

COMMENTS TO THE NEW MEXICAN SECURITIES LAW

INTRODUCTION

The purpose of this document is to summarize the most relevant provisions of the new Mexican Securities Law regarding companies who currently have their securities listed in the Mexican Stock Exchange, as well as with respect to the introduction of new provisions that promote the access of “medium size private companies” to the Mexican Stock Exchange. Given the broadness of the subject, we will not focus on other matters contemplated by the new Securities Law, including without limitation, provisions on intermediaries or participants in the stock market (such as stock brokers, depository institutions and others), registration requirements, accounting practices, the stock exchange regulations, the criminal and sanctions regime, and authority of the financial authorities, topics which will be the subject matter of another article.

The new Mexican Securities Law was published in the Official Gazette of the Federation on December 30, 2005, and substitutes in its entirety the Mexican Securities Law which had been effective since January 2, 1975. This new Law will be in force as of on June 29, 2006, that is, 180 days after its publication date.

There are two main reasons for issuing the new Mexican Securities Law, which are the following:

(a) To have a securities statute consistent with international standards that includes rights of disclosure of information to investors, minority rights and corporate governance; and

(b) To promote access of medium size private companies to the risk capital markets.

The failure of former laws which attempted to attract investments to the risk capital market in Mexican companies is obvious, mainly due to the lack of legal certainty to offer protection rights for investors, such as minority rights (in addition to the minority rights already provided for in the General Corporate Law), agreements between shareholders, exit mechanisms (such as “tag along” or “drag along” rights) and other instruments.

In order to propose a solution for the abovementioned concern, the new Securities Law introduces a new exception regime to the actual General

Corporate Law provisions, so that “medium size private companies” may voluntarily adopt corporate governance practices, minority protection rights and disclosure mechanisms. This new vehicle, called the “Investment Promotion Company” (*Sociedad Anónima Promotora de Inversión or SAPI*) which is a corporate regime that shall contain several exceptions to the current applicable regime for corporations according to the General Corporate Law. It is very likely that this new corporate regime will grant potential investors legal certainty, given that the new provisions include among other matters, clear and transparent rules for minority shareholders in the event that they elect to withdraw from such ventures (exit mechanisms).

The Investment Promotion Company is a more flexible vehicle legally located “in-between” an ordinary corporation regulated pursuant to the General Corporate Law and what the new Law calls a Public Company (*Sociedad Anónima Bursátil*), in other words, a company which stock is publicly traded. The Investment Promotion Company shall be at first, regulated by the new Securities Law and on matters not provided for by the new Law, by the General Corporate Law.

Pursuant to the new Securities Law, the Investment Promotion Company shall have the possibility to list its shares in the stock exchange within a three year transition period, which would allow such companies to gradually adopt corporate governance practices, disclosure policies and protect minority rights which would be in force for Public Companies.

There is no doubt that the Investment Promotion Company is going to be a more flexible instrument than the one contemplated for ordinary corporations under the General Corporate Law. Such flexibility might allow the flow of resources from funds or institutional investors seeking capital risk investments based on the legal certainty that the new provisions contemplated in the new Securities Law will provide, as well as the bridge for such companies to become a public company by listing their shares in a stock market. Notwithstanding the foregoing, we consider the risk that a corporation adopting the scheme of an Investment Promotion Company may never be transformed into a public company, hence, the materialization of the new Law’s intention of attracting medium sized companies to the stock market never occurs. In regards to the capital risk investment by investors in the Investment Promotion Companies, in addition to having a law granting legal certainty, we will have to wait and see if confidence exists in the country for such investors to be motivated to invest in this type of companies.

The other important reason for issuing the new Securities Law is to adapt our legislation to international practices and standards for public com-

panies, which tends to increase the flow of resources into companies already listed in the Mexican Stock Exchange. We have to take into consideration that Mexico has been trying to quickly adjust to world international practices and developments in the stock market arena, as was the case with the June 2001 amendments to the former Securities Law. Notwithstanding the foregoing, the new Securities Law intends to be an integral amendment that will provide the development and transparency of the Mexican stock market, placing Mexico at the same level of the recent evolution of world wide legislation targeted to corporations who list their securities in stock markets.

This new worldwide tendency for clearer rules governing publicly traded companies is a response to or the result of the well known corporate scandals related to information and accounting manipulations and majority shareholder abuses against minority shareholders or investors, such as the Enron, Worldcom, Parmalat and other similar cases¹. Nevertheless, we have to be aware of the risk involved in over-regulating, which may originate practical and legal problems, as well as cost increases for companies to adapt to the new set of rules imposed by the new Securities Law, which could hinder the good intentions that this new Law seeks. In addition, the Mexican stock market will have to evolve and expand in order to become more attractive so that new companies, Investment Promotion Companies or not, find the conditions required for listing their stock in the Mexican Stock Exchange.

One of the challenges of the new Securities Law will be to try to “institutionalize” Mexican public companies with similar regimes in other world markets. The great difference between Mexican public companies and the similar entities in other developed countries is that, in such countries, capital stock of such entities is pulverized and is held by institutional investors (in its majority), whereas in Mexico, the majority of the stock of public companies is held by shareholders or control groups actively involved in the management and administration of such companies.

1. INVESTMENT PROMOTION COMPANIES.

The new Mexican Securities Law (hereinafter the “LMV”) contemplates two different types of corporations which will be subject to the provisions of the new Securities Law: (i) the Investment Promotion Companies (*sociedades anónimas promotoras de inversion*); and (ii) the Public Companies (*sociedades anónimas bursátiles*). Investment Promotion Companies will not be subject to the supervision of the National Banking and Securities

¹ Including of course, the recent Unefon/Codisco case which involves the main shareholder of Television Azteca (the second TV company in Mexico), being resolved in the United States as well as in Mexico.

Commission (*Comisión Nacional Bancaria y de Valores*) (“CNBV”), as long as they remain as such. As we have mentioned above, the provisions of the LMV regarding Investment Promotion Companies (hereinafter “SAPIs”), have some exceptions to the provisions for corporations pursuant to the General Corporate Law in effect (hereinafter “LGSM”). SAPIs could be considered as an intermediary vehicle between the ordinary corporation and the Public Company (herein after “PCs”).

SAPIs may be initially incorporated as such or an ordinary corporation may adopt such modality later on, in which case, it shall have the favorable vote of the majority of its shareholders through an extraordinary shareholders meeting. The corporate name of SAPIs shall be freely chosen but shall also be composed by the expression “*Promotora de Inversión*” (Investment Promotion) or by its abbreviation “*PI*”.

SAPIs may include in their by-laws, besides the requirements provided for in the LGSM, any of the following provisions, in which case, such provisions shall also be included in its respective stock titles:

- (a) Restrictions with respect to the transfer of shares of a same series or class representing its capital stock;
- (b) Exclusion causes for shareholders or the exercise of retirement or separation rights, or the right to redeem shares, as well as to establish the price or the method to determine such price;
- (c) Issuance of shares that (1) do not confer voting rights or limit such voting rights, (2) grant non-economic rights or specifically grant only voting rights, (3) limit or broaden the economic rights, or (4) grant veto rights;
- (d) Implementation of mechanisms to be followed in the event of shareholders disagreements with respect to specific matters;
- (e) Broadening, limiting or denying their pre-emptive rights in the event of capital stock increases, or even providing for publicity methods other than the ones provided for in the LGSM; or
- (f) Liability limitation for damages and losses arising from directors’ or officers’ actions in connection with the breach of duty of care.

1.1. Management and Surveillance.

Management of SAPIs shall be entrusted to a board of directors² and they may adopt for their management and surveillance, the regime contemplated by the LMV for PCs, except for the independence requirement for board members, which will not be mandatory in this case. In the event that the SAPI elects such regime, the general manager (CEO equivalent), as well as the board of directors will be subject to the provisions set forth under the new LMV for such officers which are applicable to PCs regarding matters such as organization, tasks and responsibilities. If they do not elect such regime, then they will be subject to the provisions of the LGSM.

The SAPIs that elect the regime of the new LMV will not have the obligation to name a statutory examiner, however it will need to have an independent external auditor and an auditing committee that carries out the examiner's functions.

1.2. Minority Rights.

Regarding minority right exceptions according to the LGSM, SAPI shareholders representing ten percent (10%)³ of the shares of capital stock with voting rights (including limited or restricted) will have the right to (i) appoint a member to the board of directors, (ii) appoint an examiner (unless they elected to adopt the applicable regime of PCs, (iii) request the president of the board or an examiner to call a shareholders meeting or to adjourn any shareholder meeting in the event that they consider that they are not well informed with respect to a specific item of the agenda. Shareholders representing fifteen percent (15%) or more⁴ of the shares representing the capital stock with voting rights of a SAPI (including limited or restricted or without voting rights) may execute a civil liability action against the directors or the examiners in the benefit of the corporation pursuant to the terms of the LGSM⁵. They may also judicially oppose to the shareholders meetings' resolutions when they have a voting right in the corresponding matter, provided that they individually or jointly hold 20% or more of the capital stock of the corporation⁶.

² A SAPI may not have a sole manager as set forth in the LGSM for ordinary corporations.

³ In such cases the percentages established by the LGSM, this is 25%, would not be applicable.

⁴ In such case the percentage established in the LGSM is 33%.

⁵ The LGSM states that shareholders representing 33% of the capital stock, may exercise the civil liability action against the board members, only if the complaint comprises the total amount of liability against the company and not the personal interests of the plaintiff and that they have evidence that they did not vote in favor of the relevant resolution of the shareholders meeting.

⁶ In such case, the 33% established by article 201 of the LGSM, will not be applicable.

1.3. Agreements among Shareholders.

Shareholders of a SAPI may enter among themselves into (i) non-compete agreements (limited to 3 years, subject matter and geographic coverage), (ii) stock options to buy or sell shares (“put” or “call” options including “tag along” or “drag along” rights), (iii) agreements to restrict, transfer or regulate the pre-emptive rights for capital stock increases, not only with the shareholders as such, but with third parties as well, (iv) agreements to exercise voting rights in shareholders meetings⁷, or (v) stock placements through a tender offer.

The abovementioned agreements may not be opposed to the SAPI, unless there is a judicial resolution, and any breach of such agreements shall not affect the validity of any vote in any shareholders meeting. This means that any breach of such agreements, will only give right to sue the other shareholders for damages and losses or to the indemnity provided for in the specific shareholders agreement.

1.4. Acquisition of their Own Shares.

Another right (or exception) granted to SAPIs by the new LMV is the possibility for these companies to acquire their own shares⁸, prior the agreement of their board of directors, in which case, such shares may be acquired by the SAPI either through its (i) net worth (*capital contable*), in which case such re-purchased shares shall be kept by the SAPI without the need to reduce its capital stock or (ii) capital stock (*capital social*), as long as it is resolved to cancel them, or to convert them into issued but not paid in shares (*acciones emitidas no suscritas*) maintained as “treasury shares”. The placement of a SAPI’s own shares will not require a resolution from the shareholder’s meeting, however, the board of directors shall adopt the relevant resolutions. The issued but not paid-in shares maintained as “treasury shares” in the corporation may be subscribed by the same shareholders, in which case, the pre-emptive right established by the LGSM will not be applicable. Furthermore, SAPIs are not required to publish their financial statements pursuant to the LGSM⁹.

⁷ The new LMV establishes that for such purpose the provisions of the LGSM would not be applicable to SAPIs. The relevant provision in the LGSM states that any agreement restricting the free will voting right of a shareholder is null and void.

⁸ Again, this is an exception to the provisions of the LGSM which states an express prohibition for corporations (*sociedades anónimas*) to acquire their own shares.

⁹ The LGSM states the obligation for corporations to publish their annual financial statements in the official gazette of its corporate domicile as well as to deposit such financial statements before the relevant Public Registry of Commerce.

1.5. Transformation of a SAPI into a Public Company.

SAPIs may apply for the recording of their shares in the Mexican Securities Registry (the “Registry”) if their shareholders agree, prior to the registration, on the following: (i) the adoption of the PC modality within a period of three years as of the date that its registration is in effect; (ii) a program providing for the progressive adoption of the applicable regime for PCs within the abovementioned three year period, including the compliance of the requirements provided for in the regulations of the Mexican Stock Exchange (the “Transition Program”); and (iii) the necessary amendments to their by-laws. Also, at the time a SAPI applies for registration, it is required to have an independent director in their board (with the requirements stated in the LMV for such directors) and to have a committee that assists the board in the development of corporate governance practices in accordance with the provisions stated for PCs; provided that such committee shall be presided by the independent director.

The SAPIs that obtain the registration of its shares in the Registry may place such shares in the Mexican stock market with or without a public offer if: (i) the regulatory organization and disclosure differences between SAPIs and PCs are clearly stated in the prospectus or offering memorandum, the terms and conditions of the Transition Program, and a statement that the shares may only be acquired by institutional investors or by persons that expressly state in writing that they know the characteristics of SAPIs as well as the differences between an ordinary corporation pursuant to the LGSM and a PC and the risks that investing in this type of companies represent; and (ii) the Stock Exchange approves the Transition Program.

SAPIs that obtain and maintain the registration before the Registry will be subject to certain provisions applicable to PCs, provided that, the CNBV may, through the issuance of regulations (*circulares*), reduce the requirements for the registration and maintenance in the Registry of the shares of SAPIs as well as for the disclosure of information. The Stock Exchange will be obligated to periodically verify compliance by SAPIs of their Transition Programs and shall inform the CNBV of any breach thereto. A significant breach by the SAPI of the Transition Program will be considered as a cancellation cause of its registration.

2. PUBLIC COMPANIES.

In this chapter, we will only focus on the main modifications that the new Securities Law pretends to introduce regarding PCs. As mentioned above and notwithstanding the amendments to the former LMV on June of

2001 where some of the issues commented herein had already been matter of discussion in said amendment, the advantage of the new LMV is that it updates the corporate structure of PCs, focusing specifically on (i) the integration of the board of directors; (ii) the general management and surveillance of the company and delegating specifically in the CEO the day to day management of the PC; and (iii) clearly stating the rights and obligations of the board, the CEO, the independent auditor and the auditing and corporate governance committees.

One of the most relevant introductions of this new Law is the “consolidation” concept, not just of the entities controlled by the PC, but also by the group of companies that the PC is a part of, considering all of them as a sole economic and decision unit, hence the provisions of the new LMV are of consolidated application, specifically regarding disclosure of information or events affecting the group of companies related to the PC, board of directors’ tasks in auditing and corporate aspects (in such a way that such operation policies apply in a consolidating manner to all the group of companies that the PC is part of), as well as the accounting consolidation.

2.1. Management.

The functions of the board of directors and the general director (CEO equivalent) are modified, so that the board becomes a collegiate body focused on the strategy, surveillance, approval of relevant operations or with related parties of the PC, and the general director being responsible for the day to day operation of the PC’s businesses, which was already currently happening, hence, these modifications are considered a successful idea in the new LMV.

The management of PCs will be handled by the board of directors and the chief executive officer. The board of directors of PCs may be integrated by a maximum of 21 members¹⁰, of which at least 25% shall be independent¹¹. An alternate may be designated for each principal member of the board. The independent directors’ alternates must have the same said characteristic. In the event that the term for the appointed board members concludes, they shall continue in their functions for 30 additional days (if an alternate was not appointed)¹², provided that the board of directors may appoint provisional directors until the celebration of the corresponding shareholders meeting in which they may ratify or substitute such provisional directors.

¹⁰ The Code for Improved Corporate Practices recommends between 5 and 15 principal board members.

¹¹ Likewise, the Code for Improved Corporate Practices suggests that the independent members represent 20% of all the members of the board.

¹² For ordinary corporations, the LGSM states that the board members must continue in their functions until an alternate is appointed.

The board of directors will be assisted at least by the auditing and corporate governance committees, which will be integrated by independent board members and composed of by at least three members, with the exception of PCs that are controlled by a person or a group of persons that hold 50% or more of the capital stock of the PC, in which case, the auditing and corporate governance committees may be integrated by a majority of independent board members when this condition is disclosed to the general public.¹³

2.2. Independent Directors.

In addition to the restrictions already established in the former Law, the new LMV introduces other restrictions to the appointment of independent directors¹⁴ so that officers or employees of the PC or of the entity that forms part of the consortium or company group as well as the examiners of such companies or persons that have a “significant influence” or power to decide in the PC or in any entity that is part of the group or consortium of such PC, among others, are not considered to have the requirements to be an independent director.

The general shareholders’ meeting will qualify the independence of the board members, who must be chosen by their experience, competence and professional prestige, considering that they may carry out their functions free of conflict of interest and without being subjected to economic or personal interests. The CNBV may object the qualification of independence of the board members of a PC.

2.3. Authority of the Board.

The new LMV grants the board with non-delegation functions of the strategic management of the business, as well as the control and surveillance of the PC and of the entities and material officers controlled by such PC. The following are the main responsibilities of the board pursuant to the new LMV:

(a) to evaluate the activities of the CEO and other high rank officers;

¹³ This addition or exception was one of the most discussed issues before the Mexican Congress and one of the reasons why the approval of the new Law was delayed. It is important to take into consideration that practically all of the companies that are listed in the Mexican Stock Exchange fall into this premise, meaning that, their capital stock is held by one person or a group of persons representing more than 50% of such capital stock.

¹⁴ Pursuant to the Code for Improved Corporate Practices, the independent directors are those that are not involved in the day to day operation of the company and therefore may contribute an external and independent view, that is, that they are not linked with the corporations’ management team.

(b) to approve, with the preceding opinion of the competent committee (i) the policies for the use and possession of the assets owned by the PC or by the entities controlled by the PC; (ii) the transactions with related persons or with employees; (iii) unusual transactions or non-recurring transactions that in a fiscal year represent the acquisition or transfer of property with a value equal to or higher than 5% of the consolidated assets of the PC or the granting of security interests or the assumption of liabilities for an amount equal to or higher than 5% of the consolidated assets of the PC; (iv) the appointment, election and, as the case may be, the destitution of the CEO, as well as determining their integral salary, and the policies for retributions of other high rank officers; (v) the policies regarding the internal control systems as well as the accounting policies of the PC; (vi) the financial statements of the PC; (vii) the appointment of the external auditor; (viii) the reports that are required to be presented to the shareholders meeting pursuant to the LMV; and (ix) the terms and conditions of the power-of-attorney for acts of ownership of the CEO.

2.4. Obligations of the Members of the Board.

Members of the board of a PC must comply with the duty of care (*diligencia*) and the duty of loyalty (*lealtad*) provided for in the new LMV, namely, they must act in good faith and in the best interest of the PC and of the persons that it controls. Even though, the new LMV does not specifically define what should be considered as duty of care and duty of loyalty, the new LMV introduces guidelines on the subject or expressly includes those conducts that will give rise to a liability arising from the breach of the duty of care or from the duty of loyalty.

(a) Duty of Care. As guidelines for the duty of care, the new LMV states the following: (i) to be adequately informed in order to make the best decisions in favor of the PC, including the authority to solicit the necessary information for decision making; (ii) to request the presence of relevant directors and other persons, including the external auditor that may contribute to take adequate decisions in a board meeting; and (iii) to postpone the board meetings if they consider that they are not well informed or when the director was not called for such meeting.

The new LMV considers that board members breach their duty of care and therefore may become liable, when they cause patrimonial damage to the PC or to a company which it controls or over which it has influence, in the event that (i) they do not attend board or committee meetings and for such reason the meetings or committees are not able to validly function or make

decisions; (ii) they do not disclose material information to the board; or (iii) they breach their duties.

The responsibility to indemnify for damages or losses caused by a breach of the duty of care by board members, shall be joint and severally liable among offenders and such indemnity may be limited pursuant to the provisions stated in the by-laws of the PC or by resolution of a shareholders meeting, as long as it is not caused by willful, unlawful, or bad faith actions.

(b) Duty of Loyalty. Also as examples, the new LMV states that the duty of loyalty may consist of the following: (i) to conduct themselves and make decisions without any conflict of interest or to disclose it when a conflict of interest arises; (ii) to maintain discretion and confidentiality, obligating themselves not to disclose or use in the benefit of themselves or of third parties any information or documents that they have access to due to their office as board members.

Regarding the duty of loyalty, the board members and the secretary of the board shall maintain confidentiality with respect to material information and issues discussed in meetings which are not of public domain. In the event that a conflict of interest exists, they shall restrain from participating, as well as from being present in the deliberation and on the voting on those matters. It is important to highlight that the board members will be jointly and severally liable with the preceding directors if they had knowledge of irregularities and do not notify such irregularities in writing to the auditing committee and to the external auditor.

It is considered that board members are disloyal to the PC, and therefore, will be liable for damages and losses to the PC or to a company it controls or that significantly influences, when by virtue of its office the directors obtain benefits for themselves or in favor of a third party. Among other matters, the board members are disloyal when (i) they vote in board meetings when having conflict of interest; (ii) they do not disclose conflicts of interest; (iii) they knowingly favor a specific shareholder or group of shareholders in detriment of the other shareholders; (iv) they violate the policies and guidelines of the PC with the purpose of taking advantage of the PC's assets either for themselves or for a third party; (v) they improperly use material information that its not known to the public; or (vi) they take advantage of or exploit, for their own benefit or for that of a third party, business opportunities of the PC without the approval of the board.

2.5. General Director or CEO.

Pursuant to the new LMV and based on the functions provided for by the board, the CEO will have specific responsibilities that, according to the new LMV, include the functions of management, conduction and execution of the businesses of the PC and of the companies it controls, complying with, when applicable, the guidelines approved by the board of directors.

The principal functions of the CEO can be generally mentioned as follows: (i) the conduction of the day to day business of the PC; (ii) liability for the existence and maintenance of the accounting, control and registration systems; (iii) follow up and compliance of shareholder's meetings' resolutions; and (iv) the disclosure of material information.

The new LMV provides that the board may limit the ownership authority granted to a CEO of a PC. The CEO will also have the fiduciary duties of care and loyalty in the same terms as mentioned for board members. Lastly, the CEO will also be responsible to sign and execute all of the periodical and annual reports to be filed before the authorities and to be disclosed to the general public, together with the officer in charge of the respective area (either legal, financial or equivalents).

2.6. Board Members, CEO and other Relevant Officers' Liability.

Members of the Board, the CEO and relevant officers of a PC, as well as of the entities controlled or the persons carrying out similar functions in such entities shall not (i) generate, express, publish or grant false or misleading information; (ii) omit, order or not register transactions carried out by the PC or the entities controlled by it or in any other way, hide or alter any such transactions; (iii) to hide or omit material information, and (iv) destroy, modify all or any part of the accounting records or systems, as well as documentation supporting such accounting records. These officers shall be liable for damages or losses caused to shareholders or security holders of a PC, only when they intentionally carry out any of the abovementioned conducts.

PCs shall be jointly and severally liable before its shareholders or security holders for the payment of damages and losses in this regard, provided that, a PC may file actions against the responsible officers.

2.7. Surveillance and Control.

PCs are not subject to the provisions of the LGSM regarding the appointment of statutory examiners¹⁵, since such functions and obligations are expressly reserved to the board of directors of a PC. As mentioned above, the board of a PC will be assisted by the auditing and corporate governance committees in complying with these functions and obligations. Such committees may only issue recommendations; therefore, their resolutions will not be binding for the board, provided that, if the recommendations of the committee are not followed by the board, then, such event shall be disclosed to the market. It is not expressly mentioned but it can be interpreted that only one committee may follow up the corporate governance and the auditing functions.

2.8. Corporate Governance Committee.

The main functions of the corporate governance committee will be to review the transactions with related persons or transactions that are not within the ordinary course of business of the PC and of the persons controlled by such PC. This committee must also present in the annual shareholders meeting a report containing, among other matters, its observations regarding the CEO's activities and compensation paid, as well as an estimate of the benefits or disadvantages for the PC arising from transactions with related persons.

2.9. Auditing Committee and External Auditor.

This committee will have the main duty to carry out the surveillance of the accounting process of the PC, including without limitation, the evaluation of the independent external auditor, the elaboration of a report on the financial statements before they are presented to the board of directors, to inform the board with respect to the internal control mechanisms and to observe that the general accepted accounting practices and principles are duly followed.

The new LMV also provides for the express acknowledgement of the participation of the independent external auditor of the PC, limiting its participation exclusively to the auditing of the financial statements of the PC, provided that the most important requirements to become an external auditor of a PC are the independence as well as the lack of any kind of relation with the PC.

¹⁵ LGSM states that the surveillance of corporations will fall in one or more examiners.

2.10. Shareholders Meetings.

In addition to the provisions of the LGSM, the general shareholders meeting of PCs will gather to approve the transactions that the PC or the companies that it controls, wish to execute during a fiscal year, when such transactions represent 20% or more of the consolidated assets of the PC, and even shareholders holding limited or restricted voting shares may vote in such meeting.

An addition to the new LMV is that PCs may include measures in their by-laws in order to prevent hostile takeovers by third parties or by their own shareholders (also known as “shark repellent clauses”). In order for this type of provisions to be integrated into the by-laws of the PCs, it is required that such provisions (i) are approved in an extraordinary shareholders meeting in which 5% or more of the capital stock represented by shareholders do not vote against it; (ii) do not exclude one or more shareholders, other than the person that pretends to acquire control of the economic benefits arising from such provisions; (iii) do not absolutely restrict the takeover of the PC; (iv) do not contravene the provisions of the LMV for mandatory acquisition public offers ; and (v) do not deny the property rights of the buyer.

The new LMV states the prohibition for PCs to enter into agreements allowed for SAPIs, specifically restricting the share transfers, shareholders exclusion or execute separation rights and issuance of shares that do not provide or limit voting rights, grant non-economical social rights, limit or broaden the distribution of dividends or confer a veto right; however, PCs may issue limiting or restricted voting shares or without voting rights, only if such shares do not exceed 25% of the total paid in capital stock that the CNBV considers as placed in the trading market.

Notwithstanding the foregoing, the shareholders of a PC may enter into non-compete agreements, “put” and “call” agreements, agreements to regulate pre-emptive rights, and agreements to exercise the voting right, only if such agreements are notified to the PC within the next five (5) business days following its execution for the purpose of disclosing to the market the existence of such agreements. As in SAPIs, such agreements will not be opposable to the PC and its execution will not affect the validity of the vote in shareholders meetings, having legal effects only between the parties involved once disclosed to the market.

2.11. Minority rights.

In addition to the minority rights previously discussed¹⁶, the new LMV states that shareholders with voting right (even if limited or restricted) that individually or jointly hold 10% of the capital stock, will have the right to (i) appoint and revoke a member of the board of directors; (ii) request the president of the board or to the presidents of the committees to summon a general shareholders meeting, without applying the provisions on this matter as set forth by the LGSM¹⁷; (iii) request only once, that the voting on an issue which they consider themselves to be un-informed be postponed, disregarding the provisions set forth by the LGSM regarding the matter¹⁸.

Likewise, those shareholders that hold 20% or more of the capital stock may judicially oppose to the resolutions of the general shareholders meeting in which they have a voting right, disregarding applicable provisions of the LGSM¹⁹.

2.12 Shares of the PCs.

The PCs may issue unsubscribed shares held in the corporation's treasury for later subscription by the public, provided that (i) the general shareholders meeting approves the maximum amount of capital stock increase and the conditions for the corresponding issuance of shares; (ii) the share's subscription is effected by public offer, with previous inscription in the Registry; and (iii) the subscribed and paid in capital stock amount is announced when the authorized capital represented by the issued unsubscribed shares is published. In such event, the pre-emptive right for subscription stated in the LGSM will not be applicable regarding capital stock increases by public offers.

As previously mentioned, the CNBV may authorize the PC's issuance of shares with limited, restricted or with no voting rights, provided that they do not exceed 25% of the total paid-in capital stock that the CNBV considers placed before the market on the date that the public offer takes place. The

¹⁶ See for example, section 1.2 of this document.

¹⁷ For these cases, the LGSM establishes that the percentage for shareholders to request the board or examiners to summon a shareholders meeting is 33%.

¹⁸ Likewise, for this case, the LGSM establishes that the shareholders holding 33% of the shares represented in a shareholders meeting, may postpone the meeting when they are not properly informed on the issue.

¹⁹ The LGSM establishes that shareholders representing 33% of the capital stock may judicially oppose the resolutions of the shareholders meeting.

CNBV may broaden the percentage abovementioned in the case of compulsory convertible shares into ordinary shares within a term of no more than five (5) years or when investing schemes limiting the voting rights due to the shareholder's nationality. The shares without voting rights will not be accounted for in determining the legal quorum for the shareholders meeting and the shares with limited or restricted voting rights will be only computed in meetings in which such shareholders are allowed vote.

The new LMV prohibits any person to create mechanisms by which ordinary shares and shares with limited, restricted or non voting rights of the same PC are jointly negotiated or offered, except if they are convertible into ordinary shares within a maximum term of five (5) years. Likewise, ordinary shares with the purpose of issuing participation certificates that represent such shares and forbid the entirety of its titleholders to freely execute their corresponding voting rights may not be contributed into trusts, without such prohibitions being applicable to credit instruments representing shares of the capital stock of two or more PCs or to investing schemes limiting the voting rights due to the nationality of the shareholder.

As intended by the previous law, the new LMV states that PCs may acquire their shares without applying the prohibition stated in the LGSM, provided that (i) the acquisition is executed through a national stock exchange; (ii) the acquisition and the transfer in the stock exchange is executed at market price, except for auctions authorized by the CNBV; (iii) the acquisition is carried out against its net worth, while being able to hold them without the need to reduce its capital stock or against its capital stock, in which case they are converted into unsubscribed treasury shares without the need for a shareholders meeting resolution; (iv) the ordinary general shareholder's meeting agrees for each term the maximum amount of resources that may be destined to the purchase of its own shares, with the only limitation that the sum of resources that may be destined to such purpose does not exceed the total amount of the net earnings of the PC, including retained earnings; (v) the PC is current with the payment arising from obligations regarding debt instruments registered in the Registry; and (vi) the acquisition and transfer of shares that represent such titles does not exceed 25% of the shares without voting rights or of limited or restricted voting rights.

3. TRANSITORY ARTICLES.

The transitory articles of the new LMV state that existing PCs will have a 180 day period starting as of June 29, 2006, which is the date on which the LMV will become effective, to adapt their by-laws to the new provisions of the new LMV, meaning they have a 360 day period computed as of De-

December 30, 2005, provided that the corporations that have their shares representing their capital stock already inscribed in the Registry on the day that the LMV becomes effective, will acquire automatically the PC status by law.

In addition, PC shareholders whose holding of shares is contributed in trusts when the LMV begins to have legal effects, through which the voting right of various shareholders are carried out in the same way (or if various shareholders have granted a power of attorney for such effects), must notify such circumstances to the PC within the next 180 days following the effective date of the LMV, that is, 360 days computed as of December 30, 2005, so that such situation be disclosed to the market.

In the meantime that the financial authorities issue the general rules (*circulares*) established in the LMV, the regulations issued before effective date of the LMV will remain current in matters that do not contravene said provision.

4. CONCLUSIONS.

In general terms, we can conclude the following:

(a) It is likely that the introduction of the “Investment Promotion Companies” in the new LMV will promote access to medium size companies to the stock exchange. However, in our opinion this new type of corporation will provide a flexible vehicle that may attract risk capital investments to Mexican companies. It has been said that risk capital investment has not been developed in Mexico due to the lack of legal certainty for investors, mainly due to the rigid current regime for corporations under the LGSM. By including protection rights for minority shareholders, the possibility for shareholders to enter into agreements among themselves, in which they may validly agree on exit mechanisms or other similar agreements, this new instrument may grant investors with the legal certainty they need to invest, and in any event, withdraw from said corporations.

(b) As an additional step to convert a SAPI into a PC, the new LMV provides the necessary transitory elements to achieve such transformation, including the approval of its shareholders meeting, the adaptation of the requirements to disclose information to the market, the appointment of an independent member of its board of directors and the strategic three year transitory period to adopt PC’s obligations, which shall be approved by the relevant authority.

(c) The limitation so that only institutional investors and persons who expressly accept the risks involved in investing in PCs is reasonable, considering the required transitory period needed for the transformation of a SAPI into a PC.

(d) It shall also be interpreted that a regular corporation incorporated pursuant to the LGSM does not need to adopt the SAPI regime in order to list securities in a stock exchange. Such regular corporation may perfectly become a PC if it complies with the requirements provided for in the LMV for said effect.

(e) Considering the size of our economy, it is considered that investments in the Mexican stock exchange have not reached that same level. Therefore, even though there may be more reasons, from a legal standpoint, in our opinion the institutionalization in the management of publicly traded companies through the new LMV was a smart move, because it will give investors, shareholders and the market clear and transparent rules which will try efficiently to avoid frauds or manipulations of PCs.

(f) Due to the recent evolution in world legislation and tendencies of companies listed in stock exchanges and mainly because of the world known corporate scandals, this new LMV will place Mexico at the same level with such changes and evolutions, which will allow Mexican companies to attract new capital and more permanent investors. It is important to highlight that one of the main reasons for investors to decide on the final destination of their investments is the security or legal certainty that the legal framework provides, therefore in this particular matter, Mexico needs to be on the same level with the international standards for stock exchanges around the world.

(g) Regarding PCs, this new LMV will consolidate the applicable rules in order to improve its management and organization through the modernization of its corporate structures and its liability regime, which makes said management and organization more congruent, notwithstanding that this was happening in practice.

(h) The new LMV distinguishes the different roles to be assumed by the board of directors, the CEO, the committees as well as the independent auditor, which again, equals said provisions to what was already happening in practice.

(i) The CEO's main responsibility shall be the day to day management of the PC and the disclosure of relevant information. The board of director's main responsibilities shall be the management and the surveillance of the PC,

responsibilities which shall be assisted by the auditing and corporate practices committees and the external auditor.

(j) The consolidation concept on PCs adopted by the new LMV is very positive as long as the concept is not abused in the opposite sense. For such purpose, the PC as well as the companies controlled by it or the group of companies that are part of the PC shall disclose to the market any information of any of such companies that has an effect on the value of the securities of the PC. The consolidation concept also includes the institutionalization of management practices in all of the abovementioned companies (the PC, the companies controlled by the PC and the group of companies that are part of the PC).

(k) The role of the Auditing Committee and the Corporate Governance Practices Committee is consistent with what has been said in the Code for Improved Corporate Practices, as well as regulations issued by the CNBV on the matter. What may be criticized is the last minute exception included by the *Camara de Diputados* (Mexican House of Representatives) regarding that the integration of said committees must be by independent board members except in the case where one group of shareholders holds 50% of the capital stock, which practically includes all of the PCs listed in the Mexican Stock Exchange. Truthfully, the exception supports the reality of the companies listed in the Mexican Stock Exchange; however, this might compromise the “institutionalization” of the PCs.

(l) Furthermore, it is important to highlight that the auditing committee as well as the corporate governance practices committee, may only issue recommendations to the board of directors and in the event that such recommendations are not attended, then they must be disclosed to the market.

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