

August 30, 2005

Mexican Fiscal Update 1/2005

Fourth Modification to the Miscellaneous Tax Resolution for 2005

Today came into effect the Fourth Resolution of Modifications to the Miscellaneous Tax Resolution for 2005 ("Resolution") as published in the Federal Official Gazette ("Gazette") on August 29, 2005.

It should be born in mind that legally speaking, the Rules constitute interpretations and/or criteria of the Mexican tax authorities associated with legal tax provisions, and are not binding for the taxpayers. However, (i) their content may be rightfully taken by same taxpayers since same Rules grant rights, and (ii) they contain the construction of the tax provisions taken by the Mexican tax authorities.

In our opinion, certain rules ("Rules") have relevance in the international tax context to which we subsequently refer to:

1.- Business profits concept (Rule 2.1.1). It provides that for purposes of double tax treaties, the "business profits" concept shall be referred to the revenues derived from the performance of the entrepreneurial activities to which the Federal Tax Code refers.

In our perspective, this rule alleviates the reform made to Article 210, Section VI of the Income Tax Law which apparent intent is to limit the application of double tax treaty benefits.

2.- Corporate reorganizations (Rule 3.21.16). It establishes the possibility for non residents that are subject to preferential tax regimes (commonly named as "tax havens") that transfer shares issued by Mexican resident entities (or issued by non resident entities which accounting value derives in at least 50% from realties located in Mexico) within the same corporate group, of deferring the income tax whenever the following requirements are met:

(a) the transferee does not reside in a country or jurisdiction in which the income is subject to a preferential tax regime and with which Mexico has executed an exchange of information agreement;

(b) the transferor submits a writ with the Mexican tax authorities to authorize foreign tax authorities to furnish to the first mentioned authorities information regarding the transaction;

(c) the authorization for such transfer issued by the Mexican authorities is subject to the condition precedent of an actual exchange of tax information as established under (b).

This is a benefit, since the law does not allow foreign residents subject to preferential tax regimes to apply this tax deferral in corporate reorganizations. However, it appears troublesome from a factual perspective how the transferor may “authorize” foreign tax authorities to furnish tax information to the Mexican tax authorities.

On the other hand, a downside of this facility is to be subject to an actual exchange of information in which the taxpayer has no influence.

3.- Repatriation decree (Rules 16.2., 16.3. and 16.4). On January 26, 2005, a Presidential Decree (“Decree”) was published in the Gazette, establishing certain tax incentives for the payment of taxes with respect to foreign investments held by Mexican residents. Now, certain rules are included in the Resolution regulating the Decree’s scope.

(a) Capital repatriation (Rule 16.2). It establishes the cases under which it shall be deemed that the repatriated funds do not diminish their amount in the 3 (three) year period in which they need to be invested in Mexico subsequent to their actual repatriation.

(b) Financial securities or shares issued by Mexican resident companies (Rule 16.3). It provides that the repatriated resources need to be invested in (i) publicly traded bonds and/or securities –during the before mentioned 3 year period-, or (ii) in private companies, provided that they destine such resources to the acquisition of fixed assets, research and development of technology, or payment of liabilities with related parties acquired prior to January 27, 2005.

(c) Informative tax return (Rule 16.4). It sets forth alternatives for the extemporary compliance with the informative tax return derived from the tenure of investments in tax havens before 2005.

Should you have any comments, doubts or commentaries on the foregoing preliminary analysis, please contact us either at the phone number (52 55)52513545 or at the e-mail address info@turanzas.com.mx

Sincerely,

Turanzas, Bravo & Ambrosi
Abogados Tributarios

www.turanzas.com.mx

This document constitutes a preliminary analysis with informative purposes which has been prepared by the members of Turanzas, Bravo & Ambrosi. In no manner it intends to be an opinion or a definite position for particular cases, same that will have to be analyzed under their specific circumstances.