

2010 PROPOSED TAX BILL

On September 8, 2009, the Executive Branch submitted a proposed tax bill to Congress which, if approved, will enter into force on January 1, 2010.

The main objective of the tax bill is to increase tax revenues, for which the Executive Branch submitted adjustments to several provisions contained within the Mexican income tax, flat tax (IETU as per its acronym in Spanish) and value added tax (VAT) laws, as well as for the federal tax code (FTC).

The highlights of the proposal are as follows:

1. Enactment of a 2% general tax on sales and services, except for exports which would be levied at the 0% rate. This tax is intended to operate very similar to VAT.
2. Temporary increase in the income tax rate. For this purpose, the individual graduated rates would be adjusted, resulting in an increase in the highest marginal rate from 28% to 30%. The corporate income tax rate will also temporarily increase to 30%. The rates would return to 28% by 2014.
3. There would be an immediate recapture of the tax deferred in the tax consolidation beginning in 2010. This tax would be paid starting in the 6th following fiscal year in which the consolidation deferral benefit was received. In this regard, 60% of the tax deferred as of 2004 would be remitted in 2010 and the remaining balance within the next four fiscal years.
4. Limits would be imposed on the individual income tax exemption from the sale of the personal residence and on the deduction of mortgage interest.
5. Additional charges on telecommunication services and increase in the excise tax on tobacco, beer, and other alcoholic beverages and gambling.

Additional details are provided below.

FEDERAL REVENUE ACT

IETU credit for the excess of deductions over revenue

Solely for 2010, the credit generated from the excess of deductions over revenue provided in the IETU Law, would not be creditable against the current year's income tax. The credit would only be available for a 10 year carry forward against IETU.

INCOME TAX

Temporary increase in individual and corporate income tax rate

For the calendar years 2010-2012, the marginal rates of the last five graduated income tax rates applicable to individuals would be adjusted to increase the highest marginal rate to 30%. In 2013 and 2014 such rates would be gradually reduced to 29% and 28%, respectively.

In line with the previous measure, the corporate income tax rate would be increased to 30% for the calendar years 2010-2012 and reduced to 29% and 28% in 2013 and 2014, respectively.

Preferred income tax rate applicable to primary industries (e.g., agriculture, fishing, cattle, timber, etc.) would be increased to 21%.

Tax consolidation

The tax deferral benefits arising from filing consolidated tax returns within a group, would have to be remitted to the Mexican tax authorities as from the 6th year following that in which it was generated through a gradual payment schedule consisting in an initial payment of 60% of the deferred tax corresponding to the prior 6th year and the remaining balance would be due on a 10% straight-line basis (over the following 4 years), as depicted in the following chart:

Deferred income tax payment schedule

Fiscal year to which the deferral applies	Applicable percentage							
	2010	2011	2012	2013	2014	2015	2016	2017
To 2004 and before	60%	10%	10%	10%	10%			
2005	0	60%	10%	10%	10%	10%		
2006	0	0	60%	10%	10%	10%	10%	
2007	0	0	0	60%	10%	10%	10%	10%

As a consequence of the above, the tax consolidation benefits of deferring tax on accounting dividends distributed within the group and unamortized separate company tax losses contributed to the consolidation would only be available for up to ten fiscal years, with the largest benefit recaptured on the sixth year. Failure to comply with the remittance of deferred tax would result in deconsolidation.

In addition, the proposal foresees a requirement to include a procedure for the remittance of deferred income tax derived from the dividends or profits distributed between entities that file a consolidated return that were not paid out of the After-tax Earnings Account balance (CUFIN).

The computation of deferred tax could be determined by either the withdrawal or deconsolidation procedures established in the current income tax provisions, or through an alternate procedure consisting of adding, among others, pending net operating losses ("NOLs") of both the holding company and its subsidiaries to the consolidated taxable income as of the 6th previous year. The elected procedure would have to be used for the following five years; moreover, the CPA auditing the financial statements of the taxpayer would have to include in his report an opinion on the calculation of the deferred income tax.

Sale of personal residence by individuals

The income tax exemption on the revenue arising from the sale of personal residence by individuals would be applicable to the extent that the taxpayer had not benefited from such provision in the previous five years. Moreover, the exemption would be capped up to the sales price of the equivalent of 1,500,000 investment units (UDIs), even when the taxpayer had lived in the house for more than five years.

Deduction of mortgage interest by individuals

Deduction of actual mortgage interest paid would only be applicable when the mortgage was with an entity part of the Mexican financial system, specifically destined for the acquisition of the individual's personal residence and to the extent the total amount of loan does not exceed 1,500,000 UDIs. The interest deduction for loans used for the construction, extension and refurbishing of homes, as well as for the acquisition of a second house (not constituting primary residence), would be repealed.

Computation of taxable interest

To simplify the calculation of interest income for loans entered with entities of the financial system, a new procedure is proposed through a cash flow system, which would enter into force as from January 1, 2011.

Through this procedure, financial system taxpayers would be relieved from the requirement to withhold the corresponding income tax on the principal of the loan.

It should be mentioned that income tax withheld would be considered as final payment for individuals and considered an advance payment for corporations.

Charitable entities authorized to receive deductible donations

All entities authorized to receive donations would be obliged to calculate a tax on deemed distributable profit, when circumstances detaching the tax fall within the scope of Mexican Income Tax Law (MITL) rules, including the existence of non-deductible expenses.

In addition, all entities authorized to receive donations would

be permitted to obtain revenue from the sale of goods or the rendering of services, not related to their authorized activities to the extent they do not exceed 10% of the revenue derived from their authorized activities. Income tax would have to be paid in accordance with Title II of the MITL (i.e., as a corporation) for the excess over the threshold.

Interest paid to foreign banks

The withholding tax rate of 4.9% on interest paid to foreign banks would continue to apply to the extent the beneficial owner of such interest is resident in a country with which Mexico has a treaty for the avoidance of double taxation and that the requirements foreseen in such treaty are met.

TAX ON CASH DEPOSITS LAW

Rate and exemptions

The monthly exemption threshold is reduced so that individuals and corporations would not be obliged to pay the tax on cash deposits for a cumulative amount of \$15,000 MXN per month. Moreover, the rate is increased to 3%.

FEDERAL TAX CODE

Tax domicile

The domicile of the taxpayer legal representative would be considered as tax domicile of the taxpayer as well.

Issuance of digital invoices

Taxpayers would be required to use digital invoices obtained through the internet website of the Mexican tax authorities.

For transactions of up to \$2,000 MXN hard copy invoices would be allowed to the extent certain security measures are adopted.

Taxpayers issuing digital invoices would have certain benefits such as faster refunds of tax overpayments (up to 20 business days), as well as the relief of the obligation to file a separate annual information return on transactions with third parties, and would be able to file the annual income tax return as part of the statutory tax audit report.

Assessments by the Mexican tax authorities

Once the Mexican tax authorities have started a tax audit, prior year amended tax returns filed by the taxpayer that have a direct impact on the fiscal year under review, would not have any effect.

The tax authorities would be able to start a tax audit /review notifying the person they find at the tax domicile of the taxpayer (in the absence of the taxpayer) being relieved from the obligation to first provide a written request to the taxpayer or its legal representative.

Moreover, it would be possible to issue the final notice of the audit/review process even in absence of the taxpayer or its legal representative.

The statute of limitations of the tax authorities would be extended up to ten years, when the taxpayer changes its tax domicile more than two times within the same fiscal year.

EXCISE TAX LAW

Beverages with an alcohol proof higher than 20° G.L. would be subject to an additional tax of \$3 MXN per liter, which would be levied at the manufacturer or importer level.

Additionally, the rate applicable to the sale and import of beer would be increased temporarily to 28%, foreseeing a reduction to 27% in 2013 and 25% as from 2014.

A tax increase is also proposed for tobacco.

Tax rate applicable to gambling would be increased from 20% to 30%.

Lastly, a 4% tax is proposed on services rendered through telecommunication networks excluding public telephone, fixed rural telephone and public telecommunication networks interconnection.

TAX LAW AGAINST POVERTY

A new tax is created destined to strengthen public resources aimed to the social needs of the country.

Subject, object and base

Individuals and corporations that sell goods, render independent services and lease or import goods in national territory, would be subject to the tax against poverty.

To remain within a competitive environment, exports would be levied at the 0% rate.

Taxpayers would remit the difference between the input and output tax against poverty to the tax authorities, being entitled to reduce the tax withheld. When an overpayment arises, the business taxpayer would be eligible to credit it or to request its refund or compensation (against other taxes).

Tax rate and payment term

The tax would be computed on a monthly basis by applying the 2% flat rate to the previously mentioned acts and activities. Additionally the tax due would be remitted through a tax return in the same terms as the VAT.

Moment of taxation

The tax would be determined on a cash basis and would be applied to all the production stages on a non-cumulative basis. The timing or triggering of the obligations for this tax would be the same as those included in the VAT Law.

Exemptions

Additionally, it is proposed to exempt certain sales or alienations of goods and the rendering of certain services such as: land; national and foreign currency; gold and silver pieces; quotas; accounts receivable; certain interest paid and collected by financial institutions; some used movable property with the exception of those sold by businesses; international sea transport of goods rendered by foreign residents; temporary imports, and gratuitous services.

As a transitory rule, the consideration received from goods sold, services rendered as well as for the leasing of goods delivered or rendered before January 1, 2010 would not be subject to this tax.

This 2% tax would also apply to the sale of food, medicine, books, tuition, public ground transportation and doctor's services, among others, which traditionally had not been taxed with VAT or any other indirect or consumption tax.

FEDERAL LAW OF GOVERNMENTAL FEES

It is proposed to establish new charges for items such as the issuance of sanitary licenses for facilities that carry out activities relating to the production, manufacturing or importation of tobacco products, as well as for the re-issuance and renewal of the citizen identification registries among others, and fees for the granting of permits for the regulation and liberation of genetically engineered organisms, among others.

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