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# *T@x Bulletin*

## *Mexican Tax Reforms 2008*



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## Introduction

Last June 20, 2007 President Calderon sent the tax reform initiative for 2008 to Congress. This initiative was to be approved before last September 8 when the president was to present the revenue and expense budget for 2008, under a less-than-favorable political climate.

Once more because of this political climate, the possibility of taxing medicines and food through the Value Added Tax was not retaken, which apparently would turn out to be the more efficient way to raise funds, keeping the tax equity and proportionality so sought out by the people without creating new taxes.

To the unfavorable political climate, the problem that has already been discussed by all economic sectors of the country should be added. This problem consists of the need to not depend on the oil revenues, which can vary from one moment to the next and would cause us to lose productivity and competitiveness in the international setting. In this regard, the president explains in his initiative that in the last 18 years Mexico barely collected 9.5% with respect to Gross National Product "GNP" when the average of the Organization for Cooperation and Economic Development "OCDE" member countries is 24.9% of the GNP.

Therefore, the initiative was organized in the following fundamental issues: a) establish an equitable and simple system that prevents tax evasion and elusion; b) increase collection through flexible instruments that do not affect investment; c) reinforce tax federalism by granting more resources and faculties to the States; d) improve public spending and accountability; e) decrease tax evasion and elusion; f) make tax burden more equitable by reducing preferential treatments and exceptions found in the current legislation; and g) fight informality.

Sadly, we recognize today that the reforms approved by Congress last September 14 do not achieve the objectives suggested by the Federal Government regarding tax simplification given that at the beginning of the following year we will have two new taxes: the Flat Rate Business Tax (IETU) and the Cash Deposit Tax (IDE), which are suggested mainly for collection purposes and will require the implementation of controls or process changes for proper compliance by the taxpayers.

As usual, it is necessary to remember that when these provisions come into effect, they will render the previous administrative resolutions, authorizations or permits, general or particular, in opposition to the content of the reformed laws, ineffective.

Taking into consideration all the above information, this bulletin addresses the reforms that in our opinion are more important although the administrative authorities may not share it. Therefore, we invite you to join us in analyzing each case in particular.

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## Executive Summary

### 1. Flat Rate Business Tax Law (IETU Law)

1. The **subjects obligated to pay this tax** are:
  - a) Mexican individuals, regardless of the activity they conduct even if the revenues do not originate from business activities provided they fall under the generation of revenues from Fees, Leasing or Business Activity.
  - b) Mexican companies; general regimen, controlling, simplified regimen and overall any company since the rule makes no exceptions.
  - c) Non-Lucrative Companies, except those authorized as beneficiaries provided that they fulfill requirements regarding non-determination of the Distributable Remainder, either alleged or distributed.
  - d) Nonresident with permanent establishment in the country with respect to the revenues attributable to such establishment.
2. The **applicable rate** for the determination of the tax amounts to **17.5%**, however, for 2008 and 2009, by transitory provision rates of 16.5% and 17.0% were respectively established.
3. The **IETU base** will be determined:

	Revenues effectively collected
(minus)	(Deductions effectively spent)
	Tax Base
(times) X	Rate (16.5% in 2008, 17% in 2009 and 17.5% thereafter)
	Tax of the Period

4. **Activities that give rise to payment of tax** are contemplated to be:
  - a) **Alienation** of Goods.
  - b) The **Provision of Independent Services**.
  - c) **Granting the temporary Use or Enjoyment** of Goods.

Expressly excluded from tax are:

- Revenues from Royalties between Related Parties,
- Interests that are not part of the price of the good,
- Derivative Financial Operations with underlying revenues not subject to IETU,
- Revenues derived from the alienation of shares and outstanding documents,
- Revenues derivatives from the alienation of foreign currency, unless it is the taxpayer's activity (90%), and
- Revenues obtained as accidental business acts for Individuals.

It is important to point out that the object is limited since dividends, donations or individual compensations are not subject to the law.

The definitions of these concepts contemplated by the Value Added Tax Law (VAT Law) are taken as valid for these purposes.

5. For the **determination of revenues obtained in the calculation of the IETU base** the following guidelines will apply:
- a) We will depart from the **agreed upon price or consideration** and add the amounts charged to or collected from the counterpart including the advances or deposits made.
  - b) **Advances or deposits** granted and given back to the taxpayer as well as the rebates and discounts received will be considered revenues when in any of these instances the amounts were considered deductions at the time.
  - c) The revenue is recognized when **effectively collected** (cash) in terms of article 1-B of the VAT Law.
  - d) If payment of the consideration is received in goods or services, either the **market value** or the appraisal value will be considered the revenue.
  - e) It is specified through transitory provision that **the revenues from activities conducted before the Law became effective will not be considered for purposes of determining the IETU starting on January 1, 2008** although payment is received after that date, unless only the portion of the revenue effectively received was chosen to be considered for purposes of IT.
6. Among the problems the impossibility **for nonresidents to accredit the IETU paid in Mexico** stands out, since in terms of the international Agreements signed to prevent double taxation, Crediting or preferential treatments of taxes other than Income Tax are not contemplated. **The Tax derived from the IETU Law is not creditable** according to International agreements.
7. **Revenues exempt from contribution** will be recognized as those obtained by:
- a) The Federation, States, Cities and Parastatal Public Administration.
  - b) Revenues not subject to payment of IT, but obtained by:
    - **Unions and Political Parties,**
    - Civil Companies and Associations for **scientific, political, religious and cultural** (without sport facilities greater than 25%) **purposes,**
    - Commerce and Industry **Chambers,**
    - Civil Companies and Associations incorporated to **manage funds or savings bank,** and
    - **Parent Teacher Associations.**
  - c) Non-Lucrative Companies (PMNL) **recognized as authorized as beneficiaries as long as:**
    - Their assets are used in the development of the corporate objective,
    - No benefits over the Distributable Remainder are granted to any individual, and
    - They do not **fall under any of the remaining assumed remainder assumptions,** situation which becomes an absurdity of the standard since these are nondeductible items.
  - d) Individuals and companies from **agricultural, livestock, forest or fishing activities** exempt from the payment of IT.
8. The **limited scope of exemptions to subjects in lesser manners than contemplated by the Income Tax Law** will immediately result in that **starting January 2008 and though not obligated to pay IT, the following subjects would be obligated to pay IETU.**
- a) Neighborhood Associations and Condominium Goods Administration Associations,

- b) Education institutions with official recognition without authorization as beneficiaries,
  - c) Cooperative Goods and Services' Production Companies, and
  - d) A significant number of authorized beneficiaries that the mere fact of incurring in nondeductible items would cause them to lose all exemptions, and preventive measures will have to be taken in that regard.
9. The tax base will be determined **by deducting from the revenues the deductions** applicable for which the following rules are established:
- a) As in the revenues, in order for the deductions to be subtracted, they will have to have been **effectively spent**.
  - b) The feasibility of deducting all **acquisition of goods, provision of independent services, payments for the temporary use or enjoyment of goods** is contemplated, if all are used to obtain the revenues burdened by the IETU Law. This order of ideas includes all expenditures from the activities of the taxpayers.
  - c) Acquisition of fixed **assets, land, inventories** and goods acquired because of the conduction of the taxpayer's activities.
  - d) The following items and payments **will not be deductible within the scope of the deductions**:
    - Salaries and Wages,
    - Payments for items made similar to Salaries,
    - Benefits derived from the labor relationships,
    - Benefits paid as a consequence of terminating the labor relationship,
    - Contributions due to IMSS, INFONAVIT, Informality Tax and their own IT,
    - Interests that are not part of the price of the good,
    - Self-billing items found in valid provisions (regardless, through a transitory provision, those corresponding to the first alienation conducted by individuals from the agricultural sector prevail for 2008),
    - Donations exceeding 7% of the taxable income of the year,
    - Deduction of investments related to depreciation and amortization,
    - Tax Cost of Land acquired before the Law came into effect,
    - Creation and increase of technical reserves in insurance companies in cases of coverage of risks other than life insurance or pension plans,
    - Creation and increase of technical reserves in the case of Bond Companies.
  - e) The deductions shall meet all the deductibility requirements established by the Income Tax Law.
10. Given that the Law forbids the deductibility of the amounts corresponding to salaries and wages, payments to items similar to salary and social security contributions, the benefit that would annul the negative effect that have called "**Labor Burden Credit, Payments of Items Similar to Salary and Peripheral Cost**", which will result of applying the valid IETU rate to all of the payments made in the period is included.

Therefore, it stands out that the amount of this credit will not be calculated for the benefits derived from the labor relationship or for those revenues of individuals **that do not give rise to the calculation of tax because they are exempt revenues according to the Income Tax Law**.

The amount of this credit, applicable in estimated payments and the determination of the tax of the year, will be calculated as follows:

	Expenditures for salaries and payments for the termination of Labor Relationship.	\$10'000,000
(minus)	(Exempt portion of revenues)	(1'200,000)
	<b>Salaries and Benefits taxed in Chapter I of the MITL</b>	<b>\$ 8'800,000</b>
(plus)	Payments of Items Made Similar to Salaries	2'000,000
(plus)	Contributions to Social Security paid in Mexico	1'840,000
	<b>Total subject to "Labor Burden Credit, Payments of Items Made Similar to Salaries and Peripheral Cost"</b>	<b>12'640,000</b>
(times)	Effective rate in the period in question	16.5%
	<b>Applicable credit</b>	<b>(2'085,600)</b>

11. To try to avoid the significant imbalance not recognizing the deductions that do not imply cash flow and not recognizing the tax cost of investments that can be alienated would generate and with that break proportionality elements, a preferential treatment is established for **Investments made before the IETU Law came into effect**. This treatment generates, in the investments made during the last four months of 2007, the right to a deduction distributed in three periods and as for the investments made in the last ten years, a credit against the tax will be obtained.

The benefits include:

- a) An **Additional Deduction equivalent to a third per fiscal year from 2008 to 2010 of the value of new investments** that were effectively spent in the period from September 1 to December 31, 2007. For purposes of estimated payments, the corresponding amount of each period will be divided by twelve thus obtaining the applicable amount for each one of the months, and
- b) A Tax Credit for the deductible investments that were deducted in the period between January 1, 1998 and December 31, 2007, for which it is necessary to consider:
  - The balance pending deduction for each one of the investments as of January 2, 2008 will be determined,
  - This balance will be updated from the month in which the good was acquired and through December 31, 2007,
  - This result will be applied the tax rate in force (16.5% for 2008) and to the new result a 5% to obtain the Crediting corresponding to each period during the ten periods from 2008 to 2017,
  - Once the annual credit is determined, it will be subject to annual restatement from December 2007 through the sixth month of the period (June) in which it is applied.
  - For purposes of estimated payments, a twelfth of the annual credit will be considered in each one of the months of the period, and the restatement will be calculated as of December of the immediately previous period,
  - The credit referred to in assets acquired between September and December 2007 for which the additional deduction was taken will not be applicable,
  - In cases of investments that were not fully spent, only the amount spent up to December 31, 2007 will be considered, and
  - If any of the goods that give rise to the calculation of the credit is alienated, a recalculation should be made so as not to apply credit for this asset starting in the period when the alienation took place.

Calculation of the Credit for Investments 1998 – 2007 Machinery acquired in May 2004 (annual depreciation rate: 11%)			
	Maximum Original Amount deductible from the Good	\$	4'600,000
(minus)	(Historical deduction at closing of the previous period)		(1'813,167)
	<b>Balance Pending Deduction as of January 1, 2008</b>		<b>2'786,833</b>
(times)	Restatement (acquisition as of December 2007 assumed)		1.1150
	<b>Restated Balance pending deduction</b>		<b>3'107,319</b>
(times)	IETU rate in force in 2008		16.5%
	<b>Tax Base to determine crediting</b>		<b>512,708</b>
(times)	5% rate		5.0%
	Amount of Credit in 2007 (Previous before Current)		<b>25,635</b>
(times)	Restatement (December 2007 to June 2008 assumed)		1.0175
	<b>Applicable credit in the Period</b>		<b>26,084</b>
(divided)	by twelve		12
	<b>Amount of Credit applicable to each one of the months in Estimated Payments</b>	\$	<b>2,174</b>

12. A negative effect for the taxpayers is that the IETU Law ignores any type of benefit of deduction, decrease or credit related to:
- Tax losses carried forward** and pending subtraction from results of up to the following ten periods,
  - Land acquired before** the Law came into effect, and
  - Inventories as of December 31, 2007**, which when there was a change in the Income Tax Law always recognized some method for the transition phase.
13. For **Small Taxpayers**, the IETU, as with IT and VAT, will be determined through a fixed rate that should be paid to the tax authorities of the State in question. For these purposes, the authorities will consider the creditable IT, the deductions that took place and the tax rate to determine a contribution compatible with the capacity and characteristics of the taxpayer.
14. The tax is **determined by periods** and the taxpayer is obligated to:
- File an annual return no later than March 31 or April 30 of each year, as corresponding to individuals or companies, and
  - Make **monthly estimated payments** on the 17<sup>th</sup> of each month for which the revenues and deductions accumulated at closing of each one of the months in question should be considered.
15. If in any of the periods the taxpayer determines an **excess in deductions over revenues** (which could be equivalent to a loss but considering the limited deductions), the taxpayer would be entitled to determine a **“tax credit”** applicable to:
- The **income tax rate generated in the period**, in which case the tax credited can no longer be credited against IETU, or be entitled to any refund, or
  - The **tax of the period (IETU) and estimated payments of up to the ten following periods.**

	Revenues effectively collected		10'000,000
(minus)	(deductions effectively spent)		(12'000,000)
	Excess Deductions over Revenues		(2'000,000)
(times) X	Valid rate for the period in question		16.5%
	Applicable credit		(330,000)

**The amount of the credit will be adjusted** as per the restatement factor resulting of dividing the NCPI of the last month of the period in which the credit is generated (December) by the index of the last of the of the first half (June) of the referred-to period.

For the following period, the credit will again be adjusted until depleted, from the last time it was adjusted and through the last month of the first half (June) of the period in which it will be credited.

**If the credit is not applied in spite of being entitled to do so**, this benefit will be lost for up to the amount that could have been credited.

16. Some of the **obligations for the taxpayer** derived from the IETU Law are:

- a) Keep books,
- b) Issue vouchers for the activities conducted,
- c) When dealing with operations conducted with related parties, the prices and considerations will be determined according to the existing provisions related to comparable operations and,
- d) When dealing with taxpayers with goods subject to the co-ownership or conjugal partnership regimen, a common representative can be designated to comply with the provisions deriving from the IETU Law.

17. The special treatments contemplated by the new IETU Law include:

- a) The **Trusts**, which will be transparent for IETU purposes, and those taking part therein will be the subjects who in the end will generate the contribution that applies. For this purposes, it will be the Fiduciary Institution which will be obligated to comply with the obligations deriving from those Trusts for the conduction of business activities. However, this is not applicable to those called "Fibers", which only enjoy the benefit of not being obligated to make estimated payments.
- b) The **Tax Consolidation** is not contemplated in the IETU Law regardless of whether it was chosen according to the Income Tax Law.

18. To determine the Tax (IETU) of the Period, the following procedure will be followed:

If there were a IETU difference to pay in the period		
	Revenues effectively collected in the Period	\$ 100'000,000
(minus)	(Deductions effectively spent in the Period)	(92'000,000)
(minus)	(Additional deduction for Investments Sept.–Dec. 2007)	(460,000)
	<b>Tax Base of the Period</b>	<b>7'540,000</b>
(times) X	Rate (16.5%, 17.0% and 17.5% as applicable)	17.5%
	<b>IETU of the Period</b>	<b>1'319,500</b>
(minus)	(Credit for Investments 1998 – 2007)	(26,084)
	<b>Net IETU of the Period</b>	<b>1'293,416</b>
(minus)	Credit for excess deductions over Revenues of previous periods (Art. 11)	0
(minus)	Credit for tax burden, items made similar to salaries and peripheral costs	(875,900)
(minus)	IT of the Period (without crediting or reductions)	(120,000)
	<b>Net IETU payable of the Period</b>	<b>222,116</b>
(minus)	Estimated IETU Payments effectively made	(164,380)
	<b>Net IETU payable</b>	<b>\$ 57,736</b>

However, if it is not possible to credit fully or partially the estimated IETU payments made, the uncredited amount can be offset to the Income Tax of the same period and leave a remainder which can be asked to be refunded.

If there were estimated IETU payments in favor and that consequently can be offset or asked to be refunded		
	Revenues effectively collected in the Period	\$ 100'000,000
(minus)	(Deductions effectively spent in the Period)	(92'000,000)
(minus)	(Additional deduction for Investments Sept.–Dec. 2007)	(460,000)
	<b>Tax Base of the Period</b>	<b>7'540,000</b>
(times) X	Rate (16.5%, 17.0% and 17.5% as applicable)	16.5%
	<b>IETU of the Period</b>	<b>1'244,100</b>
(minus)	(Credit for Investments 1998 – 2007)	(26,084)
	<b>Net IETU of the Period</b>	<b>1'218,016</b>
(minus)	Credit for excess deductions over Revenues of previous periods (Art. 11)	(330,000)
(minus)	Credit for tax burden, items made similar to salaries and peripheral costs	(875,900)
(minus)	IT of the Period (without crediting or reductions)	(120,000)
	<b>Net IETU payable of the Period</b>	<b>0.00</b>
(minus)	Estimated IETU Payments effectively made	(164,380)
	<b>IETU to be offset to IT of the period or otherwise ask for the refund</b>	<b>\$ (164,380)</b>

19. When the revenues for the IETU Law are presumptively determined, the deductions, if any, that are confirmed will be deducted and the corresponding rate according to the period in question will be applied to the result. Anyway, as an option, the taxpayers can apply a 54% coefficient to revenues presumptively determined and the result will be applied the corresponding tax rate, which will result in the omitted contribution payable.

## 2. Asset Tax Law (ATL)

The Asset Tax law was revoked as of January 1, 2008 and to avoid effects that hurt taxpayers who effectively paid the tax in the last ten years and that consequently will see their right to refund limited when excesses are generated as contemplated in still-valid article 9 of the AT Law, the following preferential treatment is established:

- a) A refund can be asked of the adjusted asset tax amounts effectively paid in the ten periods immediately preceding the period in which the income tax is effectively paid, provided that these amounts have not been previously refunded or the right to ask for a refund has not been lost.
- b) For them, the amount subject to refund cannot exceed the difference between IT of the period and the asset tax paid that was the smallest in fiscal years 2005, 2006 or 2007.
- c) For these purposes, in no case can an amount exceeding 10% of the tax paid and subject to refund be requested.

### 3. Cash Deposit Tax Law (LIDE)

What was originally proposed to Congress as “Tax against Informality”, finally was approved as “**Cash Deposit Tax Law**” (LIDE) and its objective, which in our opinion will not necessarily be attained, is to tax all those individuals making cash deposits from conducting activities under informality.

The standard distinguishes as items that deserve our analysis and consideration those summarized below.

1. **This Law will come into effect on July 1, 2008** and this is essentially the result of the Bank Institutions’ immediate impossibility to collect the IDE.
2. The **tax rate amounts to 2% and will be calculated on the monthly amounts exceeding \$25,000.00 in cash deposits** made in all accounts the taxpayer has in any Financial System Institution, including those to be deposited in installments.
3. Individuals and Companies will be obligated to pay the Tax **except for**:
  - a) The Federation, States, Cities and Parastatal Public Administration Entities,
  - b) Non-lucrative Companies in terms of Title III of the MIT Law,
  - c) Individuals and Companies for monthly deposits not exceeding \$25,000.00 in each month of the fiscal year,
  - d) Financial System Institutions regarding the cash deposits made in own accounts because of financial intermediation or purchasing/selling foreign currency,
  - e) Individuals regarding deposits that come from the remuneration of subordinated personal services received by nonresidents in diplomatic functions, and
  - f) Individuals and Companies for deposits made in their accounts from credits granted by Financial System Institutions.
4. The Financial System Institutions:
  - a) Will collect the tax at the end of each month and will be jointly responsible for the payment of the tax in case of omission. If the institution cannot collect the tax due to a lack of funds of the taxpayer, it should be reported to the authorities through a monthly return.
  - b) Pay the tax collected in a period not exceeding three days.
5. The tax established in this Law effectively paid in the period in question, **will be creditable against income tax payable in said period**, unless it was previously credited to income tax withheld from third parties or offset against other federal contributions payable or if it was requested as refund.

### 4. Mexican Income Tax Law (MITL)

#### 1. Value of Assets of the Year

From the abrogation of the Asset Tax Law, all references to the ATL are eliminated and a procedure for the determination of the value of assets of the year for purposes of tax consolidation as well as to obtain the income from “Safe Harbor” for purposes of maquila companies that apply this option is included. Therefore, the method the ATL had to determine the value of the assets is included.

#### 2. Cash deposits from Loans or Contributions for Future Capital Increases

Starting January 1, 2008, there is an obligation to report to SAT within 15 business days after the cash deposits from loans or contributions for future capital increases for over \$600,000 pesos were made in either domestic or foreign currencies. The SAT will issue, through general rules, the means or formats for such

purposes, otherwise they will be considered taxable income.

**3. Deductibility of Salaries**

New rules for deduction of salaries from employers are added, such as comply with the rules of the new employment subsidy and they are given to the employees.

**4. Limitation to Donations**

The donations will now be deductible for up to an amount not exceeding 7% of the taxable income of the company or of the taxable revenues in case of individuals, obtained during the previous fiscal year.

**5. Losses from irrecoverable credits**

In the case of deduction from irrecoverable credits, the maximum amount applicable up to 2007 substantially increases from \$20,000 if overdue more than a year to 30,000 UDIS (\$118,000 pesos approximately); the deduction will be applicable in the month that marks one year past the due date.

**6. Non-deductibility of IETU and IDE**

The payments made for new taxes IETU and IDE and the new subsidy to employment will not be deductible for IT purposes, but can be credited.

**7. Losses on Alienation of Shares**

Maybe this is the most important IT reform and without a doubt it derives from the amount of verdicts issued by the Court, thus the term for amortization of losses sustained from alienation of shares starting in 2008 is extended, against gains on these operations of 5 to 10 years, and the requirements that should be fulfilled to earn the right to deduction of these losses are transferred from the regulation. The term of 5 years for the amortization of losses sustained before January 1, 2008 is maintained.

When shares are sold between related parties, a study on the determination of the sales price should be filed with the SAT within 10 days after the sale, applying the methodology established in the Law. This obligation will not be applicable to controlling companies with tax consolidation.

In operations conducted of shares issued by companies outside the group that generated losses, the deduction will only apply to earnings the controlling company has for sales of shares issued by companies outside the group.

**8. Informative return for Beneficiaries**

Starting 2008, non-lucrative companies engaged in researching or preserving wild flora or fauna and those engaged in the reproduction of endangered species should file a monthly informative return for the donations received.

Furthermore, all beneficiaries conducting operations with related parties, or acquiring goods or services from those giving donations should also report it to the tax authorities.

A 90-day term is established for SAT to issue rules for informative returns.

**9. Donations, Loans and Prizes**

The amount of donations, loans or prizes obtained during the period considered taxable revenues if not reported in a timely manner to the tax authorities is reduced from \$ 1'000,000 pesos to \$ 600,000 pesos. The amount should be considered jointly.

**10. Alienation of shares in stock exchange.**

Starting October 2, 2007, when his modification comes into effect, the alienations of shares conducted in recognized markets by individuals or group of individuals, residents or nonresidents, that directly or indirect hold at least 10% of the shares issued by the issuing company will cease to be exempt. These operations will be taxed regardless of whether they are conducted in a public bid or through any stock exchange operation.

For purposes of the above, the alienations to be taxed will be those conducted in a period of 24 months from the first alienation.

**11. Tax Rate for individuals**

The procedure used to determine IT is simplified. The tax rate and the subsidy table were integrated into a single rate for which a proportion of the subsidy of 86% was considered, resulting in a Creditable Subsidy of 72%, which means that those individuals that up to 2007 had a greater subsidy proportion will pay more taxes and those with a smaller one, will benefit from the reform.

**12. Employment Subsidy**

The Salary Credit is revoked and instead an Employment Subsidy is issued, applicable only to individuals with salary revenues. This subsidy is equivalent in money to the Salary Credit.

Method for crediting:

- a) This new subsidy will not be deductible, but can be credited to IT payable by the employer or the IT the employer withheld from third parties.
- b) A registry of payment of salaries should be kept
- c) Keep the payroll receipts or voucher of payment that shows the payment of salaries, the IT withheld and the employment subsidy amount for the employee.
- d) Fulfill employer obligations established in MITL
- e) If the employee has two or more employers, he should submit a letter, to be kept by the employer, stating whether or not the employment subsidy will be calculated for him.
- f) File the Informative Employment Subsidy Return each year.
- g) That Social Security and INFONAVIT fees were paid.
- h) Annual submit a certificate to the employee, informing him the Employment Subsidy amount determined by the employer.
- i) When applicable pay the Employment Subsidy amount in cash.

**13. Withholding Interest from Nonresidents**

Through annual provisions the possibility of applying a 4.9% rate to interest paid to foreign banks is ratified. To apply this withholding rate, it should be observed whether Mexico is under Agreement to Prevent Double Taxation with the country of origin of the foreign bank is ratified.

**14. Simulation of Acts**

The tax authority is given the faculty to determine the simulation of juridical acts for tax purposes, but only for acts between related parties. It is established that the taxable fact will be the one effectively conducted.

The authority should establish the following in its resolution: a) identify the simulated act; b) amount of the tax benefit obtained; c) indicate the elements used by the authority to determine the existence of the simulation, which can be based on any presumptive element deemed convenient.

This provision was added in the House of Representatives and may lead to abuse by the executing authority.

## 5. Special Tax on Production and Services' Law (LIEPS)

### 1. Draws and Gambling

A new 20% tax is established in this Law for games or draws requiring authorization from the Secretary of Interior and those conducted by decentralized organizations. Those conducting these activities can deduct from the amount of tax determined, the share corresponding to the Federal Government of the products obtained by the licensees, provided for in the Federal Gambling and Draws Law.

The tax on draws will be calculated taking into account the total value of the amounts effectively obtained by the participants; for bets, the total value of the bet will be taken as base.

This tax will not be generated on prizes under the following assumptions: a) conducted by charity institutions, companies engaged in teaching and Companies or Associations granting scholarships; b) in the case of draws, when all participants enter without having to pay, purchase or contract any service; c) in the case of draws, when the participant just for buying something or contracting a service enters for free, provided that the organizer of the draw obtains no more than 10 services a year and the total amount of prizes offered do not exceed 3% of the revenues obtained the previous year.

### 2. Alienation of Gas and diesel

An increase to current gas and diesel fees for final sale to the general public is contemplated as follows:

- Magna Gasoline, 36 cents per liter, at 2 cents per month for 18 months.
- Premium Gasoline, 43.92 cents per liter, at 2.44 cents per month for 18 months.
- Diesel, 29.88 cents per liter, at 1.66 cents per month for 18 months.

This increase should be included in the price and will not be broken down in the voucher. This increase will not generate VAT.

## 6. Tax on Ownership or Use of Vehicles' Law (ISTUV)

It is established that this tax will be revoked on January 1, 2012

## 7. Federal Tax Code (CFF)

### 1. Refund of Balances in Favor

It is establish that now the tax authorities can exercise the verification faculties in order to verify the origin of the balance in favor. In these cases, the 40-day term indicated in the CFF will be suspended for the time the verification faculties last. Once the authority finishes exercising the verification faculties, it should refund within ten days the balance in favor; otherwise, it will pay the taxpayer interest.

This period to verify will last 90 days and if information form third parties is required or in cases of large taxpayers, it will be 180 days.

The obligation to ask for a refund electronically is reduced from \$ 25,000 a \$ 10,000 pesos.

### 2. Joint Responsibility

When the space occupied as fiscal address is vacated without giving a notification of change of fiscal address a joint responsibility is incorporated for managers, sole administrators or directors. If the guarantee granted is insufficient, the term provided for in the current legislation is extended from 3 to 5 years.

### 3. Ratification of Signatures

In the cases where the signature of the legal representative is illegible or the authority doubts its authenticity, the authority is authorized to ask for the presence of the taxpayer to ratify the signature.

### 4. Verification faculties

With the current legislation the authority is authorized to review the same fiscal year and the same taxes already reviewed, if it is proved that there are different facts. It will now have the faculty to rely on the documentation contributed by the taxpayer as defense, that has not been provided to the authority during the inspection process.

### 5. Review of Reports

New assumptions are provide for so that the authority does not following the sequential procedure and can consequently begin its verification faculties directly with the taxpayer: a) The report is not effective; b) The Public Accountant issues his report without being registered, or else if he is suspended or canceled; c) The Public Accountant that issues his reports vacates the premises occupied without presenting the corresponding notification; and d) the taxpayer is reviewed for foreign trade taxes.

### 6. Authority presumptions

It is provided for that the deposits made in bank accounts of the taxpayers not registered in the Books of the Taxpayer will be considered taxable revenues, if the books are requested by the authority and the taxpayer does not provide them.

The deposits equal to or greater than \$1'000,000 pesos, made to individuals that are not registered in the Federal Taxpayer Registry or if they are, they are not obligated to keep books.

This is not applicable to cases where the taxpayer notified the administrative authority previously by means of the formats issued for such purposes.

### 7. Responsibility of Third Parties

Third parties providing services that end up in the partial or total omission of taxes, when provided in breaching the tax provisions, will carry responsibility in the payment of fines. However, this responsibility will be eliminated when in the service provided it is reported that the responsibility differs from the non-linking criteria or that can be opposed to the opinion of the tax provisions.

### 8. Tax Fraud

Tax fraud is assumed when there are revenues derived from operations conducted with resources of illicit origin.

## 8. FOREIGN TRADE

### 1. Reasons to migrate to IMMEX program

- a) To create an Act to promote exports to allow facing up to worldwide competition.
- b) Make the existing benefits more aggressive and create new ones.
- c) Link new benefits to other programs like PROSEC and VAT refund.
- d) Grant the same administrative opportunities, tax benefits and tariff advantages for two acts that seek the same thing.
- e) Equal the amount of processes.

## 2. New benefits of the IMMEX program

### a) New services that can be operated with the IMMEX program are created

- Call Centers.
- Human Resources (processing payroll, managing benefits).
- Accounting (accounts payable, receivable, vouching expenses, bank reconciliations).
- Supply (processing orders, following up on orders, tracking merchandise, billing).
- The car industry allows: the design, reengineering, testing
- The textile and fabrication industry: design, development of brands, quick response to market and tailoring.
- Sub-engaging informative services
- Remote operating support
- Maintenance of networks and
- Systems and infrastructure management

### b) The outsourcing method of IMMEX is created

When an AGA-certified company with no facilities for production processes conducts manufacturing operations through third parties registered in the Program.

### c) Now they are considered to obtain an industrial IMMEX program.

Disassembling, material recovery and re-manufacturing operations are considered preparation or transformation processes, which qualify them to obtain an Industrial IMMEX program.

### d) Authorization of PROSEC program when processing the IMMEX program.

IMMEX companies with a service method can temporarily import machinery and equipment under the IMMEX program applying the PROSEC preferential tariffs.

### e) Registering raw materials, parts, components and finished goods.

These materials should be registered or recorded in the program only with their tariff classification and all merchandise contained therein will be authorized.

### f) Registering in the IMMEX asset program

The machinery, equipment, tools, spares, molds, administrative equipment, etc. should be authorized in the IMMEX program with their commercial description.

### g) Benefits for companies certified by AGA

- Processing the extension to register new raw materials, finished goods and assets related to the manufacturing or maquila ("in-bond") operation to be temporarily imported will not be required.
- No additional controls for special merchandise will be necessary.
- The notification of merchandise set to sub-manufacturing or sub-maquila submitted to ALAF should be done electronically.

### h) Sub-manufacturing or sub-maquila

The benefit to include the industrial processes related directly to the manufacturing operation of a company with Program, conducted by an individual other than the holder thereof, besides services (sub-maquila), is extended with the term sub-manufacturing.

i) Permanent establishment

The benefit of not being considered permanent establishments is extensive to IMMEX companies as long as they comply with the requirements of Art. 216 Bis MITL, which PITEX companies did not have.

j) Manufacturing and sub-manufacturing operation for VAT purposes.

The manufacturing operations that companies with a Program conduct under the current IMMEX Act will be considered maquila operations, and the sub-manufacturing operation conducted in terms of this Act will be considered sub-maquila operation.

k) Refunds of VAT in favor

Companies with an IMMEX Program and exporting merchandise will be entitled to have VAT refunded when a balance in favor is obtained from the returns, in a term that will not exceed **20 business days**, except for companies certified by the AGA whose balance will be refunded in a term no greater than **5 business days**; provided that the General Foreign Trade Rules established by the SAT are fulfilled.

3. Obligations of the IMMEX program

a) Export obligation

Annually conduct foreign sales for over 500,000 U.S. dollars or the equivalent in domestic currency, or else, bill exports for at least 10% of total billing.

b) Verification of exports of intangible goods.

For purposes of IMMEX and ALTEX Acts, the holders of the programs producing intangible goods could file export filings or the following documents:

- Annual Income Tax return of the previous fiscal year or, if this return is not yet available (because the deadline for filing has not been reached), pro forma financial statements signed under oath by the legal representative.
- List of invoices of the previous or current period that includes the invoice number, date, description of the merchandise exported, value in dollars and domestic currency duly totaled and signed under oath by the legal representative of the company.

c) Certification of export of domestic or definitively imported goods

For purposes of the IMMEX and ALTEX Acts, the holders of programs conducting operations from domestic or definitively imported intermediate goods and exporting their products indirectly through other companies, can certify these operations with a letter from the final exported that includes the value and amount of goods billed and the percentage that was exported.

d) Confirmation of address

Provide the SAT with the geographical coordinates corresponding to the changes in the fiscal address and in the addresses where the operations of the Program are conducted.

e) Volume control in temporary import of fuel and lubricants

In the temporary import of fuel and lubricants used to conduct manufacturing operations under the Program, a strict volume control should be had and verify usage.

f) Review in March of each year by the Department of Economy

The applicant should have the following:

- Certificate of advanced electronic signature from the SAT.
- Active Taxpayer Identification Number.
- That the fiscal address and addresses where operations are conducted under the program are registered and active in the Federal Taxpayers' Registry.

g) Annual Foreign Trade operations' report

- The annual report should be filed by internet no later than the last weekday of May of each year.
- The benefit of importing temporarily will be suspended for those that did not file the annual operations report on time or do not fulfill the requirements of the above item.
- If on the last business day of August the requirements are not fulfilled or the annual report filed, the program will be definitively canceled on September 1.
- Economy will publish in the DOF of June the number of the program and name of the holder of those suspended and in September those canceled will be published.

h) INEGI Report

IMMEX companies should file the INEGI statistic report by Internet no later than the 20<sup>th</sup> of the following month.

4. Validity of Maquila and PITEX programs and coming into effect of IMMEX programs

The cancellation of Maquila and PITEX programs has been delayed during the period. First, to the last day of June, later to the last day of September and now the programs will be valid through the last day of January 2008.

- For companies obtaining new programs starting November 13, 2006, an IMMEX program will be authorized.
- For companies whose IMMEX numbers have already been listed in the DOF, when the program comes into effect.
- For companies whose IMMEX number has not been listed in the DOF, the Maquila and PITEX programs will be in effect through January 31, 2008.

5. New classes of filings for IMMEX companies

These codes will become effective on February 1, 2008

- Raw material, parts and components go from Maquila code "H3", PITEX code "A2" to "**IN**".
- Machinery, equipment, molds, tools go from codes "H3" in Maquila, "A6" in PITEX to code "**AF**".
- Finished goods go from Maquila code "J1", PITEX code "J2" to code "**RT**".

Companies having obtained an IMMEX program on November 13, 2006 should use the Maquila codes until the IMMEX codes come into effect. Maquila and PITEX companies listed and not listed should continue using the previous codes until the IMMEX codes come into effect.

6. Public information of IMMEX programs

According to the Federal Transparency and Access to Public Government Information Law, the following information related to authorizations granted under this Act will be at the disposal of the general public electronically in the Internet page of the Department of Economy:

- Applicant's name
- Program Number;
- Address;
- Administrative unit granting them;

- Tariff classification of the merchandise to import and export;
- Program Status, and
- Validity

7. VAT withheld from domestic suppliers of IMMEX

**Act through which tax benefits are granted related to IT and VAT (DOF 29-Nov-06)**

**Article Two.** Companies with a Program according to the Act published in the Official Gazette on November 1, 2006, related to the promotion of the manufacturing, maquila and export service industry (IMMEX), acquiring goods authorized in this domestic supplier program, **can withhold the value added tax** transferred for the acquisition of such goods, according to article 1-A, section IV of the Value Added Tax Law, for which they are released from the requirement to have a domestic supplier program that indicates authorized goods for which the value added tax should be withheld.

8. Tax Benefits

a) Regularization of raw materials, spare parts and overdue components

In regularizing raw materials, spare parts and temporarily imported components that have exceeded their deadline to return, the preferential rate of Agreements or PROSEC can be used.

b) Retroactive application of PROSEC tariffs in regularization of the tariff deferral

In the case of maquila and PITEX companies that did not make the corresponding IGI payment in the import filing covering the return or through the complementary filing, they could process the rectification of the temporary import filing, applying the IGI rates provided for in the PROSEC for temporary imports conducted during the period between November 20, 2000 and March 31, 2006, entering identifying "PS" according to Appendix 8 of Exhibit 22 of the General Foreign Trade Rules for 2006, provided that on the date the rectification of the temporary import filing is conducted, they have the authorization in terms of PROSEC and that **the procedure is conducted before January 1, 2008.**

c) Tax cancellations, transitory article 7 of the 2007 Revenue Law

- Credits up to 2002.- Cancellation of 30% IFI and Compensatory Fees, fines and surcharges at 100% and fixed fines other than omissions at 80%
- Credits from 2003 to 2005.- 100% of the fines and late charges, compensatory fees and federal contributions other than those the taxpayer should have withheld, transferred or collected are condoned.
- Credits in 2007.- The fines given due to lack of compliance with the federal tax obligations other than payment obligations, except for those imposed due to filing excess tax losses, will be reduced by 50 percent provided they are paid 30 days after notification.

**EXHIBIT  
“IETU” TABLES**

**Subjects to “IETU” and Subject Activities**

Obligated Subjects		Activities subject to tax
1)	Individuals	<ul style="list-style-type: none"> <li>✓ Alienation of Goods,</li> <li>✓ Provision of Services and</li> <li>✓ Granting the temporary use or enjoyment of Goods</li> </ul>
2)	Companies	
3)	Nonresidents with permanent establishment in Mexico	

**Tax Rate**

2008	16.5 %	Transition Regimen
2009	17.0 %	
2010 henceforth		17.5 %

**Creditable IT**

IT of the period determined and effectively paid according to the MIT Law

The Income Tax generated from the payment of dividends that do not come from the net taxable income account and that consequently should be pyramided with a 1.3889 factor

IT paid abroad for obtaining revenues taxed for “IETU” enjoying the crediting benefit per article 6 of the MIT Law

Includes the IT paid by

a)	Crediting of cash deposit tax (new 2%), and
b)	Offsetting from universal balances in favor (CFF. Art. 23).

**Comparison between IT and IETU**

	IT	IETU
Subjects	<ul style="list-style-type: none"> <li>✓ Individuals,</li> <li>✓ Companies,</li> <li>✓ Nonresidents with Revenues from a Source of Wealth outside Mexico, and</li> <li>✓ Permanent Establishment in Mexico of Nonresidents.</li> </ul>	<ul style="list-style-type: none"> <li>✓ Individuals in Revenues from Fees, Leasing and Business Activities.</li> <li>✓ Companies from Title II of the IT Law.</li> <li>✓ Companies not contributing to IT except for beneficiaries provide that requirements are fulfilled.</li> <li>✓ Nonresidents with Permanent Establishment in Mexico.</li> </ul>
Base	Revenues and Deductions as accrued, with the items agreed upon in credit having an anticipated role	Determined according to the cash flow

Rate	28.0%	17.5% With a transitory stage during: 2008.....16.5% 2009.....17.0%
Revenues	As accrued and considering revenues in credit and inflationary effects.	According to cash flow excluding some specific concepts
Deductions	As accrued and only in the case of individuals and civil partnerships it is demanded that they are effectively paid.	According to cash flow and without considering virtual items as depreciations that are replaced by Investments acquired in the period.
Loss incurred in the Period	Will be subtracted from earnings of up to ten previous periods.	When the deductions exceed revenues, the tax rate is applied and a creditable amount against IT of the year, or the IETU of up to the ten following periods.
Tax Losses Carryforward	Can be applied in the following ten periods and they enjoy restatement	There is no recognition
Estimated Payments	Monthly and taking into consideration the profit coefficient from up to five previous periods	Monthly according to a real base accumulated in the current period

**Comparison between IT and IETU**

	IT	IETU
Special Crediting	<p>The following can be credited:</p> <ul style="list-style-type: none"> <li>✓ The cash deposit tax (2%) paid in the year, with the option to include it in estimated payments, and</li> <li>✓ The IT paid due to the payment of Dividends that do not come from Cufin.</li> </ul>	<p>The following can be applied:</p> <ul style="list-style-type: none"> <li>✓ The credit for excess deductions over revenues of previous periods,</li> <li>✓ The labor burden credit, items made similar to salaries and peripheral cost,</li> <li>✓ Crediting related to IT of the period itself,</li> <li>✓ The IT paid due to the payment of Dividends that do not come from Cufin, and</li> <li>✓ The credit from investments made between 1998 and 2007.</li> </ul>

## FOREIGN TRADE

### IMMEX ACT



The content was prepared by Partners of the following firms of DFK Mexico:

- ♦ DFK – Gonzalez y Asociados, S. C.
- ♦ Méndez y Castelló – DFK, S. C.
- ♦ Vázquez Pola Consultores y Asociados, S. C.

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