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September 17, 2013

MEXICAN FISCAL UPDATE 2/2013

Mexican Tax Reform Bill for 2014

On September 8, 2013, the Executive Branch of the Mexican government submitted before Congress substantive changes to several tax laws which overall constitute the Tax Reform Bill for 2014.

Herein below please find the salient features of these proposals:

GENERAL ASPECTS

- The Tax Reform Bill proposes to enact a new Income Tax Law (*Ley del Impuesto sobre la Renta*) consisting of only 186 Articles, replacing the current law, same which consists of 238.
- It proposes to repeal the current Flat Tax Law (*Ley del Impuesto Empresarial a Tasa Única*).
- The current Cash Deposits Tax Law (*Ley del Impuesto a los Depósitos en Efectivo*) is also repealed as part of the proposal.
- The Tax Reform Bill proposes to adjust the limits of the foreign tax credit mechanism for income taxes paid in other jurisdictions.

INCOME TAX LAW

Legal Entities

- The 30% corporate tax rate is maintained.
- Profits that have been subject to the 30% corporate tax rate will now generate an additional 10% income tax upon their distribution.
- Regarding accruable income and tax deductions:
  - Expenses disbursed in restaurants will be non deductible items.
  - Cars will only be deductible up to $130,000.00 MXN (approx. USD $10,000) instead of the current $175,000.00 MXN threshold.
  - Elimination of the optional tax regime regarding estimative accrual and deduction for real estate building contractors.
  - The deduction of salaries deemed to be exempt for employees becomes limited.
  - Elimination of deductible contributions to pension funds.
  - Elimination of certain optional regimes such as the real estate development regime, the time-sharing regime, and the manufacturing of fixed assets with long fabrication process regime.

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- Elimination of special deduction regimes for banks and financial institutions.
- Elimination of the option to immediately deduct investments in fixed assets.

- The current tax consolidation regime is terminated, whilst it is established a new "integration" regime in which the tax deferral is only allowed over a three tax year period.
- Elimination of the simplified tax regime.

Individuals

- Increase in the marginal tax rate from 30% to 32% for individuals who earn more than $500,000 MXN per year (approx. USD $38,500).
- An employment subsidy is created.
- Taxation on gains realized from sales of shares in the Mexican stock exchange is introduced with a 10% tax rate.
- The exemption on sale of dwelling houses is reduced from 1'500,000 UDI's a year to 250,000 UDIs a year (approx. USD $77,000).
- Personal deductions will now be limited to whichever amount turns out to be lower out of the following: 10% of the individuals yearly income, or the result of multiplying the amount equal to two minimum wages by 365 (approx. USD $3,500).
- A new procedure for determining differences between expenses of an individual being higher than his/her income is contemplated.
- Elimination of special small taxpayers regime and creation of a new incorporation regime for irregular commerce is contemplated.
- The same irregularities regarding the interest regime and withholding of capital income are maintained.

Foreign residents

- Mexican tax authorities will be able to request information from residents for tax purposes abroad, in order to ensure compliance and applicability of benefits derived from tax treaties.
- Additional 10% on dividends paid to foreign entities and individuals.
- Foreign entities and individuals will be subject to tax at the rate of 10% on gain realized from sales of shares in the Mexican stock exchange.
- The 4.9% tax rate applicable to interest paid to financial institutions is still regulated by transitory provisions.
- As a result of the increase in the marginal tax rate for individuals from 30% to 32%, an increase in the tax rate applicable to sale of shares will occur, amongst others.

Preferential Tax Regimes (CFC regime)

- The definition of "passive income" is expanded to include new concepts such as: income derived from the sale of real estate, income derived from the granting of temporary use and enjoyment of goods, etc.
- It is established that the new 10% tax on dividends cannot be included in the 75% income tax paid in Mexico.
- Taxpayers subject to the preferential tax regime can credit the income tax withheld in Mexico to foreign entities. The tax withheld can be credited over the following 10 tax years.

Multinational Companies

- The definition for *maquila* operations is now included in the new law, as well as the requisite stating that at least 90% of their annual revenue must derive from the exportation of the goods produced.
- Certain regimes become more limited, such as the *maquiladora de albergue* regime.

VALUE ADDED TAX LAW

- The 0% tax rate applicable to food and medicine is maintained.
- There is no reference made to nutritional supplements.
- Increase of the special 11% tax rate for border areas to match the general 16%.
- The sale of the following goods is no longer taxed at the 0% VAT rate, but at the general 16% VAT rate:
    - Chewing gum.
    - Processed foods for dogs, cats, and other small species that qualify as pets.
    - Gold, jewelry, art pieces or ornaments and gold bars when not sold to the general public.
- Elimination of VAT exemptions on the following items:
    - Acquisition and sale of dwellings.
    - Mortgage payments (commission and interest).
    - Education services.
    - Land-based public transport of people, except when provided in urban, suburban, and metropolitan areas.
    - Public entertainment (except for theatre and circus events).
- Proposal to tax the import of goods which are temporarily introduced into the country to produce, transform or repair goods which are part of import, export and manufacturing programs; fiscal warehousing programs to assemble and produce cars/vehicles, or for repair in fiscalized or strategic warehouses.
- Elimination of exemption on the sale of goods between residents for tax purposes abroad, or between a resident for tax purposes abroad and a *maquiladora*.
- Elimination of exemption on the sale of goods in fiscalized warehouses.
- Elimination of the 0% VAT rate on the provision of hotel and tourist services which are deemed to be exported for VAT purposes.
- SOFOMS are now included in the VAT treatment given to financial institutions regarding the exemption of interest received and paid.
- The provision of international air transport of passengers and cargo is 100% creditable for VAT purposes.

FEDERAL TAX CODE

- In order to avoid repeated abuses regarding the interpretation of tax norms, a new anti-avoidance clause will be introduced stating that tax laws must be interpreted according to their original purpose.
- Tax authorities will be able to register individuals in the Federal Taxpayers Registry derived from the information provided by financial institutions, and will determine the individuals tax domicile from the same information.

- Creation of a "Tax Inbox" with the purpose to facilitate communication between the tax authorities and the taxpayers, allowing notices to be served, and several administrative procedures to take place through these means.
- The taxpayer will be able to propose a payment plan for tax amounts due.
- The mandatory tax audit is eliminated and in place of such document taxpayers will have to send certain information directly to the tax authorities.
- Prior to the determination of a tax assessment, taxpayers will be able to negotiate with the tax authorities with the involvement of the PRODECON.
- Criminal liability to tax advisors when they propose illegal tax schemes, or furnish advice that leads to tax evasion or any other tax crime.

TAX ON PRODUCTION AND SERVICES LAW

- The 26.5% tax rate on the sale and import of alcoholic beverages with an ethylic content up to 14º G.L., and the 53% tax rate on the sale and import of alcoholic beverages with an ethylic content above 20º G.L., are now considered in the Tax on Production and Service Law.
- Producers and importers of flavored drinks, concentrates, powder, syrup, essences and flavored extracts containing any kind of sugar will be taxed.
- Sale and importation of fossil fuels and pesticides are incorporated as taxed activities.

Should you have any comment or doubt (s) related with the content of this preliminary analysis, please contact at info@turanzas.com.mx

Sincerely,

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