepreneurs have adopted detailed due diligence investigations of a style and scope common in the UK and US to:

- Ensure the buyer's certainty to mitigate potential risks of the transaction and prevent future contingencies.
- Ensure that the target will continue operating as a going concern.
- Determine a fair purchase price in line with market standards.
- Identify the need to obtain any third-party authorizations or to deliver notices to carry out the transaction.
- Identify possible liabilities and determine the party to be held liable.
- Set the course of negotiations of transaction documents, including the scope of representations and warranties of the seller and the target, and the disclosure schedules of the relevant agreement.
- Establish indemnification procedures upon default or misrepresentations.
- Set forth conditions the occurrence of which would represent a deal breaker for the buyer.

The primary purpose of a due diligence review is to obtain enough information about the target's business to enable the buyer (or other parties with an interest in the transaction, for example, lenders financing the transaction) to decide whether the proposed acquisition represents a sound commercial investment. Due diligence is effectively an audit of the target's affairs, including, but not limited to legal, business, financial, tax, and accounting. It is therefore a crucial bargaining tool for the buyer.

Nevertheless, certain logistical or practical difficulties may affect the availability of or access to business information of the target, such as:

- Confidentiality agreements.
- Confidentiality policies within each party's organization.
- The lack of, or late delivery of, information.
- The organizational culture of each party.
- The lack of cooperation in providing information.
- Communication gaps between the parties, their officers, and the accounting, legal, tax, and financial advisors in charge of carrying out the due diligence process.
- Amendments to applicable laws and the specificity of new information requested by the authorities from time to time.

Types of Due Diligence

Due diligence may be either broad and detailed, evaluating all the information of the target to identify all open items and risks for the transaction, or high-level and focused on identifying material issues only. In principle, the type of due diligence to be implemented should be determined according to the needs of each buyer. However, other aspects should be considered to determine the most suitable level of diligence, including:

- The budget.
- The estimated timing for closing.
- The level of risk of the transaction.
- The volume of business of the target.
- Special regulations applicable to the business of the target.
- The type of transaction.

(See Scope of Due Diligence Review.)

The expected scope of due diligence should be negotiated and agreed upon beforehand through the execution of the relevant offer and acceptance, letters of intent (LOIs), term sheets, memorandums of understanding (MOUs), or any other preliminary document selected to outline the terms of the transaction agreement.

Typically, the primary information about the target or its assets that should be required for detailed due diligence in these types of transactions includes:

- Financial statements.
- Corporate books and records.

- Stock certificates.
- Evidence of title over real estate and assets and any related liens.
- Material agreements.
- Agreements with related parties.
- Tax returns.
- Licenses, permits, and authorizations.
- Documents evidencing guarantees granted by the target and registration thereof, as applicable.
- Evidence of:
 - registration before the applicable registries;
 - registration before tax and labor authorities; and
 - compliance with labor and social security obligations.
- Documents evidencing intellectual property of the target and registration thereof.
- Insurance policies held by the target.
- Does the seller have good title to the shares in the target company, and does the target have good title to its assets?
- Does the target company have any subsidiaries?
- Has the target company entered any services agreement which could potentially be considered an outsourcing scheme?
- Are there any unstated or understated liabilities or risks associated with the target company or assets?
- Are there any restrictions on the business or transfer of ownership?
- Has the company granted any option or other similar rights to third parties that could affect the transfer of equity?
- Is the declared condition of the property and assets as stated?
- Are there any liens or securities that may affect the target, the property, the assets, or the transaction in general?
- Does the target have any employees? Are such employees registered before the relevant authorities? Are there individuals at the disposition of the target company, or providing services to the target company which could potentially be considered an employment or outsourcing relationship?

Legal Due Diligence

Legal due diligence is usually carried out by an external law firm appointed by the buyer, and may include a team of attorneys who are specialized in the different legal areas involved in the transaction, up-to-date with federal, state, and local laws and regulations, and of different levels of seniority and expertise to ensure the target company is in compliance with the applicable laws and that the transaction or the operation of the target as of closing would not represent a liability or a contingency to the buyer or the target company.

In any significant acquisition, a legal due diligence investigation should establish, at least, the following key information about the target business:

- Is the target company duly incorporated, validly existing, and has it been duly registered before all applicable registries?
- Do the seller and the target company have sufficient capacity to enter the transaction as negotiated between the parties?
- Are there any corporate acts to be performed, governmental authorizations or third-party consents or waivers to be obtained, or notices to be delivered for the transaction to be valid?
- Is the target company part of a corporate group? Are there any shared services being provided among the target company and its affiliates?
- Do the seller and the target company, as applicable, have legal representatives with sufficient authority to execute the transaction documents on their behalf?
- Is the target company in compliance with its labor, employment, social security, and social welfare obligations?
- Are there any outstanding agreements between the target company and any clients, vendors, suppliers, agents, brokers, services providers, banking institutions, independent contractors, or related parties? Is the target company in compliance with those agreements? Are there any provisions in those agreements that could affect the transaction (for example, a change of control clause or required consents or notices)?
- In case of providing or receiving specialized services, is the target company in compliance with the specific requirements as per the subcontracting regulation (for example, requesting and maintaining certain information, reporting, registrations, etc.)?
- Has the seller or the target company granted any kind of guaranty or security, or executed any type of debt instrument, that could impair compliance with their obligations in the transaction or further affect the business of the target company?
- Are there any existing, contingent, or pending claims, litigations, arbitration procedures or any other judicial or non-judicial procedure involving the seller or the target company?

- Have the operations of the target company been conducted in line with applicable laws? Does the target company hold the permits, licenses, and authorizations it needs, including those required for its facilities? Will those permits, licenses, and authorizations survive the transaction, or should they be renewed?
- Are the seller and the target company each generally in compliance with their legal obligations?

Detailed information on the target business is required, so that the buyer is in a better position to:

- Confirm the value of the target business or assets and define the right purchase price.
- Define the preferred structure of the transaction.
- Request additional guarantees from the seller or a more stringent indemnification procedure.
- Determine any consents or approvals that may be required for the transaction, or any contractual prohibitions on the transfer of key contracts or assets. For example, the consent of industry regulators, trade unions, tax authorities, competition authorities, shareholders, important customers or suppliers of the target, or creditors.
- Define conditions for closing considering due diligence findings, as well as specific obligations, indemnities, or remediation processes in such regard.
- Plan the integration of the target business.
- Determine whether any ancillary documents are needed (for example, a transitional services agreement).
- Determine deal breakers and nice-to-haves.
- Bargain with the seller.

The buyer will inevitably seek contractual protection from the seller in the form of warranties and indemnities but, in practice, the protection offered may be limited by disclosures and other contractual provisions. Furthermore, the Civil Code only acknowledges guarantees in the form of pledges, bonds, and mortgages. Contractual warranties in Mexico may not be considered as guarantees but rather as mere representations, and thus, it is not possible to submit a “misrepresentation” to Mexican courts as a default like in other jurisdictions. Therefore, the buyer and its advisors should be careful to identify which of those representations should become a condition or obligation for closing and which should require specific indemnities to be included in the transaction documents.

Commercial (or Business) Due Diligence

In addition to the legal due diligence review, specialist advisers may be required to contribute commercial

(or business) due diligence. Commercial due diligence looks at issues such as the country-risk assessment, the economic and monetary policies of the jurisdictions in which the business operates, the market in which the business operates, competitors, the business’ strengths and weaknesses, the position and reputation of the seller and the target company in the market, the organizational culture of the target company, production, sales and marketing, and research and development. Some of the results of this part of the due diligence review will be relevant to the legal due diligence.

The commercial due diligence aims to test the assumptions already made in the buyer’s acquisition plan and to identify the management action required by the buyer to take effective control of, and reduce risk in, the business once the deal has closed.

Financial Due Diligence

As part of the due diligence process, the buyer may instruct accountants or financial advisors to prepare a report on the financial aspects of the target business, including a review of the target’s financial statements. Financial due diligence is not the equivalent of a financial audit. Financial due diligence focuses on the areas of the target’s financial affairs that are material to the buyer’s decision to proceed with the transaction. The buyer may then assess the financial risks and opportunities of the deal and whether, given these risks and opportunities, the target business will fit well into the buyer’s strategy. Financial due diligence may also help quantify:

- Potential synergies.
- The best acquisition and financing structure.
- The impact of the acquisition on the buyer’s performance metrics. When the buyer’s accounting policies are more conservative than those followed in the target business, it may be necessary to make appropriate adjustments to measure the true impact.
- Any accounts receivable or accounts payable of the target company that could have a material impact on the operation of the business after the transaction has closed.
- The required initial disbursement, the expected return on investment, and profits expected to be obtained by the buyer, including the estimated profit timeframe.

Tax Due Diligence

Tax due diligence is usually carried out by the buyer’s accountants as well as by tax advisers or tax lawyers. This is a key exercise to ensure the target company

is properly accounting for tax and that there are no potential tax liabilities which could be triggered by the sale.

In particular, the tax due diligence may include a review of:

- Copies of all returns (normal and amended) related to income tax (including advanced payments (*pagos provisionales*)), VAT and employees' withholding tax returns for the last five fiscal years.
- Copies of proof of payment in respect of all tax returns requested.
- All correspondence with any federal, state, or local tax authorities concerning adjustments or questioning compliance.
- The list of returns and applicable years that have been audited by federal, state, or local tax authorities.
- The list of relevant taxes applicable to the target (and any subsidiaries).
- Copies of documents concerning any tax litigation proceedings, as well as relevant correspondence with the fiscal authorities, copies of all correspondence relating to any queries, requests for information, audits, and settlements, notice of assessments, objections, appeals, settlement, and judgments.
- Copies of all legal and accounting tax opinions received by the target.
- Copies of the latest tax audits with the corresponding detail and status.
- Information regarding the calculation of the tax basis cost of capital assets.
- Details and copies of any special tax regime, exemption, special system, or tax benefit negotiated or applicable.
- Copies of the calculations related to wages and salaries and social security contributions for the last five fiscal years.
- Copies of all tax attributes, considering CUFIN (net after-tax profit account), CUCA (net paid-in capital account), tax losses pending amortization, income tax carry forward, favourable balances on taxes pending refund, negative UFIN (net taxable income) balance, and income tax credit on distributed dividends.
- Details of any cross-border transactions and financing, as well as any transfer pricing investigations by the relevant authorities.
- Intercompany agreements.
- Copies of any transfer pricing documentation.

Tax due diligence is also carried out on intragroup transactions that, for example, could trigger a

clawback of stamp duty or capital gains tax reliefs on the exit of the target.

Due Diligence for Industry Risk

The buyer will also need to identify the main areas of risk and liability inherent to the specific industry of the target. This sets the emphasis of the legal due diligence exercise and enables the buyer to seek appropriate contractual protections from the seller. The buyer should consider the following issues:

- What are the customary risks of the industry?
- What is the known reputation of the target company and how has it been run?
- What is the assessment of those who are selling the business and, if different, those who have been running it?
- Does buyer have the appropriate personnel to run the business if the management team it acquires are not up to task?
- How has this industry evolved in the past years and what is anticipated in the future years? Does it seem cost-effective for the buyer after closing?

If a buyer operates in the same industry as the seller and is purchasing the target business or assets for growth or consolidation purposes, the buyer may not engage in much operational due diligence or require a thorough legal review of certain standard contracts.

If personnel are important, enquiries will need to focus on employment conditions and motivation. If the industry sector is heavily regulated, such as financial services or pharmaceuticals, questions about compliance with applicable regulations need to be satisfactorily answered in advance. If the post-acquisition performance depends on a few critical contracts, it will be very important to ascertain the attitude of the other parties to those contracts to the acquisition before it takes place.

The parties may be required to notify the authorities in certain cases if the seller and the buyer operate in the same industry. For instance, Mexican Antitrust Law provides for certain mergers or acquisitions to be previously approved by the COFECE if the transaction exceeds certain value threshold (currently, approximately USD86,598,000).

Additionally, the Foreign Investment Law provides for certain industries reserved only for Mexicans, as well as certain industries in which the participation of foreign companies or individuals, and even Mexican companies in which foreigners participate, is limited, or whose participation requires a prior authorization issued by the Ministry of Foreign Affairs.

Scope of Due Diligence Review

Many factors influence the scope of the due diligence investigation. It is important to determine the scope at the outset because it dictates how many people are needed, how much time is required, whether outside experts are engaged and depth of review. Common factors that influence the scope of a due diligence review include:

- **Deal Structure.** Identifying the target of the transaction is crucial to determining the correct deal structure. Is the buyer looking to purchase all assets of a company or business or a specific asset? This will determine the best approach for the parties to follow, for instance, if the purchase will be documented through an SPA or if structured as a merger, pursuant to the GLBO. This determination should also influence the scope of the legal due diligence. For example, if the transaction is a stock acquisition or merger, the buyer will likely need information on the entire business. In an asset acquisition, the buyer may only focus on the specific assets and liabilities it is acquiring.
- **Industry.** The industry of the target business may influence areas of due diligence on which the buyer will concentrate, as special regulations, permits, and authorizations could be needed depending on the type of industry (see *Due Diligence for Industry Risk*).
- **Global presence.** If the target business has global operations, it is important to assess compliance with applicable trade controls and anti-bribery and corruption laws, including the Mexican Anti-bribery Law and foreign or multinational anti-bribery laws and conventions, such as the US Foreign Corrupt Practices Act of 1977 (FCPA) if applicable to the target company (such as a Mexican company that trades its securities on a US stock market). For more information, see [Practice Note, Anti-Corruption: Private Acquisitions and Joint Ventures \(Mexico\)](#).
- **Competition.** If the buyer and seller compete, they may require authorization by the COFECE to carry out the transaction and may want (or be required) to keep certain information (such as, pricing) confidential until the transaction is completed (see *Disclosure of Sensitive Information*).
- **Purpose.** For example, if two companies are looking for a trade advantage or element of synergy through a merger, the antitrust investigation will focus on matters such as economies of scale, marketing advantages and competition issues.
- **Risk tolerance.** The buyer may be willing to purchase a target business or assets without engaging in much due diligence if the price appears adequate. The buyer's legal advisers should engage in a thorough discussion with the buyer about its risk tolerance level

and advise their client about potential risks involved in the transaction.

The extent of the investigation is also likely to be governed by practical realities, such as:

- **Access to seller and target business.** The seller often restricts access to its information or the managers of the target business to limit interference and protect proprietary information.
- **Expense.** The buyer may limit the scope of the due diligence investigation to reduce expenses. Sometimes, a buyer conducts its investigation in stages and only increases spending when the likelihood of the deal closing increases.
- **Time constraints.** The parties may wish to complete the transaction within a specific timeframe (such as before fiscal year end) or the seller may have enough bargaining power to limit the time allowed for due diligence (for example, in an auction).

Even if the investigation is well-focused, there will need to be a limit on the information to be supplied. For example, a due diligence request to review all current contracts of the target business could turn up many small contracts entered in the ordinary course of business that will have little bearing on the price or risks of the transaction. One solution would be to ask only for details of all contracts entered outside the ordinary course of business and to put a monetary floor on the value of contracts entered in the ordinary course of business which are to be disclosed. The preparation of a due diligence list or checklist is advised for the seller to understand the relevant information required by the buyer (see *Due Diligence Checklist and Questionnaire*).

Although contractual protection is no substitute for a thorough due diligence exercise, it may offer some comfort where, for example, time is short and due diligence is limited. In these circumstances, the buyer should at least seek to investigate key issues and take other steps to protect itself. For example:

- Ensure that warranties and indemnities are sufficiently wide and specific.
- Consider negotiating a retention of the purchase price to cover potential warranty claims or price adjustments.
- Determine closing conditions that must be met before the transaction is completed and payment made.
- Propose a price adjustment.
- Purchase warranty and indemnity insurance protection.

Depending on the nature of the target's business, the buyer may also want to instruct experts such as environmental experts, surveyors, IT consultants, or other relevant specialists.

Environmental Due Diligence

The acquisition of a company that is a manufacturing or processing company, or whose assets include land used or previously used for industrial processes, will raise the need for environmental due diligence. The issues to investigate include the value of the target and its assets, title to land, *ejido* (a particular Mexican agrarian ownership regime) rights, permits, licenses, authorizations, concessions, potential responsibility for any clean-up, and liability generally in relation to environmental damage.

If these concerns are relevant, a buyer must decide on the level of investigation it wishes to undertake. In addition to a specific legal review of all applicable environmental provisions (such as water concessions, environmental protection, and dangerous waste management), this may range from a brief site visit and a desktop review of information including historical maps, geological or hydrological surveys and process information, to a more detailed survey involving detailed sampling of soil and ground water.

The aim will be to determine and allocate responsibility for clean-up and to obtain protection where appropriate from the seller.

IT Due Diligence

If the target company is heavily dependent on IT, or its business is the provision of IT services or products, then IT due diligence could be important to both buyer and seller.

The following three factors are key to due diligence in an IT context:

- **The relationship between target and seller, which may not cease on completion.** Following a sale, the target may continue to provide IT services to the seller (or vice versa). This continuing relationship raises the importance of due diligence, as the buyer may be reluctant to look to warranties and indemnities. Parties may have to enter into transitional service agreements where services are continued after the transaction closes.
- **IT assets are generally intangible intellectual property rights.** Therefore, due diligence will be focused on these rights to ensure that the sale of the target will not affect licenses or other rights, to establish what consents may be necessary and to determine ownership of copyright.
- **Skilled personnel are key assets for an IT company dependent on know-how.** Investigating this asset requires diplomacy and speed to prevent disgruntled personnel from leaving the target business.

Additionally, cyber security risks and data privacy breaches could result in potentially significant regulatory sanctions (including fines) and, more generally, the risk of litigation. These risks and liabilities are all relevant to the determination of the target company's value.

Some industries may require a more sophisticated level of security and privacy protection infrastructure, and be subject to certain government surveillance, especially industries related to banks and other kind of financial institutions or financial services providers (such as financial technology).

Organizing the Due Diligence Process

Discuss Scope of Due Diligence with Buyer

It will be helpful if the legal adviser meets with the buyer at an early stage to agree the parameters of the investigation. At this meeting, the adviser should find out how much their client already knows about the target business and ask the buyer to highlight any areas of concern.

Before beginning the due diligence process, the buyer's lawyers should establish with their client:

- A due diligence budget.
- The scope of review (see Scope of Due Diligence Review).
- What type of oral or written report is required (see Due Diligence Report).
- The deadline for completing the due diligence review and delivering the report.
- Whether any outside consultants should be engaged.
- If certain areas should be a primary focus.
- If there are any threshold issues that could make or break the deal (known as deal breakers).
- The process for communicating with the seller and the management of the target business. For example, the buyer's lawyers may be required to communicate through a third party such as an investment banker or to specific officers or employees of the target company.

The extent of the due diligence investigation should be in keeping with the value and importance of the acquisition to the buyer and the potential risk. It is important to agree the scope of the legal due diligence investigation at the outset and for the buyer to understand the limits of such scope.

The Due Diligence Team

It is essential that the acquisition team is made up of appropriate people under clear leadership and with good communication and reporting structures. The team carrying out the due diligence must involve the buyer's own personnel as well as its legal and financial advisers and accountants. In some cases, it may also be necessary to retain outside consultants in other areas such as regulatory compliance, environmental, or insurance. Because the due diligence team could be large and comprised of multiple organizations, it is important to have a point person to organize and coordinate the process. The point person may be the buyer, but often the buyer delegates this responsibility to its lawyers.

Generally, the legal team consists of corporate lawyers and other specialists (such as environmental, labor, tax, real estate, and intellectual property lawyers). Lawyers doing the due diligence investigation must be fully briefed as to the purpose of the acquisition, the depth of investigation required and the key areas of importance for the client. If this information is not given, the onus is on the lawyers carrying out due diligence to ask the relevant questions rather than proceed with an unfocused investigation.

Due Diligence Checklist and Questionnaire

One of the most important preliminary activities in the context of a due diligence exercise is to prepare the due diligence checklist, which is a list of the documents and information to be requested to seller and to the target company that should be uploaded in the data room. To prepare the due diligence checklist, the buyer's advisers should read the main publicly available information on the target company (see Other Sources of Information).

In drafting the due diligence checklist, the adviser should consider the scope of the due diligence exercise that has been agreed with the client (see Scope of Due Diligence Review).

The cornerstone of any due diligence exercise is the questionnaire or information request that sets out the areas of investigation and a list of questions and enquiries to be put to the seller. The due diligence questionnaire should be well organized and easy to update. Ideally, the questionnaire should not be too technical; each section should be stand-alone so that it could be considered by the appropriate adviser.

These questions will usually be supplemented by further requests as the negotiations proceed and as the buyer learns more about the target. Care should always be taken to tailor standard due diligence questions so that

they are relevant to the target company and the relevant transaction.

Data Room

The bulk of due diligence review involves reading documents of the target business, including contracts, financial reports, and corporate records. A seller usually sets up a data room, in which relevant information on the target will be made available. Sometimes, especially in smaller transactions, the seller may either send the buyer electronic or hard copies of documents.

Nowadays the data room is often virtual rather than physical at the seller's offices or the office of the seller's attorney. If the materials are stored on an online data site, the seller determines who is invited to the data site and gives password-protected access. It is important to determine which due diligence team members need access to the data site so that the buyer's lawyers could submit a comprehensive request for access to the seller.

For general guidance on due diligence data rooms, see [Practice Notes, Setting up a Data Room \(UK\)](#) and [Using a Virtual Data Room for an M&A Transaction](#).

Vendor Due Diligence Reports

Although not common in Mexico (except for financial reports), sometimes the seller may also conduct a due diligence process culminating in the preparation of one or more vendor due diligence reports (also referred to as VDD reports or VDDR) by the seller's advisers to be provided to prospective buyers.

The types of VDD reports commissioned by a seller vary from transaction to transaction. Financial VDD reports are common. Other VDD reports may cover legal, tax, commercial and property matters, although these kinds of VDD reports are not common in Mexico.

The main purpose of providing VDD reports is to accelerate the bidders' due diligence on the target company. While they require considerable management input before the sale process begins, once it is underway, management tends to spend less time answering due diligence questions from bidders.

Other Sources of Information

Information about a target company could be derived from a variety of sources, including the web site of the seller or the target business. The amount of publicly available information has expanded rapidly, particularly with the growth of the internet.

Usually, information about real property (location, owner, liens), certain corporate information (incorporation details), and liens over movable assets (pledges) are

available through public registries in Mexico. Additional corporate information could be obtained if the company trades its securities in the Mexican Stock Exchange (*Bolsa Mexicana de Valores* (BMV)).

Sources of Corporate and Financial Information

Key corporate information can be obtained from:

- **Commercial Registry (*Registro Público de Comercio*).** Although this is usually provided by the seller, general information about real property and companies could be requested at the [Public Registry of Commerce](#) of the jurisdiction in which the real property or the company is located. For details of the information available at the Public Registry of Commerce, see [Company Searches](#).
- **Statutory books.** The GLBO requires all Mexican companies to keep:
 - a stock ledger containing the number of shares/equity quotas that each shareholder/partner owns in the company, as well as general information of each shareholder/partner (such as complete name, address, and Tax ID);
 - a capital variations book registering all increases and decreases in the company's social capital;
 - a shareholders'/partners' meetings minutes book, which must contain a copy of the minutes of every shareholders'/partners' meetings held by the company; and
 - a board of directors' meetings minutes book, which must contain a copy of the minutes of every board of directors meeting held.
- **Financial Information.** Companies in Mexico are required to preserve all their accounting books and information of the previous five years.
- **Electronic Publication System (*Sistema de Publicaciones Electrónicas de la Secretaría de Economía*).** Information of the current shareholders composition of a Mexican company, as well as notices published by the companies (such as calls for shareholders'/partners' meetings or merger, conversion, or liquidation notices) could be obtained [here](#).
- **Regulators.** Government authorities publish information about companies under their supervision such as operating permits and issued fines (such as companies authorized to operate as a financial institution, financial technology provider, specialized services providers, and other industries).

Sources of Information about Real Property

Information about real property such as title deeds, mortgages or certain third-party rights or claims over the real property (such as, right of way, usufruct, or

judicial seizures) could be obtained from the [Public Registry of Property \(*Registro Público de la Propiedad*\)](#) of the jurisdiction in which the real property is located, on payment of a fee. Usually, all kind of searches before this Public Registry must be carried out directly at the Public Registry's offices.

Sources of Information about Intellectual Property (IP)

Information about trademarks and any kind of industrial property could be obtained from the Mexican Institute of Industrial Property (*Instituto Mexicano de la Propiedad Industrial*), such as ownership, term of the registration, any assignment or transfer of trademarks, or licenses. Searches with the Mexican Institute of Industrial Property are free and may be performed online on [MARCANET](#).

Information about patents, copyrights and any kind of intellectual property could be obtained from the Public Copyrights Registry (*Registro Público de Derechos de Autor*), on payment of a fee. These searches must be carried out directly at the Public Registry's offices.

Sources of Information about Moveable Assets

Public information on liens over a company's moveable assets could be obtained from the [Registry of Moveable Guarantees \(*Registro Único de Garantías Mobiliarias*\)](#), on payment of a fee. This information could be obtained online by any third-party if the third-party has the registry information (*folio mercantil*) of the company.

Liens over certain movable assets, such as boats or airplanes, are subject to special regulation, and this lien information could be obtained from special registries (such as the Maritime National Public Registry (*Registro Público Marítimo Nacional*) and the Mexican Aeronautic Registry (*Registro Aeronáutico Mexicano*)).

Contact with Target's Management

An important aspect of due diligence could be to establish contact with the target's management and to discuss the operation of the business with them. The buyer will often ask to visit the target business site and talk with members of management. The buyer's lawyers may also have follow-up questions after reading due diligence materials which could be answered more completely during a phone call.

However, due to confidentiality concerns, the target business or seller may not want its employees to be aware of the transaction, so it may only grant access to a few members of management. Accessing management of the target business or seller (in an asset sale) during the due diligence process could be a hotly negotiated matter.

Confidentiality and Data Protection

Although a seller typically requires prospective buyers to enter into a confidentiality agreement, these are difficult to enforce in practice. If the buyer is a competitor or potential competitor, a seller may be particularly reluctant to disclose sensitive information about the target business until it can be sure that the sale will go through. Usually, confidentiality obligations are included within the offer and acceptance, letters of intent (LOIs), term sheets, memorandums of understanding (MOUs), or other preliminary documents selected to outline the terms of the transaction.

The knowledge that a business is for sale could also be unsettling for employees, customers, and suppliers. It could lead to a loss of customers or key staff during the sale process. In some cases, the seller will wish to keep its intention to sell the target confidential from all but the most senior management. This will limit the scope of the information available for a full due diligence investigation. It is important to determine the key individuals or teams that will have access to all the information from day one of the due diligence process. In some cases, sensitive and confidential information must be handled by specific individuals in the due diligence team, to avoid disclosures to employees and key staff of the target company.

The seller will want to ensure that no approaches are made to its customers, suppliers, management, or employees either with a view to poaching them or obtaining more information. In an auction sale, it is more difficult to maintain confidentiality because of the number of parties involved. Bridging the gap in expectations between the seller, who is concerned to restrict the release of information, and the buyer, who wants to gather as much information as possible, is a crucial element of the initial stages of any transaction.

Disclosure of Sensitive Information

There are legal restrictions on the disclosure of sensitive information which the seller will have to be very careful to respect when providing information to the buyer in the context of a due diligence investigation.

Information classified as pertaining to national security, information relating to a criminal investigation or information disclosed to a professional in their professional capacity (such as a legal adviser) cannot be disclosed, regardless of the existence of a confidentiality agreement.

Buyers and sellers should be careful with the exchange of information that is commercially or competitively sensitive (in particular, if a buyer is a potential

competitor of the target or the seller), even if the information is shared as part of a due diligence process for the sale of a company. The COFECE sanctions agreements consisting of the exchange of information which could negatively impact the market. An exchange of this information could:

- Facilitate collusion between competing economic agents by providing the necessary elements to establish or oversee an illicit agreement.
- Result in an unfair advantage in the market, such as when the exchange improves an economic agent's ability to predict a competitor's prices, output or business strategies with some specificity and certainty.

However, the COFECE is aware that commercially sensitive information should be shared between economic agents during the due diligence process. In the context of due diligence, both buyer and seller must avoid sharing sensitive commercial information with operating personnel and any other personnel in charge of the day-to-day operations.

To facilitate the exchange of information during mergers and acquisitions, the COFECE has issued the [Guide for the Exchange of Information between Economic Agents](#), which provides certain guidelines and recommendations for the exchange of information between competitors during a due diligence process.

Data Protection Restrictions

During a due diligence process, parties should be careful not to share personal sensitive information of clients or other third parties. The Mexican Privacy Law provides that the recipients of personal information can only use the information for the limited purposes outlined in the recipient's data privacy notices. Additionally, personal sensitive information (such as gender, sexual preferences, health information, religious beliefs, among other details) cannot be compiled into any kind of data base.

Reviewing Information: What to Look For

Following the due diligence investigation, the first step in the review is to consider the completeness of the responses to the enquiries and whether all documents requested have been supplied and all questions satisfactorily answered (see Due Diligence Checklist and Questionnaire).

A review of the target's contracts may raise various issues for consideration. Are there any contractual covenants that could be triggered by the transaction, such as a change of control clause? Any provision in the

target's organizational documents imposing limitations on anyone obtaining more than a specified percentage of the voting rights might also act as an obstacle to assuming control of a business. Anti-trust or other regulatory issues may require the buyer to dispose of various brands owned by itself or the target before the acquisition can proceed.

The sections below are a guide to assessing corporate information, material agreements, licenses, and litigation disclosed as part of the due diligence investigation. It does not provide an exhaustive list, as each transaction may bring its own particularities.

Corporate Information

Company Searches

A company search at the [Public Registry of Commerce](#) (*Registro Público de Comercio*) could reveal certain information about a target company, such as:

- The company's incorporation date and original shareholders.
- List of public deeds amending the company's bylaws.
- Mortgages and charges over the company's movable assets.
- Certain judicial procedures initiated against the company.
- In some cases, powers of attorney granted by the company.
- Liquidation or winding-up resolutions.

The search must be carried out in person.

The determination of which companies to search depends on the nature of the transaction. On most share purchases, the buyer or its advisers should search against the target and its subsidiaries, any companies in which it has a significant shareholding, the corporate seller and corporate guarantor (if applicable). On an asset purchase, where there is no separate target company to search, a search against a corporate seller may be helpful.

The information available at the Public Registry of Commerce will not necessarily be completely up to date. Information should generally be filed within a given period. However, the company may not have filed information within the required period.

It is therefore advisable to run a search against all relevant companies at the outset of the due diligence investigation and then repeat the exercise immediately before exchange to check that there have been no changes since the first search (if so required). The buyer typically also requires a seller to warrant under the

purchase agreement that the company's incorporation deed, powers of attorney and bylaws are correct, up to date, and duly registered before the Public Registry of Commerce.

Corporate Information Provided by the Seller

In addition to information obtained through a search before the Public Registry of Commerce, the buyer normally requests copies of the following documents from the seller in its due diligence questionnaire:

- **Articles of association and bylaws.** In Mexico, a company's incorporation deed (articles of association) and bylaws are contained within the same document, although the articles of association could be amended from time to time. The articles of association of the company may contain provisions that would be of interest to the buyer, such as:
 - corporate purpose, especially if the target company has entered into services agreements that could potentially be considered as outsourcing schemes;
 - pre-emption rights on share transfers;
 - lock-ups;
 - drag-along and tag-along rights;
 - options;
 - provisions relating to shareholder approvals;
 - minority shareholder protections;
 - rights of appointment of directors or unusual limits on the authority of the board of directors; and
 - enhanced quorums and veto rights on certain matters.

The seller should also provide a copy of the articles of association and bylaws registered before the Public Registry of Commerce.

- **Stock register (*Libro de Registro de Acciones*).** The stock ledger contains a full list of the company's current shareholders, the number of shares, class, and series owned by each shareholder, and notes that could reveal the existence of any pledges or liens created over the company's shares. The stock ledger could also show any discrepancies between the shareholding as described by the seller and the shareholding as recorded by the company.
- **Capital Variations Book (*Libro de Variaciones de Capital*).** In addition to the stock ledger, the seller should provide a copy of the company's capital variations book (*libro de variaciones de capital*), which contains a complete description of the capital variations of the company from the date of its incorporation. This book also evidences any discrepancies between the social capital described in the accounting records.

- **Pledges.** It is important to verify that the corporate seller has not pledged its shares in the target company and that the target has not pledged any of its assets. On an asset sale, it is important to check whether there are any pledges on the assets being sold. Searches for pledges over shares and movable assets could be performed online with the company's mercantile folio before the [Movable Guarantees Registry](#) (web site user registration required).
- **Board minutes, general shareholders' meeting minutes and corresponding public deeds.** All material actions of the company should be reflected in the minutes. Both board minutes and general shareholders' minutes could be a rich source of information, containing references to, for example, acquisitions and disposals, financing, litigation, poor or unusual operating results, issues of guarantees and security interests in the company's assets. The seller should also provide a copy of the shareholders' meetings minutes book (*libro de actas de asamblea*).
- **Minutes of management committees.** A review of shareholders' meetings and board minutes alone may not be enough if the board has formed management committees (for example, an executive committee) that engage in significant business.
- **Powers of Attorney and corresponding public deeds.** Individuals currently holding authorized powers of the target company must be identified not only for the execution of the purchase agreement or any other transaction documents, but for the buyer to identify which individuals should maintain those powers, or if they should be revoked or limited in a certain way at closing.
- **Minutes of statutory auditors.** All actions of the company affecting its financial and accounting situation should be assessed by the board of statutory auditors, which may raise objections if a transaction is against the company's interest.
- **Financial statements.** It is important to review the financial statements of the last three to five years of the company to understand its financial situation. The legal due diligence team should interact with the financial adviser to coordinate their findings and better understand the accounting data of the target.
- **Tax ID.** The seller should provide the buyer a copy of its Tax ID (obtained from the *Registro Federal de Contribuyentes*) and the documentation related to its tax filings for at least the five years prior to the due diligence, for the buyer to determine any tax contingency.
- **Management accounts.** Note that the seller may be reluctant to provide management accounts if the company has recently published its annual accounts.
- **Affiliates and Subsidiaries.** Company information should also be requested for any relevant affiliates or subsidiaries of the target company.

Furthermore, through recent reforms to the Tax Code, the Income Tax Law and other tax regulations, new obligations were established for companies, trustees, settlors, beneficiaries, financial institutions, members of the financial system, and notaries, among others, for the identification of the individual or group of individuals who qualify as controlling beneficiaries (*beneficiarios controladores*) of companies, trusts and other legal entities, including keeping information of those controlling beneficiaries in their accounting records and informing the tax authorities of their existence.

Individuals can be considered controlling beneficiaries if they, directly, indirectly, or contingently, either:

- Obtain the benefit derived from participation in a company, a trust, or other legal entity.
- Exercise control over the company, trust, or other legal entity.

In addition, by means of these regulations, the tax authorities were authorized to require obligated parties to provide the controlling beneficiaries information in an audit procedure which entitles them to verify compliance of the identification obligations and truthfulness of the information of the controlling beneficiary, as well as to impose sanctions and fines upon failure or default by the obligated parties.

In general terms, the following information should be obtained for each controlling beneficiary:

- Full name and surnames, which must correspond with the official document that certifies the identity (passport for foreign individuals).
- Aliases.
- Date of birth and, if applicable, date of death.
- Gender.
- Country of birth and nationality or nationalities, if applicable.
- *Clave Única de Registro de Población* (CURP, as per its acronym in Spanish, a unique code which identifies all Mexican citizens and residents) or its equivalent, in the case of other countries or jurisdictions.
- Country or jurisdiction of residence for tax purposes.
- Type and number or code of official identification (passport for foreign individuals).
- *Registro Federal de Contribuyentes* (RFC, as per its acronym in Spanish), tax identification number, or its equivalent, in case of being a non-Mexican resident for tax purposes as well as a document evidencing the tax identification number.
- Marital status and matrimonial regime (marital property system), as well as the document evidencing the marital status, official ID (passport for foreign

individuals) of their spouses, respectively, or official ID (passport for foreign individuals) of the concubine or concubinary, if applicable.

- Contact information: e-mail and telephone numbers.
- Home address and tax domicile.

Due to the complexity of the obligations regarding controlling beneficiaries and the current lack of uniform criteria by the authorities, compliance in full by obligated parties may be complicated. However, as a part of due diligence, the buyer should ensure that the required information has been obtained and is up to date, especially considering the excessive fines that could be imposed against the target company. Additionally, depending on the structure of the transaction, the buyer could eventually fall within the definition of a controlling beneficiary of the target company, and thus, it would need to comply with the corresponding obligations as of closing.

Material Agreements

Every business has agreements that are material to the success of its operation. These might include:

- Agreements with related parties.
- Supply agreements for crucial raw materials.
- Sales agreements (for example, output or requirements contracts).
- Intellectual property licences (for example, patent or trademark licences).
- Service or management contracts (for key staff).
- Labor agreements.
- Intercompany agreements.
- Agreements with any third-party that exceeds certain value.
- Collective bargaining or trade union agreements.
- Leases for important equipment (for example, computers).
- Real property leases for facilities.
- Joint venture agreements.
- Shareholders' agreements.
- License agreements.
- Loan and other debt agreements to provide capital to run the business.
- Pledge or mortgage agreements.

Other agreements, such as agreements to dispose of assets, businesses, or shares may subject the company to continuing liability with respect to a business sold previously.

In addition, when buying a company out of a group, intra-group transactions involving the target company need to be investigated to ensure they do not give rise to any contingent tax liabilities.

The due diligence enquiries need to identify those agreements that are material to the target's business. That is, those that will affect the price the buyer is willing to pay for the target or which pose material business or liability risks. The due diligence questionnaire will typically indicate the criteria by which a contract is considered material, for example, by value.

Having identified the material agreements of the business, the reviewer should check that the contracts are effective, that they have been executed properly and that they do not contravene any competition law or regulatory requirements.

The principal commercial terms of these agreements should be noted. The following questions are relevant to almost all enquiries:

- **Parties.** Are the parties to the agreement the persons to whom the agreement relates? For example, in a license of intellectual property, is the company using the intellectual property the company named in the agreement, or is the named party the parent or associated company of the user? Is the grantor of the license the legal and beneficial owner of the intellectual property?
- **Execution of the agreement.** Has the agreement been properly executed? Did the person signing the agreement have the proper authority?
- **Effectiveness of agreement.** Is the agreement too vague to be enforceable?
- **Assignment clause.** Is the consent of a third party needed for the transfer of the benefit of the contract? Should a notice be delivered to a third party, prior to or after closing?
- **Change of control clause.** Does the agreement stipulate that the consent of the other contracting party must be given on a sale of shares in the business or a change of control of the business? Does the change of control affect any employees, for example, will it require a payment or result in an extended notice period? Customarily, control is defined as the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of a company, whether through ownership of voting shares, by contract, commitment, arrangement, or otherwise. Therefore, it is important to review the corporate documents of the target company in detail to confirm all control mechanisms. Also, depending on the business of the target, certain governmental authorities will need to be notified of or provide their consent to any change of control, which should be

evaluated and addressed if not already provided for in the relevant agreement.

- **Deliverables.** Which commitments have been assumed by the company upon entering an agreement? What products, services, or results are expected to be completed by the target company?
- **Confidentiality.** Is the target already in breach of this clause in an agreement, possibly giving a right to damages against the target should it be acquired? How much will such damages amount to? What is considered confidential in the agreement? Will entering the transaction require the disclosure of information marked as confidential? Could the relevant counterparty provide its consent to mitigate the risk of default by the seller of its confidentiality obligations?
- **Warranties, guarantees, indemnities.** Warranties in most commercial contracts either relate to compliance with applicable laws and regulations or compliance with the quality standards and the specifications of the contract. Additionally, there are certain standard indemnities relating to breach of third-party rights, breach of contract and liability for damages. The extent of these warranties and indemnities should be noted and the buyer should identify both if its participation in the transaction could breach any of such warranties and if they are in line with the warranties set forth by the seller in the transaction documents.
- **Term and termination.** What is the date of commencement of the agreement? Is the agreement subject to conditions precedent, for example, a regulatory approval? When does the agreement terminate? Will a major supply contract, for example, terminate soon? Will any compensation be payable on termination of an agreement? What notice must be given to terminate the agreement? What actions entitle the other party (or the target) to terminate for breach? Is the agreement renewable? Is the renewal of the agreement convenient for the buyer and the operations of the target after closing? Are there any post-closing actions to be carried out by the buyer to renew the agreement?
- **Liability and exclusion clauses.** Is the liability of the other party or the target limited in respect of breach of the agreement? Is there an exclusion of liability in respect of the target's obligations or the other party's? If so, is it likely to be enforceable? Will the buyer assume the liability after acquiring the target?
- **Intra-group transfers.** Are all intra-group transfers to which the target is party made at arms' length? Were such transfers made in compliance with the transfer-pricing rules under the Income Tax Law? Do any such transfers give rise to any contingent tax liabilities?
- **Restraint of trade.** Are any restrictions imposed on any party's ability to conduct its business? Could such

restrictions be surpassed through delivery of notices or obtainment of consents?

The significance of issues raised by a review of the target's legal documents will often depend on whether the proposed transaction is a share sale or an asset sale. For example, a change of control clause may be of no significance on an asset sale whereas it might be crucial on a share sale. On an asset sale, the assignment clause will be critical.

Inevitably, material agreements will raise their own specific issues in addition to the above. The buyer's intentions also have a bearing on the review of material agreements. For example, if a loan to the target is to be repaid on completion, the provisions of the loan agreement relating to prepayment and redemption are critical. If it is to be left outstanding, the buyer will want to be sure that the terms are appropriate when applied to it as the new borrower, provided that the information concerning the loan will be duly reflected on the financial documentation of the seller or the target, as applicable.

Licenses and Authorizations

Depending on the business performed by the target company, it may be obliged to hold certain licenses and permits issued by the public authorities in Mexico, either on a federal, state, or local level.

The due diligence review should identify that all necessary licenses are in place, are duly held by the target company and are still in force. The necessary licenses and authorizations will depend on the nature of the business. For example, a company in the hospitality sector must hold an activity license issued by the city council where each of the businesses are located, and a company in the telecommunications and broadcasting industries must hold a valid concession title to provide such services.

A share sale transaction would normally not impact the status of the licenses and authorizations since the entity holding the given license or authorization (that is, the target company) does not change. Nevertheless, certain authorities require notice of changes of control. Failure to promptly deliver the notice may result in sanctions that could entail the revocation of the license or authorization.

In an asset sale transaction, the transfer of the license or authorization may imply either a notice to the given public entity or even the need to request prior authorization, depending on the license or authorization. Sometimes, licenses or authorizations may be granted personally, making its transfer impossible. The buyer should analyze and determine the need to cancel the license or authorization and,

if needed, file for a new one before the competent authorities.

Employment Matters

Regardless of the structure of the transaction, the human resources of the target should be carefully reviewed. The following aspects are key to due diligence regarding labor and employment matters:

- **Employment Agreements.** Are the employment relationships between the target and its employees regulated under a collective bargaining agreement or under individual employment agreements? It is important to have employment agreements formally executed in Mexico. The Mexican Federal Labor Law presumes the existence of an agreement and employment relationship between an individual who provides personal services and the one who receives them. The employment agreement regulates benefits and working conditions in general, and the absence of a formal agreement could give rise to labor liabilities against the target for non-compliance with those benefits or working conditions.

On the other hand, Mexican laws require collective bargaining agreements to be registered before the labor authorities. Collective agreements, if any, should be carefully analysed, because any default by the target or the buyer after closing, even regarding due notices to employees of the transaction, could bring about strikes or other collective claims by the union(s) of the target and potentially hinder the target's operations. In principle, collective bargaining agreements should be re-negotiated every two years. If there is any union in the target company, the buyer should assume and comply with this obligation.

- **Employees.** Are all the employees of the target company duly registered before the social security and housing authorities? Are there any foreign employees working for the target and, if so, are they duly registered before the Mexican immigration authorities? Are there any employees on maternity leave, or under any kind of leave of absence? Are there amounts due and payable by employees in favor of the target? What is the seniority of each of the employees of the target?

The buyer should decide, as part of the transaction structure, if it will continue with the employees of the target or not post-closing. If the buyer will continue with the employees, it will be necessary to address whether the buyer will become the new employer through an "employer substitution" process, honoring the benefits and other working conditions in place prior to closing. An employer substitution process occurs through the execution of an employer substitution agreement between the buyer and the seller, or the target, as applicable, and its registration

before the labor authorities, as well as prior notice to the employees, in the understanding that the buyer and the former employer shall be jointly liable for the labor obligations prior to the substitution and for up to six months after.

However, if the buyer decides not to keep the employees, the employees should be dismissed and duly indemnified in accordance with the applicable laws to avoid mass labor claims, and any unpaid amounts due to the employees should be liquidated upon indemnification. The transaction documents should clearly state which party should assume the responsibility for any labor claims which arise after closing.

- **Benefits and Contributions.** What are the benefits granted by the target to its employees? Are those benefits limited to the provisions of the law or are there any additional benefits? Are those benefits duly documented in the employment agreements? Is it feasible for the buyer to continue granting any additional benefits after closing? Has the target or the seller been paying the relevant quotas to the Mexican Social Security Institute (IMSS), the Mexican Workers' Housing Fund Institute (INFONAVIT), the Mexican Workers' Consumption Fund Institute (INFONACOT), and retirement fund contributions? Has the target or the seller withdrawn the corresponding income tax from their employees upon payment of salaries?

In principle, Mexican law sets forth minimum benefits to be granted by employers, such as profit sharing, Christmas bonus, holiday premium, holidays, retirement fund, and training. However, it is possible for employers to provide additional benefits such as private health or life insurance, food allowance vouchers, additional holidays, and a savings fund, among others, which would be included in the working conditions that should be honored by the buyer to avoid labor claims and employee disputes post-closing.

Moreover, failure to promptly pay quotas to the corresponding authorities or withhold the corresponding amount may result in the imposition of fines and tax liabilities, in addition to any amounts due plus surcharges and updates. These amounts should be considered and addressed by the buyer either for the purchase price or for a price adjustment mechanism.

- **Outsourcing.** Is the target currently using any form of outsourcing or insourcing structure? Have the necessary filings been made to register the target as a specialized services provider, if applicable? Has the target recently undertaken any corporate restructure to comply with the recent outsourcing reform and if so, have all corporate, tax, and labor requirements been met? If the target company has contracted specialized services, has it ensured compliance

by its services providers with their corresponding obligations?

In April 2021, the Mexican Congress approved a legal reform to the tax and labor laws, which became effective in September 2021, whereby all subcontracting schemes were prohibited, including outsourcing and insourcing structures, which were very common for Mexican companies. Following the reform, companies may only provide services to other companies (including companies within their own corporate group) if such services are not already contemplated within the other companies' corporate purpose. Additionally, companies must register before the labor authorities as a specialized services provider prior to providing services to other companies, provided that the companies may assume joint liability with their specialized services providers before the labor authorities in the event of default by the services providers to their obligations under the subcontracting reform.

During the due diligence process, the buyer will need to confirm if the target company complies with the reformed outsourcing obligations, since failure to do so may result in the imposition of significant fines, and which could be factored in the purchase price or as relevant obligations, representations, or conditions for closing. Furthermore, the buyer will need to confirm if the acquisition of the target or the business could give rise to the obligation to register as a services provider after the transaction has closed.

For more information on key employment law issues to consider when acquiring a company or business in Mexico, see [Practice Note, Employees: Cross-Border Private Acquisitions \(Mexico\)](#).

Litigation and Outstanding Claims

Most businesses experience litigation or other claims from time to time. Common due diligence issues include:

- **Pending and threatened claims.** How many claims are currently pending or threatened? What is the status of each claim? What is the likelihood of success on the merits? Are there any actions or contractual defaults of the seller or the target that could give rise to any claims or disputes of any nature? What is the estimate of damages? Such estimate amounts should be considered in the purchase price.
- **Litigation history.** Were there any large claims paid out in the past? Any class actions? What kind of claims is the target business a party to? Is any resolution or ruling a potential obstacle for the target to continue carrying out its business?
- **Litigation trends.** What are the common types of litigation? What is the average amount of damages? Are most claims settled or litigated?

Communicating Results of Due Diligence

During the Due Diligence Investigation

Part of the key to a successful due diligence investigation is making a correct analysis and interpretation of the data obtained, and promptly communicating the results to those responsible for assessing the proposed transaction and making the decisions. Communication within the parties and their advisors is essential for the due diligence process to flow.

The due diligence review is usually carried out in parallel to the negotiation of the acquisition and the drafting of the acquisition agreement. Any significant information that might affect negotiations or the drafting should be communicated immediately to a senior lawyer or the client even though the due diligence exercise is not complete. All members of the team must be alerted to potential deal-breakers so that they understand what information is important and must be shared as soon as it is discovered, what information is pending to be provided, which are the nice-to-haves and which information is not relevant or not applicable for the specific transaction.

Important information that comes to light during due diligence must be communicated to the buyer and to the directors of the buyer. Any problematic issues which come to light should then be raised at a full board meeting so that they could be properly considered by those responsible for approving the deal.

Due Diligence Summaries

It is important when reviewing due diligence to keep careful notes of the findings. Often the buyer's lawyers create a written record summarizing the key terms and conditions of each document. Such summaries should be carefully reviewed and updated upon provision of new or additional information and findings. For sample US-style templates of due diligence summaries, see [Standard Documents, Due Diligence Summary Template: Agreements](#) and [Due Diligence Summary Template: Organizational Documents](#).

Due Diligence Report

Once the investigation is complete, the information will be consolidated in a due diligence report, which should cover the business, financial, legal, and other specialist areas of the investigation. For certain transactions, this may be an informal report focusing only on matters material to the transaction. For others, it will comprise a complete audit of the target's business including an in-depth summary of the target's material contracts.

While the report will often be addressed to executive management, it should be in a form that could be circulated to the board in advance of the meeting at which definitive approval of the acquisition will be considered. For general guidance, see [Standard Document, Legal Due Diligence Report: Acquisitions \(UK\)](#).

Time must be allowed to review the report, follow up on further questions, and evaluate fully the implications of what is revealed.

Third-Party Reliance on the Due Diligence Reports

Sometimes (such as when the buyer finances the acquisition) the buyer is asked to share the due diligence report with a third party (such as the financing bank or members of the buying syndicate). Some firms permit the client to share the report, provided that the third party executes a non-reliance letter. Although most non-reliance letters state that sharing the report does not serve as a waiver of attorney-client privilege, it is unsettled whether such a statement preserves privilege. While it is common in Europe and gaining popularity in the US, lawyers should find out from their client whether it plans to share the report with any third parties and whether any third parties expect to rely on the reports. They should then consult with the deal team to determine the appropriate course of action. If the client shares the report, lawyers should remind their client that the third party may review the report with a different objective and that the information in the report may reveal sensitivities about the target company that the buyer may want to keep confidential.

In certain cases, the contents of the due diligence reports may be marked as confidential or exclusive, only for the benefit of the client, with the possibility to disclose its contents to third parties only through prior written approval of the lawyers or through the execution of a non-disclosure agreement by such third party. Nonetheless, it is also common for lawyers to issue a legal opinion instead stating that the target subject to the due diligence process is in general compliance with the applicable laws and that its documents are valid and in legal order for purposes of carrying out the transaction.

The possibility to disclose due diligence reports or information to third parties will depend on the participation and interest of such third parties in the transaction itself; however, the parties and any third party should abide by the confidentiality obligations protecting the transaction, the target, the seller, and the buyer.

Seller Due Diligence

Although this Practice Note is focused on the buyer, a prospective seller may wish to conduct its own due diligence of the target business or assets before and during the transaction to help it identify risks, deficiencies, and liabilities, enabling it to mitigate them before conducting the transaction.

A seller should also conduct due diligence on the buyer. This will help the seller assess if the buyer could afford the target business or assets and obtain information about the buyer that the seller may leverage when negotiating the purchase agreement. Also, if a seller will still hold a participation in the target after closing or share ownership to the assets, it should carry out due diligence on the buyer to ensure that such sale shall be free of risks and future liabilities or determine the best structure to mitigate them.

Furthermore, if the buyer is issuing stock to the seller as consideration or if the transaction is a merger of equals, the seller needs to conduct a thorough due diligence investigation of the buyer.

If the buyer is issuing stock, the seller should:

- Confirm that the buyer has authority to issue the stock.
- Confirm the value of the buyer's stock.
- Identify any corporate impediments or additional requirements to the issuance.
- Identify third party consents and governmental authorizations required for the issuance.

In a merger of equals, each party needs to:

- Confirm the value of the transaction.
- Identify steps necessary to integrate the companies.
- Learn more about the other's businesses.
- Identify any impediments to the transaction.
- Identify legal and tax obligations, consents, and authorizations required for the validity of the transaction.

Due Diligence Considerations for Private Equity Buyers

A private equity buyer may have a different view on certain due diligence issues. Private equity

Due Diligence for Private Acquisitions in Mexico

buyers are often more risk-averse because they are trying to make a relatively quick profit on a highly leveraged acquisition. Generally, a buyer who is currently operating in the industry (known as a strategic buyer) is better equipped to absorb an operational loss or messy litigation. As a result, private equity buyers often conduct more extensive due diligence reviews than other types of buyers and may seek greater contractual protections.

As opposed to a strategic buyer, a private equity buyer may not have certain operational capabilities. For example, if a private equity buyer buys a target business that does not have its own payroll department or IT systems, the private equity buyer will have to procure those services. A strategic buyer would likely have those services already in place for its existing business. As a result, a private equity buyer may need to focus on operational due diligence.

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