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QUIBRERA SALDAÑA

DOING BUSINESS IN Mexico GUIDE 2020

Doing Business in
Mexico
Guide 2020

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INTRODUCTION

The ECOVIS handbook "Doing Business in Mexico" has been prepared to provide an overview of investment issues in Mexico. Topics covered include an overview of Mexico; the Mexican business environment; starting a business in Mexico; taxation; banking and finance; financial reporting and auditing, and labor relationship and social security.

While such handbook should not be regarded as offering a complete explanation of investment issues in Mexico, at ECOVIS Mexico we hope readers will use this handbook as a point of reference and then use our service at ECOVIS Mexico to receive specific information and advice.

ABOUT ECOVIS

INTERNATIONAL

Ecovis is a leading global consulting firm with its origins in Continental Europe. It has over 7,500 people operating in over 75 countries. Its consulting focus and core competencies lie in the areas of tax consultation, accounting, auditing and legal advice. The particular strength of Ecovis is the combination of personal advice at a local level with the general expertise of an international and interdisciplinary network of professionals. Our 360-degree approach brings together experts from many fields and helps us make sure we can give you all the advice you need to meet the specific challenges of your business, today and also tomorrow. This diversified expertise provides clients with effective support to help our clients achieve their professional goals and objectives, making it easy to offer a superior and personalized service at a reasonable price.

MEXICO

As part of this worldwide network, in Mexico, ECOVIS Quibrera Saldaña focuses on generating results in the areas of auditing, tax, and finance of its clients, providing services of the highest quality, and delivering security through tangible results that contribute to the creation of value, expansion and protection of our clients' wealth.

1. OVERVIEW OF MEXICO

1.1. GEOGRAPHY

Mexico, officially called the United Mexican States, with an area of 1,964,375 square kilometers, is the world's thirteenth largest country.

It shares its northern border with the United States (U.S.) and its southern border with Belize and Guatemala. The eastern part is surrounded by the Gulf of Mexico and the west of the country borders the Pacific Ocean. Mexico has three mountain ranges - the Western Sierra Madre, the Eastern Sierra Madre and the Southern Sierra Madre.

1.2. CLIMATE

Mexico's climate is determined by several factors, among which are the altitude above sea level, geographical latitude, various weather conditions and the distribution of land and water. Therefore, the country has a variety of climates; we can classify those according to the temperature, as warm and temperate, or according to humidity as humid, sub-humid and dry.

The rainy season usually occurs from May to October. There are very few regions, aside from the higher mountains, where it snows, usually in winter. Most of the

coastal regions have a warm, humid, tropical climate.

Mexico City has a temperate climate and the annual average temperature ranges from 7°C to 22°C.

1.3. POPULATION

Mexico's population in 2020 is approximately 129 million people. Over the years, Mexico has indicated positive population growth; however, over the past few years, the annual population growth has dropped to less than 1%. In 2019 the average age of the population was 29 years old.

1.4. LANGUAGES AND RELIGION

The official language in Mexico is Spanish. In addition, 6.5% of the population speak an indigenous language.

English is also used in the international business community in Mexico City and other cities in the country, like Monterrey and Guadalajara, as well as in the areas bordering the United States (U.S.).

Mexico has a rich and wide variety of religions including, Catholicism, Christianism, Protestantism, Evangelicalism, Adventism, Jehovah witnesses, Judaism and Islam. In 2020, the main religion in Mexico was Catholicism with an 82.72% of followers and the second is Christianism with 7.47% of followers among the general population of the country.

1.5. GOVERNMENT AND LEGISLATION

Mexico is a representative, democratic, secular and federal Republic, composed of 31 States and Mexico City. The Political Constitution of the United Mexican States establishes three branches of government – Executive, Legislative and Judicial. The head of the executive power is the President, who is elected by direct popular vote for a period of six years and may not be reelected. There is a legislative as well as a judicial branch.

The legislative branch consists of the Senate, with four representatives from Mexico City, each state (128 members), and the House of Representatives, with 500 members. Senators serve for a period of six years and Representatives for a period of three years.

The judicial system is charged with enforcing the Constitution and solving conflicts between the country's parties. The judicial branch is formed by the Supreme Court of Justice of the Nation (SCJN), and the Electoral Court, Collegiate Circuit Courts, a Unitary Circuit Court and District Courts.

The state governments are headed by popularly elected governors, who also serve for six years.

The states have their own legislatures and judicial systems.

The supreme law is the Constitution which is the foundation of the other laws.

1.6. ECONOMY

The economy is dedicated mainly to supplying the needs of the population. Mexico's economy is driven by external trade. However, proximity to the U.S. also provides a large market for the export of manufactured goods. Federal taxes on oil production and exports provide a substantial portion of the total resources of the federal government. Tourism, agriculture and mining also contribute to revenue.

Mexico's External Debt has reached 449.5 USD bn in Sep 2019, compared to 457.8 USD bn in the previous quarter. Mexico's External Debt: USD mn data is updated quarterly, available from March 2002 to September 2019. The data reached an all-time high of 457.3 USD bn in Jun 2019 and a record low of 157.7 USD bn in Sep 2003.[1]

The estimated inflation rate for 2020 is 3.60%.

In 2018, the gross domestic product per capita was of USD 9,715.[2]

The current interest rate on Treasury Certificates (CETES) at a 28-day rate is 7.12%.

1.7. BUSINESS HOURS

Business offices normally open at 9:00 a.m. for an eight–hour working day, with one or two hours for lunch, starting at around 2:00 p.m.

Some banks are open from 9:00 a.m. to 4:00 p.m. and others open until 5:00 or even 7:00 p.m.

1.8. MANDATORY HOLIDAYS

The Federal Labor Law establishes the following mandatory holidays:

- January 1 (New Year's Day),
- February 5 (Constitution Day),
- March 21 (Benito Juarez's Birthday),
- May 1 (Labor Day),
- September 16 (Independence Day),
- November 20 (Revolution Day),
- December 25 (Christmas Day).
- December 1st is an official holiday held every six years for the beginning of the new presidential period.

Some of these dates are moved to the nearest Monday. Religious holidays are also observed by most business offices and banks, including Easter Thursday and Easter Friday, November 1st and 2nd, and December 12th.

1.9. CURRENCY

Mexico's national currency is the Mexican peso (MxP).

At the beginning of 2020, the average exchange rate found itself at 20.00 pesos per U.S. dollar.

Foreign currencies can be exchanged for pesos in banks and currency exchange houses.

[1]Source: http://www.banxico.org.mx/ [2]Source: http://datos.bancomundial.org

2. BUSINESS Environment

2.1. INVESTMENT CLIMATE

Mexico is an open economy, which through its network of free trade agreements, ensures access to international markets. The country offers competitive prices and a strategic geographical position, due to the wide variety of natural resources, enabling the development of all kinds of industries. Mexico's industrial sector has been favored by free trade agreements and as of today, the Mexican Government has created an environment of openness and security for foreign investors.

In recent years, Mexico has become the largest exporter in Latin America, accounting for approximately 35% of the total trade in Latin America.

The United States (U.S.), due to its geographical proximity and much anticipated benefits of the United States Mexico Canada Agreement (USMCA), the U.S. is among the countries with greater investment in Mexico. In the Yucatan Peninsula, foreign investment is still highly attractive due to its natural appeal. The sectors that have received the most foreign investments are financial services, automotive, electronics and energy industries. The main importing countries are Germany, Japan and Korea.

Almost 80% of Mexico's exports go to the U.S. and about 50% of Mexico's imports are supplied by the United States. Perhaps the European Trade Agreements (TLCUE) shall become a major investment window in the future for the textile industry as well as the manufacturing industry.

Mexico's main foreign investors are: U.S., Spain, Canada, Germany, the Netherlands, Japan and Belgium.

Mexico has a network of 12 Free Trade Agreements with 46 countries (FTAs), 32 Agreements for the Promotion and Reciprocal Protection of Investments (APPRIs) with 33 countries and 9 agreements of limited scope (Economic Complementation Agreements and Scope Agreements) (Partial) within the framework of the Latin American Integration Association (ALADI).

In addition, Mexico participates actively in multilateral and regional organizations and forums such as the World Trade Organization (WTO), the Asia-Pacific Economic Cooperation Mechanism (APEC), the Organization for Economic Cooperation and Development (OECD) and LAIA.

Economic activity is concentrated in Mexico City. The country's economy is driven by foreign trade. In general, export earnings are related to the manufacturing, oil, agriculture and mining industries.

MEXICO TRADE AGREEMENTS

NAME OF THE TRADE AGREEMENT	MEMBER COUNTRIES
AELC	Iceland, Liechtenstein, Norway and Switzerland
Agreement with Chile	Chile
Agreement with Colombia	Colombia
Agreement with Costa Rica	Costa Rica
Agreement with Israel	Israel
Agreement with Nicaragua	Nicaragua
Agreement with Uruguay	Uruguay
T-MEC / USMCA	United States and Canada
TLCUE	European Union
TN	Salvador, Guatemala and Honduras
UNIQUE TLC	Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua

Source: https://www.gob.mx/se/acciones-y-programas/comercio-exterior-paises-con-tratados-y-acuerdos-firmados-con-mexico

2.2. STARTING A BUSINESS IN MEXICO

Conducting a business in Mexico for foreign companies is a decision that often requires consideration regarding what kind of channel should be used for that purpose. Foreign investors could act directly, through a branch office in the country, or perhaps incorporate a legal entity.

According to the applicable Mexican corporate provisions, a foreign corporation may conduct business in Mexico by registering a branch office with the right to open a bank account and issue invoices. For tax purposes, branches are considered as a Permanent Establishment (PE). However, PE's do not have a separate legal existence from the foreign corporation, which may be liable for acts performed by the branch in Mexico.

Normally when limitation of responsibilities is an important issue to the foreign corporation, it is advisable to act in Mexico through a Mexican company, such as in the case when the term for rendering of services or conducting business activities in the country is expected to be unlimited.

On the other hand, regarding the incorporation requirements and time frames (as well as the information required to incorporate a legal entity), the process is faster and less burdensome than incorporating a Mexican branch office, since it is more common and does not require an authorization from the Mexican Authorities to start operations in Mexico.

2.2.1. TYPES OF LEGAL ENTITIES

In order to incorporate a new Mexican company, it is necessary to a business form. Business entities are formed in accordance with different laws which are: The General Law of Commercial Companies (Ley General de Sociedades Mercantiles),

THERE ARE SEVERAL ENTITIES THAT ARE ACCEPTED BY THE ABOVE-MENTIONED MEXICAN LAWS, SOME OF THESE ARE:

SPANISH NAME	ENGLISH NAME
Sociedad Anonima (S.A.)	Stock Corporation
Sociedad de Responsabilidad Limitada (S. de R.L.)	Limited Liability Company
Sociedad en Nombre Colectivo (S. en N.C.)	General Partnership
Sociedad en Comandita por Acciones (S. en C.)	Limited Liability Stock Partnership
Sociedad Cooperativa (S.C.)	Cooperative Association
Sociedad Civil (S.C.)	Civil Partnership
Asociacion Civil (A.C.)	Civil Association
Asociacion en Participacion (A. en P.)	Joint Venture
Sucursal de Sociedad Extranjera	Branch of a foreign Corporation

the Securities Market Exchange Law (Ley del Mercado de Valores), the Commercial Code (Código de Comercio), or the Civil Code (Código Civil).

However, the most common are:

A. Sociedad Anónima or Stock Corporation. There must be at least two shareholders (individuals or entities) which must hold at least one share each. The Corporate Law does not establish a minimum amount of capital, but at least 20% of the fixed minimum capital must be paid off at the start. The shares are represented by nominal certificates which serve the purpose of accrediting and transferring the status and rights of their shareholders. Each share is equal in value and confers equal rights. However, it may be agreed in the deed of incorporation that certain shares will only confer a vote in special meetings held to deal with specific matters. Profit and capital are distributed in proportion to the nominal amount of the shares. The liability of the shareholders is limited to the value of their subscribed shares. The capital stock of the company is divided into shares with the same face value. A simple majority of shareholders has control, unless the bylaws establish a larger majority (e.g. for major decisions). Five percent (5%) of net profits must be allocated annually to a legal reserve until the reserve equals 20% of the value of the principal authorized. Any reduction in the reserve must be restored to the 20% level. The general meeting of shareholders is the supreme authority of the company. General meetings may be ordinary or extraordinary, in nature, depending on the matters they deal with. Annual general shareholders meetings are required to discuss, approve, or modify the financial reports submitted annually by the administrator(s). The administration of the corporation is entrusted to a sole administrator or board of directors (at least two) who may or may not be shareholders. Officers may be Mexican or foreign. A statutory auditor must be appointed to monitor execution of the administration of the company different from the shareholders of the company.

B. Sociedad de Responsabilidad Limitada or Limited Liability Company. It is comprised by partners (at least 2), but there may not be more than 50 (individuals or entities) whose liabilities are limited to the amount of their contributions. Shares in the capital may not be represented by negotiable certificates. The Law does not establish a minimum amount of capital, but at least 50% of the minimum

capital established must be paid off at the start. Partnership interests apply instead of shares and could have different values and categories with a minimum of MxP$1 or its multiples for each. Each partner may hold only one interest. If a partner makes a new contribution or takes over partial or all interests of another partner, the value of his interest is increased accordingly. The administration of the company is entrusted to one or more managers. If no appointment is made, all partners shall participate in the administration of the company. The general meeting of partners is the supreme authority of the company. Each partner has the right to participate in decisions taken at general meetings, with one vote for each MxP$1 of his contribution to the capital. General meetings are held at the company's principal place of business at least once a year, on a date specified in the articles of association.

Each of these entities may be organized as a variable capital company (Sociedad de Capital Variable).

C. Sociedad Anónima Promotora de Inversión (SAPI) or Investment Promoting Stock Corporation. Stock Market Law regulates a more type of company, which is known as Sociedad Anónima Promotora de Inversión (SAPI), and has become an interesting vehicle to promote access of medium-sized companies to the securities market by providing the company features that make it more attractive for private equity or venture capital investment. There are two types of SAPI: a closely held company, or SAPI, and a SAPIB (Sociedad Anónima Promotora de Inversión Bursátil), which has stock registered with the National Banking and Securities Commission and listed on the Stock Exchange. The SAPI enjoys specific features such as higher standards of corporate governance and flexibility in the design of economic and corporate rights adapted to its shareholders' needs).

D. Joint Venture. Joint ventures may, at the parties' option, take the form of a public or private company, a partnership, an unincorporated association or may just be a contractual arrangement between the parties. The stock corporation with variable capital is the most common form, with the shareholders setting forth their respective rights in the articles of incorporation and by-laws.

A contract is entered into for the purpose of conducting certain business activities. The contract establishes one party as the "joint venture", who is the party charged with the day-to-day administration of the business. The other parties to the agreement, the "silent partner(s)" contribute money or services in exchange for a share in the profits and losses of the business.

Unincorporated associations do not have a separate legal personality but are merely contractual arrangements between two or more persons or entities. Unincorporated associations must be established in writing but are not registered in the Public Registry of Commerce. The joint venture carries out all business activities of the joint enterprise in its own name and is only liable to third parties for all obligations assumed in relation to the joint enterprise. The silent partners have no liability towards third parties under this arrangement. The joint venture may, however, sue the silent partners under the unincorporated association agreement.

E. Branch and representative office of a foreign corporation. Foreign companies wishing to perform acts of commerce in Mexico shall request an authorization to establish themselves in Mexico and register with the Public Registry of Commerce, as well as, if they only wish to establish a representative office

To clarify the above, we have the following:

- **Branch:** establishment in Mexico of a foreign company that performs acts of commerce.
- **Representative office:** establishment of a foreign company in Mexico that does not intend to perform acts of commerce.

Pursuant to Mexican Law, a branch is a legally recognized presence in Mexico of a foreign company, which does not involve the creation of a new company. The foreign company must be incorporated in accordance with the laws of its jurisdiction of incorporation and submit to Mexican Law for commercial activities carried out in Mexico.

All business activities engaged by the branch are done in the name and representation of the foreign company.

The foreign company must obtain the authorization of the Mexican Ministry of Economy and the National Foreign Investments Commission indicating where the branch desires to operate, and must submit the articles of incorporation and by-laws of the foreign company, its inventory or latest balance sheets, and the power of attorney of the person who is to represent the branch in Mexico. The articles of incorporation, by-laws, and the power of attorney, must be translated into Spanish and legalized by the consul of Mexico in the home jurisdiction of the company, or apostilled in accordance with the Hague Convention of 5 October 1961.

The authorization of the National Foreign Investments Commission (RNIE) must be published in the Federal Official Gazette. The authorization, the articles of incorporation and by-laws must be notarized by a notary public of Mexico.

The notary public must grant a public deed which must be registered in the Public Registry of Commerce (RPPyC) of the area in which the branch shall operate. In addition, the branch must be registered in the National Registry of Foreign Investments (RNIE).

Although a few companies have established branches in Mexico, they can have disadvantages for several reasons. Branches may not own real estate and they

may not deduct payments to the head office for the concepts of interest, royalties, fees or other services. Establishing a branch takes more time and funds than establishing a company, and branch charters usually contain more restrictions than corporate charters. Because branch offices are not legally separate from the head office, the head office can be held responsible for the liabilities of a branch.

REPRESENTATION OFFICES' AUTHORIZATION

On the other hand, foreign companies that need to establish themselves in Mexico to provide information and advisory services on the activities, products or services provided by their parent abroad, are known as Representation Offices and their main characteristic is that they do not carry out commercial activities in Mexico, they do not have incomes, but rather they receive incomes for their maintenance from abroad.

In this sense, a branch is one that usually performs acts of commerce and has incomes.

For this purpose, it is mandatory to obtain the authorization issued by the Mexican Ministry of Economy (SE) presenting a written request (original and a copy), attaching any required information which must be legalized or apostilled. In case it has been written in a language other than Spanish (including the apostille), it must be translated into

Spanish by a certified translator.

This procedure may last between 15 and 20 business days

A. Permanent Establishment. Any fixed place of business through which the business activities are conducted by the foreign corporation, can trigger a permanent establishment.

2.2.2. TIME FRAME FOR THE FORMATION OF A LEGAL ENTITY

One week to 10 days from the date on which the legal counsel or notary public has been provided with the relevant information regarding the company, i.e. its name, domicile and amount of the capital of the company, the shareholders (partners) and their participation therein, the directors (or sole administrator), the auditor(s) and, as the case may be, the general and/or special attorneys-in-fact. The time needed for the above must allow for the taking of legal advice, the drafting of the necessary documents and the required research regarding the availability of the corporate name before the Ministry of Economy (SE). The issuing of a permit to incorporate a Mexican company under a particular name by the Ministry of Economy (SE) may vary but normally it takes one to ten business days.

Incorporation may take longer under certain circumstances, such as the need to obtain authorization from Mexican authorities, including the Antitrust Commission (Comisión Federal de Competencia Económica), where the company is involved with certain products or services, or the Ministry of Finance and Public Credit (Secretaría de Hacienda y Crédito Público- SHCP) for banking and other credit activities.

2.2.3. DOCUMENTS REQUIRED FOR INCORPORATION

To incorporate a new entity, there are several requirements to fulfill, the most common are:

Company's by-laws (estatutos).- The basic incorporation of the company stating company's name; domicile; purpose; the amount of the authorized capital and its division into shares (or social participations); in general, the internal rules of the company governing shares (or social participations), the transfer and issue of shares, the calling, holding, proceedings, quorum and powers of general meeting, the appointment, removal, conduct and powers of directors or sole administrator and auditors, the declaration and payment of dividends and the dissolution and liquidation of the company. This document may be drafted either by a lawyer or by a notary public.

Permit for the use of the corporate name. - A permit must be obtained from the Ministry of Economy (SE) which keeps a record of corporate names. The permit may be refused when another Mexican company is currently operating under the same or a similar name or if special restrictions are provided for by law. The permit is valid for 180 calendar days from the date of issue. If the company is not incorporated within this period, a new permit must be obtained from the same office.

Transitory articles (cláusulas transitorias).- Adopted at the first general meeting of the company. Contains the names of the shareholders (or partners) of the company

or partnership and their participation in the company; the appointment of the board of directors (or managers) or, as the case may be, of the sole administrator, and of the internal auditor or auditors and any other resolutions the shareholders (or partners) may consider it convenient to take, such as increases of the capital stock, appointment of the external auditors of the company, etc.

The most common entities are the Stock Corporation and Limited Liability Company. It is advisable to know that foreign companies and individuals may own any portion or all the equity of a Mexican company. However, there is an exemption to this rule and applies to entities engaged in activities or acquisitions that are reserved or subject to specific regulation, such as: banks, credit unions, oil and gas, electricity, postal services, and other governmental functions which are reserved for the Federal State.

2.2.4. PROCEDURES RELATED TO NEW ENTITIES

Once the company has been duly incorporated, the shareholders or their attorneys must conclude the following procedures in order to allow the entity to operate without problems:

- Get a notice to the Public Registry of Commerce and Property (RPPyC).- This step is frequently carried out by the notary public who has issued the final official copy of the company's bylaws, and shall be executed at the location of its incorporation.
- Enroll it in the National Registry of Foreign Investment (RNIE). - Any entity with foreign capital shall fulfill with this procedure. Between its liabilities it must fill out annual reports on the nature of the investment and its results.
- Get an importer's license. - If the company is required to carry out imports of raw or other materials, it must provide due notice to the Tax Authorities and get its corresponding registration, for that purpose it must provide the patent number of a customs broker.
- Enroll to Mexican Institute of Social Security (IMSS).- This procedure is required for both employers and employees.
- Housing Fund (INFONAVIT) and Retirement Savings Fund (SAR).- This liability is granted in favor to the employees.

2.3. MERGERS, SPIN-OFFS AND ACQUISITIONS

There are two different types of mergers 1) a vertical merger in which one company has already acquired the shares of the other company, and 2) a horizontal merger, where two or more companies are merged with the assets and liabilities of one company exchanged for new shares of the surviving company.

A corporate spin-off will be treated as a tax-free reorganization, provided that 51% of the shares with voting rights are maintained for three following years, beginning one year prior to the spin-off. The shareholders of the 51% must maintain the same proportionate holding in the capital of the resulting entities as they had in the original entity prior to the spin-off.

Mergers, spin-offs and acquisitions are taxed as transfers of property. Mergers and spin-offs will not be taxed if they meet the following requirements:

- Notifying merger before the Tax Authorities

- Filing a tax return for the last fiscal year, as well as any required information statements through the surviving company in the case

of a merger, or through the designated company in the case of a spin-off where a company does not survive.

- In a merger, the surviving company should continue to engage in the same activities in which it and the merged companies engaged in before the merger.

- If a merger is going to take place within five years of a previous merger or spin-off, an authorization must be obtained from the Tax Authorities.

3. BANKING and Finance

3.1. INTRODUCTION

Mexico City is among the cities that has important financial, industrial and commercial centres. The Financial System in Mexico plays a very important role in the functioning and progress of the country's economy. Within the financial system there are development banks, public credit institutions, commercial banks, savings and loan associations, and mortgage banks. In addition to market institutions, insurance companies, credit unions, factoring companies, among others. The main intermediaries are banks, offering their services directly to the public.

Likewise, there are other intermediaries and organizations that offer useful services to society.

For Mexico's economic growth and population welfare, an efficient, competitive and innovative financial system is needed. The highest administrative body is the Ministry of Finance and Public Credit (SHCP), which obtains monetary resources from various sources to finance the country's governmental function development. There are six other public institutions which aim to supervise and regulate entities that are part of the financial system, which are:

FINANCIAL SYSTEM IN MEXICO

INSTITUTION	FUNCTIONS
The Central Bank (Banco de Mexico)	Promotes the healthy develoment of the financial system. Autonomous institution within the federal government. Puts the national currency into circulation and implements monetary and exchange rate policies.
National Banking and Securities Commission (CNBV)	Supervises and regulates financial institutions. Ensures the stability and proper functioning of financial institutions. Maintains and promotes the healthy and balanced development of the financial system as a whole.
National Insurance and Bonding Commission (CNSF)	Inspection and supervision of institutions and mutual insurance companies. Inspection and surveillance of people and companies established by law on the subject.
National Commission for Retirement Saving System (CONSAR)	Regulates and supervises the proper operation of the participants of the pension system. Protects the interests of workers, ensuring efficient and transparent management of their savings, favouring a dignified retirement and contributes to economic development.
National Commission for the Protection and Defence of Users of Financial Services (CONDUSEF)	Promotes, advises, protects and defends the rights and interests of people who use or hire a financial product or service offered by the financial institutions operating within the national territory. Creates and fosters proper culture of operations and financial services among users.
Institute for Bank Saving Protection (IPAB)	Protects the deposits of small savers and thereby contributes to preserving the stability of the financial system and the smooth operation of the payment systems.

Source: http://www.banxico.org.mx/

Mexico generally does not have currency exchange controls.

There is no restriction on the import or export of capital. Repatriation payments can be made in any currency.

We can divide the Mexican financial system according to the activities that are carried out in the following sectors, currently all are directly and indirectly regulated by the SHCP through the relevant committees:

3.2. BANKING SECTOR

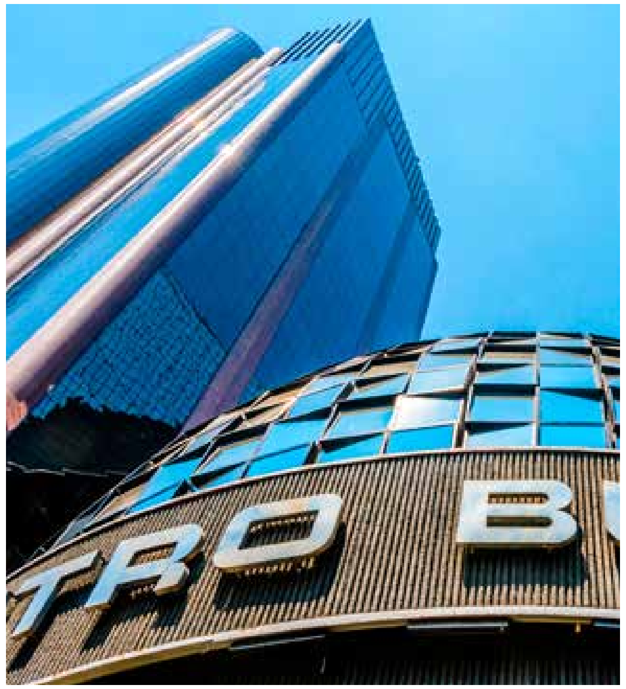
It is the sector that has increased its participation in the market and society. Banking deposits transform people into a source of financing for productive projects. This sector includes:

1. Commercial Banks

2. Development Banks

3.3. BANKING BUT NOT COMPLEMENTARY SERVICES SECTOR (PARALLEL)

Auxiliary credit businesses:
1. Money Exchange
2. Credit Unions
3. Factoring and Leasing
4. Savings and Loans
5. Sofomes



3.4. SECURITIES SECTOR

It is responsible for channelling resources directly to investors seeking credit, private companies or government. These operations are performed with securities that represent a liability or part of capital of the company to whom it delivers the borrowed resources

3.5. DERIVATIVES SECTOR

This sector is involved in the purchase price or future sale of a determined financial asset.

3.6. INSURANCE AND FINANCE SECTOR

This sector is dedicated to provide coverage on probable personal or corporate events that may cause financial losses.

3.7. PENSIONS SECTOR

Within this sector, Retirement Funds and Investment companies specialized in retirement funds are dedicated to receiving resources in order for active workers to be able to receive a pension with which to support themselves during their retirement.

3.8. MEXICAN STOCK EXCHANGE

The Mexican Stock Exchange (BMV), is a private institution, which operates by grants from the SHCP subject to the Securities Market Law (LMV). It is a place where negotiations are conducted in securities trading, whose main responsibility is to facilitate the completion of transactions in securities and to promote market development. Among its main functions is to establish the policies, means, and mechanisms to facilitate relationships and transactions between supply and demand for securities, debt securities and other documents registered in the National Securities Registry (RNV) and provide the services necessary for the conduct of the issuing processes.

3.9. FATCA'S (FOREIGN ACCOUNT TAX COMPLIANCE ACT)

The SHCP in conjunction with the Treasury Department and the Internal Revenue Service (IRS) of the United States (U.S.), signed an agreement on November 19, 2012 to adopt the automatic and reciprocal exchange of information between the two countries, where U.S. citizens have accounts in another nation.

In Mexico, since January 2013, FATCA requires foreign financial institutions to exchange information, through a report to the IRS where the existence and details of accounts of U.S. citizens are integrated. This was done in two stages, first during 2013 as a transition year for the banking

and financial institutions to prepare the technological and operational infrastructure necessary to collect information from pre-existing accounts and to transmit it to the IRS. And the second step, which began in 2014, involves reporting on any new accounts.

Financial institutions in Mexico have an obligation to provide information to the SAT regarding U.S. citizens and residents who hold bank accounts in the country, which together exceed USD 50,000 by the end of the year, so that the Mexican Government can automatically report to the authorities of the U.S. any information regarding its citizens (name, address, federal tax, average monthly balance and detail of their accounts whether they be in custody or deposit).

This obligation is also transferred to the United States of America, who through their financial institutions must also identify their clients of Mexican origin.

3.10 COMMON REPORTING STANDARD (CRS)

As a follow up to FACTA, OECD adopted in July 2014 the recommendation regarding the CRS; and in consequence, Mexico succeeded in signing in October 2014 the Multilateral Agreement between Competent Authorities on the Automatic Exchange of Information on Financial Accounts (MCAA), signed during the 7th Meeting of the Global Forum on Transparency and the Exchange of Information for Fiscal Purposes in the city of Berlin, Germany, whose main objective is to exchange information automatically and reciprocally among a total of 50 countries.

CRS is inspired by the intergovernmental approach which governs the FATCA. Despite their similarities, these agreements maintain certain differences which mainly lie in the specific purposes of the public policy pursued by their creators. The main

differences between both systems are the following:

- FATCA is bilateral, while CRS is multilateral.
- FATCA is based on nationality and residence, while CRS is based on the fiscal residence.
- FATCA establishes a tax withholding system, unlike CRS that does not establish withholding of any type.
- FATCA establishes exemption thresholds that could be applied at the financial institutions' choice for the identification and classification of accounts, while CRS eliminates any threshold of exemption from identification and review of accounts opened in financial institutions.
- FATCA establishes that to make a report the account must exceed the limit of USD 1,000,000, while in CRS it must exceed the amount of USD 250,000.

Pursuant to the CRS system, the financial institutions, as the main transmitting agents of international information, inform the interested countries of the activity of their financial accounts, which from the moment of their contracting are known to be subject to communication to the interested parties of the other countries. Subsequently, there is a phase of due diligence procedures, in which it is sought to apply the necessary operative rules to be able to transmit the information of the ID of the persons subject to be informed, balances in the financial accounts that have a certain date and the amount of the total incomes that have been generated in the respective period.

CRS is in force in Mexico as of January 1, 2016 and its regulation is through the Federal Tax Code and general administrative provisions. Currently, countries such as Barbados, Switzerland, Israel, Azerbaijan, and Panama are already reportable.

4. FINANCIAL REPORTING and Auditing

4.1. SOURCES OF ACCOUNTING REGULATION

The Mexican Council for Research and Development of Financial Reporting Standards (Consejo Mexicano para la Investigación y Desarrollo de Normas de Información Financiera – CINIF) is recognized as the principal authority for issuing financial reporting standards in Mexico (Mexican FRS- Normas de Información Financiera–NIF). The CINIF issues pronouncements on accounting and reporting standards and updates them whenever necessary. On 2008 CINIF and the National Banking and Securities Commission (CNBV) announced the mandatory application of International Financial Reporting Standars or "IFRS" from 2012 to companies listed in the Mexican Stock Exchange.

According to Mexican FRS A-8 "Supplementary", which establishes the basis for the supplementary application of International Financial Reporting Standards "IFRS" (Normas Internacionales de Información Financiera – NIIF), IFRSs are followed when a particular situation occurs that is not covered by Mexican FRS, and if neither a Mexican FRS nor an IFRS exists, FRS A-8 allows for the adoption of other standards, following the specific requirements provided by it to ensure proper application.

FRS B-10, 'Recognition of the Effects of Inflation on Financial Information' requires all companies to restate nonmonetary assets and liabilities, equity accounts and income statement items to account for the effects of inflation when cumulative inflation for the past three years is 26%. The method used to restate recognizes the effects of inflation in the financial information is the integral method.

Under this method, nonmonetary items must be restated and presented in constant-peso amounts. The original cost is restated using the national consumer price index (INPC). Monetary items are not restated; however, they generate a gain or loss in its purchasing power due to inflation. The monetary gain or loss represents the effects of inflation on a company's monetary position during a particular time period. It is included in the income statement as part of the "Comprehensive cost of financing", which incorporates interest, exchange gain or losses, and monetary gains or losses.

All financial statements must be expressed in constant peso terms at the end of the year. This presentation means that items-

including sales and operating expenses – must be re-expressed in terms of the purchasing power of the Mexican peso at the end of the year. Comparative financial statements are required, thus, amounts of previous years must also be restated in the constant peso value at the end of the last reported year.

Since January 1, 2008, the Mexican economy is in a non-inflationary environment by maintaining a cumulative inflation of the last three years of less than 26%, suspending as of this date the recognition of inflation in financial information.

4.2. ACCOUNTING REFERENCE PERIOD

The accounting reference period is 12 months. To comply with Mexican Income Tax Law (LISR as per its Spanish acronym), the Federal Tax Code (CFF as per its Spanish acronym) and the General Law of Commercial Companies (LGSM as per its Spanish acronym) an entity's fiscal year must coincide with the calendar year. However, an entity may choose a period (12 months) other than the calendar year for internal purposes. This may occur when Mexican Companies are subsidiaries of foreign entities whose fiscal year is other than the calendar year and for the purposes of worldwide consolidated financial statements.

4.3. ACCOUNTS AND REPORTS

A company must prepare individual accounts for each fiscal year of the entity comprising the following basic financial statements: statement of financial position, the statements of changes in equity, and of cash flows. Significant accounting policies used in the preparation of financial statements and notes to explain the information presented must be included. The financial statements must be presented at the annual shareholder's meeting and approved by the shareholders. Financial statements must be drawn up on a consistent basis every year.

In case a company is a holding company of a group, Mexican FRS requires preparation of consolidated financial statements of the company and its subsidiaries. In addition, holding companies whose securities are traded on the Securities Exchange are required by CNBV provisions to file individual and consolidated financial statements annually.

The company's external auditor must prepare an auditor's report addressed to the board of directors and stockholders stating whether the financial statements present fairly, in all material respects, the financial position of the company (and its subsidiaries where applicable), and the results of their operations, changes in their stockholders' equity and changes in their financial position, in conformity with FRS.

4.4. BOOKS AND RECORDS

All Mexican companies must maintain detailed accounting records in Spanish using Mexican Pesos (MxP). Mexican companies must maintain the following: a general ledger; a general journal; an "inventories and trial balances" record; books recording minutes of both board of directors' and shareholders' meetings; a record of investments in shares; a record of debts in foreign currency, credit and cash; and a record of its registered shares. The main books and records, together with all supporting documentation, must generally be maintained at the official domicile of the business and remain available for 10 years.

4.5. AUDITING STANDARDS

The Mexican Institute of Public Accountants of Mexico, A.C. (IMCP), a member of the International Federation of Accountants

(IFAC), acquired the commitment to adopt and align with the standards issued by this body.

Consequently, the IMCP membership approved on June 15, 2010 the integral adoption of the International Auditing Standards (NIA) or International Standards (ISA), for the audits of financial statements of accounting years beginning on January 1, 2012

The International Auditing Standards relating to the auditor's report state that auditors should distinguish between their responsibilities and those of the management by including in their report a statement that the financial statements are the responsibility of the company's management and a statement that the auditors' responsibility is to express an opinion on the financial statements.

Auditors must include in their report a statement that they conducted the audits in accordance with International Auditing Standards, which require the auditors to plan and perform the audit in order to obtain reasonable assurance about whether the financial statements are free of material misstatements and that they are prepared in accordance with the FRS.

A statement of the auditing process includes:

1. Examining, on a test basis, evidence supporting the amounts and dis- closures in the financial statements.
2. Assessing the FRS used, and significant estimates made by the management, as well as an assessment of the overall financial statements presentation must also be included.

The auditor's report must state whether, in the auditor's opinion, the financial statements under review present fairly, in all material respects, the financial position of the company as of (the balance sheet or statement of financial position date), its financial performance and its cash flows for the year which ended in accordance with Mexican FRS applicable in Mexico.

The auditor's report may include an unqualified or qualified opinion. The auditors may qualify their report because there is a limitation on the scope of the auditor's audit, or because of departures from FRS. They may issue an adverse opinion when the effect of the departure is so pervasive that the auditors conclude that the financial statements are misleading. They may also issue a disclaimer of opinion, whenever they are unable to form an opinion because of a limitation in the applied scope and they have not performed an audit that is sufficient in its scope to enable them to form an opinion on the financial statements.

Public accountants who issue financial statements must be registered with the tax authorities, be of Mexican nationality and must have current certifications issued by professional bodies or associations of Accountants registered and authorized by the Secretary of Public Education (SEP). This certification is the record that supports the knowledge, abilities and skills required for the exercise of the profession. Their revalidation should be performed periodically to ensure they are professionally up to date and capable of providing high quality services to customers and users.

4.6. OTHER AUDITING REQUIREMENTS

Companies with securities listed on the Mexican Stock Exchange (BMV) must comply with several disclosure requirements issued by the CNBV They are also required to have independent auditors perform annual audits of their financial statements.

Under the LISR, companies and individuals engaged in business activities that meet any of the three following criteria will be able to choose to audit their annual financial statements for tax purposes by a public accountant registered with the Ministry of Finance and Public Credit (SHCP). These criteria must be met in the preceding year in order to determine whether the obligation exists for the reporting year. The third and most common criteria are gross income exceeding MxP $100 million, assets exceeding MxP $79 million or having at least 300 employees (for each month of the fiscal year).

The amount of income and value of assets is subject to an annual restatement.

5. Taxation

5.1. TAX SYSTEM

5.1.1. MAIN TAXES

The main taxes that are payable in Mexico are those levied by the Federal Government, State and Municipal Governments. The main taxes, among others, are as follows:

1. **Federal taxes:**
    a. Income Tax (IT);
    b. Value- Added Tax (VAT);
    c. Special Tax on production and services (IEPS as per its Spanish acronym);
    d. Customs duties;
    e. Social Security Tax
2. **Local taxes:**
    a. On real property;
    b. On salaries;

5.1.2. LEGISLATIVE FRAMEWORK

The Congress annually approves the Federal Revenues Law (LIF as per its Spanish acronym), which is a legal order proposed by the Executive Branch that mainly contains the concepts under which financial resources may be raised to cover the expenses of the federation during a fiscal year, including a list of the federal taxes to be imposed during such year.

The Ministry of Finance and Public Credit (SHCP) is empowered to issue regulations for the enforcement of the Tax Laws.

The Annual Omnibus Tax Ruling published by the Tax Authorities may be relied on by the taxpayer, although they do not have the force of the law. Retroactive legislation is not allowed by the Constitution and its application is not legal.

5.1.3. CLASSES OF TAXPAYERS FOR THE INCOME TAX

Taxpayers could be divided into four main groups:

1. **Resident companies and other organizations taxable as companies and those under a joint venture contract.** These taxpayers are required to include all their incomes from all sources in an annual income tax return.

    A branch of a foreign company formally registered to do business in Mexico, as well as any other Permanent Establishment (PE) for income tax purposes, is generally taxed the same as a Mexican company, for all income attributable to such branch or PE in Mexico.

2. **Resident individuals.** These taxpayers are subject to Mexican taxation on their worldwide income of all types, most of which must be included in an annual personal income tax return.
3. **Nonresident (foreigners) companies and individuals.** The nonresident companies with a permanent establishment for income tax purposes are taxed in the same way as a duly registered branch of foreign companies, basically following the rules for resident companies.

    Nonresident or foreign individuals and companies without permanent establishment are taxed only on their Mexican-sourced income, (gross income without deductions) although under special rules they may choose to be taxed at higher rates on net taxable profits from sales of real property or capital stock or short- term construction and similar work. No annual income tax return is required of nonresidents.

4. **Nonprofit organizations.** Under the Mexican Income Tax Law (LISR as per its Spanish acronym), a limited number of organizations and government agencies are exempt from taxes. Other nonprofit organizations are generally considered non-taxpayers, rather than as being exempt from tax. These include a limited number of civil societies and civil associations that are specifically designated as such, although they are required to file the annual income tax returns to determine their net excess of income over expenses, and their members are subject to tax only as to any amounts of net income that are actually distributed.

5.2. TAX ADMINISTRATION

5.2.1. TAX AUTHORITY

The Tax Administration Service (SAT as per its Spanish acronym) is a decentralized agency responsible for assessing and collecting federal taxes and customs duties, while the Departments of Finance of each state or municipality are responsible for collecting state and local taxes. The federal government and the states have entered into agreements for tax coordination and administrative cooperation, where the states are now responsible for collecting and auditing the correct payment of federal taxes.

The rights of the Tax Authorities in relation to auditing, enforcement, assessment and collection of taxes (including electronic fiscal audit) expire after 5 years from the date on which the income tax return is due.

The statute of limitations will be extended for 5 (but no more than 10) years as from the date a restated income tax return is prepared for any category of items adjusted in a restated income tax return. The term is 10 years if the taxpayer is not registered in the Federal Taxpayer's Registry (RFC) of the SAT, and / or does not maintain accounting records and / or fails to file an income tax return. In the latter case, the 10–year term is computed from the date the return should have been submitted

5.2.2. PERIOD OF THE FISCAL YEAR

The fiscal year is the calendar year (from January 1 to December 31)

5.2.3. OBLIGATIONS OF THE TAXPAYERS

A. Advance Payments, Monthly Payments and Annual Return

Corporate Taxpayers must make 12 advance payments and definitive payments for the Income Tax (IT) and Valued Added Tax (VAT), respectively, on the 17th day of each month. The annual income tax return must be filed no later than March 31 (April 30 to individuals) of the following year and to pay the balance of tax due at that time. An annual information return regarding transactions with related parties abroad should be filed with the annual income tax return.

B. Informative Return

An annual informative tax return that includes information on withholdings, donations and salaries, loans received from or guaranteed by foreign residents, must be submitted to the tax authorities no later than February 15 of each year.

C. Withholding Taxes

In many cases a company making payments to third parties is required to withhold and pay to the Tax Authorities an amount of income tax on account of the recipient. In all such cases the company is jointly liable for the tax that should be withheld, and on failure to do so it is subject to penalty interest and fines.

The withholding obligation exists in general for all payments to individuals, including employees, and payments to foreign entities that are not registered in Mexico. In all cases where the LISR does not establish a specific period within which companies should remit taxes withheld, the period for payment will be the 17th of the month following that in which the taxes should be withheld.

D. Penalties and Fines

Penalty interest (surcharges) for late payment of tax is assessed at 0.75% per month if an extension has been granted; otherwise the rate is 1.13%.

Fines may also be assessed in the case of omitted tax, unless the taxpayer voluntarily pays the omitted tax or corrects the obligation not complied prior to a formal request for payments or to a receipt of a notification of an audit for the year in question.

E. Electronic Invoicing

Taxpayers must issue a digital tax receipt issued via the internet for selling products or rendering services. As of 2020, it is of the utmost importance that taxpayers keep their tax obligations up to date, to avoid being restricted the issuance of their invoices and can operate regularly. Likewise, the issuance of invoices can be restricted if taxpayers do not demonstrate supporting documentation of their operations and are non-existent or simulated.

F. Advanced Electronic Signature

Mexican Commerce Code defines e-signature (e.firma) as "Data in electronic format included in a message, or attached, or logically associated to the message through any technology, used to identify the signature in connection with a

encrypted message, and to indicate that the signature approves the information contained in the encrypted message. It produces the same legal effects of the autograph signature, thus being admissible in trial". In this sense, one format of the e-signature is managed by the Mexican Tax Administration System (SAT), which is in charge of regulating and granting e-signatures (e.firma) to taxpayers whether as individuals or entities in order to identify such taxpayers and whether they comply with their tax liabilities.

Taxpayers may now apply for their advanced electronic signature (e.firma) through an attorney in-fact or legal representative.

In order to avoid the establishment of companies with simulated operations, the tax authority may not authorize the issuance of the electronic signature if certain identification elements of both the partners and the address on record of the company are not verified.

G. Taxpayer's Mailbox

The purpose is to have an electronic communication system between the taxpayers and Tax Authorities whereby taxpayers may file motions, requests, notices or file tax obligations and even submit rulings about real and specific situations, and file appeals for reversal, among other issues. Taxpayers must have their advanced electronic signature to be able to use such mailbox. As of the fiscal year of 2020, any federal or state tax inspection authorities, such as IMSS, INFONAVIT, PROFECO, CONAGUA, as well as the authorities that exercise the power of control in the States, may notify through the SAT mailbox and not only the SAT.

5.2.4. RIGHTS OF THE TAXPAYERS

A. Advance Payments, Monthly Payments and Annual Return.

Taxpayers can ask a refund for undue payments or tax credit balances that comply with certain requirements.

B. Tax Offset

Taxpayers can offset their tax credit balances against taxes payable (including tax withholdings) but certain requirements are required.

During 2019, tax offset will only operate between taxes of the same type; initially, this provision was only applicable for the year of 2019; however, from 2020 it will be final.

However, by means of general tax rules, it has been clarified and allowed applying in 2019 and subsequent years the tax offset of VAT favorable balances generated as of December 31, 2018, establishing that such VAT favorable balance will be chosen to be offset against those that are obligated to pay for their own tax debts that derive from federal taxes other than those caused by importing, including tax updating and surcharges.

Derived from the above, the favorable balances of taxes generated from 2019, will only be able to be recovered through a refund application when they do not correspond to equal taxes.

C. Rulings

Taxpayers may request the Tax Authorities (SAT) for a ruling in connection with the interpretation of tax provisions in specific cases that are not already under review by the Tax Authorities.

The authorities must make decide within three months from the filing of a petition. If no decision is made within this period, the request is deemed as having been denied.

These rulings are binding for Tax Authorities only when the matter under discussion refers to a real transaction and its terms remain unchanged.

D. Opinion by Certified Public Accountant

Taxpayers that choose to have their financial statements audited by a certified public accountant must file these statements (along with the auditor's opinion on the taxpayer's compliance with the Tax Law) by July 15 of the following year of the financial year in question.

E. Types of means of tax defense or tax appeals

There are a series of instruments, mechanisms or means to protect taxpayers affected by the violation of their rights, i.e., instruments which taxpayers can go when the authority carries out acts that do not respect their rights as taxpayers, during a tax audit or as a result of it, resolving tax deficiency assessments.

The different types of means of tax defense of taxpayers could be administrative, jurisdictional or judicial process and non-jurisdictional. Likewise, tax defense cases could be handled by attorneys, but in any event, usually with assistance from accountants.

a) Administrative means of tax defense. These actions are brought through tax authorities' legal supervisory area and consist of such authority reconsidering its own tax deficiency assessment, taking into account the written document submitted by taxpayers to appeal such assessment. In other words, in this process, taxpayers submit a claim or a kind of lawsuit before tax authorities to clarify legally their tax situation and revoke the corresponding tax deficiency assessment.

Among the benefits of this procedure is to obtain the immediate suspension of any enforcement powers of the tax authorities, and the taxpayer would not have to guarantee the taxes under dispute during the process or shall not secure potential tax liabilities.

The interested party may choose to contest the tax deficiency assessment by means of an administrative appeal or to file tax trial before the Federal Court of Administrative Justice directly.

The administrative tax defense means are the following:

I. **Revocation hearing before the Administrative Authorities (Recurso de Revocación):** This administrative appeal shall be submitted by taxpayers before tax authorities in charge of federal/local taxes deficiency assessments within of the 30 days following the one in which the notification of such issued deficiency assessments has effects.

II. **Social security appeals (Recurso de Inconformidad):** This appeal is submitted against Mexican federal social security institute (IMSS) and Mexican federal institute that administers the workers' housing fund (INFONAVIT), in the event these authorities determine a deficiency assessments in charge to taxpayers as employers or employees, as the case may be, regarding their social security and housing contributions.

b) Jurisdictional means of tax defense

This jurisdictional means of tax defense whereby the taxpayer is not satisfied by the resolution of some administrative appeal or is affected by acts of authority, decrees and agreements of a general nature - different from the regulations, - may request the nullity of the act, decree or agreement before the Federal or Local Tax Court, as the case may be, submitting a tax trial, and following a judicial process in charge of an independent party different from the tax authorities legal area. Consequently, the responsible Tax Court holds jurisdictional autonomy, meaning that it does not depend on any other administrative office. This allows the taxpayers to provide evidence of any administrative records and all related documents properly submitted to tax authorities for a second evaluation. The Tax Court can partially or totally uphold, dismiss, or place the tax authority's decision on hold.

During judicial process, it is mandatory that taxpayers as a plaintiff party must secure potential and required tax liabilities, through a cash deposit, letter of credit or other forms of equivalent financial security, pledge or mortgage, bond posted with an authorized institution, among others.

This type of means of defense are the following:

I. **Tax Administrative Legal Action (annulment procedure).** This judicial action of annulment must be filed before Federal/Local Tax Court, within 30 or 15 days, as case may be, after receiving the notice of the tax deficiency assessment to dispute.

This action of annulment must be executed within the legal deadline, otherwise the tax assessment shall be deemed accepted and definitive.

Once the lawsuit is accepted, the court will require the defendant to file its appropriate arguments in defense of the tax assessment. Later, the parties shall provide evidence, arguments and a ruling will be issued, naming the effects of the judgment, i.e., the annulment of the decision being challenged.

As from 2017, there is an alternative for the taxpayer to elect a summary administrative appeal. Under this option, the reviewing authority will decide the case just with substantive arguments, excluding such formal violations, which delay the final resolution. As in the case of the general administrative appeal explained above, if necessary, the taxpayer may file an annulment procedure before the Federal Tax Court.

The legal proceedings in the Tax Court could take approximately 12-18 months after the claim is admitted.

However, if a favorable judgment is obtained by taxpayer, the authorities could appeal the judgment of the Tax Court. Likewise, if the taxpayer is not able to obtain a favorable result at this stage, it may file a final action before the Mexican Federal Judiciary Branch and / or Supreme Court of the Nation.

II. **Amparo/Constitutional Trial.** The Amparo Trial is a jurisdictional means of constitutional control whereby a person or entity comes before a judicial body to claim an act of an organ of the State or a law, when they violate their fundamental rights, in this case, as a taxpayer.

This judicial action can be promoted in two ways: direct and indirect, to enforce the unconstitutionality of any law and is submitted to the SCJN, the Collegiate Circuit Courts in administrative matters, and the District Courts in administrative matters. This procedure could take approximately 6-8 months after the claim is admitted.

c) Non-jurisdictional means of tax defense

Non-jurisdictional means of tax defense are those mechanisms that without using the jurisdictional function, they promote and protect the rights of the governed through their own processes, usually being more flexible.

Currently, one of the main non-jurisdictional tax defense alternative means are the following:

I. **Final Settlement Agreements.** These agreements are an alternative dispute resolution method when the authorities exercise their inspection or auditing powers against the taxpayers, who must request such final settlement agreement to the Office of the Taxpayer's Advocate (PRODECON-Mexican Tax Ombudsman) in order to: a) assist in the establishment of a position regarding any particular aspect disputed, or b) find a way to self- correct their tax status with regard to specific points.

   In any case, it has been considered that "final settlement agreements" will afford the parties involved a legal certainty, whereas if the relevant resolution favors the taxpayer, the authorities may not file an administrative action against the detrimental resolution (Juicio de Lesividad) and a contrary, if the resolution issued is in favor of the Tax Authorities, the tax payer may also not file any action or appeal against such resolution.

   One of the main advantages of this type of agreements is that when the taxpayer agrees to conduct a self-correction, it may have any fines due condoned in their entirety (on the first occasion), or it may be given the option to pay in installments, which also be applicable when the taxpayer wishes to conduct a self-correction in any of the available forms while the Authorities are exercising their auditing powers.

II. **Non-existent operations.** When the tax authority detects that a taxpayer has issued invoices without having the assets, employees, infrastructure or material capacity, directly or indirectly, to provide the services or produce, market or deliver the goods that cover said invoices, or that said taxpayers are not located, the operations covered by these invoices will be presumed to be non-existent. Thus, in this case, the tax authorities will proceed to notify the taxpayers that are in said situation through their tax mailbox, as well as through the publication in the Official Gazette of the Federation, in order for said taxpayers may provide the documentation and information they deem pertinent to distort the facts that led the authority to notify them. For this, interested taxpayers will have a period of 15 days from the last of the notifications that have been made. Failure with above, implies the questioned operations do not have fiscal effects.

5.3. INCOME TAX FOR ENTITIES

5.3.1. CRITERION OF TAXATION

Mexico takes the residence and source of wealth into consideration as criteria for Corporate taxation.

The Residence is met when the companies have their main business administration, or their place of effective management in Mexico, regardless of their nationality. Mexican tax laws does not contain a definition of the concept of source of wealth; nevertheless, it includes specific types of withholding in respect of income earned in Mexico.

Entities resident in Mexico are obligated to pay income tax on their worldwide income, and at the same time they have the benefit of crediting the income tax paid abroad fulfilling specific requirements.

5.3.2. TAXABLE ENTITIES

The tax system establishes a pre-tax

on a net base, and foreign entities are considered taxpayers of income tax when they obtain an income from a Mexican source. Income is deemed to derive from Mexican sources when the assets or activities are in Mexico or when sales or contracts are carried out in the country.

5.3.3. TAXABLE BASIS

Mexico has established a tax system over net basis, it consists in subtracting, from incomes earned in a fiscal year, the amount of authorized deductions, paid employees profit sharing (PTU as per its Spanish acronym) and ordinary tax loss carryforwards from prior years, if any.

It is relevant to point out that Mexican law considers inflation effects as income or deduction. There are two independent procedures i) currency exchange profits and losses, and ii) annual inflationary adjustment.

A. Gross Income

Residents in Mexico are subject to tax over its taxable income obtained in a fiscal year. Gross income could be considered those obtained in cash, goods, services, credit, and otherwise.

The income tax must be calculated every fiscal year, but it is necessary to file monthly advanced payments to pay the annual tax.

The Mexican Income Tax Law (LISR as per its Spanish acronym) distinguishes three different types of incomes: 1) taxable income, 2) non-taxable income, and 3) non-tax revenues.

1. Taxable income: Generally, all income should be taxable except if it comes from non-taxable income, or non-tax revenues, as appropriate. Taxable income comprises gross revenues plus currency and inflationary gains.
2. Non-taxable income: Dividends or profits received from another Mexican resident entity.
3. Non-tax revenues: Capital contributions, from use of the method of participation for valuation of the entity's shares, and premiums for placement of shares issued by the entity.

B. Deductions

The entity can consider all expenditures related with its corporate purpose. Nevertheless, such disbursements should meet specific requirements, among others; deductions have to be strictly necessary to realize the activity of the enterprise, and the taxpayer must obtain an electronic invoice, and the payments have to be made through wire transfer, credit card, or check. Electronic invoice must be issued in the same tax year in which the related

expense is deducted, and all mentioned conditions must be fulfilled, at the latest, on the date of filing of the tax return.

Deductible items include business expenses, depreciation of fixed assets, accrued interest, cost of sales, pre-operating and organization expenses, local taxes, certain social security taxes, donations to charitable entities and the government under certain circumstances, interest, royalties, remuneration of personnel, workers welfare, insurances, and bad debts fulfilling specific requirements for each one.

On the other hand, it is important to note that at date, to avoid the simulation of operations, the fiscal authorities require the taxpayers information or documentary evidence regarding the materiality or effective doing of their operations corresponding to their expenses, in order to admit the deductibility of them.

Regarding materiality, in order to avoid an operation from being declared non-existent, it is necessary to have the supporting documentation of the operations carried out, including the information on tax compliance, the accounting records, contracts, tax receipts and proof of payments and economic flow of said operations, and as the case may be, to gather information which

allows to locate all the situations of fact related to the operations, i.e, purchase orders, reports of services, log files, authorizations, licenses or permission, assembly minutes, deliverables and, in general, any information that proves the effective realization or materiality of the operations, as well as their business reason, i.e., the relationship with their lucrative activity and the need to carry it out.

Consequently, the fact that an operation meets the materiality requirement or not implies, among other things, the rejection of deductions for income tax purposes, or the inappropriateness of the corresponding creditable value added tax; as well as, in some cases the total or partial refusal in returns of balances in favor, which significantly affects the cash flow and operation of the companies.

It should be mentioned that it is very important to demonstrate, together with the materiality of the operation, the business reason for the operation, while even if it is demonstrated that the operation was actually carried out, it must also be verified the reason for carrying out the operation. That is, the relationship between the taxpayer's lucrative occupation and its objective of obtaining a profit. In the fiscal reform for the year 2020 the business reason will be an indispensable requirement for the tax effects of the taxpayers' operations.

On the other hand, it is important to mention that Mexico does not allow the deduction of federal taxes (IT and VAT), entertainment expenses in general, expenses allocated on a pro rata basis with foreign related parties (except for PE), amortization of goodwill, interests from thin-capitalization, penalties (except if it is established by Law), fines and indemnities when the taxpayer is responsible of them, payments made to entities located or resident in a low tax jurisdiction (unless it is proved that the transactions are carried out with non-related parties or at arm's length prices).

B.1. Limitations to Tax Deductions

I. Interest limitation deduction.

As of 2020, net interest (accrued for and against) deduction will be limited: net interest that exceeds 30% of adjusted taxable profits, will be restrictively deductible, when it exceeds $ 20,000,000 MxP annually and is deducted by the taxpayer or his group. The carryforward of the remainder of the interest not deducted in a given year, will be done in the following ten years, provided all requirements are met.

The provision is to apply beginning 2020 regardless of the types of debts consequent of the interest arising from previous years. Likewise, this rule will not be applicable for certain debts that finance public infrastructure work projects, real estate construction, and productive governmental enterprises.

II. Non-deductibility of certain cross-border related party payments

Those payments made to related parties abroad are deemed non-deductible when the recipient of the income is subject to a Preferential Tax Regime (PTR). Such limitation will apply even in cases where the recipient, in turn, forwards the payment to another entity of the group for whom the income is deemed subject to a PTR. Likewise, this limitation shall not apply when the income subject to a PTR derives from a business activity of the recipient, and such party holds personnel or employees and assets for the development of that business activity, except if the income is deemed subject to a Tax Haven Regime because of a hybrid mechanism. A hybrid mechanism will be deemed to exist when Mexican tax law and foreign law differ in the characterization of a legal entity, a legal vehicle, income or beneficial owner of income, resulting in the deductibility of a payment in Mexico and a non-taxable income abroad.

B.2. Special Treatment

There are different deductions which have a special treatment, in the following terms:

a. Cost of Sales

The deduction of the cost of sales comes when the merchandise is sold. The cost of manufacturing entities includes salaries of workforce and depreciation of fixed assets related with the production of goods.

b. Fixed Assets

Fixed assets are deductible under the depreciation scheme in accordance with the allowed rate. There are three criteria: i) intangible fixed assets, ii) tangible fixed assets, and iii) according to the activity in which the fixed assets are used. The depreciation rates currently range from 3% up to 100%; the upper depreciation rate applies to animals and vegetables, machinery used in the activity for the generation of energy from renewable sources, and adaptation of fixed assets for the benefit of people with disabilities.

In the first instance, royalties and technical assistance are treated as intangible fixed assets deductible annually at 15% on their amount, however, when the benefit of these concepts and their payment converge in

the same fiscal year, the taxpayer could deduct each concept as an expense.

C.1. Royalties, Technical Assistance and Interest Paid to Foreign Related Parties

The deduction of royalties applies as long as the payment has been done.

Furthermore, the beneficiary of the royalties and / or technical assistance must keep enough evidence to prove to the Tax Authorities that the supplier possesses the knowledge and technical elements to develop the service, and such service was directly rendered by the supplier (related party).

The LISR does not allow for the deduction of interest from debts contracted with related parties which exceed three times its net worth, as a rule the average which surpasses the limit will not be deductible. This rule is known as thin capitalization.

In addition, any payments for royalties, technical assistance, and interest are not deductible if:

- The Mexican resident entity controls its related party, or vice versa.
- The payment is made to entities located or resident in a low tax jurisdiction, and the price is not in accordance with the arm's length principle; or
- Payment is non-existent or it is exempt for income tax purposes in the supplier's jurisdiction.

C.2. Gain and Loss on the Sale of Capital Goods

Gains obtained from the sale of fixed assets, or shares, should be part of the ordinary taxable income of the year they are completed.

To determine the shares value, there are two procedures taking the period the shares were held by the partner into account (twelve months or more than this).

Regarding shares with a holding period of no more than twelve months, the cost of acquisition shall be increased by the inflation, but if the holding period were to be greater than twelve months, in addition to the inflation, the cost should be affected with the account of net taxable profit (CUFIN) and losses obtained, both prior to and after of the shares acquisition, as well as the capital redemptions performed into the holding period.

Losses on the sale of shares are only set off against gains of the same nature in the fiscal year of the sale or within next ten fiscal years, as regards losses from fixed assets, they form part of the deductions in the exercise that occurred.

D. Dividends

The companies resident in Mexico that receive dividends from a foreign resident must consider such an amount as taxable income, and the recipient has the right to credit the income tax paid at the source (withholding and the tax paid by the foreign company, if any) if certain conditions are met.

As per virtue of the tax reform of the fiscal year 2014, there is an obligation to keep two records of the account of net taxable profit, one of them should include the net tax profits generated prior 2014, and the other for those generated since that year. Dividends from net taxable profit up to 2013 are not subject to tax, however, there is a 10% withholding income tax if the dividends come from the net taxable profit of 2014 or later, and, if the receiver is an individual (regardless of his residence), or a company with a tax residence abroad.

Also, if the dividends or profit distributed by the legal entity do not come from the CUFIN, the company that distributes them will trigger the tax amount, for which it will compute the tax on a base adjusted by a factor, to which result the general rate of the income tax will be applied.

Consequently, if the recipient of the dividends or profits is a Mexican resident

legal entity, the dividend will not be a taxable income, but its amount will increase the CUFIN account balance.

Most of the tax treaties signed by Mexico contain a 5% withholding on the income tax at the source for dividends paid to members of the other contracting states; therefore, it is necessary to review each particular case taking the beneficial owner of the income into account.

5.3.4. CORPORATE TAX RATE, FISCAL YEAR AND DATE OF TAX PAYMENT

The corporate income tax rate applicable to a Mexican resident company is 30%.

The fiscal year coincides with the calendar year, except for start-up operations or liquidations, mergers or spin-offs, in which cases the fiscal year will be irregular, and will either start or end when the taxpayer files its notice to the tax authorities.

The income tax shall be paid through a tax return within three months following the close of the fiscal year.

Mexico uses the self-assessment system whereby all companies are required to file a tax return and compute their own liability. Legal entities must file the income tax return within the three months which follow to close of the fiscal year (in March).

5.3.5. TAX LOSS CARRYFORWARD

An operating tax loss incurred in a fiscal year may be decreased from the taxable profits of the 10 subsequent years until exhaustion without limit to the amount of tax losses that can be offset in a fiscal year, but if a taxpayer who was entitled to deduct in a fiscal year the tax losses of preceding fiscal years fails to do so, the right to deduct the amount thereof in subsequent fiscal years shall be forfeited. The amount of net losses is subject to inflationary adjustment based on the National Consumer Price Index (INPC).

In case of a merger, net losses are not transferable to the surviving company; but if such losses belong to said entity, losses will only be set off against profits deriving from the same type of activities that generate them.

On the other hand, in split-offs net losses accumulated by the original company may be divided in proportion to the inventories and accounts receivable if the companies are sharing the same line of business; otherwise, the net losses will be distributed in proportion to the fixed assets of the divided companies.

Should ownership and control of the company have changed, losses may be carried forward and set off only against profits from the same type of activities that generated the losses, provided the sum of the revenues derived during the last 3 fiscal years by that company is less than its losses accumulated by the end of the fiscal year where the change of ownership and control occurs.

LISR does not prevent rules regarding carry-back procedures.

5.3.6. TAXATION OF GROUPS OF COMPANIES

According to the tax reform of the 2014 fiscal year, the tax consolidation regime which allowed to defer tax payment for a 5-year period was abrogated. However, companies that obtained an authorization before that year could continue using the scheme for an additional 5 years from the date of granting of the permission.

A new regime for groups of companies was introduced in the LISR, under which corporate groups can defer part of their income tax for a maximum period of 3 years. This regime also considers the holding and subsidiaries companies; the requirements to act as holding company are: i) to be a tax resident in Mexico, ii) to be the owner of more than 80% of the voting shares of one or more entities, and iii) in no case may over 80% of its voting shares be directly or indirectly owned by one or more companies except if Mexico has signed a comprehensive agreement for the exchange of information. On the other hand, a subsidiary company qualifies if more than 80% of its voting shares are directly or indirectly owned by one holding company.

The deferred income tax is calculated applying a coefficient which is calculated from the consolidated pre-tax base divided by the sum of the pre-tax amount of each participating company. Deferred tax, plus inflation effect should be paid within 3 months following the close of the fiscal year.

The income tax must be paid before 3 years in merger and spin-off cases.

5.3.7. INCOME TAX FOR NONRESIDENTS

As a rule, the LISR imposes a withholding rate of 25% on the gross payment for the revenues with source of wealth in the country, but there are items with different withholding tax rates i.e. interest, prizes, insurance premiums, among others.

Mexico has in place over sixty double tax agreements where normally a preferential withholding rate is agreed, this measure helps to reduce the tax burden, provided that the both the taxpayer and the effective beneficial owner met certain tax requirements

5.3.8. PERMANENT ESTABLISHMENT (PE)

In Mexico, a PE is any place of business through which business activities or personal services are partially or wholly carried out: (i) branches; (ii) agencies; (iii) offices; (iv) factories; (v) workshops; (vi) installations; (vii) mines; (viii) quarries; and (ix) other places of exploration, extraction or exploitation of natural resources. However, this list is by no means exhaustive. It is important to note that unlike the PE provisions of the OECD Model, a place of business does not need to be fixed to constitute a PE.

As of 2020, a broader definition of PE is be provided under domestic law, which covers independent agents when acting mostly on an exclusive basis for a non-resident related party. A PE would also be deemed to exist in the case of dependent agents when carrying out activities that, in the aggregate, would not be considered to be of a preparatory or auxiliary nature.

For tax purposes, PE is considered as a separate entity under this legal figure, the resident abroad should only pay income tax from revenues accrued from a Mexican source of wealth. Its fiscal treatment is similar to the legal entities with the following features:

- A foreign company can have one or more permanent establishments.
- Additional taxable incomes:
    - Those derived from alienation in Mexico of merchandise or real property not belonging to the permanent establishment.

- Revenues obtained by the central office in the proportion that the PE participates of the disbursement to generate them.

- Deductions:
  - If there is a double taxation convention, the PE maydeduct pro rata expenses. (According with the domestic law)
  - The LISR does not allow for the deduction of remittances, royalties, personal services, commission fees, nor interest agreed upon with the company abroad.

5.3.9. DIGITAL ECONOMY

From 2020, a special tax regime for taxing the income obtained by Mexican resident individuals for goods sold or services rendered through all forms of digital platforms and applications is applicable to individuals, which shall be withheld by the domestic or foreign entities or figures that directly or indirectly grant the use of the digital platform, applications or similar platforms. For that purpose, a progressive withholding rate will be applicable (2% - 5.4%). However, if the individuals fail to provide their Federal Taxpayer ID (RFC), the withholding rate will be 20%.

The entities or figures that directly or indirectly grant use of the digital platform or application are also obliged to:

- Enroll in the Federal Taxpayers Registry;
- Issue digital invoices to the persons to whom they withhold taxes;
- Comply with certain reporting obligations;
- Remit the taxes withheld by filing a withholding tax return;
- Keep accounting records and;
- Comply with obligations imposed through general rules issued by tax authorities.

This regime will be effective as of June 1, 2020; likewise, authorities may issue applicable rules earlier.

5.4. INDIRECT TAXES

5.4.1. VALUE ADDED TAX

The Valued Added Tax (VAT) applies to transactions concerning transfer of goods made or services provided in Mexico by a taxable person, supplies of goods and services subject to the reverse charge, grants of temporary use or exploitation of goods and importations of goods from outside Mexico.

A taxable person is any business entity or individual, either resident of Mexico or a nonresident who makes taxable transactions in Mexico. A business entity or individual is liable to register for VAT, effective from its first taxable transaction. A nonresident without permanent establishment in Mexico must appoint a tax representative to register for VAT purposes.

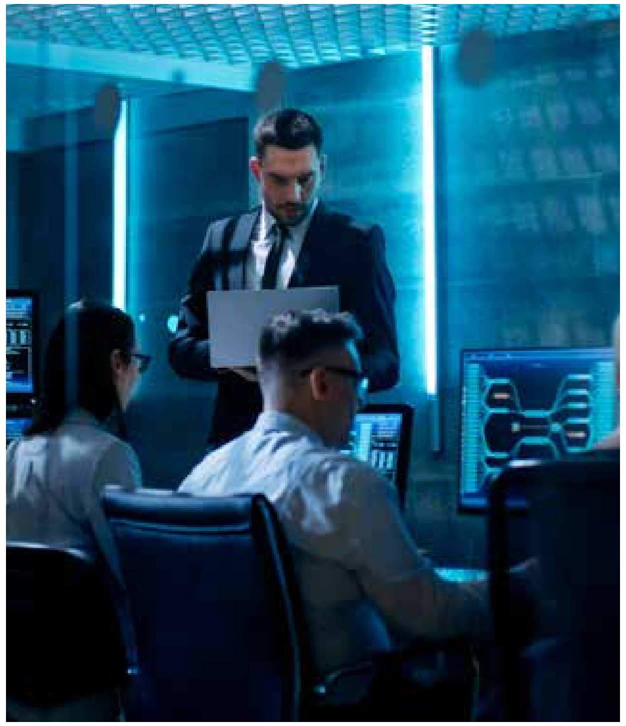
The VAT applies at the standard rate of 16%, unless a specific measure provides for the 0% rate (exported goods, certain exported services, unprocessed food and milk and patented medicines) or an exemption (supplies of goods and services that are not liable to tax. Exempt supplies do not give rise to a right of tax deduction input).

Effective 1 January 2015, all temporary imports made by companies who operate under the IMMEX program are subject to VAT at the standard rate. Previously, import VAT was not applied.

In addition, it is important to note, that from 2020, for VAT purposes, nonresidents without PE in Mexico will be subject to VAT on digital services rendered in Mexico.

In this case, the nonresidents shall comply with following requirements:

- Enroll in the Federal Taxpayers Registry;
- Include VAT on goods and services offered;
- Keep record of recipients of services located in Mexico and amounts collected from them;
- File a quarterly informative return;
- Pay VAT on digital services rendered in Mexico by filing a monthly VAT return;
- Issue digital invoices
- Appoint a legal representative and tax domicile in Mexico; and



- Obtain an electronic signature, among others.

Failure to comply with the foregoing liabilities may be sanctioned with fines.

Regarding VAT, digital services are deemed rendered in Mexico when the recipient of the service is located in Mexico. In this case, the recipient of a digital service is deemed located in Mexico when:

- It has declared to the service provider a domicile in Mexico;
- The consideration for the digital service is paid through an intermediary located in Mexico;
- When the IP address used by the electronic devices of the recipient of the service is located in Mexico; or
- When the recipient of the service has provided to the service provider a phone number whose country code corresponds to Mexico.

The taxable digital sevices are the following:

- Download or access to images, movies, text, information, video, audio, music, games (including gambling), other multimedia content, multiplayer environments, cellphone.ringtones, visualization of online news, traffic, whether or statistical information. The above will not be applicable to downloading or access to books, newspapers and electronic magazines;
- Intermediation between third parties that offer goods (except second hand movable goods) or services and the users demanding the same; Online clubs and dating sites; and
- Online teaching, tests and exercises.

These provisions are applicable as of June 1, 2020.

5.4.2. SPECIAL TAX ON PRODUCTION AND SERVICES (IEPS)

The Special Tax on Production and Services (IEPS as per its Spanish acronym) is an excise tax which is levied on sales, imports such as the following:

- Gasoline (variable percentage)
- 26.5 percent, 30 percent, and 53 percent: alcoholic beverages and services related with them (the rates depend on the percentage of alcohol and the type of beverage).
- 30.4 percent and 160 percent: tobacco/ cigarettes and related services tax (the rate depends on the tobacco product: 30.4 percent applies to hand- made products only).
- 6 percent, 7 percent and 9 percent: pesticides.

- -8 percent: food with a caloric density of 275 kilocalories (Kcal) or more per 100 grams.
- 30 percent: gambling and lotteries.
- 3 percent: rendering of telecommunications services through public networks, except for public and rural telephony and connection services between public networks and the internet.

Fees above, increase and are updated on annual basis, according to inflation.

A certification applies to this tax and is the same for VAT. In general terms, companies in good legal standing with their tax and customs obligations, may be able to obtain the certification on VAT and IEPS; likewise the certification is a benefit for the Maquila sector and aims to grant a 100% tax credit for VAT and IEPS on temporary imports that would start being paid as of January 1, 2015.

5.5. LOCAL TAXES

There are several types of local taxes that each member state of the Mexican Republic has established in its domestic legislation, however, the most common taxes are:

5.5.1. PROPERTY TAX

Whoever is the owner of the soil and/or the building constructed on it, is obligated to pay property tax on the ratable value

of the property or the appraised value, whichever is greater. The tax is calculated based on a table of increasing values.

5.5.2. TAX ON ACQUISITION OF REAL ESTATE

Any person (individual or entity) who acquires soil and / or the building constructed on it must pay the tax on acquisition of real state of from 0.5% to 4.9% on the ratable value of the property, market value, or the appraised value, whichever is greater; the rate of the tax depends of where the property is located.

5.5.3. PAYROLL TAX

The Individuals and legal entities that make payments of salaries are obligated to pay payroll tax in the State of the Mexican Republic they have located their workers, taxable base includes salaries and wages, overtime working, bonus, incentives, premiums, compensations, commissions, among others; the tax rate is of 0.5 % to 3% depending on the state in which the payment is made. In Mexico City the tax rate is 3%.

5.6. TAX TREATIES AND TAX EXCHANGE INFORMATION

5.6.1. TAX TREATIES TO AVOID DOUBLE TAXATION

In order to increase trade and investment, it is important to create tools or mechanisms which ensure that investors are not subject to discriminatory taxation in the jurisdictions in which they invest. In a broader sense, tax treaties facilitate trade and investment and can be used to strengthen bilateral relationships between countries.

Mexico is one of the member countries of the Organization for Economic Cooperation and Development (OECD), therefore most of its tax treaties have been negotiated according to the Model Convention of that organization. To this date, 59 of the tax treaties that Mexico has entered into are in force. Tax Treaties in force as of June 2019 are:

MEXICO TAX TREATY NETWORK

Australia	Denmark	Italy	Peru	Spain
Austria	Ecuador	Jamaica	Philippines	Sweden
Argentina	Estonia	Japan	Poland	Switzerland
Bahrain	Finland	Korea	Portugal	Turkey
Barbados	France	Kuwait	Qatar	Ukraine
Belgium	Germany	Latvia	Romania	United Arab Emirates
Brazil	Greece	Lithuania	Russia	United Kingdom
Canada	Hong Kong	Luxembourg	Singapore	United States
Chile	Hungary	Malta	Peru	Uruguay
China	Iceland	Netherlands	Philippines	
Colombia	India	New Zealand	Singapore	
Costa Rica	Ireland	Norway	Slovakia	
Czech Republic	Israel	Panama	South Africa	

Source: http://www.sat.gob.mx/informacion_fiscal/normatividad/Paginas/tratados_fiscales.aspx

Likewise, Mexico signed the Multilateral Convention to Implement Tax Treaty Related Measures to prevent Base Erosion and Profit Shifting (MLI) in June 7, 2017. MLI has not been approved yet by the Mexican Senate.

However, Mexico has already amended its domestic law in order to tackle certain BEPS practices. In addition, with the signature of the MLI, Mexico aligns with BEPS recommendations.

In order to eliminate potential barriers for investment, tax treaties aim to prevent tax evasion through reciprocal exchange of information provisions that apply to the tax administrations of the treaty partner countries, as well as specific treaty provisions that limit treaty benefits.

Thus, within some of the tax treaties concluded by Mexico, there are special provisions, such as limitation on benefits (LOB) and tax sparing credit provisions.

LOB provisions are included in treaties conclude with Barbados, China (People's Rep.), Colombia, India, Israel, Kuwait, Panama, South Africa, Ukraine, the United Arab Emirates and the United States, as well as other subject-to-tax and general anti-avoidance provisions, such as in the treaties with Bahrain, Brazil, Canada, the Czech Republic, Hungary, Lithuania, the Netherlands, Qatar, Russia, Singapore, the Slovak Republic and the United Kingdom.

On the other hand, regarding tax sparing credit provisions, it should be noted that the effect of tax exemptions granted by some countries to nonresident investors is not intended to be nullified by levies in the investor's country of residence. To that effect, some of Mexico's tax treaties contain provisions granting a fixed foreign tax credit on certain categories of foreign income, even if such income is exempt from foreign tax or subject only to a low level of taxation under the law of the source country.

For example, under the treaties concluded with Italy (15% dividends), Korea (Rep) (15% dividends), Singapore (15% dividends and royalties) and Spain (5% dividends), the treaty partners grant to their resident companies credits for taxes which would have been paid in Mexico if the tax had not been given up.

Finally, there are no specific provisions applicable to offshore activities in Mexico's treaties.

Furthermore, tax treaties prescribe different reduced rates of dividends, interest and royalties tax withholding, provided that taxpayers comply with specific requirements.

In the absence of a treaty, Mexico has certain unilateral relief provisions. Residents in Mexico and permanent establishments of

foreign residents have the right to credit income tax paid abroad. However, they must fulfill certain requirements, e.g. in relation to their attributable income, it has to be an income tax that has been effectively paid abroad by the taxpayer. The foreign tax will be creditable only up to an amount equal to the Mexican income tax that would be triggered by the same income obtained from a foreign wealth source according to the terms of the Income Tax Law.

It is important to point out that according to the domestic law, the benefits from the treaties to avoid double taxation shall only be applicable when, besides evidencing residence for tax purposes in the corresponding country and complying with the terms of the treaty, the nonresident fulfills all other rules of procedure set forth by the law, submitting the new informative return regarding its fiscal status and appoints a legal representative.

5.6.2. EXCHANGE INFORMATION TAX AGREEMENTS

Likewise, Mexico has executed specific exchange information tax agreements (see the chart below), and is in the process of negotiating others, to promote international cooperation in tax matters through the exchange of information and to

EXCHANGE INFORMATION TAX AGREEMENT			
Aruba	Bermuda	Gibraltar	Saint Lucia
Bahamas	Canada	Isle of Man	
Bailiwick of Guernsey	Cayman Island	Liechtenstein	United States
Bailiwick of Jersey	Cook Islands	Netherlands Antilles	
Belize	Costa Rica	Samoa	Qatar

Source: http://www.sat.gob.mx/informacion_fiscal/normatividad/Paginas/tratados_fiscales.aspx

achieve the standard of effective exchange of information for the purposes of the OECD's initiative on harmful tax practices, provided that the parties agree that the information will be treated as confidential and used only for tax purposes.

Furthermore, internal administrative rules provide that it shall be deemed that a country or jurisdiction has a broad exchange of information agreement with Mexico when the relevant country or jurisdiction subscribes to and gives effect to the Multilateral Convention on Mutual Administrative Assistance in Tax Matters, and when the said country or jurisdiction effectively exchanges information with Mexico (e.g. the British Virgin Islands and the Turks and Caicos Islands).

5.6.3. CONVENTION ON MUTUAL ADMINISTRATIVE ASSISTANCE IN TAX MATTERS

In May, 2010 with entry into force in September 2012 and applicable from January 2013, it was signed this agreement on administrative assistance with regards to taxes such as income tax (IT), value added tax (VAT) and the special tax on production and services (IEPS), which basically consists of:

- Audits upon request, simultaneous and abroad.
- Assistance in tax collection, including precautionary measures.
- Conservation and service of documents

The countries participating in this convention to December 31, 2018 are:

Albania	Colombia	Hong Kong	Mauritania	Samoa
Andorra	Cook Island	Hungary	Mauritius	San Marino
Anguilla	Costa Rica	Iceland	Mexico	Saudi Arabia
Argentina	Croatia	India	Moldova	Senegal
Aruba	Curacao	Indonesia	Monaco	Serbia
Australia	Cyprus	Ireland	Montserrat	Seychelles
Austria	Czech Republic	Isle of Man	Morocco	Singapore
Azerbaijan	Denmark	Israel	Nauru	Sint Maarten
Bahamas	Dominica	Italy	Netherlands	Slovak Republic
Bahrain	Dominican Republic	Jamaica	New Zealand	Slovenia
Belgium	Ecuador	Japan	Nigeria	South Africa
Belize	El Salvador	Jersey	Norway	Spain
Bermuda	Estonia	Kazakhstan	Pakistan	Sweden
Brazil	Faroe Islands	Kenya	Panama	Switzerland
British Virgin Islands	Finland	Korea	Paraguay	Tunisia
Brunei Darussalam	France	Kuwait	Peru	Turkey
Bulgaria	Gabon	Latvia	Philippines	Turks & Caicos Islands
Burkina Faso	Georgia	Lebanon	Poland	Uganda
Cameroon	Germany	Liberia	Portugal	Ukraine
Canada	Ghana	Liechtenstein	Qatar	United Arab Emirates
Cayman Isalnds	Gibraltar	Lithuania	Romania	United Kingdom
Chile	Greece	Luxembourg	Russia	United States
China (People's Republic Of)	Greenland	Macau	Saint Kitts and Nevis	Uruguay
	Guatemala	Malasia	Saint Lucia	Vanuatu
	Guernsey	Malta	Saint Vicent and The Grenadines	
		Mashall Islands		

Source: https://www.oecd.org/tax/exchange-of-tax-information/Status_of_convention.pdf

5.6.4. GLOBAL FORUM ON TRANSPARENCY AND EXCHANGE OF INFORMATION FOR TAX PURPOSES (GF)

The Global Forum (GF) monitors that its members fully implement the standards of transparency and exchange of information they have committed to implement. It also works to establish a level playing field, even among countries that have not joined the Global Forum. The GF has 154 members which are:

Albania
Andorra
Anguilla
Antigua and Barbuda
Argentina
Armenia
Aruba
Australia
Austria
Azerbaijan
Bahamas
Bahrain
Barbados
Belgium
Belize
Benin
Bermuda
Bosnia and Herzegovina
Bostwana
Brazil
British Virgin Islands
Brunei Darussalam
Bulgaria
Burkina Faso
Cabo Verde
Cambodia
Cameroon
Canada
Cayman Islands
Chad
Chile
China (People's Republic Of)
Colombia
Cook Island
Costa Rica
Croatia
Curacao
Cyprus
Czech Republic
Denmark
Djibout
Dominica
Dominican Republic
Ecuador
Egypt
El Salvador
Estonia
Eswatini
Faroe Islands
Finland
France
Gabon
Georgia
Germany
Ghana
Gibraltar
Greece
Greenland
Grenada
Guatemala
Guernsey
Guyana
Haiti
Hong Kong
Hungary
Iceland
India
Indonesia
Ireland
Isle of Man
Israel
Italy
Jamaica
Japan
Jersey
Kazakhstan
Kenya
King of Lesotho
Korea
Kuwait
Latvia
Lebanon
Liberia
Liechtenstein
Lithuania
Luxembourg
Macau
Malasia
Maldivas
Malta
Mashall Islands
Mauritania
Mauritius
Mexico
Moldova
Monaco
Mongolia
Montenegro
Montserrat
Morocco
Nauru
Netherlands
New Zealand
Nigeria
Niue
North Macedonia
Norway
Oman
Pakistan
Panama
Papua New Guinea
Paraguay
Peru
Philippines
Poland
Portugal
Qatar
Romania
Russia
Rwanda
Saint Kitts and Nevis
Saint Lucia
Saint Vicent and The Grenadines
Samoa
San Marino
Saudi Arabia
Senegal
Serbia
Seychelles
Singapore
Sint Maarten
Slovak Republic
Slovenia
South Africa
Spain
Sweden
Switzerland
Tanzania
Thailand
Togo
Trinidad y Tobago
Tunisia
Turkey
Turks & Caicos Islands
Uganda
Ukraine
United Arab Emirates
United Kingdom
United States
Uruguay
Vanuatu
The European Union fully participates in Global Forum work

Source: http://www.oecd.org/tax/transparency/about-the-global-forum/members/

5.7. ANTI-AVOIDANCE RULES

Tax legislation contains specific anti-avoidance rules. Among the most relevant are:

5.7.1. GENERAL ANTI-ABUSE REGULATION (GAAR)

From 2020, fiscal authorities may consider as nonexistent transaction for tax purposes, those legal acts that lack a business reason and that lead to obtaining tax benefits. In this regard, it is considered that there is not business reason when the quantifiable economic benefit (present or future) is less than the tax benefit, as well as, if the economic benefit could have been obtained through fewer transactions. In that sense, any reduction, elimination or temporary deferral of a contribution shall be understood as a tax benefit.

For this purpose, when the tax authorities exercise their powers of fiscal verification, they will be entitled to review the business reason to also determine whether the operation exists or not. However, taxpayers will have the right to distort the observations made in this regard by the tax authority.

Unless the taxpayer proves otherwise, tax authority shall conclude that a transaction does not have a business reason and be entitled to re-characterize corresponding

transaction, attributing it the tax effects that would have been produced to obtain an economic benefit reasonably expected.

5.7.2. MANDATORY DISCLOSURE AND JOINT LIABILITY

As of January 1, 2021, taxpayers and their tax advisors will be obliged to disclose to tax authorities' certain reportable schemes that are deemed as a risk scheme. Reportable transactions would be activities that generate (or may generate), directly or indirectly, a tax benefit in Mexico.

Tax advisors are mainly obligated to disclose any reportable scheme in case they participate in its design, commercialization, organization, implementation, or management. However, taxpayers will be obliged to disclose a reportable scheme too, if the scheme is designed, organized, managed, or implemented by themselves. Likewise, taxpayers will also be obliged to report the scheme when;

- The tax advisor does not provide them with a report number or with a certificate stating that the scheme is not reportable;
- The scheme is designed, commercialized, organized, implemented or managed by a person that is not considered to be a tax advisor;
- The tax advisor is a non-Mexican resident, or the tax advisor has a legal impediment to disclose the scheme; and
- When the taxpayer and its tax advisor have agreed that the taxpayer will be responsible to report the scheme.

There is a broad list of activities that are considered to be "reportable transactions," that basically reference the use of tax losses, changes in ownership, reorganizations, capital reductions, application of benefits under a tax treaty, transfer pricing considerations, etc.

Failure to comply with obligations related to reportable schemes may result in the imposition of fines, from MXN $50,000 to MXN $20,000,000, depending on the specific situation. In addition, taxpayers will be sanctioned with the range from 50% to 70% of the tax benefit achieved of the reportable scheme.

In terms of joint liability, there are proposed rules that expand the scope of joint liability for tax related matters, including managers and officers of Mexican taxpayers.

The case to release liquidators and trustees from joint liability derived from omitted taxes during the period they held such position were eliminated.

On the other hand, joint and several liability for partners, shareholders and associates will be related to the activities performed by the company during the period they held such position and only for the portion that is not guaranteed by the taxpayer, without exceeding their participation in the company´s equity and in the following cases:

- The company is not registered in the Federal Tax Registry;
- Not filing the tax domicile modification notice or vacating the facilities (tax domicile) without filing the proper notice or being considered as not reachable;
- Not having accounting records, hiding them or destroying them;
- Failing to pay withheld contributions;
- Company that bills simulated operations or transactions (EFOS);
- Company that applies deductions of simulated operations (EDOS) that within a tax year received invoices issued by one or various EFOS for an amount higher than USD$390,211;
- Taxpayers that did not prove against the legal assumption for illegal transfer of tax losses.

Finally, the several and joint liability of managing directors, general managers and sole administrators, will be applicable for the contributions triggered, not paid and/or withheld during the time they held such position, for the portion of the tax assessment that is not guaranteed by the taxpayer.

5.7.3. FISCAL CRIMES

According to criminal tax reform, the purchase or acquisition of CFDIs that support nonexistent or false transactions or simulated legal acts will be deemed as a criminal offense.

Likewise, criminal laws were amended to be consider as organized crime when the organization of three or more people carry out any conduct or conducts that have as consequence or purpose any of the following felonies:

- Smuggling and similar acts
- Tax fraud and comparable crimes; and/or
- The issuance, transfer, purchase or acquisition of tax invoices supporting non-existent or false transactions or simulated legal acts, provided the value of the invoices exceeds the amount of MXN $7.8 million.

Finally, the mentioned felonies will be deemed as threat to the national security, as well as aggravated crimes punishable with mandatory imprisonment without possibility of parole.

5.7.4. TRANSFER PRICING

Payments to domestic and foreign related parties would be agreed likewise between independent parties in comparable transactions and properly documented for them to be deducted.

According to the above, two entities are deemed to be related parties where one participates directly or indirectly in the administration, control or capital of the other, or where another person or group of persons participate directly or indirectly in the administration, control or capital of two or more other parties. Partners of an informal association, as well as the head office of a permanent establishment and other permanent establishments, are considered to be related parties. Transactions between Mexican residents and companies or entities subject to preferential tax regimes are deemed to be between related parties.

On the other hand, transactions (or enterprises) are comparable if there is no difference between them that could have a significant influence on the price or the profit margin.

The tax authorities are empowered to verify that transactions with related parties have been executed in accordance with the arm's length principle, making any necessary adjustments: unpaid taxes; restatements for inflation; interest; and fines that may range between 55% and 75% of the unpaid tax (subject to reduction where documentary requirements are met).

Mexico's transfer pricing rules generally follow the OECD transfer pricing guidelines. A transfer pricing study must be supported on the arm's length principle per fiscal year.

Likewise, tax authorities may resolve requests by taxpayers regarding the methods to be used to determine transfer prices at arm's length, provided that taxpayers meet all corresponding requirements. This agreement may be bilateral if agreed with the competent tax authorities of a tax treaty country. An advance pricing agreement (APA) may apply for up to 3 tax years following that in which it was issued, for the tax year in which it was issued, and up to 1 tax year prior to that in which it was issued (5 years in total). A longer period may be granted through a mutual agreement procedure under the terms of a tax treaty.

Finally, it is important to point out, that according to the OECD's BEPS Action Plan (Action Plan 13: Guidance on the Implementation of Transfer Pricing Documentation and Country-by-Country Reporting), as of the year 2016 the domestic legislation was amended in order to request to taxpayers who earned income equal to or greater than MXN $708,898,920.00 (this amount has not been updated or changed since the provision is in force) in the previous tax year, companies taxed under the consolidation tax regime, companies that carry out transactions with foreign companies and foreign entities with a permanent establishment in Mexico, filed annually (due by December 31, 2017) in connection with each preceding year a Local File and a Master File regarding their operations with related parties. Likewise, companies earning at least MXN $12 billion annually are also required to file a country-by-country report. The reporting must be filed electronically. Failure to file the report is subject to fines and disqualification of the taxpayer from entering into contract with the Mexican public sector.

These reports provide to the tax authorities visibility into profits, revenues, taxes paid and caused, employees, capital, retained earnings, tangible assets and business activities, as well as it helps them to identify and assess the risks of managing transfer prices

5.7.5. CONTROLLED FOREIGN COMPANIES (CFC)

Companies and individuals resident in Mexico, as well as nonresidents with an

permanent establishment in Mexico, are subject to income tax on income subject to a preferential tax regime (income are deemed to be subject to a preferential tax regime if the paid tax abroad on said income is lower than 75% of the income tax that would have been incurred and paid in Mexico if the income had been generated there) obtained through foreign companies or vehicles in which they participate directly or indirectly; also on the income obtained through companies or vehicles that are considered physically transparent abroad. Likewise, all income obtained through a physically transparent foreign company or vehicle must be subject to taxes in accordance with CFC rules, without exception.

Therefore, CFC rules apply when profits generated through foreign companies or vehicles are subject to an effective income tax rate of less than 75% of Mexico's income tax rate (i.e., 22.5%) in the country of fiscal residence. However, there are some exceptions to the application of CFC rules.

CFC rules shall not apply, among other hypothesis, where the earned income is by business / commercial activities; except when the passive income (interest, dividends, royalties, capital gains from the transfer of shares or intangibles, commissions and mediation fees) represent more than 20% of the total income of the company or the vehicle.

Likewise, CFC rules do not apply to income generated through foreign companies or vehicles where average daily shareholder ownership does not allow the taxpayer to exercise effective control over the investments made by the foreign company or vehicle, its administration or dividend payment policy.

Passive income derived directly or indirectly by a Mexican resident through a branch, entity or any other legal entity located in a preferential tax regime will be subject to taxation in Mexico in the year in which the income is derived.

According to CFC rules, companies must separately accrue income recognized in advance. However, a foreign tax credit is granted on the income tax paid abroad on the income recognized in advance. Companies shall apply general foreign tax credit rules calculating a separate foreign tax credit limitation on the overall income recognized in advance, in order to increase the foreign tax credit limitation by averaging low and high tax rates.

Furthermore, under some requirements, CFC rules grant a foreign tax credit on income tax withheld in Mexico from Mexican source payments made to the foreign company or vehicle.

There are no rules provided for relief from double taxation on actual distributions of dividends by the CFC to its shareholders.

In order to avoid tax simulation, tax authorities are entitled to determine the tax effects of operations whose aim is to benefit from a tax treatment that otherwise would not have been obtained

In addition, taxpayers earning income from a preferential tax regime must file an annual informative return in February of each year, as well as those who conduct transactions through fiscally transparent foreign legal vehicles or entities.

Payments to a CFC generally are subject to a 40% withholding tax. Regarding disregarded entities, as of 2020, the provisions on income subject to preferential tax regimes (REFIPRES) are restructured; those taxed abroad at a rate of less than 22.5%, to be applicable exclusively to Foreign Entities, which are legal entities with legal personality, resident in the country or jurisdiction of reference.

The rules of early accumulation are applicable for residents of Mexico who hold their direct or indirect

participation and have control over them. Likewise, the exception rules that allow the deferral in triggering the tax until such time as the reference income is distributed, is extended to the rules of the control assumptions of the entities. It is established that fiscal transparency will be respected in those cases that are foreseen by the double taxation agreements.

5.7.6. INVESTMENTS IN FOREIGN ENTITIES AND FOREIGN LEGAL FIGURES CONSIDERED AS REFIPRES

As of 2020, a special regime to tax in Mexico to Foreign Entities (with their own legal personality) and Foreign Legal Figures (without their own legal personality) that are considered as transparent for tax purposes in their country of incorporation or residence, independently and general, regarding the current REFIPRES regime; provided that these vehicles will be subject to lien in Mexico as a legal entity resident abroad or in Mexico and according to the type of income they receive.

Under this new scheme, the obligation for residents of Mexico (natural person or legal entity) to accumulate in the year in which the net income or profits received by Foreign Entities and Legal Figures that are considered transparent in their country is established of constitution or residence, directly or indirectly, depending on the proportional participation they have in said vehicles; which implies de facto the early recognition of this type of income for tax purposes.

5.7.7. THIN CAPITALIZATION

Interest arising from excess debt from a related party is nondeductible for income tax purposes if the amount of debt exceeds three times the shareholders' equity (i.e. a 3-to-1 debt to equity ratio applies). The thin cap rules shall not be applicable to taxpayers that obtain a favorable APA (Advanced Price Agreement) from the Tax Authorities, provided that they meet with certain administrative conditions, such as agreeing that transactions are carried out at market prices, and with financial institutions.

Likewise, thin capitalization regime does not apply to taxpayers of the financial system with respect to loans contracted in their regular financial activities.

Since 2016, thin capitalization rules are not regulated with respect to debts incurred in relation to investments in infrastructure for the generation of electricity.

In addition to the above, regarding 2020 thin capitalization rules, interest expense deductions will be limited in excess of 30% of net adjusted taxable profits. This is a new concept and is similar to the financial definition of Earnings before interest, tax, depreciation and amortization (EBITDA). Any excess interest which does not meet the deductibility requirements will be allowed to be carried forward up to 3 years. Some exceptions to this limitation will be applicable for infrastructure and energy related projects. However, financial institutions and insurance companies would be covered under the proposed rules.

5.7.8. JURIDICAL DOUBLE TAXATION

Tax authorities may request nonresidents to prove the existence of juridical double taxation in order to claim tax treaty benefits, in the case of transactions between related parties, except when a nonresident resides in a country with a territorial taxation system or is not subject to tax in its country of residence under the application of a tax treaty entered into by Mexico with that country.

Likewise, the existence of juridical double taxation shall not be required in the case of transfer of shares performed in accordance with the corporate restructuring rules contained in a tax treaty, and dividends which are paid to a nonresident who is the beneficial owner of such dividends and is exempt from tax in its residence jurisdiction by the application of an exemption method contained in a tax treaty.

5.8. TAX INCENTIVES

5.8.1 NORTHERN BORDER TAX INCENTIVE

In force from January 1, 2019 and ends December 31, 2020.

In order to strengthen the economy of the taxpayers who inhabit the Mexican northern border, in addition to stimulating investment, promoting productivity and contributing to the creation of employment sources, tax incentives of income tax and VAT have been established to apply in the mentioned border, a reduced rate of these taxes.

The border region where applying fiscal incentives, includes the municipalities of Ensenada, Playas de Rosarito, Tijuana, Tecate and Mexicali of the state of Baja California; San Luis Río Colorado, Puerto Peñasco, General Plutarco Elías Calles, Caborca, Altar, Sáric, Nogales, Santa Cruz, Cananea, Naco and Agua Prieta of the State of Sonora; Janos, Ascensión, Juárez, Praxedis G. Guerrero, Guadalupe, Coyame del Sotol, Ojinaga and Manuel Benavides of the state of Chihuahua; Ocampo, Acuña, Zaragoza, Jiménez, Piedras Negras, Nava, Guerrero and Hidalgo of the state of Coahuila de Zaragoza; Anahuac of the state of Nuevo León; and Nuevo Laredo, Guerrero, Mier, Miguel Alemán, Camargo, Gustavo Diaz Ordaz, Reynosa, Rio Bravo,

Valle Hermoso and Matamoros of the state of Tamaulipas.

A. Income Tax

This tax incentive is applicable to individuals with business activities and legal entities of the general corporate taxation regime, as well as to residents abroad with a permanent establishment in Mexico and those who are Mexican residents taxed according to the option of accumulation of income, which receive income from business activities exclusively in the northern border region (earned income represent at least 90% of the total of the taxpayer's income in the immediately preceding fiscal year).

Taxpayers who comply with the corresponding requirements may apply a tax credit equivalent to one third of the ISR caused in the year or in the provisional payments, against the ISR caused in the same fiscal year or in the provisional payments of the same fiscal year, as applicable, in the proportion represented by the total income generated in the region, from the total income of the taxpayer obtained in the fiscal year or in the period corresponding to the provisional payments.

Incentive shall not be applicable to credit, insurance and surety institutions, general deposit warehouses, financial leasing and credit unions; companies that pay in the Optional Regime for groups of companies; coordinated entities; the taxpayers who pay taxes in the Regime of agricultural, livestock, forestry and fishing activities; the taxpayers of the Fiscal Incorporation Regime; trusts dedicated to the acquisition or construction of real estate; cooperative production entities; taxpayers who issue apocryphal invoices or are not located, whose operations are deemed as nonexistent; the taxpayers who carry out business activities through trusts; taxpayers who obtain their income from intangible assets; taxpayers whose income derives from the digital economy; taxpayers who render outsourcing services or supply personnel through labor subcontracting; taxpayers who have been verified by tax authorities and have had taxes deficiency assessment in charge, without having corrected their tax status; taxpayers who apply other fiscal treatments that grant fiscal benefits or tax incentives; taxpayers who are in liquidation exercise at the moment of requesting the authorization to apply the fiscal stimulus; the companies whose partners or shareholders, individually, lost the authorization to apply the tax incentives and the State's productive enterprises, including their respective subsidiary productive companies.

B. VAT

This incentive is applicable to individuals and entities who perform the acts or activities of alienation of goods, rendering of independent services or granting the temporary use or enjoyment of goods, in establishments located within the earlier described Mexican northern border region.

It consists of a credit equivalent to 50% of the VAT rate. For administrative simplification, the tax credit will be applied directly to the mentioned rate. The reduced rate that results from applying the tax incentive shall be applied to the value of the acts or activities according to VATL's provisions.

The benefits of the VAT incentive shall not be applicable when alienation of real estate and intangible assets; the supply of digital content, such as audio or video or of a combination of the previous ones, by means of the discharge or temporary reception of the electronic files, and to taxpayers who are not located, who have a taxes deficiency assessment in charge, who have been convicted of a fiscal crime or offense, and who have a taxes deficiency which had been foregone.

5.8.2. SPECIAL ECONOMIC ZONES (ZEE)

The ZEE were introduced by the Mexican government via decrees in the later part of 2017 and are in force from 30 September 2017, in order to promote economic growth and investment in certain states of the country that have fallen behind with respect to others parts of Mexico in industrial and economic development, through granting tax incentives to ZEE which projects should be aimed at encouraging the creation of jobs and infrastructure to promote the economic development of the region.

Assigned Integral Administrators (Mexican private or parastatal Entities assigned to operate the ZEE) or authorized Investors (Mexican or foreign individuals or entities with permanent establishment (EP) dedicated to: manufacturing, agroindustry, processing, transformation and storage raw materials, scientific development and technological, support services such as logistics, financial, computer, professional or technical, among others) that are interested in operating in the ZEE may obtain the corresponding authorization, which will be valid or in force for 5 years. However, they will not be able to carry out activities consisting of oil refining and natural gas processing, storage, transportation, distribution and marketing of hydrocarbons and oil, as well as other specific activities according to applicable guidelines for each ZEE.

On the other hand, those who operate in the ZEE may receive tax, customs and financial benefits, as well as administrative facilities and competitive infrastructure, among other special conditions.

Such tax incentives for the ZEE include income tax and VAT as follow:

Income Tax:

Taxpayers obtaining income generated within the ZEE will be granted an income tax reduction of 100% during the first 10 fiscal years and a 50% income tax reduction for the following 5 fiscal years, subject to the compliance of certain requirements, as well as, among others, deductions in the sale of fixed assets and training expenses, credits in social security contributions.

VAT:

0% VAT rate will be applicable to goods acquired by investors in the ZEE as long as certain documentation requirements are satisfied. Furthermore, investors in the ZEE may be able to obtain accelerated VAT refunds for goods acquired by Mexican residents located outside the ZEE. In addition, Mexican residents outside the ZEE may apply a 0% VAT rate to services or the leasing of goods provided to investors in the ZEE, subject to the compliance of certain requirements. Likewise, no VAT is applicable to transaction among taxpayers within the ZEE.

It is important to point out that additional tax incentives may be available at a state level, agreeing with the local tax authorities on a case-by-case basis and depend on the nature of each specific investment project.

5.8.3. MANUFACTURING, MAQUILA AND EXPORT SERVICES INDUSTRY (IMMEX PROGRAM)

The Mexican Federal Government published the Decree for the Promotion of the Manufacturing, Maquila and Export Services Industry (herein and after known as IMMEX Decree), which merges the Export Decree and The Temporary Import Programs to Produce Goods for Export (PITEX).

IMMEX was created as a program which main purpose is to increase the activity of the Mexican export sector with an approach of legal certainty and transparency, reducing logistics and administrative costs through the consolidation of the benefits, which facilitates interaction with government authorities to operate under such program.

The IMMEX program allows the temporary import of goods that are used in an industrial or service process intended to produce, transform or repair foreign goods (including auto parts industry) imported temporarily for its subsequent export or the provision of export services, without covering the payment of the general tax for import, the value added tax and, where appropriate, the countervailing duties. In other words, IMMEX program, allows foreign manufacturers to import raw materials and components into Mexico, under the condition that 100% of all finished goods will be exported out of Mexico within a government mandated timeframe.

It is important to consider that in order to apply the maquilas regimen it is mandatory to meet, amongst others, the following requirements:

- The total of its income for its productive activity, must come exclusively from maquila operations.
- Processes of transformation or repair, are carried out with machinery and equipment owned by the resident abroad with which company with IMMEX (maquila) program have held maquila agreement, provided that they are not owned by the company that performs the maquila operation or another Mexican resident company that is related party.

The company which applies for IMMEX Program, can operate with the following sub-programs:

1. IMMEX Holding Companies Program: the manufacturing operations of a certified holding company and on or more subsidiaries are included in the same program;
2. IMMEX Industrial Program: goods are manufactured or transformed for subsequent export through an industrial process;
3. IMMEX Services Program: export goods are serviced, or export services are provided, solely to develop those activities established by the Ministry of Economy (SE), following review by the Ministry of Finance and Public Credit (SHCP);
4. IMMEX Shelter Program: one or more foreign companies provide the technology and the production material, without having any direct involvement in the Program, and;

5. IMMEX Outsourcing Program: a certified company lacks the facilities to perform production processes itself and performs the manufacturing operations through a third party who registers in this Program.

The Ministry of Economy is the authority in charge of authorizing the maquila or IMMEX program. In order for the company to qualify and obtain such authorization, the company must submit certain documentation and provide detailed information about the manufacturing process or service operation to be carried out.

The authorization of the Program will be granted under the commitment to have annual sales abroad of at least USD 500,000 or an equivalent amount in Mexican pesos, or invoice exports accounting for at least 10% of its total invoices.

An annual electronic report of the total sales and exports for the immediately preceding fiscal year, no later than the last business day of May, according to the form announced by the Ministry of Economy through the General Rules and Criteria on Foreign Trade, is required. If the mentioned report is not submitted, the program will be suspended, which will impede the continuity of the operations temporarily, to resume its IMMEX program. It should be noted that the Ministry of

Economy will notify the suspension in a period of 10 days.

Other general requirements are to fulfill the provisions of annex 24 of the General Rules and Criteria on Foreign Trade; in that context a specific software must be acquired in order to implement a stock control.

In addition, it is important to note that maquiladora companies may secure a special enrollment from Mexican customs authorities to operate as a Certified Company, which grants access to certain benefits that allow companies to save costs and time by being able to enjoy easier and more expedited customs clearance processes, reduction in documentation

requirements, as well as certain tax and customs advantages related to the virtual exportation and importation of goods. According to the Certified Company category under which each company is authorized, it will be granted the corresponding benefits.

Since 2016, it is in force a certified company's framework, which includes different certification modalities in accordance with the operations and level of compliance with the requirements of the companies. In this sense, certified company modalities are: VAT and IEPS; Trader and importer; Authorized Economic Operator (with the modalities of Importer and / or exporter, controller, aircrafts, SECIIT, textile and strategic bonded warehouse), Certified Commercial Partner (which includes terrestrial carrier, or customs broker, railway transport, industrial park, bonded warehouse and courier companies).

Likewise, such framework integrates the certified companies' registry, the VAT / IEPS certification, authorized economic operator (AEO), and a guarantee of interest payment and the reliable importer program (revisión en origen).

A. Immex Benefits

IMMEX companies are subject to Mexican taxes, including Income Tax (ISR) and VAT; however, they could be subjected to some tax benefits such as the following:

- The main benefit of IMMEX is to defer taxes on goods that are temporarily imported into Mexico and the ability to consolidate import tax returns;
- Avoid payment of compensatory quotas which are duties applied to products protected by Mexico's government.
- Reduction in Customs fees (Derecho de Trámite Aduanero, DTA)
- Raw materials, components and parts, associated products, and packing materials, as well as fuel and lubricants used in the production process. These goods may not remain in Mexico for more than 18 months.

- Containers and trailers. Cargo containers and trailer trucks may not remain in Mexico for more than 2 years.
- Possible deferral of the general import duty, and in some cases exemption thereof;
- Avoiding VAT: Until 2013 one of the major benefits of the IMMEX Program was to avoid the VAT applied on imports, notwithstanding the restatement carried out, it implies that now a 16% VAT shall be paid on imports. However, it could be avoided by obtaining certification from the Mexican tax authorities, which in turn is subject to several requirements.

B. Special Advantageous Tax Regime for IMMEX

Once such program is authorized, companies avoid permanent establishment (PE) risks as long as they comply with transfer pricing legislation and are deemed to the foreign principal conducting operations in Mexico through the enterprise with the mentioned program. Meanwhile, such foreign principal be resident in a country which Mexico has a double tax treaty in force.

Also, companies must comply with the transfer pricing legislation determining on arm's length level of profitability and declare a "safe harbor" that consists in

general of reporting a taxable income of at least the higher of the following values:

1. 6.9% of those assets used in the activity (inventories and fixed assets owned by the foreign related party are included),
2. 6.5% of total operating costs and expenses of the IMMEX Maquiladora.

Return of operative assets, including the net book value of machinery and equipment owned by the foreign principal, adjusting it to recognize that the financial activities (and associated risks) for the procurement of such machinery and equipment are not carried out by the Maquiladora.

Likewise, it is important to note that from 2020 regarding to "shelter maquiladora", existing limitations of operating through a "shelter" (up to 2021) would be eliminated and nonresidents would continue to be exempt from having a Mexican PE to the extent that the maquila formal requirements are met.

Regarding the tax amendment which took place in January 2014, the Government published the Resolution of Modifications to the General Rules, Mexican Income Tax Law (LISR as per its Spanish acronym) and Valued Added Tax Law (LIVA as per its Spanish acronym), which contains a modification regarding the following themes:

- Value Added Tax (VAT): Payment of the tax at the time of importation for temporary imports. This rule implies obtaining a certification in order to avoid VAT effects on temporary imports.
- Income Tax (IT): A new definition of the "Maquila Process" was amended in the Mexican Income Tax Law, the essence thereof consisted in, according to the IMMEX Decree definition, to obtain the Income tax benefits described above, the company with the IMMEX Program must nevertheless comply with:
- Concept limits: This was inserted to limit the export of manufacturing services and to restrict the ability of a maquiladora to sell or distribute the products

manufactured that it supposed to return as exportation directly in Mexico.

- Permanent establishment rule: To avoid a PE exposure, income from the IMMEX Program must be derived exclusively from the export activities concerning to the manufacturing process services.
- Miscellaneous rules: Once the income scope has been clarified as to be derived exclusively from the export of maquila services when it is derived from the rendering of maquila services (or activities related to such services) to foreign related parties.
- Foreign resident rule: Goods provided by the foreign principal to enact the manufacturing process under Manufacturing Agreement, must be temporarily imported and returned abroad, or transferred by virtual operations.
- Raw materials rule: The manufacturer must use in his process such materials owned by third foreign parties with whom he enjoys a commercial relationship, nevertheless, if he were to include goods that have been imported on a definitive basis, these goods shall be exported or returned abroad together with the temporarily imported goods.
- Foreign fixed assets rule: 30% of fixed assets used in the process of transformation must be owned by the foreign principal and temporarily imported. Such fixed assets cannot be owned previously by the Maquila Company or a Mexican related company. The IMMEX Company may also process products with fixed assets owned by a third foreign entity with who he enjoys a commercial relationship, with the foreign principal with who the holder of the Program has executed a Manufacturing Agreement, or with its own fixed assets or those leased with non-related parties.

C. Mexican Automotive Industry

The Mexican industry of manufacturing has increased continuously, the Automotive Industry, not exempt and to be considered as the most sophisticated process and manufacturing sector with more than 2.4 million vehicles shipped in the last year.

The maquila process in the automotive industry is perhaps the most dynamic industry in the process services sector, compounding the suppliers which are companies engaged to provide services to manufacture car parts involved in the process of vehicle construction. These suppliers can both carry out local commerce and export finished goods, mainly to the United States (U.S.) and abroad under Mexico's IMMEX program, taking full advantage of the taxation, fiscal and other incentives offered to them.

A significant information is that almost 80% of the value of Mexican exports including vehicles and car parts went to the U.S. The rest of the exports were divided among over 100 countries. Mexico is the main supplier of auto parts to the U.S.[1]

A. Automotive Decree

The Decree was published December 11, 1989 and its main objective is to place productive investments in national territory, provided that they include:

- Expansion or construction of facilities.
- Training and job generation.
- Investment in R&D from businesses in the sector.

The decree has been the main cause of the largest investment in our country, many companies such as Volkswagen, Fiat / Chrysler, Pirelli, Porsche and others have carried out millionaire investments to develop the vehicle business sector as well as doing business with third party suppliers in order to acquire the necessary goods to complete their production process chains.

B. Other Benefits:

The inclusion of manufacturing companies under the Customs and Manufacturing Law

[1]Source http://embamex.sre.gob.mx

under the Sectorial Promotion Program (PROSEC) for the automotive and car parts industry to import their materials with preferential tax arrangements or exemptions with the objective of maintaining their competitiveness.

Also with the IMMEX Program the procedures and requirements for companies which have a structured business plan, allows for the import of goods and services used in industrial processes for the development, transformation (modification) or repair of merchandise imported from abroad.

5.8.4. REAL ESTATE INVESTMENT TRUST (FIBRAS)

There is also a benefit for Real Estate Trusts engaged in the acquisition or construction of buildings allocated for lease or purchase of the right to receive income from the lease of such property.

The property cannot be alienated within 4 years from the termination of the construction or acquisition in order to defer the payment of income tax until the sale of participation certificates.

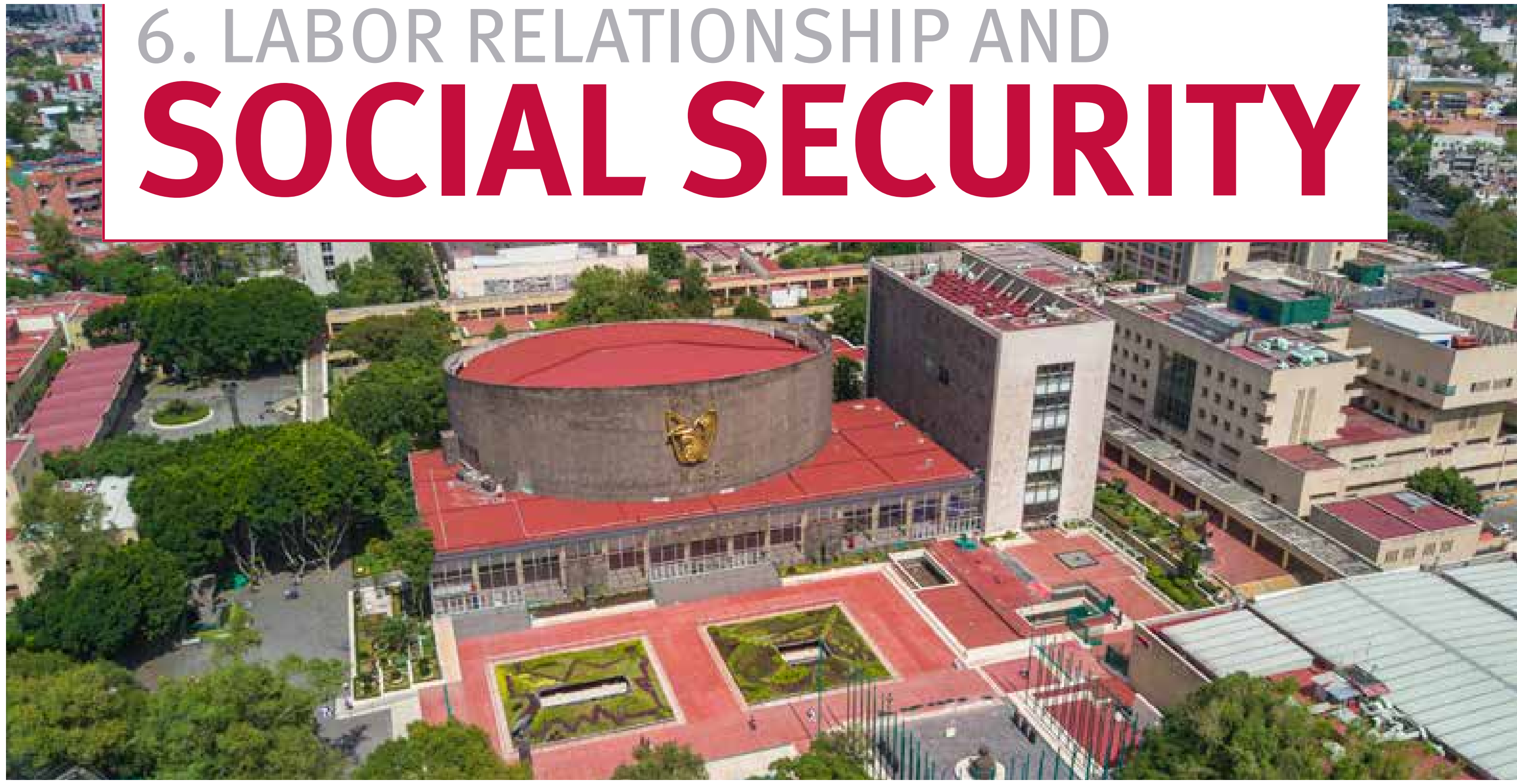
As of 2020, the assumption that certifies the participation of the assets that integrate the trust assets can be acquired by the private, will be deleted, leaving only the possibility of creating public FIBRAS. According to the latest tax reform, persons who hold the mentioned certificates will have until December 31, 2021, to pay the deferred tax, provided that such certificates have not been alienated.

5.8.5. ENERGY SECTOR

According to the 2016 tax reform, in order to optimize the industry, the 10-year limitation was removed for investment in risk capital trusts in the energy sector.

An investment account in renewable energy is created in order to enhance the deduction of 100% of fixed assets allocated to this activity.

6. LABOR RELATIONSHIP AND SOCIAL SECURITY



Labor issues in Mexico are governed by the Federal Labor Law (LFT as per Spanish acronym) and the Social Security Law (LSS as per its Spanish acronym), which set forth the rules for labor relations, labor unions and labor courts, according to the social and economic rights for workers provided by Mexico's constitution of 1917.

As we will comment later, recently, the Mexican government implemented some changes in labor law to give employers more flexibility in hiring and firing workers and to improve the labor system.

Below you will find a summary report of Labor relationship considerations in Mexico.

6.1. EMPLOYER OBLIGATIONS UNDER THE FEDERAL LABOR LAW

There is a requirement under LFT to issue a locally compliant labor agreement to the employee. The labor agreement will include personal details of the employee and the activities and responsibilities of their position. It will also include reference to the employee's minimum entitlement and benefits under LFT. The minimum details that would need to be included in an employment agreement include:

1. Name, nationality, age, sex, marital status and domicile of the employee.
2. Duration of the labor relationship

(indefinite or fixed term. Fixed term labor agreements are limited to certain circumstances prescribed under the LFT).

3. Description of the services to be rendered by the employee.
4. Place where the employee will carry out his activities.
5. Work schedule.
6. Amount of the employee's wages and terms of payment (it is customary in Mexico to pay on a fortnightly basis).
7. Day and place of payment of the wage.
8. A clause stating that the employee agrees to take the training courses established by the employer, other working conditions, such as days of rest, vacations etc

6.2. MANDATORY BENEFITS

6.2.1. SOCIAL SECURITY

Employees in Mexico are covered by the LSS and the Mexican Social Security Institute (IMSS) isresponsible for the management of mandatory social security benefits and the collection of taxes.

The LSS first enacted on January 31, 1942, has undergone a series of Amendments throughout the years. In accordance with the LSS, all employers must register their employees before the IMSS.

Such registration provides the employee with the following benefits:

1. Work related risks;
2. Health and maternity insurance;
3. Disability, pension and life insurance
4. Retirement, old age pension and old age unemployment insurance;
5. Child care and social benefits.

Upon creation of a working relationship, the employee automatically becomes entitled to the various social security benefits, which are funded by taxes paid by both employers and employees, depending on the risk factor of the company.

Unless the employer has not complied with its registration and payment obligations, the employer is released from any liability for work-related accidents or illnesses. If the employer does not comply with its registration and payment obligations, the IMSS will nevertheless provide the benefit to the employee but it will revert the actual cost thereof to the employer and will impose penalties. Social Security benefits are provided at the IMSS facilities located throughout Mexico.

Social security taxes are calculated regarding the employee's wages over an integrated base (including fringe benefits and certain payments) The minimum monthly earnings used to calculate contributions are the legal monthly minimum wage. The legal daily minimum wage is $123.22 MXN (2020). The maximum monthly earnings used to calculate contributions are 25 times the daily UMA (Unidad de Medida y Actualización). The daily UMA is $86.88. Such integrated wage includes all monetary and in-kind compensations, as well as benefits received by the employee, excluding only the following:

- Work tools and clothing;
- Savings funds, provided they include matching taxes by the employer and the employee;
- Taxes paid by the employers for social or union purposes;
- Taxes made by the employer to the SAR for workers housing;
- Profit sharing paid to the employees;
- Food and shelter, provided the employee pays a portion thereof;
- Food baskets;
- Attendance bonuses; and
- Overtime pay, unless such service is agreed upon on a permanent basis.

In this regard, if the employee receives from the employer housing or meal allowance,

his wage will be increased by 25% and if he receives both it will increase by 50%. If the meal allowance does not cover 3 meals, for each meal received, the wage will increase by 8.33%.

The employer's rate of the tax is approximately 30% of the wage.

As mentioned before, according to the LSS, there is a maximum and minimum limit to determine the base wage. This means that although the employee earns more than the maximum limit set, or less than the lower limit, the employer must pay the employee- employer taxes within the said limit, and the IMSS is required to pay benefits within this range. The insured employee shall be registered by the employer on the base of the wage earned at the time of registration, taking into account that a maximum limit is equivalent to 25 times the daily minimum wage in force in Mexico City the minimum being the limit of a minimum wage. In the case of Life and Disability Insurance, and old age, the limit up is 25 times the daily minimum wage current in Mexico City.

6.2.2. EMPLOYEE PROFIT SHARING (PTU)

Starting from the second year of operations, all employers must distribute among their employees an amount equal to ten percent (10%) of the employer's pretax profit within 60 days after the employer is required to file its year-end income tax return. Fifty percent (50%) of such amount is to be distributed in proportion to the number of days worked by each employee during the year, and the remainder according to the wages of each employee. Certain managerial employees are not entitled to PTU.

6.2.3. CHRISTMAS BONUS

All employers must pay their employees a year-end bonus equal to at least fifteen days of wages, payable before December 20th of every year.

6.2.4. PAID VACATIONS

An employee required to work on any of these vacations must be paid as working on a holiday, a penalty equivalent to three times his normal wage, including his / her regular wage.

Employees with more than one year of seniority are entitled to six days of paid vacation. Such six day period is increased by two days per subsequent year of seniority for up to twelve days. After the fourth year, the minimum paid vacation is increased by two days every five years thereafter, as follows:

YEAR OF SERVICE	DAYS OF VACATION	SENIORITY PREMIUM
1	6	25%
2	8	25%
3	10	25%
4	12	25%
5-9	14	25%
10-14	16	25%
15-19	18	25%

Source: https://www.gob.mx/se/acciones-y-programas/comercio-exterior-paises-con-tratados-y-acuerdos-firmados-con-mexico

6.2.5. VACATION BONUS

According to the LFT, this bonus shall not be less than 25% of the salaries payable to the employees during their vacation period.

6.2.6. EMPLOYER HOUSING TAX

The LFT requires employers to pay an amount equal to five percent (5%) of each employee's wages to the Housing Fund (INFONAVIT). Employers must deposit these taxes in a special account at a local bank.

6.2.7. RETIREMENT SAVING FUNDS (SAR)

As well as the taxes made for the IMSS and INFONAVIT, the employers must contribute an amount equivalent to 2% of the payroll to an employee retirement saving fund (SAR).

6.2.8. SENIORITY BONUS

Seniority (Antigüedad) as outlined in the LFT, says that the employees will have to be rewarded for Seniority, and a Seniority Bonus should be paid to them, corresponding to twelve days of wage (maximum two minimum daily salaries for each day) in the following cases:

1. If the employee has more than fifteen years of service and decides to end the labor relationship, and;
2. If the labor relationship is terminated by the employer.

6.3. LIMITED DEDUCTION ON FRINGE BENEFITS

As a tax reform, from 2014 onwards, of the remuneration payments made to employees that are partially exempt, only 47% to 53% of the payments shall be considered as exempt for the employee — for social welfare items, saving funds, final payment to employees, annual bonuses and overtime — will be deductible.

6.4. EMPLOYER MANDATORY WITHHOLDING

6.4.1. SOCIAL SECURITY TAXES

Employees as well as the employers have an obligation to pay taxes on a monthly basis to the IMSS. Notwithstanding, the employer has the legal obligation to withhold and remit the taxes of his employees to the Tax Authorities.

6.4.2. WITHHOLDING WAGES

For income tax purposes, the wages (employment incomes) include cash, goods, credit, certain, services and any other kind of benefits provided by the employer. Any Income related to employment, including the mandatory annual profit sharing distributions made to employees, as well as income derived as a consequence of termination of employment, will be subject to taxation.

Nevertheless, under certain requirements, income tax shall not be paid on the following incomes:

- Compensation other than the minimum wage.
- Indemnities for risks or illness.
- Retirement and pensions provided for in the LSS.
- Medical and funeral expenses granted generally under the laws or under labor contracts.
- Social Security Tax.
- Fringe Benefits (Disbursements for satisfaction of present or future

contingencies or needs of employees and partners or members of cooperative associations; the granting of benefits intended for the physical, social, financial or cultural well-being that allow for improvements in the quality of their life and that of their families). Among other requirements the exempt amount of general social welfare benefits is limited to the equivalent of one annual UMA, i.e., MXN$ 31,693.80 for 2020. Under no circumstances will the social welfare benefits be taxable if their amount, added to other regular compensation, does not exceed seven times the UMA. i.e. MXN $221,856.601 for 2020. INFONAVIT / Housing taxes

- Savings funds (SAR).
- Severance compensations.
- Christmas Bonus, vacation bonus, Sunday premiums.
- Collection of insured amounts.
- Inheritance or legacy.
- Donations.
- Prizes.
- Indemnities for damages.
- Alimony or child support.
- Amounts withdrawn and transfers.
- Transferred taxes.

The employer must have made a true calculation at the end of the year for each of its employees who will not file an annual tax return, in order to adjust the actual tax withholding to equal the tax liability on salaries on an annual basis. If the employee's compensation is more than MxP $400,000, the employee shall file an annual tax return.

In addition, the employer will be required to withhold yearly personal income tax on employees' taxable wage at variable rates up to 35%, and remit this to the Tax Authorities on a monthly basis.

Finally, it is important to note that as of 2017, it is mandatory for employers to issue an electronic payroll invoice (CFDI) or Payroll CFDI, including additional information regarding employment relationship or labor outsourcing services, as appropriate.

6.5. LABOR REFORMS

On December 1st, 2013, the LFT was amended; amongst the most important amendments are the following:

- New employment testing and training periods (temporary employment)
- Outsourcing regulation

A. New employment testing and training periods (temporary employment)

Before the Labor Reforms, any new employment relationship entitled the employee to certain rights, such as no termination without just cause.

Employments testing periods, or temporary employment, are now provided under the LFT for up to 30 days, which can be extended to 180 days for managerial positions, upon which such employees may be terminated by the employer.

Employment training periods are also possible for up to 3 months (6 months for managerial positions), after which employees may be terminated without employer responsibility. Both the testing and training periods are for new employees and neither apply to promotions or job changes.

On May 1, 2019, according to the terms of USMCA's Chapter 23 and Annex 23-A, the

Mexican LFT was amended as follows:

I. Employers are prohibited from forcing workers to join or withdraw from a union to which they belong, or to vote for a particular candidate.

II. Organizations formed by workers or employers must be protected from mutual interference. It is considered an act of interference to

promote an organization dominated by an employer or an employers' organization. In contrast, benefits specified in a collective bargaining agreement cannot be considered as acts of interference.

III. No person may be compelled to join, or refrain from joining a union.

IV. Votes regarding a union should always be personal, free of pressure and cast in privacy.

V. Articles of incorporation of unions must contain the procedure so that its members can vote in a personal, pressure-free, and private manner regarding their initial collective labor agreements and their revisions.

VI. In order for a union to sign a collective labor agreement or to summon for a strike, it must have the appropriate Proof of Representativeness issued by relevant authority.

VII. A Proof of Representativeness can be issued exclusively to a union that has at least 30% of the workers' representation and, when there are two or more with that percentage, to the union that obtains the largest number of votes among them.

VIII. Current administrative labor authorities will gradually be replaced by specialized labor judges.

IX. Both existing and future labor contracts shall be revised at least every four years.

B. Outsourcing Regulation

Prior to labor law amendments, companies could subcontract their employees from third parties, who would provide the employee benefits and the company would not be considered the employer.

The labor amendment defines "Outsourcing" as a contract pursuant to which an employer (called "contractor" or "subcontractor") performs work or renders services through employees under its control in favor of another entity or person who 1) Benefits from the contracted services, 2) Determines the activities to be performed by such employees and 3) Supervises / monitors the carrying out of such services or the execution of the contracted work.

In this sense, the subcontracting regime is modified and limited to work covering all the activities in the workplace, being specialized in nature and not covering similar tasks to those rendered by the rest of the company's employees. In other words, according to the reform, companies are allowed to outsource only specific or ancillary and specialized tasks. The outsourced services shall not be the same or similar to the main services rendered by employees of the company doing the outsourcing. If the three aforementioned factors are not fulfilled, the company may be subject to employer obligations, including mandatory benefits such as the PTU and social security taxes described above, in addition to fines.

LFT requires outsourcing agreements to be in writing and that the party benefitting from the services to be performed verify the contractor's credit worthiness and its compliance with social security obligations. Failure to comply with these verification

requirements can result in direct liability to the party outsourcing the services, which shall be deemed to be the employer, jointly liable with the contractor for damages to employees.

Similarly, LFT expressly prohibits the outsourcing of employees if the purpose of such outsourcing is to avoid labor obligations or to avoid payment of legal benefits (e.g., social security obligations and PTU). Any breach to this prohibition may result in monetary sanctions that may range from 250 to 5,000 times the applicable minimum wage at the time of the breach.

Until 2019, for income tax purposes, payments derived from labor subcontracting, i.e. labor outsourcing, were deductible when – among other requirements – the contractor obtains from the subcontractor (i) copies of the tax receipts for salary payments made to the employees performing the outsourced services, (ii) a copy of the acknowledgement of receipt, and (iii) a copy of the tax return showing that the income tax withholding and contributions to the Mexican Social Security Institute were remitted. However, as of 2020, these requirements were deleted, since the mechanisms implemented by the Mexican tax authority (SAT), "tax mailbox application" to date have not worked correctly and could not be used by all taxpayers.

It is important to note that as of 2020, legal entities and individuals with business activities, which hire companies that offer labor outsourcing services shall withhold and find that the 6% of VAT they are transferred derived from these subcontracting services.

Tax authorities issue general rules regarding labor outsourcing tax compliance.

In addition, it is important to note, that money laundering provisions are contained in the Federal Law for Prevention and Identification of Transactions Using Illegally-Obtained Funds (FLPITUIOF) of 2012. This law includes the Financial Intelligence Unit (UIF) which is a specialized unit from the Treasury Ministry in charge of getting all reports and notices of those involved in vulnerable activities. In 2016 the UIF included labor outsourcing services as a vulnerable activity subject to money laundering provisions. Consequently, labor outsourcing companies must comply with an extra series of administrative burden, such as: a) Identifying clients as well as retrieving specific documents and information from the client. b) Protecting and preserving information related to vulnerable activities. c) Filing official notices for vulnerable activities. Failing to do so may result in the imposition of large fines

6.6. EXPATRIATES

An expatriate is a non-resident of Mexico (his / her home is outside of Mexico) who is assigned to work in Mexico for a certain period of time. International assignment of an employee to another country is usually started through a "secondment agreement" between the home country employer and the host country employer.

Any foreigner who comes to Mexico in order to work is protected by the Federal Labor Law (LFT as per its Spanish acronym) and is subject to be registered before the Mexican Social Security Institute (IMSS).

An important issue is the immigration situation since the foreigner requires a legal status, and in order to carry out remunerative activities they need a work VISA (temporary residency for 1 year) and that process can take about one and a half months.

If the Immigration Authorities perform an inspection and detect a foreigner without a work VISA it can arrest and deport him, punish him with an economic sanction and forbid entry to Mexico for a period ranging from 1 to 10 years.

Finally, regarding fiscal issues, the payment of taxes will depend on whether the foreigner is resident in Mexico or abroad for tax purposes and the time spent in performance of his activities in the country.

Pursuant to the foregoing, Mexico taxes residents on their worldwide income. In most cases, an expatriate is a resident for tax purposes if Mexico is its primary home and it spends more than 183 days in the country.

Likewise, an expatriate will be deemed as a Mexican resident if it spends more than 183 days per year in Mexico, provided tax authorities consider its "center of vital interests", is located in Mexico.

Mexico may be an expatriate's center of vital interests if:

- More than 50% of your total income received during the calendar year is derived from Mexican sources.
- When your main center of professional activities is located in Mexico.

Nonresidents shall pay 15% or 30% tax on its Mexican sourced incomes on their Mexican sourced income. The first MXN 125,900 (USD 7,000) is exempt in most cases.

Likewise, where an expatriate's salary is paid directly by a foreign company, the expatriate employee bears responsibility for making the monthly estimated tax payments. In certain cases, when the foreign paid salary is charged to a Mexican company, the Mexican company is treated as sponsoring and employing the expatriate for immigration and tax purposes, and therefore, it must withhold and remit the income tax and social security corresponding to the employee's salary.

Finally, where an expatriate's salary is paid directly by a foreign company, expatriate employee shall submit an annual income tax return.

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