Due Diligence for Private Acquisitions (Mexico)

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A Practice Note considering the purpose, scope, and key practical aspects of a legal due diligence investigation for the purchase of a private company or business in Mexico. This Practice Note outlines the process for conducting legal due diligence under Mexican law, including how to organize the investigation, utilize virtual data rooms, and review information from various public registries. It explores specific areas of inquiry such as corporate records, material agreements, employment matters, environmental compliance, and IT infrastructure. Additionally, this Practice Note covers industry-specific risks, tax and financial due diligence, and anti-money laundering obligations under the Federal Law for the Prevention and Identification of Transactions with Illicit Proceeds (LFPIORPI). Finally, this Practice Note addresses crucial confidentiality and data protection restrictions under the Federal Law of Data Protection for Data in Possession of Private Individuals (Privacy Law), helping buyers navigate the complexities of cross-border transactions and mitigate potential liabilities before closing.

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.

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- 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 Federal Civil Code (*Código Civil Federal*) and its correlative provisions for the civil codes for the states of Mexico.

- CNA means the National Antimonopoly Commission (*Comisión Nacional Antimonopolio*), Mexico's federal competition authority. The CNA is a decentralized public entity (*organismo público descentralizado*) sectorized to the Ministry of Economy (*Secretaría de Economía*), with technical and operational autonomy. It is responsible for enforcing the Federal Economic Competition Law, reviewing reportable concentrations, investigating and sanctioning anticompetitive conduct, and promoting competition and free market access in Mexico. The CNA replaced the former Federal Economic Competition Commission following the constitutional and statutory reforms enacted in 2024 and 2025. For more information, see Practice Note, National Antitrust Commission (Mexico): Overview.

- COFECE means the Federal Economic Competition Commission (*Comisión Federal de Competencia Económica*), Mexico's competition authority that preceded the CNA.

- Foreign Investment Law means the Foreign Investment Law (*Ley de Inversión Extranjera*).

- GLBO means the General Law of Business Organizations (*Ley General de Sociedades Mercantiles*).

- Income Tax Law means the Income Tax Law (*Ley del Impuesto sobre la Renta*).

- Anti-bribery Law means the General Law of Administrative Responsibilities (*Ley General de Responsabilidades Administrativas*).

- Antitrust Law means the Federal Law of Economic Competition (*Ley Federal de Competencia Económica*).

- 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 los Particulares*). On 20 March 2025, a new Privacy Law was issued that repealed the former law. Under the new law, the Ministry of Anti-Corruption and Good Governance (*Secretaría Anticorrupción y Buen Gobierno*) replaces the Ministry of Economy as the competent body to regulate and resolve matters relating to data privacy. No secondary laws or regulations have been issued. Therefore, the former secondary laws and regulations remain in force.

- Ministry of Foreign Affairs means the Mexican Ministry of Foreign Affairs (*Secretaría de Relaciones Exteriores*).

- Tax Code means the Federation Fiscal Code (*Código Fiscal de la Federación*).

- VAT means value added tax.

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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. Nearshoring, which is the relocation of production or supply chains closer to the US, has further strengthened Mexico's strategic position as a key country for manufacturing and logistics. In addition, the 2021 reforms to Mexico's tax and labor laws that prohibited labor outsourcing schemes required Mexican entities 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:

- Give the buyer 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, deliver notices, or request and obtain specific waivers for certain obligations to carry out the transaction within the timeframe desired by the parties.
- Identify possible liabilities and determine the party to be held liable.
- Set the course of negotiations of transaction documents, including the scope of the seller's and target's representations and warranties and disclosure schedules of the relevant agreement.
- Establish indemnification procedures on default or misrepresentation.
- Set out certain conditions, the non-occurrence of which would be a deal breaker for the buyer.
- Ensure compliance with recent tax, labor, antitrust, and environmental, social, and governance-related regulations that may impact legal certainty, enforcement of contractual rights, and regulatory oversight mechanisms, including those introduced through the 2024 constitutional reforms, such as:
    - the dissolution of autonomous regulatory bodies, including the COFECE; and
    - the judiciary system restructuring.

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- Evaluate supply chain resilience and opportunities related to nearshoring trends, particularly those impacting the target's location, infrastructure, and regional trade advantages.

- Review the target's IT infrastructure, cybersecurity protocols, and data protection practices to anticipate technological and data protection risks.

- Determine whether the target carries out any activities considered vulnerable under the Federal Law for the Prevention and Identification of Transactions with Illicit Proceeds (*Ley Federal para la Prevención e Identificación de Operaciones con Recursos de Procedencia Ilícita*) (LFPIORPI) and assess compliance with applicable anti-money laundering obligations, including customer identification, recordkeeping, reporting obligations, internal compliance procedures, and appointment of the compliance representative, where applicable.

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.

However, certain logistical or practical difficulties can 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 can 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:

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- 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 parties should negotiate and agree on the expected scope of due diligence beforehand through the execution of the relevant offer and acceptance, letters of intent (LOI), term sheets, memorandums of understanding (MOU), 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 their registration, as applicable.
- Evidence of:
    - registration with the applicable registries;

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    - registration with tax and labor authorities; and
    - compliance with labor and social security obligations.

- Documents evidencing intellectual property (IP) of the target and registration of IP.
- Insurance policies held by the target.
- Documents relating to pending or threatened litigation, arbitration, or administrative proceedings.
- Cybersecurity, confidentiality, and data protection policies.
- AML compliance documentation, including evidence confirming whether the target performs vulnerable activities under the LFPIORPI and, if applicable, records evidencing compliance with customer identification, reporting, recordkeeping, internal policies, and filings with the Financial Intelligence Unit (*Unidad de Inteligencia Financiera*) (UIF).

Legal Due Diligence

Legal due diligence is usually carried out by an external law firm appointed by the buyer and can 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. This team ensures that 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 duly registered with 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 or special intercompany agreements (for example, cost-sharing arrangements, management services, IP licensing, or financing agreements) between 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?

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- Does the seller have good title to the shares in the target company?
- Does the target company have good title to its assets?
- Does the target company have any subsidiaries?
- Has the target company entered any services agreement that could potentially be considered an outsourcing scheme?
- Are there any unstated or understated liabilities or risks associated with the target company or its 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 can affect the target, the property, the assets, or the transaction in general?
- Does the target have any employees? Are these employees registered with the relevant authorities? Are there individuals at the disposition of the target company, or providing services to the target company, who could potentially be considered in an employment or outsourcing relationship with the target?
- 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 can affect the transaction (for example, a change of control clause or required consents or notices)?
- If providing or receiving specialized services, is the target company in compliance with the specific requirements regarding the subcontracting regulation (for example, requesting and maintaining certain information, reporting, registrations, and similar requirements)?
- Has the seller or the target company granted any kind of guaranty or security or executed any type of debt instrument that can 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, litigation, arbitration procedures, or any other judicial or non-judicial procedures 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?

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- Are the seller and the target company each generally in compliance with their legal obligations?
- Does the target company process personal data? If so, is it in compliance with the new Mexican Privacy Law and related regulations? Are privacy notices, databases, consent mechanisms, and cross-border transfers documented and properly managed?
- Does the target own or license any IP or technology that is core to its operations? Are all these rights duly registered or otherwise protected? Are there any IP disputes or risks of infringement?
- Does the target carry out any activities classified as vulnerable under the LFPIORPI? If so, has it complied with all applicable anti-money laundering obligations, including registration, customer due diligence (KYC), beneficial owner identification, record retention, filing of notices with the competent authorities, internal policies, and appointment of the compliance representative (where required)?

Detailed information on the target business is necessary for the buyer to be 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.
- Define certain activities that should be performed before closing to enable the parties to carry out the transaction as desired and cause the most effective financial and tax effects for the parties (for example, by transferring the shares of the target company to a trust).
- Request additional guarantees from the seller or a more stringent indemnification procedure.
- Determine any consents, waivers, 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 and specific obligations, deliverables, indemnities, or remediation processes in this regard.
- Plan the integration of the target business.
- Determine whether any ancillary documents are needed (for example, a transitional services agreement, trust agreement, or any other type of agreement that can be necessary to formalize the transaction).
- Determine deal breakers and nice-to-haves.
- Bargain with the seller.

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The buyer will inevitably seek contractual protection from the seller in the form of warranties and indemnities. In practice, the protection these offer may be limited by disclosures and other contractual provisions. Further, the Civil Code only recognizes guarantees in the form of pledges, bonds, and mortgages. Mexican courts may treat contractual warranties as mere representations rather than guarantees. Unlike in some other jurisdictions, it is not possible to submit a "misrepresentation" to Mexican courts as a ground for default. Therefore, the buyer and its advisors should carefully identify which representations should:

- Become a condition or obligation for closing.
- Require specific indemnities in the transaction documents.

Due to the 2024 constitutional reforms to restructure the Mexican judiciary system, including changes to the appointment and oversight of judges and justices, there is heightened uncertainty regarding the interpretation and enforcement of private law provisions in civil and commercial matters. These developments should be carefully considered when assessing the effectiveness and enforceability of contractual remedies in Mexico.

Commercial (or Business) Due Diligence

In addition to the legal due diligence review, specialist advisors 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's 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

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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 can 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 of 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 can have a material impact on the operation of the business after the transaction has closed.
- The required initial disbursement, 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 advisors 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 that can 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 advance payments (*pagos provisionales*)), VAT, and employees' withholding tax returns for the last five fiscal years.
- Copies of proof of payment for all requested tax returns.
- 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, relevant correspondence with fiscal authorities, correspondence relating to any queries, requests for information, audits, and settlements, notice of assessments, objections, appeals, settlement, and judgments.

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- Copies of all legal and accounting tax opinions received by the target.
- Copies of the latest tax audits with the corresponding details and status.
- Information regarding the calculation of the tax basis cost of capital assets.
- Details and copies of any negotiated or applicable special tax regime, exemption, special system, or tax benefit.
- Copies of the calculations related to wages, salaries, and social security contributions for the last five fiscal years.
- Copies of all tax attributes, considering net after-tax profit account, net paid-in capital account, tax losses pending amortization, income tax carry forward, favorable balances on taxes pending refund, negative net taxable income balance, and income tax credit on distributed dividends.
- Details of any cross-border transactions and financing and 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, can 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 the buyer have the appropriate personnel to run the business if the management team it acquires are not up to the 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?

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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, inquiries 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 is 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, the Mexican Antitrust Law provides that the CNA must approve certain mergers or acquisitions if the transaction exceeds a value threshold (currently approximately USD104 million).

Additionally, the Foreign Investment Law:

- Reserves certain industries for Mexicans only.
- Limits or requires prior authorization from the Ministry of Foreign Affairs for participation in certain industries by foreign companies, foreign individuals, and Mexican companies with foreign participants.
- Buyers should also pay particular attention to businesses that may perform activities classified as vulnerable under the LFPIORPI, even if they are not part of the financial sector. Depending on the nature of the target's business, the buyer should verify whether the target is subject to anti-money laundering obligations and whether it has complied with the applicable regulatory framework. Non-compliance may result in significant administrative sanctions and operational contingencies.

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 the 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, as a sale and purchase agreement or a merger under 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 can 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 framework and foreign or

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multinational anti-bribery laws and conventions, such as the US Foreign Corrupt Practices Act of 1977 (FCPA), if applicable to the target company (for example, 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 antitrust clearance before carrying 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). A transaction requiring CNA authorization, such as a merger exceeding the statutory value thresholds, must still be notified to the CNA and cannot close (and therefore does not become fully effective) until the relevant authorization is obtained. Therefore, the parties must discuss and determine reasonable timeframes for closing considering the regular timing to obtain authorization (about three months) or implement a gradual closing through which the parties enter into a series of preparatory transactions necessary before closing (for example, transfers of shares, trust agreements, promissory agreements, donations, and assignments) to pave the way toward a more efficient closing once authorized.

- 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 advisors 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 can 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 seller should prepare a due diligence list or checklist to understand the relevant information the buyer requires (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.

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- 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. Under Mexican law, the occurrence of the agreement's conditions retroactively changes the agreement date to the date of execution unless the parties agree otherwise. Therefore, the agreement regarding the corresponding conditions must be carefully reviewed. The retroactive effect can cause negative effects. For example, in a transfer of shares, the purchase would become effective as of the date of execution of the agreement, even if closing has not occurred, and taxes would become payable as of this date.

- 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 regarding 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), which are enforceable at the federal, state, and local level in Mexico depending on where the target company operates, 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 groundwater.

The aim will be to determine and allocate responsibility for clean-up and obtain protection where appropriate from the seller by establishing specific conditions, deliverables, and waivers for the target company to comply with environmental regulations and a reasonable timeframe for the target company's compliance, subject to the Mexican statute of limitations for environmental matters.

IT Due Diligence

If the target company is heavily dependent on IT, or its business is the provision of IT services or products, IT due diligence can 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

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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 continue after the transaction closes.

- IT assets are generally intangible IP 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, cybersecurity risks and data privacy breaches can 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 kinds of financial institutions or financial services providers (such as financial technology). Where the target company develops, deploys, or relies on AI systems, including automated decision-making processes or generative AI tools, IT due diligence should also cover the legal, ethical, and operational risks associated with these technologies. This includes reviewing compliance with existing and emerging AI governance frameworks to identify exposure to potential claims (such as bias or IP infringement).

Organizing the Due Diligence Process

Discuss Scope of Due Diligence with Buyer

It is helpful if the legal advisor meets with the buyer at an early stage to agree on the parameters of the investigation. At this meeting, the advisor 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 can make or break the deal (known as deal breakers).

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- 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 to the scope of the legal due diligence investigation at the outset and for the buyer to understand the limits of this scope.

The Due Diligence Team

It is essential that the acquisition team is made up of appropriate people under clear leadership 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 advisors and accountants. In some cases, it may also be necessary to retain outside consultants in other areas, such as regulatory compliance, environment, or insurance. Because the due diligence team can be large and comprise 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 environment, labor, tax, real estate, and IP 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 from the seller and target company that should be uploaded in the data room. To prepare the due diligence checklist, the buyer's advisors should read the main publicly available information on the target company (see Other Sources of Information).

In drafting the due diligence checklist, the advisor 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 inquiries 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 questionnaire section should be stand-alone so that it can be considered by the appropriate advisor.

The questionnaire should also include specific requests to determine whether the target performs vulnerable activities under the LFPIORPI and, if applicable, request the documentation evidencing compliance with corresponding anti-money laundering obligations.

These questions are usually 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

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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 is made available. Sometimes, especially in smaller transactions, the seller may send the buyer either 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 can submit a comprehensive request for access to the seller.

One key for successful due diligence is to maintain data rooms that are updated with new information that is promptly made available to the buyer.

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 advisors 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. 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 can be derived from a variety of sources, including the website 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 can be obtained if the company trades its securities on the Mexican Stock Exchange (*Bolsa Mexicana de Valores*).

Sources of Corporate and Financial Information

Key corporate information can be obtained from:

- The Commercial Registry (*Registro Público de Comercio*). Although this is usually provided by the seller, general information about real property and companies can be requested at the Public Registry of Commerce of the jurisdiction in which the real property or the company is located (see Company Searches).

- Statutory books. The GLBO requires all Mexican companies to keep:

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- a stock ledger containing the number of shares (or equity quotas) that each shareholder (or partner) owns in the company and general information of each shareholder (or 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' (or partners') meetings minutes book, which must contain a copy of the minutes of every shareholders' (or partners') meeting 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.

For more information, see Practice Note, Company Records and Registers (Mexico).

Companies in Mexico must preserve all their accounting books and information for the previous five years.

- Electronic Publication System (*Sistema de Publicaciones Electrónicas de la Secretaría de Economía*). This provides access to information on the current shareholder composition of a Mexican company and notices published by the company (such as calls for shareholders' (or partners') meetings or merger, conversion, or liquidation notices).
- Regulators. Government authorities publish information about companies under their supervision, such as operating permits and issued fines (for example, companies authorized to operate as a financial institution, financial technology providers, specialized services providers, and companies in other industries).

Sources of Information About Real Property

Information about real property, such as title deeds, mortgages, and certain third-party rights or claims over real property (for example, right of way, usufruct, or judicial seizures) can be obtained from the Public Registry of Property (*Registro Público de la Propiedad*) of the jurisdiction in which the real property is located (for a fee). Usually, all kinds of searches with this Public Registry must be carried out directly at the Public Registry's offices.

Sources of Information About IP

Information about trademarks and other types of industrial property can 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, or licenses. Searches with the Mexican Institute of Industrial Property are free and can be performed online on MARCANET.

Information about copyrights and related rights can be obtained from the Public Copyrights Registry (*Registro Público de Derechos de Autor*) for a fee. These searches must be carried out at the Public Registry's offices.

Sources of Information About Movable Assets

Public information on liens over a company's movable assets can be obtained from the Registry of Movable Guarantees (*Registro Único de Garantías Mobiliarias*) for a fee. This information can be obtained online by any third party that has the registry information (*folio mercantil*) of the company.

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Liens over certain movable assets, such as boats or airplanes, are subject to special regulation. This lien information can 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 can 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 that can 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 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 can 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 in the offer and acceptance, LOIs, term sheets, MOUs, or other preliminary documents selected to outline the terms of the transaction.

The knowledge that a business is for sale can also be unsettling for employees, customers, and suppliers. It can 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.

For more information about the use of confidentiality agreements in Mexico, see Practice Note, Key Documents for Acquiring a Private Company (Mexico): Confidentiality (or Non-Disclosure Agreement).

Disclosure of Sensitive Information

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

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

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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 CNA sanctions agreements consisting of the exchange of information that can negatively impact the market. An exchange of this information can:

- 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 CNA is aware that commercially sensitive information should be shared between economic agents during the due diligence process. In the context of due diligence, both the 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 help the exchange of information during mergers and acquisitions, the former COFECE 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 the 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 preference, health information, religious belief, and other details) cannot be compiled into any kind of database.

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 inquiries 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 can 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. Antitrust 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 review should also identify whether the target is subject to anti-money laundering regulations under the LFPIORPI and whether any deficiencies in compliance could give rise to administrative sanctions, reporting obligations, reputational risks, or post-closing remediation measures.

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

Corporate Information

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Company Searches

A company search at the Public Registry of Commerce can reveal certain information about a target company, such as:

- The company's incorporation date and original shareholders.
- A 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.
- Sometimes, powers of attorney granted by the company.
- Liquidation or winding-up resolutions.

The search must be carried out in person.

Which companies to search depends on the nature of the transaction. In most share purchases, the buyer or its advisors should search against the target and its subsidiaries, any companies in which the target has a significant shareholding, the corporate seller, and the corporate guarantor (if applicable). In 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 is not necessarily 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 at the Public Registry of Commerce.

Corporate Information Provided by the Seller

In addition to information obtained through a Public Registry of Commerce search, 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 in the same document, although the articles of association can be amended from time to time. The articles of association of the company can contain provisions of interest to the buyer, such as:
    - corporate purpose, especially if the target company has entered into services agreements that can potentially be considered as outsourcing schemes;
    - pre-emption rights on share transfers;

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- 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 with 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, including the number of shares, class, and series owned by each shareholder, and notes that can reveal the existence of any pledges or liens created over the company's shares. The stock ledger can 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, which contains a complete description of the company's capital variations from the date of its incorporation. This book also evidences any discrepancies with 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 can be performed online with the company's mercantile folio of the Movable Guarantees Registry.

- 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 can 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,

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but for the buyer to identify which individuals should keep 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 company's financial statements for the last three to five years to understand its financial situation. The legal due diligence team should interact with the financial advisor to coordinate their findings and better understand the target's accounting data.

- Tax identification number. The seller should provide the buyer a copy of its tax identification number, which is obtained from the Federal Taxpayer Registry (*Registro Federal de Contribuyentes*) and the documentation related to its tax filings for at least five years before the due diligence, for the buyer to determine any tax contingency.

- Management accounts. The seller may be reluctant to provide management accounts if the company has recently published its annual accounts.

- Affiliates and subsidiaries. The buyer should request company information for any relevant affiliates or subsidiaries of the target company.

Further, recent reforms to the Tax Code, the Income Tax Law, and other tax regulations established new obligations for companies, trustees, settlors, beneficiaries, financial institutions, members of the financial system, notaries, and others. The reforms include:

- Identifying the individual or group of individuals who qualify as controlling beneficiaries (*beneficiarios controladores*) of companies, trusts, and other legal entities.

- Keeping information on the controlling beneficiaries in accounting records.

- Informing the tax authorities of the controlling beneficiaries' existence.

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

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

- Exercise control over a company, trust, or other legal entity.

In addition, these regulations authorized the tax authorities to require obligated parties to provide the controlling beneficiaries' information in an audit procedure that allows the authorities to verify compliance with the identification obligations and truthfulness of the controlling beneficiary information and impose sanctions and fines on failure or default by the obligated parties.

Generally, the following information should be obtained for each controlling beneficiary:

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- 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.
- Unique public identification code (*Clave Única de Registro de Población*), which is a unique code that identifies all Mexican citizens and residents, or its equivalent for other countries or jurisdictions.
- Country or jurisdiction of residence for tax purposes.
- Type and number or code of official identification (passport for foreign individuals).
- Federal Tax Registry tax identification number, or its equivalent for a non-Mexican tax resident and a document evidencing the tax identification number.
- Marital status, matrimonial regime (marital property system), and document evidencing the marital status, as applicable.
- Official identification (passport for foreign individuals) of the controlling beneficiary's spouse, concubine (similar to common law marriage partner), or concubinary, as applicable.
- Contact information, including email 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 applied by the authorities, compliance in full by obligated parties can 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 significant fines that can be imposed against the target company. Additionally, depending on the structure of the transaction, the buyer can eventually fall within the definition of a controlling beneficiary of the target company and need to comply with the corresponding obligations at closing.

Material Agreements

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

- Agreements with related parties.

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- Supply agreements for crucial raw materials.
- Sales agreements (for example, output or requirements contracts).
- IP licenses (for example, patent or trademark licenses).
- Service or management contracts (for key staff).
- Labor agreements.
- Intercompany agreements.
- Agreements with any third party that exceeds a 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.
- Agreements with banking institutions.
- Pledge or mortgage agreements.

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

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

The due diligence inquiries 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 that pose material business or liability risks. The due diligence questionnaire typically indicates the criteria by which a contract is considered material, for example, by value.

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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 inquiries:

- Parties. Are the parties to the agreement the persons to whom the agreement relates? For example, in an IP license, is the company using the IP 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 IP?

- 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 before 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 the direct or indirect possession of the power to direct or cause the direction of the management and policies of a company, whether through ownership of voting shares or 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 must be notified 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 on 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 do these damages amount to? What is considered confidential in the agreement? Will entering the transaction require the disclosure of information marked as confidential? Can 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. The buyer should identify if its participation in the transaction could breach any of these warranties and whether they are in line with the warranties set out 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, regulatory approval? When does the agreement terminate? Will a major supply contract, for

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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 regarding breach of the agreement? Is there an exclusion of liability regarding the target's obligations or the other party? 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 arm's length? Were these transfers made in compliance with the transfer pricing rules under the Income Tax Law? Do these transfers give rise to any contingent tax liabilities?

- Restraint of trade. Are any restrictions imposed on any party's ability to conduct its business? Can these 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 often depends 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, but may be crucial in a share sale. In an asset sale, the assignment clause will be critical.

Inevitably, material agreements 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, if 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 require certain licenses and permits from public authorities in Mexico on a federal, state, or local level.

The due diligence review should identify that all necessary licenses are in place, duly held by the target company, and still in force. The necessary licenses and authorizations depend on the nature of the business. For example, a company in:

- The hospitality sector must hold an activity license from the city council where each of the businesses is located.

- The telecommunications and broadcasting industries must hold a valid concession title to provide these 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. However, certain authorities require notice of changes of control. Failure to promptly deliver the notice can result in sanctions that can entail the revocation of the license or authorization.

In an asset sale transaction, the transfer of the license or authorization can imply either a notice to the given public entity or the need to request prior authorization, depending on the license or authorization. Sometimes, licenses or authorizations can be granted personally, making a 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.

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Employment Matters

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

- Employment agreements. Are the employment relationships between the target and its employees regulated under a collective bargaining agreement or individual employment agreements? It is important to have employment agreements formally executed in Mexico. The 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 can give rise to labor liabilities against the target for non-compliance with those benefits or working conditions.

  Mexican laws require registration of collective bargaining agreements with the labor authorities. Any collective agreements should be carefully analyzed. Any default by the target or the buyer after closing, even regarding due notices of the transaction to employees, can bring about union strikes or other collective claims of the target and potentially hinder the target's operations. In principle, collective bargaining agreements should be renegotiated 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 with the social security and housing authorities? Are there any foreign employees working for the target? Are any foreign employees duly registered with the Mexican immigration authorities? Are there any employees on maternity leave or 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 employee of the target?

  As part of the transaction structure, the buyer should decide if it will continue with the employees of the target 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 before 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 with the labor authorities, as well as prior notice to the employees, in the understanding that the buyer and the former employer are jointly liable for the labor obligations before the substitution and for up to six months after.

  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. Any unpaid amounts due to the employees should be liquidated on indemnification. The transaction documents should clearly state which party should assume the responsibility for any labor claims that 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, the Mexican Workers' Housing Fund Institute, the Mexican Workers' Consumption Fund Institute, and retirement fund contributions? Has the target or the seller withheld the corresponding income tax from their employees on payment of salaries?

  In principle, Mexican law sets out 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, a savings

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fund, and other benefits that would be included in the working conditions that should be honored by the buyer to avoid labor claims and employee disputes post-closing.

In addition, failure to promptly pay quotas to the corresponding authorities or withhold the corresponding amount can result in fines and tax liabilities in addition to any amounts due plus surcharges and updates. The buyer should consider these amounts 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?

  A 2021 reform to the tax and labor laws prohibited all subcontracting schemes, including outsourcing and insourcing structures that were common for Mexican companies. Following the reform, companies can only provide services to other companies (including companies in their own corporate group) if these services are not already contemplated by the other companies' corporate purposes. Additionally, a company must register with the labor authorities as a specialized services provider before providing services to other companies. The companies can assume joint liability with their specialized services providers before the labor authorities for non-compliance by the services providers with their obligations under the subcontracting reform.

  During the due diligence process, the buyer must confirm whether the target company complies with the reformed outsourcing obligations. Failure to comply can result in significant fines, which can be factored into the purchase price or as relevant obligations, representations, or conditions for closing. Further, the buyer must 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? These estimated 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

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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.
- Pending to be provided.
- A nice-to-have.
- 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 that come to light should then be raised at a full board meeting so that they can 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. These summaries should be carefully reviewed and updated when provided 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 is 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 material matters to the transaction. For others, it includes a complete audit of the target's business, including an in-depth summary of the target's material contracts.

While the report is often addressed to executive management, it should be in a form that can be circulated to the board in advance of the meeting at which definitive approval of the acquisition will be considered. For general guidance (from a UK perspective), 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 the findings.

Third-Party Reliance on the Due Diligence Reports

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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 this 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 can be marked as confidential or exclusive for only the client's benefit with the possibility to disclose its contents to third parties only through prior written approval of the lawyers or the third party executing a non-disclosure agreement. 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 depends on the participation and interest of the third parties in the transaction itself. However, the parties and any third party should abide by the confidentiality obligations protecting the transaction, target, seller, and buyer.

Seller Due Diligence

Although this Note focuses 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 can 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 the sale is free of risks and future liabilities or determine the best structure to mitigate them.

Further, 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:

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- 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 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.

END OF DOCUMENT

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