

## **Mexico: Detailed Assessment of Observance of International Organization of Securities Commissions (IOSCO) Objectives and Principles of Securities Regulation**

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FINANCIAL SECTOR ASSESSMENT PROGRAM

MEXICO

THE IOSCO OBJECTIVES AND PRINCIPLES OF SECURITIES  
REGULATION

DETAILED ASSESSMENT OF  
IMPLEMENTATION

MARCH 2012

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THE WORLD BANK  
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## GLOSSARY

AMAI	<i>Asociación Mexicana de Asesores Independientes de Inversiones</i> (independent investment advisors)
AMIB	<i>Asociación Mexicana de Intermediarios Bursátiles</i> (securities intermediaries)
AML	Anti-Money Laundering
Asigna	Central Counterparty for the Clearing of Derivatives
BANXICO	Bank of Mexico (Banco de México)
BMV	<i>Bolsa Mexicana de Valores</i> (Mexican Stock Exchange)
BoM	<i>Banco de México</i>
CCV	Central counterparty for equity clearance and settlement
CEO	Chief Executive Officer
CINIF	<i>Consejo Mexicano para la Investigación Desarrollo de Normas de Información Financiera</i> (Mexican Council for Research and Development of Standards of Financial Reporting)
CNBV	<i>Comisión Nacional Bancaria y de Valores</i> (National Banking and Securities Commission)
CNSF	<i>Comisión Nacional de Seguros y Fianzas</i> (National Insurance and Sureties Commission)
COFEMER	<i>Comisión Federal de Mejora Regulatoria</i> (Federal Commission for Regulatory Improvement)
CONDUSEF	<i>Comisión Nacional para la Protección y Defensa de los Usuarios de Servicios Financieros</i> (National Commission for the Protection and Defense of the Users of Financial Services)
CONSAR	<i>Comisión Nacional del Sistema de Ahorro para el Retiro</i> (Pension regulator)
CRA	<i>Instituciones calificadoras de valores</i> (credit rating agency)
DMA	Direct Market Access
ETF	Exchange Traded Fund
FSAP	Financial Sector Assessment Program
GAAP	Generally Accepted Accounting Principles
GDP	Gross Domestic Product
IASB	International Accounting Standards Board
IAASB	International Auditing and Assurance Standards Board
IFAC	International Federation of Accountants
IFRS	International Financial Reporting Standards
Indeval	Central depository for equity securities
IMCP	Mexican Institute of Public Accountants
IMF	International Monetary Fund
IOSCO	International Organization of Securities Commissions
ISA	International Standards on Auditing
LCNBV	<i>Ley de la Comisión Nacional Bancaria y de Valores</i> (National Banking and Securities Commission Law)
LIC	<i>Ley de Instituciones de Crédito</i> (Banking Law)
LMV	<i>Ley del Mercado de Valores</i> (Securities Market Law)
LSI	<i>Ley de Sociedades de Inversión</i> (Investment Companies Law)

LSM	<i>Ley General de Sociedades Mercantiles</i> (Corporations Law)
MexDer	<i>Mercado Mexicano de Derivados</i> (Mexican derivative exchange)
MexDer	Mandatory Rules for Corporations and Trusts Participating in the
Mandatory	Establishment and Operation of a Market for Exchange Listed Futures
Rules	and Options
MOU	Memorandum of Understanding
MMOU	IOSCO Multilateral Memorandum of Understanding
MXGAAP	Mexican GAAP issued by CINIF
NAV	Net asset value
OTC	Over-the-counter
PGR	<i>Procuraduria General de la República</i> (Attorney General's office)
RNV	<i>Registro Nacional de Valores</i> (National registry of securities)
SHCP	<i>Secretaria de Hacienda y Credito Publico</i> (Secretariat of Finance and Public Credit)
SI	<i>Sociedade de inversion</i> (mutual fund)
SIC	<i>Sistema Internacional de Cotizaciones</i> (International quotation system)
SRO	Self-Regulatory Organization
UDI	<i>Unidad de inversion</i> (1 UDI = about 4.5 pesos)

## I. SUMMARY, KEY FINDINGS, AND RECOMMENDATIONS

### A. Executive Summary

1. **As the supervisor of the securities markets in Mexico, the National Banking and Securities Commission (*Comisión Nacional Bancaria y de Valores, CNBV*) has developed a robust supervisory framework that exhibits high levels of implementation of the International Organization of Securities Commissions Objectives and Principles of Securities Regulation (IOSCO Principles) in many areas.** The regimes governing the regulation of issuers, collective investment schemes, and secondary markets, and with respect to co-operation and information sharing, are extensive. However, there are gaps in the commission's enforcement powers and in the capital requirements that apply to securities firms that should be addressed.

2. **The most significant issues regarding full implementation of the Principles fall under the Regulator Principles.** These issues flow from two sources. First, there is no specific statute governing derivatives (whether exchange traded or over-the-counter (OTC)), nor any other express legislative provisions that govern the regulation of that growing market. This statutory gap results in a lack of assured jurisdiction and powers and the potential for gaps and overlaps among the other authorities involved (the central bank and the Secretariat of Finance and Public Credit (*Secretaria de Hacienda y Credito Publico, SHCP*)). Second, there are significant weaknesses in the protections afforded members of the Board of Governors and staff and with the resources of the Commission that lead to concerns about its independence and ability to carry out its mandate fully.

### B. Introduction

3. **The assessment was conducted during the IMF/World Bank Financial Sector Assessment Program (FSAP) mission to Mexico during the period September 7 to September 21, 2011,** by Tanis MacLaren, an external technical expert employed for this purpose by the IMF.

4. **The assessment was carried out using the 2003 IOSCO Methodology for Assessing Implementation of the IOSCO Principles (the Assessment Methodology).** In using the Assessment Methodology, the assessor sought to focus on the substance of the regulatory outcomes of the key requirements under each Principle. In June 2010, IOSCO approved a revision to the IOSCO Principles, which split one existing principle into four and added six completely new Principles. A draft revised methodology was circulated for consultation in May 2011 and the final version was published shortly after the mission's completion. The final version of the revised Assessment Methodology is expected to be endorsed at the IOSCO annual meeting in 2012. The CNBV agreed to allow the informal assessment of the status of implementation of the newly added Principles, using the guidance provided in the draft revised Assessment Methodology as issued in May 2011. A summary of these discussions is included as an annex to this report.

5. **The assessment relies on information from a detailed self assessment submitted by the authorities**, as well as extensive interviews with the CNBV staff, a review of legislation, rules and related materials, along with interviews with market participants and other stakeholders.
6. **Caution should be applied when comparing the results of this assessment to any previous reviews.** This assessment is being done after the recent global systemic financial crisis and therefore the “bar” for these assessments has gone up in terms of the rigor and thoroughness of the reviews, as well as the increased weight being given to the effective implementation of the various key issues and questions. The net result is that this assessment is not comparable to prior evaluations. Any changes in ratings from prior assessments generally *do not* reflect a decline in the quality or level of regulation; rather they result from increased rigor of the application of the assessment criteria.
7. **The assessor is grateful to the staff of the CNBV for their extensive cooperation and assistance in the conduct of this assessment.** The staff was informed, forthright and helpful throughout. The assessor would also like to thank the regulated entities, market participants and other stakeholders who generously provided their time and honest insights. The industry participants with whom the assessor met spoke extremely highly of the quality of the staff at the CNBV and this assessor shares those views.

#### **Institutional and market structure—overview**

8. **The CNBV is a supervisory authority with broad powers to regulate certain aspects of the capital markets in operation in Mexico.** The CNBV has regulatory authority over a broad range of securities market participants, including securities firms, self regulatory organizations, securities exchanges, market infrastructure providers (central counterparties and securities depositories), external auditors, public issuers, rating agencies, price vendors, and collective investment schemes. The CNBV also is responsible for the supervision of banks, development banks and agencies, cooperatives, credit unions and other deposit-taking institutions. The CNBV reports to the SHCP.
9. **The National Commission for the Protection and Defense of the Users of Financial Services (*Comisión Nacional para la Protección y Defensa de los Usuarios de Servicios Financieros*, CONDUSEF) is the consumer protection agency in the jurisdiction.** Its responsibilities include promoting financial education, setting certain consumer protection requirements and receiving and responding to consumer complaints about financial services firms. For example, CONDUSEF requires Mexican financial institutions, including securities firms, to have specialized units dedicated to responding to inquiries and complaints from clients. CONDUSEF lacks the resources and powers to function effectively as a consumer protection authority. It has no power to order a financial services provider to compensate an investor for losses or to arbitrate a dispute. The weakness of this agency is of concern as gaps in the consumer protection regime may have a negative effect on investors and undermine confidence in the system as a whole.

10. **The regulator's responsibilities, powers and authority with respect to the securities market are established by statute.** The CNBV was created as a regulator under the National Banking and Securities Commission Law (*Ley de la Comisión Nacional Bancaria y de Valores*, LCNBV). The LCNBV gives the commission the authority to administer, enforce and give effect to the provisions of the laws related to financial services in the jurisdiction. In the securities markets, the two key laws are the Securities Market Law (*Ley del Mercado de Valores*, LMV), which was effective as of the end of 2005, and the Investment Companies Law (*Ley de Sociedades de Inversión*, LSI), which dates from 2001. These laws are supplemented with detailed secondary legislation in specific areas, including the Securities Firms Rules, Issuers Rules and *Sociedade de Inversión* (SI) Rules.

11. **The Commission's responsibilities, powers and authority with respect to the derivatives market rely on the general authority granted to SHCP, the central bank and the Commission to regulate financial markets and their participants in Mexico.** These provisions do not refer to derivatives specifically. The responsibilities and authority for regulation is split in practice among the CNBV, the SHCP and the central bank of Mexico (Banco de Mexico, BoM). All three entities have the authority to issue secondary legislation/rules for this market, which creates opportunities for duplication, overlap and conflict in the provisions that govern.

12. **There is one stock exchange (Bolsa Mexicana de Valores, BMV) and one derivatives exchange (MexDer) operating in Mexico under permissions granted by the Federal Government.** New offerings of securities to the public in the jurisdiction must be made via a prospectus and the securities must be listed on the BMV. Trading in equities or listed derivatives is required to take place on the exchanges. Trading in some fixed income instruments and most derivatives takes place over-the-counter, often through electronic facilities operated by authorized inter-dealer brokers. The BMV, MexDer, the central securities depository (Indeval) and the central counterparties (CCV and Asigna) are all part of the BMV Group, a public company self-listed on the BMV. The BMV is a member of the World Federation of Exchanges.

13. **The BMV has a very low number of domestic listings and the liquidity of these is limited for all but the very largest companies.** There has been virtually no growth in the number of domestic listings over the past five years, while market capitalization has increased 30 percent and trading volumes were up 131 percent. There are a fairly large number of family controlled private companies that would be prime targets for listing. However, the consensus among the regulators and market participants is that they have alternative sources of funding that are more attractive as these do not entail the public disclosure obligations that come with public listing. Trading is concentrated in the largest

issuers, with the five most active issues making up 68 percent of total traded value in 2011.<sup>1</sup> Only about 30–40 stocks are considered liquid.<sup>2</sup>

14. **Most of the growth in listings at the BMV has been in foreign equities, and some exchange traded funds (ETFs).** These instruments are listed and traded on the International quotation system (*Sistema Internacional de Cotizaciones*, SIC). Securities eligible for trading on the SIC are ones that have not been publically offered via a prospectus in Mexico; are not listed in the National Securities Registry (*Registro Nacional de Valores* (, RNV); and are listed on a foreign securities market recognized by the CNBV or whose issuers have otherwise been approved for listing by the CNBV. The CNBV has recognized several foreign stock markets as having comparable standards, such as disclosure rules. These exchanges include NASDAQ, the New York Stock Exchange, the London Stock Exchange, the TMX Group Inc., and the Deutsche Börse AG. Unlike domestic listings in which any investor may participate, only qualified investors (institutions and high net worth individuals) may purchase securities listed on the SIC. Trades executed through the SIC settle through Indeval and are subject to the same operational rules and regulations as other trades executed on the domestic side of the BMV. The number of listings on the SIC has increased by more than 200 percent over the last five years, with the largest growth in exchange traded funds (ETFs)—up 471 percent. As for the domestic market, the trading on the SIC is highly concentrated in the five most active listings, with these ETFs making up 58 percent of the total traded value in 2011.<sup>3</sup>

**Table 1. Mexico: Trading on BMV**

	Number of Listings				
	2006	2007	2008	2009	2010
Domestic					
Industrial, retail and services	117	109	110	108	116
Financial institutions	19	20	20	23	18
ETFs	1	5	6	13	20
<b>Total</b>	<b>137</b>	<b>134</b>	<b>136</b>	<b>144</b>	<b>154</b>
Global BMV Market (SIC International Quotation System)					
Shares	150	191	225	267	335
ETFs	55	108	153	240	314
<b>Total</b>	<b>205</b>	<b>299</b>	<b>378</b>	<b>507</b>	<b>649</b>
Warrants	1	1	8	8	8
Shelf Listing	0	8	0	1	1

Source: CNBV.

<sup>1</sup> Information from BMV.

<sup>2</sup> Estimates of the number of liquid issues varied. Some industry members said as few as 10, while the BMV estimate was 70–80.

<sup>3</sup> Information from BMV.

**Table 2. Mexico: BMV Market Size and Trading Data**

(In U.S. dollars)

	2006	2007	2008	2009	2010
Total Market Capitalization (US\$ millions)	346,613	399,485	237,910	351,957	453,496
Annual Trading Volume	34,509,592	43,400,578	54,322,816	63,683,504	79,886,196
Annual Trading Value (US\$ millions)	85,697	133,139	131,483	111,331	187,229
Value of new issues listed (US\$ 000)	395,993	744,688	1,425,474	551,571	1,483,383

Source: CNBV.

**15. Much of the activity on the BMV comes from computer-driven program trading orders that are placed to take advantage of price asymmetries between markets.**

According to the BMV, up to 90 percent of total orders in the market represent orders driven by computer trading algorithms. Most are cancelled before the order is filled. The ratio of orders to trades is about 20 to 1. The BMV has added significant systems capacity in recent years to handle the volume of orders. Its trading rules and the related CNBV Securities Firms Rules have recently undergone significant changes to: modernize the provisions regarding trading; permit direct market access to institutional investors through member brokers; and facilitate cross trading.

**16. Growth of listings and trading on MexDer has been mixed.** The market has experienced growth in the number of listed options (up 450 percent) and options trading volumes (up 36 percent) over the past five years, while the number of listed futures and trading volume has declined (11 percent and 85 percent, respectively). The values of exchange-traded instruments show a similar pattern: options trading values are up 83 percent and futures are down 85 percent. The overall decline on the futures side is largely because of a decline in listing and trading of interest rate related instruments. MexDer officials indicated virtually all trading on the exchange represents trades by institutional investors or proprietary trading by the members.

**17. The BMV recently established an order routing agreement with the Chicago Mercantile Exchange (CME) that expands the access of Mexican market participants to a wider array of products.** Most of the listings on the CME are now available to Mexican participants through local MexDer members. Trades are cleared through MexDer clearing members and settled in Mexico through Asigna, the central counterparty, which also collects and holds margin for these trades.

**Table 3. Mexico: Exchange Traded Derivatives—Number of Contracts Listed**

	2006	2007	2008	2009	2010
<i>Futures</i>					
Currencies	4,415	2,168	2,095	2,961	3,448
Equity Index	33,238	61,693	73,915	66,144	85,322
Interest Rates	87,811	61,497	39,790	28,255	22,569
Individual Equities	2	2	2	0	92
<b>Total</b>	<b>125,466</b>	<b>125,360</b>	<b>115,802</b>	<b>97,360</b>	<b>111,431</b>
<i>Options</i>					
Equity index	909	6,191	4,417	3,390	3,008
Currencies	9	2	3	24	62
Individual Equities	62	10	6,104	3,268	2,398
<b>Total</b>	<b>980</b>	<b>6,203</b>	<b>10,524</b>	<b>6,682</b>	<b>5,468</b>

Source: CNBV.

**Table 4. Mexico: Exchange Traded Derivatives—Annual Trading Volume**

	2006	2007	2008	2009	2010
<i>Futures</i>					
Currencies	6,077,409	3,225,149	3,231,004	1,652,185	5,698,630
Equity Index	620,557	951,955	1,085,663	1,130,528	1,321,686
Interest Rates	267,950,710	224,664,425	65,187,423	45,611,400	34,794,951
Individual Equities	3,000	2	2,000	0	12,054
<b>Total</b>	<b>274,651,676</b>	<b>228,841,531</b>	<b>69,506,090</b>	<b>48,394,113</b>	<b>41,827,321</b>
<i>Options</i>					
Equity index	117,568	130,410	52,556	40,723	147,411
Currencies	306	10	7	145	963
Individual Equities	448,120	78	585,037	345,718	619,880
<b>Total</b>	<b>565,994</b>	<b>130,498</b>	<b>637,600</b>	<b>386,586</b>	<b>768,254</b>

Source: CNBV.

**Table 5. Mexico: Exchange Traded Derivatives—Annual Trading Value**

(In U.S. dollars)

	2006	2007	2008	2009	2010
<i>Futures</i>					
Currencies	62,006,803	32,520,759	26,655,647	17,906,474	58,796,537
Equity Index	12,236,136	26,110,142	20,841,871	22,294,574	35,731,183
Interest Rates	2,461,861,695	2,048,018,991	479,158,659	354,738,137	291,240,417
Individual Equities	1,933	0	503	0	3,270
<b>Total</b>	<b>2,536,106,567</b>	<b>2,106,649,892</b>	<b>526,656,680</b>	<b>394,939,185</b>	<b>385,771,407</b>
<i>Options</i>					
Equity index	2,137,505	3,383,644	1,039,660	722,440	3,893,708
Currencies	3,106	99	55	1,460	10,252
Individual Equities	76,712	21	124,906	80,086	157,735
<b>Total</b>	<b>2,217,323</b>	<b>3,383,764</b>	<b>1,164,621</b>	<b>803,986</b>	<b>4,061,695</b>

Source: CNBV.

18. **As with the stock and derivatives markets, the growth in the collective investment scheme (SI) market has been slow.** The number of SIs has grown only marginally over the past five years (9 percent). Assets under management have grown much faster—up almost 60 percent over the same period. Most of the growth, both in the number of funds and assets under management, is in equity funds, chiefly owing to their greater flexibility. Debt funds may only invest in debt instruments, while equity funds only have to have 20 percent invested in equities. In fact, most equity funds are operated as balanced funds, with a varying percentage of the funds invested in each type of securities. In the two years since the crisis, SIs have seen increased flows of funds. Various market participants attributed this growth to the fact that investors in SIs lost less money during the crisis than those who invested directly in the markets.

**Table 6. Mexico: Collective Investment Schemes (Sociedades de Inversion)**

<b>Number of Funds</b>					
	2006	2007	2008	2009	2010
Equity funds	129	147	199	205	223
Debt	325	316	303	272	283
Venture Capital	21	20	20	19	12
<b>Total</b>	<b>475</b>	<b>483</b>	<b>522</b>	<b>496</b>	<b>518</b>

  

<b>Total Assets Under Management</b>					
(In millions of U.S. dollars)					
	2006	2007	2008	2009	2010
Equity funds	10,374	14,098	8,401	11,496	17,050
Debt	53,083	64,134	49,679	60,839	84,642
Venture Capital	416	456	409	412	473
<b>Total</b>	<b>63,873</b>	<b>78,688</b>	<b>58,489</b>	<b>72,747</b>	<b>102,165</b>

Source: CNBV.

19. **The Mexican system makes limited use of self-regulatory organizations (SROs) in carrying out the oversight of market participants.** The exchanges and central counterparties are automatically classified as SROs under the LMV. There are two other SROs recognized by the CNBV and by the Association of Independent Investment Advisors (*Asociacion Mexicana de Asesores Independientes de Inversiones*, AMAII), a voluntary association of independent investment advisors and the Mexican Association of Securities Intermediaries (*Asociacion Mexicana de Intermediarios Bursatiles*, AMIB), an association to which securities brokers and SI operators and distributors must belong. These two associations operate more as trade associations than SROs. The regulatory functions the SROs carry out vary by SRO and run from virtually none for AMAII and AMIB through to MexDer that conducts regular examinations of its members.

20. **There are a relatively small number of authorized market intermediaries operating in Mexico and the numbers are static.** Market intermediaries include brokerage firms, credit institutions, SI operators, pension fund managers and SI distributors (whether independent companies or financial institutions acting as distributors). Brokerage firms must comply with the provisions of the LMV; the other entities must comply with the specific legislation governing their respective activities, such as the LSI. Credit institutions and brokerage houses may carry on similar capital market activities. Certain of the rules that govern securities market activities are written to apply to both types of institutions. However, some securities markets rules presently apply only to brokerage houses.

**Table 7. Mexico: Number of Authorized Firms 1/**

	2006	2007	2008	2009	2010
Commercial Banks	31	40	43	43	41
Development banks	6	6	6	6	6
Securities firms	31	32	34	35	35
Mutual fund operators	44	43	44	45	41
Mutual fund distributors*	8	9	8	8	5
<b>Total</b>	<b>120</b>	<b>130</b>	<b>135</b>	<b>137</b>	<b>128</b>

Source: CNBV.

1/ Not including banks or securities firms authorized to distribute SIs.

21. **Further, there are five inter-dealer brokers (*Sociedades que administran sistemas para facilitar operaciones con valores*) operating in Mexico.** These entities are authorized by the Commission to provide services and facilities for OTC trading in securities—mostly debt and derivatives—only to credit institutions and brokerage houses. They may also provide price information to anyone on the instruments that trade through their facilities. They do not deal in listed equity securities and are not licensed as intermediaries under the LMV.

22. **Mexico's financial system is small and very concentrated.** The system is dominated by large financial conglomerates, which include all types of market intermediaries. Several of the conglomerates are among the largest public companies in the country. These financial groups control or manage about 73 percent of all financial assets. This structure creates some potential capital markets regulatory issues, particularly ones related to conflicts of interest and consumer protection more broadly. In this environment, strong consumer protection requirements are essential to maintain confidence in the market and for market development. Market participants, regardless of their institutional character should be subject to equivalent rules when carrying on similar activities.

23. **The number of staff at the CNBV has declined and turnover at the senior level is high.** Staff salaries have been frozen for almost a decade, resulting in a decline in compensation of about 40 percent on a real basis, while at the same time demands on

Commission staff have increased. Salary levels are now well below comparable positions in the private sector. This has had a predictably negative effect on attracting and retaining experienced and skilled staff. As a result, many experienced staff, particularly at senior levels, have left the CNBV for the private sector. This loss in expertise and institutional memory is an important problem that needs to be addressed before it hampers the CNBV's effectiveness in carrying out its mandate.

**Table 8. Mexico: Staffing at the CNBV**

	2006	2007	2008	2009	2010
Number of employees	1320	1375	1328	1503	1453
			Staff Departures		
Titles	2007	2008	2009	2010	TOTAL
Vice Presidents	3	3	0	0	6
General Directors	1	4	2	4	11
Assistant General Directors	12	6	2	6	26
Area Directors	3	5	1	5	14
Deputy Directors	33	31	9	15	88
Inspectors/Technical Staff	56	20	20	14	110
<b>Total</b>	<b>108</b>	<b>69</b>	<b>34</b>	<b>44</b>	<b>255</b>

Source: CNBV.

24. **There has been an effort within the CNBV to codify the circumstances in which its discretion will be exercised.** The aim is to reduce the opportunities for challenges to its authority and the application of political influence. Clarity and transparency with respect to Commission policies is admirable. However, this does have the potential effect of limiting its flexibility to deal with novel situations and may be incompatible with effective regulation of fast-moving capital markets.

#### **Preconditions for effective securities regulation**

25. **The preconditions for effective supervision (a stable macroeconomic environment, sound legal and accounting framework, and effectiveness of procedures for the efficient resolution of problems in the securities market) appear to be in place in the jurisdiction.** As in many jurisdictions, the bankruptcy of market intermediaries is governed by the same legislation that governs any other corporate bankruptcy and it operates very slowly. While client assets held at the central depository are protected, it is not clear how the default procedures of the central counterparties would work in the event of a brokerage firm or large financial conglomerate bankruptcy.

### **C. Main Findings**

26. **Principles 1–5, Principles relating to the regulator:** The CNBV has clear statutory authority over and responsibility for the securities markets. Its authority with respect to derivatives markets is less clear-cut and needs to be rectified by the passage of express

legislation. The rules governing certain market activities may differ depending on the type of institution engaging in the activity. The operational independence of the agency is compromised by a lack of resources, the fact that 75 percent of the Board of Governors are appointed by the SHCP and may be dismissed without cause at any time, and the lack of statutory immunity for the Commission, its Board and staff members. Persons affected by decisions of the Commission are afforded a full range of protections, including the right to be heard, to written reasons and to rights of appeal. The laws should be amended to permit the conduct of surprise inspections of any regulated entity and to provide additional powers for the Commission with respect to enforcement matters, including enhanced transparency and the ability to settle matters. Staff is very professional and subject to detailed conduct rules. Market participants uniformly praised the quality and openness of CNBV staff.

27. **Principles 6–7, Principles relating to self-regulation:** The Mexican system makes limited use of self-regulatory organizations (SROs) in carrying out the oversight of market participants. The regulatory functions the SROs carry out vary by SRO and run from virtually none to full rule-making and conducting regular examinations of its members. In all cases, the CNBV retains full authority to oversee SRO members. There is an appropriate SRO supervision program in place that varies by the nature of the SRO in question. The exchanges and central counterparties are subject to regular on-site inspections and their rules are subject to prior review and approval. MexDer has a compliance officer who is in charge of the surveillance of its members.

28. **Principles 8–10, Principles relating to enforcement of securities regulation:** The Commission has broad inspection, investigation and surveillance powers, but lacks the power to conduct inspections of regulated entities without notice. It has powers to investigate and take action against anyone who breaches the laws it administers. If there is evidence of possible illegal conduct, investigation inspections may be conducted with same day notice. The Commission carries on active inspection and enforcement programs. Both on-site and off-site reviews are performed of regulated entities. Market surveillance is performed at the exchanges and at the CNBV in parallel. There are some gaps in enforcement powers that should be filled and the sanctions available across the laws administered by the Commission should be brought into alignment. Fine levels should be reviewed to ensure they are consistent and high enough to be effective deterrents. The provisions restricting disclosure of investigations and enforcement actions should be revised to permit fuller and earlier publication of information.

29. **Principles 11–13, Principles for cooperation in regulation:** The Commission has the ability and capacity to share information and cooperate with regulators, both domestically and internationally, subject to the general requirement that there be an MOU in place. It can share confidential information with any other country through an MOU. It is a signatory to the IOSCO Multilateral MOU and to many bilateral MOUs with its counterparts in key jurisdictions, such as Argentina; Brazil; Canada; El Salvador; Panamá; Peru; the United

States; United Kingdom; and Venezuela, as well as Germany; the Netherlands; and Spain, and various other European countries.

30. **Principles 14–16, Principles for Issuers:** Extensive requirements are in place for offering and continuing disclosure documents for securities. The disclosure provided for trading instruments listed on MexDer include details of the terms of the contracts and the mechanics of trading, but no disclosure of the risks of leverage. New issues of securities (debt, equity, or collective investment schemes) to the public in Mexico are required to be offered via prospectus and listed on the BMV and are subject to the exchange's listing standards, in addition to the requirements set out in the LMV and the Issuers Rules. Both the BMV and the CNBV conduct reviews of the prospectus of the issuer. Continuing disclosure documents are made public through the facilities of the exchange and the Commission. Investors are treated equitably with respect to voting, access to information and the ability to participate in any takeover bid. Full information must be provided for any takeover bid. Information is publicly available regarding shareholdings of directors, officers and other insiders of the corporation but the threshold triggering reports of changes in ownership is high and should be lowered. Accounting and auditing standards are in place, and auditors are subject to oversight by the CNBV and detailed independence standards apply. By the beginning of 2012, public issuers will have to prepare their financial statements using International Financial Reporting Standards (IFRS) and be audited using International Standards of Audit (ISA). The publication of annual audited financial statements could be more timely and the access to information about shareholder meetings should be enhanced by requiring electronic publication of the materials. If and when MexDer develops a retail client base, additional disclosure regarding the risks of leverage should be provided to clients.

31. **Principles 17–20, Principles for collective investment schemes:** The framework for regulation of SIs is largely compliant with the Principles. All SIs and their operators and distributors are subject to authorization and reporting requirements. All funds offered to the public must be registered with the CNBV, which process includes the review of a detailed prospectus. Funds must be established as corporations, with assets segregated from those of the operator and distributor. All SIs and their operators and distributors are subject to both off-site and on-site supervision. Any asset of an SI that can be held at a central depository must be so held. The central depository for securities is independent of the SIs. The fund's securities and its assets are subject to valuation by authorized third party service providers (valuation companies and price vendors) that are required to be independent of the fund and its operator. Continuous disclosure of information and prices is provided through the fund or its distributor's website. In addition, prices must be reported daily through the BMV's system. The CNBV has the authority to suspend new placements, but no authority to order a fund to suspend or resume redemptions.

32. **Principles 21–24, Principles for market intermediaries:** A framework is in place for licensing and to apply on-going requirements for market intermediaries. Applicants are subject to detailed reviews before being authorized. There are initial and ongoing risk-based capital requirements that are based on a simplified version of Basel II and that address market, credit, and operational risk. Liquidity is subject to separate testing but no specific capital requirements apply. Requirements regarding capital calculations and prompt (early) reporting of deficiencies by market intermediaries should be more rigorous. Market intermediaries are required to have extensive systems of risk management and internal controls in place. Client assets must be held in segregated accounts at central depositories. Intermediaries are required to know their clients and make suitable recommendations for those clients. The rules regarding conflicts of interest need improvement and the rules regarding conduct of business should be made consistent across all types of intermediaries. There is no specific written plan in place to address the failure of a broker; however, the law gives the CNBV broad powers to take action against a failing firm and require it to reduce its business, raise capital and give notice to its clients. As in most countries, the bankruptcy of many types of authorized firms, such as brokerage firms and SI operators, would be governed the general bankruptcy laws, which may not be capable of dealing with the demands of a market participant failure.

33. **Principles 25–30, Principles for the Secondary Markets:** Exchanges are subject to authorization by the SHCP with the advice of the CNBV (and the BoM with respect to derivatives). Alternative trading systems for listed instruments are not permitted. The MexDer and central clearinghouses are subject to minimum capital requirements set by the authorities via MexDer's Mandatory Rules. The SHCP may set capital requirements for the stock exchange, but has not yet done so. Market surveillance is performed at the exchanges and the CNBV in parallel. The CNBV has a comprehensive oversight system for exchange supervision that includes on-site examinations and off-site reviews of rules and other matters. The Commission may suspend the operations of a stock exchange and the SHCP has the authority to revoke the authorization of any exchange. There is both pre-trade and post-trade transparency of prices of shares in real time, but not for fixed income securities. The rules against market abusive transactions are extensive and there are mechanisms in place to detect and take action against improper conduct. Trades on both BMV and MexDer are cleared and settled through central counterparties that have detailed and transparent provisions designed to protect the markets against a default by any participant.

**Table 9. Mexico: Summary Implementation of the IOSCO Principles—Detailed Assessments**

Principle	Grade	Findings
Principle 1. The responsibilities of the regulator should be clearly and objectively stated	<b>PI</b>	The CNBV has clear statutory authority over and responsibility for the securities markets. Its authority with respect to derivatives markets is less clear-cut and needs to be rectified by the passage of express legislation. CONDUSEF is the consumer protection agency in the jurisdiction. There are some overlaps in authority and activities between the central bank and the Commission, particularly with respect to derivatives, but there are MOUs in place and good working relationships in practice. The rules governing certain securities market activities differ, depending on the type of institution engaging in the activity. Insurance products that are functionally equivalent to securities are subject to different rules by the insurance supervisor and no MOU or practical working relationship exists between the two regulators. There is no MOU in place with CONDUSEF. These gaps should be rectified.
Principle 2. The regulator should be operationally independent and accountable in the exercise of its functions and powers	<b>NI</b>	The operational independence of the agency is compromised by a lack of resources, the fact that 75 percent of the Board of Governors are appointed by the SHCP and may be dismissed without cause at any time and the lack of statutory immunity for the Commission, its Board and staff members for the <i>bona fide</i> discharge of their functions and powers. The transparency of Commission activities and processes is acceptable but could be enhanced. Persons affected by decisions of the Commission are afforded a full range of protections, including the right to be heard, to written reasons and to rights of appeal.
Principle 3. The regulator should have adequate powers, proper resources and the capacity to perform its functions and exercise its powers	<b>NI</b>	As noted under Principle 1, the powers of the Commission with respect to derivatives need to be settled in law. The Commission lacks sufficient expert resources necessary to carry out its critical functions appropriately and the regulator has no funding autonomy. Staff training budgets are sufficient, but salaries have been frozen for nearly a decade and are well below that of the private sector. Despite these challenges, the industry participants with whom the assessor met spoke extremely highly of the quality of the staff at the CNBV and this assessor shares those views. The law should be amended to permit the conduct of surprise inspections and to provide additional powers for

Principle	Grade	Findings
		<p>the Commission with respect to enforcement matters including enhanced transparency and the ability to settle matters.</p> <p>CONDUSEF is the consumer protection agency in the jurisdiction. It lacks the resources and powers to function effectively as a consumer protection authority.</p>
Principle 4. The regulator should adopt clear and consistent regulatory processes	<b>BI</b>	<p>The CNBV operates within clear and consistent processes. The consultation process for rule making is transparent and operated by a separate agency of the government. Laws and rules are available on the CNBV website. Persons affected by decisions of the Commission are afforded a full range of protections, including the right to be heard, to written reasons and to rights of appeal. If anything, the protections afforded defendants in the enforcement process may well impede the effectiveness of that process. The Commission should have the power to publish full details of enforcement proceedings once the sanction has been imposed.</p>
Principle 5. The staff of the regulator should observe the highest professional standards	<b>FI</b>	<p>Staff observes high standards of professional conduct and subject to detailed ethical rules both as federal employees and under the conduct rules of the Commission.</p>
Principle 6. The regulatory regime should make appropriate use of self-regulatory organizations (SROs) that exercise some direct oversight responsibility for their respective areas of competence and to the extent appropriate to the size and complexity of the markets	<b>N/A</b>	<p>The Mexican system makes limited use of self-regulatory organizations (SROs) in carrying out the oversight of market participants. The regulatory functions the SROs carry out vary by SRO and run from virtually none to full rule-making for members and conducting regular member examinations.</p>
Principle 7. SROs should be subject to the oversight of the regulator and should observe standards of fairness and confidentiality when exercising powers and delegated responsibilities	<b>FI</b>	<p>The CNBV has not delegated any functions to any SRO, retains full authority to oversee SRO members and in practice performs the same regulatory reviews and activities performed by the SRO—such as market surveillance. There is an appropriate SRO supervision program in place. The exchanges and central counterparties are subject to regular on-site inspections, and their rules are subject to review and approval.</p>
Principle 8. The regulator should have comprehensive inspection, investigation, and surveillance powers	<b>PI</b>	<p>The Commission has broad inspection, investigation and surveillance powers. While it may conduct an investigation visit (where a breach of the law is suspected) with same day notice, the CMBV lacks the power to conduct routine inspections of regulated entities without notice.</p>

Principle	Grade	Findings
Principle 9. The regulator should have comprehensive enforcement powers	<b>BI</b>	The CNBV has powers to investigate and take action against anyone who breaches the laws it administers. There are some gaps in enforcement powers that should be filled, such as the power to order restatement of financial statements and to disclose full details of the results of enforcement proceedings once the Commission hearing process is completed.
Principle 10. The regulatory system should ensure an effective and credible use of inspection, investigation, surveillance, and enforcement powers and implementation of an effective compliance program	<b>BI</b>	The Commission carries on active inspection and enforcement programs. Both on-site and off-site reviews are performed of regulated entities. Market surveillance is performed at the exchanges and the CNBV in parallel. Firms must have effective compliance systems. There are some gaps in the Commission's enforcement powers that should be filled. The sanctions available across the laws administered by the Commission should be brought into alignment. Fine levels should be reviewed to ensure they are consistent and high enough to be effective deterrents.
Principle 11. The regulator should have the authority to share both public and nonpublic information with domestic and foreign counterparts	<b>FI</b>	The Commission has the ability and capacity to share information and cooperate with regulators, both domestically and internationally, subject to the general requirement that there be an MOU in place. It can share confidential information with any other country through an MOU and has a record of active cooperation.
Principle 12. Regulators should establish information sharing mechanisms that set out when and how they will share both public and nonpublic information with their domestic and foreign counterparts	<b>FI</b>	The CNBV is a signatory to the IOSCO Multilateral MOU and to many bilateral MOUs with its counterparties in key jurisdictions.
Principle 13. The regulatory system should allow for assistance to be provided to foreign regulators who need to make inquiries in the discharge of their functions and exercise of their powers	<b>FI</b>	The Commission may provide extensive assistance to foreign supervisors in carrying out their responsibilities, including by obtaining and sharing information and cooperating on inspections. The Commission does not require the permission of any outside authority to share information and an independent interest, or dual illegality is not required as a precondition to cooperation.
Principle 14. There should be full, timely and accurate disclosure of financial results and other information that is material to investors' decisions	<b>BI</b>	Extensive requirements are in place for offering and continuing disclosure documents. Securities (debt, equity, or collective investment schemes) that are offered publicly via prospectus are required to be listed on the BMV and are subject to the exchange's listing standards, in addition to the requirements set out in the LMV and the Issuers Rules. Both the BMV and the CNBV conduct reviews of the prospectus of the issuer. Continuing disclosure documents are made

Principle	Grade	Findings
		public through the facilities of the exchange and the Commission.
Principle 15. Holders of securities in a company should be treated in a fair and equitable manner	<b>BI</b>	Investors are treated equitably with respect to voting, access to information and the ability to participate in any takeover bid. Full information must be provided for any takeover bid. Information is publicly available regarding shareholdings of directors, officers and other insiders of the corporation, although the trigger for reporting of changes should be lowered. Access to information about shareholder meetings should be enhanced by requiring electronic publication of the materials.
Principle 16. Accounting and auditing standards should be of a high and internationally acceptable quality	<b>FI</b>	Accounting and auditing standards are in place, and auditors are subject to oversight by the CNBV and detailed independence standards apply. By the beginning of 2012, public issuers will have to prepare their financial statements using International Financial Reporting Standards (IFRS) and be audited using International Standards of Audit (ISA). The publication of annual audited financial statements could be more timely.
Principle 17. The regulatory system should set standards for the eligibility and the regulation of those who wish to market or operate a collective investment scheme	<b>FI</b>	All SIs and their operators and distributors are subject to authorization and reporting requirements. All SIs and their operators and distributors are subject to both off-site and on-site supervision. There is a regime governing conflicts of interest. Delegation is not a particular issue in this jurisdiction, as SIs are required to appoint service providers to carry out specified tasks for the SI, such as valuation companies and prices vendors. These service providers are also authorized and supervised by the CNBV.
Principle 18. The regulatory system should provide for rules governing the legal form and structure of collective investment schemes and the segregation and protection of client assets	<b>FI</b>	Funds must be established as corporations, with assets segregated from those of the operator and distributor. Any asset of an SI that can be held at a central depository must be so held. The central depository for securities is independent of the SIs and their operators and distributors.
Principle 19. Regulation should require disclosure, as set forth under the principles for issuers, which is necessary to evaluate the suitability of a collective investment scheme for a particular investor and the value of the investor's interest in the scheme	<b>FI</b>	All funds offered to the public in Mexico must register the securities with the CNBV, which process includes the review of a prospectus that must contain full information about the SI and its service providers. The SI must also prepare a short form document containing key information that investors should know before they invest. Material changes in the prospectus and key disclosure document are subject to prior approval of the Commission and may trigger a right of investors to redeem their investments prior to the change going into effect.

Principle	Grade	Findings
Principle 20. Regulation should ensure that there is a proper and disclosed basis for assets valuation and the pricing and the redemption of units in a collective investment scheme	<b>BI</b>	The fund's securities and its assets are subject to valuation by third party service providers (valuation companies and price vendors) that are authorized and supervised by the Commission. These service providers must be independent of the fund and its distributor. Continuous disclosure of information and prices is provided through fund or distributor websites. In addition, prices must be reported daily through the BMV's system. The CNBV has the authority to suspend new placements, but no authority to order a fund to suspend or resume redemptions.
Principle 21. Regulation should provide for minimum entry standards for market intermediaries	<b>FI</b>	A framework for licensing and on-going requirements for market intermediaries is in place. Applicants are subject to detailed reviews before being authorized. Brokers must undergo comprehensive on-site inspections of all systems before they are permitted to begin business. The regime for investment advisors may leave supervisory gaps. The CNBV should be given express authority to supervise this activity.
Principle 22. There should be initial and ongoing capital and other prudential requirements for market intermediaries that reflect the risks that the intermediaries undertake	<b>PI</b>	There are initial and ongoing risk-based capital requirements in place that are based on a simplified version of Basel II and address market, credit and operational risk. Liquidity is subject to separate testing but no specific capital requirements. There are no specific provisions for legal or reputational risk. Market intermediaries are subject to active oversight by the regulator and the CNBV's powers to act where there are problems are extensive. Requirements regarding capital calculations and prompt reporting of deficiencies by market intermediaries authorized to trade in derivatives on MexDer are adequate but those for securities brokerage houses should be more rigorous.
Principle 23. Market intermediaries should be required to comply with standards for internal organization and operational conduct that aim to protect the interests of clients, ensure proper management of risk, and under which management of the intermediary accepts primary responsibility for these matters	<b>BI</b>	Market intermediaries are required to have extensive systems of risk management and internal controls in place. The firm's internal audit function must review these systems annually and the results of that review must be reported to the Board of Directors of the firm and the CNBV. Client assets must be held in segregated accounts at central depositories. Intermediaries are required to know their clients and make suitable recommendations for those clients. The rules regarding conflicts of interest need improvement.

Principle	Grade	Findings
Principle 24. There should be a procedure for dealing with the failure of a market intermediary in order to minimize damage and loss to investors and to contain systemic risk	<b>BI</b>	There is no written plan in place to address the failure of a broker; however, the law gives the CNBV broad powers to take action against a failing firm and require it to reduce its business, raise capital and give notice to its clients. Early warning systems are in place for securities brokers, but see comments under Principle 22 regarding timely reporting. Where a failure has cross border implications, MOUs are in place to facilitate information sharing. The bankruptcy laws do not specifically address market-related issues.
Principle 25. The establishment of trading systems including securities exchanges should be subject to regulatory authorization and oversight	<b>FI</b>	Establishment of stock and derivatives exchanges requires authorization from the SHCP with input from the CNBV (and from the BoM for derivatives exchanges). There are specified criteria that any applicant must meet, including requirements regarding systems and other infrastructure capacity, technical competence, etc. Alternative trading systems for listed equity instruments are not permitted.  Oversight of the exchanges includes both on-site examinations and off-site reviews. All new rules and proposed rule changes for securities require CNBV approval. All new rules and proposed rule changes for securities require CNBV approval. New rules changes and proposed rule changes at MexDer require SHCP approval and are also subject to review by the BoM and CNBV. On-site reviews are comprehensive and are performed regularly.
Principle 26. There should be ongoing regulatory supervision of exchanges and trading systems, which should aim to ensure that the integrity of trading is maintained through fair and equitable rules that strike an appropriate balance between the demands of different market participants	<b>FI</b>	The CNBV has a comprehensive system for supervision of the exchanges that includes both on-site examinations and off-site reviews of rules and trading reports to ensure the markets operate fairly. Surveillance of the markets is carried on by the exchanges and CNBV in parallel. The CNBV has the power to suspend trading in individual securities and to suspend the operations of an exchange in appropriate circumstances. The SHCP retains the right to revoke an authorization.
Principle 27. Regulation should promote transparency of trading	<b>FI</b>	There is both pre-trade and post-trade transparency of prices in real time for listed shares and ETFs. The trading rules at BMV were recently modernized to facilitate high frequency trading, crossing of large trades, and direct market access. The implementation and operation of these new rules should be monitored closely to ensure the current level of transparency and risk management is not negatively affected.

Principle	Grade	Findings
Principle 28. Regulation should be designed to detect and deter manipulation and other unfair trading practices	<b>FI</b>	The rules against abusive transactions in the markets are extensive, and there are mechanisms in place to detect improper conduct. The Commission collects and analyses extensive trading data—down to receiving daily reports from each broker on each trade executed that day. Sanctions may be too low, given market values, and should be examined. (See Principle 10.)
Principle 29. Regulation should aim to ensure the proper management of large exposures, default risk and market disruption	<b>FI</b>	Trades on both BMV and MexDer are cleared and settled through central counterparties that have detailed and transparent provisions designed to protect the markets against a default by any participant. The bankruptcy laws do not specifically address market-related issues.
Principle 30. Systems for clearing and settlement of securities transactions should be subject to regulatory oversight, and designed to ensure that they are fair, effective and efficient and that they reduce systemic risk	<b>N/A</b>	A separate CPSS-IOSCO assessment will be conducted
<i>Aggregate:</i> Fully implemented (FI) – 15, broadly implemented (BI) – 8, partly implemented (PI) – 3, not implemented (NI) – 2, not applicable/not assessed (N/A) – 2.		

#### D. Recommended Action Plan and Authorities' Response

##### Recommended action plan

**Table 10. Mexico: Recommended Action Plan to Improve Implementation of the IOSCO Principles**

Principle	Recommended Action
Principle 1	<p>The gap in legislative coverage and authority with respect to derivatives should be filled promptly, either by development and passage of dedicated derivatives legislation or by extensive additions to the LCNBV and LMV.</p> <p>The Commission should consider establishing a cross-agency committee with the CNSF to look at differences in requirements between securities and similar insurance products and develop the appropriate responses to ensure investors and policyholders are fully protected. (See also the recommendation set out in Principle 23 regarding conduct of business rules.)</p> <p>The CNBV should have MOUs in place with all significant financial markets regulatory authorities, including CONSAR, CONDUSEF and CNSF and agreements with these organizations should be concluded when practicable.</p>

Principle	Recommended Action
Principle 2	<p>The LCNBV should be amended to include specified terms of office for Governors and the President of the Commission and delineate limited criteria for removal from office (such as bankruptcy, persistent failure to attend meetings, acting in conflicts of interest, etc.).</p> <p>Consideration should be given to conducting an examination of the overall governance structure of the Board with a view to including participation of independent members, rather than most being representatives of specified authorities.</p> <p>Where the legislation requires the Commission to obtain the advice of another authority, such as the BoM, consideration should be given to amending these requirements to require a response from the other authority within a reasonable period of time (6,090 days, for example), failing which the Commission may take final action.</p> <p>The LCNBV should be amended to provide statutory immunity for the Commission, its Governors, officers and employees for actions taken in good faith in the performance of their governmental, regulatory and administrative functions and powers. Further, the protection should extend to persons who were acting on behalf of the Commission at the time of the actions in question.</p> <p>Consideration should be given to enhancing the efficacy of the appeal process and the quality of the judicial decisions reached by the establishment of specialized courts to hear financial sector matters or by giving judges additional training on the complex issues in the capital markets.</p>
Principle 3	<p>Receipt of the full amount of fees charged to the industry and full control over how those funds are allocated would enhance the CNBV's independence. Additional freedom from government salary constraints would also be valuable.</p> <p>Either CONDUSEF needs to be provided with full powers and resources to function effectively as a consumer protection agency, including the power to enforce its requirements and arbitrate consumer complaints, or its responsibilities should be transferred to another authority with suitable authority.</p> <p>See also the recommendations regarding derivatives under Principle 1, those under Principle 2 regarding the structure of the Commission and the protections afforded its Board members and staff and those under Principles 8–10 on the additional inspection and enforcement powers needed.</p>
Principle 4	<p>Consideration should be given to making rules that have been amended several times more easily accessible by posting consolidated versions on the Commission's website.</p> <p>The Commission should enhance the disclosures it makes to the public regarding its activities—both for accountability reasons and to assist the industry in understanding the applicable expectations. For example, regular publication of reports containing common findings from its inspection process, whether common deficiencies or good practices noticed, should be considered.</p> <p>The limitations on when the Commission may disclose enforcement actions and the information that may be disclosed should be amended</p>

Principle	Recommended Action
	to permit full disclosure of facts, parties, reasons for action and sanctions taken when the Commission has issued its order in the matter.
Principle 7	Additional regulations to address conflicts of interest at the SROs would be advisable. In addition to those planned to address SROs carrying on lobbying activities, the Commission should consider strengthening the controls at the BMV, particularly over the listing function. Taking the functions of the listing committee of the BMV into the CNBV, at least as concerns the BMV Group's shares, should be considered.
Principle 8	The Commission should be given the authority to conduct a 'surprise' inspection; that is, one conducted with no prior notice to the regulated entity and without having to have a suspicion of a breach of the law.
Principle 9	<p>Consideration should be given to a complete review of the level of fines available for misconduct under the statutes administered by the Commission, with a view to bringing those fines into alignment across all the laws and ensuring the fines are high enough to be dissuasive.</p> <p>The laws (LSI, LMV, and if necessary, the LCNBV) should be amended to ensure the Commission has the power to:</p> <ul style="list-style-type: none"> <li>• be fully transparent about enforcement matters, by permitting the Commission to publish full details of offences and sanctions imposed once the Commission process is completed;</li> <li>• settle disciplinary matters by agreement with a defendant without a hearing;</li> <li>• order financial statements be revised and reissued; and</li> <li>• order restitution to compensate defrauded investors.</li> </ul>
Principle 10	<p>The new asset management and investment advisory services examination program is a good initiative and additional resources should be obtained to expand it.</p> <p>See also the recommendations under Principle 9.</p>
Principle 14	<p>MexDer and the Commission should ensure full information on the risks posed by leverage is routinely disclosed to less sophisticated investors trading on the exchange.</p> <p>The necessary resources at the CNBV should be allocated to periodic reviews of the continuous disclosure documents provided by public issuers to ensure appropriate standards continue to be met.</p>
Principle 15	<p>Consideration should be given to:</p> <ul style="list-style-type: none"> <li>• requiring public companies to post shareholder meeting materials on line or file this information with the BMV for publication over its information system. A longer notice period might also be advisable, so these investors can exercise their right to an informed vote in practice; and</li> <li>• substantially reducing the threshold for reporting changes to insider ownership positions in public issuers. Ideally all changes should be reported promptly; passive institutional investors might be granted a</li> </ul>

Principle	Recommended Action
	higher threshold, such as only reporting changes of more than 2 percent.
Principle 16	<p>Consideration should be given to:</p> <ul style="list-style-type: none"> <li>• requiring the audited annual financial statements of public issuers to be published within 90 days of the year end; and</li> <li>• amending the LMV to give the Commission express powers to require issuers to restate their financial statements. (Also noted under Principle 9.)</li> </ul>
Principle 17	<p>The project considering alternative permitted structures for SIs, such as trusts or segregated portfolio companies should be pursued.</p> <p>The new asset management and investment advisory services examination program is a good initiative and should be expanded. The Commission's resources need to be enhanced to allow for more of these examinations to take place regularly.</p>
Principle 20	<p>The Commission should review the valuation methodologies used by valuation companies and price vendors for illiquid securities to ensure that appropriate practices are being followed and that the methodologies are consistent across the service providers.</p> <p>The LSI should be amended to ensure the Commission has full power to intervene in the sales and redemption process in appropriate circumstances in order to protect investors or the market as a whole, including the power to order redemptions cease or resume at an SI.</p>
Principle 21	<p>The ongoing project to ensure comparability of regulation that applies to all types of market intermediaries when carrying on similar activities, particularly those relating to business conduct and conflicts of interest should be completed as soon as possible.</p> <p>The Commission's initiative to obtain express supervisory authority over investment advisors should be supported.</p>
Principle 22	<p>The Commission should review the current capital formula to ensure that the amounts provided are sufficient to address the full range of liquidity, legal and reputational risks to which the firms may be exposed.</p> <p>The Securities Firms Rules should be amended to require firms to ensure their capital is adequate at all times, calculate it as often as necessary to ensure compliance with this requirement and report immediately to the Commission if there is any deficiency. Best practice would suggest that the capital level triggering immediate reporting should be set somewhat above the minimum capital level required to give the Commission time to take appropriate action. Given the existing capital regime that requires corrective action when the index of required capital to regulatory capital rises above 80 percent, it might be appropriate to use this as a threshold for immediate reporting.</p>

Principle	Recommended Action
Principle 23	The projects to develop a more comprehensive regulatory regime for conflicts of interest and conduct of business should be completed and the appropriate rule changes put in place as soon as possible. These rules should apply to all market participants in dealing with clients on securities or derivatives, regardless of the category of intermediary (bank, brokerage house or other market intermediary).
Principle 24	<p>See the recommendation under Principle 22 with respect to prompt capital reporting requirements.</p> <p>A written plan should be developed outlining what steps must be taken to protect investors if a securities firm is in financial difficulty.</p> <p>Consideration should be given to amending the bankruptcy legislation to ensure it effectively addresses market-related issues, such as close out of derivatives positions.</p>
Principle 27	<p>The implementation and operation of the new BMV trading rules that facilitate high frequency trading, faster crossing of large trades and direct market access should be monitored closely to ensure the current level of transparency is not negatively affected.</p> <p>The exchange and the CNBV should continue to keep abreast of the discussions in several major jurisdictions and at IOSCO of the market implications of high frequency trading, dark pools and similar market developments in order to maintain consistency of their approach to these issues.</p>
Principle 28	Consideration should be given to a complete review of the level of fines available for misconduct on the market, with a view to ensuring the fines are high enough to be dissuasive. (Also noted under Principle 9).

### **Authorities' response to the assessment (CNBV)**

34. **Mexican financial authorities agreed, in general, with the conclusions, observations, and recommendations of the assessment regarding the implementation of IOSCO Principles in the Mexican financial sector.** Most of the written comments provided by these authorities on the preliminary draft were included in the final report. Authorities consider that the exercise represented a good opportunity to discuss both strengths and weaknesses on securities markets, as well as to draw attention to main issues that should be addressed in the future. Authorities believe that the evaluation of the principles is fair and objective.

35. **The authorities found the IOSCO report both comprehensive and useful.** Also, they believe that assessors' advice and proposals will become part of their agenda for the upcoming years, and that the assessment identifies improvements that should be implemented in order to enhance the performance and development of securities markets. The report properly addresses main concerns, which are shared by authorities. On this behalf, they agree that two relevant weaknesses of Mexican securities market are its reduced number of listings and its low level of liquidity and, as a consequence, they welcome advice on how to move forward. Also, they agree that high concentration of portfolios might raise concerns, although they consider that this should not be seen as a problem unique to the securities market, but that should be considered as a characteristic of the Mexican economy as a whole. Authorities also share the assessors' point of view regarding that some enhancements should be made to CNBV's powers to publish information regarding investigations and sanctions in order to improve transparency and strengthen market discipline.

36. **While they acknowledge that Mexico lacks a Law to regulate the domestic derivatives market, they believe that most of the recommendations suggested in the report might be implemented through secondary regulation,** due to the fact that the SHCP, Banxico, and CNBV have broad powers to do so.

37. **Regarding the assessment on Principle 14 (there should be full, timely, and accurate disclosure of financial results and other information that is material to investors' decisions) they believe that Mexico complies with most of the standards of this principle.** In fact, compliance with this particular principle is similar to that observed in the most developed markets. Therefore, authorities are of the opinion that this principle should be assessed as Broadly Implemented (BI).

## II. DETAILED ASSESSMENT

38. **The assessment of the country's observance of each individual Principle is made by assigning to it one of the following assessment categories: fully implemented, broadly implemented, partly implemented, not implemented, and not applicable.** The Assessment Methodology provides a set of assessment criteria to be met in respect of each Principle to achieve the designated benchmarks. The Assessment Methodology recognizes that the means of implementation may vary depending on the domestic context, structure, and stage of development of the country's capital market and acknowledges that regulatory authorities may implement the Principles in many different ways.

- A Principle is considered *fully implemented* when all assessment criteria specified for that Principle are generally met without any significant deficiencies.
- A Principle is considered *broadly implemented* when the exceptions to meeting the assessment criteria specified for that Principle are limited to those specified under the

broadly implemented benchmark for that Principle and do not substantially affect the overall adequacy of the regulation that the Principle is intended to address.

- A Principle is considered *partly implemented* when the assessment criteria specified under the partly implemented benchmark for that Principle are generally met without any significant deficiencies.
- A Principle is considered *not implemented* when major shortcomings (as specified in the not implemented benchmark for that Principle) are found in adhering to the assessment criteria specified for that Principle.
- A Principle is considered *not applicable* when it does not apply because of the nature of the country's securities market and relevant structural, legal and institutional considerations.

**Table 11. Mexico: Detailed Assessment of Implementation of the IOSCO Principles**

<b>Principles Relating to the Regulator</b>	
<b>Principle 1.</b>	The responsibilities of the regulator should be clear and objectively stated.
Description	<p>The <i>Comisión Nacional Bancaria y de Valores</i> (CNBV or the Commission) has regulatory authority over a broad range of securities market participants, including securities firms, self regulatory organizations, securities exchanges, market infrastructure providers (central counterparties and securities depositories), price vendors, credit rating agencies, financial analysts, external auditors, public issuers and collective investment schemes, among others. The CNBV also is responsible for the supervision of commercial banks, development banks and agencies, cooperatives, credit unions and other deposit-taking institutions.</p> <p>The regulator's objectives, responsibilities, powers and authority with respect to securities are clearly defined and transparently set out in the <i>Ley de la Comisión Nacional Bancaria y de Valores</i> (National Banking and Securities Commission Law – LCNBV) and in the <i>Ley del Mercado de Valores</i> (Securities Market Law – LMV). Art. 2 of the LCNBV says:</p> <p style="padding-left: 40px;">The Commission's objective shall be to supervise and regulate, within its competence, the financial entities part of the Mexican financial system set out herein, in order to ensure their stability and adequate operation, as well as to maintain and foster a sound and balanced development of the entire financial system while protecting the interests of the public.</p> <p>Art. 1 of the LMV contains similar objectives of overall development of a competitive and efficient market, minimization of systemic risk and protecting the interests of the investing public. Both of these laws contain detailed provisions setting out the Commission's responsibilities and powers (see for example, LCNBV, Art. 4).</p> <p>The LMV and LCNBV establish the framework for regulation of the securities market in Mexico. Detailed provisions supplement the framework of laws and requirements are set out in secondary regulations made by the Commission. The laws and regulations are enforceable at law.</p>

The CNBV may interpret how its authority applies in a given situation, but has no authority to expand the scope of authority given by law. Also, the LMV expressly permits the *Secretaría de Hacienda y Crédito Público* (Ministry of Finance and Public Credit—SHCP) to interpret the law for administrative purposes, such as the application of international treaties to the law regarding the operation of foreign securities firms (LMV, Art. 161). All interpretations must be consistent with the spirit of the LMV and other applicable laws (LMV, Art. 1 and 5). Additionally, there has been an effort within the CNBV to codify the circumstances in which its discretion will be exercised to reduce the opportunities for challenges to its authority or the application of political influence. This does, however, have the potential effect of limiting its flexibility to deal with novel situations.

The situation with respect to the responsibility for regulating the securities markets is fairly clear. While the CNBV has primary responsibility in most areas, the LMV contains some shared powers across the Commission, the SHCP and the Banco de México (BoM), where the Commission requires the opinion or permission of another financial authority to make certain decisions. For example, the SHCP must give its consent for the Commission to adopt regulations and procedures to implement the requirements of the LMV. Similarly, the opinion of the BoM may be required to be provided for certain actions. The fact that the regime governing securities activities is contained in one law helps to reduce gaps or inequities in regulation. Many, but not all, of the secondary regulations are written to apply to the activity being carried on and the requirements apply to all types of institutions carrying out that activity.

However, the authority of the Commission over the derivatives market is far less clear as the regulation of this market is based on very general, residual authority provisions across the SHCP, BoM and CNBV without any explicit reference in that legislation to derivatives. There is no single statute and virtually no mention of derivatives in the current legislation to provide a clear delineation of functions and responsibilities in many areas of this market. All three of the SHCP, BoM and CNBV are involved in the supervision and regulation of the market and may issue secondary regulations in the area, which gives rise to the potential for overlap, duplication and conflict. In some cases, their roles overlap. For example, all three bodies are involved in the regulation of the Mexican Derivatives Exchange (MexDer) under the Mandatory Rules for Corporations and Trusts Participating in the Establishment and Operation of a Market for Exchange Listed Futures and Options (MexDer Mandatory Rules). (See the discussion under Principle 25). The CNBV presently has no power whatsoever over the OTC derivatives market. Working arrangements are in place between the CNBV and BoM regarding MexDer. The division of roles and responsibilities with respect to the OTC market are under discussion but have not yet been determined.

Further, insurance companies in Mexico may issue insurance contracts that in substance are equivalent to securities products. These securities-like insurance contracts are regulated by the *Comisión Nacional de Seguros y Fianzas* (the National Insurance and Sureties Commission—CNSF) and are subject to very different rules regarding disclosure, management of the products, sales practices, etc. There is very little interaction between the CNSF and the CNBV on a day-to-day basis, beyond the representative of CNSF who sits on the Commission's Board. There are no formal or informal arrangements in place to share information or coordinate approaches to functionally similar products.

The *Comisión Nacional para la Protección y Defensa de los Usuarios de Servicios Financieros* (CONDUSEF) is the consumer protection agency in the jurisdiction. Its responsibilities include promoting financial education, setting certain consumer protection requirements and receiving and responding to consumer complaints about financial services firms. The consensus is that CONDUSEF lacks the resources and powers to function effectively as a consumer protection authority. For example, it has no power to

	<p>order a financial services provider to compensate an investor for losses or to arbitrate a dispute.</p> <p>The recently created Financial Stability Council contemplates formal channels for information sharing between authorities. There is regular coordination with the BoM. In addition, the Federal Public Administration Organic Law (LOAPF) sets out the obligations for authorities to help each other regarding reports, information or technical cooperation. (LOAPF, Articles 21 and 25). All financial authorities are represented on the CNBV's Board. In addition, the Commission gives opinions to the Federal Government on financial topics.</p> <p>In practice, there is good cooperation on day-to-day matters with BoM. Also, there are formal information sharing agreements in place with the BoM and SHCP. No such agreements are in place with CNSF, CONDUSEF or the pension funds regulator (CONSAR).</p>
Assessment	Partially Implemented
Comments	<p>While the CNBV's responsibilities and jurisdiction with respect to the securities markets is clearly defined in the laws, there are gaps with respect to the supervision of the derivatives market owing to the fact that there is no specific legislation in this area. There are also overlaps in jurisdiction regarding this part of the capital markets between that of the Commission and the BoM. While there do not appear to be any gaps in practice, the specifics of each authority's jurisdiction is not clear. This gap in legislative coverage and authority should be filled promptly, either by development and passage of dedicated derivatives legislation or by extensive additions to the other relevant laws, such as the LCNBV and LMV. This gap in legislation is particularly problematic given the G20's drive for additional regulation in the OTC and exchange traded derivatives markets.</p> <p>For banks and securities firms subject to the CNBV's authority, similar requirements generally apply to similar activities. Many of the provisions in the laws and the secondary regulations focus on activities, not institutions. However, there are some gaps, notably with respect to conduct of business and conflict of interest rules related to securities market activities. Further, insurance companies under the supervision of the CNSF may offer securities-like products and these activities are subject to different requirements regarding disclosure and business conduct than the equivalent securities product. Gaps in the conflicts of interest requirements are particularly of concern, given the high level of concentration of ownership in the market among issuers and financial services providers.</p> <p>The projects to develop a more comprehensive regulatory regime for conflicts of interest and conduct of business that are currently underway should be completed and the appropriate rule changes put in place as soon as possible. These rules should apply to all market participants in dealing with clients in securities or derivatives, whether the firm conducting the activity is a bank, brokerage house or other market intermediary.</p> <p>The Commission should consider establishing a cross-agency committee to look at the differences in requirements between the securities and insurance sectors and develop the appropriate responses to ensure investors and policyholders are properly and equivalently protected. This would also have the benefit of enhancing the familiarity of CNBV staff with those at the other supervisor, thereby building positive working relationships.</p> <p>Cooperation and information sharing agreements are in place with the SHCP and BoM and cooperation works well in practice on a day-to-day level. There are no agreements in place with CONSAR, CNSF or CONDUSEF and no history of practical working relationships with the CNSF. The CNBV should have MOUs in place with all significant domestic financial markets regulatory authorities, including CONDUSEF, CONSAR and CNSF and agreements with these organizations should be concluded when practicable.</p>

<b>Principle 2.</b>	The regulator should be operationally independent and accountable in the exercise of its functions and powers.
Description	<p>The CNBV is a decentralized body of the SHCP, with technical autonomy and executive powers (CNBV Law, Article 1). While the regulator operates free of interference by the industry, it may not have the ability to operate on a day-to-day basis without external political interference owing to the control the SHCP exerts over the appointment and termination of members of the Board of Governors of the Commission. The Board of Governors consists of 13 members. Five members, including the President of the Commission (who is also the Chairman of the Board), are appointed directly by the SHCP and three members are appointed by the BoM. CONSAR and the CNSF each appoint one member. Ten of these members may be removed from office by the SHCP at its discretion, including the Commission's President. There are no terms of office for Governors and no criteria for removal from office set out in the law or by contract. The Board of Governors meet every two months.</p> <p>Further, as part of the SHCP, the Commission has no independent ability to contract without the permission of the SHCP and is obligated to follow government procedures for procurement, hiring and other activities.</p> <p>The LMV sets out where prior approval or consent of other authorities is required in order to issue a rule or give an authorization under that legislation. The required consultation process is also specified. Some of these areas may well overlap into the day-to-day functions of the Commission. However, where the legislation requires the Commission obtain the 'advice' of another authority, such as the BoM, there is no obligation on the Commission to follow that advice. Each relevant authority carries out the process of formulating that advice independently. There is one complicating factor: if the advice is not provided, the Commission may not take final action and there is no requirement in the law for the other authority to provide the advice in a timely manner.</p> <p>CNBV's budget is set annually by the SHCP, based in part on fees paid by regulated entities, as determined under a formula developed by the CNBV and approved annually by Congress. (LCNBV, Article 16, XI). The fees paid by supervised financial entities exceed the amounts returned to the CNBV; the Commission generally receives 70 percent to 80 percent of the fees remitted to the government by market participants.</p> <p>Once allocated, the Commission has no discretion on how to spend the budget monies. Funds may only be spent on the categories as fixed in the budget. Staff salaries are set by the government in accordance with the usual civil service pay scales and have been frozen for nine years. Civil service salaries are well below industry rates and turnover, particularly at the higher, more experienced staff levels, has been high. The government process that must be followed is cumbersome and that adds to the difficulty of filling vacant positions.</p> <p>None of the Commission, Chairman/President, Board members and staff of the Commission are accorded statutory legal immunity for the <i>bona fide</i> discharge of their governmental, regulatory and administrative functions and powers. However, the LCNBV requires the Commission to provide legal services and assistance to these individuals when sued in connection with acts performed in the exercise of the Commission's regulatory mandate (LCNBV, Art. 21). This assistance is only available to persons who continue to be associated with the Commission at the time of the lawsuit. Former Board members or employees are not covered. If the person is found liable, the costs of the legal assistance must be repaid to the Commission.</p> <p>Accountability and transparency of the Commission's activities is provided through the requirements of the governmental transparency law. According to this law, the CNBV must publish an annual report including information on:</p>

	<ul style="list-style-type: none"> <li>• its organizational structure;</li> <li>• staff remuneration;</li> <li>• the assigned budget and its execution; and</li> <li>• the audit results, among other information.</li> </ul> <p>Disclosure of reserved or confidential information is not required (Federal Law of Transparency and Access to the Public Governmental Information, Article 7).</p> <p>The CNBV's use of funds is reviewed by the Internal Control Unit, a unit of the Public Function Secretariat (Federal Administration Organic Law, Article 37) and by the <i>Entidad Superior de Fiscalización</i>, a legislature body with technical autonomy that audits the income and expenditures, the management and application of government resources (Mexican Constitution Act, Art. 79).</p> <p>There are provisions in the law and processes followed by the Commission to ensure the rights of parties affected by Commission decisions are protected. Affected parties have the right to be heard and give evidence before a decision is reached (LMV, Article 391). The Commission has to provide written reasons for its material decisions. Any person who is adversely affected by CNBV decision can appeal via an administrative procedure at CNBV (LMV, Article 396) or through the courts (via a lawsuit at "Contentious federal administrative court"), at an Administrative Court (Federal Law of Contentious Administrative Procedure, Article 20), or via a writ of <i>habeas corpus</i> (<i>Juicio de amparo</i>) in front of a judge.</p> <p>The legal system in Mexico creates some challenges for the Commission when its decisions are appealed. As in many countries, there is a dearth of expertise in the courts on sophisticated market issues and the judicial process is very slow. Further, unlike most common law countries, the courts in Mexico do not afford any special deference to the Commission as an expert tribunal. This combination of factors means that it is more difficult for the CNBV's position to be upheld on appeal. (See also the discussion under Principle 10.)</p>
Assessment	Not Implemented
Comments	<p>The Commission operates free of influence from the industry on a day-to-day basis. However, its ability to operate free of political interference is less than it should be both in law and in practice. The structure of the Board of Governors of the Commission and terms of appointment set out in the law give the SHCP unfettered ability to remove most of the Governors and the President of the Commission at the SHCP's pleasure, without cause or notice. The LCNBV should be amended to include specified terms of office for Governors and the President and delineate limited criteria for removal from office (such as bankruptcy, persistent failure to attend meetings, acting in conflict of interest, etc.). Consideration should be given to conducting an examination of the overall governance structure of the Board with a view to including the participation of independent members, rather than most being representatives of specified authorities.</p> <p>The CNBV is accountable to the government for its operations and use of funds. It also publishes an annual report detailing its activities. However, Commission's funding is outside its control and it does not receive all the fees charged to market participants for its services. This results in limited or no resources available to carry out necessary functions. The Commission's fee structure presently raises more funds than it receives from the SHCP in the budget. Receipt of the full amount of fees charged to the industry and full control over how those funds are allocated would enhance the CNBV's independence.</p> <p>Where the legislation requires the Commission to obtain the 'advice' of another authority, such as the BoM, consideration should be given to amending these requirements to require a response within a reasonable period of time (60–90 days, for example), failing which the Commission may take final action.</p>

	<p>None of the Commission, Chairman/President, the Board members and the staff of the Commission is accorded statutory legal immunity for the <i>bona fide</i> discharge of their governmental, regulatory and administrative functions and powers. The LCNBV should be amended to add the necessary provisions to accord this protection to all of these persons and the Commission. Further, the protection should extend to persons who were acting on behalf of the Commission at the time of the actions in question: i.e., coverage should not depend on continued employment by the Commission; former employees also should be covered.</p> <p>There are provisions in the law and processes followed by the Commission to ensure the rights of parties affected by Commission decisions are protected. There is a right to be heard, a requirement for the Commission to provide reasons and extensive rights to appeal. However, consideration should be given to enhancing the efficacy of the appeal process and the quality of the judicial decisions reached by the establishment of specialized courts to hear financial sector matters or by giving judges additional training on the complex issues in the capital markets.</p>
<b>Principle 3.</b>	The regulator should have adequate powers, proper resources and the capacity to perform its functions and exercise its powers.
Description	<p>While the CNBV's authority with respect to securities matters is fairly complete, there are significant gaps on the derivatives side owing to a lack of legislation specifically referring to derivatives. (See the description above under Principle 1 regarding the Commission's authority (and the limitations thereon) with respect to securities and derivatives.) It also lacks certain other powers that would make achievement of its regulatory objectives more assured, such as the power to be more transparent about enforcement matters (prior to the point at which all further rights to appeal have been exhausted or waived) and to settle disciplinary matters without a hearing. It also lacks the authority to order financial statements be revised and reissued. (See the discussion of these under Principle 9.)</p> <p>The CNBV's budget is set annually by the SHCP, based in part on fees paid by regulated entities, as determined under a formula developed by the CNBV and approved annually by Congress. (CNBV Law, Article 16, XI). The CNBV receives only a part of the fees paid by supervised entities (approximately 70 percent to 80 percent is remitted back to the Commission). Fines imposed in enforcement actions are paid to the SHCP.</p> <p>The Commission has no ability to affect the operational allocation of resources once funded.</p> <p>The level of resources has had a negative effect on attracting and retaining experienced and skilled staff. The budget limitations have prevented increases in the wages over in the last decade. As a result, many experienced staff, particularly at senior levels, have left the CNBV for the private sector.</p> <p>By law, all staff must receive at least 40 hours of training per year and the training budget is sufficient to meet these needs. The training is focused on supporting development of staff skills along identified career paths. Staff have been sent to foreign training programs, such as those provided by the U.S. Federal Reserve, U.S. Securities and Exchange Commission or U.S. Commodity Futures Trading Commission.</p> <p>CONDUSEF lacks the resources and powers to function effectively as a consumer protection authority. For example, it has no power to order a financial services provider to compensate an investor for losses or to arbitrate a dispute.</p>
Assessment	Not Implemented
Comments	While the supervision of the derivatives market appears to work in practice, the legal underpinning of the powers wielded by the various authorities is not assured. The powers and authority of the Commission need to be clarified and enhanced with respect to derivatives. See the discussion and recommendations above under Principle 1 regarding

	<p>the Commission's authority (and the limitations thereon) in this area. The CNBV also lacks certain other powers that would make achievement of its regulatory objectives more assured, such as the power to be more transparent about enforcement matters prior to the point at which all further rights to appeal have been exhausted or waived or to settle disciplinary matters without a hearing (see the discussion of these under Principle 9). These gaps should be rectified by prompt amendments in the LMV and by the passage of the appropriate derivatives legislation.</p> <p>The Commission's funding is outside its control and it does not receive all the fees charged to market participants for its services. It has no ability to reallocate funds between budget categories. The salary structure and levels do not reflect the challenges of hiring and retaining experienced and skilled staff. Many experienced staff, particularly at senior levels, have left the CNBV for the private sector. This loss in expertise and institutional memory is an important problem that needs to be addressed before it hampers the CNBV's effectiveness in carrying out its mandate.</p> <p>These factors limit the ability of the Commission to perform its functions and exercise its powers effectively. The Commission's fee structure presently raises more funds than it receives from the SHCP in the budget. Receipt of the full amount of fees charged to the industry and full control over how those funds are allocated would enhance the CNBV's independence. Additional freedom from government salary constraints would also be valuable.</p> <p>Where an authority is responsible for supervising more than one industry, it faces an additional challenge in balancing the attention devoted to each industry appropriately. The CNBV, in deciding in how it should structure itself and how to apply its limited resources to carrying out its overall mandate, should be cognizant of this issue and make sure sufficient weight is given to securities issues.</p> <p>The lack of powers and resources at CONDUSEF undermine its ability to function effectively as a consumer protection agency thereby putting both consumer protection and confidence in the markets at risk. Either CONDUSEF needs to be provided with full powers and proper resources to carry out its consumer protection mandate effectively or these tasks need to be transferred to another authority.</p>
<b>Principle 4.</b>	The regulator should adopt clear and consistent regulatory processes.
Description	<p>In exercise of its powers, the CNBV is required to act in accordance with the applicable laws: the LCNBV and the other laws it administers, such as the LMV and LSI.</p> <p>Secondary regulations (rules) are drafted with the active participation of members of the financial services industry. Each of the rules issued by CNBV contains an initial section that sets out the purposes and reasons for the rule or modification of the rule.</p> <p>All CNBV regulations are subject to review by the <i>Comisión Federal de Mejora Regulatoria</i> (COFEMER), which is a Mexican agency created in 2001 with the responsibility to publish proposed governmental regulations on its website and oversee the mandatory public comment process. It requires agencies to include a Regulatory Impact Statement and cost-benefit analysis with any proposed regulations. Draft regulations are published for 20 days through COFEMER's web site and public comments are requested. (Federal Law of Administrative Procedure, Articles 69 H–69 L). If there are public comments on a regulatory proposal, COFEMER sends these to the CNBV and the CNBV provides a response to the points raised. Following completion of the comment period, COFEMER must provide a public opinion of support or nonsupport for the proposal. (Federal Law of Administrative Procedure, Articles 69 H–69 L). The Commission may go ahead with a proposed rule, even if the opinion from COFEMER does not support the proposal.</p>

	<p>The CNBV also has an Internal Regulatory Process that establishes a framework for the rulemaking process. It sets out responsibilities, powers and priorities within the CNBV's Regulatory Agenda.</p> <p>The COFEMER process is mandated by law, as is the Commission's authority to make rules and the process for obtaining SHCP consent. The Commission's internal process for developing rules is not public.</p> <p>The Commission does not have a practice of publicly disclosing and explaining its policies in operational areas, such as through interpretations of regulatory actions or issuing opinions stating the reasons for its regulatory actions. The Commission does not publish reports containing common findings, whether common deficiencies or good practices noted, from its inspection process. The Annual Report is the only routine publication that contains a detailed description of the Commission's activities carried out during the year.</p> <p>There are rules in place that provide procedural fairness in the operations of the Commission. The general criteria for granting, denying, or revoking a license are made public. (See also the description under Principle 2 regarding the procedural fairness accorded affected parties, including applicants for licensing, in the jurisdiction.) Further, CNBV staff must adhere to a code of conduct, which includes requirements to avoid any situation where there may be a conflict of interest. Staff must report any such potential conflict to their immediate superior and are expected to not be involved in that matter thereafter (CNBV Code of Conduct, I.7).</p> <p>The Commission does not play an active role in promoting investor education; this is CONDUSEF's responsibility (<i>Ley de Protección y Defensa al Usuario de Servicios Financieros</i>, Art. 5). Industry consensus is that this agency does a reasonably good job promoting financial literacy.</p> <p>The authority of the Commission to make public disclosure of matters related to investigations and enforcement actions is very limited. Once a disciplinary matter is final, as in when all rights of appeal have been exhausted or waived, the CNBV can release a notice containing only the most basic facts. It may identify only the person, the violation and the sanction. It is never permitted to issue a full description of the acts or misconduct upon which the violation was based (LMV, Art. 391 and LSI, Art. 84). Also, the Transparency Act provides extensive protections for confidential information.</p> <p>The regulator's exercise of its powers is consistent and, as noted under Principle 1, efforts have been made to specify the circumstances in which it will exercise its discretion in order, among other things, ensure consistency. Also, last year the Commission has carried out (through a third party survey firm) a survey of market participants to get feedback (on an anonymous basis) on the effectiveness and consistency of regulatory actions and attitudes. The Commission has taken actions to improve performance in response to the feedback received and plans to repeat the survey this year.</p>
Assessment	Broadly Implemented
Comments	<p>The CNBV is subject to clear and reasonable procedural requirements. Its processes for consultation with the public are set out in law and are conducted through an arm's length agency of the government. New rules and changes to existing rules are subject to disclosure regarding the reasons for the rules. The rules and laws are all available on the Commission's website, although consideration should be given to posting consolidated versions of all rules that have been amended several times.</p>

	<p>There are provisions in the law and processes followed by the Commission to ensure the rights of parties affected by Commission decisions are protected. There is a right to be heard, a requirement for the Commission to provide reasons and extensive rights to appeal.</p> <p>However, the Commission does not have a practice of publicly disclosing and explaining its policies in operational areas, such as through interpretations of regulatory actions or issuing opinions stating the reasons for its actions. The Commission does not publish reports containing common findings, whether common deficiencies or good practices noticed, from its inspection process. It should enhance the disclosures it makes to the public regarding its activities – both for accountability reasons and to assist the industry in understanding the applicable expectations.</p> <p>The safeguards on confidential information are extensive. In fact, the limitations described above on when the Commission may disclose enforcement actions and the information that may be disclosed go too far. Effective enforcement requires clear communication to the public of what has been done and why. This constraint on the effective exercise of its powers should be eliminated.</p>
<b>Principle 5.</b>	The staff of the regulator should observe the highest professional standards, including appropriate standards of confidentiality.
Description	<p>The CNBV staff must adhere to a code of conduct, which includes requirements regarding</p> <ul style="list-style-type: none"> <li>• avoiding any situation that gives rise to a conflict of interest, reporting this situation to the employee's immediate superior and avoiding involvement in the matter thereafter;</li> <li>• prohibiting the use or public disclosure of any confidential information, including information concerning investigations, inspections or disciplinary actions taken by the CNBV;</li> <li>• maintaining the confidentiality of information in that person's control and preserving financial secrecy; and</li> <li>• behaving legally and fairly, and avoiding any relationship with people who might bring the Commission's reputation into disrepute (CNBV Code of Conduct).</li> </ul> <p>CNBV employees are prohibited from directly owning individual securities, although they may own mutual funds directly and individual stocks may be beneficially owned through trust accounts managed by others on a 'blind trust' (not disclosed) basis. Additionally, all public servants have to make an annual declaration of their financial position to the Public Function Secretariat (LMV, Article 372 and Federal Law of Administrative Responsibilities of the Public Employees, Title III).</p> <p>The processes to investigate and resolve allegations of violations of the standards apply generally to all public servants (Federal Law of Administrative Responsibilities of the Public Employees, Articles 8 and 49).</p> <p>There are no specific administrative sanctions for failing to adhere to CNBV Code of Conduct, although staff in breach may be subject to warnings and other disciplinary measures. However, many of the principles contained in the Code are also contained in the law or rules that apply generally to the public or to all government employees (such as acting in conflict of interest situations or breaching confidentiality rules). Breach of these may give rise to administrative (warning, fines, dismissal) and/or criminal sanctions. (Federal Law of Administrative Responsibilities of the Public Employees, Articles 8 and 49). Staff of the Internal Control Unit, a unit of the Public Function Secretariat (Federal Administration Organic Law, Article 37) carries out investigations of breaches of the latter law. The Internal Control Unit is an internal control body with offices within the CNBV and it is responsible for oversight of the CNBV's performance of</p>

	its duties in a manner similar to that performed by the Inspectors General within the US governmental system.
Assessment	Fully Implemented
Comments	Market participants uniformly praised the quality and openness of CNBV staff. The assessor was equally impressed.
<b>Principles of Self-Regulation</b>	
<b>Principle 6.</b>	The regulatory regime should make appropriate use of Self-regulatory Organizations (SROs) that exercise some direct oversight responsibility for their respective areas of competence, and to the extent appropriate to the size and complexity of the markets.
Description	<p>The LMV provides the CNBV with authority to recognize and oversee entities as self-regulatory organizations (SROs). The law recognizes stock exchanges, central counterparties and central securities depositories as SROs automatically. These SROs include the BMV and MexDer, the CCV (the central counterparty for equities) and Asigna (MexDer's clearance and settlement entity).</p> <p>Other market participant organizations may be recognized as SROs upon application. There are two such SROs presently recognized by the Commission: <i>Asociacion Mexicana de Asesores Independientes de Inversiones</i> (Association of independent investment advisors, AMAII) and <i>Asociacion Mexicana de Intermediarios Bursatiles</i> (the SRO for securities intermediaries, AMIB). Each may impose rules on its members; compliance with these rules is required under the membership agreement.</p> <p>The LMV empowers SROs with supervisory and rule-making authority to set standards of conduct and operations for their members with the aim of contributing to the soundness of the securities market. (LMV, Art. 228). SROs may set rules regarding:</p> <ul style="list-style-type: none"> <li>• requirements for membership;</li> <li>• causes for termination of membership;</li> <li>• enhancing the efficiency and transparency of the securities market;</li> <li>• the process for adopting self-regulatory rules;</li> <li>• procedures to monitor and ensure compliance with the rules; and</li> <li>• disciplinary procedures and sanctions for breaches. (LMV, Art. 229).</li> </ul> <p>The rules of the SROs are binding on their members. The SROs may penalize breaches by imposing fines, suspending or terminating a member's membership.</p> <p>The BMV performs limited self-regulatory organization functions such as monitoring trading activity and imposing trading halts when a stock moves more than 15 per cent within a day or when it may be that an issuer has not disclosed material information. It also reviews the prospectuses of all new listings in conjunction with the CNBV to ensure that the BMV's listing standards are met. Because the BMV does not have the authority to compel testimony or disclosure of information by its members or its members' employees, it is unable to conduct investigations. Accordingly, it does not take disciplinary actions against member firms or their employees. It may, but is not required to conduct regular examinations of its members. All suspicious activity is referred to the CNBV.</p> <p>CCV is responsible for acting as central counterparty for each equities trade entered into on the BMV. As such, it establishes procedures to manage risk and satisfy failed transactions.</p> <p>MexDer, which is owned by the BMV, performs analogous functions to the BMV in the futures market. However, under the MexDer Mandatory Rules under which MexDer operates, it is required to perform regular audits of its clearing members and participants (art. 5(d)). The Compliance Officer at MexDer performs these audit programs and MexDer has the power to impose sanctions on its participants.</p>

	<p>Asigna is responsible for acting as central counterparty for each futures and options contact entered into on MexDer. It also is required to perform oversight of clearing members under the MexDer Mandatory Rules</p> <p>AMAII is a voluntary organization. It has 25 members who have agreed to be inspected periodically. AMAII has contracted with a big four accounting firm to perform regular inspections on a three year cycle. AMAII is largely a trade association.</p> <p>The SRO activities of AMIB are very limited. It conducts licensing exams for employees of securities firms, mutual funds, and bank employees who are involved in selling securities and co-sponsors the Code of Professional Ethics of the Mexican Securities Community. It too carries on lobbying/trade association functions.</p> <p>SHCP and BoM also play a role in the authorization and oversight of some SROs, particularly MexDer, Asigna and CCV. For example, the licence to operate a central counterparty is granted by SHCP with the advice of the CNBV and BoM.</p>
Assessment	Not assessed
Comments	<p>The regulatory framework has a very limited role for self- regulation relating to the rules for members of specific exchanges or business activities. The obligations of SROs are clearly set out and subject to oversight by the CNBV. The SROs are expected to enforce their own rules on their members. These entities do not, however, operate as formal delegates of the regulator and the primary supervision of market participants rests with the Commission.</p> <p>This Principle is rated 'not assessed' because IOSCO has set no specific assessment criteria for the Principle. It is used for descriptive purposes only.</p>
<b>Principle 7.</b>	SROs should be subject to the oversight of the regulator and should observe standards of fairness and confidentiality when exercising powers and delegated responsibilities.
Description	<p>The requirements and process for authorization as an SRO that is a stock exchange or central counterparty are set out in the LMV and the MexDer and Asigna Mandatory Rules.</p> <p>The details of the requirements and process for authorization for other SROs are set out in the CNBV's SRO Rules. These other organizations seeking recognition must file an application that contains information including:</p> <ul style="list-style-type: none"> <li>• specific functions of self-regulation sought to be carried out;</li> <li>• requirements and procedures for admission and exclusion of its members;</li> <li>• rights and obligations of its members;</li> <li>• governance matters: representation and participation of its members at meetings of the Board and technical committees; and</li> <li>• procedures to be followed to: <ul style="list-style-type: none"> <li>○ develop the self-regulatory rules;</li> <li>○ ensure members and others subject to the SRO rules are in compliance;</li> <li>○ enforce those rules; and</li> <li>○ prevent and resolve conflicts of interest (between members and between members and the SRO).</li> </ul> </li> </ul>

An applicant for authorization must have processes in place to ensure its administration, committees and working groups are equitable and consistent with its objectives, staffed with people with the appropriate professional and technical experience to carry out its functions effectively and that its leadership is independent (SROs Rules, Art. 2).

Other than the avoidance of conflict of interest requirement, there is no express requirement that the SRO treats all members of the SRO, applicants for membership and similarly situated market participants subject to its rules in a fair and consistent manner.

Overall, there is not a lot of delegation of front line regulation to these SROs. The Commission retains the full authority to act in all areas and in many cases, such as surveillance of the markets, conducts those regulatory activities in parallel to those of the exchanges.

The Commission has veto powers regarding self-regulation standards set by SROs (LMV, Art. 231). In no case may an SRO rule contravene the law (LMV, Art. 229). In practice, all new rules and amendments to existing rules of the exchanges, central counterparties and central depository are submitted to the Commission for review and approval prior to implementation. Competitive issues, among other matters, are taken into account in these reviews. In some cases, the rules of an SRO are also subject to review and approval by SHCP and/or BoM. For example, both CNBV and BoM must approve the rules and any amendments to the rules of a central counterparty (LMV, Article 315). The rules of MexDer and Asigna are subject to the review by BoM and it may veto any rule.

On Commission request, the SROs must provide information and documentation related to the exercise of its self-regulatory functions. (LCNBV, Article 2). SROs are required to sanction their members based on their own rules and enforcement procedures. The results of all compliance examinations are to be provided to the Commission within 5 days of completion and the disciplinary and corrective actions for members are subject to the CNBV's approval (LMV, Article 229).

Additionally, the CNBV has powers to suspend or revoke the authorization granted to SROs or require the removal/replacement of directors and officers of any SRO when their conduct violates the LMV (LMV, Article 231). The CNBV can also direct the SROs to change their rules, processes, etc.

The CNBV has set specific objectives for its SRO supervision activities. These are to:

- conduct an objective assessment of the performance of the SRO;
- ensure compliance with requirements and fair practices in their operation;
- assess the quality of its administration and, in general, its soundness and solvency;
- identify possible weaknesses or areas of risk regarding the supervised entities as well as determine the actions required to strengthen them (CNBV Markets Supervision Manual).

The CNBV has statutory powers to carry out inspections to review, clarify, or evaluate supervised entities, including all SROs. Detailed on-site inspections are carried out every 12–24 months. The inspections of the exchanges and central counterparties cover all aspects of their operations – including operational capacities, systems, information technology, etc. If the CNBV has information that would indicate a breach of a law or other applicable provision, it may conduct an investigation (CNBV Markets Supervision Manual).

	<p>The CNBV may take over the SRO's responsibilities upon the withdrawal of the authorization to act as an SRO, which may occur in case of a breach of the SRO's legal duties (LMV, Article 231). The existence of an SRO does not affect the Commission's authority to regulate market participants directly.</p> <p>The same public law requiring confidentiality applies to the Commission and the SROs.</p> <p><i>Conflicts of Interest</i></p> <p>At present, AMIB and AMAII conduct both regulatory and industry representation (lobbying) functions in the same organization. The CNBV is considering new regulations to eliminate the potential conflicts of interest to which these dual functions gives rise.</p> <p>The BMV is a public company listed on itself. It is a vertically integrated company owning all or a large majority of the shares of Indeval, MexDer and the central counterparties (CCV and Asigna). There may be conflicts between its self-regulatory functions and its interests as a listed company. Its self-listing could give rise to potential conflicts of interest between its oversight of listed companies and its interests as a listed company. To address these potential conflicts of interest, certain measures were put in place in 2008 when the BMV went public including:</p> <ul style="list-style-type: none"> <li>• requiring the committees of its Board of Directors be comprised of at least a majority of independent members; and</li> <li>• providing that the surveillance function of the exchange report directly to the Board of Directors, rather than to the CEO.</li> </ul>
Assessment	Fully implemented
Comments	Additional regulations to address conflicts of interest at the SROs would be advisable. In addition to those planned to address SROs carrying on lobbying activities (which should be pursued promptly), the Commission should consider strengthening the controls at the BMV, particularly over the listing function. Taking the functions of the listing committee of the BMV into the CNBV, at least as concerns the BMV's shares, should be considered.
<b>Principles for the Enforcement of Securities Regulation</b>	
<b>Principle 8.</b>	The regulator should have comprehensive inspection, investigation and surveillance powers.
Description	<p>The CNBV has authority to conduct inspections of any supervised financial entity and request all information and documentation necessary to verify compliance with the applicable laws and rules (LMV, Article 350ff). The CNBV may conduct an on-site visit for investigation purposes with same day notice if there is a suspected misconduct/breach of the law or rules (Rules of Inspection, Article 21 and 9). Routine and special (focused) inspections may be done <u>only</u> with prior notice to the institution being examined. (See the description of the CNBV's investigation powers in Principle 9.)</p> <p>The inspection program for securities firms is carried on by the CNBV area that also examines banks. (See the discussion under Principle 21.) The CNBV can conduct additional special visits such as ones required for international cooperation purposes (LMV Article 356 and Rules of Inspection, Article 6 and 8). Also, the CNBV recently created a special group devoted to oversight of asset management and collective investment schemes that conducts targeted inspections.</p> <p>The LMV gives full powers to the CNBV for authorizing, supervising, investigating and imposing sanctions on securities exchanges and OTC trading systems for debt and derivatives operated by inter-dealer brokers (<i>sociedades que administran sistemas para facilitar operaciones con valores</i>). (LMV, Articles 253–259). It has real time access to trading data and this data is under active review. Surveillance of exchange trading is conducted both at the exchanges and the Commission.</p>

	<p>There are extensive record-keeping and record retention requirements for all regulated entities that generate a complete audit trail for each trade, including the cash flows associated with the trade. Entities are required to keep various records regarding the services provided by them for a period of 5 years (LMV, Article 208).</p> <p>Regulated entities are required to keep specific records concerning client identity (Money Laundering Rules, Rule 4). The records permit tracing of funds and securities in and out of brokerage and bank accounts related to securities transactions. The Commission has access to all information held by regulated entities, including information about the identity of all customers (LMV, Article 357). The LMV (Article 212) and rules issued by the SHCP (<i>Disposiciones de caracter general a que se refiere el artículo 212 de la LMV</i>) require firms to put in place measures to minimize potential money laundering. In fact, firms file daily reports with the Commission setting out details on each trade executed, including price, amount traded and the beneficial owner of the account.</p> <p>The CNBV does not outsource the inspection of regulated entities to third parties. Where the SROs supervise the conduct of their members, the Commission has oversight authority over those activities and full access to information maintained or obtained by the SROs. (See also the discussion of SRO supervisory activities under Principles 7 and 22.)</p>
Assessment	Partially Implemented
Comments	<p>While the Commission has broad authority to carry on almost the full gamut of inspection, investigation and surveillance activities with respect to regulated entities, it has no authority to conduct a 'surprise' inspection; that is, one conducted with no prior notice to the regulated entity. The IOSCO Assessment Methodology identifies this as a crucial power for securities regulators and its lack is a significant gap in the CNBV's powers. The assessor noted that the Commission may conduct an investigation visit with same day notice where a breach of the law is suspected and this power may alleviate the concern about this gap somewhat. However, the existence of 'just cause' for an investigation may be subject to legal challenge. Further, the Assessment Methodology is clear that both the right to inspect and investigate should be available to be exercised <u>without</u> notice. The relevant law/rules should be amended to provide clear authority for these sorts of inspections.</p>
<b>Principle 9.</b>	The regulator should have comprehensive enforcement powers.
Description	<p>The Commission has authority to investigate any matter allegedly constituting a violation of any provision of the LMV or the rules and regulations. It may –</p> <ul style="list-style-type: none"> <li>• require all kinds of information and documentation from any person or authority it believes may have information of use to the investigation;</li> <li>• conduct inspections of anyone relevant;</li> <li>• require the attendance of persons who may have relevant information;</li> <li>• hire auditors and other professionals to help in the conduct of the investigation (LMV, Article 355)</li> </ul> <p>The CNBV may impose fines, suspensions and bar participation in the industry via administrative action. It may stop the issue of securities and suspend trading in listed securities. It is able to investigate and take action against lawyers who issue opinions required under the LMV (these are required for new issues of securities), external auditors, and corporate officers and directors responsible for violations by public companies. Individuals may be prosecuted criminally by referral to the <i>Procuraduria General de la República</i> (Attorney General's Office – PGR). All criminal referrals must be submitted to the PGR through the Fiscal Attorney's Office in the SHCP.</p>

	<p>Any sanction imposed administratively by the CNBV may be challenged in court. The Commission lacks certain other powers that would make achievement of its regulatory objectives more assured.</p> <ul style="list-style-type: none"> <li>• It is not permitted to be fully transparent about enforcement matters. No disclosure of any kind is permitted until all opportunities for appeal have been exhausted or waived. Even then, only limited information about the parties, offence and penalty imposed may be disclosed.</li> <li>• It has no power to settle disciplinary matters without a hearing.</li> <li>• It lacks the authority to order financial statements be revised and reissued.</li> <li>• The CNBV cannot order restitution to compensate defrauded investors.</li> </ul> <p>Where an authority other than the Commission must take enforcement or other corrective action, the CNBV may share information obtained through its activities with that other authority. The procedures are well defined in financial laws. Those procedures establish the protocol for the request, the cases where it may proceed and the persons that are allowed make the request (Banking Law, Article 117).</p> <p>The fines that the Commission may impose were substantially revised with the new LMV as of the end of 2005. The fines for insider trading may reach two times the profit gained. The maximum fines for some other breaches go to about US\$50,000 (per event/violation). These amounts may not be high enough to be dissuasive for capital markets participants. The fines under the <i>Ley de Sociedades de Inversion</i> (Investment Companies Law – LSI) date from 2001 and are lower than those under the LMV.</p>
Assessment	Broadly Implemented
Comments	<p>The CNBV generally has powers to investigate and take action against anyone who breaches the laws it administers. However, there are some gaps that should be filled with respect to its powers to act and the sanctions that are available in particular areas.</p> <p>The fines that may be levied by the Commission vary from statute to statute. Consideration should be given to a complete review of the level of fines available for misconduct under the statutes administered by the Commission, with a view to bringing the fines into alignment across all the laws and ensuring the fines are high enough to be dissuasive.</p> <p>For enforcement activities to be effective, action must not only be taken by the regulator, the regulator must also be seen by the public and the industry to be taking action. Publication of details of offences and sanctions imposed once the Commission process is completed would be valuable information to the marketplace and make the overall process of ensuring the market operates properly more effective. It should be noted that the <i>Comisison Federal de Competencia</i> that is responsible for the enforcement of competition policy in Mexico is permitted to publish details of its actions when they commence. Publication of details of noncompliant behavior also provides useful guidance to market participants on what is unacceptable behavior. Further, while there are clear merits in pursuing matters in court or in an administrative hearing process in front of the Commission, the ability to settle cases by agreement with the defendants would add to the efficiency of the enforcement process by allowing matters to be completed expeditiously.</p> <p>The laws (LSI, LMV, and if necessary, the LCNBV) should be amended to ensure the Commission has the following powers:</p> <ul style="list-style-type: none"> <li>• to be transparent about enforcement matters, by permitting the Commission to publish full details of offences and sanctions imposed once the process at the Commission is completed;</li> </ul>

	<ul style="list-style-type: none"> <li>• to settle disciplinary matters by agreement with a defendant without a hearing;</li> <li>• to order financial statements be revised and reissued; and</li> <li>• to order restitution to compensate defrauded investors.</li> </ul>
<b>Principle 10.</b>	The regulatory system should ensure an effective and credible use of inspection, investigation, surveillance and enforcement powers and implementation of an effective compliance program.
Description	<p><i>Inspection process</i></p> <p>The CNBV conducts a comprehensive inspection program of brokers, collective investment schemes (SIs) and exchanges. Its staff conduct regular reviews of registered securities firms, asset management activities and investment advisory services (at SIs and at brokers) and exchanges. Securities firm inspections cover the firm's:</p> <ul style="list-style-type: none"> <li>• automated systems and back-office operations;</li> <li>• financial operations and net capital computations;</li> <li>• risk management systems;</li> <li>• segregation of client security holdings from firm proprietary positions; and</li> <li>• customer files and accounts and records of order executions.</li> </ul> <p>Securities firms are also subject to comprehensive on-site inspections of their operations prior to being authorized to begin business. (See the description of these processes set out in Principle 21.)</p> <p>SIs and their operators are also subjected to periodic inspections. Every fund operator receives an onsite inspection during the CNBV review of its application to be authorized as an operator. Thereafter, they are inspected periodically. The Commission used to inspect every SI group annually. These reviews had a wide scope and were primarily concerned with ensuring the technical requirements were met. This program produced detailed reports and lots of instances of minor breaches. It was very resource intensive and the staff felt obliged to follow up each breach with enforcement action, thereby overburdening the enforcement process with a lot of minor matters.</p> <p>In 2010, a new program was instituted to bring a more strategic focus to the inspections of asset management and investment advisory services, both at the SI groups and brokerage houses. The focus is compliance with conduct of business (know your client, suitability, advice provided is in client's best interests) and conflicts of interest requirements, the latter particularly of concern with the high level of concentration of ownership in the market among issuers and financial services providers. As of the date of this assessment, six of these special examinations have been conducted and one enforcement action resulting in a sanction of more than 10 million pesos has been imposed. Expansion of this program is resource constrained. (The drop in number of routine inspections of mutual fund entities set out in the table below reflects this movement to more targeted reviews.)</p> <p>The CNBV also performs regular, in-depth inspections of the exchanges (see the description set out in Principle 25).</p> <p>In all cases where inspections have been conducted, a written report is prepared and a formal letter is sent to the company detailing the inspection findings and the expectations for corrective action. The corrective actions are followed up by staff to ensure the required changes have been implemented.</p> <p>The number and type of inspections conducted by the CNBV over the past five years is set out below.</p>

	2006			2007			2008			2009			2010			Total
	Ordinary	Special	Investigation	Ordinary	Special	Investigation	Ordinary	Special	Investigation	Ordinary	Special	Investigation	Ordinary	Special	Investigation	
Banks	26	2	3	33	6	0	33	4	5	27	5	1	27	5	15	192
Securities firms	23	7	0	31	5	0	44	10	0	17	2	2	26	2	1	170
Mutual funds, distributors and operators 1/	23	0	0	28	1	0	0	0	0	0	2	1	0	4	0	59
<b>Total</b>	<b>72</b>	<b>9</b>	<b>3</b>	<b>92</b>	<b>12</b>	<b>0</b>	<b>77</b>	<b>14</b>	<b>5</b>	<b>44</b>	<b>9</b>	<b>4</b>	<b>53</b>	<b>11</b>	<b>16</b>	<b>421</b>

Source: CNBV.

1/ The drop in number of routine inspections of mutual fund entities reflect the movement to more targeted reviews described in the text.

The Commission does not publish reports containing common findings of its examination processes, whether common deficiencies or good practices noted. In part, this is because there is concern that these observations might be used against Commission in subsequent enforcement matters.

The Commission has a market surveillance area that has the capacity to detect and investigate market anomalies that might indicate market manipulation or insider trading is taking place. There are automatic systems that identify unusual transactions on the two exchanges. The Commission and the exchanges conduct surveillance in parallel. Suspicious activities are reported to the Commission for action.

It is the responsibility of CONDUSEF to receive and respond investor complaints, not the Commission. However, that agency has very limited powers. The CNBV's website includes a link to provide information to the CNBV about possible improper behavior in the markets – an informal tip line. These complaints are reviewed and may serve to initiate supervisory actions.

*Compliance systems requirements:*

Regulated entities are required to have in place an internal control and record keeping framework, including internal audit and continuous monitoring requirements to ensure compliance with the laws and rules (Securities Firms Rules, Article 105-117). These rules require firms to have internal control manuals, which contain complete policies and procedures covering the intermediary's full scope of business. Directors, officers and other employees of the firm must acknowledge the objectives and policies, including their modifications (Securities Firms Rules, Art. 116). The firm's compliance with these requirements is assessed on inspections.

Securities firms are responsible for the actions of their employees. Each firm must have a compliance function that is responsible for the design of controls that ensure the firm complies with internal and external rules. If there were a breach owing to failure to supervise, the Commission would review the compliance function's involvement in the matter and take the corresponding measures (Securities Firms Rules, Article 115).

The CNBV actively monitors market activity and may summarily suspend trading in a security on the BMV if a listed company fails to file disclosure reports on time or fails to issue a public notice explaining events that have resulted in abnormal trading. The surveillance programs of the BMV and the CNBV automatically halt trading in securities

when aberrant trading patterns appear or when the price of a stock moves 15 percent or more in a day.

The Commission, through its enforcement process, has imposed some significant penalties on market participants. In one recent case regarding breach of disclosure requirements, the company and the CEOs were each fined US\$2 million and the Chief Financial Officer was suspended from acting for any issuer or regulated entity for five years. In another case, the fine for improper sales practices was 10 million pesos. The enforcement actions taken that led to administrative or criminal sanctions over the past five years are set out in the table below.

The enforcement process is not particularly rapid. On average, it takes at least two years for a matter to move from the initial investigation to the point at which recommendations for sanctions are made. This stems from a combination of too few enforcement personnel, a rigorous process and from the large number of matters pending (see the comments above of the outcome of the old SI examination process). The fact that the Commission cannot settle cases also adds to the delays.

#### Enforcement Actions

	Administrative Sanctions	Criminal Offenses
2006	1,073	119
2007	698	136
2008	633	110
2009	524	119
2010	551	154
<b>Total</b>	<b>3,479</b>	<b>638</b>

Source: CNBV.

As noted under Principle 9, the Commission may disclose the sanctions imposed for violations to the law only when the matter is final, all appeals have been exhausted and the case is closed (LMV, Article 391 and LSI, Article 84). Even then, only limited information about the parties, offence(s) and penalty imposed may be disclosed.

Assessment

Broadly Implemented

Comments

Overall, the Commission's inspection, investigation and enforcement powers seem to be exercised effectively. As noted in the comments and recommendations under Principle 8 regarding the ability to carry out inspections without notice and Principle 9 regarding the Commission's powers with respect to enforcement matters, certain enhancements would assist its efforts in these areas. See also the comments and recommendations under Principle 4 regarding the value of regular publication of the aggregate results of the inspection processes.

The new asset management and investment advisory examination program is a good initiative and additional resources should be obtained to expand it.

<b>Principles for Cooperation in Regulation</b>	
<b>Principle 11.</b>	The regulator should have authority to share both public and nonpublic information with domestic and foreign counterparts.
Description	<p>CNBV has power to sign agreements with other domestic governmental agencies with supervisory and regulatory powers (CNBV Law, Article 4, XXIV). It may share the full scope of information with other domestic authorities with financial supervisory responsibilities without the need for external approval. The Commission must ensure the receiving supervisory entity will apply the required confidential treatment to any information relating to personal financial information and ensure the data is appropriately protected (per the Government's Transparency Law and the confidentiality provisions set out in financial sector legislation). Also, CNBV might share the information in response to a specific request by some agency or through some other mechanism (like an information technology system) as part of a previously signed agreement with the other authority (CNBV Law, Article 4, XXIV).</p> <p>CNBV can share the full scope of information with financial supervisory and/or regulatory authorities of other countries, subject to the limitations noted above on financial secrecy and data protection. The Commission has entered into a large number of bilateral MOUs with foreign regulators and supervisors in the Americas and Europe that address these issues. Sharing does not require an external approval. CNBV is entitled to sign collaboration agreements with such authorities (CNBV Law, Article 4, XXIV) and has the authority to give technical assistance and information required by such foreign governmental agencies (CNBV Law, Article 4, XXV). Also, it is empowered to collaborate with foreign authorities by exchanging information and coordinating supervisory reviews (LMV, Article 358). Such information sharing may take place even if the alleged conduct would not constitute a breach of the laws of Mexico.</p> <p>Although most of the information is provided by the CNBV in response to particular requests made by domestic or foreign authorities via a formal collaboration agreement, information might be provided by CNBV on an unsolicited basis to foreign or domestic authorities, when appropriate (CNBV Law, Article 4, XXV).</p> <p>Information and records identifying the beneficial owners or controllers of bank accounts related to securities and derivatives transactions and brokerage accounts may be shared only with some specific domestic governmental entities, including the judiciary and fiscal (tax) authorities. The CNBV may only provide this information (or other confidential protected data) to foreign authorities under a formal signed agreement of cooperation that includes reciprocity clauses (<i>Ley de Instituciones de Crédito</i> [LIC], Article 177 and 177Bis).</p>
Assessment	Fully Implemented
Comments	
<b>Principle 12.</b>	Regulators should establish information sharing mechanisms that set out when and how they will share both public and nonpublic information with their domestic and foreign counterparts.
Description	<p>The CNBV has the authority to sign collaboration agreements with domestic and foreign supervisory and regulatory authorities (CNBV Law, Article 4, XXIV). The collaboration permitted includes information-sharing among the participant authorities. Also, it has statutory power to give technical assistance and information on any matter, if requested by foreign authorities (CNBV Law, Article 4, XXV).</p> <p>CNBV actively participates in cooperation schemes to provide and receive technical assistance and to coordinate supervisory activities, especially if the cross-border activity is important. Accordingly, CNBV fosters its relationships with foreign counterparties and tries to establish information-sharing mechanisms as well as other cooperation schemes.</p>

Cooperation agreements are documented formally, mainly through bilateral or multilateral MOUs.

The terms of the cooperation agreements establish safeguards to protect the confidentiality of information transmitted to the other authorities. CNBV always makes sure that any information sent to other authority (domestic or foreign) strictly complies with legal restrictions; is limited to those matters included in the cooperation scheme and the specific request; and is afforded best practices regarding data security. Information that is provided is labelled to identify its permitted use and the CNBV periodically follows up with the receiving regulator to obtain assurances that those restrictions have been followed.

The CNBV has a formal MOU with each of the SHCP and BoM domestically and one with CONDUSEF is in process. There is no agreement with the insurance supervisor (CNSF) or the pension regulator (CONSAR), although both of these entities are represented on the Board of the Commission. It has established formal information-sharing mechanisms and cooperation schemes (which include assisting in licensing and surveillance responsibilities, if necessary) with financial authorities of many countries, mainly through signing Memorandum of Understanding (MOU) with foreign regulators. It has MOUs in place with regulatory and supervisory authorities in the Americas and Europe, including the United States, Brazil, Canada, United Kingdom, Argentina, Peru, El Salvador, Venezuela, Panamá, as well as Spain, Germany, the Netherlands and various other European countries. It also a signatory to the IOSCO Multilateral Memorandum of Understanding (MMOU).

The CNBV keeps records of all the information requests it receives from and the responses it gives to other domestic authorities (both financial and not) and foreign counterparties. The general type of information requested by or from the CNBV includes:

- fit and proper information (i.e., related to the authorization process for individuals and/or entities);
- information for investigation purposes (matters involving cross-border issues, such as reconstruction of transactions; insider dealing, market manipulation, misrepresentation, etc.);
- information related to the supervision and oversight of the supervised entities/persons (supervisory concerns, findings of inspection visits, imposition of supervisory sanctions, etc.); and
- information related to technical issues (i.e., regulation, consultation on international standards implementation, etc.).

During the period from 2006 to the first half of 2011, the CNBV has had 86 cases that required requests for information to be sent to foreign counterparts. Of that number:

- 54 were related to fit & proper information;
- 29 were related to investigations; and
- 3 were related to supervision.

One matter may generate requests for information to more than one other regulator. For example, for a fit & proper inquiry, the person in question may have links with more than one jurisdiction, thereby requiring information from authorities in all the jurisdictions. Therefore, over this period, the CNBV has made 175 requests for information related to the 86 cases above mentioned. The numbers per year are broken down in the table below.

Number of Requests for Information CNBV to Foreign Counterparts (Exchange of Information)							
Type of Request	2006	2007	2008	2009	2010	2011	Total
Fit & proper	7	4	13	12	14	4	<b>54</b>
Investigations	1	4	6	12	2	4	<b>29</b>
Supervision						3	<b>3</b>
Technical Assistance							
<b>Total</b>	<b>8</b>	<b>8</b>	<b>19</b>	<b>24</b>	<b>16</b>	<b>11</b>	<b>86</b>
Sub-requests with different foreign authorities or jurisdictions	12	11	76	32	22	18	<b>175</b>
Source: CNBV.							
<p>During the period from 2006 to the first half of 2011, the CNBV received 206 requests for information from its foreign counterparts. Of that number:</p> <ul style="list-style-type: none"> <li>• 80 were related to fit and proper information;</li> <li>• 55 were related to investigations;</li> <li>• 25 were related to supervision;</li> <li>• 43 were related to very specific technical assistance; and</li> <li>• 3 were related to very specific alerts (i.e., cross-border ponzi schemes).</li> </ul> <p>As above, one request may result in more than sub-request of information that the CNBV has to manage internally (i.e., involve different divisions, such as the legal, supervision, IT or AML-CFT divisions). During the period from 2006 to the first half of 2011, the CNBV has responded to 273 requests for information related to these 206 cases. The numbers per year are broken down in the table below).</p>							
Number of Requests for Information Foreign Counterparts to CNBV (Exchange of information)							
Type of Request	2006	2007	2008	2009	2010	2011	Total
Fit & proper	21	9	16	11	11	12	<b>80</b>
Investigations	14	13	6	14	4	4	<b>55</b>
Supervision	7	9			1	8	<b>25</b>
Technical Assistance	9	17	2	7	5	3	<b>43</b>
Alert						3	<b>3</b>
<b>Total</b>	<b>51</b>	<b>48</b>	<b>24</b>	<b>32</b>	<b>21</b>	<b>30</b>	<b>206</b>

	<p>Number of coordination (sub-requests) with different divisions at the CNBV/ other authorities in Mexico</p> <table border="1"> <tr> <td>56</td> <td>59</td> <td>52</td> <td>18</td> <td>14</td> <td>74</td> <td><b>273</b></td> </tr> </table>	56	59	52	18	14	74	<b>273</b>								
56	59	52	18	14	74	<b>273</b>										
	<p>The average length of time between receipt of request and response depends on the nature and urgency of the request, the complexity of the information required and the number of departments or authorities that need be consulted. To shorten response times, it is the practice of the CNBV (and the CNBV requests the same of its foreign counterparts) to transmit the information as it is produced or gathered (i.e., not to wait until all the requested information is gathered). In the Commission's experience, the average length time between receipt of request and response is:</p> <table border="1"> <thead> <tr> <th>Type of Request</th> <th>Requests made by the CNBV to its foreign counterparts (Average time of response by counterparts)</th> <th>Requests made by foreign authorities to the CNBV (Average time of response by CNBV)</th> </tr> </thead> <tbody> <tr> <td>Fit &amp; proper</td> <td>45 days</td> <td>35 days</td> </tr> <tr> <td>Investigations</td> <td>60 days</td> <td>50 days</td> </tr> <tr> <td>Supervision</td> <td>25 days</td> <td>25 days</td> </tr> <tr> <td>Technical Assistance</td> <td>30 days</td> <td>30 days</td> </tr> </tbody> </table> <p>Information may be able to be provided more quickly in case of urgency.</p>	Type of Request	Requests made by the CNBV to its foreign counterparts (Average time of response by counterparts)	Requests made by foreign authorities to the CNBV (Average time of response by CNBV)	Fit & proper	45 days	35 days	Investigations	60 days	50 days	Supervision	25 days	25 days	Technical Assistance	30 days	30 days
Type of Request	Requests made by the CNBV to its foreign counterparts (Average time of response by counterparts)	Requests made by foreign authorities to the CNBV (Average time of response by CNBV)														
Fit & proper	45 days	35 days														
Investigations	60 days	50 days														
Supervision	25 days	25 days														
Technical Assistance	30 days	30 days														
Assessment	Fully Implemented															
Comments	The Commission should complete the MOU process with CONDUSEF as soon as practicable and move promptly to put a similar agreement in place with CNSF and CONSAR.															
<b>Principle 13.</b>	The regulatory system should allow for assistance to be provided to foreign regulators who need to make inquiries in the discharge of their functions and exercise of their powers.															
Description	<p>The regulatory system generally allows for assistance to be provided to foreign regulators who need to make inquiries in the discharge of their functions and exercise of their powers, subject to the formal collaboration conditions mentioned under Principle 12. There is no need for the subject behaviour to meet any dual illegality requirement and the CNBV does not have to have an independent interest in the matter. As noted above, the CNBV is a signatory to the IOSCO MMOU.</p> <p>The CNBV can assist foreign counterparties in order to share the necessary information to reconstruct securities and derivatives transactions. This assistance might be provided under formal collaboration agreements (CNBV Law, Art. 4, XXIV and XXV) or through other coordination schemes (LMV, Article 358).</p> <p>The CNBV can share records for securities and derivatives transactions that identify the client (account holder/authorized trader), the amount purchased or sold; time and price of the transaction and the firm that carried out the trade. The CNBV keeps records of the</p>															

	<p>characteristics of securities and derivatives transactions (amount, time, price, etc.) and has access to records kept in another domestic financial authority such as the BoM or BMV.</p> <p>The CNBV may obtain the kind of information necessary for a foreign regulator to determine if some activity carried on in, or from, Mexico constitutes a breach of the law in the foreign jurisdiction regarding:</p> <ul style="list-style-type: none"> <li>• insider dealing, market manipulation, etc.;</li> <li>• issue, offers or sale of securities and derivatives;</li> <li>• market intermediaries, collective investment schemes, or other entities required to be registered; and</li> <li>• markets, exchanges and clearing and settlement entities.</li> </ul> <p>The CNBV is able to assist foreign regulators in obtaining information on the regulatory processes as it is directly responsible for issuing rules on prudential regulation, accounting criteria and disclosure standards, among other things (CNBV Article IV). Also, the CNBV collaborates with other Mexican authorities which are in charge of or administer laws or issue rules with respect to financial institutions, as an expert consulting body (CNBV Article IV).</p> <p>In practice, the Commission can require regulated entities to produce documents and can request documents from other parties to assist a foreign regulator. It has no authority to take testimony under oath but can compel the personnel of regulated entities to appear to give information and request the appearance of other persons. All information given to the Commission is required to be truthful.</p> <p>The Commission cannot get court orders or injunctions for other regulators, but could provide guidance to foreign regulators on the domestic process and requirements.</p> <p>The CNBV is able to provide assistance to foreign regulators about the financial conglomerates under its supervision and can provide information about their ownership, structure, capital, investments in other group members, exposures and management.</p> <p>Additionally, the CNBV has the authority to carry out inspections abroad. These have been conducted several times in coordination with the Commission's counterparts in the foreign country. The CNBV exchanges information very actively with foreign financial authorities. The CNBV is a signatory to the IOSCO MMOU and has many bilateral MOUs with other countries. (See the list in Principle 12.)</p>
Assessment	Fully Implemented
Comments	
<b>Principles for Issuers</b>	
<b>Principle 14.</b>	There should be full, accurate and timely disclosure of financial results and other information that is material to investors' decisions.
Description	<p>The law and regulations provide a comprehensive public issuer disclosure system, including requirements to file periodic reports, provide prospectuses when securities are issued and make timely disclosure of material events.</p> <p>In order to issue securities to the public, it is necessary to file a disclosure document (prospectus or an informative supplement) with the Commission, which must include extensive specified information, as well as the rights and obligations of the offer (LMV, Article 86). The securities must be registered with the <i>Registro Nacional de Valores</i> (National registry of securities, RNV). Any entity registering its securities (debt, equity or SI) with the RNV also must simultaneously apply for their listing on the BMV. The BMV and the CNBV both must give their consent before a security is listed and registered.</p>

Each may refuse to grant approval if the issuer does not meet their respective requirements.

Private offers of securities are permitted to take place without registering the securities in the RNV or listing them on the exchange. These offers are restricted to those conducted only to qualified investors (high net worth individuals and institutional investors); those made to fewer than 100 persons (legal or natural); and those made to officers, employees, etc. of the offering company (LMV, Article 8).

The initial application materials for a new issue of securities and the continuous disclosure documents are filed electronically with the CNBV and the BMV. The BMV's electronic system gives the public immediate access to all final prospectuses and the continuous disclosure materials of the issuers (financial statements, material change reports, etc.).

Issuers must file an Annual Report in prescribed form, including audited financial statements with the BMV and the Commission (LMV, Article 104, III). In addition to the annual audited financial statements, public issuers must provide CNBV with unaudited quarterly financial statements in prescribed format. All financial statements must include a management discussion and analysis of the results and information on liabilities, operating segments (sales per product and geographically), advances in implementation of IFRS and derivatives. This information is sent to the BMV in order to be disclosed to the market and is also published on the CNBV's website (LMV, Article 104, I).

Issuers must disclose information about material changes immediately through the electronic means provided by the Exchange. All material information that an issuer has must be disclosed immediately (LMV, Article 105). "Material information" is defined as acts, facts or events of any nature that influence or could influence the prices or value of listed securities (LMV, Article 2). The Issuers Rules sets out criteria to determine when an event has to be considered as material information. The disclosure obligation also applies to a number of events, such as corporate restructurings, the results of shareholder votes on important matters, mergers and acquisitions, etc. (LMV, Article 104).

Disclosure of material information (such as trade secrets or pending mergers) may be omitted or delayed with the permission of the Commission. This permission will only be granted if the:

- transaction in question has not yet taken place;
- information is not already public from another source; and
- market price of the stock has not started to move (movement suggesting the information is being used by someone for trading).

The LMV has been recently modified to establish the issuer's obligation to deliver specific reports to CNBV about their trades in derivatives, including collateral, notional amounts and payment conditions of those trades, as well as their possible contingencies (LMV, Article 104, VI Bis).

The application for approval of a new issue must include extensive specified information, including the issuer's articles of incorporation, by-laws, prospectus, the audited financial statements, a legal opinion, credit rating (if applicable), etc. (LMV, Article 85). The required contents of the offering document are set out in LMV Article 86, supplemented by the Issuers Rules. When the most recent financial statements included in the prospectus are more than 6 months' out of date, listed companies must provide additional financial statements and comparative figures for the previous year (Issuer Rules, Article 2, I, f).

General advertising of offers of securities is subject to prior approval from the CNBV. The CNBV has authority to establish circumstances where no prior approval is required. An offer may not be promoted using information that is not included in the prospectus (LMV, Article 6).

The regulated derivatives market has standardized contracts set by MexDer rule. Under the regulations, any new contract to be negotiated on MexDer needs to be approved by the Board of Directors of MexDer, and the terms of each new contract need to be approved by the SHCP, with input from BoM and the CNBV. The terms of new contracts must be published by MexDer at least five business days prior to the beginning of trading of the contract. Generally, terms of each new contract published include sufficient information to fully identify the characteristics of the product and the terms and mechanics of trading. Disclosure about the risks related to gearing or leverage is not required to be disclosed in the standard information about exchange-traded derivatives.

The CNBV has several ways to ensure the accuracy and timeliness of the required disclosure. For example, it may:

- demand additional information when it considers that the information already disclosed to the market is insufficient, vague or confusing; also, the CNBV has powers to order an issuer to rectify, ratify or deny material information that has been disclosed by third parties and could influence the price of the securities (LMV, Article 106);
- order the BMV to halt trading in a security if filings are not made on time; the trading halt continues until the filing is completed or the issuer provides a satisfactory explanation for the delay or the failure to disclose (LMV, Article 107); and
- impose fines on issuers that fail to comply with their disclosure obligations (LMV, Article 392).

It is forbidden to disclose false or misleading information about securities or related to the issuer's financial, economic or legal position (LMV, Article 368). The Issuers Rules establish clear and defined disclosure obligations for each person responsible for gathering and providing information to the public and the regulators. For example, two members of the Board of Directors, the internal auditor, the CEO, the financial and legal directors and the external auditor, among others, must sign the prospectus. The Issuers Rules establish the scope and content of these persons' obligations and liabilities (Issuer Rules, Article 2).

No one in possession of material undisclosed information is permitted to trade on that information or pass that information to anyone else (LMV, Article 364). Persons with access to material undisclosed information acquired through their positions must maintain the confidentiality of such privileged information (LMV, Article 363). Issuers are required to keep extensive records of meetings at which material information was discussed, including the substance of the discussions and who was present. Officers, directors, significant shareholders, etc. are also subject to limitations on short term trading. They cannot sell any securities of the issuer with whom they are associated (including options and derivatives linked to the issuer's securities) for three months after their last purchase (and vice versa—they cannot buy securities until three months after their last sale) (LMV, Article 365). CNBV can impose a fine on those who breach these obligations (LMV, Article 392, IV). Further, trading on inside information or breaching one's obligations of confidentiality are criminal offences.

Foreign issuers must register their securities with the Securities National Record (RNV) in order to issue them publicly via prospectus in Mexico. To be permitted to register, they must establish that in their home jurisdiction they are subject to disclosure obligations equivalent or superior to those established for Mexican issuers (LMV, Article 58).

	<p>For foreign equities and ETFs to be listed on the BMV for trading on the <i>Sistema Internacional de Cotizaciones</i> (SIC), CNBV has granted direct recognition of foreign stock markets that have similar disclosure rules, among other requirements (SIC Rules, Article 4). These are securities that:</p> <ul style="list-style-type: none"> <li>• were not subject to a public offering in Mexico (that is, not issued in Mexico under a prospectus);</li> <li>• are not registered in the RNV; and</li> <li>• are listed on foreign securities markets recognized by the CNBV (including NASDAQ, the New York Stock Exchange, the London Stock Exchange, the TSX Group, Inc. and the Deutsche Börse AG), or whose issuers have otherwise been sponsored by a Mexican bank or broker and approved for listing by the CNBV.</li> </ul> <p>For sponsored recognition, the sponsor must assume the issuer's disclosure obligations (SIC Rules, Article 10). Securities listed on the SIC may only be traded on behalf of sophisticated investors - Mexican institutions and other qualified investors, such as foreign financial institutions and high net worth individuals.</p> <p>The disclosure requirements for foreign issuers are consistent with IOSCO's International Disclosure Standards for Cross-Border Offerings. In the case of the SIC, the CNBV grants a direct recognition to those securities that are regulated by countries that are members of the IOSCO Technical Committee. These issuers are permitted to use the continuous disclosure documents that they file in their home jurisdiction to meet the equivalent disclosure requirements in Mexico and these documents do not have to be translated into Spanish if they are in English.</p>
Assessment	Broadly Implemented
Comments	<p>The regulatory regime generally provides for full and accurate disclosure of financial results and other information that is material to investors' decisions. However, there are a few gaps that should be addressed. Additional disclosure with respect to the risks of leverage on derivatives contracts is required under the Assessment Methodology. Best practices would suggest certain information should be provided more quickly to investors. Changes need to be put in place to give investors effective access to the information regarding shareholder meetings in order to make informed decisions and vote.</p> <p>Disclosure about the risks related to leverage is not required to be included in the standard information about exchange-traded derivatives provided to customers. Given that at the present time virtually all transactions are undertaken either for sophisticated institutional investors or for the intermediaries' own accounts, this gap in disclosure is not a concern in practice. However, as the client base expands beyond sophisticated parties, MexDer and the Commission should ensure full information on the risks posed by leverage are routinely disclosed to these investors.</p> <p>(See the comments and recommendations below under Principle 15 regarding disclosure of shareholder meeting information and those under Principle 16 regarding the timeliness of annual audited financial statement reporting.)</p> <p>Finally, effective regulation requires there be appropriate oversight of market participants to ensure the rules are being followed in practice. Few resources at the CNBV are devoted to structured, routine reviews of the continuous disclosure provided by public issuers. While not strictly required by the Assessment Methodology, a program of this type is useful, both to provide an incentive for compliance by the issuers and to identify areas where additional disclosures might be useful more generally. The necessary resources at the CNBV should be allocated to periodic reviews of the continuous disclosure documents provided by public issuers to ensure appropriate standards continue to be met. It should be noted that the Commission has taken action against</p>

	issuers for disclosure failings and in one recent case imposed significant penalties on the issuer, its CEO and CFO (see the discussion under Principle 10).
<b>Principle 15.</b>	Holders of securities in a company should be treated in a fair and equitable manner.
Description	<p>The rights of shareholders in public companies are governed by a combination of the LMV and the <i>Ley General de Sociedades Mercantiles</i> (Corporations Law, LSM). The shareholders' general assembly is the ultimate governing body of the company (LSM, Article 178). Shares of the same class must carry equal rights, including rights to vote and to receive dividends (LSM, Articles 112 and 113). The shareholders vote for the election of directors at the annual general meeting. Further, shareholders owning 10 percent of the shares of the company are able to designate and to revoke the appointment of a member of the Board of Directors at the annual shareholders meeting (LMV, Article 50, I). Under the LSM, only someone with 30 percent of the shares could exercise this power.</p> <p>Issuers are permitted to be organized other than as companies. Most of the other issuers are organized as special purpose vehicles via a trust structure. The LMV contains provisions providing investors in these types of vehicles similar protections to those afforded shareholders under the LSM.</p> <p>Most shares of public issuers are held in the central depository (Indeval) in noncertificated form. The LMV provides that certifications issued by Indeval, coupled with certifications issued by Indeval participants (brokers and banks through which the investors hold the securities), are sufficient to permit investors holding voting securities at Indeval to attend and vote at securities holders meetings and to exercise corporate, economic and other available rights.</p> <p>Important items like poison pills, share splits, mergers, acquisitions and corporate changes are subject to approval at a shareholders' extraordinary meeting (LMV, Article 48, I). Three quarters of the capital of the company must be represented at the meeting and the resolution must be approved by votes representing at least 50 percent of the company shares (LSM, Article 182 and Article 190).</p> <p>Notice of meetings and the agenda must be published at least two weeks before the meeting (LSM Article 186). The shareholders have the right to free access to the information and documents related to each of the topics to be discussed at a shareholders meeting at least 15 working days ahead of the meeting. This information must be made available at the offices of the company (LMV, Article, I). The issuer is not required file this information with the BMV for publication over its information system. Shareholders may attend in person or vote by proxy (LMV, Article 49, III).</p> <p>There is a regime for tender offers/takeover bids that includes requirements related to disclosure and the procedures that must be followed, as well as minority rights (LMV, Articles 95–102). Also, the LMV permits issuers to include poison pill provisions in their by-laws that would apply in the case of a take-over bid (LMV, Article 48). These poison pills must be approved by virtually all the shareholders present at a shareholders meeting and are subject to general limitations on scope and effect set out in the law.</p> <p>Board members and officers have fiduciary duties to the company and its shareholders; they owe the company and its shareholders duties of due care and loyalty. The law specifies acts and circumstances that would violate these duties. The directors and officers are subject to personal civil or criminal liabilities for failure to perform their duties (LMV, Article 30–40). Public companies are required to have at least 25 percent independent directors. All audit committee members must be independent directors and the duties of that committee are laid out in detail in the law (LMV, Article 25).</p> <p>The CNBV can bring an action under the law to suspend or bar an officer or a director from acting for a public company for up to five years and has done so in practice.</p>

The bankruptcy or insolvency of the company is ruled by the ordinary process established in the LSM and the *Ley de Concursos Mercantiles* (Bankruptcy Law).

*Take over bids*

The regime to govern takeover bids is set out in the LMV (Article 95–103). Bids to acquire securities may be voluntary (LMV, Article 95 & 97); a bid becomes mandatory at 30 percent (Article 98).

- A take-over bidder must obtain the authorization of CNBV to launch the bid. As part of the application process, the bidder must provide an offering document that contains all the material information related to the bid, such as the price, amount of shares to be acquired, etc. Related agreements with other purchasers or with shareholders or directors of the target company must also be disclosed (LMV, Article 96).
- The bid must be open for at least 20 working days (LMV, Article 97, I).
- The offering document must be provided to the owners of shares subject to the bid;
- The amount offered for each share has to be the same, independent of the class or type of stock (LMV, Article 98, II).
- The offering must be done for 100 percent of the share capital when the bidder intends to obtain control (more than 51 percent) of the company (LMV, Article 98, III, b).
- The directors and relevant executives of the target company must avoid performing acts or operations that might affect the company or hinder the development of the bid. Within 10 days after the start of the bid they must publicly disclose (through the stock exchange) their opinion on the offer, including the price and the conflicts of interest that each of its members face in respect of the bid. This opinion may be accompanied by one from an independent expert. The directors must disclose whether or not they will tender their own shares to the bid (LMV, Article 101).

There have been very few takeover bids, so the operation of these rules in practice is difficult to assess.

The prospectus and annual report must contain the information on substantial shareholdings of the issuer. This disclosure includes the name of:

- beneficial owners of more than 10 percent of the share capital of the issuer;
- Shareholders who exercise significant influence in the issuer (holders of 20 percent or more of the share capital); and
- shareholders who exercise control (holders of 51 percent or more of the share capital) (Issuer Rules, Appendix H, II, C. 4. c. and Appendix N, II, C. 4. c.).

Any person who acquires more than 10 percent and less than 30 percent of the share capital of the issuer must disclose this acquisition to the market on the next working day (LMV, Article 109). The disclosure obligation applies to a person or group of persons who acquire those percentages of share capital directly or indirectly through related persons or companies (LMV, Article 109). The calculation of percentage ownership must take into account ownership of securities convertible to or otherwise equivalent to ordinary shares (including options or derivatives based on such shares). Changes in ownership of 5 percent (up or down) must be disclosed by the next business day. Since intermediaries are required to provide daily information to the CNBV on all trades executed, which information includes the names of the beneficial owner on the accounts, the CNBV has

	<p>sufficient independent information to ensure these obligations are met.</p> <p>The prospectus and issuer's annual report must contain information on the aggregate shareholdings of all directors and senior management who have an individual interest between 1 percent and 10 percent (Issuer Rules, Appendix H and Appendix N). Owing to concerns about personal security, the precise number of shares owned by each person does not have to be publicly disclosed but must be provided to the Commission. Changes of 5 percent (up or down) must be disclosed to the market on the next working day (LMV, Article 110). Once one of these persons acquires 10 percent or more of the securities of the issuer, the usual insider reporting obligations apply.</p> <p>The CNBV may impose a fine for each breach of disclosure obligations (LMV, 392, I, g.). It has imposed substantial fines for late filing of disclosure documents, incomplete or omitted information and failure to file insider reports.</p> <p>Any foreign issuer that wishes to register its shares in the RNV for direct public offer in the jurisdiction will have to demonstrate to CNBV that in its home jurisdiction it is subject to requirements regarding shareholders rights equivalent or superior to those applicable to domestic issuers (LMV, Article 58). When deciding whether to recognize a foreign stock exchange for the purposes of listing foreign securities on the SIC, the considerations include whether that foreign exchange or market has similar provisions to protect shareholders' rights, among other requirements (SIC Rules, Article 4, I). (See the discussion of the SIC under Principle 14.)</p>
Assessment	Broadly Implemented
Comments	<p>The law requires prior notice of shareholder meetings and the information on the matters to be discussed must be made available to shareholders in advance of shareholder meetings, as contemplated by the Assessment Methodology. However, neither the notice period, nor the method of making the information available recognizes the current realities of how shares are held and by whom. The short notice period, coupled with the lack of a requirement to send the materials to shareholders or otherwise make them easily available to investors by posting them on a website or through the BMV's information system, may effectively disenfranchise all but local investors. Informed and active investors enhance corporate governance standards, thereby enhancing shareholder value. Consideration should be given to requiring public companies to post the materials on line or file this information with the BMV for publication over their information system. In a market with a significant number of international investors, 15 days notice of the meeting may not be sufficient. A longer notice period so these investors have time in practice to exercise their informed voting rights might also be advisable.</p> <p>The insider reporting regime incorporates certain best practices by recognizing that the calculation of an insider's position involves more than just voting securities; it requires the inclusion of other instruments convertible to or otherwise equivalent to ordinary voting shares (including options or derivatives based on such shares). Changes in ownership also must be disclosed by the next business day. However, the trigger for subsequent reporting is not particularly sensitive. A change in ownership of 5 percent is quite high by other markets' standards, where passive institutional investors may only be required to report changes of 1 percent or 2 percent, but directors and officers and anyone in a position to exert control over the issuer has to report <u>any</u> change in ownership. It also is quite high given the relatively low public float requirements for listed securities (15 percent initially and 12 percent on an on-going basis). Consideration should be given to reducing substantially the threshold for reporting changes. Ideally all changes should be reported promptly. Passive institutional investors might be granted a higher threshold, such as only reporting changes of more than 2 percent.</p>

<b>Principle 16.</b>	Accounting and auditing standards should be of a high and internationally acceptable quality.
Description	<p>As part of the registration of any class of securities, the issuer must file financial statements audited by external auditor of the issuer and its affiliates, for the last three financial years or the date of incorporation of the company, if the company has been in existence less than three years. The most recent audited financial statements should not be older than 15 months (Issuers Rule, Article 2).</p> <p>By law, an issuer must send their financial statements, including the related notes, to the Commission, the BMV and the public. These statements must be prepared in accordance with the Articles 78, 79, and 81 of the Issuers Rules. All references to financial statements in the Issuers Rules mean: the balance sheet, statement of income (or of the results of operations), statement of changes in stockholder's equity and statement of cash flows.</p> <p>All public issuers have a December 31<sup>t</sup> year-end and must provide:</p> <ul style="list-style-type: none"> <li>• unaudited interim financial statements within 20 days of the end of the first, second and third quarters of the year; fourth quarter unaudited results are due within 40 days of the year end;</li> <li>• within four months' of the issuer's year end, the audited annual financial statements, as well as those of its affiliates that contribute more than 10 percent in its income or consolidated total assets, accompanied by the external auditor's report; and</li> <li>• not later than April 30th of each year, an annual report in the form specified by the Rules (form varies by type of issuer), with the final page signed by the external auditor, certifying that the financial statements attached to the annual report were reviewed under the required auditing standards (Issuers Rule, Article 33).</li> </ul> <p>Mexico is in the process of transitioning to International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB). Until the end of 2011 all the financial statements of issuers (other than financial institutions) are to be prepared in accordance with the generally accepted accounting principles in Mexico (MXGAAP) issued by <i>Consejo Mexicano para la Investigación y Desarrollo de Normas de Información Financiera</i> (CINIF). As of January 1, 2012 the financial statements of these issuers must be prepared in accordance with IFRS (Issuers Rule, Article 78). The transition period from MXGAAP to IFRS will be subject to IFRS 1 <i>First-time Adoption of International Financial Reporting Standards</i> that sets out the procedures that an entity must follow when it prepares its general purpose financial statements under IFRS for the first time.</p> <p>Financial institutions, such as banks, investment funds, securities firms, etc. are required to follow the accounting regulations issued by the Commission. These accounting standards consist of MXGAAP with additional guidance set by the Commission in certain areas—such as the treatment of financial assets. The Commission has deferred the decision on adopting IFRS for these financial institutions until pending debates at the IASB on significant issues are resolved. The Commission acts as the interpreter of the accounting standards for financial institutions.</p> <p>The accounting standards that apply to both financial institutions and nonfinancial issuers are viewed by the regulators and market participants as requiring the financial statements to be comprehensive, reflect consistent application of accounting standards and be comparable across at least three years.</p> <p>Until the end of 2011, the required annual audit and external auditor's report must be prepared and presented under local auditing standards issued by the Mexican Institute of Public Accountants (IMCP), the auditing standard setting body in Mexico. From 2012, the audit of both public issuers and financial institutions must be based on International</p>

	<p>Standards on Auditing (ISA) issued by the International Auditing and Assurance Standards Board of the International Federation of Accountants (Issuers Rules, Article 78). The auditor is required to be independent in both fact and appearance of the company being audited and the Issuers Rules contains an extensive list of factors to be assessed in determining whether this requirement is fulfilled (Article 83).</p> <p>The external auditor generally is appointed by Audit Committee of the issuer and approved by the shareholders at the annual shareholders meeting.</p> <p>Issuers must disclose (to the BMV and Commission) any change of external auditor responsible for the financial statements, indicating the causes for the change. The Commission may ask the auditors that have been removed for their views regarding the reasons for the change and may order the BMV to make these reasons available to investors. (Issuers Rule, Article 42)</p> <p>The Commission has no power to require issuers to restate their financial statements when they deviate from accepted standards. However, in practice, issuers may voluntarily undertake restatements when faced with enforcement action as an alternative.</p> <p>Under the LMV, the Commission has power to oversee the firms that act as external auditors to public companies, including the partners or employees on the audit team and may conduct investigations, require them to provide information and documentation, and require the attendance of partners, representatives and other employees of the auditing firms to answer questions. Also, the Commission has the authority to set auditing standards to be observed by the auditing firms. The Commission may issue rules and audit procedures where there are gaps in the applicable standards or where, in the opinion of Commission, the standards are not enough (LMV, Article 352).</p> <p>IMPC is an active member of the International Federation of Accountants (IFAC). As a member, IMPC has implemented IFAC's quality control processes for accounting firms. These entail reviews of accounting firm processes and activities. Resources have been mobilized and examinations by IMPC of firms have been underway for the past two years.</p> <p>The Commission has completed a project that developed a framework for the oversight of the quality of external audit firms' processes and performance. However, currently there is no rule that allows the Commission to review the audit process followed by auditing firms on a routine basis.</p> <p>The financial statements of foreign issuers must be prepared in accordance with any of the following options:</p> <ul style="list-style-type: none"> <li>• IFRS issued by IASB.</li> <li>• United States GAAP (USGAAP), plus additional footnotes explaining the principal differences between the accounting standards and methods used to prepare its financial statements and the IFRS.</li> <li>• Accounting principles applicable in the country of the Issuer, plus additional footnotes explaining the principal differences between the accounting principles used to prepare financial statements and IFRS and a reconciliation of the most important accounts to quantify the differences between the two accounting standards. (Issuers Rule, Article 79).</li> </ul>
Assessment	Fully Implemented
Comments	<p>The Commission requires public issuers to provide regular disclosure of financial results. Most of these reporting requirements are comprehensive, timely and meet or exceed international standards. The accounting and auditing standards applied are viewed as being of internationally acceptable quality. External auditors are subject to oversight by the Commission.</p>

	<p>Internationally, the general trend is to shorten the delivery time for public companies' financial statements. At 20 days, the current Mexican deadline for interim statements is much shorter than that in most major jurisdictions, but the deadline for audited annual financial statements (120 days) is longer; 90 days is more the norm and 75 days is becoming more common. Consideration should be given to requiring the audited annual financial statements to be published within 90 days of the year-end.</p> <p>In practice, the Commission may be able to persuade issuers to voluntarily undertake restatements of their financial statements that deviate from accepted accounting standards when faced with enforcement action as an alternative. But it would be better if the LMV were amended to give the Commission express powers to require issuers to restate their financial statements.</p> <p>Each of these observations has been taken into account under prior Principles (3, 9, 10, and 14) and so no additional downgrade has been applied here.</p>
<b>Principles for Collective Investment Schemes</b>	
<b>Principle 17.</b>	The regulatory system should set standards for the eligibility and the regulation of those who wish to market or operate a collective investment scheme.
Description	<p>The regulation of collective investment schemes offered to the public in Mexico (known as <i>sociedades de inversion</i> (SI)) is governed by the LMV, the <i>Ley de Sociedades de Inversion</i> (LSI) and the detailed rules set out in the SI Rules promulgated by the Commission.</p> <p>The Commission is empowered to supervise and regulate entities participating in the Mexican financial system, including SIs, and their operators and distributors in order to ensure stability, proper operation, and to maintain and promote the sound development of the system in protection of public interest (LCNBV, Article 2).</p> <p>The organization and operation of SIs requires prior authorization from the Commission. Four types of SIs are contemplated by the LSI, based on their permitted investments: equity, debt, venture capital and limited scope (LSI, Article 6). All must be incorporated as companies under the law. The authorization process requires applicants to file:</p> <ul style="list-style-type: none"> <li>• the proposed articles of association;</li> <li>• names and qualifications of founders and directors;</li> <li>• draft prospectus;</li> <li>• names of service providers to SI (asset management company(operator); distributor; valuator of SI's securities; rating agencies; price vendors for portfolio assets; depository and custodian of assets; auditor; administrator); and</li> <li>• manual of conduct of service providers and directors (LSI, Article 8).</li> </ul> <p>Before authorization is granted, a detailed review of the materials is performed, with a particular emphasis on the proposed prospectus.</p> <p>SIs are managed by entities licensed by the CNBV as <i>sociedades operadora de sociedades de inversion</i> or SI Operators) (LSI, Article 10) and sold to investors by firms authorized by the CNBV as SI distributors.</p> <p>The request to the Commission for authorization as an SI operator must be accompanied by the following:</p> <ul style="list-style-type: none"> <li>• articles of association;</li> <li>• list of shareholders, directors, principal officers and compliance officer;</li> <li>• share capital composition;</li> </ul>

- certification from the applicant of the technical skill, honesty, satisfactory credit record and the knowledge and experience of its principal directors and staff in financial or administrative areas (fit & proper); and
- a satisfactory general operating program, which describes the basis for its organization and internal control (LSI, Article 34).

During the due diligence process to authorize a new SI operator, the officers must establish their fit and proper qualifications for the roles they are to perform. Before the authorization is granted the Commission verifies the entities' technical resources through on-site inspections (LSI, Article 34).

SI operators must comply with a minimum paid-in capital requirement, which must be invested in the assets necessary to support its operation and in those shares representing the minimum paid in capital of the SI that they manage (SI Rules, Article 29). SI operator minimum capital is 1 million pesos if it is part of a financial conglomerate and 12 million pesos if it is independent. The minimum paid in capital for a new SI is 1 million pesos in permanent equity.

Persons who offer asset management services to SIs must be organized and authorized as SI operators, and sign a contract of services with the SI. The SI operator makes investment decisions on behalf of the SI (LSI, Article 39).

SI operators must designate a compliance officer who has specific responsibilities mandated by law; including establishing procedures to prevent conflicts of interest, protect confidential information, and ensure the firm and its employees comply with all legal requirements (LSI, Article 34). Additionally, the SI's Board of Directors has responsibilities regarding supervising the management and performance of the SI, including the design of investment and operating policies for the SI and to adopt the necessary measures to ensure the operations meet the requirements set out in the prospectus (LSI, Article 13).

Funds incorporated outside the country may not be authorized as SIs in Mexico. However, an SI may be established with the objective of investing in foreign funds using a 'fund-of-fund' structure. The assets of the Mexican fund may be held outside the country by a custodian that operates in a jurisdiction that is a member of the Technical Committee of IOSCO. Appropriate information sharing arrangements are ensured through the IOSCO MMOU and various bilateral MOUs that are in place.

The Commission has powers to investigate any act that may contravene the provisions of the LMV and the LSI (CNBV Law, Article 4). There is an extensive regime for sanctions under the LSI. Violations of the LSI or SI Rules may be punished with administrative fines imposed by the Commission. Fines vary by offense and range from a low of 100 days' wages to 50,000 days. (A "day's wage" refers to a minimum daily salary as specified by the government: currently just over 50 pesos.) Recurrence of the offense is punishable by a fine whose amount is equivalent to twice the original fine. These fines may be imposed not only on the firm, but also on its managers, officers, employees or agents who were responsible for the failure in compliance (LSI, Article 84). (See the comments under Principle 9 and 10 regarding the need for updating these maximums.) Unlicensed operation of a SI would attract a significant fine or imprisonment: minimum of 5 to a maximum of 15 years for performing acts reserved by the LSI to the SIs, SI operators or distributors without being appropriately licensed (LSI, Articles. 86 and 88).

The Commission, after a hearing, may revoke an SI's authorization if the SI:

- operates with less than the minimum capital required;
- violates the provisions forbidding foreign individuals from owning its fixed capital or performing functions of authority;

- breaches the portfolio composition requirements (allowed investment limits) after several warnings from the Commission;
- carries out transactions other than those allowed under the law;
- failed to ensure all transactions are recorded properly and promptly in its books;
- repeatedly fails to provide the information required by law; and
- is insolvent or begins a procedure of dissolution and liquidation (LSI, Article 82).

After a hearing, the Commission may revoke the authorization of an operator, distributor or valuator for repeated breaches of the law, failure to perform the services contracted for, providing the Commission with false information, carrying on operations that do not adhere to sound practices in the securities market or declaring bankruptcy (LSI, Article 83).

The Commission has powers to supervise service providers of SIs, like SI operators, distribution entities, and valutors (CNBV Law, Article 2, and LSI, Article 80). The Commission conducts examinations aimed at assessing the conduct of SI operators and also has powers to make inspection visits whenever it considers necessary. In addition, the *Asociación Mexicana de Intermediarios Bursátiles* (AMIB), which is recognized by the Commission as an SRO, is empowered to review its members' performance on a periodic basis, although this is not done in practice.

Since 2010, a new program has been instituted to bring a more strategic focus to the inspections of asset management services, both at the SI groups and the brokerage houses. The focus is compliance with conduct of business (know your client, suitability) and conflicts of interest requirements, the latter particularly of concern with the high level of concentration of ownership in the market among issuers and financial services providers. At the time of the assessment, six of these special examinations had been conducted and one enforcement action resulting in a sanction of more than 10 million pesos had been completed. Expansion of this program is constrained by a lack of resources. (See the data on inspections of SIs and their service providers set out in Principle 10.)

The SI, SI operator and SI distributors must provide the Commission with regular reports and financial information, such as performance, total assets, number of investors, investment portfolio composition, risk management indicators, etc. (SI Rules, Article 74). This reporting is extensive, timely and takes place daily (next business day), monthly (within 5 days of the end of the month), quarterly (within 10—30 calendar days) and annually (within 90 days), depending on the report. The Commission communicates with SI operators where breaches have been detected in the reports submitted.

The obligation to make prompt disclosure of material events applies to SIs and their service providers such as SI operators (Issuers Rules, Article 50). SIs and SI operators must disclose changes in the prospectus, management, organization and by-laws to both the Commission and investors.

By law, the SI operators and other services providers are responsible for keeping records of the SI's operations and performance (LSI, Article 32). Additionally, the SIs must record their portfolio transactions and other financial affairs according to accounting principles issued by the Commission. The SI's records must be available for inspection by the Commission at all times.

#### *Conflicts of interest*

The regulatory framework contains provisions intended to prevent conflicts of interest, such as a prohibition on buying assets from or selling assets to any subsidiary or affiliated entity of the SI operator (SI Rules, Article 4). Also, the risk management

	<p>function must be independent from the business units, in order to avoid conflicts of interest and ensure an adequate separation of responsibilities (SI Rules, Article 96).</p> <p>The LSI sets out the compliance officer's obligation to propose policies and guidelines needed to prevent conflicts of interest in general to the SI's Board of Directors for review and approval. (LSI, Article 34). Also, when the SI operator is a brokerage house, it must establish measures to prevent conflicts of interest as part of the broker's comprehensive internal control system (Securities Firms Rules, Article 113).</p> <p>SI operators must trade the SI's assets in accordance with the terms of the prospectus, looking for the best market conditions in the best interest of the SI (SI Rules, Article 6 Bis). While there is no mandatory rule, the usual practice is for the SI operator to have predetermined and fair criteria in place to allocate trades among its managed SIs.</p> <p>The LSI prohibits entities that provide ratings, valuations or price vendor services from acquiring shares of an SI to which they provide services (LSI, Article 52). Every service provider is required to adhere to the SI's manual of conduct, which would include conflict of interest rules. The Board of the SI must approve the manual and review the performance of the service providers annually.</p> <p><i>Delegation</i></p> <p>Delegation is permitted and the investor has full information regarding the company legally responsible for the delegated functions. The LSI requires the SI to appoint service providers to carry out specified functions for the SI: asset manager, distributor, valuator of the SI's securities, rating agency, price vendor for portfolio assets, depository and custodian of assets, auditor and administrator (LSI, Article 32). The prospectus of the SI is required to disclose information on the service providers, including any firm with delegated responsibilities (SI Rules, Annex 2 The prospectus' content).</p> <p>Services, other than asset management and valuation, can be subcontracted if the service contract permits, the prior consent of the SI in question is obtained and notice is filed with the Commission. When there is outsourcing, the outsourcing company remains responsible to the SI and its shareholders (LSI, Article 56). The Board of the SI must evaluate the performance of every service provider annually. The Board has the power to deny the renewal of the contract (LSI, Article 13). Also, the Commission has the authority to review service contracts and intervene where it deems appropriate.</p> <p>ETFs are not subject to the same regulatory framework that applies to SIs. ETFs are issued by private trusts (special purpose vehicles) and are listed on the stock exchange. They are treated like corporate issuers—see Principle 14.</p>
Assessment	Fully Implemented
Comments	<p>The process for incorporation of a company in Mexico is slow, thereby delaying and adding costs to the establishment of new SIs. The Commission is considering permitting alternative structures, such as trusts or segregated portfolio companies in an effort to sidestep this impediment. This project, which likely would require legislative changes in both corporate and securities laws, should be pursued.</p> <p>The new asset management examination program is a good initiative and should be expanded. The Commission's resources need to be enhanced to allow for more of these reviews to take place regularly.</p>
<b>Principle 18.</b>	The regulatory system should provide for rules governing the legal form and structure of collective investment schemes and the segregation and protection of client assets.
Description	<p><i>Legal Form/Investors' Rights</i></p> <p>The organization and operation of SIs requires prior authorization be granted by the Commission (LSI, Article 6), which has the power to supervise such entities (LSI, Article 80). The LSI establishes that an SI must be incorporated as a company. There</p>

are several requirements for obtaining the authorization of the Commission in order to sell shares to the public that are designed to ensure a fair and equitable treatment of investors, including corporate governance and disclosure requirements (LSI, Articles 12 and 20).

The SI's offering document must meet the prospectus requirements specified. All relevant information that contributes to decision-making by investors must be included, such as:

- general information about the SI;
- the detailed policy for the sale of shares;
- the form of negotiation and settlement for purchases and sales;
- detailed policies for investment, liquidity, selection and acquisition of assets, and, where appropriate, diversification; and
- risk disclosure (LSI, Article 9 and SI Rules, Annex 2 The prospectus' content).

No material changes to the SI or SI operator may take place without Commission approval. Changes to investor rights would require a modification to the prospectus, which must be approved by the Commission (LSI, Article 80). Also, as issuers, the SIs must fulfill material change disclosure obligations (to the market and the Commission) for the events that could affect the rights of its shareholders (Issuers Rules, Article 50).

With the prior agreement of its Board of Directors, an SI may request the Commission's permission to make changes to the prospectus. The SI must give notice to its investors, through the SI operator or distributors, of any proposed changes to the prospectus, stating where the shareholders can review the proposed changes and the deadline for comments (LSI, Article 10). In the case of amendments relating to the SI's policies on investment or purchase and sale of its own shares, the SI must give shareholders notice within the first five working days following the CNBV's authorization. For these types of amendments, the SI's shareholders have the right to sell their shares at the valuation price within 30 working days from the date on which notice of the changes has been given. After this period, the amendments to the prospectus are effective. (SI Rules, Article 11).

#### *Separation of assets/safekeeping*

The SI, its operators and distributors must have distinct accounting systems, in accordance with the accounting standards issued by the Commission (LSI, Article 76). The portfolio assets that are securities listed on the RNV must be deposited in a separate account to be maintained by the SI at the central securities depository. The same obligation applies to the shares representing the permanent capital of such SIs (SI Rules, Article 44).

Foreign investment assets are to be held in a central depository whenever possible. Investment assets that by their nature cannot be deposited in a securities depository (domestic or foreign) must be held as generally required by the Commission (LSI, Article 16). Foreign assets must be held with custodians (financial institutions or other legal entities) authorized to provide such services and supervised by a relevant regulator in an EU country or member country of the IOSCO Technical Committee. Additional reporting to the Commission is required for these assets (SI Rules, Article 44).

SIs are obliged to keep complete records and establish a reporting system for asset management, including the disposition of their own shares. The books and records of the SI must be available to the Commission at all times (LSI, Article 78). Additionally, the Commission receives weekly information regarding the assets traded and the total number of SI shares redeemed and sold in the previous week.

	<p>The annual financial statements of the SI must be audited by an independent external auditor who is appointed directly by the Board of the SI (LSI, Article 77). The external auditors, as part of their annual audit, must review the SI's performance, including the valuation of the SI's shares and its portfolio assets. The Commission periodically verifies SI assets by comparing the central depository's records to the portfolio records of the SI.</p> <p>The Commission has never had to force the winding-up of an SI. An SI may come to the Commission for permission to be wound up and in this case the SI usually has already redeemed all publicly held shares of the SI. This was the case with some Stanford-related funds. The bankruptcy of an SI would be subject to the same rules as the bankruptcy of any other company. However, the portfolio assets of the company held at the central depository would be treated as belonging to the investors, in priority to creditors of the SI.</p>
Assessment	Fully Implemented
Comments	
<b>Principle 19.</b>	Regulation should require disclosure, as set forth under the principles for issuers, which is necessary to evaluate the suitability of a collective investment scheme for a particular investor and the value of the investor's interest in the scheme.
Description	<p>SIs are subject to the general materiality principle that applies to all public issuers: the prospectus must contain all relevant information necessary for investors to make informed investment decisions. The valuation methodology used by the valuation company engaged by the SI is not disclosed in this document but is generally known in the marketplace. Disclosures about returns on investments are reported through the monthly account statements to the clients. The regulatory framework includes a Key Information Document—a kind of simplified prospectus—that contains the most relevant information for making investment decisions. This document highlights the objectives and investment regime of the SI, the risks associated with the invested assets, past performance, as well as fees and charges to customers (SI Rules, Article 10 and SI Rules, Annex 2—Prospectus' content).</p> <p>The regulatory framework specifically requires that the offering documents include the full range of information required under Key Question 3 of the Assessment Methodology for this Principle, other than as noted above re: valuation of the fund's securities. As noted under Principle 17, the SI is required to appoint both a valuation company to calculate its net asset value and a price vendor to supply prices for the assets in its portfolio. These service providers must be identified in the prospectus. The methodology used by these service providers does not have to be disclosed, but the Commission has rules governing these activities (see Principle 20, below).</p> <p>The Commission has the power to deny the approval of a SI prospectus or make any kind of observations when the document does not appear to comply with the legal framework. (LSI, Article 9)</p> <p>The advertising by SIs, operators and distributors is subject to the guidelines and criteria established in the SI Rules. Advertisements do not require prior Commission approval, but the company concerned is strictly responsible if the information results in contravention of the provisions of the LSI or SI Rules (SI Rules, Article 90).</p> <p>The SI, with the agreement of its Board of Directors, must obtain Commission permission to make changes to the prospectus (SI Rules, Article 11), other than changes to information that, by its nature, should be updated continuously. The SI Rules set out the information that may be updated without requiring prior permission, such as financial information. Additionally, the SI is obliged to disclose material events in accordance with the rules applicable to issuers (SI Rules, Annex I –Prospectus content). In practice, prospectuses are updated no less than annually; the Key Information Document is required to be updated monthly.</p>

	<p><i>Periodic reporting</i></p> <p>The SI Rules specify several periodic reporting requirements, including quarterly and annual financial statements for SIs, SIs operators and distributors. The annual financial statements must be audited by an independent external auditor appointed directly by the relevant entity's Board of Directors. The auditors must provide the Commission with reports and other evidence in to support their opinions and conclusions (LSI, Article 77).</p> <p>The consolidated financial statements for March, June and September should be submitted for approval by the management to the Boards of the companies within the month immediately following the end of the period, accompanied with the necessary supporting documentation, so that such bodies have sufficient information to understand and evaluate the operations of major importance, determining fundamental changes during the current year. In the case of the annual financial statements, these must be submitted to the Board within sixty calendar days following the closing of the respective year (SI Rules, Article 69).</p> <p>SIs, SI operators, and SI distribution companies must publish (in print or electronic media), their quarterly statements for March, June and September each year in the month immediately following the closing date. Audited annual financial statements must be published by these persons, along with the audit report, within 90 days after the year end. Publication may be carried out using the SI's own website (SI Rules Article 71).</p> <p>Disclosures about returns on investments are reported through the monthly account statements of the clients.</p>
Assessment	Fully Implemented
Comments	
<b>Principle 20.</b>	Regulation should ensure that there is a proper and disclosed basis for asset valuation and the pricing and the redemption of units in a collective investment scheme.
Description	<p><i>Asset valuation</i></p> <p>An SI must hire a service provider to value its shares and these entities must be authorized by the Commission as valuation entities or SI operators. The valuation must conform to provisions of the SI Rules issued by the Commission. The Commission does not approve the valuation methodology. There are only two authorized SI valuers. In the case of certain types of SIs (capital and limited purpose SIs), the price of their shares may be determined by valuation entities or valuation committees appointed by the SI's Board of Directors (LSI, Article 44)</p> <p>SIs that invest in equity and debt instruments must value their invested assets daily, using current prices for valuation provided by price vendors that are authorized by the CNBV (SI Rules, Article 39). These valuations must be accounted for using the accounting standards set by the Commission for financial institutions (see the discussion under Principle 16). The CNBV is of the view that these rules are in line with IFRS asset valuation rules (SI Rules, Annex 4—Criteria for accounting for SIs). Industry members expressed some doubt regarding IFRS-equivalence of the valuation methods actually applied to illiquid securities by the price vendors. The prices of assets, as determined by the price vendors, are provided to the Commission daily.</p> <p>Both the price vendor and valuation company must be independent of the SI. The legal regime sets out detailed situations where two parties are seen not to be independent.</p> <p>When market prices are not available, price vendors are required to determine fair valuation of assets in accordance with their methodologies. Additionally, SI operators and equity and debt SIs must consider the fair value of the SI's investment assets and update the corresponding price valuation (SI Rules, Article 39). All prices are sent to the Commission by the price vendors and these are tested for accuracy. Any discrepancies are followed up with the service providers.</p>

	<p>The valuation prices of the shares representing the capital of the SI and transactions with respect to these shares must be certified monthly. The certificate must be signed by the responsible managers of the SI, SI operator and the independent valuator. The external auditors, as part of their annual audit, must review the SI's performance, including the valuation of the SI's shares. The Commission periodically verifies SI assets by comparing the central depository's records to the portfolio records of the SI.</p> <p><i>Pricing and Redemption of Interests</i></p> <p>There are specific regulatory requirements regarding the pricing of interests in an SI on sale or redemption. The terms must be set out in the prospectus. The price will be that determined by the authorized independent valuator of the SI (SI Rules, Article 12). The Commission has authority to enforce these requirements and has taken action against a valuation company for its accounting practices.</p> <p>SIs are listed on the BMV and their prices are made public on the exchange daily via the operator carrying out a trade at the net asset value on the exchange. Also, SI operators and distributors are obliged to disclose information about the SIs they manage or distribute, usually on the SI and/or service providers' websites (LSI, Article 45).</p> <p>Price vendors must resolve objections raised by an SI regarding prices and delivery of information, when in opinion of the SI there may be an incorrect application of the valuation methodology or models used for pricing or that they do not adequately represent the market. The SI must inform the Commission at the same time as it files the objection with the price vendor. When a price is updated due to valuation changes, price vendors must communicate the amendment to all its users and to the Commission (LSI, Article 50). Investors harmed by pricing errors must be compensated by the party responsible for the error.</p> <p>The regulatory framework addresses the circumstances in which there may be suspension or deferral of routine valuation and pricing or of regular redemption, particularly in cases of market disruptions or disorderly conditions (LSI, Article 80). The prospectus must disclose when this may take place. When there is pressure on redemptions and the SI lacks sufficient liquidity to meet redemption request, the framework permits the SI to continue to redeem shares but at a discount (i.e., 90 percent of net asset value). The discount remains in the fund. If this is to be invoked, there must be public disclosure of its application and the method used to calculate the discount. The Commission checks on these arrangements to ensure the discounts are applied consistently.</p> <p>The SI Rules require that if a SI temporarily does not meet its investment program/restrictions or suspends negotiation of its shares, it must make disclosure to the public and to the Commission no later than the next working day. (SI Rules, Article 7)</p> <p>The Commission has the discretion to order the temporary suspension of share placements due to disorderly market conditions, where there have been transactions that do not conform to sound market uses and practices or when required by the composition of the portfolio of investment assets (LSI, Article 80). The Commission has no power to suspend redemptions or order redemptions resume at an SI.</p>
Assessment	Broadly Implemented.
Comments	The fund's securities and its assets are subject to valuation by third party service providers (valuation companies and price vendors) that are required to be independent of the fund and its operator. These service providers are also authorized and supervised by the CNBV. Continuous disclosure of information and prices is provided through fund or distributor websites. In addition, prices must be reported daily through the BMV's system.

	<p>The BMV only provides the prices of assets trade on that exchange.</p> <p>The CNBV is of the view that the valuation rules applied to illiquid assets of SIs are in line with IFRS asset valuation rules. Industry members expressed some doubt. The Commission should review the methodologies used by valuation companies and price vendors to ensure appropriate practices are being followed for illiquid assets and that the methodologies are consistent across the service providers.</p> <p>The LSI should be amended to ensure the Commission has full power to intervene in the sales and redemption process in appropriate circumstances in order to protect investors or the market as a whole. It has the power to suspend new placements. It should also have the power to order redemptions cease or resume at an SI, as the Assessment Methodology requires.</p>
<b>Principles for Market Intermediaries</b>	
<b>Principle 21.</b>	Regulation should provide for minimum entry standards for market intermediaries.
Description	<p><i>Initial licensing and authority</i></p> <p>Market intermediaries include brokerage firms, credit institutions, SI operators, pension fund managers and SI distributors (whether independent companies or financial institutions acting as distributors). Brokerage firms must comply with the provisions of the LMV; the other entities must comply with the specific legislation governing their respective activities, such as the LSI (LMV, Article 113). Authorization of the Commission is required to carry out any of these activities. Certain of the rules that govern market activities are written to apply to all types of institutions supervised by the Commission carrying on that function. For example, the rule setting standards for the formulation and dissemination of investment recommendations applies generally, regardless of the type of intermediary. However, some securities market rules presently apply only to brokerage houses. The Commission is working to ensure comparability of regulation that applies to each of these entities, particularly across the expected business conduct that applies with respect to their clients.</p> <p>There are inter-dealer brokers (<i>Sociedades que administran sistemas para facilitar operaciones con valores</i>) operating in Mexico. These entities are authorized by the Commission under the LMV to provide services and facilities for OTC trading in securities—mostly debt and derivatives—only to credit institutions and brokerage houses (LMV, Article 253ff). They may also provide price information to anyone on the instruments that trade through their facilities. They do not deal in listed equity securities and are not registered as intermediaries under the LMV. Interdealer brokers must adhere to limited regulatory standards focused on system capacity rather than capital adequacy. They are prohibited from acting as counterparties and so do not function as risk principals in trading (LMV, Article 258).</p> <p>The LMV and the Securities Firms Rules set out clear minimum standards that all applicants for licensing as securities firms must meet before a license is granted. Prior to starting its operations, a securities firm must demonstrate to the CNBV that:</p> <ul style="list-style-type: none"> <li>• it has the minimum capital required by law; minimum capital is based on the kind of activities and services that the firm intends to provide, varies based on the perceived risk of these activities and runs from US\$1.147 million (or 3 million UDI) to US\$4.778 million (12.5 million UDI);</li> <li>• its advisers, CEO, senior executives, personnel who will deal with the public and trading operators comply with all the requirements established by law and by regulatory provisions (that is, are fit and proper); and</li> </ul>

- it has the necessary infrastructure, organization and internal control to operate, and that these comply with regulation (LMV Article 116; Securities Firms Rule, Articles. 1 Bis and 10).

The CNBV may grant an authorization to an intermediary only if the applicant meets all the requirements established by law; if the applicant does not comply fully, the authorization is refused (LMV Article 114).

Securities brokerage houses are subject to a two-stage authorization process. The initial step is a detailed review of the application against the minimum requirements. Commission staff in both the authorization and legal areas perform this review. The second stage takes place prior to granting authorization to begin business. A detailed review of all required manuals is performed, as is an on-site examination that covers all aspects of the operations of the firm, including trading and settlement infrastructure, internal controls, information technology (IT) and risk management systems, etc. A specialist group from the Commission reviews the IT and systems.

Similarly detailed reviews and on-site processes apply to authorizations of credit institutions. Other securities market intermediaries are subject to a complete review, but less intensive on-site process, prior to authorization.

The BoM grants authority to authorized banks and brokerage houses on a case-by-case basis to carry on the derivatives business (BoM Circular 4-2006). To trade on MexDer, the brokerage firm must fulfill its membership requirements, including meeting the additional capital requirements specified in the MexDer Mandatory Rules.

The CNBV has the authority to order the suspension of activities or to limit operations of securities firms that fail to meet relevant requirements on an ongoing basis (LMV Articles 137 and 138). Also, the CNBV is entitled to revoke a securities firm's license if specified conditions are met, such as providing false, inaccurate or incomplete information or suffering losses that reduce its capital below the minimum required (LMV Article 153).

Potential members of the Board of Directors, CEO and principal executive officers of a securities firm must submit their curriculum vitae and must demonstrate that they comply with all the legal and administrative requirements for the position in question (Securities Firm Rules, Article 1 Bis). AMIB manages the initial process of certification of fit and proper for these persons.

#### *Ongoing requirements*

Securities firms are obliged to get the permission of the CNBV for any change in the information set out in their licensing application, including an expansion in the firm's securities activities. The changes must be published in the Official Gazette of the Federation if they include amendments to its articles of incorporation; changes to the activities and services that may be provided by the entity; mergers and spin offs; or changes in control of the firm (LMV, Article 115). Capital increases do not require prior approval from the regulator, but information on any new investor must be provided in advance and the Commission may object if an investor is not fit and proper. The Commission has full information on all beneficial owners of the shares of a securities firm. Ownership changes are subject to review and approval.

A list of authorized intermediaries is posted on the Commission's website and appears in the Official Gazette. Customer service offices of securities firms cannot operate without legal representatives authorized by the CNBV. A list of authorized agents must be displayed in these offices in a spot visible to the public. This list is also available at the website of the CNBV (Securities Firms Rule, Article 3).

The CNBV verifies that authorized intermediaries comply with all applicable requirements via its inspection program. All brokers are inspected on a regular basis, with a cycle of 12—36 months. The frequency of the review is based on an assessment

	<p>of the risk of the firm. The risk assessment turns on several factors: the businesses the firm is in, the results of past visits, compliance issues (if any) revealed in its regular reporting, etc. Risky firms are reviewed at least yearly. The level of detail in the examination varies. The first examination of a new firm is a comprehensive one. Thereafter, the reviews may be more focused on areas of higher concern. Brokers and clearing members of MexDer are subject to additional reporting and on-site reviews by the exchange.</p> <p>The CNBV often conducts special inspections. These may be reviews of a particular firm (where it has started to carry on new activities or analysis of the firm's reporting indicates a matter of particular concern) or across a number of firms, such as to test the implementation of new rules.</p> <p>The CNBV has the power to take action, including issuing preventive and corrective measures, if intermediaries do not meet legal requirements or do not fully comply with regulation (LMV, Article 135).</p> <p><i>Investment advisers</i></p> <p>Investment advisers are persons who carry on the business of providing advice with respect to securities. They give investment advice and may only forward trading instructions to authorized brokers for execution by those brokers if the contract with their clients expressly permits this. They may issue investment recommendations and may make decisions on behalf of clients on a discretionary basis if so authorized by the client contract. Investment advisers are not intermediaries and are not authorized or directly supervised by the CNBV (LMV, Article 225).</p> <p>Investor advisers are not subject to capital or operational requirements. Investment advisers are not permitted to keep custody of client assets, offer guaranteed returns or receive fees from intermediaries for referrals or for promotion of any products. They are not subject to regulations on record-keeping requirements. They are not required to be members of any SRO.</p> <p>They are required to:</p> <ul style="list-style-type: none"> <li>• know their clients and make suitable investment recommendations and decisions;</li> <li>• obey the rules issued any SRO of which they are members;</li> <li>• obtain certification of their fit and proper status from a recognized SRO (AMIB) in connection with the services they provide to the public, or use the services of individuals who have such certification; and</li> <li>• inform their customers that they are not subject to supervision by the Commission and provide specific disclosure of any conflicts of interest (LMV, Article 226).</li> </ul> <p>The Commission has an initiative under way to revise the law to give it express supervisory authority over these firms. The rules that will govern the activity will focus on sales practices to ensure that the clients' interests are protected, particularly from conflicts of interest.</p>
Assessment	Fully Implemented
Comments	<p>The framework for licensing and on-going requirements for market intermediaries is in place. Applicants are subject to detailed reviews before being authorized. Brokers must undergo comprehensive on-site inspections of all systems before they are permitted to begin business.</p> <p>The ongoing project to ensure comparability of regulation that applies to all types of market intermediaries when carrying on similar activities, particularly across the expected business conduct that applies with respect to their clients, should be completed as soon as possible.</p>

	<p>However, the provisions in the LMV governing investment advisers are confusing and may create a potential gap in regulation. It imposes limitations on the business activities that these entities may carry on but then expressly states that investment advisers are not subject to supervision by the Commission, raising issues with its authority to ensure these firms are complying with the restrictions. On the other hand, the Commission has wide-ranging authority to investigate any suspected breaches of the law, which would include ensuring these limitations have been obeyed. The Commission's initiative to revise the law to give it express supervisory authority over these firms should be encouraged.</p>
<b>Principle 22.</b>	<p>There should be initial and ongoing capital and other prudential requirements for market intermediaries that reflect the risks that the intermediaries undertake.</p>
Description	<p>Commercial banks and securities firms require a minimum initial share capital of approximately US\$34.81 million and US\$4.84 million, respectively. Ongoing minimum capital requirements apply to all commercial banks and securities firms. The minimum capital adequacy standards for banks and securities firms are based on the Basel II Capital Accord and require institutions to maintain capital of 8 percent of risk-adjusted assets.</p> <p>The capital adequacy requirements for commercial banks and securities firms only address market, credit and operational risks expressly (Securities Firms Rules, Article 147). No separate amount for liquidity, legal and reputational risks are included, although risk management systems at the firms are required to address these risks. Further, the relevant rules include a separate calculation of liquidity. If this indicates the firm's liquidity is declining to a level of concern, the regulator may order a firm to restrict its business or add more capital. Commission staff was of the view that the capital formula, coupled with this additional liquidity measure, provided an adequate buffer to address the significant risks a firm would face.</p> <p>Capital adequacy requirements are set out in detail in the Securities Firms Rules and vary based on the risk of the position held or exposure undertaken. Larger positions and those considered to be higher risk attract the need for more capital. The capital required for market, credit and operational risk are calculated separately and the ultimate capital requirement is a function of the sum of these requirements. The formula for brokers uses the building block approach for market risk, the basic method for calculating operational risk and the simplified approach for credit risk calculations.</p> <p>The Commission has authority to increase the amount of capital that an individual firm must hold, taking into account factors including the composition of its assets, efficiency of its systems of internal control, its exposure and overall risk management (Securities Firms Rules, Article 169).</p> <p>The CNBV expects that these capital standards allow the absorption of some losses prior to the default of the firm. The ability of these capital standards to allow the firm to be wound down in a relatively short period without loss to its customers depends on the seriousness of the default of the firm and on the applicable resolution scheme. In normal circumstances, this process is expected to work adequately to protect investors. As client assets must be held at the central depository in an account separate from that of the firm, these assets would be protected. As in most jurisdictions, there are some risks to client funds in the hands of intermediaries prior to delivery to the central depository or clearinghouses.</p> <p>Market intermediaries subject to capital adequacy requirements must submit detailed reports showing their capital positions to the Commission. Reports must be submitted on a monthly basis within 30 days after the month end. The CNBV reviews this information to make sure that capital levels fulfill legal requirements. The CNBV may request additional information and may take action if needed to implement preventive and corrective measures if there are material deficiencies.</p>

Upon receipt of the monthly filings, the Commission calculates each firm's 'index of capital consumption', which is the ratio of the sum of the required capital for credit risk, market risk and operational risk to the total amount of regulatory capital the firm holds. It then places the firm on one of four categories and gives notice of that category to the firm. A firm that has an index of 80 percent or less is considered to have adequate capital. If it has an index of more than 80 percent it is required to take the preventative and corrective actions specified in the Securities Firms Rules and Commission notice. The actions the firm is required to take get more severe as the index increases.

For example, when a firm's index lies between 80 percent and 100 percent it must report the matter to its Board and file a report with the Board and the Commission as to the reasons for its financial situation. If the index exceeds 100 percent it must submit a capital restoration or risk reduction plan to the Commission for approval within a specified period and will be required to suspend payment of dividends to shareholders (Securities Firms Rules, Article 204 Bis to Bis15).

The Commission may calculate the index of capital consumption of a firm at any time if it has reason to believe that the firm is taking risks that are higher than those that shown on the previous month end figures (Securities Firms Rules, Article 204 Bis). Further, the Commission has a very wide range of actions it may take to intervene in a firm with an index that is above 100 percent of the required levels (Securities Firms Rules, Article 204 Bis 13). For example, the CNBV has powers to impose restrictions on business activities of commercial banks and securities firms (LMV, Articles 135–136; Banking Law, Article 134 and 134-Bis).

All commercial banks and securities firms must be ready, at any time, to prove their capital adequacy when the financial authorities require them to do so. The CNBV may require firms to carry out a capital adequacy calculation within the time-limit and in the format set out by the CNBV. Further, the Risk Committee of a brokerage house must ensure at all times that all staff involved in risk-taking for the firm have knowledge of the overall and specific limits for discretionary risks. However, there is no express obligation on securities firms to ensure that their capital is adequate at all times, nor is there an obligation to inform the CNBV immediately if the firm becomes aware of a capital deficiency.

The MexDer Mandatory Rules stipulate additional minimum equity requirements for clearing members of the greater of 2.5 to 5 million UDI or 4 percent or 8 percent of the sum of the minimum initial contribution that the member maintains at the clearing house for each open contract (amounts depend on whether member is acting only for related parties or third party clients). The minimum equity amounts must be held in cash or short-term government securities. Brokers must have minimum capital of 100 thousand to 1 million UDI held in cash or cash equivalents. In both cases, the firm must notify the clearing house (Asigna) or the exchange within one day of any capital deficiency. In addition, Asigna is responsible for monitoring the capital of all clearing members continuously.

Intermediaries must produce and publish annual audited financial statements within 60 days after their year end. The audit must be conducted by an independent and qualified auditor. Firms are required to disclose to the public their financial statements, including their capital structure, the level of capital adequacy with respect to the legal requirements and the amount of their risk assets. They also must obtain and disclose credit ratings from two authorized credit rating agencies. This information is also made available to the public on the Commission's website (Securities Firms Rules, Article 169 Bis).

The capital requirements include all domestic operations, transactions carried out by agencies and branches located abroad, as well as transactions with licensed and unlicensed affiliates. It also covers off-balance sheet risks undertaken by any of these

	entities (Securities Firms Rules, Article 167). Consolidated supervision is applied by the CNBV to all financial firms authorized by the Commission.
Assessment	Partially Implemented
Comments	<p>There are initial and ongoing minimum capital requirements in place for market intermediaries. The capital requirements for brokerage houses are risk based and expressly address market, credit and operational risk. Contrary to what is stated in the Assessment Methodology, there are no specific capital provisions with respect to liquidity, legal or reputational risks. Liquidity risks are to be addressed via Basel III. The Commission should review the current capital formula ensure that the amounts provided are sufficient to address the full range of liquidity, legal and reputational risks to which the firms may be exposed. Reputational risk may be of significant concern in a market such as Mexico's given the concentration in the market and prevalence of financial conglomerates.</p> <p>The Assessment Methodology for this Principle requires a jurisdiction to have capital reporting requirements to the regulator or SRO that provide sufficient detail often enough and soon enough to reveal a significant deterioration in the capital adequacy position of market intermediaries. Further, the Assessment Methodology for Principle 24 expects that there are early warning systems or other mechanisms in place to give the regulator prompt notice of a potential default by a market intermediary in sufficient time to address the problem and to take corrective actions</p> <p>The CNBV reporting requirements provide extensive detail on capital, but on a 30-day delay from month end. While a firm has to be able to calculate its capital at any time and the Commission may require it to do so, there is no express obligation on securities firms to ensure that their capital is adequate at all times, nor (other than for MexDer participants) is there an obligation to inform the regulator immediately if the firm becomes aware of a capital deficiency. In a worst case scenario, this would allow the firm to be capital deficient for about 60 days before the CNBV would have any notice from the firm of there being a problem.</p> <p>The Securities Firms Rules should be amended to require firms to ensure their capital is adequate at all times, calculate it as often as necessary to ensure compliance with this requirement and report immediately to the Commission if there is any deficiency. Best practice would suggest that the capital level triggering immediate reporting should be set somewhat above the minimum capital required to give the Commission time to take appropriate action. Given the existing capital regime that requires corrective action when the index of required capital to regulatory capital rises above 80 percent, it might be appropriate to use this as a threshold for immediate reporting.</p>
<b>Principle 23.</b>	Market intermediaries should be required to comply with standards for internal organization and operational conduct that aim to protect the interests of clients, ensure proper management of risk, and under which management of the intermediary accepts primary responsibility for these matters.
Description	The management of a securities firm is entrusted to a Board of Directors and a chief executive officer. Persons who act as Board members, the CEO and senior executives must be fit and proper (LMV, Articles 122, 124, 125, 128 and 129). Before starting their operations, securities firms must demonstrate that they have an adequate infrastructure and internal control system (LMV, Article 116). The Securities Firms Rules establish a whole framework for internal control and operational risk management. The Commission tests these systems during inspections. The Board of Directors must approve codes of conduct and ethics for the firm and promote their dissemination and implementation in coordination with senior management (Securities Firms Rules, Article 106).

The internal audit function of the firm must conduct extensive annual reviews of the firm's risk management and controls systems covering specified areas. The results of these audits must be submitted no later than February of each year to the Board of Directors, the risk management committee and the CEO of the securities firm, and must be filed with the CNBV within the first ten days of March of each year (Securities Firms Rules, Article 132).

See the comments under Principle 22 on capital reporting. In addition, firms file extensive information and reports with the CNBV on their day-to-day activities. For example, firms file daily reports with the Commission setting out details on each trade executed, including price, amount and the beneficial owner of the account.

#### *Customer protection*

CONDUSEF is the consumer protection agency and it is its responsibility to receive and respond to investor complains, not the Commission. CONDUSEF requires Mexican financial institutions, including securities firms, to have specialized units dedicated to responding to inquiries and complaints from clients (*Ley de Proteccion y Defensa al Usuario de Servicios Financieros*, Article 50 Bis). The general consensus of market participants is that CONDUSEF is reasonably capable of fulfilling its responsibilities in enhancing financial literacy, but it lacks the resources and powers to function effectively as a consumer protection authority. For example, it has no power to require firms to compensate their clients for harm caused.

Securities firms must keep clients' securities in an authorized securities depository whenever possible. If the firm holds assets that by their nature cannot be held at a depository, these must be held at a deposit institution or other type of institution determined by the Commission. These institutions are to be independent of the securities firms. (LMV, Article 182). Also, securities firms may not hold client assets for any purpose other than those contracted by it (LMV, Article 196).

Additionally, securities firms must establish internal controls in order to ensure that the assets of customers are provided legal, accounting and physical separation from the firm's own resources (Securities Firms Rules, Article 204, Bis 12).

The brokerage firms are responsible to their clients for acts performed by their directors, officers, agents and employees in fulfilling their duties, without prejudice to any civil or criminal liability that they otherwise incur (LMV Article 198).

Intermediaries are required to have guidelines and policies to identify and know their customers and to determine the customers' investment objectives. The securities firms must have customer information that allows them to classify the clients according to their investment profiles for suitability purposes (Securities Firms Rules, Article 61). Know your client and suitability of trading also applies at the firm level for derivatives trading. Brokerage firms must preserve original books, records and documents related to operations and services (Securities Firms Rules, Article 185), and must ensure the proper management and control of confidential information (Securities firms, Article 186).

The terms set out in a "securities investment contract" govern the transactions performed by securities firms for their customers. Through this contract, the client mandates the securities firm to deal on the client's behalf (LMV, Article 199).

Securities firms must provide their clients with:

- all the information necessary to make informed investment decisions, taking into account the defined investment profiles, in accordance with the rules issued by the CNBV (LMV, Article 190); and

- a statement of account on a monthly basis. Such statement must include disaggregated data about the relevant contracts and securities transactions, as well as clear information about the fees charged for the activities and services provided (LMV, Article 191).

#### *Internal Controls*

The Securities Firms Rules establish a whole framework for internal control and operational risk management that securities firm must have in place.

The firm must have an Audit Committee of the Board, whose chairman must be an independent member. The Audit Committee has the responsibility to oversee the compliance of the internal control system, as well as to verify and evaluate its performance (Securities Firms Rules, Article 108). The Board of Directors must review, at least annually, the objectives, guidelines and internal control policies of the firm, and must evaluate the audit committee's oversight of same (Securities Firms Rules, Article 106).

Also, the internal control system of a securities firm must include a person who acts as "Commissioner". The duties of a firm's Commissioner must include evaluating the performance, observance, adequacy and fairness of the internal controls system. The Commission must have full access to all information necessary to carry out this task and must examine the securities firms' trade documentation, registration and any supporting evidence as necessary (Securities Firms Rules, Article 107).

The firm's risk management processes must clearly define different roles, activities and responsibilities for comprehensive risk management across the firm (Securities Firms Rules, Article 123). There must also be guidelines to ensure that the organizational structure of the firm has distributed functions appropriately to avoid potential conflicts of interest between the various business units and ensure the independence of the internal audit department (Securities Firms Rules, Article 106). Remuneration structures must support prudent risk management (Securities Firms Rules, Article 169 Bis). As noted, the internal audit function must review the operation of the risk management and control systems annually and report to the Board and the CNBV on the results of that audit.

Securities firms must maintain adequate and reliable books and records. Securities firms' trading records and accounting books must meet the detailed requirements established by regulation. Also, all the information must be accessible to the internal and external auditors and the CNBV (Securities Firms Rules, Article 110).

Securities firms must:

- provide timely and adequate disclosure of information, especially material information, both to their clients and the market (LMV, Article 190); and
- safeguard client's assets (LMV, Article 182).

All securities firms must have a designated compliance officer who is responsible for undertaking activities to ensure the firm complies with relevant legal and regulatory requirements. The compliance officer's duties include the design, establishment and implementation of measures and controls that facilitate compliance with internal and external regulations (Securities Firms Rules, Article 115).

The setting of standards for professional conduct is primarily the responsibility of SROs. The SRO Code of Professional Ethics of the Mexican Securities Industry (that has been adopted by AMIB, Asigna, BMV, Indeval and MexDer) includes guidance on acting in compliance with the law, acting in the best interests of clients, avoiding conflicts of interest, prompt and complete disclosure of information and maintaining confidentiality of information received in the course of business. In addition, the LMV requires that securities firms have a conduct code that is approved by the Commission as part of the authorization process (LMV, Article 228).

	<p>The overall rules on conflict of interest are fairly simplistic. The Commission has the authority to act if the firm engages in activities that are a conflict of interest if that conflict risks harm to the client. There are a few rules that require conflicts to be disclosed and the consent of the client obtained, such as for purchase of a new offering of securities issued by a related party of the brokerage house selling the instruments. Banks and security firms that produce analyst reports are subject to internal control regulations that must include detailed provisions to address conflicts of interest. The analysts themselves and firms are subject to several prohibitions and restrictions on trading activities, financial interests and business relationships (Analyst Rule, Articles 3 and 5). A project is underway to develop a more complete regime to address conflicts of interest that would classify types of conflicts/transaction and apply the appropriate requirement—from an absolute prohibition on the transaction to additional mandated disclosure to permission subject to protections like the trade being carried out at a market price.</p>
Assessment	Broadly Implemented
Comments	<p>Securities intermediaries are required to have extensive systems of risk management and internal controls in place and these must be reviewed annually. Client assets are suitably segregated in identified accounts at central depositories. Firms are required to know their clients and make suitable recommendations for those clients, whether the client is trading in SIs, other securities or derivatives.</p> <p>Given the high degree of concentration in the Mexican markets—from intermediaries to banks to issuers—good conflict of interest rules are of particular concern. The current regime needs significant enhancements to provide appropriate safeguards for clients. The CNBV's project to develop a more comprehensive regulatory regime should be completed and the appropriate rule changes put in place as soon as possible. These rules should apply to all market participants dealing with clients on securities or derivatives, whether the firm conducting the activity is a bank brokerage house or other regulated entity, such as an SI operator.</p> <p>Also, the conduct of business rules described above presently are written to apply to securities firms only, not banks when carrying on similar activities. The projects to develop a more comprehensive regulatory regime for conflicts of interest and conduct of business should be completed and the appropriate rule changes put in place as soon as possible. These rules should apply to all market participants in dealing with clients on securities or derivatives, whether the firm conducting the activity is a bank, brokerage house or other market intermediary.</p>
<b>Principle 24.</b>	There should be a procedure for dealing with the failure of a market intermediary in order to minimize damage and loss to investors and to contain systemic risk.
Description	<p>There is no official written plan in place to address the failure of a securities firm. Staff expressed the view that the regime set out in the law and regulations would be followed.</p> <p>The LMV empowers the CNBV to dictate preventive and corrective measures for securities firms that fall below the required levels of capital, including: the suspension of the payment of dividends, submission of a plan of capital restoration, revision of staff compensation policies, deferral of the payment of principal of subordinated debt obligations, or prohibition on performing transactions that would require additional capital (LMV, Articles 135 and 136). (See also the description under Principle 22 of the calculation of the index of capital consumption and actions taken in response to an index that rises above 80 percent.)</p> <p>When in the CNBV's opinion of the CNBV, a securities firm shows irregularities that affect its stability, solvency or liquidity and jeopardize the interests of its clients or creditors, the CNBV's chairman may propose to the Governing Board, that the</p>

	<p>Commission intervene and designate a person to take charge of the administration of the firm (LMV, Article 141). In a bankruptcy, the SHCP and the Commission may appoint the liquidator/trustee in bankruptcy.</p> <p>When a securities firm requests the revocation of its authorization to enter into a voluntary default process, the CNBV must publish the declaration of revocation and it must be recorded in the public commercial register (LMV, Article 155). The Commission also has the authority to require the firm to update its risk profile that it is required to post on its public website.</p> <p>No intermediary has failed since the widespread problems in the jurisdiction in the 1990s.</p> <p>See the discussion below under Principle 29 on the operations of the central counterparties on a default by a securities firm on the organized markets.</p>
Assessment	Broadly Implemented
Comments	<p>This principle was rated as broadly implemented because there are areas where the expectations of the Assessment Methodology are not fulfilled in their entirety.</p> <ul style="list-style-type: none"> <li>• The law and rules set out the actions that the Commission may take if a firm's capital position is weakening, but there is no formal plan in place to deal with an insolvency. Every insolvency poses different challenges and it is impossible for any written plan to encompass the contingencies that might arise. However, a written plan, even at a high degree of generality, may help to ensure all concerned know what steps must be taken to protect investors and so such a plan should be in place at the Commission.</li> <li>• There are detailed measures set out in the Securities Firms Rules to address an intermediary's deteriorating financial position that are triggered once the Commission receives the intermediary's monthly capital report. These corrective measures go into effect while the firm's capital is still above the minimum required. However, see the comments under Principle 22 on the gaps in the capital reporting system with respect to providing prompt notice of such deterioration between reporting periods.</li> <li>• As in many jurisdictions, the bankruptcy of a market intermediary is governed by the same legislation that governs any other bankruptcy and it operates very slowly. While client assets held at the central depository are protected, it is not clear how the default procedures of the central counterparties would work in the event of a brokerage firm or large financial conglomerate bankruptcy. The bankruptcy laws do not contain specific provisions dealing with market-related issues, such as closing out open derivatives positions.</li> </ul>
<b>Principles for the Secondary Market</b>	
<b>Principle 25.</b>	The establishment of trading systems including securities exchanges should be subject to regulatory authorization and oversight.
Description	<p>There is one stock exchange and one derivatives exchange operating in Mexico under permissions granted by the Federal Government in 1933 in the case of the BMV and 1998 for MexDer. There are no alternative trading systems permitted for listed instruments.</p> <p>There are inter-dealer brokers (<i>sociedades que administran sistemas para facilitar operaciones con valores</i>) operating in Mexico. These entities are authorized by the Commission under the LMV to provide services and facilities for OTC trading in securities—mostly debt and derivatives—only to credit institutions and brokerage houses (LMV, Article 253 &amp; ff). They may also provide price information to anyone on the instruments that trade through their facilities. They do not deal in listed equity securities and are not registered as intermediaries under the LMV. Interdealer brokers must adhere to limited regulatory standards focused on system capacity rather than capital adequacy. They are prohibited from acting as counterparties and so do not function as risk</p>

principals in trading (LMV, Article 258).

The Federal Government, acting through the SNCP and with the advice of the Commission, has the authority to grant a license to an applicant to organize and operate as a stock exchange (LMV, Article 234). Applicants must file detailed applications including information on:

- Names and details of capital contributed, probable directors, CEO and senior executives of the company.
- Plan of operation:
  - securities to be traded;
  - premises, facilities and trading platforms to be used;
  - security measures to preserve the integrity of information;
  - draft rules to comply with the legislative requirements of the LMV;
  - manual of policies and operating procedures;
  - description of programs to be conducted on members and listed issuers to ensure compliance; and
  - description of market surveillance programs to be carried out.
- Policies and guidelines to apply to listed companies and members (LMV Article 235)

Authorization decisions are to be based on an assessment whether the new exchange would support the objective of the best development of the Mexican market.

Prior to beginning actual operations, a new stock exchange must certify to the Commission that it has in place:

- Required minimum capital.
- Fit and proper personnel as specified.
- The infrastructure and internal controls needed to perform its activities and services in accordance with the applicable provisions.

Based on what is done during the routine oversight of the brokers and the exchanges, no new exchange would be authorized to do business without satisfying the Commission, after a detailed examination, that its systems and infrastructure could support its proposed operations. The Commission may deny permission to begin operations if the exchange does not certify the compliance with these provisions (LMV Article 236).

Stock exchange trading systems must meet the specified requirements, including:

- be capable of ensuring continuity in the trading of securities;
- have contingency plans in place to avoid trading interruptions; and
- include mechanisms to maintain the integrity of the stock market (LMV, Article 245).

Similar requirements are imposed and processes contemplated by the MexDer Mandatory Rules on persons proposing to set up an organized derivatives exchange or derivatives clearing house. For MexDer, the opinion/concurrence of BoM is required in addition to that of the CNBV. The regulator and central bank would perform their own independent technical analysis of the proposed new entity and provide their advice to the Minister. While the CNBV does not have recent experience of the authorization of an exchange on which to base its opinion, staff stated they have no reason to believe that the SHCP would not follow the advice given by the Commission.

SHCP has the authority to set minimum capital requirements that apply to BMV and MexDer, along with extensive capital and risk management requirements that are applicable to the central counterparties (CCV and Asigna) and central depository (Indeval). No minimum capital requirements have been set for the BMV. The MexDer Mandatory Rules set out the minimum capital for MexDer (4 million UDI in paid up capital) and Asigna (15 million UDI held in cash or cash equivalents). The Mandatory Rules also set minimum capital requirements for clearing members and brokers on the exchange (see Principle 21).

The rules of the BMV and MexDer are subject to review and approval by CNBV. The rules of MexDer are also subject to review and approval/veto by BoM. In some cases, the CNBV may be directly involved in the development of new rules. For example, Commission staff was active participants in the project at the BMV leading to new rules on direct market access, algorithmic trading and high frequency trading.

Under the LMV, the BMV's internal regulations are required to address the following issues: (i) the requirements that a broker-dealer must satisfy to trade listed securities on the Exchange; (ii) the rights and obligations of admitted broker-dealers and listed issuers of securities; (iii) the requirements regarding the maintenance and cancellation of listings; (iv) the terms by which trading may be conducted and the basis for suspending trading of securities, (v) the procedures for supervising trading and imposing sanctions on member firms, and (vi) the measures to ensure the continuity of operations at the Exchange.

The Commission is informed of the types of securities to be traded and it approves the rules governing the admission of the securities to the stock exchange. The listing and trading of new products on MexDer is subject to the review and approval of SHCP, with input from CNBV and BoM.

By law, the operating systems for trading on a stock exchange must allow its members to participate on equal terms. The LMV requires that BMV trading systems satisfy certain minimum requirements consisting of (i) providing access to bids or offers, transactions undertaken and market information generally; (ii) identifying parties to any transaction, including the time and date of the transaction, number and type of securities that were the subject of the transaction, price of the securities and amount applicable, and type of settlement; (iii) identifying irregularities arising from any transaction; and (iv) maintaining a record of the relevant transaction, without permitting the amendment of any record.

The rules governing trading on the BMV and MexDer are publicly available on their respective websites. Order execution procedures (based on price and time priority) are clearly disclosed and applied by the automatic systems at the exchanges and are consistent with relevant requirements with respect to precedence of client orders and prohibition of front-running. The proper functioning of these systems is verified during on-site inspections.

As part of the inspection and supervision of markets, the Commission must review, verify and assess the operational performance, processes, systems of internal control, risk management, handing of information and recordkeeping, as well as verifying compliance with the relevant legal provisions and sound financial practices (CNBV, Manual of Markets Supervision).

On-site reviews take place approximately every 18 months. The primary focus of the review is on the trading operations: order management, exception reports, capacity issues, etc. Staff matches actual trading records against the trading algorithms to ensure the systems are working as they are supposed to. Staff reviews the operations of the BMV listing committee, including the analysis of proposed new offerings. They also meet with and review the reports of the exchanges' internal auditors. The exchanges' SRO functions are reviewed, as are surveillance operations.

	<p>There are extensive record keeping requirements that apply to the exchanges, the securities firms, central depository and central counterparties that generate for a full audit trail for transactions, from receipt of the order at the firm through to final settlement. These records are kept electronically and must be provided to the Commission on request.</p>
Assessment	Fully Implemented
Comments	<p>Establishment of stock and derivatives exchanges requires authorization from the SHCP with input from the CNBV (and from the BoM for derivatives exchanges). There are criteria set out in the law, regulations and the MexDer Mandatory Rules that any applicant must meet, including requirements regarding systems and other infrastructure capacity, technical competence, etc. While the CNBV does not have recent experience of the authorization of an exchange on which to base its opinion, staff stated they have no reason to believe that the SHCP would not follow the advice given by the Commission. Certainly the practice has generally been to rely on the expertise of the regulator and central bank in technical matters.</p> <p>Oversight of the exchanges includes both on-site examinations and off-site reviews. All new rules and proposed rule changes require CNBV approval after reviews are conducted. On-site reviews include an assessment of the operational performance, processes, systems of internal control, risk management, handling of information and recordkeeping, as well as verifying compliance with the relevant legal provisions and sound financial practices. The Commission reviews and approves new products. There is equal access to membership for firms that meet the membership criteria.</p>
<b>Principle 26.</b>	<p>There should be ongoing regulatory supervision of exchanges and trading systems, which should aim to ensure that the integrity of trading is maintained through fair and equitable rules that strike an appropriate balance between the demands of different market participants.</p>
Description	<p>Transactions in listed securities must be executed through the BMV. Transactions in listed derivatives must be conducted through MexDer.</p> <p>All exchanges are required to have in place systems for monitoring and surveillance of operations conducted on its trading systems, as well as certifies the quotations of securities and transactions carried out. (LMV, Article 244). The exchanges and CNBV carry out real time market surveillance programs in parallel to one another. These systems monitor day-to-day trading activity on the exchange and by market intermediaries. They collect and analyze the information gathered. There are automatic triggers built in that send alerts when unusual trading patterns (volumes, prices) are seen.</p> <p>The stock exchange, acting as an SRO, is empowered to issue rules related to the efficiency and transparency in the stock market. (LMV Article 229) The BMV sets rules for member firms, including requirements that they have in place systems that are compatible with those of the exchange and have appropriate redundancies to ensure they operate continuously. Similar provisions are in place with respect to MexDer.</p> <p>The BMV has the authority to conduct examinations of its members to ensure compliance with the SRO requirements, but only exercises that authority infrequently. MexDer is required to conduct regular examinations of clearing members and member brokers.</p> <p>The CNBV verifies compliance by the exchanges with their statutory and legal responsibilities related to integrity of the markets, market surveillance, and monitoring of risks. The CNBV has powers to verify this compliance by conducting inspection visits or requiring information. (See the discussion of the oversight program set out under Principle 25.) Often, CNBV staff is active participants in projects at the exchanges to develop new rules.</p>

	<p>There are extensive record keeping requirements that apply to the exchanges, the securities firms, central depository and central counterparties that generate for a full audit trail for transactions, from receipt of the order at the firm through to final settlement. These records are kept electronically and must be provided to the Commission on request. The Commission gets daily reports from all brokers regarding the beneficial owners associated with each trade carried out.</p> <p>The rules of the BMV and MexDer are subject to review and approval by CNBV, SHCP and BoM.</p> <p>The Commission can intervene in the administration or the management of the stock exchange and suspend operations that endanger its solvency, stability or liquidity, or those that violate the laws (LCNBV, Article 4). The Commission has exercised to intervene in the market to order the exchange to take action. For example, in 2004, after the volume of program trading threatened the capacity of the systems at BMV, the Commission directed the exchange to add significant new capacity. The Commission also has the power to order the removal or dismissal of directors and executives of the stock exchange if they commit serious or repeated infringements of the law (LMV, Article 221). SHCP, on a discretionary basis or at the request of the CNBV, may revoke the concession to operate a stock exchange if it: (i) suspends its activities for a period equal to or exceeding six months; (ii) initiates a procedure for liquidation or dissolution; (iii) is declared in bankruptcy under applicable law; or (iv) fails to comply with material provisions of applicable law on multiple occasions. The authorization of MexDer may be terminated by SHCP, on the advice of the CNBV or BoM, as a result of (i) losses having an impact on their minimum paid-in capital; (ii) providing false, inaccurate, or incomplete information to the Mexican government; (iii) failing to keep accurate accounting records; or (iv) failing to comply with applicable law.</p>
Assessment	Fully Implemented
Comments	
<b>Principle 27.</b> Regulation should promote transparency of trading.	
Description	<p>The law and relevant rules in the jurisdiction and at the exchanges provide for real time pre- and post-trade transparency of trading information. Pre-trade transparency is provided to exchange members by the exchanges' terminal and systems. Post-trade transparency is provided to members via the terminals and publicly on the exchanges' websites (with only a short administrative delay to get the information posted).</p> <p>The trading systems of stock exchanges are required to allow members to participate on equal terms. For this purpose the systems must:</p> <ul style="list-style-type: none"> <li>• provide access to information on positions and trades in particular securities and on the market in general; and</li> <li>• identify the parties to the transactions (other broker), as well as the date and time of trading, price, volume and amount of the transaction, class and type of securities and way of settlement (LMV, Article 245).</li> </ul> <p>The trading rules at the BMV and the related CNBV Securities Firms Rules have recently undergone significant changes to modernize the rules regarding trading orders, permit direct market access (DMA) and facilitate cross-trading. These changes include:</p> <ul style="list-style-type: none"> <li>• replacing the set of permitted orders that dated from the days of open outcry trading on the floor of the exchange with a simpler set of orders, including those that facilitate high frequency and algorithmic trades;</li> <li>• permitting DMA to the exchange order book for certain qualified investors; this trading is required to be routed through a member broker and is subject to "low touch" supervision by that broker to ensure appropriate risk controls are in place and</li> </ul>

	<p>followed; the broker is responsible for settling all DMA trades that are processed through its system (Securities Firms Rules, Article 68); and</p> <ul style="list-style-type: none"> <li>introducing simpler cross order rules that (as of October 2011) permit all debt, equity and warrants listed on either part of the BMV to be crossed at an intermediary at a price within the best bid/ask spread without intervention by other members (Securities Firms Rules, Article 89).</li> </ul> <p>These rules were developed by the BMV, the CNBV and industry participants over several years, with the aim of being consistent with similar market developments and rules in other major markets, such as the rules on the New York Stock Exchange and those of the U.S. Securities and Exchange Commission Rule NMS.</p>
Assessment	Fully Implemented
Comments	The trading rules at BMV were recently modernized to facilitate high frequency trading, faster crossing of large trades and direct market access. The implementation and operation of these new rules should be monitored closely to ensure the current level of transparency is not negatively affected. Several major jurisdictions and IOSCO are actively reviewing the market implications of high frequency trading, dark pools and similar market developments. The exchange and the CNBV should continue to keep abreast of these discussions in order to maintain consistency of the Mexican approach with the international consensus on these issues.
<b>Principle 28.</b>	Regulation should be designed to detect and deter manipulation and other unfair trading practices.
Description	<p>The LMV prohibits conduct that constitutes:</p> <ul style="list-style-type: none"> <li>manipulating the market;</li> <li>false/wash trading;</li> <li>distorting the proper functioning of the trading system or computer hardware of the stock exchanges or inter-dealer brokers (brokers who operate in the OTC market for debt and derivatives );</li> <li>intervening in transactions with conflicts of interest;</li> <li>violating good market practices; and</li> <li>front running (LMV, Article 370).</li> </ul> <p>The monitoring systems operated by the CNBV and the exchanges allow detection of these types of conduct.</p> <p>Insider trading and tipping is prohibited (LMV Articles 364 and 365), as is the dissemination of false or misleading information regarding securities or issuers (LMV, Article 368). Market manipulation, insider trading and giving false information are criminal offences and are prosecuted as described under Principle 9. The Commission may sanction all other actions.</p> <p>Real time surveillance of trading on the markets is conducted by the BMV and at MexDer and a number of measures may be imposed to promote an orderly and transparent trading price. For example, at the BMV there is a system that automatically suspends trading in the shares of a particular issuer when price fluctuations exceed 15 percent. When prices fluctuate more than 10 percent the shares are moved to trade by auction. The BMV may also suspend trading in capital stock of a particular issuer as a result of (i) nondisclosure of material events; or (ii) prices rising above or falling below predetermined levels or material changes in the general offer or sale of securities, volume traded or prevailing share price, when such changes are inconsistent with the relevant security's historical performance and cannot be explained through publicly available information.</p>

	<p>There are extensive record keeping requirements that apply to the exchanges, the securities firms, central depository and central counterparties that generate a full audit trail for transactions, from receipt of the order at the firm through to final settlement. These records are kept electronically and must be provided to the Commission on request.</p> <p>The surveillance area of the Commission has access in real time to information concerning trading activities at both exchanges.</p> <p>There is a detailed regime of sanctions set out in Titles XIV and XV of the LMV (Article 362 &amp; ff) that specifies clear penalties (both fines and terms of imprisonment) for violations. For example, persons involved directly or indirectly, in acts of manipulation of the market, who obtain a benefit for themselves or a third party, can be punished with a fine or a term of imprisonment from two to twelve years, depending of the amount of the benefit. A benefit includes obtaining a profit or avoiding a loss (LMV, Article 382). The maximum fine for insider trading is two times the profit realized. Some of the fines are not particularly high (for example, the maximum may only be US\$50,000 per violation/event).</p> <p>The BMV is the only stock exchange across the country, so there is no domestic trading of equity securities between markets. In debt securities, where it is possible to obtain different quotations for the same security, the CNBV has the power to investigate trading systems and to require information about transactions in which securities firms act as principals with their clients. There are a few cross products between the derivatives and stock exchanges, such as single stock futures and options. However there is no trading in these derivatives at the moment. In any event, the CNBV has full access to information from both exchanges.</p> <p>The Commission is empowered to share all kind of documentation, records, files and other information that it receives on the exercise of its powers or as required to comply with a request for information by outside authorities with which it has an MOU in place (LMV, Article 358). These cooperation arrangements would allow for sharing of information relevant to address manipulation or other abusive trading practices. (See the discussion under the Principle 12 and 13, above.)</p>
Assessment	Fully Implemented
Comments	<p>The only weakness seen under this Principle was the question of whether the maximum fines available were high enough to deter market misconduct, given the potential profits that can be made for breach of the rules. This gap has been taken into account in assessing Principles 9 and 10 and no further downgrade has been applied here. As noted under Principle 10, the CNBV should consider carrying out a complete review of the level of fines available for misconduct on the market, with a view to ensuring the fines are high enough to be dissuasive.</p>
<b>Principle 29.</b>	Regulation should aim to ensure the proper management of large exposures, default risk and market disruption.
Description	<p>Purchasers of 10 percent or more of a security must be disclosed promptly and the reports must be updated if additional shares are purchased. See the discussion under Principle 14 above.</p> <p>Large position reporting and monitoring are done at the central counterparties at each exchange. The central counterparties (CCV and Asigna for securities and derivatives, respectively) must have an overall plan of operation that includes extensive reporting and risk management mechanisms to limit and reduce exposures to participants, including access to sufficient funds to promptly fulfill their obligations, and operational, prudential and self-regulatory requirements in place to support their fulfillment of their roles in the marketplace (LMV, Article 302 and the MexDer Mandatory Rules).</p> <p>In order to cover large exposure and default risk, positions of intermediaries are limited by means of a series of prudential ratios set by regulation. The central counterparties</p>

also set position limits for members. There are clear market default and unwind procedures, as well as rules to halt trading in the rules of the relevant exchanges and central counterparties. These rules are published on the websites of the respective organizations.

The primary function of the CCV is to act as the legal counterparty for all equity transactions executed on the Exchange and thus to guarantee settlement of these transactions, thereby reducing counterparty and overall systemic risk within the Exchange. Each broker-dealer that engages in securities trading in Mexico settles securities transactions through the CCV.

The principal permitted activities of the CCV include:

- acting as central securities counterparty in respect of transactions undertaken by its broker-dealer members (or by broker-dealer members on behalf of nonmember broker-dealers);
- establishing procedures to manage risk and to satisfy failed transactions;
- requiring, receiving and managing funds from members to reduce risk and apply funds maintained at the CCV Contribution Fund to cover breaches by members;
- buying and selling securities to settle transactions as central counterparty, with the assistance of designated broker-dealers; and
- receiving loans necessary to duly avoid risks as central counterparty.

By law, transactions undertaken by the CCV with broker-dealer counterparties must be netted; netted transactions are satisfied at the end of each trading day. The CCV conducts intraday monitoring of firm concentrations and open positions and requires collateral deficiencies to be satisfied within thirty minutes.

Broker-dealers must transfer amounts to the CCV for settlement purposes (initial contributions and contributions made to the CCV Contribution Fund). These are deemed transferred to the CCV and may be applied to satisfy failed transactions. The CCV's regulations set out a detailed regime that governs how breaches by any broker dealer member are covered by the CCV, what actions must be taken and by whom.

Under the rules of MexDer and Asigna, clearing members (called Settlement Trusts in those rules) and brokers are required to provide periodic information to each of MexDer and Asigna so that they may monitor compliance with applicable law. Failure to comply with applicable law may result in sanctions (including open contracts having to be settled, transferring contracts to other clearing members or brokers or permanently suspending the breaching clearing member or Broker).

Extensive information must be provided to MexDer and Asigna daily, including daily information (i) for each transaction on a per account basis; (ii) for each order received and the account to which such order relates, and (iii) on open positions and applicable limits (per client and per underlying asset).

To ensure the safety and soundness of MexDer and Asigna, each of MexDer and Asigna may impose or reduce limits per client and per type of underlying asset, may impose Extraordinary Settlements, may order that positions be closed and may suspend certain transactions or operations as a whole. The president of MexDer or Asigna may order suspensions if extraordinary circumstances arise. Any such order must specify the reasons for the suspension.

Under Asigna's regulations, Asigna operates a settlement system or safety net designed to avoid systemic and counterparty risk. If a client fails to satisfy a Daily Settlement or an Extraordinary Settlement, the relevant clearing member must so inform MexDer, Asigna, the SHCP, BoM, the CNBV, and the other clearing members and brokers. Thereafter, the

	<p>default procedures set out in the regulations must be followed. These regulations are transparent, set out when action is to be taken, who is to take action and the specifics of what actions may be taken.</p> <p>Trades by foreign investors in Mexican publicly traded instruments must be routed through a Mexican firm authorized by the CNBV. The Commission has MOUs in place that allow it to share information on a cross-border basis routinely or in a crisis to manage the effects of a widespread market disruption.</p>
Assessment	Fully Implemented
Comments	<p>The requirements that traded instruments be held at the central depositories and the default procedures at the central counterparties are designed to permit the prompt isolation of the problem of a failing firm by addressing its open proprietary positions and positions held for clients. The aim is to minimize and manage the risks to client assets and the system as a whole from an intermediary's default. Client assets properly deposited at the central depositories are protected on a brokerage house's bankruptcy. However, given that brokers are subject to the ordinary bankruptcy regime that applies to any company, these default procedures and close-out processes may not work as designed if the firm actually has been declared bankrupt. As for most jurisdictions, client funds and assets not yet deposited may be at risk in a bankruptcy. This places a premium on there being a mechanism to assure timely settlements and reconciliations between the books of the brokers and the clearing house.</p>
<b>Principle 30.</b>	Systems for clearing and settlement of securities transactions should be subject to regulatory oversight, and designed to ensure that they are fair, effective and efficient and that they reduce systemic risk.
Description	Not assessed under IOSCO methodology; subject to separate assessment under CPSS-IOSCO methodology for securities settlement systems.
Assessment	Not assessed.
Comments	

## ANNEX I. STATUS OF IMPLEMENTATION OF THE NEW IOSCO PRINCIPLES

IOSCO approved a revised set of principles in 2010, which included the addition of nine principles. IOSCO has approved a revised methodology for consultation. Given that the revised methodology has not yet been officially approved, these principles have been assessed on a voluntary basis and thus have not been graded. This chart sets out the new principles and a discussion of the relevant current regulatory environment in Mexico.

**Annex Table 12. Mexico New Principles and Current Regulatory Environment**

<b>Principles Relating to the Regulator</b>	
<b>New Principle 6.</b>	<b>The regulator should have or contribute to a process to monitor, mitigate and manage systemic risk, appropriate to its mandate.</b>
Description	<p>The CNBV has restructured itself in order to apply risk-based supervision more comprehensively. The Commission set up a new area that is dedicated to monitoring all the risks across financial sectors: banks, securities firms, mutual funds, etc. The supervision is focused on financial groups, in order to identify and monitor all the risks inherent in these entities and their inter-relationships, including the potential for systemic risk. This area has introduced and adopted a range of new techniques for measuring and monitoring risks.</p> <p>For example, the CNBV monitors changes in asset prices in order to flag possible asset bubbles. It also monitors conduct of business across all authorized financial market participants where this conduct might contribute to systemic risk, such as offloading risky assets from a bank's book onto less sophisticated investors via structured products.</p> <p>In 2010, Mexico established a body for regulatory coordination to strengthen the stability of the financial system: the Financial System Stability Council. The Council is made up of the supervisory and regulatory financial system authorities and its functions include identifying risks that can disrupt or substantially alter the functioning of the financial system in a timely manner; and recommend and coordinate policies and measures that each financial authority, within their respective areas of action, should take to avoid those risks or, in given case, to minimize its impact.</p> <p>There are extensive MOUs between domestic regulators and between the CNBV and foreign supervisory authorities that facilitate information sharing between regulators for any supervisory purpose, including management and mitigation of systemic risks. (See the discussion under the Coordination Principles.)</p>
Comments	The gaps in the early warning requirements noted under current Principle 22 and 24 may limit comprehensive and timely assessment of the risks across the system.
<b>New Principle 7.</b>	<b>The regulator should have or contribute to a process to review the perimeter of regulation regularly.</b>
Description	<p>The Commission has established a new regulatory process, which incorporates the inputs given by surveillance and legal areas to identify and assess whether its regulatory requirements and framework adequately address risks posed by products, markets, market participants and activities. Also, the Commission has a regulatory policy vice-presidency, which is in charge of the design of financial regulation for all market participants on an integrated basis across the financial system.</p> <p>As part of the new regulatory process, there is financial regulation committee that periodically discusses the topics under development by the policy vice-presidency.</p>

	<p>Significant areas within the Commission attend this committee, which serves as a forum to hear concerns, evaluate past regulatory decisions and identify current situations that need to be addressed.</p> <p>The CNBV actively seeks legislative or other changes when it identifies a regulatory weakness that needs such to be addressed appropriately. Financial authorities frequently propose legislative changes in order to maintain a solid regulatory framework for the financial system. Examples of this are the recent amendments to several financial laws in order to include prompt corrective actions and money laundering prevention.</p> <p>The Financial System Stability Council, mentioned above, also performs a role in identifying risks that can disrupt or substantially alter the functioning of the financial system. The Council is not, however, concerned with matters related to the promotion of investor protection or fair and efficient markets.</p>
<b>New Principle 8</b>	<b>The Regulator should seek to ensure that conflicts of interest and misalignment of incentives are avoided, eliminated, disclosed or otherwise managed.</b>
Description	<p>In 2009, the CNBV created a new area, whose main activities are aimed to evaluate the behaviour of institutions in the investment services provided to clients. Using various surveillance processes, this new area is able to identify incentives that could encourage intermediaries to act on conflicts of interest, to the detriment of its customers and the market. As part of its surveillance function, the Commission evaluates trades in securities where there might have been a misalignment of incentives with the parties involved. Particular attention is placed on certain IPOs or trades on the secondary market where there are business relationships between the issuer, the securities firm and the potential investors (such as mutual funds for example). Further the supervision of sales practices at intermediaries includes reviewing situations where there may be conflicts of interest.</p> <p>Since it was established, this specialized area of CNBV has conducted several inspections of firms in order to identify potential conflicts of interest inherent in providing advisory services. As a result of these inspections corrections have been ordered, recommendations have been made and in some cases, sanctions processes have begun.</p> <p>The Commission has extensive information about related parties of public issuers and authorized market participants such as banks and brokerage houses. The prospectus and the annual report of a public issuer must include a section containing information regarding operations with related parties and possible conflicts of interest (Issuers Rules, Annex H).</p> <p>The LMV gives the Commission authority to take action against a securities firm that offers services when it is in a conflict of interest situation that may harm its clients. Therefore, when a conflict of interest is detected, strong actions are taken to remedy the situation and apply suitable punishment.</p> <p>In accordance with IFRS and MexGAAP, transactions with related parties are to be disclosed in an entity's financial statements. In certain initial public offerings, where there could be potential conflicts of interest, investors are obliged to sign a letter acknowledging of this situation prior to acquiring the securities.</p>
Comments	<p>A project is underway to develop a more complete regime to address conflicts of interest that would classify types of conflicts/transaction and apply the appropriate requirement— from an absolute prohibition on the transaction to additional required disclosure to permission subject to protections like the trade being carried out at a market price. This will add to the protections available to reduce the risks of conflicts of interest.</p>

<b>Principles for Auditors, Credit Rating Agencies and Other Information Service Providers</b>	
<b>New Principle 19.</b>	<b>Auditors should be subject to adequate levels of oversight.</b>
Description	<p>At the moment, there is no separate independent oversight body in charge of the quality and implementation of auditing, independence, and ethical standards. The Commission has power to oversee the auditing firms, including the partners or employees on the audit team and can:</p> <ul style="list-style-type: none"> <li>• Require production of all audit work papers.</li> <li>• Conduct inspections.</li> <li>• Require the attendance of partners, representatives and other employees of the auditing firms.</li> <li>• Recognize auditing standards to be observed by the auditing firms.</li> </ul> <p>The Commission may issue rules and audit procedures in the event that in connection with any matter, there are no rules or procedures or when in the opinion of Commission, the standards mentioned are not enough.</p> <p>The LMV includes general fit and proper requirements for auditing firms, including a requirement that they meet the internal control and quality control requirements established by the Commission. In addition, the external auditors, the auditing firm and the partners or persons belong to the audit team, are required to meet detailed independence tests established by the Commission, which consider, among other things, financial ties or economic dependence or the provision of non-audit services. Also, there are maximum periods during which auditors can provide external audit services to public companies, brokerages, stock exchanges, securities depositories and the central counterparty for securities. (LMV, Article 343)</p> <p>The audit firm's are required to participate in a quality assessment program that includes at least:</p> <ul style="list-style-type: none"> <li>• The degree of compliance with generally accepted auditing standards referred in these rules.</li> <li>• The content and degree of compliance to the required policies and procedures manual referred above.</li> </ul> <p>The quality evaluation program must comply with the policies, rules and procedures established by the Commission (Issuers Rules, Article 86).</p> <p>Compliance with these requirements may be assessed on an inspection.</p> <p>The Commission recognizes the accounting standards for the development and formulation of financial statements or equivalent, and could distinguish between types of issuer. The Commission has authority to issue accounting standards, when the standards mentioned are not enough, there are different alternatives for accounting treatment or not reflect a real and current financial position for the Issuers.</p> <p>There is no specific rule establishing requirements for supervision of the audit process to be followed by auditing firms. The Commission, with the agreement of the Board of Governors, may order the removal or suspension (from three months to five years) of external auditors of a financial institution or issuer if they do not demonstrate the requisite level of technical quality, reputation or satisfactory credit record in the performance of their duties; or they engage in serious or repeated violations of the LMV (LMV, Article 393).</p> <p>See also the discussion under Principle 16 above.</p>

<b>New Principle 20.</b>	<b>Auditors should be independent of the issuing entity that they audit.</b>
Description	<p>See the discussion under existing Principle 16 regarding the extensive independence requirements that apply to external auditors. The external auditor is required to be independent in both fact and appearance of the entity being audited. Also, as noted in the discussion under new Principle 19, the audit firm is required to have a manual of policies and procedures that allow them to maintain an adequate quality control in the audit service and monitor compliance with the requirements of independence.</p> <p>The Issuers Rules (Article 83) contain an extensive list of non-audit services that may not be provided by the external audit firm</p> <p>The external auditor is selected by the audit committee of the public issuer and formally appointed by the shareholders.</p> <p>All audit committee members of a public company must be independent directors and the duties of that committee are specified (LMV, Article 25). Generally the audit committee is responsible for:</p> <ul style="list-style-type: none"> <li>• evaluating the company's internal controls and procedures;</li> <li>• identifying material deficiencies;</li> <li>• following up with corrective or preventive measures adopted with respect to the noncompliance with the operation and accounting guidelines and policies;</li> <li>• evaluating the performance of the external auditors;</li> <li>• identifying and valuing nonaudit services rendered by the external auditor;</li> <li>• reviewing the company's financial statements;</li> <li>• assessing the effects of any modifications to the accounting policies approved during a fiscal year;</li> <li>• overseeing measures adopted as result of observations made by shareholders, directors, executive officers, employees or third parties with respect to accounting, internal controls and internal and external audit, as well as complaints regarding management irregularities , including anonymous and confidential methods for addressing concerns raised by employees; and</li> <li>• ensuring the execution of resolutions adopted at shareholders' or Board of Directors' meetings.</li> </ul> <p>An independent director must chair the audit committee of a securities firm. The LMV and the Securities Firms Rules assign the committee specified oversight duties.</p> <p>Issuers must disclose to the BMV and the Commission any change of external auditor, indicating the causes for the change. The Commission may ask the departing auditors for its views and may order the BMV to make such views publically available to investors.</p> <p>IMPC is an active member of the International Federation of Accountants (IFAC). As a member, IMPC has implemented IFAC's quality control processes for accounting firms. These entail reviews of accounting firm processes and activities. Resources have been mobilized and examinations by IMPC of firms have been underway for the past two years.</p> <p>The Commission has completed a project that developed a framework for the oversight of the quality of external audit firms' processes and performance. However, currently there is no rule that allows the Commission to review the audit process followed by auditing firms.</p>

Comments	The gap in the rules regarding Commission authority to review the audit process followed by auditing firms should be filled.
<b>New Principle 21.</b>	<b>Audit standards should be of a high and internationally acceptable quality</b>
Description	Until 2011, the audit and the external auditor's report are required to be prepared and presented under local auditing standard issued by IMCP, the auditing standard setting body in Mexico. In the view of the CNBV and the accounting profession members that the assessor met with during the assessment, these constitute a comprehensive set of auditing standards. From 2012, the audit must be based on International Standards on Auditing issued by the International Auditing and Assurance Standards Board of International Federation of Accountants. (Issuers Rule, Article 78).
<b>New Principle 22</b>	<b>Credit rating agencies should be subject to adequate levels of oversight. The regulatory system should ensure that credit rating agencies whose ratings are used for regulatory purposes are subject to registration and ongoing supervision.</b>
Description	<p>The LMV includes a definition of <i>Instituciones calificadoras de valores</i> (credit rating agency, CRA) and reserves this activity solely to those companies that are granted authorization by the Commission and comply with the requirements of the law. The Commission has powers to supervise and regulate their activities. Only authorized CRAs are allowed to issue ratings in Mexican territory and only ratings issued by authorized CRAs are allowed to be used for regulatory purposes (Bank regulation, Article 2 Bis 11). At the present time there are four authorized CRAs: one is a domestic company, the other three are subsidiaries of CRAs that operate globally.</p> <p>The LMV empowers the Commission to request any information from the rating agencies in order to accomplish its supervisory objectives. The Commission has powers to obtain information regarding their main processes, methodologies and internal controls. As part of the registration requirements, the applicants must prove they fulfil the requirements of the law.</p> <p>The Commission has powers to withdraw the authorization in the case of certain events such as repeatedly committing infractions of the law or rules (LMV, Article 340).</p> <p>There is an informal minimum initial capital requirement of two years' operating expenses, assuming no income over that period. All four authorized firms are examined yearly by on-site visits.</p> <p>The rules for CRAs establish the obligation to adopt written procedures and methodologies. The Commission reviews the methodologies used by these institutions and requires any material changes to be reviewed. The Commission has powers of veto in respect of modifications to those procedures and methodologies. (CRAs Rule Article 3). The Commission is developing additional rules that would require the CRAs to publish information on their methodologies in Spanish to increase the accessibility of that information.</p> <p>The rules establish several independence criteria to be met, including prohibitions to participate in a rating action when there's a potential conflict of interest. This includes owning securities issued by the client, having a business relationship, participating in the fee or contract determination process, etc. The rule requires that the CRA have in place an internal control system to address, manage and deter conflicts of interest.</p> <p>The CRA Rules oblige CRAs to hold non-public information confidential, including all the information used for the purposes of setting and amending ratings. CRAs analysts and other personnel are obliged to refrain from disclosing information about rating actions until these are made public. They are subject to requirements to preserve confidentiality according to the policies required by the rules (CRA Rules, Annex 1). The general insider trading rules would apply if a CRA or any staff member disclosed or used material nonpublic information.</p>

<b>New Principle 23.</b>	<b>Other entities that offer investors analytical or evaluative services should be subject to oversight and regulation appropriate to the impact their activities have on the market or the degree to which the regulatory system relies on them.</b>
Description	<p>The Commission periodically considers whether the different types of entities that provide analytical or evaluative services warrant regulation and oversight. This review has been done for external auditors, financial analysts, and independent experts, among others and resulted in new requirements for some of these entities. For example, recently, there has been a regulatory action towards restricting certain opinions related to the track record of the SPV's administrator, made by independent experts in the context of certain securities offerings (<i>Certificados de capital de desarrollo</i>). In this sense, the prospectus might include those opinions, only if they do not contain a judgement about the appropriateness of the investment</p> <p>Banks and security firms that produce analyst research reports are subject to regulations that require internal controls that include detailed provisions to address conflicts of interest. The analysts themselves and their firms are subject to several prohibitions and restrictions on trading activities, financial interests and business relationships (Analyst Rule, Articles 3 and 5).</p> <p>Analysts' recommendations are required to be accompanied by certain disclosures regarding situations that could raise a conflict of interest for the analyst or the financial entity for which the analyst works. (Analyst Rule, Article 4). Employees of securities firms and banks are subject to a mandatory code of conduct that includes the obligation to act honestly and fairly with clients (Securities Firms Rules, 109).</p>
<b>Principles for Collective Investment Schemes</b>	
<b>New Principle 28.</b>	<b>Regulation should ensure that hedge funds and/or hedge funds managers/advisers are subject to appropriate oversight.</b>
Description	<p>Currently there are no requirements that would oblige a person to be registered to manage or operate a hedge fund structured as a trust or other special purpose vehicle for sale only to sophisticated parties. The present policy decision of the Commission is not to permit the registration of any public SI that would constitute a hedge fund. The requirement to register as a manager of a fund presently is tied to the SI structure. Authorized securities firms could carry on certain hedge fund management activities.</p> <p>Collective investment schemes offered other than to the public (see the description of a private offering in Principle 14) would not be subject to any mandatory requirements on public disclosure, reporting to the Commission or otherwise.</p> <p>However, the risk that a hedge fund operating in the exempt market in Mexico would pose a systemic risk is mitigated by other factors present in the regulatory regime. The CNBV has extensive and timely access to all account information at regulated firms, including the positions of all clients. It gets daily reports of all trading that includes disclosure of the beneficial owner of the account trading. Also, there is a process in place to monitor build-ups of position at firms, exchanges and in OTC derivatives (this last by the BoM) that might lead to systemic issues.</p>