

THE UNIQUE ALTERNATIVE TO THE BIG FOUR<sup>SM</sup>

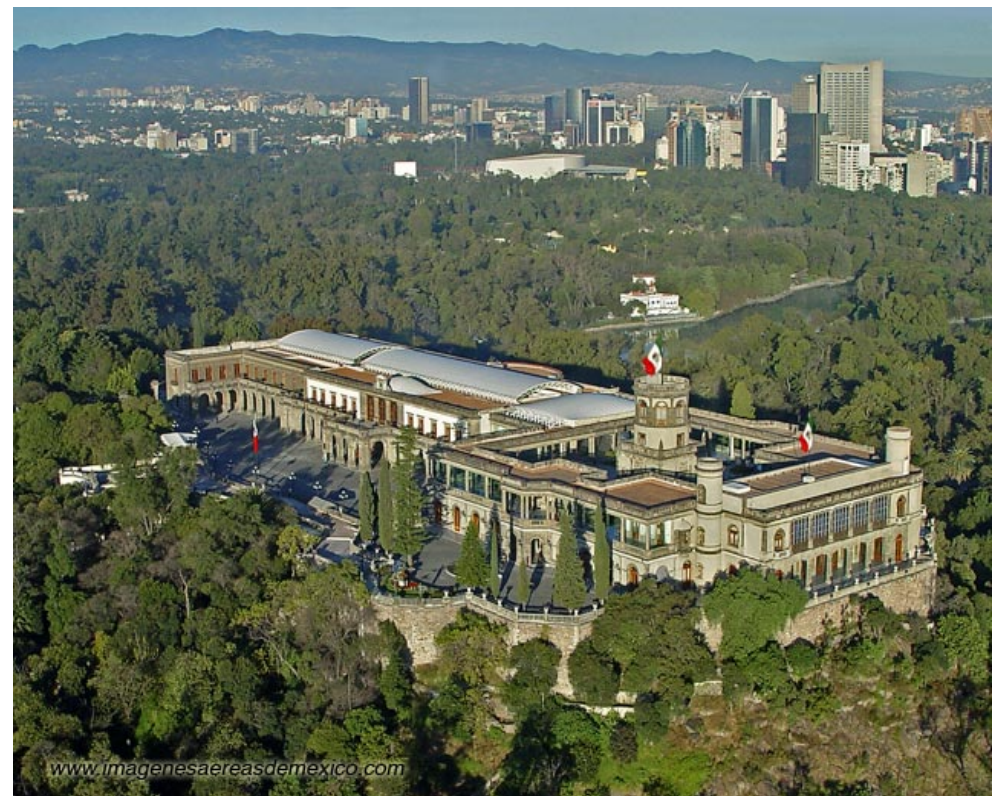


Horwath Castillo Miranda

## Accounting and Tax Structure in Mexico

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## Mexican Tax Structure

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- Corporate Income Tax (ISR), Flat Tax (IETU), Value Added Tax (VAT).
- Land Taxes.
- Payroll Taxes: Including state taxes and Federal Social Security Contributions.
- Import taxes and duties.
- Production and Service Special Tax.
- Other rights and contributions.

## Tax Structure: Corporate Income Tax (ISR)

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- Corporate Income tax rate in 1999, 35%. Now in 2009 is 28%, for 2010 will be 30%
- The tax is calculated on the Taxable Profit that differs from the Financial Profit.
- Special tax rates on depreciation and amortization of fixed assets.
- Monthly advanced payments (that will be credited against annual tax) are mandatory required.
- To determine the advanced payment a profit coefficient, using previous year results, is applied.

## Tax Structure: Corporate Income Tax (ISR)

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- Dividends paid that come from profits that paid ISR will not be subjected to additional deductions or withholdings. Special rules and restrictions apply.
- Is important to observe the formal and others requirements, to obtain the benefit of expenses deduction from taxable basis of ISR.
- Specific concepts are consider nondeductible expenses.

## Tax Structure : Business Flat Tax (IETU)

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- Starting in 2008 there is be a new tax, that “substitutes” the “old” Asset Tax.
- It will be a “Business Flat Tax”, known as IETU, calculated in cash flow basis.
- The “IETU” rate is for 2009 17% and is expected for 2010 a rate of 17.5%.

## Tax Structure: Business Flat Tax (IETU)

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- The determination of IETU will be as follows:

Accumulative Collections / Deposits

Less:

Authorized Deductions / Payments

Base of IETU

Times Rate

IETU Determined

Less:

Tax Credits

NET IETU to be paid

## Tax Structure : Business Flat Tax (IETU)

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- Aspects to consider:
  - Purchase of Land in Real State.
  - Salaries and benefits paid to employees.
  - Inventory and cost of sales.
  - Payments, in bank statement.

## Tax Structure: Value Added Tax (VAT)

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- The VAT is calculated on top of all products and services, between companies and to final users.
- Rates: 15%, 10%, 0% and exempted products and services.
- The general rate may change to 16% in 2010.
- Is a cash flow basis tax.
- Most imports of products are taxed at 15% VAT plus duties and other import taxes and required to be paid through the customer broker.



## Accounting Considerations

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- Very formal process. Importance of support in paper.
- Is required to elaborate financial statements in Spanish and according to Mexican Financial Information Standards NIF, (former General Accepted Accounting Principles, PCGA).
- Accounting registries and books of accounting in Spanish according to the Mexican laws.
- All records must be in *Mexican pesos*, special rules apply to value foreign currency and the recognition of gain and losses.

## Accounting Considerations

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- The accounting software has to be able to produce “accounting books”.
- The chart of accounts should include specific tax accounts, where tax concepts should be registered / controlled.
- Invoices are required to be printed with an authorized printer. Also the option of electronic invoices is possible.
- Specific rules for inventory valuation and cost of sales determination.

## Accounting Considerations

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- Internal controls.
- Time to keep accounting books: Five years.
- Other periods for corporate documents and tax returns.
- Valuation of foreign currencies: Specific rules to calculate gain or loss in exchange rate.

## Other Considerations

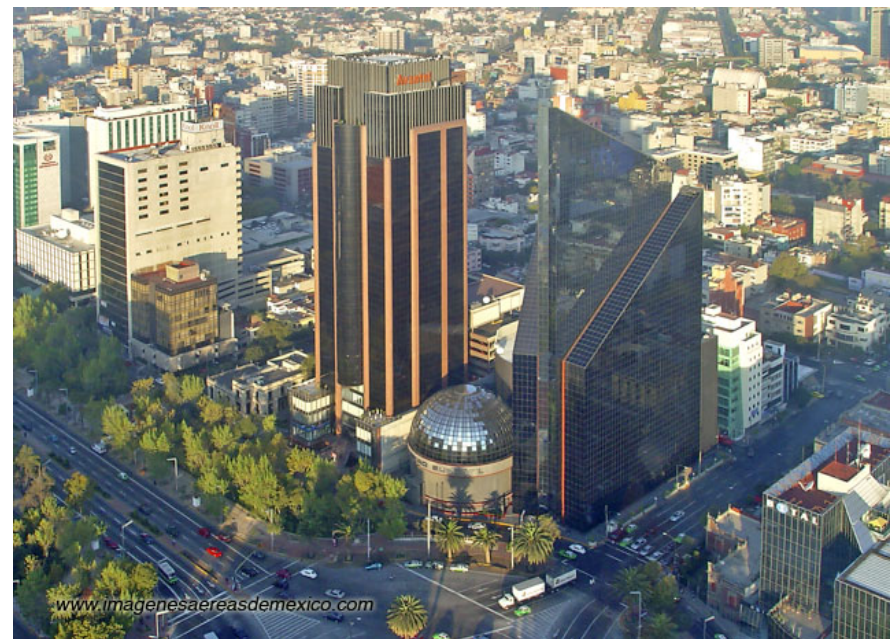
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- Tax Losses can be carried forward for 10 years.
- The fiscal year begins on January 1st and ends on December 31st of the same year.
- Mandatory tax opinion of an external accountant, in specific cases. The accountant must have an authorization of the government.
- Obligation to withhold tax in specific payments:
  - Salaries.
  - Professional fees and rents paid to individuals.
  - In payments to foreigners.
  - Others according to industry and activity to be performed in Mexico.

## Other Considerations

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- Obligation to carry out a Transfer Pricing Study in operations with related parties (entities with common shareholders).
- All of the corporate federal tax returns (monthly and annual) are filled (and paid) through the Internet.
- It is required to have a tax domicile / fiscal address.
- Determined products, like cigarettes and alcoholic beverages are subjected to the Production and Service Special Tax.



## Tax Benefits / Incentives

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- To better compete and be more attractive, several benefits and tax incentives have been established in the laws.
- Specific Rulings apply to be eligible for benefits and incentives.
- States governments according to their own strategic plans are entitled to give additional or special benefits in order to attract investment in their states and the creation of jobs.
- For example reductions in land tax, exemptions for payroll tax, etc.

## Income Tax Benefits / Incentives

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- For tax payers that fulfilled in time the payment of the monthly advance Corporate Income Tax.
- Will be eligible for a credit of 0.50% on the fiscal result of 2009.
- If the difference between provisional payments presented and according to Law does not exceed 5% and additional credit of 0.25% can be taken.
- The above applies for companies audited for tax purpose.
- Accelerated depreciation of specific type of fixed assets, only in certain cities / areas.

## Import - Export Benefits / Incentives

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- One of the goals is to encourage exportation, several benefits have been created.
- **Incentives**
- Export most common programs:
  - (New) Manufacturing, Maquila and Service Export Industries (IMMEX) is the unification of the exportation programs known as “Maquila” and “Pitex” into IMMEX program, effective date of statute, November 13, 2006.
  - Certified companies.
  - Refund of customs duties paid on goods used to produce exports (Drawback).
  - Major export companies (Altex).
  - Foreign trade companies (Ecex).
  - Sector programs (Prosec).
  - Fiscal deposit.
  - Strategic fiscal premises.
- Nonpayment Value Added Tax in imports.
- Immediate return of balances in favor of Value Added Tax within 5 days.

## Import - Export Benefits / Incentives

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- **Benefits** of the IMMEX Program
  - Main concept: IMMEX companies are able to differ (or postpone) the import duty payment for NAFTA Merchandise to add a process and return to the US.
  - No VAT in importations of assets (machinery), for temporary use in Mexico.
  - No generation of Permanent Establishment for IMMEX Companies as follows;
  - The goods to be imported temporarily (raw materials, parts, components, fixed assets, etc), can be property of the IMMEX Companies or of a foreign resident.
- Income Tax in base to Safe Harbor
  - 6.5% over expenses.
  - 6.9% over assets.

## Other Benefits / Incentives

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- Special benefit on Research and Technology Development.
- 30% of refund on expenses and investments.
- Is required to be informed in the annual tax return.
- Other formal requirement apply.



## Conclusions

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- Mexico's size and diversity are often under appreciated by U.S. exporters. It can be difficult to find a single distributor or agent to cover this vast market.
- The Mexican legal and tax system differs in many significant ways from the U.S. system. U.S. firms should consult with competent advisors.
- The banking system in Mexico has shown some signs of growth after years of stagnation, but interest rates remain relatively high.

## Conclusions

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- U.S. companies need to conduct thorough due diligence before entering into business with a Mexican firm.
- Mexican customs regulations, product standards and labor laws may entail pitfalls to unwary U.S. companies.
- Define a proper strategy to enter the market.
- Select a reliable costumes broker.
- Perform budgets of all the costs related to the initial investment and working capital for the initial period.

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**THANK YOU**