Tax Reform Proposals for 2016

On September 8, 2015, the Executive presented an economic reform package to Congress containing federal income laws applicable to the 2016 tax year. The decree proposes reforms, additions and deletions to various provisions of the Income Tax Law (ISR), the Special Tax on Production and Services (IEPS), the Federal Tax Code (CFF), the Federal Budget and Fiscal Responsibility Law (LFPRH) and the Federal Law of Rights (LFD).

In general terms, the proposed package of reforms incorporates Mexico´s legislative commitment to the Organization of Economic Cooperation and Development (OECD) with respect to the exchange of information on bank accounts and informational returns for multinationals on transfer pricing and seeks to promote greater international taxation goals. It also contains a series of measures to stimulate investment in the energy and infrastructure sectors, alleviate the tax burden for groups which engaged in tax consolidated until 2013, and encourage long-term savings by individuals.

Below is a brief discussion of the most relevant aspects of these initiatives, which if approved by Congress by the October 31, 2015 deadline, will enter into force on January 1, 2016.

Federal Revenue Law for 2016

For purposes of preparing this initiative, the Executive considered the following economic assumptions for 2016:

- Average price of a barrel of oil: USD 50
- Economic growth: 2.6%-3.6%
- Inflation: 3%
- Exchange rate: $15.9 pesos per USD
- Public income: 4,746,945.7 million pesos, which represents an increase in real terms of 1.01% over 2015.
- The income tax (ISR) withholding rate applicable to interest paid by the financial sector will be 0.53% on capital, instead of 0.6%.

In practice, the same economic stimuli from fiscal year 2015 will remain in effect.

Income Tax Law

- In 2015 (only for investments made in the final four months), 2016 and 2017, companies with income under 50 million pesos in the prior fiscal year, as well as those dedicated to transportation infrastructure or which invest in activities related to hydrocarbons and the generation of electric energy, will be able to deduct immediately their investment in fixed assets.

- Companies which have made investments in renewable energy which were depreciable at a rate of 100% will be able to distribute dividends without paying corporate tax to the extent the earnings derive from an account denominated "earnings from investment in renewable energy," calculated as a function of the profit the company would have generated had it not depreciated the investment at the 100% rate.

- Debts incurred for the purpose of investing in infrastructure related to the generation of electric energy will be excluded from the calculation of "debts that exceed three times accounting capital" (i.e., thin capitalization). This measure will allow companies in the electric energy industry to deduct interest paid to foreign related parties.

- Individual shareholders of publicly traded companies which reinvest profits generated from 2014-2016 will be subject to a reduced tax of 5% on dividends if profits from such companies are distributed in 2019 or later.

- Individuals and companies who in the first half of 2016 repatriate through the financial system those resources held abroad until 2014, will be considered to have satisfied their formal tax obligations so long as they pay the current omitted tax (without penalty or fines) within 15 days of the date of such repatriation and comply with other requirements, including that such investment remain in Mexico for three years.

- Companies which engaged in tax consolidation with their subsidiaries through 2013 will be able to reduce deferred taxes by crediting against the consolidated tax the tax on dividends paid among the group, and reduce by up to 50% the consolidated tax by applying losses incurred by subsidiaries in which they control 15%. Companies that exercise this option must be able to satisfy various requirements, including participation for five years in a real-time verification program implemented by the Tax Administration Service (SAT).

- In addition, a controlling company that suffered losses on the alienation of shares issued by a subsidiary which were not reversed for purposes of calculating tax will be able to rectify its tax position in ten payments.

- Individuals will be able to deduct contributions to their personal retirement plans, without regard to the general limitation on personal deductions, up to 10% of taxable income or five times the minimum salary (approx. 127,000 pesos), whichever is lower, and 152,000 pesos for deposits made to special long term savings accounts.

Special Tax on Production and Services (IEPS)

- The tax on gasoline and diesel will be imposed as a function of fixed quotas.

- The exportation of high-calorie food by manufacturers will be subject to 0% tax, and the IEPS transferred to such manufacturers on the acquisition of raw materials to produce such food will be creditable.

Federal Tax Code

- Beginning in 2017, financial institutions must provide information on financial accounts existing as from December 31, 2015 and on those accounts opened as from 2016, in compliance with the Standard for Automatic Exchange of Information on Financial Accounts and Tax Matters.

We invite you to learn more about the different aspects of the proposal as PwC Mexico experts analyze the 2016 economic reform package and explain in detail its reach and challenges

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