



Independent legal & accounting firms

Doing Business in Mexico

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MSI's Guide on Doing Business in Mexico provides current information about the financial, regulatory and legal considerations that could affect business dealings within Mexico. For further assistance please contact our MSI member firms in Mexico.

Country overview

Population

Mexico has got a total population of almost 120 million inhabitants.

Government

The Mexican Government is a representative, democratic, secular, federal Republic. The current President is Andres Manuel López Obrador. His wife is Beatriz Gutiérrez Muller, a well-known writer, researcher and journalist. The Mexican Government is presidential. The President is Head of State and Head of Government. As Head of Government, the President is entitled to appoint several Ministers, who will be in charge of each Ministry.

Mexico has got 32 states, each with its own local government.

Languages

The national language is Spanish. However, a considerable amount of people, especially in large cities like Mexico City, Monterrey and Guadalajara, speak English.

Currency

The national currency is the Mexican Peso. For business purposes companies can choose to apply a different currency.

Economic summary

GDP: \$ 1,223,808,885 USD.

Income per capita: \$9,698.1 USD.

Inflation: 3.95% (estimated by the end of 2019).

Main sectors of the economy

Historically, Mexico has achieved a very good commercial relationship with the United States and Canada. This principally can be attributed to the North American Free Trade Agreement (NAFTA), which was negotiated in the early nineties.

Notwithstanding the foregoing, Mexico has become an important business partner for major industries in many countries around the world.

Some of the most important activities in relation with the economic growth in Mexico are the manufacturing services (especially in the automotive sector), the food industry, the tourism industry and the real estate industry.

Perspectives on 2019

Pursuant to a recent publication of the OECD, "Moderate growth is underpinned by a strong macroeconomic framework. Commitment to fiscal targets, sound debt management, a flexible exchange rate and an appropriate monetary policy stance have supported moderate growth [...]"¹.

In connection with the foregoing, the President recently ensured that there will not be a significant tax reform that increases the tax rates or creates new taxes, during the next years.

Hence, the Mexican market is an attractive target for new investors and foreign entities that wish to expand their businesses in new countries.

Setting up a business

The principal schemes of business in Mexico are Companies, Branches of Foreign Corporations and Partnerships. Companies in Mexico must be incorporated and duly registered before a Notary Public and the Local Public Property and Commerce Registries, respectively.

The companies are incorporated by means of their corporate bylaws, which contain detailed and clear provisions regarding the name of the shareholders or partners of the company, corporate structure, company's purpose, duration, capital stock, corporate domicile, management, reserve fund, dissolution and liquidation process of the company, among others.

Legal types of business entities

The main types of Companies in Mexico are the following:

1. Limited Liability Company (Sociedad de Responsabilidad Limitada, S. de R.L.).
2. Stock Corporation (Sociedad Anónima, S.A.), from this type of companies derives the Investment Promotion Corporation (Sociedad Anónima Promotora de Inversiones, S.A.P.I.), among others.
3. Simplified Joint-Stock Company (Sociedad por Acciones Simplificada).

For international businesses, we recommend using one of the following

¹ <https://www.oecd.org/economy/mexico-economic-snapshot/>

types of legal entities to carry out their commercial activities in Mexico:

(i) Stock Corporation with Variable Capital (Sociedad Anónima de Capital Variable) (the "S.A. de C.V.") or

(ii) Limited Liability Company with Variable Capital (Sociedad de Responsabilidad Limitada de Capital Variable) ("S. de R.L. de C.V.").

The aforementioned legal entities are the most common and convenient types of commercial entities used in Mexico to conduct businesses. The addition of the term "*capital variable*" after the name of the company, indicates that said entity may increase or decrease its capital stock within the provisions set forth in the Corporate Bylaws.

Shareholders in stock corporations and partners in limited liability partnerships are only responsible up to the amount of their contributions. Either in individuals or corporation's cases, it is necessary to have two shareholders, at least.

Companies with a variable capital are commonly used due to their adaptability, which translates in the possibility of decreasing or increasing the stock capital after its incorporation.

Procedure of setting up a business Incorporation

The incorporation of a business must be formalized before a notary public after having obtained the corresponding authorization to use the name chosen for the company. This authorization is provided by the Ministry of Economy (see below).

Authorization from the Ministry of Economy

The Ministry has a registry of corporate names of all entities incorporated pursuant to Mexican laws. A person must file an application to the Ministry to obtain an authorization to use the name chosen for the company. The Ministry usually authorizes the use unless the proposed name is already in use or is

similar to the name of an existing company.

Number of Shareholders or Partners

Both the S.A. de C.V. and the S.R.L. de C.V. need to be incorporated by at least two shareholders or partners respectively. The shareholders or partners can be individuals or entities, either Mexican or foreign. In the event that any of the shareholders or partners is not a Mexican national, the provisions of the Foreign Investments Law described below would need to be followed.

To expedite the incorporation process, any foreign shareholder or partner should grant a bilingual special power of attorney (the "Power of Attorney") in favour of members of the law firm authorizing them to take the necessary incorporation steps before the notary public and the Mexican authorities. If not, the foreigner would need to travel to Mexico to appear before the notary public and Mexican authorities. Should the foreigner choose to appear in person in Mexico, such person may need to apply for a visa depending on its nationality.

Once the authorization from the Ministry of Economy is approved for the use of the proposed name for the Company, the law firm will need the corresponding documentation regarding this matter, and have it executed before a local notary public and apostilled/legalized to be valid in Mexico.

The Incorporation Deed

The Incorporation Deed (Acta Constitutiva) is the document executed before the Notary Public to formally create the company, which has to be registered with the Public Registry of Commerce of the company's domicile.

The incorporation deed must contain, amongst others, the following:

- a. The names, nationality and domicile of the initial shareholders (individuals or corporations).
- b. The purpose of the company.
- c. The corporate name (with the permit of the Ministry of Economy.

- d. The term.
- e. The amount of capital. The applicable law does not require a minimum amount of capital to incorporate an S.A. de C.V. or an S.R.L. de C.V. However, we recommend having an initial capital sufficient to cover the initial operations.
- f. Corporate domicile.
- g. Choice of management and appointment. The company can be managed by a manager or a board of directors.
- h. Appointment of officers.
- i. Approval of issuance of powers of attorney granting authority to one or more officers or managers to represent the company (see section 4 below for additional information).
- j. Appointment of one or several statutory auditors (comisarios/interventores). The manager, directors and officers may be non-Mexican. If so, such individuals will need to apply for an authorization to do business in Mexico.
- k. Powers reserved to the shareholders through General Ordinary and Extraordinary Shareholders' Meetings.

Legal representatives and attorneys in fact

Every Mexican entity acts through its legal representatives and attorneys in fact. The legal representation derives directly from the law and is bestowed to the administrative body of the company. Powers of attorney on the other hand must be granted by an express resolution of the company in favour of certain person(s).

Under Mexican law, powers of attorney may be general or special in scope and for different purposes: (i) for litigation and debt collection; (ii) for management acts; (iii) for ownership acts (disposal of assets); or (iv) to issue negotiable documents, such as promissory notes or checks, opening and closing bank accounts. Said powers of attorney may be granted to one or several persons, who shall act jointly or severally, as ordered by the company. Several levels of authority may be established in such a

manner that an attorney in fact may be required to act individually or jointly, as is more convenient to the company.

Foreigners may serve as attorneys in fact of the company. Foreign representatives will need an authorization to do business issued by the Ministry of Public Affairs.

Registration before the tax authorities

A new company must obtain a federal tax identification number by filing an application with the Federal Tax Registry of the Ministry of Finance and Public Credit to be able to do business in Mexico. The application must include a domicile within Mexico.

Registration before the Foreign Investments' National Registry

Pursuant to the Foreign Investment Law, the Mexican entity incorporated by foreign investors must be registered with the Foreign Investments' National Registry. Additionally, the entities with foreign shareholders are obliged, if applicable, to file an annual renovation of their registration in the abovementioned registry, as well as a quarterly update reports under the applicable legislation.

Opening a bank accounting

Once the company is incorporated and registered before the tax authorities, and in order to proceed with the opening the Bank account, the following information and requirements are necessary:

- ✓ Incorporation deed;
- ✓ Certification issued by the Notary Public informing that the incorporation deed is in process to be registered before the Public Registry of Commerce;
- ✓ Public deed containing the powers of attorney granted in favour of the authorizing persons;
- ✓ Tax ID of the company;
- ✓ Utility bill of the physical office;
- ✓ ID of the authorizing persons.

Financial year of taxes and financial accounts

The fiscal year is equal to the calendar year, excepting these companies which were duly notarized after January 1st of the corresponding year.

In Mexico, there are different types of taxes according to the federal, state and municipal level. Among the federal taxes are Income Tax (Impuesto sobre la Renta), Value Added Tax (VAT or Impuesto al Valor Agregado, IVA for its Spanish acronym), Special Tax on Production and Services (Impuesto Especial sobre Producción y Servicios, IEPS for its Spanish acronym), General Taxes on Imports and Exports.

The General Mexican Corporate Law provides that an Ordinary Shareholders/Partner Meeting must be held within the first four months following of the closing of the corporate year (December 31), in order to approve, among other issues, the report of the Board of Directors, the financial statements for the prior year, the designation or re-election of Directors and Statutory Auditors.

Ministry of Finance and Public Credit (Secretaría de Hacienda y Crédito Público) is the authority responsible for the collection of taxes. Every year, the Mexican Congress updates the existing tax laws, as the Federal Tax Code (Código Fiscal de la Federación) which contains supplementary legislation, applicable in those cases that the tax laws are not clear enough. Usually, non-residents, whether corporations or individuals are subject to pay taxes on incomes arising from a Mexican source.

Accounting and auditing

In accordance with the current Mexican Fiscal Code an external auditor is no longer mandatory for legal entities. Instead, it is optional for those companies that exceed any of the following in the prior tax year:

- Incomes of more than \$122'814,830.00 Mexican pesos
- Net assets more than \$97'023,720.00 Mexican pesos.
- An average of 300 or more employees during the corporate year

It is important to mention, that it must be performed by an independent authorized auditor.

Fiscal years for tax purposes

The fiscal years are equal to the calendar years. However, when a legal entity begins to carry out their business activities in a date that is different from the beginning of the calendar year, or terminates their business activities during a date that is different from the end of the calendar year, said entity's year will be deemed as *irregular*.

Accounting and auditing

Every legal entity is obligated to do accountancy and bookkeeping. Their accountancy must be kept for 10 years.

Legal entities are not obligated to audit their financial statements; nonetheless, it is a common practice for large entities to do so.

The statute of limitations for the tax authority to audit a legal entity is 5 years.

Economic and fiscal incentives

The Mexican government has recently issued some tax incentives that aim to enhance economic growth in the Mexican market.

One of those incentives, for instance, is a reduction of the corporate tax rate and the value added tax rate for legal entities that carry out business activities in the Mexican northern border (which neighbours with the USA).

There are some very important tax incentives regarding business activities related with trusts whose business activities are to perform real estate developments for buildings or malls.

In this sense, it is important to mention that our country has held several treaties to avoid the double taxation.

Incentives for foreign investors

Several free trade agreements have been signed, leading to competitive advantages for investors who wish to establish a business in Mexico.

In order to boost the Mexican bonds market, the President issued a tax incentive regarding foreign residents who acquire corporate bonds that have been issued through the Mexican Stock Exchange by Mexican legal entities.

Said incentive allows Mexican legal entities that issue said bonds to withhold at a 0% income tax rate when performing interests' payments to the foreign residents who acquired the bonds.

Arm's length principle

Like other Members of the OECD, the Mexican tax legislation sets forth an obligation for Mexican taxpayers to operate at fair market value prices with their related parties. The appropriate way to support said prices is a transfer pricing study that follows the general methodologies established by the OECD.

Taxation

Federal corporate income tax applies to Mexican residents on the income from worldwide sources, as well as to foreign residents on the income attributed to their PEs located in Mexico and from their income perceived from source of wealth in Mexico.

All legal entities are subject to the tax rules applicable to Mexican corporations (unless specifically ruled out, such as non-for-profit organizations).

Mexico follows a management approach to tax residency rather than solely based on country of incorporation.

Income is generally acknowledged on an accrual basis. However, the service revenues of non-for-profit entities that render professional services (e.g. law and accounting firms) are reported on a cash flow basis.

The main difference between the calculation of net income for bookkeeping and tax purposes is that the procedure to recognize inflationary effects is different (e.g. tax adjustments for inflation).

Transactions between related parties must be carried out complying with the **arm's length** principle (market value).

VAT

VAT is a "cash basis" tax. The general VAT rate is 16% for the following acts or activities within Mexican territory:

- Alienation of assets.
- Rendering of independent services.
- Granting of temporary use or enjoyment of assets; and,
- Import of goods and services.

Subject to certain rules, an entity that is required to collect and remit VAT, may offset its VAT liability against VAT paid to suppliers of goods and services, and the amount paid on imported goods.

Some supplies are zero rated, such as foodstuffs, water, agricultural supplies, books and magazines, as well as exports, among others.

Some supplies are VAT exempt such as real estate, lands, financial services, insurances, cultural exhibitions and events, among others.

VAT returns, detailing sales and purchases, must be submitted on a monthly basis and are considered as definitive.

Such VAT returns should be filed on day 17 of the month following the period that has ended, and any tax due must be paid by this date too. Returns are filed electronically.

Additionally, as the case may be, favourable VAT balances can be requested from the Mexican Tax Authority, or else, they might be offset in future periods against VAT due.

Taxable income

Entities residing in Mexico, including joint ventures, shall accrue as taxable their total revenues in cash, in kind, in services, in credit and those of any other nature obtained in the fiscal year, including those proceeding from their establishments abroad.

Corporate income tax

The income tax is a federal tax. There are no corporate state or local income taxes. Companies are required to pay income tax on worldwide income, regardless of location or source, at the 30% general rate.

Deductible expenses must satisfy several general (e.g., to be "strictly indispensable" for the business activity of the taxpayer) and specific requirements.

Certain deductions are allowed, such as returns, discounts and rebates on sales, cost of sales, net expenses, investments (i.e., depreciation or amortization of fixed assets, deferred expenses and deferred charges), among others.

Technical assistance, royalties, and interest payments. In order to be deductible, payments of technical assistance fees and for the transfer of technology or royalties must be made directly to companies with the required technical capabilities to provide the corresponding service and should correspond to services actually received.

A deduction for technical assistance, interest, or royalty payments is not allowed when paid to a foreign entity that controls or is controlled by the Mexican entity and (i) when and to the extent that the recipient is a flow-through entity whose owner or owners are not subject to tax in its jurisdiction, (ii) the recipient country of tax residence considers the payment to be disregarded, or (iii) the recipient does not include the payment as part of its taxable income under its jurisdiction's rules.

Payments made to overseas group entities may be subject to withholding tax (ranging from 4.9% to 40%), or may be entitled to double tax treaty relief.

The income tax has to be paid on an annual basis before the Mexican Tax Authority; however, taxpayers have the obligation to submit monthly advanced income tax payments, which are calculated on current year's revenues multiplied by a "profit factor" determined

on prior year's figures (taxable income/total revenues).

Once a corporation has paid the income tax, after-tax earnings may be distributed to the shareholders with no tax charge at the corporate level.

If a corporation makes a distribution out of earnings that for any reason have not been subject to income tax, such as distributions of book earnings (i.e. not yet recognized for tax purposes in Mexico), the corporation will also be subject to income tax on the grossed-up distributed earnings (gross-up factor is 1.4286).

Tax paid on dividends distributed in excess of after-tax earnings account can be credited against the income tax of the year or in the two fiscal years following the year in which the tax on the non-after-tax earnings account distributions was paid. The after-tax earnings account of the tax years in which the credit is applied must be reduced by an amount equal to the grossed-up dividend distribution.

Net operating losses may be carried forward for a period of ten years. No carryback is allowed. They will also be subject to inflationary effects.

There are no limitations on the amount of losses that can be used to offset each year's taxable income, except for the NOLs derived from the disposition of shares.

Salaries income tax

Individuals who receive payments as salaries will be subject to a progressive income tax rate. Said rate can vary from 1.92% to 35%. The payments will be made via withholding. To that effect, employers must withhold the corresponding amount and submit it before the Mexican Tax Authority when the payroll is performed.

Registration procedures

Legal entities are obligated to register before the Mexican Tax Authority and are provided with a Tax ID number.

Communication with the tax authorities is largely done in an electronic way.

Customs

Mexican Customs Law establishes that all imports are subject to custom duties and VAT. The VAT rate on imports is 16%.

General Imports Duty is calculated by applying the corresponding rate defined by the type of merchandise imported. Goods can be imported on a temporary or permanent basis.

Profit sharing participation (PTU)

Profit sharing participation with employees is 10% of profit. The procedure to determine the profit for PTU purposes is –in general– similar to the one followed to determine the profit for income tax purposes.

Excise tax

The Excise Tax Law sets forth substantial federal excise rates on the importation and/or sale of certain taxable items, such as gasoline, beer, wine, spirits, and cigarettes and other tobacco products, and on certain services related to these activities, such as commission, mediation, and distribution of excise taxable items, as well as services for raffles, gambling and telecommunications.

In general terms, goods are exempt from excise tax when exported. The input excise tax paid by exporters on their purchases is not creditable, and that tax becomes an additional cost.

Excise tax is payable (output tax) and creditable (input tax) on a cash basis. It is payable on the date that the charge invoiced is collected from the client and can be credited when the respective payment is made to the supplier. On imports, excise tax is creditable when paid at the customs offices.

Among other obligations, excise tax taxpayers must file information returns before the Mexican Tax Authority, periodically.

Withholding taxes

The most common withholding tax is the dividend tax. The tariff is usually 10%, but it can be reduced for up to 5% or even 0% by means of applying the benefits set forth in some treaties to avoid double taxation, as long as the requirements set forth in the corresponding treaty are fulfilled.

HR/ Labour Law

Employment law

The Federal Labour Law ("FLL") has been effective as from 1970, and applies to all employers and companies. Its provisions govern existing labour relations. The FLL sets forth the minimum rights and conditions to be granted by the employer in favour of the employees.

Pursuant to the FLL, any individual that renders services to another individual or entity is considered an employee provided that such individual works under the supervision of, or is subordinate to, the contracting individual or entity and receives a salary in exchange for his/her work.

Main labour provisions:

Individual employment contracts

Employers must mandatorily execute written individual employment contracts setting forth the working conditions applicable to each employer-employee relation as well as the Unique Population Registry Key ("CURP") and the Taxpayer Federal Registration ("RFC") of the employer and the employee.

The employment contract must specify if the employment relation is for a task or a determined period of time, for a season, for initial training, or for an undetermined period of time, and as the case may be, if it is subject to a trial period.

Working Hours

Under the FLL, the maximum work week is determined depending upon the work shift. There are three types of work shifts:

- a) Daytime shift: from 06:00 A.M. to 08:00 P.M., with a maximum of 48 eight hours per week.

- b) Night shift: from 08:00 P.M. to 06:00 A.M., with a maximum of 42 two hours per week.
- c) Mixed shift: includes hours of the daytime and night shifts. The night shift hours may not exceed three and a half hours; otherwise, the shift shall be considered a night shift. The maximum number of hours permitted per week is 48.

Social security

Generally, employers and employees are required to make contributions to the social security system. To that effect, employers must withhold a bi-weekly amount when performing the payroll.

These contributions are based on daily salary caps that are determined based on a multiple of the minimum daily salary in the area in which the work is performed.

When starting a business and employing staff, legal entities must register each employee before the social security authorities (Mexican Institute of Social Security "IMSS"), and in this sense pay the corresponding fees regarding the benefits of social security, which cover job-related risks, general illnesses and maternity, disability and life, retirement, old age and unemployment at an advanced age, children's nurseries, among others.

Pension

The FLL sets the employees and employers rights and obligations; employees' rights go well beyond those provided in many industrialized countries. It also rules working conditions such as business days per week, overtime, mandatory non-business days, vacation leave, Christmas bonus, retirement, housing, training, profit sharing, union plans, pension plans, social security, health and safety matters, so on.

Foreign Employees

The FLL provides that at least 90% (ninety percent) of the employees of each company must be Mexican, except directors, administrators and general managers. Foreign employees are subject to the same legal requirements

as Mexican employees and are treated equally regarding both benefits and penalties.

Local Taxes

In general, the most relevant state and local taxes in Mexico are the following:

- Automobile property tax;
- wage tax;
- lodging tax;
- annual property tax; and
- real estate transfer tax.

The applicable tax rates depend on the legislation of the state where the employee, automobile or real estate is located.

Visa and work permits

Migration in Mexico requires VISA excepting for tourism purposes or foreigners that will not stay longer period of 180 days, the VISA gives authorization from the consular office indicating validation to obtain a migration status in order to fulfil an obligation and get the proper residence condition.

As set forth on Mexican Migration Law, foreigners may stay on Mexico, under the following residence conditions:

1. Visitor with license to perform business.
2. Frontier Worker Visitor.
3. Temporary Resident
4. Permanent Resident

Visa for Employment Offer:

In order to process a Visa for employment offers, it is necessary to file the following documentation in original and a copy:

1. Employment Application Registry
2. Legal Representative ID
3. Foreign Passport
4. Employment offer letter that specifies charge according to the National Classification of Occupations System (SINCO for its Spanish acronym), as well as, temporality required, workplace, and wage amount.
5. Authorized persons ID to process and receive notifications.

Employment Application

Prior the issuance of an employment offer, it is mandatory that the Mexican company is registered before the Immigration National Institute.

Therefore, it is necessary the filing of the original and a copy of the following documents in order to obtain the Employment Application Registry:

1. Incorporation deed
2. Public Deed by which, are granted the powers and authorities to the legal representatives (in case that those are not contained in the Incorporation deed)
3. Legal Representative's ID.
4. Proof or address or Lease Agreement.
5. Federal Taxpayer Registry.
6. Last Annual Tax Return (only copy)
7. Last Monthly Tax Return (only copy)
8. A letter with the list of all the employees, including its nationality.

Contact us

The information provided in this guide cannot be exhaustive and we recommend anyone considering doing business in Mexico should seek professional advice from our member firms before making any business or investment decision.

Contact our member firms in Mexico to further discuss your requirements:

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