

# Doing Business in **Mexico 2019**



The purpose of this handbook is to enable a better understanding of the legal, financial and other aspects involved when establishing a company in Mexico.



Prepared by Gossler, S.C. January 2019.

**Audit / Tax / Advisory**

**Content**

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# Preface

The purpose of this handbook is to provide the necessary background information to those contemplating doing business in Mexico. In it we include the legal framework, the financial and employment regulations, which we consider to be of particular interest to businesspersons. However, we did not intend to go in depth with any of these topics. The text reflects the laws implemented during 2018.

Our recommendation for anyone intending on doing business in Mexico is for them to seek professional assistance before undertaking any business commitments. Many complex and important financial and tax implications must be considered and discussed with a professional adviser regarding organizational policies, in addition to the formalities, when establishing a new business.

Gossler, S.C., with its specialized team, is ready to assist you with all the necessary steps to establish a new venture in Mexico.

Gossler, member of Crowe Global, offers a wide range of financial and advisory services including Audit, Tax, Business Consulting, Transfer Pricing, Trade, Corporate and Legal Advisory.

We will be glad to meet with businesspersons who visit Mexico and to provide them with any consulting or advisement requested. We encourage you to address any questions you may have directly with Mr. Héctor García, our international liaison partner at our Monterrey City office, or the corresponding partner located in the city in which you intend to establish a business.



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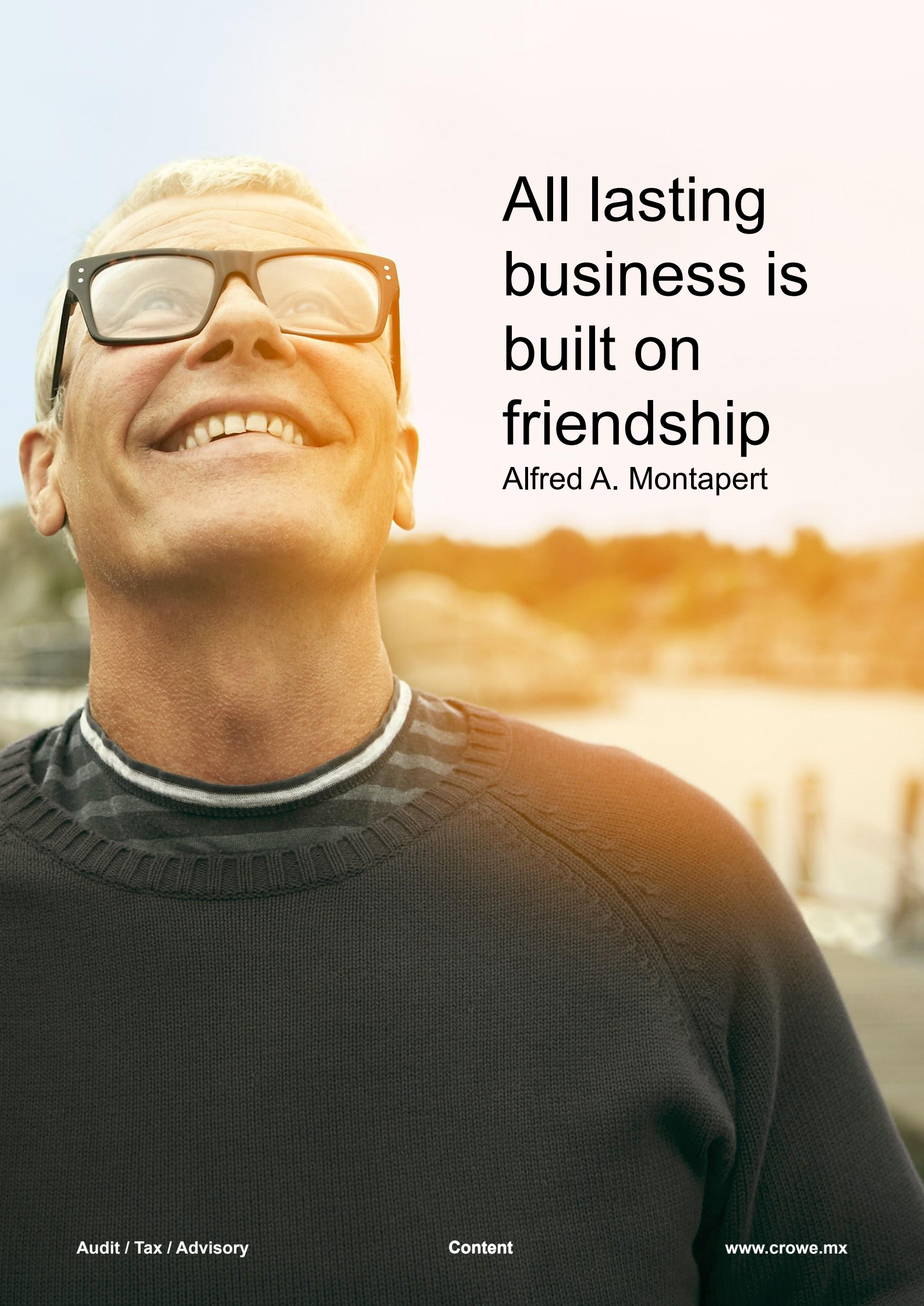
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A close-up, low-angle shot of a man with short blonde hair and black-rimmed glasses. He is smiling broadly, looking upwards and to the right. The background is a bright, warm, out-of-focus outdoor setting, possibly a waterfront or a park, with a body of water and some structures visible in the distance. The lighting is soft and golden, suggesting a sunrise or sunset.

All lasting  
business is  
built on  
friendship

Alfred A. Montapert



# Part 1 General Business and Legal Requirements

## Chapter 1 General information about Mexico

### Government / Federation

The United Mexican States, commonly known as Mexico, is a federal republic conformed of 31 federal entities and Mexico City, which used to be a Federal District up until 2016. The executive branch of the country is led by the President, who is elected through popular voting for a term of six years with no right for re-election. Eighteen cabinet secretaries, the Attorney General and 299 government entities are

also part of the executive branch. The legislative branch is made up of the House of Representatives (Cámara de Diputados) and the Senate (Cámara de Senadores).

The House of Representatives is powered by 500 representatives elected for a three-year period, 300 of which are elected by simple majority in each electoral district of the country and 200 are proportionally assigned by political party elected from 5 main areas with 40 seats each.



The Senate is powered by 128 senators elected for a six-year period, two for each of the 32 states elected under the principle of relative majority, one for each 32 states assigned under the principle of first minority and 32 national senators divided among the parties in proportion to their share of the national vote. Neither Senators nor House Representatives are eligible for re-election for consecutive terms.

The judiciary power is conformed by 11 Supreme Court judges nominated by the President and ratified by the Senate.

### State and Municipalities

The 31 states and Mexico City are similarly delegated, each state has its own constitution, congress and a judiciary, which its citizens elect by direct voting a governor for a six-year term and representatives to their respective unicameral state congress for three years. Each state is divided into municipalities, governed by a mayor or municipal president, elected by its residents through plurality.

### Physical & Geographical Characteristics

Mexico's geographical area covers almost 2,000,000 square kilometers (770,000 square miles), the fifth largest country in the Americas by total area.

To illustrate, the distance from Merida to Tijuana is equivalent to the distance from Barcelona to Moscow. The length of the US-Mexico border is 1,954 miles (3,145 km). It's located in the southern portion of North America, bordered by the United

States to the North, the Pacific Ocean to the South and West, Guatemala, Belize and the Caribbean Sea to the Southeast and the Gulf of Mexico to the East.

Although it's formally considered as part of North America and Central American countries, it constitutes a barrier between North and South America. Mexico has access to two oceans and has more than eleven thousand kilometers in shorelines, as demonstrated by the map below.

Mexico's strategic geographical location gives it access to many markets, hence the reason why Mexico has trade agreements with more than 46 countries. Mexico is placed on number 13 among other exporting countries in the world and number 1 among Latin America. Some of the main manufactured products being exported from Mexico include: automobiles, auto parts, cellphone parts, computers, crude oil, televisions, electric cords, medical equipment, tractors, seats and refrigerators.

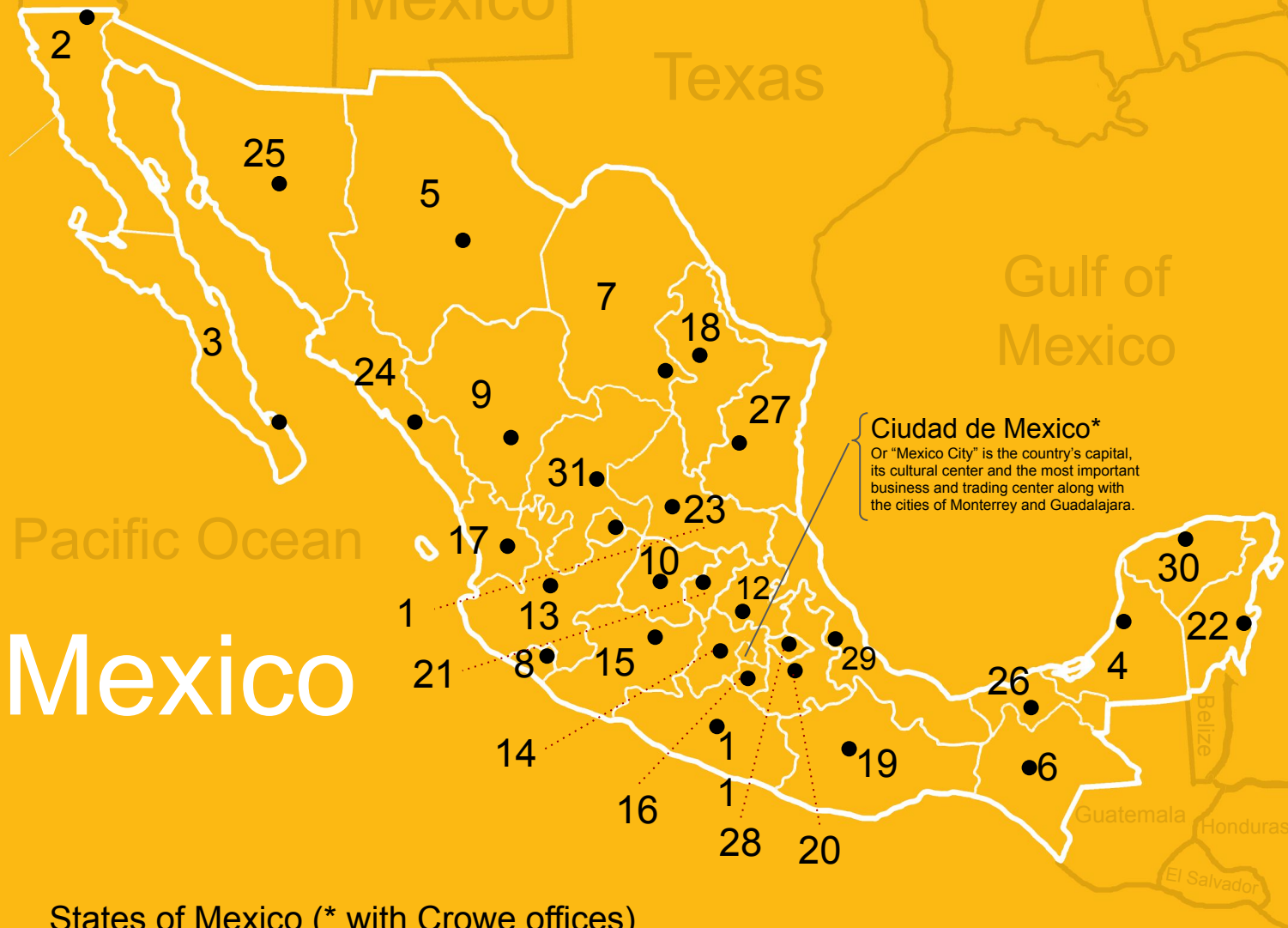
Mexico is an important leader in the agro-food industry; avocado, vanilla, cocoa, cactus, amaranth, dahlias and agave are some of the 200 varieties of crops originating in Mexico. The Ministry of Economy (SE) indicates that the growth of the food industry is due to Mexico's production capacity, agricultural resources and low manufacturing costs<sup>1</sup>.

### Language

The official language in Mexico is Spanish with several other indigenous languages spoken by 5.4% of the population. It's the largest Spanish speaking population in the world and for its industrialized cities, their secondary language is English.

1. ProMexico, Special Feature: Mexican food industry / Mexico feeding the world.

# United States of America



## Mexico

### States of Mexico (\* with Crowe offices)

- |                          |                  |                       |                  |                       |                  |
|--------------------------|------------------|-----------------------|------------------|-----------------------|------------------|
| 1. Aguascalientes*.      | 7. Coahuila*.    | 12. Hidalgo.          | 17. Nayarit.     | 22. Quintana Roo*.    | 27. Tamaulipas*. |
| 2. Baja California*.     | 8. Colima.       | 13. Jalisco*.         | 18. Nuevo León*. | 23. San Luis Potosí*. | 28. Tlaxcala.    |
| 3. Baja California Sur*. | 9. Durango.      | 14. Estado de México. | 19. Oaxaca.      | 24. Sinaloa*.         | 29. Veracruz*.   |
| 4. Campeche.             | 10. Guanajuato*. | 15. Michoacán*.       | 20. Puebla.      | 25. Sonora*.          | 30. Yucatán*.    |
| 5. Chihuahua*.           | 11. Guerrero.    | 16. Morelos.          | 21. Querétaro*.  | 26. Tabasco.          | 31. Zacatecas*.  |
| 6. Chiapas.              |                  |                       |                  |                       |                  |

● Geographical position of the capital of each State.



Mexico as exporter, compared with the rest of the World:

- 4th in computers.
- 5th on home appliances,
- 7th largest exporter of cars, exports on medical equipment also stand out.

About 19.4% of all exports require medium or high levels of technology.

Mexico is the 3rd country with the most airports with 64 international airports, 12 for domestic traffic, and 117 sea ports.

General Information	
Population	130,759,074
GDP	\$1,150.88 Billion USD
GDP per capita	\$9,865.79 USD
Exports	\$413,042 million USD
Imports	\$428,583 million USD

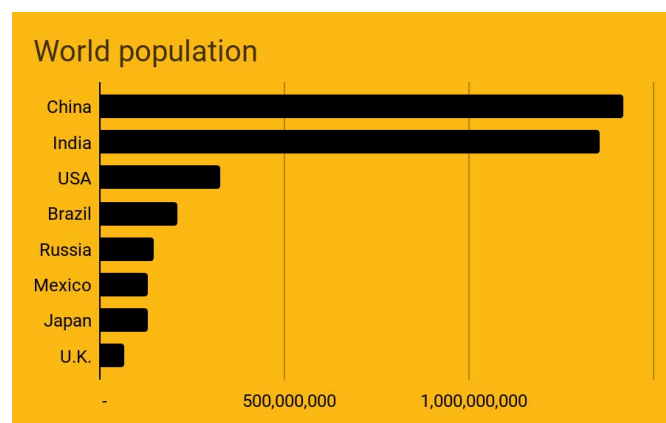
## Population

Mexico's population at the end of 2018 was approximately 130 million, equivalent to 1.71% of the total world population. Its capital known as Mexico City is the most populated city in North America and home to more than 150 museums, the second with the most in the world after London.

Mexico City has the highest population concentration, followed by the cities of Guadalajara with 4,434,252 and Monterrey with 1,135,512 citizens. During the last 50 years the population in Mexico has grown four times, nevertheless, the annual growth rate has decreased since 1970.

According to the World Factbook, China and India both have populations of over a billion while the US places third with 325 million. Brazil, Russia, India and China also called the BRIC, are known as the four major economies in the world. Mexico has the largest population after Russia with about 130 million.

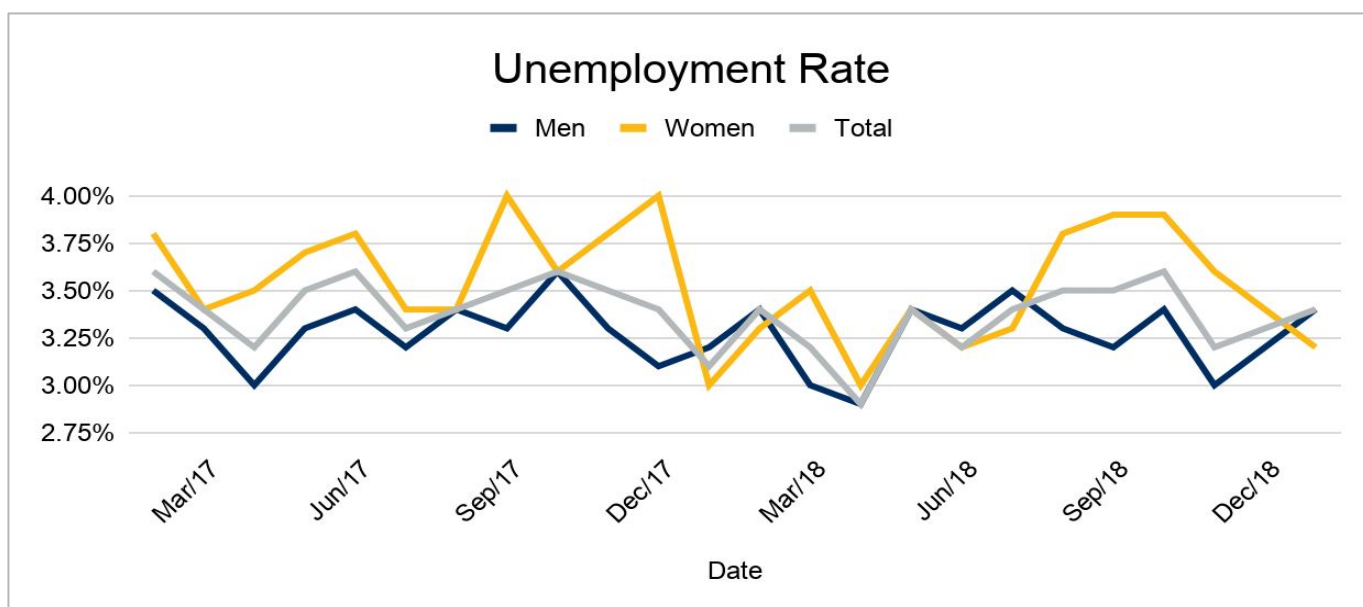
Population in millions (2018)				
Age	Mexico	%	World	%
0-14	34	26	1,984.5	26
15-64	87.6	67	4,961.5	65
65+	9.2	7	687.0	9
<b>Total</b>	<b>130.8</b>		<b>7,633.0</b>	



## Unemployment

Mexico's unemployment rate decreased throughout 2017 reaching a low of 3.1% at the end of the year. During March of 2018 unemployment reached a record low of 2.93%, the lowest in 10 years. At the end of 2018, unemployment rate was 3.4% an equivalent to 1.8 million people, as expected by seasonality.

Unemployment levels between men and women throughout 2017 were higher for women and higher for men throughout the first half of 2018. The gap between them closed off on April 2018 and since then unemployment rates have been higher for women.



## Trading, Industry and Infrastructure

### Currency

The monetary unit in Mexico is the "PESO" represented by the letters "MXN"<sup>1</sup>. The exchange rate on April 17, 2018 was 17.9787 MXN, with the highest being 20.7160 MXN per USD as of June 15, 2018.

minimum and closing exchange rates for the last two years, as measured by the FIX:

USD/MXN			
	2017	2018	2019
Min	17.4937	17.9787	18.928
Max	21.9076	20.7160	19.6073
Closing	19.6629	19.6512	

Source: Bank of Mexico.

The following chart from Bank of Mexico summarizes the Maximum,

1. Source: <https://www.iso.org/iso-4217-currency-codes.html>

## Government Role

Mexico has a mixed economy, which is made up of both privately-owned and state-owned companies. In 2016, there were thorough changes implemented after 11 reforms were passed by the legislative chamber. Above all these approved new reforms, the "energy reform" has significantly transformed the country's oil and gas industry.

The Mexican commerce is regulated by the Ministry of Economy, whose functions include: the supervision of distribution and consumption, promotion of foreign trade, analysis of official prices and related indexes, regulating import and export and initiating tax incentives for promoting price controls on fees for services with public interests, whose number are limited.

Mining plays an important role in the economy of the country, since Mexico was the largest producer of silver, fluorite and arsenic in the world. Nowadays, it's still one of the biggest mining producers.

## Communications

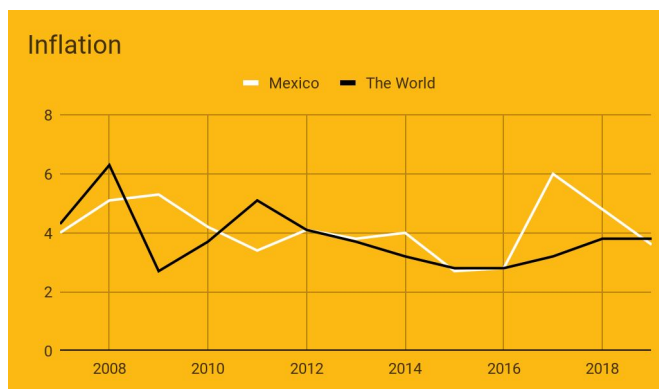
The main highways of the country pretty much crisscross the country. The most traveled highways are those that link the three most populous cities: Mexico City, Monterrey and Guadalajara in the form of a triangle.

The main seaports on the Gulf of Mexico are Altamira, Coatzacoalcos, Veracruz, Tuxpan, Campeche and Progreso. The main seaports on the Pacific Ocean are Acapulco, Mazatlan and Manzanillo. The railroad system was state controlled but

faced a privatization process in the 1990s and was closed to promote the private investment on roads and highways. Mexico has more than 58 international airports with flights connected all over the world, with major foreign airlines servicing the country. The main airline company flying in Mexico is AeroMexico.

## Government Policies Affecting Business

### Economic Policies



Source: Bank of Mexico.

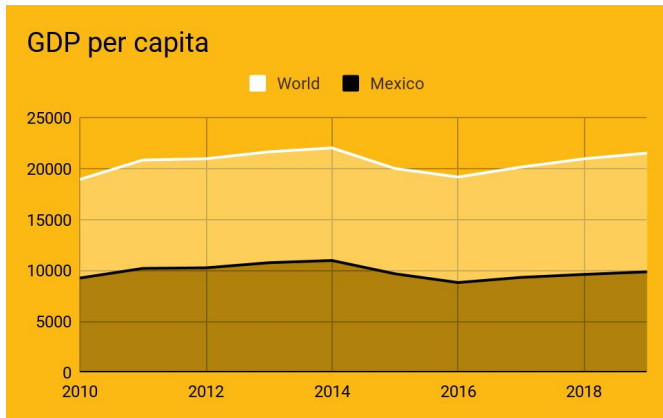
The annual percentage change on inflation from 2007 until 2019 is shown in the previous graph.

In the last decade, economic policies contemplated a national plan for recovery emphasizing a high growth rate in productivity.

During 2007, inflation was around 4% but by the end of 2016 it was as low as 2.8%. Throughout 2017 inflation increased to 6%, its highest in 17 years due to the liberalization of oil prices. As of 2019, inflation is down to 3.6%; for 2019 year's end, Bank of Mexico Analyst consensus expect inflation to be around 3.4%.



The world's Gross Domestic Product (GDP) throughout the last 8 years has been positively increasing except for a slight decrease in 2015. The main macroeconomic variables seem to only slightly deviate from their original targets despite the presence of an unfavorable international environment. According to the World Bank, GDP per capita reached US\$ 18,535 at the end of 2016. As of 2018, the GDP per capita converted to dollars was equal to US\$ 19,093.



Source: World Bank.

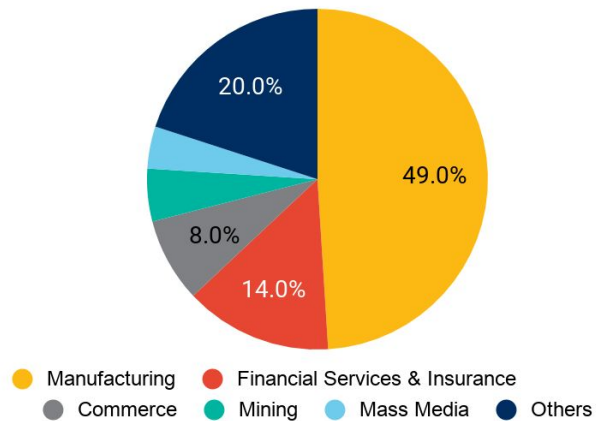
The graph above shows that Mexico's GDP per capita has had a positive correlation to the world's GDP, even though it's had its ups and downs throughout the last 8 years. Mexico's GDP per capita is positioned in the 90th place in the ranking by the World Factbook among 230 countries.

Mexico's GDP has recently experienced a steady growth, showing great potential in some economic sectors, such as maquiladoras. Mexico has the second largest economy in Latin America, ranking second to Brazil whose economy experienced a slow growth in 2017.

The fastest growing sectors in the economy in comparison with the overall performance

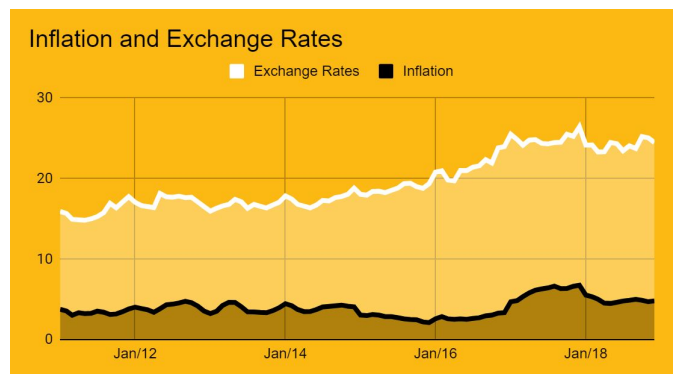
of the Mexican economy can be seen in the following graph. Manufacturing is also included because it is one of the most important sectors in the economy despite not having one of the highest growing rates.

Foreign Direct Investment per sector



Source: ProMexico.org

The next graph shows the comparison between inflation and USD/MXN rates for the past 7 years. The two variables show no correlation between them, the exchange rates show currency fluctuations while inflation has remained relatively stable until the beginning of 2015 and began to increase throughout 2016 due to many reforms being approved that year.



Source: Bank of Mexico

According to the Bank of Mexico's economic perspectives, the future trajectory of the exchange rate remains sensitive to commercial deals and changes to the monetary policy normalization in the US. The USD/MXN rate appreciated over the course of 2018 relative to the US dollar, although a weakening has been observed in recent months.

The USD had a noticeable increase in value against some other major currencies (CCY), which shows that the depreciation of currency was extremely affected by external factors. The table below presents the USD depreciation, which can be analyzed facing other important currencies.

CCY	Jul/16	Jul/17	Jul/18	Dec/18
MXN	18.309	18.2064	20.1453	19.3208
EUR	1.1139	1.14249	1.17015	1.1445
GBP	1.32695	1.30276	1.31155	1.2746
RUB	0.01565	0.01697	0.01602	0.01442
ZAR	0.06873	0.07646	0.07632	0.06946
BRL	0.3092	0.30233	0.2665	0.2577
CAD	0.77491	0.77068	0.7678	0.7323

Source: ProMexico.org

A depreciation was seen between the years 2016 and 2018 but some currencies have recovered against the dollar while others, such as emerging market economies have shown weak signs of recovery.

### GDP Growth per State

In 2016, the states that showed the highest growth rates were Aguascalientes and Quintana Roo. During 2017, Baja California Sur, Morelos and Puebla experienced the highest growth rates. Baja California Sur also experienced the highest growth rate

seen during the first quarter of 2018.

The States with the highest growth rates show their potential being worth investing in.

According to the following graph the growth per state in 2016, 2017 and 2018 were the following:

GDP growth at constant prices per State			
	2016	2017	2018
Aguascalientes	9.50%	7.09%	3.10%
Baja California	3.60%	4.73%	3.50%
Baja California Sur	2.20%	9.14%	21.40%
Campeche	-5.80%	-7.05%	-6.50%
Coahuila	1.80%	4.58%	-0.30%
Colima	5.70%	3.14%	4.60%
Chiapas	-1.10%	-2.12%	-1.60%
Chihuahua	5.10%	3.26%	-0.50%
Mexico City	4.60%	3.78%	2.20%
Durango	3.70%	2.28%	-2.60%
Guanajuato	4.50%	5.63%	1.00%
Guerrero	2.80%	-2.33%	5.00%
Hidalgo	4.00%	-2.80%	5.10%
Jalisco	4.70%	3.11%	5.50%
Mexico	2.90%	3.17%	5.00%
Michoacán	4.00%	2.33%	4.10%
Morelos	2.70%	7.58%	-2.50%
Nayarit	3.60%	1.77%	1.30%
Nuevo León	1.40%	3.93%	2.40%
Oaxaca	-0.90%	-2.97%	1.60%
Puebla	3.10%	7.58%	2.90%
Querétaro	3.60%	5.87%	-0.40%
Quintana Roo	7.60%	3.31%	4.50%
San Luis Potosí	4.30%	4.87%	8.40%
Sinaloa	5.50%	0.09%	3.90%
Sonora	5.60%	3.52%	0.90%
Tabasco	-6.30%	-9.90%	-3.20%
Tamaulipas	-0.80%	-0.05%	1.30%
Tlaxcala	0.80%	-0.54%	0.90%
Veracruz	1.60%	-0.60%	-0.90%
Yucatán	3.80%	4.11%	2.90%
Zacatecas	-0.20%	1.21%	2.70%

Source: INEGI 

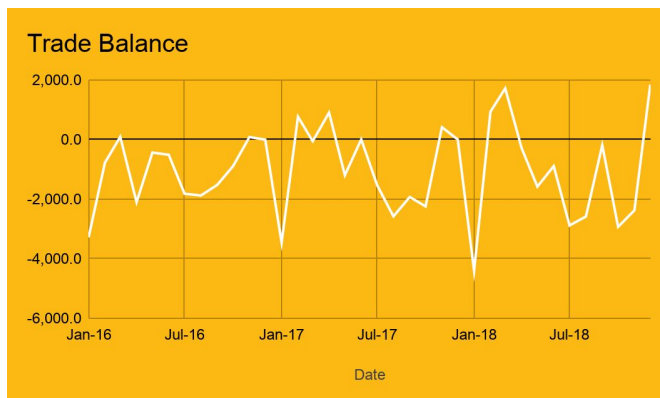
## Import - Export Policies

As a result of the United States housing crisis of 2009 and other world effects, exports, especially the maquiladora industry and manufacturing were affected. In 2008, the Ministry of Finance and Public Credit (SHCP) and the Ministry of Economy issued a decree to expedite and streamline their operations in order to mitigate any negative impact they could. The measures taken benefited the users of foreign trade with a reduction of paperwork in order to expedite and streamline their operations.

Mexico was the main promoter of the North American Free Trade Agreement (NAFTA) in which Canada, USA and Mexico signed one of the most important tariff and trade agreements in the world, second to the European Union. Since the new presidential elections for both US and Mexico, this agreement was renegotiated and renamed United States, Mexico and Canada agreement (USMCA) and kept 80% of the original deal with some modifications.

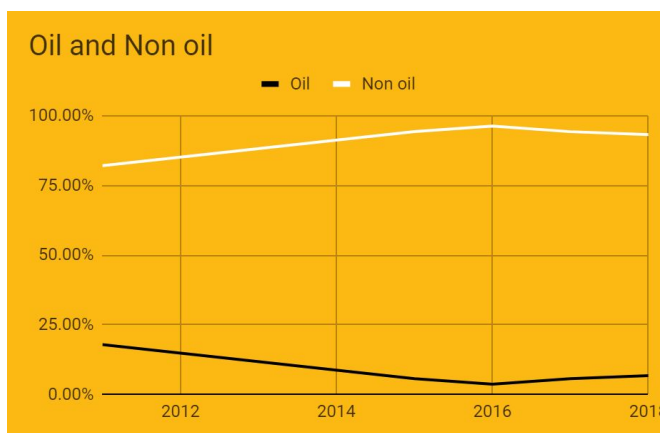
Mexico has Free Trade Agreements with other countries such as: Colombia, Venezuela, Costa Rica, Bolivia, Nicaragua, Chile, Israel, El Salvador, Guatemala, Honduras, Norway, Liechtenstein, Japan and Switzerland, among others.

Mexico's trade balance from January 2016 to December 2018 is demonstrated in the following graph. It is important to note that the trade balance in the first quarter of 2018 was one of the most negative since the beginning of the 2000s, at - US\$ 4,419,826 million. One of the causes for this fall was due to the manufacturing exports falling by 3.3%.



Source: INEGI

It is a common assumption that Mexico's biggest export is oil but that is not the case. We can see the importance of each type of export in the following chart.

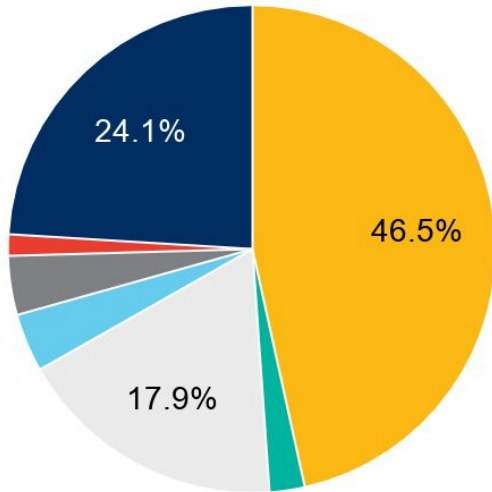


Source: INEGI

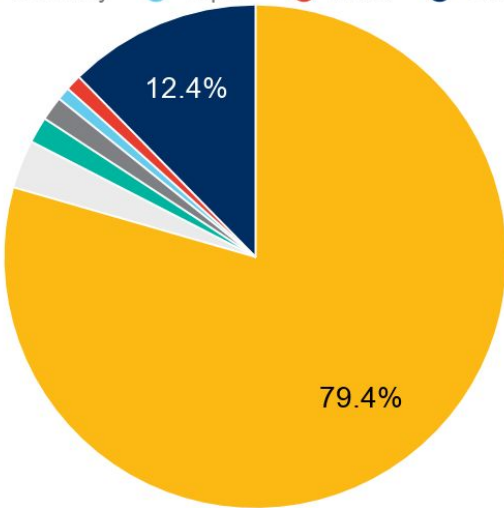
According to data provided by the Bank of Mexico, the major trading partners are the US and China. In 2018, the US received the most exports from Mexico with 79% of total exports while Canada only 3%. Mexico received 47% of its imports from the US, 18% from China and 4% from Japan.



## Imports



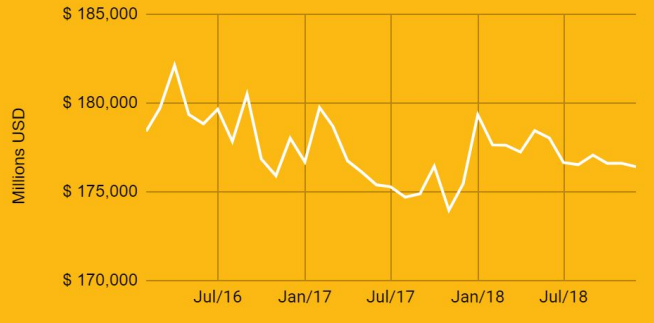
## Exports



Source: Bank of Mexico.

The decrease in reserves is due to the country stabilizing its currency against the USD by auctioning and selling dollars. Its intervention in the Forex markets is limited to curb the pass-through effect of the exchange rate into inflation.

## Official Asset Reserves



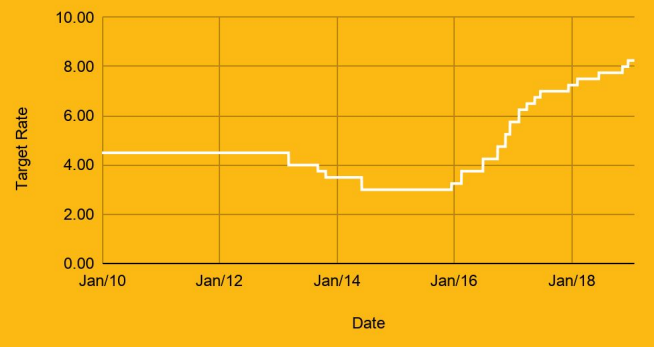
Source: Bank of Mexico.

## Central Bank

Mexico's central bank is a fully autonomous institution whose main function is to provide stability to the purchasing power of the currency. As stated before, Mexico's inflation has been stable and has permitted its currency to maintain its purchasing power.

Mexico had been lowering its interest rates in the last years in tandem with the Federal Reserve Board. When a country increases its interest rates it is expected to see an appreciation in its currency. The two most recent increases made to the target rate were registered on November to 8% and on December to 8.25%.

## Target Rate



Source: Bank of Mexico.

According to the Bank of Mexico, as of January 24, 2019 other interest rates are the following:

Target rate	8.25%
TIIE	Rate
28 days	8.5950%
91 days	8.6100%
182 days	8.5944%
CETES	
28 day	7.91%
91 day	8.18%
182 day	8.40%
364 day	8.62%
Bonds	
10 year	8.71%
20 year	8.93%
UDI bonds	
30 year	4.25%

## Foreign Investment

Mexico has become an attractive location for foreign direct investment (FDI) due to its proximity to the US and its macroeconomic stability. The aforementioned reforms set in place to improve competition, labor regulations and education quality, are essential to increase competitiveness and to encourage more Foreign Direct Investments (FDI).

In 2015, Mexico ranked 15<sup>th</sup> among the largest worldwide investment destinations according to World Investment Report of 2016 by the United Nations Conference on Trade and Development (UNCTAD).

Mexico's foreign direct investment inflows show that Mexican investments are

primarily focused on the US and other Latin American markets while also expanding into Europe. Hence, the countries that show the most percentage change increase are Brazil, France, Germany, Indonesia and Republic of Korea.

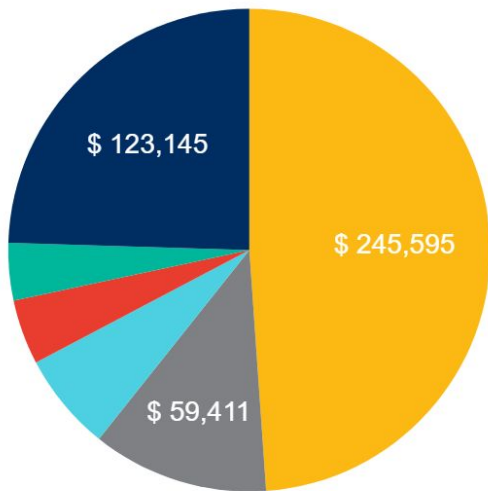
The Ministry of Economy reported that foreign direct investment in the country was \$17.842 billion in the first half of 2018, with 43% corresponding to the manufacturing sector and 19.4% in financial services coming from the U.S., Spain, Germany, Canada and Japan.

Country	2016	2017	% Change
United States	457	275	-39.82%
China	134	136	1.49%
Hong Kong	117	104	-11.11%
Brazil	58	63	8.62%
Singapore	77	62	-19.48%
Netherlands	86	58	-32.56%
France	35	50	42.86%
Australia	48	46	-4.17%
Switzerland	48	41	-14.58%
India	44	40	-9.09%
Germany	17	35	105.88%
Mexico	30	30	0.00%
Ireland	15	29	93.33%
Russia	37	25	-32.43%
Canada	37	24	-35.14%
Indonesia	4	23	475.00%
Spain	20	19	-5.00%
Israel	12	19	58.33%
Italy	22	17	-22.73%
Korea	12	17	41.67%

Source: UNCTAD , World Investment Report 2018

## Millions of USD

● USA ● Spain ● Canada ● Japan  
● Belgium ● Others



## Investment incentives

The new federal government took office on December 1, 2018 and has since set in place numerous reform plans, such as increasing minimum wage and tax cuts for northern regions of the country. President Andres Manuel Lopez Obrador's candidacy was focused on the equality of economic opportunities and ending with corruption. The President launched a plan to stimulate the economic activity on the Mexican side of the U.S-Mexico border, which will cut income and corporate taxes from 30% to 20% for 43 municipalities in 6 bordering states with the U.S., while also cutting the value-added tax from 16% to 8%. An initiative was also set in place to double the minimum wage to 176.2 pesos a day in the northern border region: these initiatives were set in place to stimulate wage and job growth through tax incentives and productivity gains.

Mexico has 10 Foreign Trade Agreements with 45 countries, 32 Reciprocal Investment Promotion and Protection Agreements (RIPPAs) with 33 countries, 9 trade agreements with Latin America and is a member of the Trans-Pacific Partnership Agreements (TPP). The most important trade agreements are the United States, Mexico and Canada Agreement (USMCA) and the Free Trade agreement with the European Union and the Latin American Integration Agreement (ALADI).

Since the implementation of new reforms and the abolition of rules that happened in the last 5 years, other programs were designed to promote exports and imports for the country. **The most attractive incentive for foreign companies to invest in Mexico is the Manufacturing, Maquila and Export service industry (IMMEX)**, which allows for cross-border manufacturing to import duty free equipment and materials required to assemble and manufacture products for export services, without covering the payment of general import tax, value added tax and, where appropriate, countervailing duties.

There are numerous tax incentives set in place such as accelerated depreciation of fixed assets and the immediate deduction to encourage investment in the country. Taxpayers engaged in agriculture, livestock, fishing or timber-based economic activities are provided special tax exemptions based on the number of shareholders that make up the firm's corporate structure. Companies engaged in research and development for technology are eligible for special financing grants and incentives through the National Council of Science and Technology.



Mexico is considered attractive for IOCs (International Oil Companies) that invest in the Oil and Gas sector. In a time period from 2018-2021, it's expected to drill 43 oil wells derived from new contracts, with an average of 11 wells a year. The projects are bid based on a competitive tendering process, aimed to ensure transparency and getting companies with the corresponding financial and technical expertise to exploit the country's resources.

According to ProMexico (2018), some of the main factors related to doing business in Mexico include the regulation for starting a business, dealing with construction permits, getting electricity, registering property, obtaining a credit, protecting minority investors, paying taxes, trading across borders, enforcing contracts and resolving insolvency.

## Anti-money laundering law environment

As of October 2012, the federal law of prevention and identification of anti-money laundering activity was published. This law seeks to enforce the requirements of the Financial Action Task Force (FATF), improve inter-institutional coordination, and gather useful information to make better quality investigations and to pursue crimes with more efficiency.

With this new law set in place, more non-financial professional activities, which are vulnerable against this type of crimes were included in the regulatory framework. The government is working on improving these types of regulations, which are different to the financial framework.

The anti-money laundering law for financial institutions has had a higher level of maturity and regulatory enforcement. The authorities published a national risk policy that guides financial institutions to make improvements towards the money laundering risk analysis. The challenge for Mexico is to achieve their goal of having the financial institutions fulfill these regulations by materializing reports of strange activities and turning them into the authorities.

Mexico has a strong financial system that is constantly evolving in its regulatory framework. GAFI's objective is to establish standards and to promote the implementation of effective laws and regulations against money laundering.

Its latest evaluation concluded that Mexico has a mature regimen with a well-developed legal framework, while also having improved in some areas since the last evaluation. Out of the 40 recommendations, only one has fully not accomplished with all the others being accomplished or mostly accomplished.

## Final thoughts

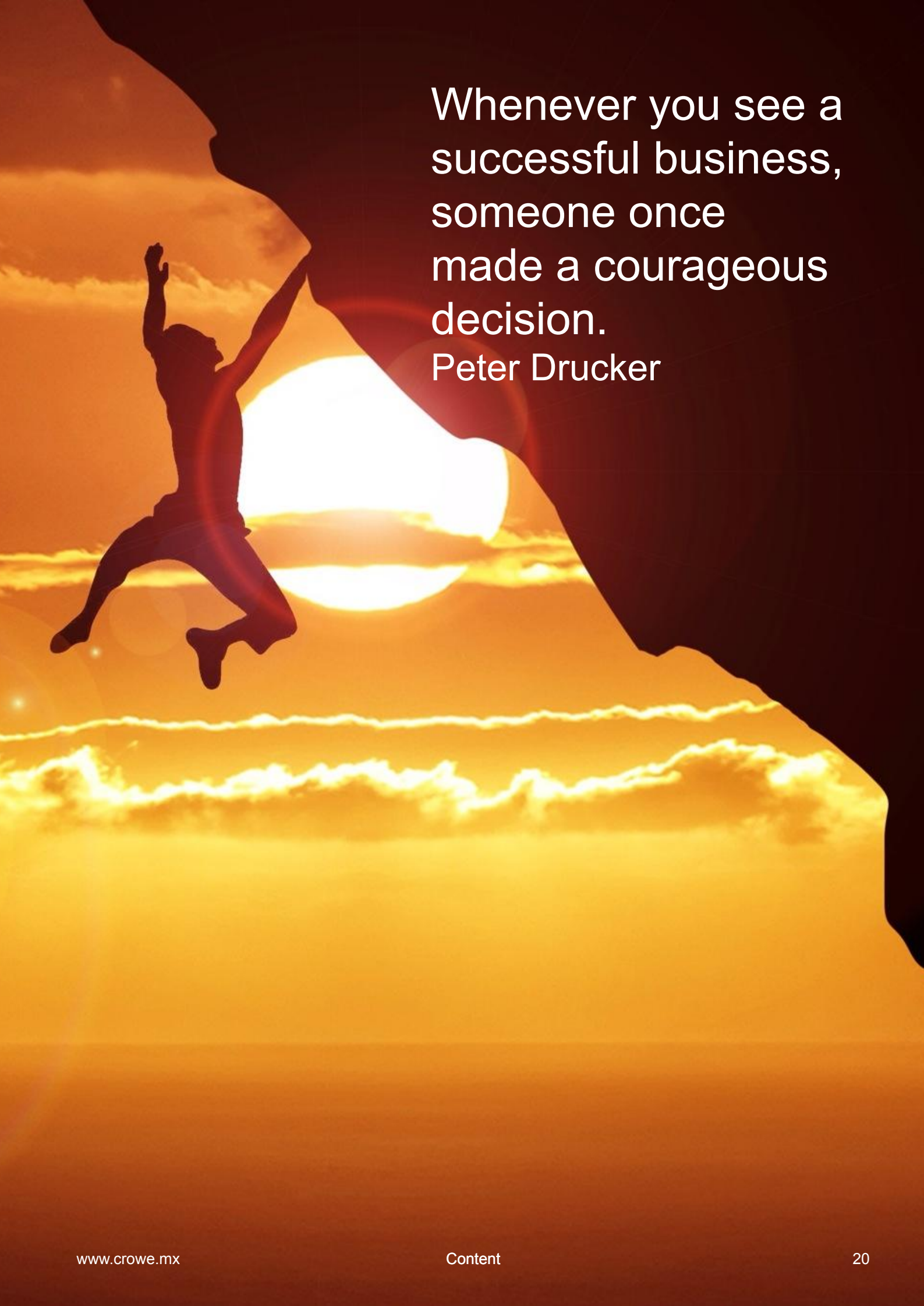
During the last decade, Mexico has made a noticeable improvement in terms of the quality of life for its citizens. About 61% of people aged 15 to 64 have a paid job and the country gets about 76.6 million visitors each year. The advantages of being closer to Mexico may increase the productivity for each investment, the US is the greatest investor in the economy but other countries such as Spain and Great Britain also make investments in Mexico.

Living expenses in Mexico are relatively cheap compared to the rest of North America. The luxury living is among the 5 % and the tourism development in the gulf coast as well as on the east coast has been developed and receive millions of visitors each year.

The long coasts surrounding Mexico are the main attraction for tourists, including the beach, food and recreational areas. The most notable attractions are the Mesoamerican ruins, cultural festivals, colonial cities, nature reserves and the beach resorts located along the coast of Mexico. The Yucatan peninsula, the pacific coast Acapulco, and the southern tip of Baja California receive the most tourists.

Throughout the past years, the trading balance has suffered a deficit, but the new Federal Government has made its goal to avoid suffering a deficit in the following years. The exports depend less on oil, which shows Mexican exports have changed in composition. Mexico can be considered as a stable economy showing great investment opportunities in many sectors.

Failing to consider this country for investment purposes may prove to be a mistake as it is becoming easy to do business and the economy is expected to continue enjoying both a stable growth and low inflation. Indeed, this country's potential is the advantage of treaties which allow trading to be done with less barriers.

A silhouette of a person jumping over a large rock at sunset. The person is in mid-air, with arms raised and legs bent, as if clearing the rock. The background is a bright orange and yellow sunset sky with a large sun and clouds. The rock is dark and jagged, partially obscuring the sun.

Whenever you see a  
successful business,  
someone once  
made a courageous  
decision.

Peter Drucker



# Chapter 2 Sources of Financing

## The Banking System

The Bank of Mexico (Banco de México), established in 1925, is the country's central bank. By Constitutional mandate, it is autonomous in exercising its functions and administration.

The main objective of the Bank is to procure the national currency's purchasing power stability. Bank of Mexico has always given the utmost importance to the publication of information that will help decision-making and allow the public to evaluate the execution of its policies. Given that the information is presented in the timeliest manner, discrepancies could eventually arise due to revisions to the information.

### Secretariat of Finance and Public Credit

- Undersecretary of Finance and Public Credit.
- Bank of Mexico (autonomous).
  - ..... National Banking and Stock Commission.
    - Banks.
    - Public Funds and Trusts.
    - Saving and loan.
    - Stock market.
    - Derivatives sector.
    - Nonbank financial intermediaries.
  - ..... National Commission of the Pension System.
  - ..... National Insurance and Bond Commission.
    - Insurance and bonds.

## Types of financial institutions

Banking Law has created several different types of institutions of credit. The purpose of such institutions is to provide a means for savings and for short, medium and long term financing. The most common are the private banks that provide services to the general public and private sector business. It is important to mention that after the bank crisis of the ninety's, the principal Mexican banks were acquired by international banks, such is the case of:

- Banamex, S.A. - Citigroup.
- BBVA Bancomer, S.A. - BBVA.
- Banco HSBC, S.A. - HSBC.
- Banco Santander, S.A.
- Banco Mercantil del Norte, S.A.
- Scotiabank Inverlat, S.A.

More recently impulse have been given to the creation of new banks such as:

- Banco Walmart de México Adelante S.A.
- Banco Azteca S.A.
- Banco Compartamos S.A.
- Banco Ve por Mas S.A.
- Banco Regional de Monterrey, S.A.
- Banco del Bajío, S.A.
- Banco Base, S.A.
- Banco Famsa, S.A.

A list of other financial institutions that operate in Mexico are the following:

- Bank of America.
- American Express Bank.
- Merrill Lynch.
- UBS.
- ABN Amro Bank.
- Deutsche bank.

In addition to the above banking institutions, which operate with the general public, the Federal Government operates several specially designated banks assigned to a specific development purpose.

## Short & Long Term Financing

### Short term financing

Companies may obtain short term financing from one of the following alternatives:

- Direct Loans.
- Discounting of notes.
- Trade paper.
- Factoring.

Orders of payments are used to remit for purchases of goods to foreign suppliers. Other financing mechanisms are also available to companies exporting goods for sale in foreign markets.

In Mexico, short-term credit is extended for a period of two to five years. Most of this credit is used to finance equipment or as a working capital. Alternatively, companies may pursue short-term financing by issuing debt in the money market, either in secure notes or in debentures.

### Long-term financing

Long-term credit extends for periods of over five years. This debt is usually secured by a trust deed and is usually obtained only through commercial banks. Such credit is generally used for real estate construction.

Alternative long-term financing may be available through the issue of long-term debt in the Money Market or by marketing

the company's stock in the public market.

## Stock Market and Money Market

### Development

The National Committee for Banking, Securities and Exchanges regulates the Mexican Stock Market (Bolsa Mexicana de Valores, S.A.B. de C.V.). The Mexican Stock Market is a private institution that operates under the supervision of the Ministry of Finance and Public Credit under the Stock Market Law.

Presently, the Mexican Stock Market represents a financial system that operates parallel to the banking system, that is, through acceptance of money from investors. The resources for companies requiring finance are obtained either by public offer of commercial paper (financial or extra financial), placing direct loans or mortgage bonds, or by the issue of capital stock.

In the process of issuing any financial instrument, a company will follow some of these markets:

**Primary Market.** This market is used when a company makes its first issue. It is mandatory to use an intermediate.

**Secondary Market.** After its first issue, investors can buy or sell its financial public instruments in this market. The companies are not the only ones who purchase and sell in the secondary market, but any investors, including the same with previously issued titles in primary offer.

The growth of the stock market after the “crash” of December 1994, has been substantial, Despite the less than desirable economic situation of the country, the modifications in the securities regulations have given the investors more confidence.

## **Money Market**

Financial instruments, which are operated within the money market, are, among others:

- Commercial Paper and other medium and long term bonds (financial or extra financial), issued by private companies.
- Bonds, promissory notes and certificates of credit issued and backed by the Federal Government in terms varying from 28 to 180 days and currency terms could go higher than ten years. Some of these securities are payable in U.S. currency.
- Certificates of credit backed not only by Petróleos Mexicanos (PEMEX), but other government agencies such as Nafinsa and Bancomext payable in U.S. currency.

## **Derivatives Market**

The Mexican Derivatives Market (MEXDER) constitutes one of the most important improvements among the SIFIMEX’s internationalizing and development process. International Finance Organizations such as The International Monetary Fund (IMF) and The International Finance Corporation (IFC) have been spoken about the importance of this new Market. MEXDER is ready to accomplish requirements from International

Organization of Securities Commissions (IOSCO), The International Federation of Stock Exchanges (known as FIBV in French), and the Futures Industry Association (FIA), among others. MEXDER offers contracts of Futures, Options, Bonds, Swaps, Interest Rates, Commodities prices and so forth.

## **Other financial intermediaries**

Foment fund. Are financial entities of public character type dependent from federal government whose objective is to drive certain economic activities related to production, properties and services distribution and consumption. Its principal function is to assume risks in selected projects due to its high social leasing. They are regulated by the federal state entities law.

Financial corporations with multiple purpose (SOFOM). These institutions were created in 2006 as a consequence of a deregulation of the SOFOLS. The SOFOMS are financial corporations which in most of the cases are not supervised by the National Commission of Securities and Banking, but functioning under the legal frame of credit institutions and of Credit Organizations and Activities Law.

## **Auxiliary credit organizations**

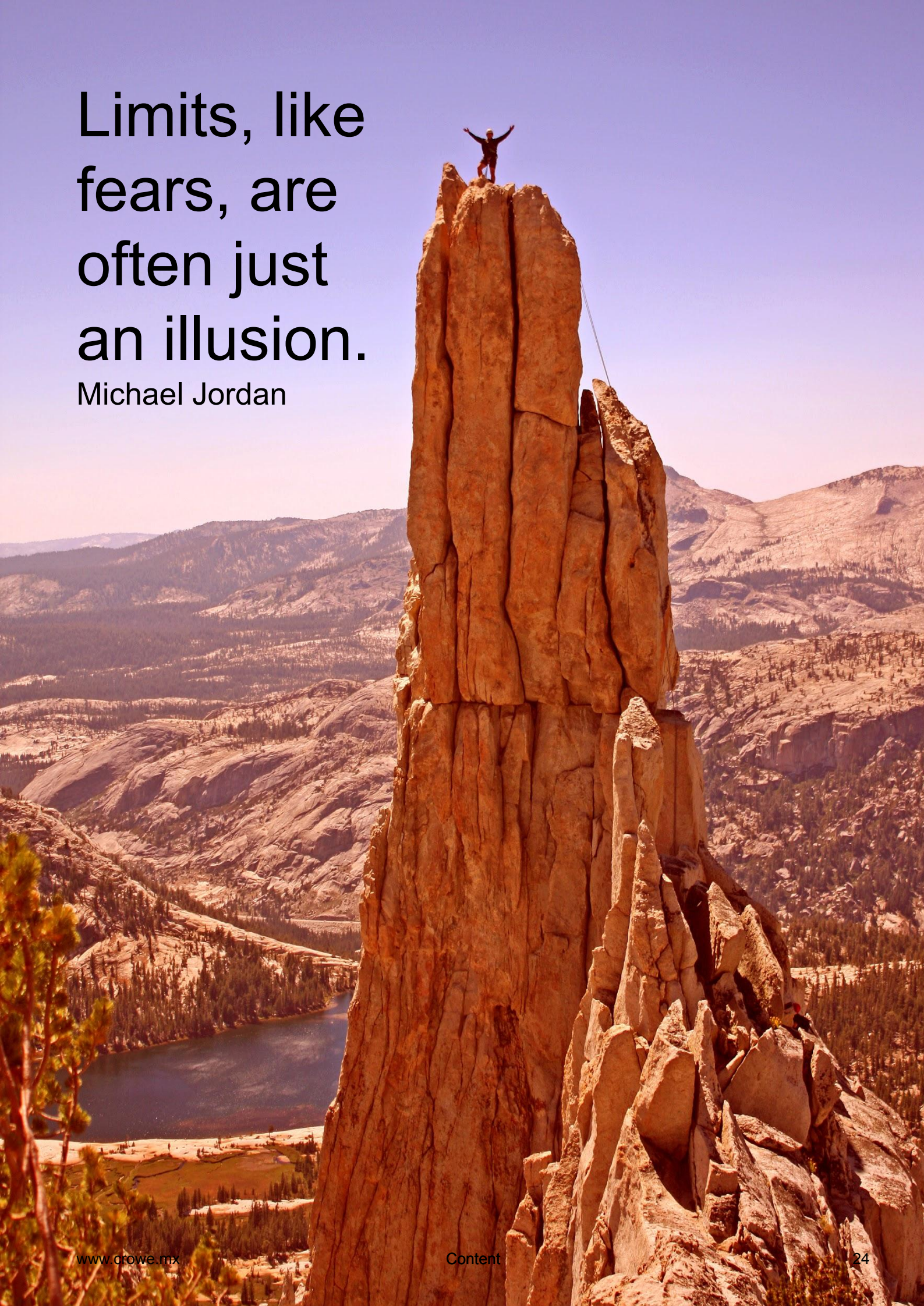
With the exception of savings and loans corporations, the rest of the Auxiliary Credit Organization should be constituted under form of a legal Stock Corporation.

- Credit Unions.
- Savings and loans corporations.
- General Deposit Warehouses.
- Factoring corporations.
- Money Exchange Office.



Limits, like  
fears, are  
often just  
an illusion.

Michael Jordan





## Chapter 3 Types of Business Entities

Mexico recognizes various types of business organizations such as corporations, limited liability companies, limited partnerships, joint ventures and co-operative, among others.

### Foreign Investment

Effective as of December 28, 1993, the new Foreign Investment Law (the "FIL") opened the doors to foreign investors in general to invest in various economic activities previously restricted by the former law. The following comments do not address NAFTA rules, which on occasions are less restrictive than the FIL.

With the exception of some activities, which are reserved exclusively to the Mexican Government or to Mexican individuals or corporations with a "foreign exclusion clause", the FIL allows foreign investors to own up to 100 percent of equity in Mexican Companies without prior approval from the Government.

The activities exclusively reserved to the Mexican government are:

1. Exploration and extraction of oil and other hydrocarbons;
2. Matters relating to planning and control of the national electrical power system and the public service relating to transmission and distribution of electrical power;
3. Generation of nuclear energy;
4. Radioactive minerals;
5. Telegraph and radiotelegraph industry;
6. Postal service;

7. Issuing of currency;
8. Coin minting;
9. Control, supervision and surveillance of ports, airports and heliports.

The following are activities reserved exclusively to Mexican individuals or corporations which expressly forbid foreign investment in their capital stock in its by-laws:

- Passenger, tourism and freight land transportation (exclusive of courier and parcel service);
- Development bank institutions; and
- Professional and technical services expressly provided in the applicable law.

Foreign investment in activities such as domestic air transportation, cable television and financial leasing companies are limited to certain percentages that range between 10% and 49%.

Other economic activities such as port services, cellular telephone services and insurance agents require prior resolution from the National Foreign Investment Commission in order for foreign investment to participate with a percentage greater than 49.

### Corporation

A corporation (Sociedad Anónima) is the most common type of business entity in Mexico. Subject to any applicable limitations under foreign investment laws and regulations, this type of entity can be fully owned by foreign shareholders.

Approval must be sought from the Ministry

of Economy to secure a corporate name. The principal features of a Mexican Sociedad Anonima are as follows:

1. Its ownership is comprised of stockholders whose obligations are limited to the amount of their contributions.
2. Mexican law requires a minimum of 2 shareholders to form a corporation, who may be individuals or corporate entities. Each shareholder must hold at least one share of stock.
3. Mexican law also requires an initial non-redeemable contribution to be made by the shareholders. This amount may be freely decided by the shareholders upon formation and should be spelled out in the articles of formation. The stock must be totally issued.
4. At least twenty percent of the initial contributions must be paid in cash upon formation.
5. A corporation may be organized as "Variable Stock", meaning that in addition to the initial contributions, the shareholders may provide for additional contributions which, as opposed to the founding contributions, are redeemable in nature. If the entity is formed as such, the corporate name must be followed by the designation "Capital Variable" or by its abbreviation "C.V."
6. The formation of a corporate entity (articles of formation and by-laws) must be passed before a Mexican Public Notary.

### **Limited Liability Company**

A Mexican limited liability company (Sociedad de Responsabilidad Limitada or S.R.L.) is a corporate entity organized by

individuals or business entities referred to as partners (as opposed to shareholders) who are liable only to the extent of their contributions. It is similar to a closed corporation in the United States. The principal features of a Mexican Sociedad de Responsabilidad Limitada are as follows:

1. The name of the company is selected at will and must be succeeded by the designation "Sociedad de Responsabilidad Limitada" or by its abbreviation "S. de R.L."
2. The company must be formed by no less than 2 and no more than 50 partners, who may be individuals or corporate entities. Each partner must hold at least one equity interest (as opposed to shares of stock).
3. As with the SA, Mexican law requires an initial non-redeemable contribution to be made by the partners. This amount may be freely decided by the shareholders upon formation and should be spelled out in the articles of formation.
4. At least fifty percent of the initial contributions must be paid in cash upon formation.
5. As with the SA, the formation of a Mexican Sociedad de Responsabilidad Limitada (articles of formation and by-laws) must be passed before a Mexican Public Notary.

Since the S.R.L. appears to be similar to limited liability partnerships in the United States (L.L.P.); some observers comment that they may be treated as partnerships for U.S. tax purposes under the "check the box" rule.

All business entities (as opposed to non-business entities) are governed by

federal statutes, which apply the same throughout the land.

## Limited Partnership

In this booklet, the phrase “limited partnership” is intended to convey the idea of an entity which is similar to LP’s in US corporate practice, which are common among law firms, accounting firms, finance firms and film production companies. These are in essence, non-business entities because they are not involved in commercial activities and as such, are governed by State law.

Generally speaking, the Civil Codes of the states of Mexico follow the footsteps of Federal Civil Code, which provides for two types of non-business entities:

- The “*Asociación Civil*” (A.C.), in which the partners decide to carry out a common purpose not prohibited by law and without a preponderantly economic objective. This structure is used by non-profit or charitable oriented organizations.
- The “*Sociedad Civil*” (S.C.), in which the partners join their resources and efforts to achieve a common purpose, which might have an economic objective but which should not have profit as its primary motive.

As noted above, service providers such as lawyers and accountants use this company structure, which has no minimum capital requirements. There are no limitations on the number of partners in a limited partnership (*Sociedad Civil or S.C.*), but there is a managing partner (which acts as general partner or member) who is jointly

and personally liable for obligations and debts.

## Branch

A foreign company can do business in Mexico by opening a branch, provided it has secured prior approval of the Ministry of Economy (*Secretaría de Economía*). The branch must be filed with the Public Registry of Commerce (*Registro Público de Comercio*).

Tax wise, there are no advantages to operate through a branch as opposed to operating through a subsidiary; on the contrary, from a liability point of view, a foreign corporation acting in Mexico through a branch is not a separate legal entity and therefore the foreign company may be liable for the obligations incurred by the branch.

Unlike a branch, a parent company is a separate legal entity and therefore, it has no liability for actions of its subsidiary.

## Joint Venture

Foreign investors may enter into a business together with other persons or companies by way of a joint venture. Under Mexican law a joint venture agreement is not deemed to be a corporate entity per se (unless it leads to the formation of a corporate entity, as explained below), and thus, there are no alter ego provisions which are similar to corporate entities. Partners usually enter into a joint venture agreement which may call for:

- The formation of a new separate entity or entities, or the restructuring of an

existing entity with additional shareholders, among other modifications (“joint venture company”), or

- The creation of a “joint venture” (*Asociación en Participación*) whereby one party (an individual or company) is active and the other inactive (an individual or company), which does not lead to the creation of a new entity.

### **Joint Venture Company**

Various persons may decide to incorporate a joint venture company to take advantage of the partners' knowledge of the Mexican business and industrial sectors, and to join efforts by bringing capital, technical assistance and technology together. The new entity or entities, formed or restructured company or companies, will be used precisely for the purpose determined, for example, to distribute products, render services, or build infrastructure.

Each of the shareholders or partners of the new or restructured entities may contribute capital, goods, services, and technology, thus enabling them by their efforts and knowledge to comply with the intended business purpose.

The new or restructured entity or entities will be a Mexican company, operating in accordance with the type of company chosen, will pay taxes and comply with its obligations as a normal company. The types of entities they may form are analyzed in Section XII.

### **Joint Venture Agreement**

If the parties to a project decide not to engage in the costs of creating a corporate entity, they may opt to execute an

agreement of “Asociación en Participación” (otherwise known as “A. en P.”), pursuant to which they agree to join efforts for a specific purpose or project, with the identity of only one of the partners known to third parties (the active or general partner), and the other or others having a more silent role (the limited partner or partners), who agree to the contribution of capital, services or otherwise.

The contract will set forth the agreement of the parties on how to distribute profits or share the losses deriving from the transaction.

Responsibility before third parties will reside with the active or general partner; but he or she will share responsibility with the silent or limited partner if the agreement so provides. Therefore, there will not be any relationship between the limited partner and third parties.

Typically the agreement will conclude upon completion of the project. Corporate wise, such an agreement does not create a new entity (although the JV will be taxed as a corporate entity), and each of the parties is liable to the other, without liability limitations, as per undertakings in the contract.

For tax purposes the active partner will comply with tax obligations of their common operation, including registration at the Taxpayers' Registry and provisional tax payments.

Every fiscal year each one of the active and the silent partners will have to accrue to their income, during the tax period, that part of the taxable profit corresponding to each one of them, or if applicable, they will deduct their proportional tax loss.





All things are  
difficult  
before they  
are easy.

Thomas Fuller



# Chapter 4 Organizing a Company

## Procedure of organizing a Company

Once the company type and ownership issues have been resolved, you will need to follow these steps:

1. **Corporate Name.** You will need to select a corporate name and apply for it with the Ministry of Economy. The permit will be released to the extent the corporate name is available and is not currently in use by another entity.
2. **Foreign Ownership.** Whenever any portion of the equity is held by foreigners, Mexican law requires that the by-laws include a covenant whereby any present or future equity holder agree to be treated as Mexican citizens and not to invoke any type of immunity from their countries of origin.
3. **Charter and By-laws.** The by-laws must spell out provisions relating to corporate governance, corporate purpose, term of existence, domicile, capital stock provisions, management powers and special provisions for winding-up the entity. In addition, you will need to decide how the initial capital will be contributed, how the Board of Directors and officers will be appointed and what powers will be specifically granted to individuals. Also, it is regular practice in Mexico to grant powers of attorney. The charter and by-laws must be taken along with the permit from the Ministry of Economy to a Notary Public (Notario or Corredor Publico) to formalize the incorporation. If the actual founding shareholders or partners will be executing the articles of incorporation, proper visas need be obtained. A temporary businessman visa for this event (FMN) is acceptable. If one or more corporate entities will be acting as founding shareholders, an individual with power of attorney for these entities must sign the document.
4. **Tax Registration.** Immediately after incorporation, the company must be filed with the Federal Taxpayer's Registry (Registro Federal de Contribuyentes, otherwise known as RFC), with the Mexican Tax Administration Service (simply known as SAT), who will assign a tax identification number to the entity. Your tax ID number is necessary for all tax and accounting records, bank account openings and it must be on all company's invoices.
5. **Registry of Commerce.** After the notary public issues a notarial transcript, he or she usually handles registration with the Public Registry of Commerce (Registro Público de Comercio). If your company is not registered, it may create personal liability for shareholders and managers.
6. **Importer's Registry.** If your company will be doing any foreign trade, such as importing raw materials, components or finished products, you will need to register with the Importer's Registry (Padrón de Importadores) with the SAT. This step will take approximately 20 to 30 days, and the entire process is handled through the mail.
7. **Import/Export Programs.** Permits for maquila programs or IMMEX or other similar import/export programs can be obtained from the Ministry of Economy (Secretaría de Economía, herein

- referred to as SECON).
8. Foreign Investment Registry. Registration with the Foreign Investment Registry (Registro Nacional de Inversiones Extranjeras, herein referred to as RNIE) is normally handled by your attorney or sometimes by the accounting firm, who will need information about your shareholders, domicile and company directors.

■ **Additional Required Registrations.**

- The entity must be filed with the relevant Chamber of Commerce or Industry for your business. Under Mexican law, every business company must be affiliated with at least one of these chambers.
- Mexican Institute of Social Security (Instituto Mexicano del Seguro Social, known as IMSS).
- Employee Housing Institute (Instituto Nacional del Fondo de la Vivienda para los Trabajadores, known as INFONAVIT).
- National Institute of Statistics and Geography (Instituto Nacional de Estadística y Geografía, known as INEGI).

### **Starting operations**

Once your company has been formed in Mexico, you may start operations. Keep in mind these requirements.

### **Zoning and Environmental Regulations**

In most urban areas you will need to obtain a zoning permit from municipal authorities which identifies land use. In the

metropolitan area of Mexico City, many industrial activities are restricted, and business operations in residential areas are strictly controlled.

To carry out manufacturing activities, you must first submit an environmental impact statement with the Ministry of the Environment and Natural Resources (*Secretaría de Medio Ambiente y Recursos Naturales*, known as SEMARNAT). Your company may also need special permits for air or noise emissions, water discharge or solid waste.

### **Health or Sanitary Licenses**

Any activities that involve food preparation or the manufacture of medicines, nutrients, soil enhancers, fertilizers, pesticides or health products require licenses from the Ministry of Health (*Secretaría de Salud*).

### **Employment Issues**

Once you select your personnel, have labor contracts prepared. If no contract is executed, Mexican law will deem that an employment relationship exists and default rules will apply.

### **Immigration**

Any non-Mexican must secure a business visa to work legally in Mexico. These permits are obtained through the Mexican Immigration Institute (*Instituto Nacional de Migración*) and due to recent amendments, a two-tier process must be followed, starting with the Consular office having jurisdiction over the applicant. Securing a working visa in Mexico is a time consuming process and should be properly anticipated

because special requirements apply to specific nationalities. Please seek assistance from your legal counsel for your specific needs.

## Administration of a Corporation

The administration of a corporation is responsibility of one or several executives, who may be shareholders or non-shareholders.

### Board of Directors

When two or more executives are involved in the administration, they form the Board of Directors.

Depending on how your by-laws have been prepared, the Chairman of the Board will be appointed by the Board or by the shareholders meeting.

Unless to the extent specific requirements to the contrary have been adopted in the by-laws, the Board of Directors needs a quorum of at least 50% of its members to be able to conduct business. To be binding, a Board resolution must be approved by a majority of the directors present. In the event of a tie, the Chairman of the Board casts the deciding vote.

### General Managers

At a general shareholders' meeting, the Board of Directors or the corporate administrator may appoint one or more general or special managers who may or may not be shareholders.

The managers have some expressly conferred authority. Managers do not

require special authority from the Administrator of the board of directors to carry out their designated responsibilities.

### Powers

The Chairman of the Board of Directors and designated managers may, within their respective authority, grant authority in the name of the entity. Such authority is revocable at any time by the shareholders' meeting.

### Shareholders' Meeting

The shareholders' meeting is the supreme authority of a corporation. As such, in general shareholders' meetings, shareholders may agree to confirm all acts and operations by the company.

Shareholders' meeting may be classified as general or special (depending on whether or not special categories of shares have been issued), and these in turn may be ordinary or extraordinary (which refers to specific quorum requirements).

### General meetings

Must be held at least once a year within four months after the year end in order to discuss at least, the next topics:

1. Discussion, approval or modification of the Director's report.
2. Confirmation or nomination of the Board of Directors and officers.
3. Confirmation or nomination of the Statutory Auditor.
4. Determination of the fees payable to administrators and Statutory Auditor.
5. Approval of the financial statements for the prior year.



## Extraordinary meeting

May be held at any time. Non-recurring matters are usually discussed in these kinds of meetings requiring a higher quorum of attendance.

## Accounting and Reporting Requirements

### Books and Records

The Federal Fiscal Code establishes that the accounting records (for tax purposes) are composed of:

1. Ledger.
2. Accounting systems and entries.
3. Working papers.
4. Account statements.
5. Special accounts.
6. Corporate books (minutes of shareholders and board meetings).
7. Control of inventories and valuation method.
8. Disk, tapes or any other means of data storage that may be processed.
9. Tax-registrations electronic systems and equipment and the records produced by such equipment.
10. Documentation used to support the respective entries.
11. All documentation and information associated to compliance of tax provisions that proves income and deductions.
12. Other documentation required by other statutes.

As of 2015 and pursuant to the amended Federal Fiscal Code and its regulations, Mexican entities must send by electronic means the chart of accounts by only one occasion and every time it get changed.

Also, Mexican entities must send a monthly trial balance with initial balances, credits/debits of the period and ending balances. Your accounting software shall be able to process the following XML reports structured and ruled by the Tax Authority: chart of accounts, trial balance, journals, auxiliary of tax-invoice folios, ledger of accounts.

Every records made into the accounting could be audited by tax authorities.

A Company must retain its accounting records and supporting documentation for a period of five years (statute of limitation).

### Annual Reports

The Sole Director or the Board of Directors is required, as a matter of law, to submit to the shareholders' meeting an annual report, presenting as a minimum, the following:

1. The Company's business policies.
2. The accounting standards and procedures used in preparing the financial statements.
3. A balance sheet presenting the financial position of the company, a statement of income presenting the results of operation, a statement of changes in the shareholders' equity and a statement of cash flows.
4. Full disclosure notes to clarify or elaborate on information within the financial statements.
5. The opinion of the Statutory Auditor.

Unless other arrangements have been provided for in the by-laws, the annual report must be prepared and presented to the shareholders at least fifteen days before the scheduled date of the meeting in which the report is discussed.

Action is the  
foundational  
key to all  
success.

Pablo Picasso





# Part 2 Taxation

## Chapter 5 Introduction

### The Mexican Taxation System

#### **Federation**

The Federal Government through the Ministry of Finance & Public Credit (SHCP) imposes the General Tax charges on several sources, and the State Government Agents conjointly with the Local Governments Commissioners imposes the minor taxes. All taxes serve for the public good.

Nowadays, the Tax Administration Service (SAT), which is a division of the SHCP, strictly enforces the compliance of the Tax Laws, through its Central and Deconcentrated Offices.

#### **Legal Tax Treatment for Business**

When doing business in Mexico, operations must be carefully structured to achieve the desired legal tax treatment. It is convenient for the business parties to have available a copy of the Mexican Taxation Reference

Handbook, the be aware of which is the most suitable tax treatment to use. For that reason, professional advisory is recommended on the following items:

- The importance and complex implications on the legal and corporate structure of the entity we intend to start.
- The tax implications of the Mexican entity on your country of residency.
- Potential transfer pricing issues.
- Thin Capitalization restrictions.
- Labor-related tax issues.
- Business firm opening and operation formalities.

## Workers Profit Sharing Scheme (“PTU”)

One of the most uncommon obligations for a non-resident to understand is the “Employees Statutory Profit Sharing”, known as *PTU* scheme. Companies and individuals in Mexico having employees at their service must distribute 10% of the profit specifically calculated for this purpose. In some cases, this payment is limited to the employees’ monthly salary.

The Income Tax Law allows for the taxpayers to reduce their taxable income for an amount that represents the profit sharing paid within the year.

## Federal Taxation System

For Business Entities and individuals, the Fiscal year is the Calendar year as well.

Financial year may be any fixed twelve-month period scheduled by the

Entity, in compliance with the Incorporation Agreement articles of the Business Entity. For individuals, it may also be any fixed twelve-month period, according to the type of business performed.

In recent years, Mexican Tax Authorities had amended several Tax Laws not only to increase the amount of revenues collected but also to improve the rules observance by the Taxpayers.

Annual Tax returns must be filed before March 31<sup>st</sup> of each year for business entities and before the end of April for individuals.

The following is a list of the most important Tax Laws that affect a company or an individual doing business in Mexico.

### Federal Tax Laws

- Income Tax Law.
- Regulations of the Income Tax Law.
- Value Added Tax Law.
- Regulations of the Value Added Tax Law.
- Special Product & Services Tax Law (excise tax).
- Regulations of the Special Product & Services Tax Law.
- Customs Law.
- Regulation of the Customs Law.
- Federal Fiscal Code.
- Regulations of the Federal Fiscal Code.
- Annual Tenancy of Automobile & vehicle Tax Law.
- Automobile & Trucks Acquisition Tax Law.
- Social Security Quotas Law.
- National Housing Fund for Workers Law.
- Anti-money Laundering Law.



## Deductible Fringe Benefits for Employees

Employers contributions made for the social security system are deductible for tax matters.

## Non Taxable Fringe Benefits for Employees

This concept is not taxable for those who receive the benefits, if they do not exceed the set limit established.

In relation to the wages paid, the exempt part from income tax will be deductible for the amount equal to 53%, but when the employer reduces the benefits to its employees compared to those granted on a year before, then the deduction will be limited to a 47%.

## Social Security System

Companies or individuals who hire employees must make contributions to the Social Security System at a rate between 15.77% up to 35% on employee's basic income. Employees working for business entities or individuals also contribute for the Social Security but at a lower rate.

## National Housing Fund for Workers (known as INFONAVIT)

In addition, employers must contribute with an amount equal to 5% of their employees salaries to the National Institute for the Promotion of House Building to give the employees the possibility of acquiring their own home.

## Pension and Retirement Benefits

The income derived from these sources is not taxable provided that it does not exceed fifteen times the Measure Unite and Upgrade ("UMA") ➡. There is a tax payable over the part that exceeds this limit.

## Retirement Savings Fund (known as SAR)

Employees must also contribute to the Retirement Savings Fund in an amount of 2% of their employees' salaries.

INFONAVIT as well as SAR contribution are paid every two months and can be deductible for the employer taxes.

## State and Municipal Tax Laws

In the Mexican territory, almost every state imposes the same taxes. A list of the most important State Tax Laws is presented below:

- Annual Tenancy of Real Estate Tax Law.
- Payroll Tax Law.
- Acquisition of Real Estate Tax Law.

## Provincial Rates

There are no provincial rates. There is only one tax on income levied on a Federal Basis.

## Annual Tenancy of Real Estate

Acquisition of land and building properties is liable to taxation at a rate of 2% on the value in compliance with the city tax regulations on the property dealing business transaction price or the price list approved by the local government office authorities.

Property taxes are the major source of income for the interior cities of Mexico. This

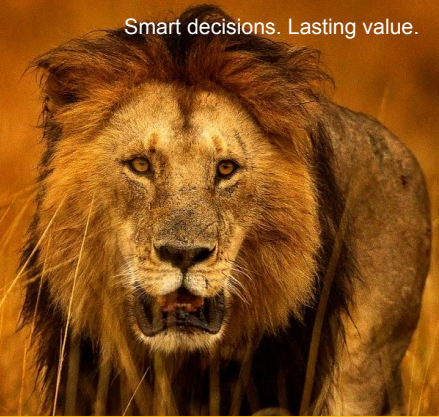
state tax is based upon a periodical reassessment set with very similar rates of the value market ratio. Each interior city applies specific estate rules, property values and taxation rates.

## Payroll Tax

In the majority of states, a tax is due on wages paid at a rate that may go from 1% to 3%.



**Business  
is in itself  
a power.  
Garet Garrett.**



## Chapter 6 Corporate Taxes

### Taxable Entities

According to article 1 of the Mexican Income Tax Law, every corporation, whether a resident or a non-resident, is subject to such a tax in Mexico. For tax matters, residents are also those who have permanent establishment in Mexican territory developing business activities. The following are some definitions.

#### Resident Firms

Headquarters, plants and facilities must be located into the Mexican territory. Resident Firms are taxable in their worldwide income obtained in cash, credit, services and so forth.

#### Non-resident Firms

Residents abroad with permanent establishment in Mexico for carrying out business activities or professional services are also taxable. If such a country had signed a Tax Treaty with Mexico, we

suggest to take a look into it in order to find any special treatment about permanent establishments.

### Tax payments

The majority of payments are due in respect of a financial year ending December 31<sup>st</sup>, except in cases of liquidation, mergers, acquisitions and splits.

Corporate Annual Income Tax Return must be filed before March 31st and some Annual Information Returns no later than February 15th. Penalties may be imposed when the taxpayer is delayed in these obligations.

Advanced payments of estimated tax (monthly, quarterly, biannual, depending on your tax regime) are made during the actual year as partial payments of Annual Tax. If the advanced payments exceed the amount due, a credit balance is created to be cleared or refund which may be requested.

During the first year of a Company there is



no obligation to pay these tax installments, but it is to pay the annual income tax.

### Tax offset

Starting 2019, the way taxes are offset changed, meaning that it is no longer applicable for withholding taxes, and VAT could only be credited against future VAT in charge.

## Income Tax

### Income and Deductions

Companies must include all income received, whether in cash, credit, payment in kind, service of any other type, including income originating abroad.

It is compulsory to take into account for taxation purposes the inflation gain and/or loss. The Income Tax Law (*Ley del Impuesto Sobre la Renta*) defines how to make all these calculations.

Exchange fluctuation also must be observed given that the exchange gain is taxable since the income tax installment. Exchange losses could be deducted only on annual basis. Federal Fiscal Code commands taxpayers to observe the official exchange rates published in daily basis on the Federal Official Gazette by the Central Bank of Mexico.

Attention is drawn to those deductions allowed by law, including most notably acquisition of raw materials and goods for transformation and sale, depreciation, overheads, interest, and so forth. Both general and certain specific conditions must be met in respect of certain types of

expense. The main condition is that the expense be strictly necessary for the purposes of the business.

Since year 2012, the Income Tax rate rate has been taxing the Net Profit of each Business Entity since its first year of operations, at a rate of 30%.

### Losses

Losses may be reduced from taxable profit during the next ten years from the date they were incurred.

The amount of the loss is adjusted to present value taking into consideration the inflation effects since the year in which it was incurred to the date it will be reduced. Subsequent adjustments can be added in case there is an excess still remaining after the first reduction.

### Depreciation

For tax matters, the only method allowed is that known as straight line, by application of fixed percentages on annual basis. As an example, among others:

Investment	Max %
Buildings	5
Vehicles	25
Office Equipment	10
Computers	30
Industrial Plan	Varying
Land	N/A
Renewable energy M&E	100

Inflation adjustment is allowed among the acquisition date and the half of the period during the year in which the fixed assets were utilized.



## Cost of Goods Sold

According to Income Tax Law, taxpayers are allowed to deduct the Cost of Goods Sold (COGS). The COGS shall be computed using the absorbing costing based on historic or predetermined costs.

Taxpayers with commercial (non-manufacturing) activities consisting in purchasing and selling finished products may compute the COGS considering only the purchased inventory, the inventory consumed and the ending inventory.

As for the inventory valuation, accepted methodologies are the following:

- First In - First Out
- Identified cost
- Average cost
- Detailed

## Transfer Pricing Regulations

According to the OECD international rules, transfer pricing regulations were adopted in the different Mexican Tax Provisions. Among others, these rules requires from the taxpayers to have documentation concerning the international related-party transactions such as sales, royalties, services, interests and so forth, in order to avoid an estimated tax adjustment from the Tax Authorities.

Article 180 of the Income Tax Law provides different methods to prove that companies met the transfer pricing regulations, which are:

- Comparable Uncontrolled Price Method (CUP).

- Resale Price Method (RPM).
- Cost Plus Method (C+).
- Participation Profit Method (PPM).
- Comparable Profit Method (CPM).
- Transaction Margins for Operating Profits Method (TMOPM).
- Statistic Method (SM).

A mandatory information return must be submitted during February of each year for those companies that performed any kind of transactions between related parties. This addition to the Federal Fiscal Code includes fines and penalties in the case of not filing it on time.

Also, since it is very common for a foreign company to work in Mexico under a *Maquiladora* Tax Regime, special rules applies in order to calculate its minimum taxable profit.

## Corporate Groups

Groups formed by a holding company have the option of calculating their tax liability based on their consolidated result.

Thereby benefiting from the possibility of compensating the losses of one or more subsidiaries against the profits earned by the remaining companies during the financial year.

Prior authorization is required from the SAT to exercise this option.

## Other Federal Taxes

### Value Added Tax

This tax is charged at a rate of 16% over the whole country, but some municipalities on the northern border region, can be granted a credit of 8%. This rate is not only for the final customer, but also for every time a transaction is made.

It is not paid on exports or on sales of (or services rendered to) food products, commodities, agriculture, medicine and grazers, which are zero-rated (0%), enabling the tax to be refund.

Starting year 2014 and onwards, there's a rate of 16% tax charged in the following activities;

- Imports in the border line,
- Purchase of bubble gums,
- Purchase of pets such as dogs, cats and other little species,
- Purchase of food for pets such as dogs, cats and other little species,
- Hotel services,
- Public transportation for people,
- Other transitional dispositions of 2014.

Also for year 2014, due to the reform of the Value Added Tax Law, the temporary import of goods for specified purposes is no more exempt from this tax.

As a result of the reform, companies under the correct tax and customs compliance could obtain a Certification (under some modalities), in which it would apply a consistent tax credit equivalent to 100% of the Value Added Tax or the

Special Tax on Products Services, on the temporary importation of goods.

### Special Tax on Products and Services

This indirect or special tax is due principally on the consumption of taxable goods and services, such as alcoholic beverages, filter cigars, gasoline, beer, wine, flavored beverages with any kind of sugar added, snacks, confectionery products, chocolates or any product with cocoa, flans, ice creams and popsicles, peanut butter and hazelnuts, products based on cereals, fossil fuels, pesticides, and this tax is applied at varying rates.

As well as for VAT, companies could obtain a certification for the 100% tax credit for the temporary importation of goods for specified purposes relates to the Special Tax on Products and Services.

This certification applies for both taxes, Value Added Tax and Special Tax on Products and Services, and once a company has it, it works for both purposes.



**Adapt.  
Build.  
Grow.**



# Chapter 7 Personal Taxes

## Taxable Individuals

Either an individual resident or a non-resident in Mexico can be subject to such a tax over his generated income.

## Residents

Individuals that have established their house in Mexico. When the individuals have a house in another country they will be considered as Mexican residents if their vital center of interest is on Mexican Territory. The vital center of interest will be considered in the following cases:

- When more than the 50% of the total income obtained by the individual comes from a source of wealth in Mexico.
- When in the Mexican territory the individuals have their main center of professional activities.

## Non-residents

Non-residents pay on income received from sources located into the Mexican Territory. They also pay taxes in Mexico if they set up a permanent establishment for the purpose of carrying out business activities or if they have a fixed base from which to offer professional services.

## Tax Payments

The majority of taxes are due in respect of a financial year ending December 31st except in cases of individuals paying taxes under the simplified rules, lower taxpayer rules, and so forth. Personal Income Tax

Return must be filed before April 30th and Annual Information Returns no later than February 15th. Penalties could be assessed when the individual is late on this obligation.

Advanced payments of estimated tax (monthly or quarterly) are made during the actual year as partial payments of Annual Tax. If the advanced payments exceed the amount due, a credit balance is created to be cleared or refund which may be requested.

## Taxes on Income

### Business Activities

Business entities and individuals carrying out business activities must include all income received, whether in cash, credit, payment in kind, service or any other type, including income originating abroad. It is compulsory to take into account for taxation purposes the inflation gain and/or loss. The Income Tax Law (Ley del Impuesto Sobre la Renta) defines how to make all this calculations.

Deductions, depreciation, amortization, losses and other concepts follow the same rules established for corporations (see Corporate Taxes paragraphs).

Pursuant to the Mexican Income Tax Law reform, since 2014, the maximum tax rate for individuals is 35%.

The rank for individual's annual income goes as follows:

Lower Limit	Upper Limit	Flat	Rate
0.01	6,942.20	0.00	1.92 %
6,942.21	58,922.16	133.28	6.40 %
58,922.17	103,550.44	3,460.01	10.88 %
103,550.45	120,372.83	8,315.57	16.00 %
120,372.84	144,119.23	11,007.14	17.92 %
144,119.24	290,667.75	15,262.49	21.36 %
290,667.76	458,132.29	46,565.26	23.52 %
458,132.30	874,650.00	85,952.92	30.00 %
874,650.01	1,166,200.00	210,908.23	32.00 %
1,166,200.01	3,498,600.00	304,204.21	34.00 %
3,498,600.01	From here	1,097,220.21	35.00 %

## Income on Personal Services

This type of income arises from the provision of services by an employee or by self-employed person. A progressive rate that may go up to 35% depending on the amount of the earnings applies on every individual activity except on the business activities explained below.

### Employee

In the case of income received by an employer, the employer must withhold at source the relevant amount of tax and prepare and to do annual tax return except those employees that:

- Inform by written to their employer that they will prepare their own annual return.
- Their annual salary exceeds 400,000 pesos.
- Working time with the same employer is less than the calendar year.
- They have simultaneously worked for two or more employers.
- When they earn income for the items referred to in this Chapter, from a source of wealth located abroad or

from individuals or entities not required to make the withholdings set forth in article 96 of this Law.

### Rights and obligations

They will be obligated to make retention and monthly declarations that will have a character of provisional payments on behalf of the annual taxes. There will not be retention to the individuals that only receive on daily basis an amount equivalent to the Measure Unit and Upgrade (\$102.68 MXN per day).

### Self-employed Individual

Income derived from the provision of services by a self-employed person is permitted to deduct the expenses related to his business activities at the time of the calculation of the tax due for the financial year. In the course of the financial year, he must cover monthly payments in advance in settlement on his tax liability.

Business entities making payments to self-employed individuals, must withhold 10% at source, this being an amount which the individual may use as a credit towards his provisional monthly payment.

## Capital gain on sales of assets

It is possible to calculate the tax liability charged on sales of assets by deducting the historical cost adjusted to the current date value, from the income obtained. It is permitted only when the sale of assets is not at all in relation with the business activities of the individual or the entity. In order to make the historical cost to current date value adjustment, it is necessary to consider the inflation factor held between the acquisition date and the disposal date, this in the case of land, buildings and movable assets.

## Dividends

The shareholders that receive dividends from a business entity may elect to include them with their other income and apply a progressive rate, being able to obtain repayment of tax, resulting in a rate lower than 30%. At no time, a higher rate will result.

A withholding tax applicable for dividends paid to foreign residents or Mexican individuals apply since 2014 year. This withholding tax is not imposed for dividends coming from profits generated before 2013 year.

## Leasing of Property (Rentals)

Cost incurred during the year may be deducted from the income arising from rentals when these are properly documented or the taxpayer may elect to a relief of 35% over the total rental income without the need of gathering any type of document. Besides the tax relief, taxpayers could also deduct the payment of the annual property tax.

## Royalties

This type of income is liable to taxation at a progressive rate. Royalties must be included in the annual tax return.



Care.  
Share.  
Invest.  
Grow.



# Chapter 8 International Rules

## International Rules

In the last few years Mexican Tax Laws had been amended and adopting worldwide tax trends in order to improve its business conditions. International organizations like OECD had been asked Mexican Government for better tax circumstances. Furthermore, Mexican Government has taken part of the Convention on Mutual Administrative Assistance in Tax Matters → currently, 127 jurisdictions participate on it.

### Tax Treaties

Treaties for the avoidance of double taxation (DTT) with many countries including Canada and the United States are now effective. Many other treaties are in the process of being negotiated and it is expected that Mexico's treaty network will be greatly expanded in the next few years. Nowadays there are 56 DTT in force.

### Taxes covered by treaties

The majority of treaties apply on income taxes imposed by each of the contracting states. Every country applies different rates depending on the types of income or transaction done under the treaty.

### Withholding Taxes

Withholding Tax on payments made by Mexican resident to a non-resident is due by application of the following rates (according to domestic law), among others:

Double Taxation Treaties may provide reduced withholding tax rates depending on the country of residents of the foreigner.

Treaties for avoidance of double taxation		
Argentina	Hong Kong	Panama
Australia	Hungary	Peru
Austria	Iceland	Poland
Bahrain	India	Portugal
Barbados	Indonesia	Qatar
Belgium	Ireland	Romania
Brazil	Israel	Russia
Canada	Italy	Singapore
Chile	Jamaica	Slovak Republic
China	Japan	South Africa
Colombia	Korea	Spain
Czech Republic	Kuwait	Sweden
Denmark	Latvia	Switzerland
Ecuador	Lithuania	Turkey Republic
Estonia	Luxembourg	Ukraine
Finland	Malta	United Kingdom
France	Netherlands	United Arab Emirates
Germany	New Zealand	Uruguay
Greece	Norway	USA

Income (pesos)	%
Salaries	
\$0 - \$125,900	Exempt
\$125,900 - \$1,000,000	15%
\$1,000,000 – on	30%
Professional Fees	25%
Interests	Varying
Tech. Assistance & Royalties	25%
Goodwill	30%
Leasing	25%



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