

Mexico Tax Alert

2010 tax reform proposed

On 10 September 2009, the Mexican President submitted to Congress the 2010 economic bill, which contains proposals to amend the tax laws and the federal fiscal code, as well as general economic policy criteria and provisions for the federal expense budget. The most important tax proposals are as follows:

- Increase the corporate and maximum individual income tax rate from 28% to 30%, and impose limits on companies filing consolidated tax returns;
- Eliminate the flat tax "loss credit" against income tax due in the same fiscal year;
- Increase the tax on cash deposits and lower the exemption cap;
- Introduce a new contribution similar to value added tax (VAT) to combat poverty that would tax all activities at a 2% rate; and
- Significantly increase the excise tax on specific goods and services

It is hoped that the above measures will improve tax administration and collection, simplify the tax rules, provide legal certainty for taxpayers and combat tax avoidance and evasion.

Income tax

The corporate and individual (maximum rate) income tax rate would be increased temporarily from 28% to 30% for the years 2010-2012. The rate would decrease to 29% in 2013 and back to the current 28% in 2014. For the primary sector (i.e. agriculture, cattle, etc.), the maximum rate would increase from 19% to 22.5%.

Significant changes would be made to the consolidated tax regime. Although qualifying taxpayers would continue to be allowed to offset losses against profits of other entities within a consolidated group and to distribute dividends tax-free between group members, the following changes are proposed:

- Sixty percent of any deferred income tax would have to be paid in the fifth year following the year in which such losses were offset or dividends paid, with the

balance of 40% to be paid in equal amounts over the subsequent four-year period. This provision would be applicable for all prior fiscal years under tax consolidation (current rules allow deferral until certain deconsolidation events take place)

- A group would be deemed to be deconsolidated if the deferred tax was not paid
- An independent auditor would be required to review and certify the calculation and payment of the deferred tax

The 30% research and development tax credit incentive would be abolished, although grandfather rules would apply where credit is pending as of 31 December 2009.

The 4.9% withholding on interest paid to foreign banks resident in a tax treaty country would continue to apply in 2010.

Income exceeding 10% of total income from the alienation of goods and the provision of services derived by a nonprofit entity other than those for purpose of which the nonprofit entity was created would have to be determined and tax paid on such income in accordance with the rules that apply to corporations.

A new method for the recognition of interest derived by individuals is proposed. Interest received and expenses would have to be recognized when accrued and a ring-fencing provision would prevent losses from being offset against other types of income. Financial institutions would be required to make monthly income tax withholdings on the positive balance of the investment account. A one-year transitional period is proposed.

The deduction of mortgage interest expense would be limited to interest on a mortgage on a single residence, although the current UDIS 1.5 million loan limit would be maintained. In addition, gains on the sale of a residence would be tax-free only once every five years (instead of annually, as is currently the case).

Flat rate business tax

Through a rule included in the Federal Revenue Law, it is proposed to disallow the current tax loss credit against income tax due in the same fiscal year. Currently, if a taxpayer generates a tax loss credit for flat tax purposes, the credit may be applied against the income tax of the year.

Tax on cash deposits

The tax on cash deposits currently applies to monthly deposits exceeding MXN 25,000 or the equivalent in a foreign currency. It is proposed to increase the rate of tax from 2% to 3% on all cash deposits made in a specific month and to reduce the exempt amount to MXN 15,000.

The existing exemption for corporations and individuals carrying on business and professional activities for cash deposits made in accounts opened to obtain loans granted by financial institutions would be abolished as from 1 July 2010. Other individuals who wish to continue to qualify for the exemption would have to prove to the financial institution concerned that they are not carrying on business or professional activities.

Contribution to fight poverty

The proposed reform would introduce a new indirect tax of 2% levied on income derived from all types of economic activities carried on in Mexico, with a zero rate applying to export activities. Exemptions would be limited to the acquisition of local and foreign currency, shares, credit documents, accounts receivables, land and some interest income or expense paid or received by financial institutions.

Revenue from the contribution would be used to combat poverty. The tax would be levied on a cash flow basis, with the tax base, mechanics and procedures being similar to those under the VAT rules. It is proposed that, if the tax is not paid during a specific month, the taxpayer would forfeit its ability to apply credits in that month.

Under transitional rules, income deriving from activities carried on before 1 January 2010 would not be subject to the contribution when collected.

Excise taxes

The proposed reform measures include a number of changes to the excise tax rules, as follows:

- A tax on services rendered through a public telecommunications network would be introduced, with exemptions for rural and public phone services and interconnection services (i.e. connection services within telecommunication companies);
- A quota would be levied on cigarette sales, at the rate of 80 cents per pack cigarettes, increasing over four years to reach MXN 2.00 per pack;
- The rate of excise tax on beer would increase to 28% in 2010, 2011 and 2012, and then be reduced to 27% in 2013 and 25% in 2014. An additional quota of MXN 3 per liter would be levied on alcoholic beverages that are more than 20 proof alcohol; and
- The rate of excise tax on betting games and lotteries would be increased from 20% to 30%, and measures would apply to strengthen supervision and control

Federal fiscal code

The proposals include several changes to the Federal Tax Code:

- Tax domicile would be extended in certain cases to encompass the tax domicile of a legal representative, and there would be changes with respect to the circumstances in which a change of domicile is effective for tax purposes
- Limits are proposed with respect to the filing of amended tax returns for fiscal years prior to a year that is subject to a tax audit, certain legal procedures would be eliminated to facilitate the audit process and the statute of limitations would be increased in certain cases
- Control of the invoicing process would be at once strengthened, and simplified, primarily by the standardization of the use of electronic invoicing
- Other changes and clarifications proposed in this area address the falsification and reproduction of invoices, as well as the use of fake invoices
- Shareholders would have unlimited liability for the tax liability of a corporation that is unable to pay the tax in proportion to their holding in the company

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