

Mexico's FIBRA E Legal Framework

In the framework of the third government report of Mexico's Constitutional President, Enrique Peña Nieto, early in September this year, it was announced the implementation of several actions seeking to promote Mexico's economic development. Among such initiatives, it was announced the creation of "FIBRA E" as a new investment vehicle that will allow private and public participants to monetize assets characterized by having stable and predictable cash flow, under a tax regime that reduces levels of taxation and therefore allows for greater distributions. Mexico's FIBRA E introduces an investment alternative substantially similar to the MLPs (*Master Limited Partnerships*) that have been traded in the United States since 1981, which market capitalization in the US, in accordance with the Alerian MLP Index, reaches US\$511bn, as of December 31, 2014.

Following the announcement of FIBRA E, the Executive Branch, through the Ministry of Finance and Public Credit (*Secretaría de Hacienda y Crédito Público*) published on September 17, the resolutions that amends the current tax framework in order to incorporate the tax regime applicable to FIBRA E, which will contribute to the capital advantage of FIBRA E over other financial instruments. Likewise, even date, the Mexican Banking and Securities Commission (*Comisión Nacional Bancaria y de Valores*) submitted for public consultation with the Federal Commission on Regulatory Improvement (*Comisión Federal de*



Mejora Regulatoria – “Cofemer”), the draft of proposed amendments to the securities regulations, in order to regulate the FIBRA E as an issuer under the Mexican securities market and to provide for minimum corporate governance requirements for such investment vehicle (the “Proposed Amendments”). Note that the provisions contained in the Proposed Amendments may be modified as a result of the process of public consultation currently undertaken by the Cofemer.

What is FIBRA E?

FIBRA E is a trust created in accordance with the laws of Mexico with a Mexican banking institution acting as trustee, qualified as a FIBRA E for tax purposes, that issues publicly traded securities in the form of trust bonds or *certificados bursátiles fiduciarios de inversión en energía e infraestructura* (“CBFEs”), registered with the National Securities Registry (*Registro Nacional de Valores* – the “RNV”) and listed in the Mexican Stock Exchange (*Bolsa Mexicana de Valores, S.A.B. de C.V.* – the “BMV”), in accordance with Securities Market Law (*Ley del Mercado de Valores* – the “Securities Law”) and its regulations (*Disposiciones de carácter general aplicables a las emisoras de valores y otros participantes del mercado de valores* – the “Regulations”). As provided in the Securities Law, the CBFEs shall grant its holders a pro rata property right with respect to trust assets.

To qualify for tax purposes as a FIBRA E, among other requirements¹, the main purpose of the issuer trust shall be to invest in the capital stock of Mexican companies (hereinafter, the “Promoted Companies”), which 90% of its annual taxable income derives from the following activities (hereinafter, the “Qualifying Income”):

- The treatment, refining, transportation and storage of oil; the processing, compression, liquefaction, decompression, regasification, transportation, storage and distribution of natural gas; the transportation, storage and distribution of oil products; and the transportation by pipeline and subsequent storage of petrochemicals, among others.
- The generation, transmission and distribution of electricity, in compliance with the Electric Industry Law and its Regulations.
- Infrastructure investment projects that include concessions, services or any other contractual arrangement executed between private parties and the government for performing services for the public sector or the final user, provided that such projects are currently in operations and have a remaining term of at least 7 years, in the following areas:
 - (i) Roads, highways, railways and bridges;
 - (ii) Ports, maritime terminals and port facilities
 - (iii) Civilian airfields, excluding private ones;
 - (iv) The expansion of the country’s telecommunications network;
 - (v) Public safety and social reintegration;
 - (vi) Drinking water, sewerage and wastewater treatment.
- The administration and management of the FIBRA E trusts.

Formation of FIBRA E

A corporate sponsor (the “Sponsor”) typically would form and contribute to the FIBRA E, equity interests in Promoted Companies (in whole or in part) that generate Qualifying Income via share transfer or contributions in kind, spin-off or merger, and the Sponsor would typically receive CBFEs in exchange and other rights to receive a greater portion of the FIBRA E incremental cash flow in the future, subject to the payment of a preferred return to the security holders² (“incentive distribution rights” or “IDRs”). Structuring the contribution of such interests will be directly driven by the tax regime applicable to the formation of the FIBRA E and other legal issues, such as contractual prohibitions on asset transfers, consent requirements, licenses and permits, debt covenants, among others.

¹ Please refer to our Tax Alert “Mexico’s FIBRA E tax regulations – General Requirements of the FIBRA E Regime” in the following link [http://www.eyboletin.com.mx/boletines/energy_alert/Energy_Alert_FIBRAE_18_de_septiembre_2015ENG.pdf], for a detailed description of the requirements that the issuer trust must comply in order to be eligible for the FIBRA E’s tax regime.

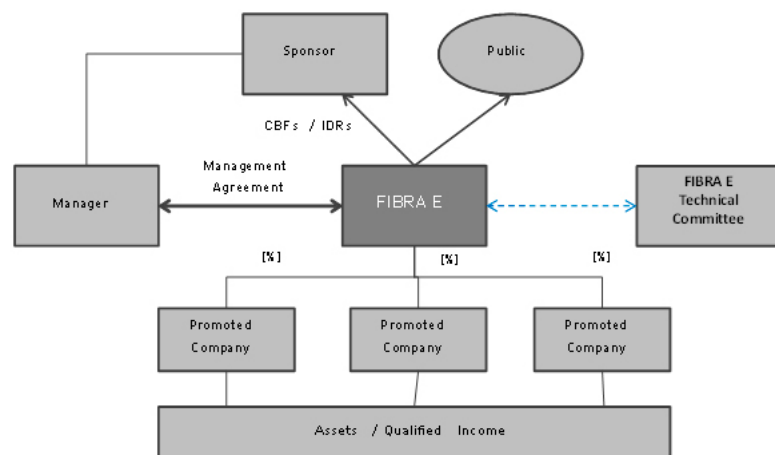
² In accordance with the applicable tax regulations, in order for the issuer trust to be treated as a FIBRA E for tax purposes, any compensation, commissions, fees, incentives or distributions to the Manager shall be subordinated to a preferred return to the holders of CBFEs, except for commissions, fees or distributions that are required for the proper functioning of the trust.

The Promoted Companies will be treated for tax purposes as a “pass through” entity – under the applicable regulation of a Mexican business trust – and would not be subject to the 10% dividend tax withholding applicable to other Mexican legal entities³.

The ownership of a FIBRA E may be divided into two main groups of security holders: the public and the Sponsor. In accordance with the Proposed Amendments, the FIBRA E may issue different series of CBFEs, including preferred (with limited voting rights) and subordinated CBFEs, the latter typically held by the Sponsor.

The Sponsor or any other person generally controlled by the Sponsor (the “Manager”), would manage the assets of the FIBRA E, in accordance with terms and conditions of the relevant Management Agreement and subject to the security holders’ rights provided in the Securities Laws and its Regulations, as described further herein.

Below is a chart summarizing a typical structure for FIBRA E:



Distributions by the FIBRA E

In accordance with the tax regime recently approved for the FIBRA E, the trustee shall distribute to the security holders at least 95% of the FIBRA E's tax result⁴.

Securities laws regulations applicable to FIBRA E

In view that the FIBRA E undertakes a public offering in Mexico, the issuer trust needs to satisfy all procedures before the CNBV and disclosure requirements contained in the Securities Law and its Regulations, in order to obtain the CNBV's authorization to carry out the public offering. Such requirements include, without limitation, the preparation and authorization of a prospectus and other documents directly related to the offering, such as financial statements, underwriting agreement, trust bonds certificate, opinions of external counsel and auditors, among other documentation.

After the IPO, the FIBRA E would be required to periodically furnish certain information to the CNBV and the BMV, including unaudited quarterly financial statements and audited annual financial statements, as well as various periodic reports related to material events.

Governance of FIBRA E

In accordance with the Proposed Amendments, the FIBRA E would be subject to certain corporate governance minimum requirements. Below is a brief description of the applicable corporate governance requirements for FIBRA E, pursuant to the Proposed Amendments:

³ Please refer to our Tax Alert "Mexico's FIBRA E tax regulations – Tax Regime Applicable to a Promoted Company" in the following link [http://www.eyboletin.com.mx/boletines/energy_alert/Energy_Alert_FIBRAE_18_de_septiembre_2015ENG.pdf], for a detailed description of tax treatment of Promoted Companies.

⁴ Please refer to our Tax Alert "Mexico's FIBRA E tax regulations – Tax Regime Applicable to FIBRA E Investors" in the following link [http://www.eyboletin.com.mx/boletines/energy_alert/Energy_Alert_FIBRAE_18_de_septiembre_2015ENG.pdf], for a detailed description of tax treatment of FIBRA E's security holders.

Security Holders Meeting

The security holders meeting has the authority, among others, to approve the following matters: (i) any amendment to the investment policy of the trust estate, (ii) the approval of the financing policy of the FIBRA E or any amendments thereto; and (iii) the removal of the Manager upon the occurrence of the events of default provided in the governing documents of the FIBRA E, with the vote of security holders of 66% of the outstanding CBFES. The governing documents shall contain, in any case, the following events of default: (a) omission by the Manager to inform the security holders of its management activities; (b) fraud, negligence or willful misconduct by the Manager; and (c) material breach by the Manager to its duties and obligations.

Minority rights

The Regulations provide for the following minority rights of CBFES holders:

- Security holders having, individually or as a group, 20% or more of the outstanding CBFES, may judicially oppose to the resolutions of the security holders meeting. The holders representing 20% or more of the outstanding securities shall have not attended the meeting or otherwise voted against the relevant resolution in order to exercise the aforementioned right.
- Security holders having, individually or as a group, 15% or more of the outstanding CBFES, may claim corporate liability against the Manager for any breach of its obligations.
- Security holders having, individually or as a group, 10% or more of the outstanding CBFES, may nominate and appoint one member of the Technical Committee, per each 10% of CBFES; except in the event that the governing documents of the FIBRA E grant to the Manager the right to appoint all members of the Technical Committee.
- Security holders having, individually or as a group, 10% or more of the outstanding CBFES, may request the common representative to call for a general security holders meeting or postpone a meeting only once, by three calendar days without need for further call, if they deem to have not been properly informed regarding the items of the agenda.
- All security holders are entitled to receive all information and documentation related to or subject matter of any security holders meeting, with at least 10 days in advance of such meeting.
- Security holders may enter into voting agreements, which shall be disclosed to the public.

Series of CBFES

The governing documents of the FIBRA E may provide for different series of security holders, including preferred and subordinated CBFES. In the case of subordinated CBFES, any distributions to the holders of such securities would be subordinated to the payment of any agreed distributions in favor of the holders of preferred CBFES.

The holders of preferred CBFES, which would typically have limited voting rights, shall be, in any case, entitled to vote with respect to the following matters: (i) any increase to the compensation or commissions of the Manager or the members of the Technical Committee; and (ii) any amendments to the purpose of the issuer trust or the extinction of such trust.

Technical Committee

In accordance with the Proposed Amendments, the FIBRA E's Technical Committee shall be integrated by a maximum of 21 members of which at least a majority of such members must be independent. Independence shall be qualified with respect to the Promoted Companies, the Sponsor and the Manager. Any auxiliary committees (i.e. Conflicts Committee, Audit Committee, among others) created by the Technical Committee, shall be integrated by independent members only.

The members of the Technical Committee may enter into voting agreements, which shall be disclosed to the public; in the understanding that, if the FIBRA E has issued CBFES with limited voting rights or its governing documents grant the Manager the right to appoint all members of the Technical Committee, any such agreements shall not contain any provision by which the members of the Technical Committee are required to vote in agreement with the members of such Committee appointed by the Manager.

The Technical Committee would have the following duties:

- Supervise the Manager's activities.
- Review the quarterly report submitted by the Manager to the Technical Committee.
- Request the Manager any information that the Technical Committee deems necessary to carry out its activities.
- Request the trustee to call for a security holders meeting to discuss specific items, when the Technical Committee deems that the Manager has materially breached its obligations.
- Implement internal control procedures to identify all of the assets held, directly or indirectly, by the FIBRA E or the Promoted Companies, and its current state.

Conflicts Committee

If the Technical Committee approves the creation of a Conflicts Committee, such Committee shall approve any transactions with related parties or that may represent a conflict of interest, in an amount equal or exceeding 10% the trust estate. Any such transactions, when approved by the Conflicts Committee, shall be disclosed to the public as a material event.

Upon completion of the public consultation process before Cofemer, the Proposed Amendments (including any amendment thereto) shall be published in the Official Gazette of the Federation (Diario Oficial de la Federación), indicating the effective date of such Proposed Amendments.

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