

January 11, 2010

MEXICAN FISCAL UPDATE 2010

Tax Reforms for 2010

On November 25 and 27, as well as on December 7 of 2009, the Tax Reform for the fiscal year of 2010 was published in the Official Gazette of the Federation. Such reform comprehends modifications to IT, VAT, IETU, excise tax and cash deposits tax, among others. Most of the enacted reform is in force since January 1, 2010.

Following please find a brief practical analysis of some of the salient issues contained therein, which are relevant to the majority of our international clients.

INCOME TAX

1. Domestic transactions. There are two main changes in the IT Law concerning residents in Mexico:

- a) The corporate IT rate is increased to 30% during the next 3 years (2010-2012). The tariff for individuals is also increased to a maximum 30% rate, applicable to the highest bracket.
- b) As of 2011, IT withholding on interest performed by financial entities will be determined based on real interest (interest minus inflation) received by taxpayers.

2. Non-profit institutions. Among other changes, donations made to international organizations of which Mexico is a member, will be deductible as long as the organizations' objectives coincide with those activities listed in the IT Law for non-profit entities.

3. Alienation of shares by financial entities in which the Mexican Government participates. The Mexican Federal Government participates in the capital of some non-resident financial entities. Such entities, may calculate the IT triggered for the alienation of shares, based on the gain obtained on such transactions.

4. Alienation of shares of Debt and Variable Income CIVs. Part of the gain obtained by non-Mexican residents for the alienation of shares of Debt CIVs or Variable Income CIVs is deemed as interest for tax purposes.

There are new rules to determine the gain considered as taxable interest, that are based on the proportion of taxable debt securities in the CIVs' portfolio. Said calculation and withholding is in charge of the entity that distributes the CIVs shares.

On the other hand, the CIVs will determine the gain obtained by non-Mexican residents for the gain obtained from the alienation of shares of CIVs with respect to their taxed equity portfolio. The procedure in order to determine such gain is similar to the one previously mentioned, however, the CIV will be bound to withhold and pay the tax.

These modifications will enter in force on January 1st, 2011.

5. **Debt derivative transactions.** With the objective of granting full effectiveness to the manner in which IT is determined over debt derivative transactions liquidated in cash, an inexact reference to the general definition of interests contained in the IT Law, is eliminated.

6. **Tax consolidation.** As it is known, certain intra-group transactions that consolidate for income tax purposes do not create taxable consequences until certain conditions occur (ex. mergers, sale of stock of tax consolidated entities, variation of equity participation of the controlling company in its subsidiaries); hence, same consequences are commonly referred to as "differed" income tax.

As of 2011, the tax deferred by the consolidated group should be paid since the sixth subsequent tax period to that in which the deferral was created.

Additionally, an obligation is established for tax consolidating groups to pay since June, 2010 the tax deferrals that they have until their 2005 tax period.

FLAT BUSINESS TAX - IETU

1. **Tax credit derived from the excess of deductions over income for IETU purposes.** Taxpayers will not be able 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.

In our view, such prohibition should not apply to the IETU and IT corresponding to the fiscal year of 2009.

2. **Rate increase.** As provided since 2008, the tax rate will increase from 17 to 17.5% for this fiscal year.

VALUE ADDED TAX

Rate increase. The VAT rates applicable to all activities are raised in 1%. Therefore, the general rate will be of 16% and the rate applicable in border zones will be of 11%.

There are transitory and administrative provisions stating special rules for activities carried out in 2009, if the corresponding consideration is effectively paid in 2010.

CASH DEPOSITS TAX

Rate increase and amount of the exemption. The tax rate is increased from 2 to 3% and the amount of the exemption is reduced from MXP\$25,000 (approx. USD\$1,900 to MXP\$15,000 (approx. USD\$1,150), per month for all cash deposits made in all the taxpayer's accounts in each financial entity.

EXCISE TAX

1. **Increases.** Significant increases were made to excise tax over the following activities:

- a) Alcoholic beverages of more than 20 G.L.
- b) Beer
- c) Tobacco
- d) Games and sweepstakes

2. **Telecommunication services.** A new excise tax over services provided in Mexico through one or more public telecommunication networks was enacted, stating an *ad valorem* rate of 3%.

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

FEDERAL FISCAL CODE

1. Fiscal invoices / vouchers. In order to stimulate the use of digital invoices, certain changes to the procedures for their issuance were incorporated to the Federal Fiscal Code. Among such changes, the tax authorities will provide the necessary software in order to issue digital invoices, through their web page. This procedure will be compulsory for all taxpayers.

Paper invoices may be issued, only when the amount of the transaction is lower than MXP \$2,000 (approx. USD \$150), and with new security measures.

Most banking statements, including those for service cards and those issued electronically will be considered as fiscal invoices, without the need for additional documentation.

Such reform will enter into force until July 1st, 2010.

2. 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 considered as tax crimes.

Abbreviations

*IETU	(single rate business tax	–	<i>impuesto empresarial a tasa única)</i>
*IT	(income tax	–	<i>impuesto sobre la renta)</i>
*CIVs	(collective income vehicles	–	<i>sociedades de inversión)</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

Sincerely,

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