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## MEXICAN FISCAL UPDATE 4/2009

### Tax Reforms Initiative for 2010

On September 8<sup>th</sup> of the present year, the Mexican President submitted before the Mexican Congress a bill of reforms to several tax laws. Following please find a brief practical analysis of some of the salient issues contained therein, which are relevant to the majority of our clients.

These initiatives will surely suffer modifications during the legislative process, which should conclude on the 15<sup>th</sup> of November, as per constitutional mandate.

### INCOME TAX LAW

**1. Rate and tariff increase.** The Initiative proposes to increase the corporate income tax rate applicable to entities and the tariff applicable to individuals, from 28% to 30% during the 2010, 2011 and 2012 fiscal years.

**2. Definitive withholding for interest.** It is proposed that since 2011, financial institutions carry out a monthly withholding of real interests earned by entities and individuals, applying a 30% rate. This withholding would be deemed as a definitive payment.

According to the Initiative, this would provide a simple procedure in order to determine and pay IT over interest.

**3. Tax consolidation.** The Mexican President proposes that the IT differed due to the consolidation in income tax matters, be limited to a period of five fiscal years. Once this period has expired, taxpayers will be bound to pay 60% of the differed tax on the sixth year, and the rest over the next four years (10% per year).

Accordingly, the Initiative provides that those taxpayers that have been in the fiscal consolidation regime since before 2005 and until December 31, 2009, will have to pay 60% of their differed tax balance during the fiscal year of 2010 and the remaining balance over the next four years, according to the procedure previously mentioned.

**4. Non-profit institutions.** It is suggested that non-profit institutions are taxed for the alienation of goods different from their fixed assets or for the rendering of services to persons different from their membership, when such activities exceed 5% of the total income of such entities.

Likewise, when those institutions obtain income from activities other than those authorized by the tax authorities that exceeds 10% of their total income, they will have to determine the corresponding IT for the exceeding amount.

It is suggested, that non-profit institutions file a new annual informative return.

The Initiative provides that donations made to international organizations will be deductible, as long as the organization's objectives coincide with the activities listed in the IT Law.

5. **Alienation of dwelling house.** The Executive Branch proposes to limit the exemption for Mexican resident individuals who alienate their **dwelling house** (up to an amount of approx. USD \$460,000), to one event every five years.
6. **Deduction of interest derived from mortgage loans.** The Initiative contemplates limiting the deduction of interests derived from mortgage loans, to those related to the acquisition of the taxpayer's household and as long as the total financed amount does not exceed approx. USD \$460,000.
7. **Tax incentive for investigation and development of technology.** The Initiative provides for the elimination of the tax incentive for expenses and investments made in projects for investigation and development of technology, given that as of 2009 funds from the Federal Budget are being awarded to these types of projects.

#### CASH DEPOSITS TAX LAW

1. **Rate and amount of the exemption.** The tax rate would be increased to 3% and the amount of the exemption would be reduced to MXP \$15,000 (approx. USD \$1,150), per month for all cash deposits made in the taxpayer's bank accounts in each institution.
2. **Exemption for payment of debts.** The Executive Branch proposes that the exemption for cash deposits made for purposes of payment of debt, is limited solely to individuals, with the exception of those who are taxpayers under the entrepreneurial and professional activities regime (including the intermediate and small taxpayer regimes)

#### FEDERAL FISCAL CODE

1. **Tax domicile.** The tax domicile of entities could also be considered that of their legal representative, aside of where its effective place of management is located.

The notices of change of domicile would only produce effects when the new domicile is materially proved.

2. **Exercise of powers to review.** Important changes are proposed for the exercise of powers to review:
  - a) Supplementary returns for years prior to the one currently under review will not produce effects when the taxpayer files them after the review procedure has been initiated.
  - b) The tax authorities may notify the initiation of their powers to review with any person located in the fiscal domicile, without leaving a citation. The above, in order to secure the accounting records on that same day.
  - c) The tax authorities may issue the conclusion of the review procedure, without the requirement of leaving citation for the taxpayer or its legal representative.
  - d) It is suggested that the time periods set to conclude review procedures, should be suspended when notices of change of fiscal domicile are filed, and until the tax authority notifies the taxpayer of the substitution of authority resolution.
  - e) When a taxpayer changes its fiscal domicile in two or more occasions in one same tax year, the term for the extinction of the tax authorities powers to review, could be extended to 10 years.
3. **Fiscal invoices / vouchers.** In order to stimulate the use of digital invoices, certain changes to the procedures for their issuance, are proposed. Through such changes, the tax authorities will provide

the necessary software in order to issue such invoices, free of charge. It is suggested, that this reform enters in force until July 1<sup>st</sup>, 2010.

New security measures to fiscal invoices issued in paper, are suggested in the Initiative.

Bank statements for service cards as well as electronic bank statements, will be considered as fiscal invoices, without the need for additional documentation.

**4. Tax crimes.** The falsification and reproduction of fiscal invoices, the commercialization of such falsified or reproduced documents, as well as giving tax effects to apocryphal invoices, are proposed to be considered as tax crimes.

**5. Administrative collection procedure.** Changes to the administrative collections procedure are proposed, in order for the tax authority to secure the collection of tax credits, some of which are: *(i)* the elimination of the conditions that limit the joint and severable liability of shareholders or partners that no longer have such quality, regarding the taxes triggered by the entity; *(ii)* the increase in the tax authority's powers to review, in order to obtain information from several other financial institutions, including information contained in the taxpayers' bank statements; *(iii)* precautionary securing goods and the use of public force, in case there is opposition in the exercise of powers to review; and *(iv)* financial institutions may immobilize bank deposits, investment accounts and financial products of taxpayers and the secured funds may be transferred to the Federal Treasury.

#### CONTRIBUTION TO COMBAT POVERTY LAW

**1. General aspects.** The CCP is established in order to tax, at a 2% rate, the same persons and activities provided in the VAT Law; that is, over the following activities carried out in Mexico: the alienation of goods, rendering of services, temporary use or enjoyment of goods and import of goods and services.

It is noteworthy that, except some cases (gold, jewelry, etc. and some exported goods and services), all activities taxed by a 0% VAT rate, will be subject to this new tax created.

As it can be derived, this new tax is by its nature, a new VAT.

**2. Differences in exemptions.** Notwithstanding that these are deemed as VAT exempted activities, the following would constitute CCP taxed activities:

- a) Alienation of goods: *(i)* Constructions destined for housing, *(ii)* books, newspapers and magazines, and *(iii)* lottery tickets, raffles and sweepstakes.
- b) Rendering of services: *(i)* Commissions and considerations for granting mortgage loans for housing, *(ii)* commissions related to retirement funds (*AFORES*), *(iii)* teaching services, *(iv)* public ground transportation for persons, *(v)* insurance for agricultural activities, housing credits, financial guarantees and life, as well as the corresponding commissions, *(vi)* interest derived from VAT exempt or 0% rate transactions, and *(vii)* interests derived from mortgage loans.
- c) Temporary use and enjoyment of goods: *(i)* Real estate destined for housing, *(ii)* land destined for agricultural or live stock purposes, and *(iii)* tangible goods that have been leased (or similar) by foreign residents, that paid VAT upon import.
- d) Import of goods and services: Goods alienated or services rendered that do not trigger VAT or are subject to a 0% rate.

**3. Export of goods and services.** Similar to the VAT Law, a 0% rate applies to the alienation of goods and rendering of services considered as exported under the VAT Law. However, it is suggested that such treatment is not be applied to: *(i)* filming or recording services, *(ii)* call centers, and *(iii)* lodging related services.

#### EXCISE TAX LAW

**1. Alcoholic beverages.** In addition to the *ad valorem* scheme, it is proposed that importers and producers of alcoholic beverages pay a specific quote of MXP \$3.00 (approx. USD \$0.23 cents) per liter for those beverages with an alcoholic content of 20° G.L. The monthly payment will be obtained from applying the corresponding quota to those goods alienated during the month, diminished by the tax paid upon import.

Through a transitory provision, it is provided that alienations of alcoholic beverages carried out in 2009 and paid in 2010, will trigger the excise tax according to the new provisions, that is, applying the new specific quotas. The above, will not apply if the merchandise is delivered prior to January 1<sup>st</sup>, 2010 and if payment is done during the first 10 days of 2010.

**2. Beer.** A temporary increase of the applicable rate for alienation or import of beer is proposed. The rate is increased to 28%, for the fiscal years of 2010, 2011 and 2012. For 2013 the rate will be reduced to 27%, returning to the actual rate of 25% in 2014.

**3. Tobacco.** In addition to the *ad valorem* system, a new quota of MXP \$0.1333 (approx. USD \$0.01 cent) per gram of tobacco, is being suggested. Through transitory provision, the quotas per gram applicable will be MXP \$0.0533 (2010), MXP \$0.800 (2011) and MXP \$0.1067 (2012).

**4. Games and sweepstakes.** Regarding the applicable regime for betting games and sweepstakes, the Initiative proposes to increase the applicable tax rate to 30% (instead of the 20% rate applicable in 2009).

Additionally, a provision is added by which it will be compulsory to keep the following computing systems: *(i)* central betting system, which registers that totals the transactions carried out; and *(ii)* cash register control system, which registers the amounts effectively received.

The systems will require information to be provided to the tax authorities, online and in real time.

Breaching any of the abovementioned obligations will be sanctioned with closure of the establishment, for one or two months.

**5. Telecommunication services.** Services provided in Mexico through one or more public telecommunication networks will be taxed with an *ad valorem* rate of 4%.

The following services are exempt from this tax; *(i)* rural telephony, *(ii)* public telephony; and *(iii)* interconnection services.

**6. Payment through checks and other credit documents.** A new provision is added to establish that for purposes of the excise tax, considerations are to be regarded as effectively paid in the same cases established in the VAT Law.

#### FEDERAL REVENUES LAW FOR THE FISCAL YEAR OF 2010

**1. Interest paid to financial institutions.** The Executive Branch proposes that the withholding IT rate for interest paid by financial institutions is reduced to 0.60% over capital, different from the 0.85% rate applicable in 2009.

**2. Tax credit for superior deductions from income in IETU.** The Initiative prohibits taxpayers to apply the aforementioned credit against the IT triggered in the same fiscal year. In this sense, the credit could only be taken against the IETU for future years and its provisional payments.

According to the Mexican President, applying this credit against the IT (as it is provided in the IETU Law) is contrary to the nature of IETU, as it would cease to be a minimum tax, and even diminish the revenue obtained from IT payments.

#### Abbreviations

*CCP	(contribution to combat poverty –	<i>contribución para el combate a la pobreza)</i>
*IETU	(single rate business tax –	<i>impuesto empresarial a tasa única)</i>
*IT	(income tax –	<i>impuesto sobre la renta)</i>
*VAT	(value added tax –	<i>impuesto al valor agregado)</i>

Should you have any comment or doubt related with the content of this preliminary analysis, please contact us in the e-mail address [info@turanzas.com.mx](mailto:info@turanzas.com.mx)

Sincerely,

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