

# International Tax

## Mexico Highlights

In Plain English



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## Investment basics:

**Currency** – Mexican Peso (MXN)

**Foreign exchange control** – None, and no restrictions are imposed on the import or export of capital. Repatriation payments may be made in any currency. Both residents and nonresidents may hold bank accounts in any currency in any part of the world; however, for some accounts located in Mexico but kept in a foreign currency, the currency must be the US dollar.

### **Accounting principles/financial statements**

– Financial statements must be prepared annually. Publicly listed Mexican companies must use IFRS. Otherwise, companies may use Mexican GAAP or IFRS

**Principal business entities** – These are the corporation (SA), limited liability company (SRL) and a branch of a foreign entity.

## Corporate taxation:

**Residence** – An entity is resident in Mexico if it is managed and controlled in Mexico.

**Basis** – Residents are taxed on worldwide income; nonresidents are taxed only on Mexican-source income. Foreign-source income derived by residents is subject to tax in the same way as Mexican-source income. Branches are taxed in the same way as subsidiaries.

**Taxable income** – Corporate tax is imposed on a company's profits, which consist of business/trading income, passive income and capital gains. Normal business expenses may be deducted in computing taxable income. Inflationary accounting for tax purposes is applicable to certain types of revenue and expenses.

**Taxation of dividends** – Dividends received by a Mexican resident company from another Mexican resident company are exempt from corporate tax. Dividends received from a foreign company are subject to corporate tax in the period the dividends

are received, but a credit for underlying corporate and withholding taxes paid abroad generally is available.

Mexican companies can freely distribute dividends on profits that have been taxed in Mexico; otherwise, corporate taxes must be paid as a consequence of the dividend distribution. Companies must maintain a special "CUFIN" account to track previously taxed profits.

Mexican companies with investments in renewable sources of energy may create a special net profit account (CUFIER), and if such a company distributes dividends that are not paid from the CUFIER account, the payer will be required to pay tax (30% on a grossed-up amount) on the distribution.

Dividend payments generally are subject to a 10% withholding tax. See "Withholding Tax," below.

**Capital gains** – Mexican entities are not subject to special tax treatment on capital gains, and the use of capital losses is restricted in some cases.

**Losses** – Losses may be carried forward for 10 years, subject to applicable inflation adjustments. The carryback of losses is not permitted.

**Rate** – 30%

**Surtax** – No

**Alternative minimum tax** – No

**Foreign tax credit** – Income taxes paid abroad may be credited against Mexican tax on the same profits, but the credit is limited to the amount of Mexican tax payable on the foreign income.

**Participation exemption** – No

**Holding company regime** – No

**Incentives** – Special rules apply to maquiladoras. Incentives are granted for national cinematographic and theatrical

productions, as well as investments in high performance sports, electric vehicle power feeders, technology and R&D projects, the FIBRAS (real estate investment trust) regime, risk capital and hiring the elderly and/or people with disabilities. A tax credit is available for companies purchasing diesel or biodiesel fuel and using it for specific activities.

Seven special economic zones have been launched in the southern part of the country, which provide preferential income tax, VAT and customs treatment for companies operating in the zones.

Taxpayers operating in the “northern border region” may be eligible for tax incentives (in the form of an income tax credit and a reduced VAT rate) during 2019 and 2020. Among other requirements, taxpayers must file a request with the tax authorities by 31 March of each fiscal year.

Qualifying projects involving CAPEX investment and job creation may benefit from discretionary grants provided by State and Municipal authorities. In addition, Mexico City provides green incentives.

### **Withholding tax:**

**Dividends** – A company that distributes dividends (including distributions derived from investments in renewable sources of energy and made from the CUFIER account) to a nonresident or resident individual must withhold a 10% tax, which is considered a final tax. For nonresidents, the 10% rate may be reduced under a tax treaty, if certain requirements are met.

Under a grandfathering rule, profits obtained before 31 December 2013 are not subject to withholding tax, as long as they form part of the CUFIN balance of the entity as of that date.

The 10% tax may be reduced for dividends paid to Mexican resident individuals if profits generated in 2014, 2015 and 2016 are reinvested and distributed as from 2017.

**Interest** – Interest paid to a nonresident generally is subject to withholding tax at rates ranging from 4.9% (interest paid to foreign banks and listed debt instruments) to 35%. A 40% rate applies where interest payments are made to a related party located in a tax haven. The rate may be reduced or relief may be available under a tax treaty.

**Royalties** – Royalties paid to a nonresident are subject to a withholding tax of 35% (patents and trademarks) or 25% (other kinds of royalties), unless the rate is reduced under a tax treaty. A 40% rate applies where royalties are paid to a related party located in a tax haven. The leasing of machinery and equipment generally is considered a royalty.

**Technical service fees** – Fees paid for technical assistance are subject to a 25% withholding tax, unless the rate is reduced under a tax treaty.

**Branch remittance tax** – Rules that are similar to the CUFIN rules for dividends apply. Permanent establishments distributing dividends or gains to their head office are subject to an additional tax of 10% on such dividends or gains.

**Other** – There are certain other circumstances in which withholding tax may apply on payments made to nonresidents, such as payments relating to immovable property, salaries, fees, capital gains, etc.

### **Other taxes on corporations:**

**Capital duty** – No

**Payroll tax** – Payroll taxes apply at the state level.

**Real property tax** – The municipal authorities levy “rates” on the ownership of real property. Rates are deductible in calculating the corporation tax liability.

**Social security** – Employer contributions for social security and other related

contributions (e.g. housing and retirement) are mandatory, with rates ranging from 15% to 25%, depending on the salary structure of the group of employees.

**Stamp duty** – No

**Transfer tax** – A transfer tax of between 2% and 5% applies to the transfer of real estate and is imposed by the municipality where the property is located.

**Other** – While not a tax, under the mandatory profit sharing rules, an entity is obliged to distribute 10% of taxed profits to its employees no later than May of the year following the year in which the profits were generated.

A special excise tax on production and services is levied on the import and sale of certain goods and the provision of certain services.

#### **Anti-avoidance rules:**

**Transfer pricing** – Rules following the OECD guidelines apply to cross-border and domestic transactions. The following transfer pricing methods may be used in Mexico: the comparable uncontrolled price (CUP) method is considered the preferred method, followed by the cost plus and resale price methods. Profit-based methods are to be used if the CUP, cost plus and resale price methods are not applicable. The profit split and residual profit split methods, and the transactional operating margin method are not applicable in specific circumstances.

Documentation rules apply. Advance pricing agreements are available.

**Thin capitalization** – Interest payments made by a Mexican resident company on a loan from a nonresident related party are nondeductible for income tax purposes to the extent the debt-to-equity ratio of the payer company exceeds 3:1.

Debts incurred for the construction,

operation or maintenance of productive infrastructure linked to strategic areas, or for the generation of electricity, are excluded from the application of the thin capitalization rules.

**Controlled foreign companies** – Income is attributed to Mexican tax residents (including resident foreigners) from “controlled” entities where more than 20% of their income is passive income (broadly defined) that is taxed locally at a rate less than 75% of Mexico’s statutory rate. Reporting rules may apply.

**Disclosure requirements** – External tax auditors are required to disclose on the tax audit report when a taxpayer has entered into a transaction that is not considered viable by the Mexican tax authorities.

Mexico has adopted country-by-country (CbC) reporting in accordance with the recommendations under the OECD’s BEPS project. Under the rules, companies that enter into transactions with related parties (in Mexico or abroad) and receive income equal to or greater than MXN 791 million must file a master file and a local file, and Mexican multinational enterprise groups that receive income equal to or higher than MXN 12 billion also must file a CbC report.

**Other** – An optional tax audit report may be filed for taxpayers that have more than 300 employees, gross income exceeding MXN 122 million or assets exceeding MXN 97 million.

#### **Compliance for corporations:**

**Tax year** – Calendar year

**Consolidated returns** – A tax integration regime allows a group to defer income tax for up to three years.

**Filing requirements** – Under the self-assessment regime, advance corporate tax must be paid in 12 installments. The annual tax return must be filed within the

first three months of the following year (no extensions are available).

An advance electronic signature certificate must be available, electronic accounting records must be maintained and the general ledger must be submitted to the tax authorities on a monthly basis.

All taxpayers are required to issue digital invoices with respect to their transactions.

**Penalties** – Penalties apply for noncompliance with the tax rules.

**Rulings** – The tax authorities will issue rulings on the tax consequences of actual transactions.

### **Personal taxation:**

**Basis** – Mexican nationals are taxed on their worldwide income. Nonresidents are taxed only on Mexican-source income.

**Residence** – An individual is considered resident if he/she has a permanent home in Mexico. If an individual has a home in two countries, the key factor in determining residence is the location of the individual's center of vital interests. Mexican nationals are, in principle, considered tax residents, subject to the permanent home and/or the center-of-vital-interests test.

**Filing status** – Tax returns are filed individually, regardless of marital status.

**Taxable income** – Income is taxed, in part, under a schedular system, although some categories of income can be mixed to determine taxable income. Profits derived from the carrying on by an individual of a trade or profession generally are taxed in the same way as profits derived by companies. A separate regime applies to interest earned by individuals.

**Capital gains** – Capital gains arising from an individual's sale of publicly traded shares, including financial derivatives, are subject to a 10% tax on the gains.

**Deductions and allowances** – Subject to certain restrictions and caps (the lower of MXN 187,000 or 15% of taxable income), deductions are granted for medical expenses and medical insurance, retirement annuities, mortgage interest, etc. Medical, dental and hospital expenses (among others) are deductible with no restrictions when they derive from an "inability" or disability under the terms of the relevant laws.

Personal allowances are available to the taxpayer and his/her spouse, children and dependents.

**Rates** – Rates are progressive up to 35%.

**Other** – See "Incentives" under "Corporate taxation," above, related to taxpayers operating in the northern border region.

### **Other taxes on individuals:**

**Capital duty** – No

**Stamp duty** – No

**Capital acquisitions tax** – No

**Real property tax** – The municipal authorities levy "rates" on the ownership of real property. Rates are deductible in calculating the individual's taxable income related to leasing of real property.

**Inheritance/estate tax** – No

**Net wealth/net worth tax** – No

**Social security** – Employed individuals are required to make social security contributions, with the amount based on the individual's salary.

### **Compliance for individuals:**

**Tax year** – Calendar year

**Filing and payment** – Tax on employment income is withheld by the employer and remitted to the tax authorities. Other

types of income, such as income from the provision of services and leasing income, are subject to withholding. Income not subject to withholding is self-assessed; the individual must file a tax return and make prepayments of tax. Final tax is due on 30 April following the tax year (no extensions are available).

An advance electronic signature certificate must be available. For individuals carrying on a business activity, electronic accounting records must be maintained and a general ledger submitted on a monthly basis.

**Penalties** – Penalties apply for noncompliance with the tax rules.

### **Value added tax:**

**Taxable transactions** – VAT is levied on the sale of goods, leasing and the provision of services, as well as on imports.

**Rates** – The general VAT rate is 16% and a 0% rate applies to food, medicine and certain other items (with some exceptions).

An 8% rate applies to taxpayers operating through establishments in the northern border region that meet certain requirements provided certain requirements are met. Among other transactions, the reduced rate does not apply to the importation of goods, the transfer of immovable property and the transfer of intangibles.

**Registration** – All persons must be registered to be able to credit the VAT paid to vendors, suppliers or at the border. Nonresidents supplying goods or services in Mexico must register.

**Filing and payment** – The VAT return must be submitted monthly, within the first 17 days of the following month.

VAT paid for expenses and investments made during the preoperational period is (i) creditable on the VAT return for the month the taxpayer begins business operations; or (ii) submitted for refund during the month following the VAT payment, based on an estimation of future VAT-taxable activities.

**Source of tax law:** Income Tax, Value Added Tax, Federal Tax Code

**Tax treaties:** Mexico has 59 income tax treaties in force. Mexico signed the OECD MLI on 7 June 2017.

**Tax authorities:** Servicio de Administración Tributaria (SAT or Tax Administration Service)

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