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Doing business in Mexico 2017

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This guide is one of a series on business conditions in the countries in which Moore Stephens is represented and is based on the information in force as of May 2016. We believe the information given to be correct as of this date, but we cannot accept any responsibility for any loss occasioned to any person acting or refraining from action as a result of information herein.

Introduction

This guide is designed to give an insight into doing business in Mexico jointly with relevant background information, which could be useful for organizations considering establishing a business in this country, either as a separate entity, as a subsidiary of an existing foreign company, or anyone who is considering to work or live in Mexico.

It is essential to obtain advice from local professional sources before undertaking any business. This booklet contains information and includes legislation references in force as of May 2016.

Moore Stephens International Limited (MSIL) is regarded as one of the top 10 worldwide accounting and consulting networks, consisting of 299 independent member firms and correspondents in 106 countries with over 657 offices and some 21,128 principals and staff.

MSIL is divided into regions: Asia Pacific, Australasia, Europe, Latin America, Middle East, North America, South Africa and the rest of the world. Due to its geographic location, Mexico is considered as part of the North American region (Canada, United States of America and Mexico).

The Mexican member firms cover the following cities: Aguascalientes, Ciudad Victoria, Colima, Guadalajara, Hermosillo, León, Mérida, Mexicali, Mexico City, Monterrey, Piedras Negras, Puebla, Querétaro, Reynosa, San Luis Potosí and Saltillo.

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1 The business environment

Key features of Mexico

1.1 Population

Mexico has a population of 120 million inhabitants approximately.

Mexico City, formerly Federal District (D.F.), is located in the central part of the Republic at an altitude of 2,240 meters above sea level and has a population of 9 million inhabitants (21 million including the metropolitan area). Other important industrial and commercial cities are Guadalajara, Monterrey, Puebla, Tijuana, Ciudad Juárez, San Luis Potosí, Saltillo, Querétaro and Aguascalientes.

Spanish is the official language. English is also understood by many members of the business community in the capital and larger cities.

1.2 Religion

Mexico enjoys full religious freedom. Roman Catholicism was for a long time the state religion. However, the influence of the church has been greatly reduced since the separation of church and state in the 1860s. A majority of the population consider themselves active members of the Roman Catholic Church.

1.3 Education

The Mexican federal and state governments provide universal free education through six years of primary school and three years of secondary school. The federal government also provides the funds for the three largest universities in Mexico City, which are operated as autonomous entities. These universities have established schools for bachelor degree. A large number of private schools and colleges, as well as full-fledged private universities, some of which are operated by religious orders, have also been licensed by the Ministry of Education.

The tremendous increase in population has resulted in an enormous demand for new school facilities at all levels. According to the OCDE's Cooperation Agreement for Improving School Education in Mexican Schools signed in 2008, the allotment of government expenditure invested in Mexican education was 22%, the highest among the countries that subscribed to the OCDE's agreement.

1.4 Geography and climate

Mexico is located south of the United States of America and north of Guatemala and Belize, with an area of approximately 1,973 thousand square kilometers (760 thousand square miles) and 10 thousand kilometers of sea coast, bordered by Pacific Ocean to the west and south, the Gulf of Mexico to the east and the Caribbean Sea to the southeast.

The climate varies widely, from warm temperatures -above 26° C (78° F)-, to cold ones, -below 10° C (50° F)-, in part due to the wide variation in altitudes in the country, and the effect of the Pacific Ocean and Gulf of Mexico on the coastal areas.

1.5 Time, weights and measures

A large part of the Mexican territory is located in the U.S. Central Time Zone. However, part of the western territory is in the U.S. Pacific Time Zone, and the southeast in the East Coast Time Zone.

The metric system (gram, meter and liter) is used with regard to weights and measures.

1.6 Government

Mexico is a Federal Democratic Republic divided into 32 Federal Entities. The executive power is held by the President, head of state and head of government, elected by direct popular vote, and serves one six-year term. The President appoints the members of his cabinet under approval of the Senate.

The legislative power consists of two bodies elected by direct popular vote: the Senate, to which four members for each state and Mexico City (formerly the Federal District) are elected for six-year terms and the Chamber of deputies, to which 500 representatives are elected for three-year terms.

The Supreme Court of Justice is vested with the judicial power, whose 21 members are appointed by the President and ratified by the Senate.

The elections held in July 2000, were the first elections since the 1910 Mexican Revolution in which the opposition party PAN (Partido Acción Nacional) overran the PRI (Partido Revolucionario Institucional), which had been the one and only ruling party.

1.7 Currency

The Mexican peso is the unit of currency, which is divided into 100 cents. The symbol of the peso in Mexico is Ps\$, however, the symbol \$ is generally used.

1.8 Inflation

Inflation rates were constantly decreasing from triple digits in the '80s to double digits in the early '90s and to single digits in 1993 and 1994. Due to the financial and monetary crisis in 1995, the inflation rate rose to 51.97% whereas in 1996 it dropped to 27.7% and in 1997 it fell again to 15.7%. In 1998, it rose to 18.6% dropping in 1999 to 12.3%. From the year 2000 and on, inflation rates continued to decrease. In 2003 the rate dropped to 3.98%; the lowest figure since 1968. In 2004 the inflation rate slightly rose to 5.2%. During 2005 and 2006 the inflation rate was 3.3% and 4.05% respectively, and in 2007 slightly decreased to 3.76%. For years 2008 and 2009 the inflation rate was 6.53% and 3.57% respectively, and in year 2010 it was 4.4%. The inflation rate in Mexico in 2011 was 3.82%. For 2015 and 2014 the inflation rates were 2.13% and 4.08%, also respectively.

1.9 Gross Domestic Product

By the end of 2007, Mexico's gross domestic product registered an increase in pesos of 3.36% in regard to the previous year. In 2008, as a result of the global economic situation, which turned out into a crisis by the end of that year, as a consequence of the great number of mortgage loans granted by North American banks in recent years and which had to be recognized as irrecoverable, the GDP of Mexico, which economy is tightly linked to that of the USA, only grew 1.22%. In 2009, derived from the economic crisis which began in 2008, Mexico's GDP had a 6.28% decrease. In 2010, the variation of the GDP was positive, representing a growth of 5.56%; while evaluating said rate, however, it should be considered that the basis (2009 GDP), had been considerably reduced in regard with 2008 data, as mentioned before. The Gross Domestic product of Mexico increased, from 2nd. quarter 2015 to 2nd. quarter 2016, 2.4%, annualized.

1.10 Forms of business organization

1.10.1 *The principal forms of business*

- Companies and branches of foreign corporations, as well as partnerships.
- Companies are formed by incorporation and registration under the appropriate legal articles of incorporation. These articles contain detailed stipulations concerning the incorporation, management, administration, dissolution and liquidation of companies. Every company has a corporate charter which contains the articles of incorporation, formalizes its constitution and establishes rules for its administration and management.

1.10.2 *The main sources of law for companies in Mexico*

- The General Mercantile Corporations Law
- The General Credit Securities and Operations Law
- The Commerce Code

1.10.3 *The main types of companies in Mexico*

- Corporation (Sociedad Anónima [S.A.])
- Corporation with Variable Capital (Sociedad Anónima de Capital Variable [S.A. de C.V.]).

These two are the most commonly used forms by domestic and foreign investors. At least two shareholders are needed for incorporation, either individuals or corporations. The second is differentiated from the first one due to the flexibility allowed in increasing or decreasing its capital stock after the incorporation. As a result of this feature, the S.A. de C.V. form has become more common. Up to 15, 2012, the Ministry of Foreign Affairs granted the permission to use a commercial or business name. From June 16, 2012, the Ministry of Economy will be the one responsible for the authorization to use a commercial or business name, either for start-ups or companies previously incorporated which have decided to change their name. A Notary drafts the corporate charter and articles of incorporation containing the rules to be followed for the operation of the company and registers the corporate charter when it has been approved and signed at the first shareholders' meeting.

However, there are other legal forms including:

- Partnerships (general or limited)
- Limited Liability Company (LLC) (Sociedad de Responsabilidad Limitada, S. de R.L.)
- Civil companies
- Joint ventures

> *Common Mexican limited companies*

The majority of businesses are constituted as S.A. Its main feature is the capital, whose minimum amount is established in the articles of incorporation, divided into transferable shares which confer limited rights to shareholders.

This form of entity is most frequently used by investors, although the S.A. de C.V. form has become popular in recent years.

> *Capital*

The contributions of shareholders are represented by shares; the capital amount for this kind of businesses will be established in the articles of incorporation as agreed by partners. Twenty per cent of each share value must be paid at least, if the contribution is to be done in cash. The contribution also may be paid in kind, but in this case the contribution should be paid totally (100%), immediately.

Any modification of capital stock entails a certain number of formalities; in the S.A. form it involves amendments to the clauses of the by-laws, as well as permission from the Ministry of Foreign Affairs for such amendments to the articles of incorporation. When properly signed, it has the full legal effect of the original document. Under the S.A. de C.V. form, the described formality is not necessary; the agreement of the General Ordinary Shareholders' Meeting is enough, having the related charter certified by a Notary Public.

> *Management*

The management of an S.A. can be structured in two ways:

- having a board of directors (consejo de administración), or
- having a sole administrator (administrador único), in every case working under the control of a supervisory board (general shareholders' meeting).

> *The board of directors*

Usually, it appoints an individual to be the General Director or General Manager, who is responsible for the company's management and may be assisted by one or more area managers. The board of directors is appointed at the general stockholders' meeting.

> *General shareholders' meeting (stockholders)*

There must be general stockholders' meetings to ratify the transactions and operations of the board of directors or the sole administrator. The resolutions of the general stockholders meeting are executed by either the board of directors or the sole administrator, as the case may be.

The general stockholders' meeting may be either ordinary or extraordinary. The decisions made in both types of meetings must be agreed upon by the majority of the shareholders. The corporation must hold an ordinary stockholders' meeting at least once a year to approve the annual financial statements. An extraordinary meeting may be necessary to deal with certain matters stipulated by law.

> *Limited Responsibility Company (Sociedad de Responsabilidad Limitada [S. de R.L.])*

This is an organization of specific persons; its articles of incorporation can be drafted in such a way as to give it the characteristic of a U.S. Limited Liability Company (LLC); otherwise, it is similar in operation to a corporation because incorporation can be accomplished with as few as two shareholders, who are responsible only for the amount of their capital contributions. The maximum number of shareholders allowed for this type of company is 50. The capital stock for this kind of business will be agreed by the partners and established in the articles of incorporation and at least 50% of the capital share must be paid upon issue.

> *Incorporation of an S.A. or S. de R.L.*

The incorporation of a business is carried out by a Notary Public who requests the permit to incorporate the company from the Ministry of Foreign Affairs, informing it about the domestic and foreign investment that comprises the capital stock; it is also requested the authorization to use the proposed trade name. The Ministry normally grants these permits without delay, unless there is non-compliance with regulations

of the Foreign Investment Law or if the proposed name for the corporation is the same as that of an existing corporation.

The corporation must then be registered before:

- The Ministry of Finance and Public Credit (Secretaría de Hacienda y Crédito Público [SHCP])
- The Ministry of Economy (Secretaría de Economía) [SE]
- The Ministry of Health (Secretaría de Salud)
- The Public Registry of Commerce (Registro Público de Comercio)
- The Federal and local tax authorities
- The Social Security Mexican Institute (Instituto Mexicano del SeguroSocial [IMSS])
- The National Housing Fund Institute for Workers (Instituto Nacional del Fondo de la Vivienda para los Trabajadores [INFONAVIT])
- Various other agencies depending upon the activities of the corporation.

Every business in Mexico must be included in the Mexican Business Information System (Sistema de Información Empresarial Mexicano [SIEM]), where every year, the main data of the business must be updated.

> *Partnerships*

General partnership (*Sociedad en Nombre Colectivo [S. en N.C.]*). Only used by foreign investors in those cases when they desire foreign partnership status in their home country. It is the form of business most analogous to a U.S. partnership. Partners have unlimited responsibility. No minimum capital is required, but the consent of all partners is necessary for modification of the partnership interests. The partners are jointly and indefinitely liable for the partnerships debts. Profits and losses are divided in proportion to each partner's contribution.

Limited partnership (*Sociedad en Comandita Simple [S. en C.]*). Commercial company with at least one unlimited general partner and one or more partners whose liability is limited to their capital contribution. Limited liability partners cannot participate in the management of the company.

Partnership limited by shares (*Sociedad en Comandita por Acciones [S. en C. por A.]*). Similar to the limited partnership, this type of company is different because at the members' contributions are supported by shares.

> **Other forms**

Civil Company (*Sociedad Civil [S.C.]*). Non-commercial form of business organization which resembles a Limited Liability Company. Used mainly by professional practitioners and administrative service units. Partners have unlimited responsibility.

Joint Venture Contract (*Asociación en Participación [A. en P.]*). This is a vehicle utilized for a specific venture. The joint venture contract will be taxed as a corporation. Although a contract is normally formalized in written, it needs not be recorded at the Public Registry of Commerce.

Branch of a Foreign Corporation (*Sucursal de Sociedad Extranjera*). Few exist and few new ones are formed. The entity must receive authorization by the National Commission of Foreign Investment (Comisión Nacional de Inversión Extranjera [CNIE]). It must be noted that branches may not own Mexican real estate. A foreign investor may open a branch operation rather than set up a separate Mexican subsidiary. However, a more practical approach is to establish a Mexican corporation with foreign capital.

Civil Association (*Asociación Civil [A.C.]*). Used by charitable and non-for-profit organizations (e.g. scientific, cultural and religious institutions). Profits may not be distributed to members.

Sole Proprietorship (*Empresa de Persona Física*). A most popular form of organization for a small business. The Commerce Code allows individuals to engage in all kinds of trade. A foreigner may only use this vehicle if he has qualified as a permanent resident. The difference between an individual enterprise and a corporation is that stockholders have limited liability, whereas an individual's liability is unlimited.

1.11 Labor relationships and working conditions

1.11.1 Legislation on employee/employer relationships.

Working relationships are regulated by Federal Labor Law based on Article 123 of the Mexican Politic Constitution.

Legislation provides considerable safeguards for the employee in terms of employment and working conditions.

Labor Unions. Labor Unions take care of their members' interests basically through collective contracts with employers. These agreements generally are reviewed annually. Workers have the right to strike in extreme cases when there is a disagreement between the employers and the Labor unions. At present, labor relationships in Mexico, in general terms, may be described as good, largely as a result of a special effort done by the government to maintain high production standards.

The main Labor union confederations in Mexico are the following:

- Mexican Workers Confederation (Confederación de Trabajadores de México [CTM])
- Mexican Revolutionary Workers Confederation (Confederación Revolucionaria de Obreros de México [CROM])
- National Peasant Confederation (Confederación Nacional Campesina [CNC])

The largest unions are the teachers, the telephone, the petroleum and the electricity labor unions.

1.11.2 **Working conditions**

Wages and salaries. All employees must be paid at least the minimum daily salary (salario mínimo general [SMG]). The Minimum Salary Commission (Comisión de Salario Mínimo [CSM]) determines the minimum salary that employers of the country must pay.

Fringe benefits. As a part of legislation for the protection of employees, the Mexican Institute of Social Security (IMSS) was created by the Government to cater for the welfare of workers in areas such as medical care, retirement and insurance.

The IMSS receives quotas from all the business companies and institutions through contributions which are paid by employees, employers and the government.

Contribution rates vary in relation to the amount of salaries paid as well as labor risks. These contributions represent approximately 28% of the basic salary, from which 23% is paid by the employer and 5% by the employee.

By law, employers must register all their employees in the social security system, without exception.

The social security benefits cover: accidents, medical care, maternity, pensions, unemployment compensation after a certain age, life insurance, retirement fund and day-care.

Housing. The National Institute of Worker's Housing Fund (INFONAVIT) was founded in March 1972, for the purpose of financing homes for workers at a very low cost. Loans are granted at preferential rates, with terms ranging from 10 to 30 years.

Contributions from employers are levied at a rate of 5% of normal salaries paid, with an upper limit of 25 times the minimum annual salary.

Retirement Savings System (Sistema de Ahorro para el Retiro [SAR]). It was founded in February 1992, with the purpose of providing an employee retirement fund to which the employer contributes 2% of the employee's monthly salary, with an upper limit of 25 times the minimum salary, to the employee's individual bank account. There has been a small change in its administration format. Each employee may choose the bank which will manage his (her) fund (the company used to do this before). This system is known as Administration of Retirement Funds (Administradoras de Fondos de Ahorro para el Retiro [AFORES]).

Profit sharing. According to the Mexican Labor Law, employers must share 10% of their net taxable income with their employees. Income Tax Law establishes the rules for computing it. Companies are exempt from profit sharing during the first operation year.

Legal workday. The legal working day in Mexico is eight hours, with a six days work week. An employee can work up to nine hours of overtime in any week, with a maximum of three hours per day. For every six days of work, the employee must have one fully paid day off.

Under collective agreements, the 40-hour, Monday to Friday work week is the most common agreement. Overtime is paid at a rate of twice the normal salary.

Holidays. Mandatory ones for the year are as follows:

January 1	New Year's Day
February	First Monday, for Constitution Day
March	Third Monday, for birthday of Former President (Benito Juárez)
May 1	Labor Day
September 16	Independence Day
November	Third Monday, for Revolution Day
December 1	Every six years, when the new President takes office
December 25	Christmas Day

Employees are also entitled to paid vacation. The term varies according to seniority (6 working days for the first year of service and up to 22 working days for more than 25 years of service). In practice, two weeks' paid vacation is granted to white-collar employees after one year of service.

Indemnity and severance payment. Employees who are discharged without justifiable reasons are entitled to a payment of three months' salary plus 20 days' salary for each year of service.

Seniority premium. Employees are also entitled to a seniority premium after 15 years of service, equivalent to 12 days' salary for each year of service. In computing the daily salary a limit is imposed. A daily salary cannot be higher than twice the minimum salary. This payment must be made if the employee is discharged or if he/she resigns voluntarily after 15 years of service.

Christmas bonus. The employer, by law, must pay 15 days' salary to each employee before the 20th of December of each year.

1.11.3 **Work permits**

Under Mexican immigration legislation, a foreigner may enter the country to work as a non-immigrant or as an immigrant.

> **Non-immigrant**

The non-immigrant may enter with a permit issued by the Ministry of the Interior as: non-immigrant board member or non-immigrant technical visitor.

> *Immigrant*

A foreigner is classified as an immigrant when legally entering Mexico in order to live, until he has five consecutive annual renewals on his immigration permit.

All foreign employees must get their corresponding immigration status from the Ministry of the Interior.

A foreigner may enter the country as an immigrant in order to:

- fill a management position in a Mexican company or institution, running for at least two years prior to the date of application, having a minimum capital stock or a certain amount
- carry out, as a technician or scientist, research in production, technical or specialized functions in a Mexican company or institution, fulfilling the above requirements

There are several requirements for entering the country as an immigrant in order to cover the above described positions.

2 Legal aspects

2.1 Law for the Promotion and Protection of Industrial Property

The law for the “Promotion and Protection of Industrial Property” contains significant elements which substantially improve the previous Mexican legislation regarding these matters.

> *Investment incentives*

The Government grants business incentives aimed at decentralizing industrial development and increasing employment levels. Incentives are normally granted through tax benefits.

2.2 Foreign investment legislation

2.2.1 *General information*

For its prime importance in the Mexican economy, the government has established rules to encourage the growth of foreign capital.

On December 27, 1993, the government issued a new “Foreign Investment Law”, which replaces the former “Law for Promotion of Mexican Investment and Regulation of Foreign Investment”.

The Foreign Investment Law is flexible and has significant advantages for investors in addition to being time saving in the establishment of corporations.

Mexico is one of the most suitable countries for foreign investment in the Latin American region considering the advantages of the Mexican market itself, the proximity of the U.S. border, the North American Free Trade Agreement (NAFTA) between Mexico, the U.S. and Canada, the opportunities offered by the Latin American Integration Association (Latin American Common Market of ALADI), the lack of restrictions for capital repatriation or for paying dividends to foreign investors, as well as Mexico’s political stability. Foreign investment is welcome, the applicable rules are already established and no adverse policy changes are expected in this area.

It will be considered as foreign investment, the following:

- The participation of foreign investors, in any proportion, in the capital stock of Mexican companies;
- The investment by Mexican companies with majority of foreign capital; and
- The participation of foreign investors in the activities and acts foreseen by the Foreign Investment Law.

It is not necessary to submit projects for formal review and approval by the National Foreign Investment Commission (CNIE) in most sectors. The CNIE may authorize a higher percentage for foreign investment in regulated activities if the project meets the following criteria:

- the project must be funded by foreign financial resources, such as capital contributions from shareholders or loans granted by foreign corporations or credit institutions with resources obtained abroad
- industrial projects must be located in areas other than those geographical zones with heavy industrial concentration such as Mexico City, Guadalajara and Monterrey
- accrued foreign exchange flows must be balanced within three years of the investment
- the investment must create permanent jobs and establish training and personnel development programs
- the project should use adequate technologies and satisfy environmental requirements

All projects which do not meet the above criteria or come under partial restriction because of specific industrial or investment considerations, are required to obtain full authorization from the CNIE. However, approval is automatic if a formal response is not received from the Commission within 45 working days after the date of application.

One of the main issues that the Foreign Investment Law regulates is the percentages in which foreigners are allowed to invest in Mexico. This law provides two kinds of investment, direct investment and indirect investment.

2.2.2 **Foreign Direct Investment**

Direct investment gives foreigners direct and full rights and obligations in an entity. Foreign investors are allowed to directly participate in

most economic sectors without fulfilling too many requirements. Nevertheless, if the foreign investment is intended to be higher than 49% (when permitted) and its total assets value is higher than the amount determined by authorities, an authorization will be required.

Although most economic activities are open to foreign investment, some are classified by this new law as “restricted”, “reserved” and “regulated”. Description of this classification is as follows:

Restricted activities. These are activities which only the Mexican government can perform. Since they are regarded as “strategic”, foreigners or Mexican nationals are not allowed to invest in them directly. Restricted activities are as follows:

- petroleum and hydrocarbons
- electricity
- nuclear energy generation
- radioactive minerals
- telegraph
- radiotelegraphy
- postal service
- bank notes issuance
- coin minting
- control and supervision of ports, airports and heliports
- others contained in specific laws

It must be taken into account that, during the current Federal Administration, the Congress approved the so called “structural reforms”; the energy reform allows foreign and domestic investors to participate in certain areas of both, petroleum and electric industries.

Reserved activities. Certain activities can only be performed by Mexican nationals or Mexican corporations with the “exclusion clause for foreigners” (which states that a Mexican corporation will not accept foreign shareholders). The new Foreign Investment Law states that foreign investment is not allowed under any circumstances in these activities. Such activities are:

- passenger, tourist and cargo transportation throughout the Mexican territory, excluding delivery of packages and documents
- development banking institutions, under the terms of applicable legislation.

- professional and technical services, in accordance with the corresponding laws

Regulated activities. The activities in which direct foreign investment is allowed in different percentages are as follows:

- manufacturing and commercialization of explosives, guns, ammunition and fireworks, excluding the acquisition and utilization of explosive for industrial and extractive activities and for the process of explosive mixtures used in the above-mentioned activities
- newspaper printing and publishing for exclusive circulation in the National Territory
- share series "T" of companies that own agriculture, farming and forested land property river, coastal, and exclusive fishing economic zone, excluding water hatcheries
- integral port administration
- piloting services in internal waters, according to the corresponding laws
- navigation in internal and coastal waters, excluding tourist navigation
- supply of fuel and lubricants for trains, airplanes and ships
- telecommunications concessionaire companies as provided by the corresponding law.

As in the case of "reserved" activities, under the law, these allowed percentages may not be exceeded under any circumstance.

Nevertheless, a percentage higher than 49% can be authorized in the following activities if specific criteria are fulfilled. The provision of the total asset value will also apply for these activities:

- port operation services, such as towing and piloting shipping companies engaged in the exploitation of ships solely for high-seas traffic; concessionaires and permit holders companies airfields public service
- pre-school, primary, secondary, preparatory and university private education
- legal services
- construction, operation and exploitation of general railways, and public services of railway transportation.

2.2.3 **Foreign investment in restricted zones**

Direct investment by foreigners in real estate located in “restricted zones” is allowed provided that such investment is intended for nonresidential facilities. The “restricted zones” include all land within 100 kilometers of the Mexican borders and within 50 kilometers of the coastline.

2.2.4 **Foreign Indirect Investment**

Indirect investment grants limited rights and obligations to foreigners through special legal procedures, such as trusts and neutral investment. Before applying for indirect investment, specific laws and provisions regarding these legal procedures must be considered.

> **Real estate investments through trusts in restricted zones**

If foreigners intend to invest in residential facilities in restricted zones, a 50 year trust must be established. The 50 year period can be extended upon request. A trust must always be established with a financial institution as intermediary.

2.2.5 **Neutral investment**

Foreigners can make neutral investment in Mexican entities or through trusts, and this will not be considered as foreign direct investment in Mexican corporations. It is performed by issuing special share certificates which grant only economic benefits, no granting voting rights in board meetings.

> **Expansion of existing foreign investments**

The expansion of existing investments through new projects, activities or product lines and relocation of the enterprise do not require specific authorization, providing one of the following conditions is met:

- the existing investment involves an in-bond facility (“maquiladora”) or other export-oriented operation, or if the expansion is the result of a merger
- the new investment equals 10% of the fixed assets of the company
- there is majority investment in classified activities

2.2.6 **National Foreign Investment Commission (CNIE)**

This commission consists of the Ministries of the Interior, Foreign Affairs, Finance and Public Credit, Social Development, Environment, Natural Resources and Fishery, Energy, Trade and Industrial Development,

Communication and Transportation, Labor and Social Welfare and Tourism. It is headed by a President (the Minister of Trade and Industrial Development)), who designates an Executive Secretary.

The Commission is in charge of granting all authorizations regarding foreign investment in Mexico. Such authorization is considered to be automatically granted, if it does not reply to a duly requested authorization within a 45 working days term.

The Commission has the following responsibilities:

- Dictate policy guidelines on foreign investment and design mechanisms to promote investment in Mexico.
- Resolve through the Secretariat, on the origin and where applicable on the terms and conditions for the participation of foreign investment activities or business acquisitions subject to specific regulations
- The mandatory consultation on foreign investment from agencies of the Federal Public Administration
- Set criteria for the application of the laws and regulations on foreign investment.

2.2.7 **National Foreign Investment Registry (Registro Nacional de Inversión Extranjera [RNIE])**

The Registry will not be public and will be divided into sections established by its rules; it will determine its organization and the information to be provided.

The following business activities must be registered:

- Mexican corporations with foreign investment
- Foreign individuals or entities with commercial activities in Mexico
- Trusts in which foreigners participate with the purpose of performing acts regulated by relevant provisions

The ruling of the National Registry describes the different steps that must be followed for registering foreign investment.

The entities required to be registered in the Registry. Annually shall be renewed their registration just submitting an economic-financial questionnaire in the terms established by applicable regulations.

A transitional provision establishes different dates or which foreign investment could hold up to 100% of the capital of Mexican companies, without having to obtain a favorable resolution by the Commission was established. At present, all these dates are accomplished. The inherent activities are as follows:

International road transport of: passengers, tourism and cargo between points into Mexican territory.

The management service passenger bus stations as well as its auxiliary services,

Manufacturing and assembly of: parts, equipment and accessories for the automotive industry

Provision of services videotext and packet switching

Construction in general and installation works

2.3 Taxation

2.3.1 Tax structure

Mexico has federal, state and municipal taxes. The main federal taxes are Income Tax and Value Added Tax [VAT] (IVA for its Spanish acronym).

> Taxing authorities

Taxes are levied by the Ministry of Public Finance and Credit (SHCP), which has administrative offices in major cities, or by local authorities. These offices deal with interpretation of the law, responses to consultations, authorizations and tax audits.

Each year, the Mexican Congress updates and modifies the existing tax laws, including the Federation Tax Code, which contains supplementary legislation, applicable where the tax laws are not clear enough.

> Main taxes

Direct taxes

- income tax
- taxes on companies that exploit natural resources (mining and territorial waters)
- tax on salaries

Indirect taxes

- Value Added Tax (VAT)

- tax on the production and sale of specific goods or services (beer, alcoholic beverages, tobacco and gasoline)
- duties
- customs duties

> *Miscellaneous taxes*

State taxes

- payroll taxes
- real estate acquisition tax

Local taxes

- Land tax

> *Corporate and income tax structure*

Taxable income is classified according to its source. Different rules are used to compute the net taxable income of each category. The main categories within the structure of the Income Tax Law are the following:

- general provisions
- corporations
- non-for profit organizations
- individual (divided into: salary, professional fees, rent of goods, commercial activities, dividends, interest and deductions)
- income obtained by non-resident aliens with a source of income in Mexican territory

Tax exemptions and special tax treatments are established for activities such as agriculture, fishing, cattle raising and forestry.

According to the general provisions section, individuals and corporations subject to income tax are:

- all residents in the country at all levels of income, regardless of the location of income source
- foreign residents with a permanent establishment in Mexico
- foreign residents, in respect of income from income sources in Mexico.

If they do not have a permanent establishment, or, if they do, when the income does not derive from such establishment.

- individuals who establish their residence in Mexico if their vital interest is in the country, and those individuals whose income is generated, in more than 50%, by a source of income located in Mexico.

These categories will be explained in more detail in the following chapters.

2.3.2 Administration

> Corporate taxpayers

Tax prepayments. Monthly prepayments should be made on or before the 17th of the month following the one to which it corresponds. These advanced or provisional payments are computed applying the Income Tax rate to the result of applying the earning rate of the last accounting period, to each month's income. Corporations are not obligated to make advance payments during the first year of operation.

Tax return. A corporation is required to file a corporation tax return within the three months term following the closing of each fiscal period. The tax return must show the company's taxable income and tax liability, as well as profit sharing to employees.

Penalties. Taxpayers must pay due taxes, restated with the regarding inflation rate and monthly surcharges must be computed and paid. If the tax authorities request the payment of due taxes, additional penalties will apply, such as fines.

Surcharges are levied for a maximum period of five years. Taxpayers that do not file tax returns for more than two years may be subject to a fiscal crime. There are other penalties (either imprisonment or fine) for a variety of violations covering tax provisions.

Authorities' tax audits. The Mexican tax administration has access to significant resources in order to verify the tax returns of corporate taxpayers.

The Mexican fiscal authority has the power to ask for and request information from taxpayers, as well as the right to request information from banks and government agencies. It may carry out audits of the

accounts and make inquiries at corporate offices concerning information dating back up to five years prior to the regarding fiscal year.

Appeal procedures. Taxpayers have the right to appeal against administrative actions according to several procedures established in the Federal Fiscal Code. They may submit an appeal for reversal of the payments made according to the assessments of tax authorities or they may take the option to submit a claim to the tax Court. Occasionally, certain matters are resolved by the Federal Courts.

Rulings. Taxpayers may ask the tax authorities for confirmation of criteria regarding the interpretation of tax provisions; however, such criteria must deal with specific cases. The majority of individual rulings favorable to taxpayers take effect only during the calendar year. Individual rulings issued by Tax authorities are binding solely in the particular cases to which they refer and may be voided only by Court order.

Taxpayer requests for a ruling must be resolved by Tax authorities within a 3 month term. If Tax authorities do not answer the request, the taxpayer may assume a negative response and file an appeal.

Individual taxpayers. Each year, before April 30th, the individual Mexican resident for tax purposes must file a tax return to report taxable income received during the previous fiscal year.

Employees with an annual salary lower than Ps\$ 400,000, whose only source of income is their employment, and who have worked for only one employer during the calendar year, do not have the obligation of filing an annual tax return.

Withholding tax. Tax on income from Mexican sources paid to foreign Residents is collected by withholding at source. The payer of the income is required to withhold the tax and pay it, by means of a tax return, to the Mexican tax administration before the 17th of the month following that in which the payment was made, as in the case of wages, salaries, royalties and services.

Tax audits by Accountants (CPR). The Tax Code authorizes CPR to issue Audited reports for tax purposes. There is a regular audit on Financial

Statements with special emphasis on tax matters. So, audited reports include also a series of charts and notes showing comparative and detailed tax information. These reports are sent to the Ministry of Finance by Internet. This procedure is voluntary and applicable just for certain taxpayers.

The audit reports for tax purposes must be sent to tax authorities within a six-month period after the end of the fiscal year.

2.3.3 *International affairs*

> *International aspects*

Non-residents (corporations or individuals) are generally subject to Mexican tax on income arising from a Mexican source.

> *Treaties to avoid double taxation*

Certain treaties to avoid double taxation between Mexico and other countries are in effect. Some of these treaties include those reached with the United States of America, Germany, England, Spain, Canada, Sweden and France; there is also a Convention between the government of Mexico and the government of the United States for the exchange of information with respect to taxes.

> *International tax affairs*

The General Directorate of Income Policy and International Tax Affairs of SHCP, is mainly in charge of the following international aspects:

- formulation of standards and policies for the negotiation of conventions and treaties regarding tax and customs affairs between Mexico and other countries
- consultations with residents abroad who have no permanent establishment in Mexico, regarding taxable regulations and application of rules of origin within international treaties
- auditing to verify the fulfillment of tax obligations, as well as inspections to obtain information and documents for tax authorities of countries which have conventions and treaties with Mexico regarding tax and customs affairs

> *Transfer pricing*

The SHCP may modify the taxable income of a taxpayer, by determining product or service prices performed by resident and non resident in the

country companies, resident and non resident in the country individuals, trust, or related parties whenever:

- sales or services are invoiced at a price under the market value or when the transfer price is lower than the acquisition cost
- sales are made at cost or lower, with the exception of the cases in which cost equals market value and the products have declined in value
- operations involve imports and exports and payments abroad, or
- sales or services are performed between related parties, which means, affiliated companies

The Ministry may consider the following criteria in determining transfer prices for modification of the taxable income:

- current internal or external market prices, or appraisals by tax authorities
- cost of goods or services plus the taxpayer's gross profit declared on the annual tax return

As a matter of fact, since 1997, the Income Tax Law amendments were specifically for the regulation of transfer pricing matters. The Law stipulates that taxpayers who perform any kind of operations with related parties, are obliged to perform their transactions with related parties on the base of prices or considerations that were applicable in transactions between independent parties, in comparable conditions and in a similar economic environment.

The taxpayer is also obliged to keep the documentary support of the methodology used to determine transfer pricing.

3 Taxes on business

3.1 Corporate tax system

3.1.1 Taxable entities

The following entities are subject to corporate tax:

- mercantile corporations, such as: S.A., S. de R.L., S. en C., S. en C. por A.
- organizations involved in business activities
- banks, stock exchange companies, insurance, security and auxiliary credit organizations
- civil partnerships and civil associations
- branches of foreign companies, if considered permanent establishments
- A. en P. (joint ventures)

> Territoriality

Corporate tax is usually estimated on earning registered in the country and on the earnings of permanent establishments of foreign companies in Mexico.

> Gross income

Accounting period. According to the Federal Fiscal Code and to the General Mercantile Corporations Law, the tax accounting period and the financial accounting period must coincide with the calendar year.

Accounting methods and business profits. Company profits are computed in accordance with Mexican Financial Reporting Standards, although they may be adjusted for tax purposes.

Inventory valuation. Inventory is valued at cost or net realizable value, whichever is lower at the year-end date.

Any method used by the company which is in accordance with Mexican Financial Reporting Standards can be used for tax purposes.

In such terms on the balance sheet, inventory is shown at cost or net realizable value, whichever is lower.

Capital gains. Capital gains are subject to corporate tax as a normal business profit. The acquisition cost of fixed assets is subject to restatement due to inflation effects. The Income Tax Law establishes maximum depreciation rates for fixed assets, which is computed using the straight line method.

Income tax. In accordance with Income Tax Law, corporations earnings are taxable as earned rather than as received. However, special rules apply in some cases, such as leasing, in which earnings are taxable as received; this procedure applies also to individuals.

Income Tax Law is designed in such a way that some items, proceeding from inflation effects, are taxable and some other are deductible.

3.1.2 **Main Rules**

Business expenses. Under certain conditions, the following expenses are deductible for Income Tax purposes:

- depreciation and amortization, must be in accordance with maximum rates and must be computed according to rules set forth in Income Tax Law
- the expenses must be related with normal business operations, except for donations, which have a special tax treatment
- they must be entered in the books
- they must be supported with digital invoices providing certain information such as the name, address and Federal Taxpayers Registry of the seller, the name and address of the company, a description of services or merchandise, the amount and VAT.

There are special rules for the deduction of fringe benefits, royalty payments and technical assistance, as well as imports and research and development.

The most significant deductions for Income Tax purposes are the following:

- discounts and returns on sales
- cost of sales

- expenses (salaries, bonuses, fringe benefits, travel, rental, etc.)
- non-recoverable credits
- technology funds assigned for research and development
- the creation of or increase in reserves assigned to pensions for employees
- interests paid, exchange rate losses and bank commissions
- certain other expenses

Depreciation is charged on the base of a restatement of the assets value, done by applying updating factors derived from the National Consumer Price Index (INPC) to the original cost. The straight line depreciation method is used. Income tax law specifies the maximum depreciation rates to be used for each kind of asset.

The main depreciation rates are:

- buildings (20 years - 5% per year)
- furniture and office equipment (10 years - 10% per year)
- automobiles and trucks (4 years - 25% per year)
- electronic data processing equipment (30% per year)
- moulds, tools and dies (35% per year)
- equipment for new product research or technology development in Mexico (35% per year)
- deferred charges (20 years - 5% per year)
- deferred expenses and certain pre-operating expenses (10 years - 10% per year)

For other kinds of specialized equipment, specific depreciation rates are set forth.

The inflation effect on the net of financial assets and liabilities is included as taxable or deductible.

Non deductible expenses. The following expenses are not deductible:

- income tax
- gifts, and similar expenses (except in publishing matters)
- certain expenses made abroad
- estimated provisions regarding income
- losses for sales made at a price below cost
- expenses in connection with recreation facilities, planes and boats (with certain exceptions)

- goodwill
- 75% of entertaining expenses, including expenses in restaurants and bars, having the option to deduct 100% complying with some requirements established in the Income Tax Law
- indemnity and damage payments to third parties
- investments and expenses, in the proportion that the exempt income represent in relation with the total income, as the case may be.
- credit on salary paid to employees
- sanctions, fines and penalties

Gifts are deductible if related to the sale of products or services and if offered to clients in general. Donations are deductible when certain requirements are complied.

Carrying forward of losses. Fiscal losses can be carried forward to be amortized for up to ten years after the year in which they were determined. They can be restated by applying factors derived from the National Consumer Price Index.

Coordinated Regime: Income Tax Law contains this Regime, for the corporations that operate and manage fixed assets and land related with the activity of transportation, both of persons and merchandises, which members perform exclusively such activity.

Regime of agriculture, livestock, silvicultural and fishery activities: Income Tax Law also contains a Regime for taxpayers dedicated to this type of activities. Since this regime rules activities of the Primary Sector of Economy, it contains some income levels that are exempted for Income Tax purposes.

3.1.3 **Rates of taxes**

The Income Tax rate for corporations is 30%, computed on taxable incomes less authorized deductions.

Dividends paid from the Net Tax Profit Account or CUFIN (corporate profits that already paid income tax). When profits came from 2013 or prior years are not taxable. When profits come from 2014 and following years will be subject to 10% of income tax. Dividends paid from out of

the CUFIN will be taxable at 30% plus the rate of 1.4286%. These rules are applicable for individuals or corporations, Mexican or foreigners.

Regime of fiscal integration: starting at 2014, an optional regime for corporation groups, which allows to defer up to three years Income Tax determined in each year for each Company of the Group, was embodied. For that purpose, the integrative company (parent company), must be the owner of more than 80% of the shares with vote right of the integrated corporations (controlled) and will compute a factor of integrated fiscal result, which will be used to determine Income Tax to be paid and Income Tax that could be deferred.

3.2 Taxation of foreign companies

3.2.1 *Trading as a branch*

Foreign companies are subject to Mexican corporate tax if they have a permanent establishment in the country. A foreign company is considered to have a permanent establishment in Mexico if:

- it performs any established business activity (commercial, industrial or agricultural, including cattle raising, fishing and forestry)
- it realizes activities in Mexico through an independent representative or the representative delivers goods owned by the foreign company
- it provides services in the construction, installation, maintenance or assembly of buildings if more than 183 days are required to complete the job

The foreign associate of a joint venture which operates through a Mexican place of business is considered to have a permanent establishment.

3.2.2 *Mexican subsidiaries*

Mexican subsidiaries of foreign companies are subject to corporate tax in the same way as Mexican companies.

3.2.3 *Taxation of foreign operations*

Income received by foreign residents from a source of income located in Mexican territory is taxable in Mexico whether or not the non-resident is permanently established in the country.

Tax is withheld on the basis of total income by the person doing the payment. This tax payment is considered final unless the individual obtains residence in Mexico during the year, in which case it is considered a prepayment.

3.2.4 **Taxable income**

Wages and fees. Salaries and fees for services performed in Mexico and fees paid to the board of directors if they are paid by companies residing in Mexico.

Withholding tax rate is 30%, 15% or 0% without deduction in the case of wages; it depends on the amount received by the foreign person, and it is considered to be a definitive payment. Regarding fees, the withholding tax rate will be 25%.

The salaries of diplomats, members of scientific and humanitarian delegations and employees of an embassy, consulate or delegation, are tax exempt.

Salaries and fees paid to foreign residents by a foreign resident, would not be subject to income tax.

Rental income on real estate. Rental property in Mexico is considered as a source of income. The withholding tax rate for this activity is 25% without deduction.

Rental income on other goods. If movable goods are utilized for commercial, industrial or agriculture (including cattle raising and fishing) activities in the country, they are considered as a source of income. The withholding tax rate is 25% without deduction. The rental income of railroad cars, airplanes, containers and shipments is taxed at 5%.

Income on sale of real estate. When goods are located in Mexico, the source of income is considered to be in Mexico.

The withholding tax is 25% of the total income. If there is a representative for the seller in Mexico, the tax rate is 35% of the net gain. This is calculated by adjusting the original cost for inflation and deducting this cost from the net sale.

Income on sale of shares, credits or securities. If the sale is made in Mexico or the company is resident in Mexico, it is considered to be a source of income.

The withholding tax is 25% of the gross income. If there is a representative for the seller in Mexico, the tax rate is 35% of the net gain. This is calculated by adjusting the original cost for inflation and deducting this cost from the gross sale.

Interest. When a loan or investment is made in Mexico, the income source is considered to be in the country. This includes the yielding or benefit proceeding from any kind of credit bonds or obligations.

For foreign taxpayers in a country with a treaty to avoid double taxation with Mexico, the tax rates are as follows: (according to the treaty to avoid double taxation reached with the United States)

- 4.9% on interest paid to foreign Banks for granted loans; bond or other credit titles negotiated in a recognized market and to financing entities belonging to foreign governments
- 10% on interest paid to creditors such as suppliers of machinery and equipment or to banks
- 15% on other interest

Financial leasing. If goods are used in Mexico, this constitutes a source of income. The withholding tax rate is 15% on interest paid and is computed according to income tax legislation.

Royalties. If goods or rights are used in the country, they are considered as a source of income.

Tax rates are as follows:

- 25% on royalties covering the use or temporary benefit of literary, artistic, or scientific rights, including films and recordings for radio and television, designs and models, blueprints, formulae or procedures, commercial and scientific industrial equipment, as well as industrial, commercial or scientific know-how and general technical assistance or technology transfer.

- 35% on royalties from the temporary benefit proceeding from invention patents improvement, certificates, brands, commercial names and publicity.
- 5% on royalties for the rent of railroad cars.

When there are treaties to avoid double taxation, the withholding rate may be 10% or 15%; it depends on the country with which the treaty has been signed.

The tax is computed on the income obtained with no deductions.

Construction, installation, maintenance and assembly. When these are performed in Mexico, they are considered as a source of income.

The tax rate is 25% of the income; or 35% of the earning. The income figure used for calculating the tax is before deductions. The earning figure is corporate income less deductions, provided there is a representative in Mexico who fulfills certain requirements.

Payment is done through tax withholding or by the representative filing a tax return to the nearest local fiscal authority, within a month of completion.

3.2.5 **Value-Added Tax (VAT)**

Mexico also has a specific VAT charged on sales of goods, which is passed down the production chain from supplier to distributor until it reaches the final consumer who must pay it and is not able to pass it on. Taxpayers must file monthly tax returns; the VAT paid monthly will be considered as a definitive payment.

VAT must be determined on the basis of transactions that generate cash flow; this means that the tax to be paid will be computed not on the value of invoices issued, but collected and the tax to be credited, will be computed on the basis of the invoices effectively paid to suppliers of goods and services. Such transactions should be verified in the bank statement of account.

This tax applies to:

- sales of goods

- providing of services
- use or temporary benefit of goods
- import of goods and services

Nevertheless, there are certain exemptions to each of these basic categories.

The tax is computed by crediting the tax amounts paid on purchases of goods and services received, with the tax collected from sales. The tax is charged on the total selling price of the goods and services, rent of goods and on the value of the imported goods or services.

The main tax rates are the following:

- 16% general tax rate
- 0% on export as well as on the sale of food products (with some exceptions), patented medicines, and farm equipment, among others

3.3 Taxes on individuals

3.3.1 *Taxation of individuals*

> *Territoriality and residence*

An individual is considered as a resident in Mexico for tax purposes when he (she) has established a permanent home in Mexico. If he (she) spends more than 183 days in a calendar year, consecutive or not, in another country, and is able to show documentary proof of his residence in that country, he may be considered as non-subject for taxes, but tax residency must be proven. This is proven through a letter issued in the country from which he proceeds, stating he is a tax resident in that country.

A resident in Mexico is subject to taxation on all his worldwide income, regardless of where that income is earned.

> *Years of arrival and departure*

An individual is liable for tax on the date he becomes a tax resident in Mexico.

Mexican tax liability ceases when an individual leaves the country due to the termination of his employment contract. The employer must

withhold tax from salaries and fringe benefits on a monthly basis and is liable for any income tax on the employee's salary not paid by him. For non-resident aliens a tax liability arises only on income from sources within Mexico.

3.3.2 **Income tax**

Individuals are subject to income tax on their annual taxable income. Taxable income is determined by adding together the various categories of income and deducting expenses and, in certain cases, some losses. Individuals who during a fiscal year receive only salaries or wages or interest income, are not obliged to file a tax return, provided that the amounts do not exceed \$400,000 for salaries and interests and that the latter does not exceed \$100,000. The corresponding withholding tax should have been done by the employer, as well as by the person who pays interests.

Individuals can deduct medical and dental expenses, as well as premiums for major medical expense insurances, hospital and funeral expenses of their spouse, children or other dependents, and donations to duly authorized public services, welfare or benefactor institutions, and real interest paid on mortgage loans.

> **Taxable income**

Three most significant categories of income comprise the following:

- salary
- income from professional and business activities
- income from rents or sale of goods
- general regime
 - tax system for small business
- dividends

Income from salary. Companies must withhold income tax on employees' salaries based on a progressive rate of up to 35%.

Professional and business activities. Professionals must file monthly provisional statements of income less expenses on which they must pay income tax at a progressive rate of up to 35%. When services are carried out to corporations, they must withhold at source ten percent

of professional fees. This withholding may be applied by individuals for their prepayments.

Individuals who perform business activities should also file monthly provisional returns, paying tax on the surplus of resting expenses from income, applying to it a progressive rate, up to 35%. Income and expenses must be considered on a cash flow basis.

Income from real estate rental and goods realization. Individuals obtaining income from rentals or other disposition of goods must remit a provisional statement of income determining a surplus which would be the result of subtracting some expenses or applying “blind” deduction from the income; such surplus is taxed at a progressive rate of up to 35%. Again, 10% of the rental is withheld at source and applied with the income tax payable when the payer is a corporation.

Income tax on dividends. As mentioned before, when dividends proceed from “CUFIN” generated up to December 31, 2013, it is not accrued for Income Tax purposes; however, dividends proceeding from “CUFIN” generated starting at January 1st, 2014, will be object of a 10% additional tax rate.

3.3.3 ***Family and dependents***

In determining income tax, there are certain deductions applicable for family and dependents. The Mexican taxation system imposes an income tax on the individual, not the family. However, married couples who adopt the concept of joint ownership, regarding income from capital gains (such as interest and rents), must declare each individual's proportion of such income.

No tax will be paid on:

- compensation for accidents or illness
- reimbursement of medical and hospital expenses for the taxpayer and dependents, paid to persons or institutions resident in Mexico (dependents include the spouse and direct ascendant and descendant relatives not earning annual income equal to or greater than the yearly minimum wage)
- compensation for funeral expenses

- social welfare fringe benefits such as workman’s compensation, scholarships for employees or their children, day care and cultural and sport activities, as long as they are granted to all employees. There is a limit on exemptions on social welfare fringe benefits of seven times the minimum salary
- social security paid by the employer which is ordinarily paid by the employee
- savings fund
- year-end or Christmas bonus, up to 30 days’ minimum salary
- meals and travel expenses if actually incurred while working (must be supported by receipts or invoices)

The Federal Government issued a decree which grants individuals resident in Mexico, the benefit of being able to deduct from their taxable income, tuition payments for the basic and higher levels when studies are being conducted in private schools by the taxpayer or his spouse or his ascendants or lineal descendants. For such purpose, annual limits were established for such deduction, according to the educational level concerned and are as follows:

	<i>Mx Pesos</i>
Preschool	14,200
Primary school	12,900
High school	19,900
Technical school	17,100
High school diploma or equivalent	24,500

3.3.4 **Other contributions**

> **Federal taxes**

Special production and services tax. This tax is applicable to corporations or individuals producing beer or other alcoholic beverages, table wine or cider, processed tobacco and oil industry products.

It is similar to VAT, except that it is chargeable only on specific activities, and is charged in addition to any VAT transferred on these activities.

Law for Hydrocarbons. Within the context of the Energy Reform implanted in Mexico in recent years, a gradual transition is previewed, towards a free market for fuels; by this reason, it will be possible the following:

That starting at 2016, permissions to sell fuels to consumers be granted to private investors.

That starting 2017, or before, if market conditions allow it, it will be possible to grant permissions, to any interested that comply the applicable legal provisions, for gasolines and diesel import.

That, starting at 2018, the prices of fuels be determined under market conditions and, therefore, the market of automotive fuels become an open market, with free prices determination.

Social security quotas. The Mexican Social Security Institute (IMSS) receives quotas (revenues) from all companies and institutions, through contributions paid by employees, employers and government.

Contribution rates are fixed, except for work risks. These contributions represent approximately 33.925% on the integrated salary (nominal salary plus some benefits); 30.35% is paid by the employer and 3.575% by the employee.

Housing. Companies must pay a contribution to the National Institute for Workers Housing (INFONAVIT). The housing contribution is equivalent to 5% of the integrated salary paid by the company or institution to each employee, not exceeding 25 times the minimum general salary.

Tax on Acquisition of new automobiles. This tax is paid by vendors of new automobiles in Mexico and individuals or corporations that import them, but it is finally charged to the individuals or corporations that acquire the vehicle.

Duties. It is applicable to all goods and services that are sold or given by the Federal Government, including those that are imported, in accordance with the Duties Law.

> **State taxes**

2% on salaries. Companies must pay a 2% flat tax on salaries paid. This rate may vary depending on the state. Mexico City, Guadalajara, and Monterrey 2% on payroll tax is the highest rate.

Tax on the acquisition of real estate. Residents and non-resident individuals or corporations are subject to this tax, which is computed on the appraisal value, at 2% rate.

Municipality taxes. Land tax is paid based on the value of land and buildings.

3.4 Tax regime for maquiladoras

In accordance with the Income Tax Law, “maquiladoras” (in-bond production) will be subject to the following:

1. The tax in charge of the “maquiladoras” shall be the larger amount resulting from applying each of the following computations:
 - The 6.9% of the asset value used in the “maquila” activity, and including the assets property of the foreign resident, resident in Mexico or related party, as the case may be.
 - The 6.5% over total costs and operation expenses related to the “maquila” operation.

When applying for the aforementioned computations, the “maquiladoras” should submit before the Central Administration of International Tax Audit, a written notice in which they express that they fulfill them.

When applying for the aforementioned computations, the “maquiladoras” will be exempted from submitting the informative tax return of operations with related parties, in accordance with Article 182 of Income Tax Law.

2. In case of not choosing the aforementioned computations, the “maquiladoras” should request and obtain from Tax Authorities, after an analysis of transfer prices, favorable resolution related to the methodology used in the determination of prices or amounts of the considerations in operations with related parties.

4 Foreign trade

4.1 Foreign market

Mexico has signed free trade agreements and trade liberalization agreements with more than 40 countries, having access to a potential export market of over one billion consumers, representing 75% of global GDP, and being one of the most privileged and competitive economies with regard to international trade. These agreements have been executed with countries in North, Central and South America, Europe, Asia and the Middle East.

These business relations with such countries result in more competitive advantages for investors who wish to establish a business in Mexico, since 90% of negotiated tariffs are tax deductible. Non-payment of customs duties has also been negotiated.

In order to obtain such benefits, it is necessary to comply with the Rules of origin set forth in all the executed treaties and agreements, as well as with Mexican legislation.

When importing goods from a country with which Mexico has not executed a trade agreement, the cost of the highest tariff at a 35% rate, and customs processing fees at 0.008%, must be copnsidered; both duties are computed on the customs value of goods, plus any other taxes, according to the type of merchandise.

4.2 Export incentive programs

Federal Programs grant export incentives to investors in Mexico such as the return of import duties paid on processed or unprocessed products that are subsequently exported.

4.3 Specialized infrastructure in foreign trade

In recent years, the Mexican government has invested in building infrastructure aimed at supporting international trade performed by foreign investors established in Mexico.

Such infrastructure comprises various industrial and logistics complexes also known as Strategic Bonded Warehouses, inland ports and industrial parks, as well as highways connecting directly Mexican cities with the United States of America and Guatemala, as well as seaports, airports and railways stations.

Strategic Bonded Warehouse is a fiscal control customs regime similar to an in-bond plant (Maquiladora), where goods can be manufactured, processed or repaired, and be subject to handling, storage, custody, exhibition, sale and distribution with the advantage of performing imports free of taxes and countervailing duties. Merchandise will not be subject to comply with non-tariff regulations except for security and public health. Also, this system offers various tax benefits including services export, and tax incentives with regard to Income Law. Moreover, the stay of foreigners in the country for such reasons is not considered as residence.

Inland Ports are large multi-service cargo terminals (airports, cargo terminals, etc.). The name comes from the absence of water, sea and ships; however, it is also technically called a "logistic intermodal hub" which includes cargo handling, loading and unloading, transportation, load consolidation and distribution, storage, repackaging, labeling, finishing, etc., as well as special storage for inventories under customs custody and collaterals.

Industrial parks represent a very important factor to determine the location of foreign direct investment projects in Mexico since they offer land property and permanent maintenance of public areas and internal security of tenants, and ensure availability of basic infrastructure (water, electricity, paved roads, sewer system, lighting, water treatment plants, etc.).

4.4 **What to consider before carrying out imports in Mexico**

Investors should consider the following procedures as established by the Ministry of Finance, prior to carrying out import or export activities in Mexico.

In relation to exports, it is worthwhile mentioning that it is not necessary to be enrolled in a Registry, except if the merchandise contains alcohol.

These procedures are as follows:

- To enroll in the Registry of Importers
- To enroll in the Registry of Importers of Specific Sectors

- To enroll in the Sector-based Registry of Exporters
- To hire a customs broker
- To comply with the provisions required by the Mexican Official Standards and additional public health authorities.

4.4.1 **Registry of importers**

As established in the Customs Law, companies performing imports are required to enroll in the Registry of Importers. By doing so, all sorts of products can be imported, excluding those products expressly stipulated in any law that may be restricted or prohibited.

The registration is processed online at the site of the Tax Administration Authority (SAT) (www.sat.gob.mx), accessing My Site using the Tax Number (RFC) and password (CIEC), in the Online Services section, clicking on Registers.

Requirements are: current electronic signature issued by SAT (FIEL), password (CIEC), domicile for tax purposes as registered in the Tax Number (RFC), or in verification process by the local Tax Administration, be up to date in the compliance with their tax obligations, be registered and active in the tax payers registry, and register customs brokers to conduct their foreign trade operations online.

4.4.2 **Importers list by specific sector**

Likewise, companies are subject to enroll in this Registry when importing goods which includes chemicals, chemical precursors and essential chemicals, as well as chemical substances.

Such registration is processed online at the site of the Tax Administration Authority (SAT) (www.sat.gob.mx), accessing My Site using the Tax Number (RFC) and password (CIEC), in the Online Services section, clicking on Registers.

Requirements are: current electronic signature issued by SAT (FIEL), password (CIEC), domicile for tax purposes as registered in the Tax Number (RFC), or in verification process by the local Tax Administration, be up to date in the compliance with tax obligations, be registered and active in the taxpayers registry, and attach one of the following documents issued by the National Commission for Nuclear Safety and

Safeguards of the Ministry of Energy: Authorization for Acquisition and Transfer; Authorization for Service Providers; Operation License; License for Possession and Use of Material.

4.4.3 **Sector-based exporters' registry**

It is mandatory for corporations that, due to their commercial activity, need to export goods which are regulated by the Law of Special Taxation on Production and Services such as: alcohol, beer, tequila, wine, liquor, cigarettes and processed tobacco, among others.

A format in writing is processed and presented personally, or sent through courier service to the Control Service Office at the Ministry of Finance.

Requirements are: current electronic signature issued by SAT (FIEL), domicile for tax purposes as registered in the Tax Number (RFC), or in verification process by the local Tax Administration, be up to date in the compliance with their tax obligations, be registered and active in the tax payers registry.

4.4.4 **Customs brokers**

In Mexico, it is mandatory to hire customs brokers since they are the only ones authorized by the Ministry of Finance to perform import or export procedures. Therefore, fees for their services must be considered for each import or export. Such fees amount the equivalent to 0.45% calculated on the customs value of imported or exported goods, however, flat rates are plausible.

4.4.5 **Non-tariff regulations**

Before starting any import activities, it is recommendable to analyze the regulations which the products must comply with in Mexico with a view to saving costs and any unexpected difficulties.

Such is the case of the Mexican Official Standards with which goods must generally comply before being cleared at customs (imports).

On the other hand, there are Mexican Official Standards for commercial labeling. Compliance with such standards may occur even though products have been imported already. There are more than 900 Mexican

Official Standards for a wide variety of products including electronics and electrical goods, as well as food.

In Mexico, product certification involves costs as the related with samples of the products under certification that must be imported at first, as well as logistics services, customs broker services and customs contributions, which must be covered as well. Furthermore, fees of companies that offer certification services must be also considered, since they evaluate and certify import goods. It is recommended to allow up to ninety days for this certification process.

4.5 Essential documents for imports and exports

The Customs Law in Mexico requires submitting the following documents:

Imports

- Import entry
- Commercial invoice
- Airway bill (air transportation) and/or bill of lading (ocean transportation)
- Documents confirming compliance with Mexican Official Standards and additional regulations.
- Certificate of origin
- Any additional information needed to identify goods.

Exports

- Export entry
- Commercial invoice or any document indicating the value of goods
- Documents confirming compliance with Mexican Official Standards and other regulations

4.6 Temporary Import Program IMMEX

Duty deferral programs promote import of supplies and fixed assets on a temporary basis without paying foreign trade fees. These programs can be found in the Decree for Promotion of Manufacturing, Maquiladora and Export Services Industry (IMMEX), which is a result of the combination of the PITEX and Maquiladora programs, in force up to 2006

The program aims at encouraging and facilitating manufacturing companies, maquiladoras and export services when performing industrial processes or services, with regards to export goods and services.

To have access to such program, it is necessary to access the website of the Ministry of Economy at www.economia.gob.mx. Replies often occur within five business days.

Companies which request to enroll in this program need approval and may obtain one or more modes, as listed below:

- Holding Company Mode: Manufacturing operations of a certified company –known as controller– and one or more controlled companies are integrated into the same program.
- Industrial Mode: For industrial production or transformation processes of export goods.
- Services Mode: When export goods require a service or when export services are provided to the activities determined by the Ministry of Economy upon previous opinion of the Ministry of Finance.
- Shelter Mode: One or more foreign companies provide both technology and material for production, but do not operate the program directly.
- Outsourcing Mode: For certified companies that do not have facilities for manufacturing processes. Thus, manufacturing operations are performed by third parties registered under their program.

Goods temporarily imported under this program will not pay foreign trade fees and may remain in Mexico for the following terms:

- Up to eighteen months; for fuels, lubricants and other materials to be used during the production process of export goods, raw materials, parts and components that will be used completely to generate export goods, containers and packaging, labels and brochures. There are some special requirements for specific goods that belong to certain industrial sectors.
- Up to two years; for containers and trailer bodies.
- For the lasting of the program; for machinery, equipment, tools, instruments, molds and parts used in production processes, pollution control equipment and devices for research or training, industrial safety, telecommunications and computers, laboratory, measuring, product testing and quality control, as well as those involved in materials handling and management which are directly related to export goods, and others associated with production processes and administrative equipment.

The most recent modification of this program occurred in December 2010, where certain specific requirements for the temporary importation of alcohol, alcoholic beverages, sugar and iron products were established. Likewise, the program stipulates maximum amounts for the temporary importation of textile and clothing sectors, as well as activities that may be performed in the form of services.

Some of the advantages that this program offers are the following: alienations companies perform, since importers can transfer goods to other IMMEX companies, often regarded as an export. On the other hand, IMMEX companies purchase goods temporarily without payment of duties and VAT. These operations engage customs entries and brokers whose fees must be considered.

Maquila operations that occur under this program have a positive effect on Income Tax and Value Added Tax.

Two export promotion programs joined IMMEX in 2010. Such programs are the Market domestic goods abroad (formerly known as foreign trade companies or ECEx) and obtain a VAT return within twenty days approximately. Certified companies can obtain such return within five working days (also known as highly exporting companies or ALTEX).

4.6.1 **Submaquila operations**

Authorization from SE for submaquila operations is required when the operations are treated as a complement to the production process of the main activity of the program. The products are returned to the IMMEX that contracted the service thereby completing the product for exportation.

This operation can be performed between companies which are beneficiaries of the regarding decree or between these and other companies without an IMMEX program. Authorization is valid for one year.

Financial support for maquiladoras. The National Bank of Foreign Trade (Bancomext) provides important financing packages in order to support the IMMEX export industry.

All beneficiaries of the credit must be registered in the National IMMEX Industry Registry controlled by the Ministry of Economy

Financial resources are granted for the following:

- Capital work: applicable to production, purchases from domestic suppliers and export sales
- Fixed investments: applicable for the acquisition of machinery, equipment and transportation equipment.
- Promotional projects: applicable to market studies, technical and financial feasibility studies, studies on improvement of products, development of new technology, advertising, advising and training, promotional trips, international fairs and commercial missions.

5 North American Free Trade Agreement

The North American Free Trade Agreement (NAFTA) between Canada, the United States of America and Mexico which came into effect on January 1, 1994, created the largest market in the world with an estimated consumer potential of 370 million people.

The objectives of NAFTA are to eliminate commercial barriers, promote conditions for fair competition, increase investment opportunities, provide protection of intellectual property rights, and establish effective procedures for the application of the treaty in addition to promoting trilateral cooperation both regionally and multilaterally

5.1 Rules of origin

NAFTA foresees elimination of tariffs on goods between Canada, the United States of America and Mexico with a transition period. These rules of origin determine which goods are eligible for NAFTA benefits.

NAFTA's rules of origin are designed to:

- ensure that NAFTA's advantages are granted only to goods produced in North America and not to goods which are totally or mainly produced outside the region
- establish clear rules and obtain foreseeable results
- reduce bureaucracy for exporters, importers and producers that have commercial activities within NAFTA

These rules state that goods are considered as originating from a certain region whenever they are totally produced in Canada, the United States or Mexico (North America). Goods which contain materials that do not originate in the trade zone will also be considered "original", provided such materials are transformed by a NAFTA member. Such transformation must be sufficient to modify the customs heading in accordance with NAFTA's rules. In some cases, besides modifying the customs heading, goods must incorporate a specific percentage of regional content.

The percentage mentioned above will be calculated using the transaction value or net cost methods. The transaction value method is based upon the paid or payable price of a good. The net cost method is obtained from the total cost of the good, plus royalties, marketing, packing and shipping. Producers may use both methods; nevertheless, according to the World Trade Organization (WTO) Customs Valuation Code, the net cost method must be used when the transaction value is not acceptable, or for some products of the automotive industry.

NAFTA establishes the principles for WTO's national treatment. Goods imported or exported to a NAFTA member firm from another treaty member will not be subject to discrimination.

5.2 Customs administration

To ensure that only NAFTA members enjoy preferential trade tariffs when complying with rules of origin and that importers, exporters and producers undergo minimal formalities, NAFTA includes customs regulations that establish the following:

- regulations that ensure consistent application, administration and interpretation of rules of origin
- certification requirements as well as certificates of origin for importers and exporters who desire preferential trade tariffs
- common accounting requirements for those goods
- rules for importers, exporters and customs authorities
- previous rulings regarding origin of goods, issued by customs authorities of the final destination country
- equal rights and treatment for importers from one country and exporters from the other two
- trilateral work groups that modify rules of origin and regulations when necessary
- specific dates for resolution of disagreements between member countries regarding rules of origin

5.3 Tariffs

There are established regulations on tariffs and other duties, as well as quantitative restrictions on quotas, licenses, permits and price regulations on imports or exports for regulation of commerce. Furthermore, these regulations

are intended to ensure market access for goods that are produced and traded within North America.

5.4 **Technical norms**

NAFTA acknowledges that official governmental standards and technical regulations from the government and its processes used for verification are fundamental for the promotion and protection of human, animal and plant life and health, as well as consumer and environmental protection. However, member countries have agreed not to use these standards as unnecessary obstacles to commerce.

Each of the three countries preserves the right to adopt, apply and enforce its own standards for the establishment of desirable protection levels. Additionally, NAFTA confirms rights and obligations derived from WTO's Technical Barriers Code and other international agreements, including environmental and conservation treaties.

Each member country will use international rules as a base for its own standards. Nevertheless, each nation has the right to adopt, apply and enforce measures which would allow it to obtain a protection level higher than that provided by international standards.

5.5 **Government purchases**

The treaty will open the market to all NAFTA member suppliers of goods and services to government, to include those purchases made by governmental departments and entities in each member country.

However, NAFTA does not allow for the purchase of armaments, ammunition, weapons or other items related to national security.

5.6 **Investment**

Basic guarantees for investors from the three countries are provided in NAFTA. It also establishes a mechanism for the solution of possible controversies between investors in separate NAFTA countries. All the various types of investment are fully explained in NAFTA.

No NAFTA member may impose restrictions on investments in its territory, such as on export levels, minimum national content, special treatment to national suppliers, imports subject to export levels and technology transfer. Nevertheless, the above mentioned will not apply to government purchases, export incentive programs or activities involving international relief.

Investors from NAFTA countries may exchange currency at market exchange rates from earnings, sales income, interest payments or other transactions related to investment. Each NAFTA member country will ensure that these currencies are freely transferred.

No NAFTA member may expropriate investments from other member countries, directly or indirectly, unless:

- they are used for public purposes
- they are based on non-discriminatory principles and applicable laws
- investors receive compensation at market value plus any corresponding interests

5.7 Commerce of goods

5.7.1 *Energy and basic petrochemicals*

NAFTA sets obligations and rights for the three countries relating to petroleum, gas, refined products, basic petrochemicals, coal, electricity and nuclear energy.

As Mexico considers this sector to be strategic, a special chapter within NAFTA was included. Mexican government keeps complete rights and exclusivity on energy production, oil and gas industries. At present other countries may participate in joint ventures contracts together with our government for exploring, exploiting and distributing oil, gas and electricity too.

5.7.2 *Agriculture*

NAFTA establishes bilateral agreements between Canada and Mexico and between the United States and Mexico regarding the trade of agricultural produce. Both agreements recognize infrastructural differences between the countries and include special safeguard mechanisms for this industry.

5.7.3 **Environment**

NAFTA establishes rules for the development and execution of environmental standards and determines that no member country may lessen or disregard any environmental law in order to attract foreign investment.

5.7.4 **Others**

NAFTA includes regulations on basic petrochemicals, agriculture, emergency measures, telecommunication, financial services and intellectual property, among others.

Abbreviations and acronyms

A. en P.	<i>Asociación en Participación</i>	Joint Venture Contract
A.C.	<i>Asociación Civil</i>	Civil Association
Afores	<i>Administradoras de Fondos de Ahorro para el Retiro</i>	Administrators of Retirement Funds
Bancomext	<i>Banco de Comercio Exterior</i>	Mexican Bank of Foreign Trade
CIEC	<i>Clave de identificación confidencial</i>	Confidential electronic identification code
CNIE	<i>Comisión Nacional de Inversión Extranjera</i>	National Foreign Investment Commission
CSM	<i>Comisión de Salario Mínimo</i>	Minimum Salary Commission
CUFIN	<i>Cuenta de Utilidad Fiscal Neta</i>	Net Fiscal Profit Account
D.F.	<i>Distrito Federal</i>	Federal District
FIEL	<i>Firma electrónica avanzada</i>	Electronic advanced signature
GPT	<i>Tarifas Generales Preferenciales</i>	General Preference Tariffs
IMMEX	<i>Industria Manufacturera, Maquiladora y de Servicios de Exportación</i>	Manufacturing, Maquiladora and Exportation Services Industry
IMSS	<i>Instituto Mexicano del Seguro Social</i>	Mexican Social Security Institute
INFONAVIT	<i>Instituto Nacional del Fondo de la Vivienda para los Trabajadores</i>	National Housing Fund Institute for Workers
IVA	<i>Impuesto al Valor Agregado</i>	Value Added Tax, VAT
LIE	<i>Ley de Inversión Extranjera</i>	Foreign Investment Law

NAFTA	<i>Tratado de Libre Comercio de Norteamérica</i>	North American Free Trade Agreement
OCDE	<i>Organización para la Cooperación y el Desarrollo Económico</i>	Organization for the Economic Cooperation and Development
RFC	<i>Registro Federal de Causantes</i>	Taxpayers Registry / Tax Number
RNIE	<i>Registro Nacional de Inversión Extranjera</i>	National Foreign Investment Registry
S. de R.L.	<i>Sociedad de Responsabilidad Limitada</i>	Limited Responsibility Company
S. en C.	<i>Sociedad en Comandita</i>	Simple Limited Partnership
S. en C. por A.	<i>Sociedad en Comandita por Acciones</i>	Partnership Limited by Shares
S. en N.C.	<i>Sociedad de Nombre Colectivo</i>	General Partnership
S.A.	<i>Sociedad Anónima</i>	Corporation
S.A. de C.V.	<i>Sociedad Anónima de Capital Variable</i>	Corporation with Variable Capital
S.C.	<i>Sociedad Civil</i>	Civil Company
SAR	<i>Sistema de Ahorro para el Retiro</i>	Retirement Savings System
SAT	<i>Servicio de Administración Tributaria</i>	Tax Administration Service
SE	<i>Secretaría de Economía</i>	Ministry of Economy
SHCP	<i>Secretaría de Hacienda y Crédito Público</i>	Ministry of Finance and Public Credit
SIEM	<i>Sistema de Información Empresarial Mexicano</i>	Mexican Business Information System
SMG	<i>Salario mínimo general</i>	Minimum daily salary
WTO	<i>Organización Mundial de Comercio</i>	World Trade Organization

Moore Stephens has independent member firms
and correspondents in the following countries:

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Andorra	Czech Republic	Kazakhstan	Romania
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Australia	Dominican Republic	Kuwait	Saudi Arabia
Austria	Ecuador	Latvia	Senegal
Azerbaijan	Egypt	Lebanon	Serbia
Bahamas	El Salvador	Liechtenstein	Seychelles
Bahrain	Estonia	Lithuania	Singapore
Bangladesh	Finland	Luxembourg	Slovakia
Belgium	Former Yugoslav	Macedonia, Fyrom	South Africa
Belize	Republic of	Malaysia	South Korea
Bermuda	Macedonia	Malta	Spain
Bolivia	France	Mauritius	Sri Lanka
Botswana	Germany	Mexico	Sweden
Brazil	Gibraltar	Monaco	Switzerland
British Virgin	Greece	Mongolia	Taiwan (ROC)
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Bulgaria	Guernsey	Netherlands	Tunisia
Burundi	Honduras	New Zealand	Turkey
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Canada	Hungary	Norway	United Arab Emirates
Cayman Islands	India	Oman	United Kingdom
Channel Islands	Indonesia	Pakistan	United States of
Chile	Irak	Panama	America
China	Ireland	Papua, New Guinea	Uruguay
Colombia	Isle of Man	Paraguay	Venezuela
Congo (DRC)	Israel	Peru	Vietnam
Cook Islands	Italy	Philippines	Yemen
Costa Rica	Japan	Poland	Zambia
Croatia	Jersey	Portugal	Zimbabwe

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