Taxation and Investment in Mexico 2014
Reach, relevance and reliability
Contents

1.0 Investment climate
   1.1 Business environment
   1.2 Currency
   1.3 Banking and financing
   1.4 Foreign investment
   1.5 Tax incentives
   1.6 Exchange controls

2.0 Setting up a business
   2.1 Principal forms of business entity
   2.2 Regulation of business
   2.3 Accounting, filing and auditing requirements

3.0 Business taxation
   3.1 Overview
   3.2 Residence
   3.3 Taxable income and rates
   3.4 Capital gains taxation
   3.5 Double taxation relief
   3.6 Anti-avoidance rules
   3.7 Administration
   3.8 Other taxes on business

4.0 Withholding taxes
   4.1 Dividends
   4.2 Interest
   4.3 Royalties
   4.4 Branch remittance tax
   4.5 Wage tax/social security contributions

5.0 Indirect taxes
   5.1 Value added tax
   5.2 Capital tax
   5.3 Real estate tax
   5.4 Transfer tax
   5.5 Stamp duty
   5.6 Customs and excise duties
   5.7 Environmental taxes
   5.8 Other taxes

6.0 Taxes on individuals
   6.1 Residence
   6.2 Taxable income and rates
   6.3 Inheritance and gift tax
   6.4 Net wealth tax
   6.5 Real property tax
   6.6 Social security contributions
   6.7 Compliance

7.0 Labor environment
   7.1 Employee rights and remuneration
   7.2 Wages and benefits
   7.3 Termination of employment
   7.4 Labor-management relations
   7.5 Employment of foreigners

8.0 Deloitte International Tax Source

9.0 Office locations
1.0 Investment climate

1.1 Business environment

Mexico is a federal republic made up of 31 states and a federal district. The political system is comprised of federal, state and municipal governments. The federal government is comprised of executive, legislative and judicial branches. The president is the head of state and there is a bicameral legislature (senate and chamber of deputies). The judicial branch consists of a supreme court, circuit courts and district courts.

Mexico’s economy is driven by external trade. Export earnings are fueled by manufacturing, although petroleum, tourism, agriculture and mining also contribute to revenue.

The US is Mexico’s largest trading partner, due to its geographical proximity and the benefits of the North American Free Trade Agreement (NAFTA). Despite increasing competition from China and India, many foreign firms still choose Mexico for their assembly plants and other operations. Other major export markets include Canada, Japan and Spain. Major importers include Germany, Japan and Korea.

Mexico has 10 free trade agreements (FTAs) in force with 45 countries (and one of the most important ones with the EU and Canada) and 39 commercial agreements, 9 of them with limited scope and the rest for reciprocal promotion and protection for investments. The main benefit granted under the commercial agreements is the application of preferential rates on the import of goods that are considered as originating goods from the FTA member nations.

As a member of the World Trade Organization (WTO), Mexico has eliminated most export limitations and substantially reduced export taxes and direct export subsidies. However in 2012 Mexico joined the Wassenaar Arrangement, to implement export controls for conventional weapons, its parts and components, goods with dual usage, software and susceptible diverted technologies for the manufacturing and spreading of conventional and destruction weapons.

On the other hand, there are several export incentive programs, including special temporary import programs, are in place to encourage export sales. The legislation promoting in-bond facilities in Mexico (maquiladoras) makes the country an attractive place to manufacture goods for export to the US and other markets. Additionally, to encourage and support national exports and promote foreign investment in Mexico, the government implemented the Decree Establishing Sector Promotion Programs (PROSEC), which provides preferential duty treatment for goods to be used for Mexican producers in the manufacturing process.

Mexico also is a member of the OECD.

Economic activity is concentrated in Mexico City. The six northern border states are home to much of the country’s manufacturing, particularly maquiladoras producing goods that are exported.

Price controls

Mexico generally does not have price controls.

Intellectual property

Under the Federal Copyright Law, the National Copyright Institute (INDA), an independent agency of the Ministry of Education, is responsible for the administrative enforcement of the copyright laws. The INDA is authorized to conduct investigations, request inspections, address copyright violations and impose sanctions.

The law grants an author “moral” and “patrimonial” rights (moral rights recognize the author as the first and sole perpetual owner of the rights of his/her works and patrimonial rights allow the author to “exploit the work exclusively or authorize others to exploit the work”). Penalties apply for violations of the copyright law.

The Industrial Property Law protects the exclusive right to use trademarks throughout the registration period. Trademark protection covers the goods and services registered under Nice Classification standards.
Patents are granted for up to 20 years and allow the owner the exclusive right to exploit an invention.

1.2 Currency

The currency in Mexico is the peso (MXN).

1.3 Banking and financing

Large foreign groups dominate Mexico’s financial system. Their affiliates compete with independent financial firms operating as public development banks, public credit institutions, private commercial banks, private investment banks, savings and loan associations and mortgage banks. Other components of the financial system include securities market institutions, development trust funds, insurance companies, credit unions, factoring companies, mutual funds and bonded warehouses. The banking sector remains highly concentrated, with a handful of large banks controlling a significant market share, and the remainder comprised of regional players and niche banks.

Mexico City is the country’s main financial center, although Guadalajara and Monterrey (the country’s second and third ranked cities, respectively) are important financial, industrial and commercial centers.

1.4 Foreign investment

Mexico offers an attractive business environment, legal certainty, a large free trade agreement network and developed economic sector.

Foreign investment is permitted in all sectors except those specifically reserved to the Mexican government or to Mexican nationals or companies. Foreign investors may hold up to 100% of the capital stock of a Mexican corporation or partnership, except in areas reserved exclusively for the state (i.e. petroleum and other hydrocarbons, basic petrochemicals, electricity, radioactive minerals, etc.) or reserved exclusively for Mexicans and Mexican corporations (e.g. retail trade in gasoline and liquefied petroleum gas, radio broadcasting, radio and television services other than cable television, etc.). Investment in a classified or regulated sector such as banking, railways or telecommunications must be approved by the Foreign Investment Commission.

Foreign investment has been simplified by legislative changes, a reduction in legal and administrative bureaucracy and local content requirements, the elimination of most import license requirements and an overhaul of the intellectual property legislation. There are no general restrictions or limitations on the remittance of dividends or repatriation of capital.

1.5 Tax incentives

The 2013 tax reform abolished tax incentives, such as accelerated depreciation of fixed assets, land deductions for real estate developers and the special SIBRAS (real estate investment companies) regime as from 1 January 2014. The FIBRAS (real estate investment trust) regime has been maintained, but with some adjustments.

Maquiladoras

The maquiladora regime (or IMMEX) is designed to promote exports and encourage foreign investment.

Maquiladoras are Mexican companies that process, transform, assemble or repair imported materials, parts and components into finished goods that subsequently are exported out of the country. Maquiladora companies typically are owned by a foreign corporation (often a US company since many maquiladoras are located near the US border) with which the maquiladora contracts to produce semi-finished or finished goods for shipment to the foreign company. To qualify to operate under maquiladora status, a foreign investor must have a corporate presence in Mexico (which may be up to 100% ownership of a Mexican corporation). The foreign parent furnishes most of the machinery and equipment (M&E) required for the maquiladora activities, as well as raw materials or the parts to be processed and/or assembled; these items are imported by the maquiladora but remain the property of the foreign company. One of the most relevant characteristics of a
Maquiladora is that goods could be imported only on a temporary basis. Further, the foreign principal company must be resident in a tax treaty country.

There are different types of maquiladoras: industrial (used for manufacturing), services, holding, outsourcing and shelter maquiladoras.

Maquiladora operations generally create a permanent establishment (PE) in Mexico for the foreign principal that provides the raw materials and M&E to the maquila company; PE status would expose the foreign principal to Mexican income tax. However, as explained below, one of the benefits of the maquiladora regime is that PE status can be avoided if the maquiladora complies with certain requirements, in particular, special transfer pricing rules.

Under the maquiladora regime, maquiladoras have been allowed to import materials and M&E with a suspension of duties payment and value added tax (VAT) exempt to produce the finished products (as transformed or repaired by the maquiladora) to be a nonresident, which normally acts as a principal that then sells the products outside Mexico.

In addition to the indirect tax benefits available to maquiladoras, there are income tax benefits that have been refined over the years. These benefits include an additional tax deduction equal to 47% of certain benefits provided to employees (e.g. contributions to pension and retirement funds, overtime payments, the exempt portion of profit sharing, Christmas bonuses, vacation premiums, food coupons, and savings funds, among other benefits) and protection for the foreign principal company from exposure to the creation of a PE in Mexico. There are two ways for a maquiladora to avoid creating a Mexican PE: (1) adopt the safe harbor rules; or (2) elect to obtain an advance pricing agreement (APA) via a private letter ruling. Under the safe harbor, a maquiladora must report taxable income corresponding to the higher of the following:

- 6.9% of the value of its assets (taking into account the value of all assets employed in the maquila operations, including foreign-owned assets (both fixed assets and raw materials/inventory)); and
- 6.5% of its costs and expenses (taking into account operating costs and expenses as computed under Mexican GAAP).

The 2013 tax reform tightened the requirements for a maquiladora to qualify for PE protection and significantly limits some of the benefits that had been granted to such companies. The partial income tax exemption granted to maquiladoras since 2003 to continue to promote investment in Mexico and dissuade maquiladoras from shifting their operations to other countries was abolished as from 1 January 2014, as is the business flat tax. Additionally, the VAT and excise tax exemptions on the temporary import of materials and M&E by maquiladoras have been abolished (and a 16% VAT is now due), although the maquiladora can avoid paying VAT/excise tax upon import by obtaining certification from the Mexican tax authorities. If a maquiladora is certified, VAT technically will be imposed on goods imported for use in maquila production activities, but will be eliminated by a full tax credit so that no cash VAT will be imposed on such transactions. If the maquiladora cannot obtain certification, it will be able to satisfy its liability for VAT/excise duty on temporary imports by providing security via a bond issued by an authorized entity.

### 1.6 Exchange controls

There are no restrictions on the import of export of capital. Repatriation payments can be made in any currency. Both residents and nonresidents can hold bank accounts in any currency in any part of the world; however, for some accounts located in Mexico but kept in a foreign currency, the currency must be the US dollar and these accounts may only be held by companies and not individuals.
2.0 Setting up a business

2.1 Principal forms of business entity

Investors in Mexico can operate through any form of entity. Mexico has several forms of business organization, including the stock company (sociedad anónima – SA) and the limited liability company (sociedad de responsabilidad limitada – SRL), both of which can be forms of variable capital (CV).

The SA and the SA de CV are the most frequently used forms of organization for foreign investors. The SA most closely resembles the public limited company or corporation. Foreign investors with wholly owned subsidiaries that want added flexibility in increasing or decreasing capital have favored the SA de CV. The only difference between the SA and the SA de CV is the variable portion of an SA de CV’s capital stock, which is usually unlimited and not subject to notary certification upon fluctuation.

In an SA and SRL, the shareholders/partners are liable only to the extent of their contributions.

A foreign corporation also may conduct business activities in Mexico through a registered branch or permanent establishment or a representative office.

Formalities for setting up a company

Organizing a local corporation can take four weeks or longer, depending on the complexity of the project. A permit must be obtained from the Ministry of the Economy. Foreign companies can carry out business in Mexico only after registering with the Public Registry of Commerce.

Approval must be obtained from the Ministry of Economy to use a specific corporate name. Also as noted in the previous section 1.4, it may be necessary to obtain authorization from the Foreign Investment Commission to engage in certain activities.

At least two shareholders must appear before a notary public to sign the deed of incorporation (except in case of public subscription), which must contain the names, nationalities and other particulars of the founders; the name, domicile, purpose and duration of the company; a breakdown of its capital and a statement of the founders’ contributions and their value; a description of the manner of administration; names of directors, managers and supervisors; the manner of liquidation; and all other special agreements that will regulate the operation.

Regarding SA, at least 20% of the capital shares generally must be paid immediately, and in case of public subscription, all the shares must be duly subscribe within one year.

Forms of entity

Requirements for SA/SRL

**Capital:** SA The law does not provide a minimum amount of capital, but at least 20% of the set minimum capital must be paid in at the outset. SRL: The law does not provide a minimum amount of capital, but at least 50% of the set minimum capital must be paid in at the outset.

**Shares:** SA: Shares usually have a stated par value. Although no par value shares are allowed, it can be agreed that some shares will have limited rights to vote or special rights. All shares must be registered shares. SRL: Partnership interests apply instead of shares and could have different values and categories (a minimum of MXP 1 or its multiples).

**Shareholders/partners:** SA: There must be at least two shareholders (individuals or entities). The liability of shareholders is limited to the value of their subscribed shares. SRL: At least two partners are required, but there may not be more than 50 (individuals or entities). Both: For tax purposes, the liability of shareholders and partners is limited to the amount of their contributions.

**Ownership:** SA: The capital stock of the company is divided into shares with the same face value. SRL: The capital stock is divided in partnership interests that may have different values and categories (a minimum of MXP 1 or its multiples).

**Control:** Both: A simple majority of shareholders/partners has control, unless the bylaws establish a larger majority (e.g. for major decisions).
Reserves: Both: Five percent of net profits must be allocated annually to a legal reserve until the reserve equals 20% of the value of the authorized. Any reduction in the reserve must be restored to the 20% level.

Meetings: Both: Annual general shareholders/partners meetings are required to discuss, approve or modify the financial report submitted annually by the administrator(s).

Management: SA: Sole administrator or board of directors (at least two) that could be or not shareholders. SRL: Sole manager or board of managers (at least two) that could be or not partners.

Officers: Both: Officers may be Mexican or foreign.

Labor: Both: There is no requirement that labor be represented on the board. No more than 10% of the workforce may be foreigners.

Taxes and fees: Taxes and fees on incorporation are minor, but legal fees may be substantial depending on the complexity of the structure.

Statutory auditor: SA: A statutory auditor must be appointed to monitor execution of the administration of the company and the auditor could be or not shareholder must be a person or company different from the shareholders or partners of the company. SRL: A statutory auditor is not mandatory, but, if the partners approve the use of one, the role can be carried out only by a board of statutory auditors.

Branch of a foreign corporation

A foreign company from any country must obtain approval from the Ministry of the Economy to set up a branch office in Mexico.

A branch of a foreign corporation formally registered to do business in Mexico, as well as any other permanent establishment for income tax purposes, generally is taxed the same as a Mexican corporation.

Although a few companies have established branches in Mexico, they are at a disadvantage for several reasons. Branches may not own real estate and they may not deduct payments to the head office for interest, royalties, fees or other services. Establishing a branch takes more time and funds than establishing a corporation, and branch charters usually contain more restrictions than corporate charters. Because branch offices are not legally separate from the head office, the head office can be held responsible for the liabilities of a branch.

2.2 Regulation of business

Mergers and acquisitions

Large mergers and acquisitions must be reported in advance to the Federal Competition Commission to obtain authorization. Failure to comply can result in penalties, or a suspension or denial of the execution of the merger or acquisition. Before a merger or acquisition, it is necessary to verify the type of entity that will be involved to ensure compliance with the legal and tax rules.

Mergers, spinoffs and acquisitions are taxed as transfers of property. Mergers and spinoffs will not be taxed if they meet certain requirements, such as:

- Notifying the tax authorities;
- Filing a tax return for the last fiscal year, as well as any required information statements through the surviving company in the case of a merger, or through the designated company in the case of a spinoff where a company does not survive.
- In a merger, the surviving company should continue to engage in the same activities in which it and the merged companies engaged in before the merger.
- If a merger is going to take place within five years of a previous merger or spinoff, an authorization must be obtained from the tax authorities.
Monopolies and restraint of trade

The Federal Competition Commission also is the agency responsible for enforcing the Competition Law. The Commission has broad investigative and enforcement powers to address monopolies and restraints of trade.

Mexico's antitrust law prohibits monopolies and certain horizontal restrictive practices deemed to be “absolute monopolistic practices.” Price fixing, restrictions on production and distribution, market sharing and concerted bidding in public tenders are prohibited.

The law also prohibits the following practices (among others) by firms that have substantial power in the marketplace and that restrain or intend to restrain competition: vertical market sharing; restrictions on re-sales; tie-ins; exclusivity contracts; refusal to deal; and boycotts. Substantial market power is subject to a case-by-case investigation based on factors such as: market participation of the economic agent and whether it has the unilateral power to fix prices; presence of barriers to market access; existence and market power of competitors; access of the economic agent and its competitors to inputs and other raw materials; and recent market performance.

Although the law technically prohibits monopolies per se, in practice, focus is placed on the abuse of monopoly power. The president of the Federal Competition Commission and other officials have made it clear that the law will be applied only against companies that engage in prohibited practices, not against those that merely have the potential to exercise monopolistic powers.

2.3 Accounting, filing and auditing requirements

For corporate purposes, companies are obliged to maintain a shareholders’ minutes book of meetings held, regardless of whether the meetings are ordinary, extraordinary or special. Companies must maintain a shareholder registry in which the company officially recognizes the shareholders and records the company’s shares, as well as a registry of its capital (both increases and decreases) and share purchases.

Accounting standards are set by regulatory bodies, such as the Mexican Council of Investigation and the Development of Financial Information Standards. Mexican companies are required to prepare their financial statements in Spanish and according to Mexican Financial Information Standards (“NIF,” formerly “Generally Accepted Accounting Principles (PCGA”)). Accounting registries and books of accounting must be recorded in Spanish.

Corporations with gross income exceeding MXP 100 million, assets exceeding MXP 79 million or having at least 300 employees (for each month of the tax year) may file with the tax authorities a special report (dictamen fiscal) prepared by an independent public accountant. If the report is filed, the tax authorities will not audit on general principles, but will instead review to verify that the audit was properly carried out.
3.0 Business taxation

3.1 Overview

The principal taxes affecting companies doing business in Mexico are the federal corporate income tax, withholding taxes, VAT, tax on cash deposits, tax on real property and social security contributions that must be made on behalf of employees. Some taxes are levied at the state and municipal levels.

Under mandatory profit sharing rules, employers are required to distribute and pay 10% of their “adjusted” taxable income to employees. The actual distribution of profits must be paid within 60 days after the corporate income tax return has been submitted (and no later than 31 May of the following year).

As noted above under 1.5, incentives are available for maquiladoras.

Mexico has transfer pricing, thin capitalization and controlled foreign company rules, as well as a general anti-avoidance rule.

The business flat tax, as well as the flat tax credit granted to maquiladoras, was abolished in the 2013 tax reform.

The Congress approves a federal revenue law on an annual basis, which generally includes a list of the federal taxes to be imposed during the year. The Ministry of Finance is authorized to issue regulations for the implementation of the tax law. The State Administration of Taxation (SAT) is the body charged with collecting tax and enforcing compliance.

<table>
<thead>
<tr>
<th>Mexico Quick Facts for Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corporate income tax rate</td>
</tr>
<tr>
<td>Branch tax rate</td>
</tr>
<tr>
<td>Capital gains tax rate</td>
</tr>
<tr>
<td>Basis</td>
</tr>
<tr>
<td>Participation exemption</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Loss relief</th>
</tr>
</thead>
<tbody>
<tr>
<td>Carryforward</td>
</tr>
<tr>
<td>Carryback</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Double taxation relief</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ordinary credit</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Tax consolidation</th>
</tr>
</thead>
<tbody>
<tr>
<td>No, but there is a tax integration regime</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Transfer pricing rules</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Thin capitalization rules</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Controlled foreign company rules</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Tax year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Calendar year</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Advance payment of tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>12 installments</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Return due date</th>
</tr>
</thead>
<tbody>
<tr>
<td>31 March</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Withholding tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dividends</td>
</tr>
<tr>
<td>Interest</td>
</tr>
<tr>
<td>Royalties</td>
</tr>
<tr>
<td>Branch remittance tax</td>
</tr>
</tbody>
</table>
Capital tax  No
Net wealth tax  No
Payroll tax  State level
Social security contributions (estimated)  30%
Real estate tax  State level
Transfer tax  2%-5%
Environmental tax  Varies
VAT (standard rate)  16%

3.2 Residence
A company is resident in Mexico if its place of effective management is located in Mexico.

3.3 Taxable income and rates
Residents are taxed on their worldwide income. Nonresident companies are taxed only on their Mexican-source income. Income is deemed to derive from Mexican sources when the assets or activities are in Mexico or when the sales or contracts are carried out in the country, regardless of where title passes.

The corporate tax rate is 30%.

Taxable income defined
The gross income of a resident legal entity includes all income received in cash, in kind, in services or in credit, including income derived from abroad. This includes all profits from operations and income from investments not related to the regular business of the corporation, and capital gains.

The taxable income on which the corporate income tax rate is applied is the difference between taxable revenue and expenses. The recognition of revenue and expenses is made on an accrual basis.

The taxable income of a company is the amount remaining from its gross income in a tax year after the deduction of allowable expenses and losses. Taxable income generally includes profits, capital gains and passive income, such as interest, royalties and rents.

The taxation of dividends paid by resident entities to resident shareholders depends on whether the profits out of which the dividends are paid have been subject to tax at the corporate level. Relief for corporate income tax is provided at the shareholder level if the dividends already have been subject to tax at the corporate level. (If the dividends are received by a Mexican resident corporate entity, that entity does not consider dividends as taxable income for income tax purposes, because the profits are taxed only once at the level of the distributing entity.) The Mexican payer company must keep a record of the profits that have been taxed in a special account, known as the “CUFIN” account. If the dividends distributed come from a source other than the CUFIN account, the distribution is subject to a 30% income tax at the level of the distributing entity (and may reach 42.86% due to gross-up). The tax, however, may be carried forward for up to two years.

Payments received in the form of royalties for the use of patents, trademarks, trade names and service fees are taxable in Mexico.

Corporate capital gains or losses arising from the sale of fixed assets are treated as ordinary income or losses, taxable at the normal corporate rate. In calculating the taxable gains arising from the sale of land, buildings, equity shares and other capital interests, companies may apply an official schedule of inflation adjustments to the acquisition cost of the asset.

Deductions
Business expenses are deductible if they are properly documented, necessary for the taxpayer’s business operations and supported by relevant invoices. Examples of allowable deductions include:
• Returns received or discounts or rebates granted during the tax year;
• Cost of goods sold;
• Expenses net of discounts, rebates or returns;
• Investments (depreciation under the straight line method, adjusted for inflation);
• Bad debt credits and losses arising from acts of God;
• Contributions for the creation or increase of employee pension or retirement funds (with some limitations); and
• Accrued interest, subject to the thin capitalization rules.

An employer can deduct a certain percentage of specified benefits provided to employees (e.g., contributions to pension and retirement funds, overtime payments, the exempt portion of profit sharing, Christmas bonuses, vacation premiums, food coupons, and savings funds, among other benefits), provided certain conditions are satisfied. Employee profit sharing paid during the year may be credited against taxable gains for income tax purposes.

Dividends are not deductible by the distributing corporation or included in the gross income of the recipient (although they are included in the income base for calculating profit sharing). Other nondeductible items include:

• Items that do not meet the formal invoice requirements, income tax or VAT payments;
• Inflation adjustments made due to extemporaneous tax payments;
• Provisions for employee liability and indemnity reserves; and
• Goodwill.

In response to the OECD Base Erosion and Profits Shifting (BEPS) project, the 2013 tax reform includes measures that limit the deduction of payments made to related parties in Mexico and abroad:

• All payments made to a related or an unrelated individual, entity, trust, joint venture, investment fund or any other legal person subject to a preferential tax regime must be made on an arm’s length basis; otherwise, the payment is nondeductible for tax purposes.

• Interest, royalties and technical assistance fees paid to a foreign company (whether the foreign company is a controlled or controlling company) that fall within any of the following categories are nondeductible:
  − The foreign entity is a transparent entity (except where shareholders or members are subject to an income tax and the payment is made on arm’s length terms);
  − The payment is disregarded for tax purposes in the country or territory in which the foreign entity is located; or
  − The foreign entity does not consider the payment to be taxable income (unless the foreign entity recognizes the payment as taxable income in the same fiscal year or in the following year).

The income tax law aims to recognize the “real” reduction in debt that occurs as a result of inflation and the corollary decrease in the return on assets. Under the law, any excess of the inflationary reduction in debt over the amount of interest paid is taxable as an “inflationary profit,” but any excess of the inflationary increase in the value of assets over the return on assets is tax deductible. The system treats as interest both foreign exchange losses and net gains from the sale of financial instruments, such as petro bonds.

**Depreciation**

Depreciation is calculated on a straight-line basis. Depreciation rates are set by the government and vary by industry and type of asset.
Losses
Tax losses may be carried forward and deducted from the taxable profits obtained in the following 10 fiscal years. The carryback of losses is not permitted; thus, losses not carried forward are forfeited.

3.4 Capital gains taxation
Capital gains arising from the sale of fixed assets, shares and real property are considered normal income and are subject to the standard corporate tax rate. Mexican law allows the proceeds from the sale of real property, shares and other fixed assets to be indexed to inflation.
Nonresidents that sell shares of a Mexican company are subject to a 25% tax on the gross proceeds or 35% (increased from 30% as from 1 January 2014) on the net proceeds if the nonresident has a representative in Mexico (provided the nonresident is not located in a tax haven or benefiting from a preferential tax regime). A tax return relating to the sale must be filed and a dictamen fiscal obtained from a Mexican public accountant certifying that the reported gain is calculated correctly.
As from 2014, nonresidents that realize gains on the sale of publicly traded shares are subject to a 10% withholding tax on the net gain. The withholding will be made by the intermediary (i.e. the broker).

3.5 Double taxation relief
Unilateral relief
A resident taxpayer that is taxed in Mexico on foreign-source income is, in principle, granted both a direct and an indirect tax credit that may be used against the taxpayer’s liability to Mexican income tax to the extent the foreign income is taxable in Mexico. This is an ordinary foreign tax credit, i.e. it is limited to the amount of income tax due on the resident’s total taxable income for the year calculated under Mexican law attributable to the foreign-source income.
Income tax paid by a nonresident company that distributes dividends to another nonresident company, that, in turn, distributes dividends to a Mexican corporation, may be credited against the Mexican corporation’s income tax liability if the following conditions are satisfied:

- The dividend and the income tax are accrued by the Mexican corporation;
- The Mexican corporation owns at least 10% of the first-tier company;
- The first-tier company owns at least 10% of the second-tier company;
- The Mexican government has concluded a broad exchange of information agreement with the country in which the second-tier company is resident.

Tax treaties
Mexico has a solid tax treaty network, with most treaties following the OECD model treaty. Among other things, treaties establish rules for the taxation of permanent establishments, generally provide for relief from double taxation on all types of income, limit the taxation by one country of companies resident in the other and protect companies resident in one country from discriminatory taxation in the other. The relevant treaty should be reviewed to determine the applicable rates. Absent a treaty, Mexico’s domestic rules will apply. Mexico’s treaties generally contain OECD-compliant exchange of information provisions. Mexico also has concluded a number of tax information exchange agreements with various jurisdictions.

To obtain benefits under one of Mexico’s tax treaties, the beneficiary must produce a tax residence certificate or a copy of its tax return filed for the most recent fiscal year that shows that the beneficiary is resident in the treaty partner country. Any relevant conditions in the treaty also must be satisfied, including the filing of an information return related to the tax situation of Mexican residents and nonresidents with a permanent establishment in Mexico or the filing of the special report (dictamen fiscal) if that option was exercised.

The Mexican tax authorities may request proof that double taxation would, in fact, arise in the absence of treaty benefits, by means of an affidavit signed by the taxpayer’s legal representative, explaining the rules in the beneficiary’s jurisdiction and providing any relevant documentation.
Mexico Tax Treaty Network

<table>
<thead>
<tr>
<th>Country 1</th>
<th>Country 2</th>
<th>Country 3</th>
<th>Country 4</th>
</tr>
</thead>
<tbody>
<tr>
<td>Australia</td>
<td>Estonia</td>
<td>Japan</td>
<td>Romania</td>
</tr>
<tr>
<td>Austria</td>
<td>Finland</td>
<td>Korea (ROK)</td>
<td>Russia</td>
</tr>
<tr>
<td>Bahrain</td>
<td>France</td>
<td>Kuwait</td>
<td>Singapore</td>
</tr>
<tr>
<td>Barbados</td>
<td>Germany</td>
<td>Latvia</td>
<td>Slovakia</td>
</tr>
<tr>
<td>Belgium</td>
<td>Greece</td>
<td>Lithuania</td>
<td>South Africa</td>
</tr>
<tr>
<td>Brazil</td>
<td>Hong Kong</td>
<td>Luxembourg</td>
<td>Spain</td>
</tr>
<tr>
<td>Canada</td>
<td>Hungary</td>
<td>Netherlands</td>
<td>Sweden</td>
</tr>
<tr>
<td>Chile</td>
<td>Iceland</td>
<td>New Zealand</td>
<td>Switzerland</td>
</tr>
<tr>
<td>China</td>
<td>India</td>
<td>Norway</td>
<td>Ukraine</td>
</tr>
<tr>
<td>Colombia</td>
<td>Indonesia</td>
<td>Panama</td>
<td>United Kingdom</td>
</tr>
<tr>
<td>Czech Republic</td>
<td>Ireland</td>
<td>Poland</td>
<td>United States</td>
</tr>
<tr>
<td>Denmark</td>
<td>Israel</td>
<td>Portugal</td>
<td>Uruguay</td>
</tr>
<tr>
<td>Ecuador</td>
<td>Italy</td>
<td>Qatar</td>
<td></td>
</tr>
</tbody>
</table>

3.6 Anti-avoidance rules

Transfer pricing

Mexican taxpayers engaging in transactions with domestic and foreign related parties are required to charge or pay the prices that would be agreed to between independent parties in comparable transactions, i.e. transactions with related parties must be on arm’s length principle for all transactions. Mexico’s transfer pricing rules generally follow the OECD transfer pricing guidelines.

As discussed in 1.5 above, maquiladora operations must comply with special transfer pricing rules to avoid creating a PE for a foreign principal.

Taxpayers should prepare and retain documents proving that transactions with foreign related parties were agreed using prices that would have been used by independent parties in comparable transactions. Taxpayers also are required to file with their tax returns a detailed information return on transactions with foreign related parties. Penalties apply for failure to comply.

Mexico recognizes six transfer pricing methods:

1. Comparable uncontrolled price method (CUP);
2. Resale price method (RPM);
3. Cost plus method (CPM);
4. Profit split method (PSM);
5. Residual profit split method (RPSM); and
6. Transactional operating margin method (TOPMM).

The methods are hierarchical, that is, starting with the CUP method, there should be an acceptance or rejection of this method, and then the taxpayer may use any other method, provided it can demonstrate that such method was the most appropriate or trustworthy method based on available information.

Transactions within the scope of the transfer pricing rules are financing operations; the provision or receipt of services; the use, enjoyment or transfer of tangible assets, the use or transfer of intangible assets; and stock transfers.

The tax authorities are empowered to verify that transactions with related parties have been executed in accordance with the arm’s length principle, make any necessary adjustments and
request: unpaid taxes; restatement for inflation; interest; and fines that may range between 55% and 75% of the unpaid tax (subject to reduction where documentary requirements are met).

Unilateral and bilateral advance pricing agreements may be negotiated (but transfer pricing documentation still must be kept for five years). Mutual agreement procedures may apply under Mexico’s tax treaties.

**Thin capitalization**

Under Mexico’s thin capitalization rules, interest arising from excess debt from a related party is nondeductible for income tax purposes if the amount of debt exceeds three times the shareholders' equity (i.e. a 3-to-1 debt-to-equity ratio applies).

Although the excess interest is not deductible, it is not reclassified as a constructive dividend. The thin cap rules are not applicable to taxpayers that obtain a favorable APA from the tax authorities, agreeing that the transactions are carried out at market prices, and to financial institutions.

**Controlled foreign companies**

Companies, individuals and resident foreigners must pay tax on all earnings from companies or accounts in low-tax jurisdictions. Foreign-source income is deemed to come from a low-tax jurisdiction if it is not subject to taxation abroad or if it is subject to an income tax that is less than 75% of the income tax computed under Mexican tax legislation. Mexico’s current statutory rate is 30%, thus providing for a 22.5% rate threshold.

Passive income (i.e. dividends, interest, royalties, capital gains, the sale and use or enjoyment of immovable property, and those obtained without consideration) derived directly or indirectly by a Mexican resident through a branch, entity or any other legal entity located in a preferential tax regime will be subject to taxation in Mexico in the year in which the income is derived.

Specific rules apply that permit the nontaxation of active income in certain cases. Taxpayers earning income from a preferential tax regime must file an annual information return in February, as must taxpayers generating income from a jurisdiction on the black list and those that conduct transactions through fiscally transparent foreign legal vehicles or entities.

Payments to a CFC generally are subject to a 40% withholding tax.

Some exceptions to the rules apply.

**General anti-avoidance rule**

The Income Tax Law allows the tax authorities to deem transactions to have occurred between related parties and to calculate the Mexican-source income arising from such transactions. This rule is intended to be applied to counter tax avoidance associated with preferential tax regimes and multinational companies. However, the scope may be broader based on the actual wording of the rule, given that it makes reference to Mexican-source income.

This is the only general substance-over-form rule in the Mexican tax legislation. The Mexican tax regime generally is formalistic and standard Mexican policy has been to provide for specific anti-avoidance rules.

**3.7 Administration**

**Tax year**

The tax year is the calendar year.

**Filing and payment**

Corporate taxpayers must make 12 advance income tax payments on the 17th day of the month. Advance payments are based on the preceding five most recent fiscal years in which a profit could be calculated, even if there was a loss in the immediately preceding fiscal period. All corporations must use the calendar year for financial and tax purposes. Corporations may apply for a reduction in advance payments, although any delay in making advance payments will result in interest charges. Higher charges are applicable for unauthorized delays.

The annual tax return must be filed no later than 31 March of the year following the tax year, with the balance of tax due at that time.
Taxpayers that are required (as an option) to have their financial statements audited by a certified public accountant must file these statements (along with auditor’s opinion on the taxpayer’s compliance with the tax law) by 15 July.

An information tax return that includes information on withholding, donations and salaries, etc. must be submitted to the tax authorities no later than 15 February of each year.

Penalty interest for late payment of tax is assessed at 0.75% per month if an extension has been granted; otherwise the rate is 1.13%. Penalty rates are adjusted monthly.

**Tax integration**

The tax consolidation regime was abolished after 31 December 2013 and consolidated groups are effectively deconsolidated. Affected groups will have to pay deferred income tax in annual installments between the 2014 and 2018 fiscal years. However, taxpayers that are within the mandatory five-year deferral period as of 31 December 2013 can continue to consolidate until the deferral period ends; they will then have to pay the deferred tax using the mechanism established in the transition rules.

An optional "tax integration" regime replaces the consolidation regime, under which corporate groups can elect to calculate income tax on a consolidated basis. The new regime provides certain benefits for payment of tax when companies have profits or losses in the same year within a corporate group. (For tax purposes, a group consists of the Mexican holding company and the subsidiaries in which it has effective direct or indirect ownership interests in excess of 80% of the voting shares.) Tax may be deferred for a maximum of three years.

**Statute of limitations**

The rights of the tax authorities in relation to audit, enforcement, assessment and collection of taxes expire after five years from the date on which the tax return is due. The income tax return initially is filed by 31 March of the year following the taxable year end and the statute of limitations begins on 1 April of each given period. A tax audit report (optional) prepared by an independent certified public accountant is filed by 15 July of the following year. An amended return is filed if there are any differences between the figures used in the tax return and the outcome of the tax audit report.

The statute of limitations will be extended for five (but no more than 10) years as from the date an amended return is prepared for any category of items adjusted in an amended return. The term is 10 years if the taxpayer is not registered with the tax administration, does not maintain accounting records or fails to file a tax return. In the latter case, the 10-year term is computed from the date the return should have been submitted. The statute of limitations is suspended if the taxpayer files an administrative appeal or commences litigation, if the authorities begin an audit of the taxpayer’s accounting records or if the tax authorities are unable to initiate an audit because the taxpayer failed to notify the authorities of a change in domicile.

**Tax authorities**

The SAT (Servicio de Administración Tributaria) is a decentralized agency responsible for assessing and collecting federal taxes and customs duties, while the Departments of Finance of each state or municipality are responsible for collecting state and local taxes. The federal government and the states have entered into agreements for tax coordination and administrative cooperation, with the states now responsible for collecting and auditing the correct payment of federal taxes.

**Rulings**

Taxpayers may petition the tax administration for a (non-hypothetical) ruling in connection with the interpretation of tax provisions in specific cases that are not already under review by the tax authorities.

The authorities must make a decision within three months from the filing of a petition. If no decision is made within this period, the request is deemed denied. Where the request is denied or is deemed denied, the taxpayer may appeal to the Federal Tax Court only for purposes of obtaining the written resolution.
For favorable resolutions issued in writing, the taxpayer is granted the rights in the resolution, but the resolution is not binding on the taxpayer. However, the taxpayer can only contest the favorable resolution after the tax authorities have actually applied it to the taxpayer's situation.

Administrative resolutions concerning the taxation of a specific taxpayer or group of taxpayers are effective only for the period in which they are issued. If the resolution is issued within three months from the end of the tax period, it may be applied for the preceding tax period. At the end of the period for which the resolution remains effective, the interested party must take steps to obtain a new resolution if so desired.

This rule is not applicable to authorizations for deferrals of payments and approvals of guarantees, depreciation allowances and sales of shares that are publicly traded.

3.8 Other taxes on business

Taxation of mining income

The 2013 tax reform created new mining duties on owners of mining concessions and assignments as follows:

- A special mining right royalty of 7.5% will apply to net profits derived by a concession holder from the sale or transfer of the extraction activities. Profits for purposes of the royalty will be determined in a manner similar to the calculation of general taxable income, with some exceptions (e.g. interest and the annual inflation adjustments are not included in income and deductions are not available for investments in fixed assets, interest and the annual inflation adjustment, etc.). The mining royalty must be paid annually by the last business day of March of the year following the tax year.

- If a concession holder does not carry out exploration and exploitation activities for two continuous years within the first 11 years of its concession title, it will be required to pay an additional charge equal to 50% of the maximum fee. The fee will be increased to 100% for continued inactivity after the 12th year. Payment of the additional mining duty is due 30 days after the end of the two-year period.

- Owners of mining concessions also will be required to pay an additional 0.5% tax on gross income derived from the sale of gold, silver and platinum. The mining royalty is due annually by the last business day of March of the year following the tax year.
4.0 Withholding taxes

Mexican entities that make payments to resident individuals or nonresident entities or individuals are required to withhold and pay the tax over to the Mexican tax authorities on behalf of the recipient. Withholding agents must file an annual information return detailing transactions with nonresidents. Tax withheld generally must be paid by the 17th day of the month following the month of the withholding. Withholding agents are jointly liable for the incorrect withholding and/or failure to pay, and may be subject to additional interest and penalties.

4.1 Dividends

As from 1 January 2014, Mexico imposes a 10% withholding tax on dividends distributed by a Mexican entity to a nonresident company or individual. The tax is considered a final tax and the rate may be reduced under an applicable tax treaty.

4.2 Interest

Mexico levies several different withholding tax on interest paid abroad. The rates are as follows:

- A 4.9% rate applies to interest paid to foreign banks registered as banks in Mexico and resident in tax treaty countries; and interest paid to nonresident financing institutions in which the federal government owns a percentage of the paid-up capital, provided certain conditions are satisfied and they are the beneficial owners of the interest. The 4.9% rate also applies to interest paid in respect of publicly traded securities in Mexico and securities publicly traded abroad through banks and stockbroking firms in a country that has concluded a tax treaty with Mexico; however, if these conditions are not satisfied, the rate is 10%.

- A 15% rate applies to interest paid to reinsurance companies and interest on finance leases.

- A 21% rate applies to interest that is not subject to the 4.9% or 10% rates and interest paid to nonresident suppliers financing the acquisition of M&E that is included in the fixed assets of the acquirer.

- 40% where interest is paid to a related party located in a tax haven.

- 35% in all other cases.

4.3 Royalties

Payments made abroad for technical assistance, know-how, use of models, plans, formulas and similar technology transfer, including use of commercial, industrial or scientific information or equipment, are subject to a 25% withholding tax. Royalties paid to a foreign licensor of patents, trademarks and trade names—without the rendering of technical assistance—are subject to a 35% withholding tax, unless the rate is reduced under an applicable tax treaty.

Business enterprises that pay fees or make rental payments to a nonresident must withhold a 25% tax on such payments. An information statement must be submitted to the tax authorities in February of the following year.

Mexican-source royalty payments made to related parties located in a tax haven are subject to a punitive 40% withholding tax rate rather than the normal withholding tax rates applicable to payments abroad.

4.4 Branch remittance tax

Permanent establishments distributing dividends or gains to its head office are subject to an additional tax of 10% over such dividends or gains.

4.5 Wage tax/social security contributions

Payroll taxes apply at the state level at rates ranging between 1% and 3% of salaries (2.5% in Mexico City); such tax is withheld by the employer. All types of remuneration paid to an employee,
including fringe benefits that are not tax free, must be taken into account in calculating the monthly income tax withholding.

Some local tax authorities also require withholding on payments for personal independent services rendered in their territory where the service provider is not registered as a taxpayer and is domiciled outside the territory. The tax is deductible for income tax purposes.

Employers must contribute an amount equivalent to 2% of payroll to an employee retirement fund and 5% of the total payroll to a housing fund (which will be added to the retirement fund if not used for a housing credit) that, together, constitute a pension fund managed by private financial institutions.
5.0 Indirect taxes

5.1 Value added tax

VAT is levied on the supply of goods, the provision of services, the import of goods or services and leasing transactions. Interest on non-business loans and credit card debt also are subject to VAT.

The standard VAT rate is 16%; VAT on imports is assessed on the customs value of the import, plus the import duty. The 2013 tax reform eliminated the reduced VAT rate of 11% on activities carried out in the border zone. A zero rate applies to exports and services used abroad if the services are contracted and paid by a nonresident with a PE in Mexico. The following supplies are exempt: land and residential buildings; books and newspapers; share transfers; used chattels; tickets and other documentation permitting participation in lotteries, raffles, games of chance and competitions; national and foreign currency and gold and silver pieces; and the alienation of goods among nonresidents or by a nonresident to a Mexican entity registered in an authorized program to promote the export of goods.

Special customs rules are applicable to maquiladoras that enable the sale of goods between nonresidents at an exempt VAT rate when the goods are delivered from one maquiladora to another maquiladora, following certain customs formalities to virtually export the goods. Before the 2013 tax reform, it was possible to apply the exempt treatment when goods were sold by a nonresident and delivered to another maquiladora following the virtual export rules. However, now there is a VAT withholding obligation on the purchasing entity.

Companies may credit VAT payments against income or other tax payments; if the excess cannot be credited in its entirety, the taxpayer may apply for a refund.

Under the VAT regime, each party in the chain of production charges VAT to its customer and pays the difference between the tax charged by its suppliers and the tax charged to its customers to the tax authorities. VAT is borne by the ultimate consumer.

Since export activities are zero-rated, exporting companies may derive favorable VAT balances that are subject to refund/offset.

Companies must submit a VAT return on a monthly basis, making the VAT payments for the preceding month, by the 17th day of the month. Additionally, an annual VAT return also must be submitted with the annual income tax return. For imports, VAT is based on the customs value plus tariffs.

VAT taxpayers must, periodically, submit information on main clients, service providers and suppliers.

All entities engaging in VATable transactions in Mexico must register for VAT purposes. Nonresident entities that have a PE in Mexico for income tax purposes, also must register.

Mexico does not allow VAT grouping.

5.2 Capital tax

Mexico does not levy capital tax.

5.3 Real estate tax

The municipal authorities levy “rates” on the ownership of real property. Rates are deductible in calculating corporation tax liability.

5.4 Transfer tax

A rate between 2% and 5% applies to the transfer of real estate.

5.5 Stamp duty

Mexico does not levy stamp duty.
5.6 Customs and excise duties

Customs duties arise on the import or export of goods according to the following:

- General Import Tax – Determined according to the tariff classification number of the goods;
- Customs Processing Fee – Paid for using the Customs facilities and its personnel and systems, etc.;
- VAT – At a rate of 16% on import and 0% on export; and
- Special Tax on Production and Services – See below under 5.7 and 5.8.

The treatment of goods imported into Mexico and the tax and customs obligations are determined based on the purpose of the foreign trade transaction. These purposes are classified into five customs regimes for imported goods: definitive; temporary; transit of goods; fiscal deposits “in bond”; and strategic bonded warehouse.

As noted above, Mexico has concluded a number of FTAs and has introduced the PROSEC and IMMEX regimes.

PROSEC aims to encourage the manufacture of products in Mexico within strategic industrial sectors, with the main objective of improving competitiveness. PROSEC basically enables the import of specific goods (e.g. components, parts, raw materials, capital assets, etc.) and application of listed preferential general import duty rates, provided these are used only in the manufacturing process, without any condition of the origin or export.

The IMMEX regime also was created to encourage foreign investment by granting authorized companies certain tax and customs benefits, which include:

- Possible deferral of the general import duty, and in some cases exempt;
- Administrative and customs benefits to facilitate operations and reduce costs; and
- Tax benefits (see above under 1.5).

Under the IMMEX program, a 16% VAT is paid on imports. However, a maquila company can avoid paying the VAT/excise tax upon import by obtaining certification from the Mexican tax authorities. If a maquiladora is certified, VAT technically will be imposed on goods imported for use in maquila production activities, but will be eliminated by a full tax credit so that no cash VAT will be imposed on such transactions. If the maquiladora cannot obtain certification, it will be able to satisfy its liability for VAT/excise duty on temporary imports by providing security via a bond issued by an authorized entity.

5.7 Environmental taxes

The 2013 tax reform introduced a new environmental tax on the import and sale of fossil fuels other than natural gas, with specific rates for certain types of fuel. The tax will be payable through carbon credits, which are defined as those authorized in the Kyoto Protocol and supported by the UN within the UN Framework Convention on Climate Change. A second environmental tax applies to the import and sale of pesticides at rates ranging between 6% and 9%, depending on the degree of toxicity. Reduced rates between 3% and 4.5% apply for calendar year 2014.

5.8 Other taxes

Tax on production and services

A tax on production and services is charged on manufacturers and wholesalers of certain goods, including alcoholic beverages and tobacco. The rates vary by product.

“Junk food” tax

A tax is levied on beverages containing sugar at a rate of MXP 1 per liter and an 8% tax is imposed on food with a calorific density of 275 kilocalories or more for every 100 grams.
6.0 Taxes on individuals

<table>
<thead>
<tr>
<th>Mexico Quick Tax Facts for Individuals</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Income tax rates</strong></td>
</tr>
<tr>
<td><strong>Capital gains tax rates</strong></td>
</tr>
<tr>
<td><strong>Basis</strong></td>
</tr>
<tr>
<td><strong>Double taxation relief</strong></td>
</tr>
<tr>
<td><strong>Tax year</strong></td>
</tr>
<tr>
<td><strong>Return due date</strong></td>
</tr>
<tr>
<td><strong>Withholding tax</strong></td>
</tr>
<tr>
<td>- Dividends</td>
</tr>
<tr>
<td>- Interest</td>
</tr>
<tr>
<td>- Royalties</td>
</tr>
<tr>
<td><strong>Net wealth tax</strong></td>
</tr>
<tr>
<td><strong>Social security</strong></td>
</tr>
<tr>
<td><strong>Inheritance tax</strong></td>
</tr>
<tr>
<td><strong>Real estate tax</strong></td>
</tr>
<tr>
<td><strong>VAT</strong></td>
</tr>
</tbody>
</table>

6.1 Residence

An individual is resident if he/she has a permanent home in Mexico. If an individual has a home in two countries, the key factor is the location of his/her center of vital interests. Foreign nationals, in principle, are considered tax residents, subject to the permanent home and/or center-of-vital-interests test.

In terms of the immigration law, foreign nationals permanently residing in Mexico enjoy the same rights as citizens (absent the right to vote) and incur the same responsibilities. Permanent Resident status may be obtained after residing in Mexico for five years, which is completely different to tax status.

6.2 Taxable income and rates

Resident individuals (regardless of their nationality) are subject to Mexican income tax on their worldwide income. Nonresident individuals are taxed only on Mexican-source income.

**Taxable income**

Individuals are taxed on income received in cash, in kind or credit, and in certain cases, in services. Taxable income includes remuneration for personal services (including salary, bonuses and special allowances, such as housing), interest, corporate dividends paid out of gross income, capital gains, rental income, etc. Pension benefits are tax-exempt up to nine times the legal minimum salary for the region. Severance payment benefits are exempt up to 90 times the daily base salary of the region multiplied by the number of years employed.

Individuals with business or professional income are subject to ordinary income tax rates, and the individuals may deduct their normal business expenses according to the rules similar to those for business enterprises.

In calculating capital gains for tax purposes, individuals increase the historical cost by a factor to for inflation and reduce the cost by accumulated depreciation at a rate varying with the type of asset. The difference between the result and the selling price constitutes the net gain.
the number of years the asset was held, a certain proportion of the net gain is added to other taxable income to determine the top tax rate payable.

Capital gains arising from an individual’s sale of publicly traded shares, including financial derivative operations relating to such shares, are taxable.

Some states and the federal district impose separate taxes on wages and salaries, which are usually an employer tax liability.

**Deductions and reliefs**

The following expenses are deductible in computing personal income tax:

- Medical and dental fees and hospital expenses incurred by the taxpayer and the taxpayer’s spouse or other dependents with income no higher than the annual minimum salary;
- Health insurance premiums and charitable donations;
- Mortgage interest payments (real interest) when mortgage credit is up to 750,000 investment units or UDIS;
- Personal pension account contributions up to five minimum annual salaries; and
- School transportation expenses of direct descendants, when such transportation is mandatory under domestic law.

All personal deductions are limited to the lowest amount between the amount of four annual minimum salaries or 10% of the total income (taxable and nontaxable).

Taxpayers whose income consists of professional fees may deduct normal and documented expenses, similar to those deductible by businesses. A simplified tax system for individual taxpayers that engage in business activities is available.

**Rates**

The personal income tax rates are progressive up to 35%. Employers withhold provisional tax payments on wage income.

Dividends received by an individual are cumulative to other taxable income utilizing progressive rates as stated before.

Capital gains arising from an individual’s sale of publicly traded shares, including financial derivative operations relating to such shares, are subject to a 10% tax on the gains.

Nonresidents on temporary assignment working for firms or subsidiaries based in Mexico are exempt from income tax on the first MXP 125,900 for a period of 12 months; they are taxed at 15% on income of MXP 125,901 to MXP 1 million. All income exceeding MXP 1 million is taxed at 30%, with no deductions allowed. Nonresidents on temporary assignment that are paid by nonresident foreign firms are exempt from income tax if the employee spends less than 183 days (consecutive or not) in Mexico in a 12-month period. Otherwise, the employee will be subject to tax. Taxes paid as a nonresident are considered final and there is no obligation to file annual tax return.

**6.3 Inheritance and gift tax**

Mexico does not levy inheritance or gift tax.

**6.4 Net wealth tax**

Mexico does not levy a net wealth tax.

**6.5 Real property tax**

The municipal authorities levy “rates” on the ownership of real property. Rates are deductible in calculating the individual’s taxable income applicable to leasing of real property.

**6.6 Social security contributions**

Employed individuals are required to make social security contributions, with the amount based on the individual’s salary with a ceiling up to 25 times the daily minimum wage salary of the region.
6.7 Compliance

The tax year for resident individuals is the calendar year. The tax year for nonresidents who pay income tax on Mexican-source compensation is the 12-month period that commences with the first month the nonresident is subject to tax.

Married individuals may not file a joint tax return; each spouse must file a separate return if both spouses have taxable income.

Tax on employment income is withheld by the employer and remitted to the tax authorities. Income not subject to withholding is self-assessed; the individual must file a monthly tax return by the 17th of the following month. An annual tax return must be filed during the month of April of the following year.
7.0 Labor environment

7.1 Employee rights and remuneration

Mexico’s labor legislation is set forth in the Federal Labor Law and the constitution. This legislation regulates labor contracts, minimum wages, hours of work, legal holidays and paid vacations, among other working conditions, as well as labor unions, strikes and dismissal compensation, as well as subcontracting.

Regulations issued by the Ministry of Labor and Social Welfare outline allowable workplace practices with a focus on assessing risk, preventing accidents and educating workers on potential hazards. The safety regulations emphasize self-regulation and allow private sector “certifiers” to conduct safety inspections.

Working hours

The work week consists of six eight-hour days for the day shift, seven-hour days for the night shift and seven and a half-hour days for a mixed shift, with a half-hour break in all cases. For every six-day work period, a worker is entitled to one day of rest with full pay. (Wages are calculated on a seven-day week.) Overtime is paid at twice the normal rate and may not exceed nine hours per week. Additional weekly work hours are forbidden and must be paid at triple the normal rate. Workers receive a 25% premium for Sunday work.

7.2 Wages and benefits

The National Minimum Wage Commission, a tripartite group, comprising representatives of business, labor and government, sets a two-tiered minimum wage (reflecting Mexico’s two main regions). Minimum wage increases have varied in size and frequency.

An average minimum wage hike of 3.9% was approved for 2014. The variable increase is an attempt to equalize wages throughout the country, with the lowest percentage for Mexico City employees (since they receive the highest wages). The minimum wage is subject to a premium (often 60%-70%) for mandatory fringe benefits and premiums for work considered hazardous. Actual industry wages are higher than the legal minimum. Often, a salary of two to three times the minimum wage is considered acceptable in many industries.

The overall burden of fringe benefits is substantial as the costs are frequently in excess of 70%-100% of payroll, depending on salary levels. A relevant employee benefit is profit sharing, under which all firms must distribute 10% of their pretax profits to employees (some exceptions apply in case of partnerships).

Pensions

Employee remuneration that represents an exempt item of income for the employee, such as fringe benefits, employees’ savings and loan funds, severance payments, annual bonus, overtime, vacation premium, Sunday premium and exempt portion of employee profit sharing, may be deducted for income tax purposes only up to 53%. If an employer decreases such items of employee compensation, the deductibility threshold will be reduced to 47%.

Social insurance

The social security system, administered by the Social Security Institution, provides many benefits. Its programs cover work-related accidents and illness; non-occupational diseases and paid maternity leave; old age and various death benefits; and unemployment insurance. The cost of the system is shared among employers, employees and the government. The employer generally picks up most of the cost, with its share roughly totaling 20% to 30% of payroll.

Other benefits

The labor legislation grants seven paid holidays annually, plus one for inauguration day every sixth year. Labor contracts call for another nine to 10 paid holidays. After working for a year, employees are entitled to at least six days’ paid vacation, increased by two days for each of the subsequent three years. A bonus of 25% of normal pay during the vacation period is mandatory. A Christmas
bonus of 15 days’ pay also is obligatory and must be paid before 20 December. Companies must contribute a sum equal to 5% of payroll to the national workers’ housing institute (Infonavit); funds go into special accounts for employees.

Companies with more than 100 employees must maintain a fully equipped infirmary under the direction of a qualified doctor; firms with more than 300 employees must establish hospital facilities. A mandatory worker-training program has added to employer costs.

In addition to the mandatory fringe benefits, most labor contracts provide for such “voluntary” benefits as savings plans, life insurance, lunches and vales de despensa (redeemable for food and general merchandise at supermarkets). Most large companies maintain a cafeteria on the premises that provides below-cost meals to employees. Many companies supply work clothes. Some employers set up additional incentive plans to stimulate production and sales. To qualify for tax deductions, fringe benefits must generally be provided to all employees.

7.3 Termination of employment

Unless dismissed for cause (such as dishonesty or excessive absenteeism), laid-off employees are entitled to three months’ pay, plus 20 days’ additional pay for every year employed. Workers employed for more than 15 years receive an additional 12 days’ pay for every year of service, up to a ceiling of twice the minimum wage at the time of dismissal multiplied by 12 days and the number of years. An employee who wins a dismissal appeal receives full pay from the date of termination until the matter is judicially resolved.

Unjustifiably dismissed workers may choose between reinstatement and indemnification amounting to three months’ severance pay. Employers may refuse to reinstate apprentices and workers with less than one year of service, but they must then add 20 days of pay for each year of service to the standard three months’ severance pay or pay half the time worked, if less than a year.

7.4 Labor-management relations

Nearly 40% of Mexico’s workforce is unionized; unions represent some 80% of industrial workers in establishments with more than 20 employees. Most of these employees belong to one of the nine national labor federations. Only about 20% of unionized workers belong to single-company unions; the remainder are members of nationwide organizations. Federal law requires that collective bargaining agreements be renewed at least once every two years. Salaries must be reviewed annually.

Strikes are legal only when employers refuse to comply with a legal or contractual obligation (e.g., to make or revise a union contract, to accept an award by an arbitration board or to make mandatory profit-sharing payments). A strike also may be called to support another strike, provided the majority of workers agree. Unions must follow specific procedures in instituting job actions.

7.5 Employment of foreigners

Under NAFTA, and as part of a nationality law, Mexico has agreed to permit temporary entry to four categories of non-Mexican North Americans: business visitors; traders and investors; intracompany transferees; and certain other professionals. The three NAFTA signatory countries also have agreed to provide access to nationals who hold professional licenses (e.g. lawyers, doctors and accountants).

The federal labor law requires that at least 90% of a company’s skilled and unskilled workers be Mexican nationals. A special provision permits temporary employment of foreign technicians (up to 10%) if a company can prove that skilled workers are not available locally. The 10% limit does not apply to managers, directors and other key officers, who must secure special immigration permits. Operations along the border with the US are exempt from the personnel requirements.
Mexico has several categories of immigrants, but the following are of special interest to foreign investors:

- **Cargo de confianza** (management employee) status may be obtained by foreigners who fill key executive posts or other positions of responsibility in established corporations or institutions. The Ministry of the Interior will grant such status only if it is satisfied that the work is necessary and cannot be performed by a local national. Companies should apply for this status well in advance, since the process may take several months. Occasionally, a foreigner may qualify for initial non-immigrant status, which may subsequently be amended to immigrant status upon re-entry into the country.

- **Inversionista** (investor) status may be obtained by foreigners who invest in industrial activities that contribute to the economic and social development of the country. The one-year visa may be renewed up to four times and allows for multiple entries.

- **Técnico** (technician) status may be granted to persons who undertake research, technical or other specialized activities for which no qualified residents are available.

Mexico provides immigrant status for scientists, professionals, persons with independent income, dependants of immigrants, permanent immigrants and retirees. Generally, to obtain immigrant status for employees, a company must file an application with the Ministry of the Interior and submit evidence of investment and tax payment. Some Mexican consulates grant visas directly, waiving filing requirement with the Ministry.

In general, a new company may not apply for permanent residence visas for its personnel unless the government considers its activity of importance to the nation and it has been operating for two years. If approved, the permit is granted provisionally for five years and reviewed every year.
8.0 Deloitte International Tax Source

The Deloitte International Tax Source (DITS) is a free online database that places up-to-date worldwide tax rates and other crucial tax information within easy reach.

Connect to the source and discover:

A database that allows users to view and compare tax information for 65 jurisdictions that includes –

- Corporate income tax rates;
- Historical corporate rates;
- Domestic withholding tax rates;
- In-force and pending tax treaty withholding rates on dividends, interest and royalties;
- Indirect tax rates (VAT/GST/sales tax); and
- Information on holding company and transfer pricing regimes.

Guides and Highlights – Deloitte’s Taxation and Investment Guides analyze the investment climate, operating conditions and tax systems of most major trading jurisdictions, while the companion Highlights series concisely summarizes the tax regimes of over 150 jurisdictions.

Tax publications – Global tax alerts and newsletters provide regular and timely updates and analysis on significant cross-border tax legislative, regulatory and judicial issues.

Tax resources – Our suite of tax resources includes annotated, ready-to-print versions of holding company and transfer pricing matrices; a summary of controlled foreign company regimes for the DITS countries; an R&D incentive matrix; monthly treaty updates; and expanded coverage of VAT/GST/Sales Tax rates.

Webcasts – Live interactive webcasts and Dbriefs by Deloitte professionals provide valuable insights into important tax developments affecting your business.

DITS is free, easy to use and readily available!

http://www.dits.deloitte.com
9.0 Office locations

To find out how our professionals can help you in your part of the world, please contact us at the offices listed below or through the “contact us” button on http://www.deloitte.com, or visit the Deloitte Mexico website at http://www2.deloitte.com/mx/es.html

**Mexico City**
Paseo de la Reforma 489 – 6
Col. Cuauhtémoc
06500 México, D.F.
Tel: (55) 5080 6000