LATIN LAWYER REFERENCE TAX IN CROSS-BORDER DEALS 2019

Mexico

Ana Paula Pardo and Jorge San Martín
SMPS Legal

DECEMBER 2018

LATIN LAWYER INSIGHT

1 In your jurisdiction, can the acquisition of a domestic target limit the target's use of existing tax attributes, such as net operating loss carry forwards or tax credits? Are there strategies or structures to preserve such attributes?

When planning on acquiring a target company that is a Mexican tax resident, the different alternatives available for such purposes should be carefully evaluated given that the tax consequences arising from the transaction could vary depending on how the acquisition is structured. For instance, if the acquisition of a target company is structured as a stock deal, the purchaser could benefit from existing tax attributes. However, it is worth noting that the existing tax liabilities would also be retained.

If a target company acquired in a stock transaction (with a change of stockholders therein) had pending tax loss carry-forwards and its income in the previous three years is less than the amount of such losses updated for inflation at the end of the year in which the change of stockholders took place, the relevant tax losses could only be carried forward in order to offset tax profits that correspond to the same business activities from which the tax losses derived.

The acquisition of a Mexican target company could also be structured in the form of an asset deal. This strategy would allow the purchaser to handpick the assets deemed to be valuable for the operation of the target company, while discarding assets considered as a burden. Furthermore, in an asset deal tax authorities could allow the purchaser to claim certain deductions when assessing income tax due as consequence of the relevant transaction (certain exception apply).

Nonetheless, the purchaser involved in an asset deal could be held as jointly liable for up to the full price paid for the businesses' assets, for any and all contributions owed by the target company before it was acquired acquisition. Additionally, existing tax attributes cannot be transferred in such deals.

Concerning the acquisition of a Mexican target company as consequence of a merger, the following should be noted. First, provided that the entities involved in the merger are Mexican tax residents and that certain requirements are met, such transaction could be treated as a tax-neutral. Second, tax attributes of the merged company could be incorporated to the surviving company. However, certain limitations should be observed. For instance, tax losses generated at the level of the merged company would not be transferrable to the surviving entity. Likewise, tax losses of the surviving company could only be applied against profits deriving from the same type of business activities from which the first were generated.

2 When companies that are resident in your jurisdiction are sold to foreign investors, is it more common to sell stock or assets?

As per mentioned in question 1, different tax treatments can apply to the acquisition of a Mexican resident target company depending on the way in which the transaction is structured. Therefore, the virtues and disadvantages of conducting either a stock or asset deal should be thoroughly analysed as regards the target company.

Be that as it may, in general terms, purchasers often opt to structure the acquisition of Mexican target companies as stock deals given that such operations tend to be more tax-neutral than asset deals. That is, while stock transactions are generally not subject to value added tax, asset deals are commonly subject thereto and even subject to other federal or state taxes whenever real estate is involved in the relevant transaction.

Likewise, a stock deal could allow the purchaser to benefit from the existing tax attributes of the target company (keeping in mind that any tax liabilities existing at the moment of the operation would also be transferred along with its potential liabilities).

Nevertheless, it should be noted that tax consequences could arise at the level of a non-resident purchaser in so far as certain tax requirements are not met. Indeed, in cases where stock issued by a Mexican target company is acquired by a non-resident purchaser and tax authorities determine that the purchase price was below market value by more than 10 per cent, income tax could be due.

Regarding asset deals, purchasers are entitled to select valuable items and discard others deemed as not relevant. Moreover, tax authorities could permit purchasers to claim certain deductions when determining income tax due as consequence of the transaction at hand.

However, asset deals tend to trigger value added tax or other federal or state taxes when real estate is involved in the transaction. Additionally, the acquirer of the ongoing business' assets could be held as joint liability for any and all tax liabilities existing prior to the acquisition, for up to the business' value.

Consequently, regardless of the way in which an acquisition is structured, it is of the outmost importance to conduct thorough due diligences to identify the strengths and potential liabilities in relation to the transaction. In particular, since such attributes and liabilities could serve as key elements during the relevant negotiation. Likewise, the corresponding agreements should be vested with adequate warranties to minimise the purchaser's exposure to potential liabilities and to entitle the purchaser to seek indemnity.

3 Are there particular structures that generate a step-up in the tax basis of assets in a tax-efficient manner?

In stock deals, no step-up in the tax basis could be considered to exist in connection with the assets of the target company. That is, the step-up could only occur in regard to the consideration paid for the relevant stock (the price of the assets of the target company is not altered).

On the other hand, the tax basis in the acquisition of a target's business assets would be the amount effectively paid and allocated to each asset. Consequently, a step-up in the basis could be deemed to exist.

Moreover, the tax basis in asset deals could be offset by certain deductions such as fixed assets, certain intangible assets, deferred costs or charges, preoperative expenses, technical assistance or royalty fees according to the corresponding limits set forth in the Mexican Income Tax Law.

4 Are there structuring opportunities that would enable a foreign acquirer to provide equity consideration to the shareholders of a domestic target in a tax-deferred manner? Are the rules similar if both the acquirer and the target are domestic?

Generally speaking, no particular tax benefits could be achieved by the issuance of equity as consideration for the acquisition of a target company. In fact, even if the issuance itself could avoid triggering taxes, the tax consequences faced by the recipient of such shares could be quite similar to those that would have been triggered by an ordinary cash deal.

Therefore, issuing stock as consideration for such a transaction could mainly be deemed as beneficial in cases where cash shortages are a determinant factor in the negotiation, but not necessary convenient from a tax perspective.

Furthermore, transactions structured as share exchanges tend to be inefficient from a tax perspective since a double sale could be deemed to have taken place. Accordingly, the operation could be considered as taxable for both parties involved. Nevertheless, share exchanges could prove to be efficient from a tax standpoint in cases where corporate restructures are being planned with respect to legal entities of a same group and in so far as specific requirements are met.

5 Can management generally roll over its equity in an acquisition in a tax-deferred manner? Are there certain circumstances where a tax-deferred rollover is difficult or impossible?

Assuming certain requirements are met, tax authorities could authorise the deferral of income tax relating to profits derived by a non-resident from the disposal of stock issued by a Mexican legal entity performed between companies of the same corporate group. The resulting income tax would be payable within the following 15 days after that in which a second transaction by means of which the stock in question ceases to belong to a company of the same corporate group takes place.

6 Which holding company structures are typically used by foreign investors to acquire domestic targets in your jurisdiction?

Aside from the strategy to be followed in order to acquire a Mexican resident target company (ie, stock or asset deal), foreign investors should also consider the potential tax consequences that could arise depending on whether the acquisition is directly or indirectly completed. That is, depending on the vehicle used to acquire the target company.

If a non-resident investor decides to directly acquire a domestic target company (or uses another foreign legal entity or vehicle in order to do so), the wide range of tax treaties concluded by Mexico could provide relief in relation to the allocation of resources between the holding legal entity and the target company (for instance, when dividends or interests are paid) by means of reduced withholding rates, tax credits or even certain exemptions depending on the relevant treaty.

Regardless of the foregoing, it is important to point out that in cases where a foreign investor directly purchases the assets that are essential for the target company and decides to continue the operation thereof, a permanent establishment of the non-resident could be deemed to have been set up within national territory. Consequently, all income attributable thereto could be subject to income taxation in Mexico.

On the other hand, in cases where a foreign investor uses a Mexican legal entity to acquires stock in the target company, the cost of the transaction would firstly be generated at the level of the holding company as consequence of the capital increase decreed for purposes of the purchase and an indirect cost could be generated at the level of the target company.

The above-mentioned transaction could result in a tax-wise adverse or beneficial strategy, depending on several factors such as the financial position of the domestic target company. Therefore, the importance of conducting thorough legal and tax due diligences is once again outlined.

Foreign investors could also be inclined to plan the acquisition of a Mexican target company by means of special purpose vehicles or joint ventures in order to mitigate their exposure to potential tax liabilities.

Either way, when designing their investment strategy non-residents should always bear in mind that while Mexican tax residents (individuals or legal entities) are subject to income tax on a worldwide basis, foreign tax residents could be subject to income tax in Mexico both for any and all income whose source is deemed to be located in Mexico and any and all income attributable to a permanent establishment set up within national territory.

7 What types of tax benefits typically arise in connection with transactions in your jurisdiction? Do the parties typically address allocation of such benefits in the transaction documents?

Depending on how a transaction is structured, certain benefits such as tax deferrals or tax-neutral restructures (mergers or spin-offs) could be achieved. Additionally, corporate restructures involving Mexican resident entities could be subject to a beneficial tax treatment.

Concerning non-residents involved in a transaction, Mexico's tax treaty network could provide tax benefits in the form of tax credits, reduced withholding rates or even tax exemptions could be attained.

Nonetheless, it is worth noting that the possibility of profiting from such tax benefits depends on the nature of the relevant transaction and that of the parties involved therein, on how it is structured and on the compliance with the requirements set forth in the applicable laws. Bearing this in mind, tax benefits themselves do not tend to be agreed upon or incorporated into transaction documents given that, strictly speaking, they are not the subject matter of agreements.

8 Do real estate transactions (or transactions involving real estate holding companies) create special tax issues in your jurisdiction?

Mexican tax laws do provide special tax treatments whenever real estate is involved in a transaction. In general terms, whenever real estate is transferred both federal and local taxes could be triggered. Additionally, real estate in Mexico is subject to property tax on many states within the Republic.

As per mentioned in question 6, non-residents could be liable for income tax in Mexico with respect to any Mexican-sourced income they derive and/or for all income attributable to a permanent establishment of theirs set up within the country.

In consideration of the foregoing, a transaction could be deemed to have its source in Mexico whenever shares or securities that represent the property over assets that were issued by a Mexican tax resident are sold or more than 50 per cent of the book value thereof directly or indirectly derives from real estate located within national territory. Therefore, even in cases where such a transaction is exclusively entered into by non-resident parties, the source thereof could be considered to be located in Mexico if any of the aforesaid conditions are met. Consequently, the relevant transaction could be subject to income tax in Mexico.

Furthermore, assuming certain legal requirements are met, trusts whose purpose consists of acquiring and constructing real estate in order for it to be leased, acquiring the right to derive income resulting from the lease thereof, or financing such operations could be entitled to apply a tax incentive incorporated to the Mexican Income Tax Law.

Likewise, under the understanding that certain legal requirements are met, real estate developers could be allowed to deduct the cost of acquisition of land or lots used for their corporate purposes in the same year in which they were acquired.

9 Are there other categories of transactions (involving other types of assets or specific types of entities) that raise distinctive tax issues (for example, in the United States, transactions involving real estate investment companies and regulated investment companies)?

Since 2006, a tax incentive for the development of private equity investments in Mexico was included in the Mexican Income Tax Law. However, it was seldom used owing to its lack of versatility for purposes of structuring operation of the like.

Nevertheless, as of 2016, the legal provisions that regulate these investment vehicles have been amended for purposes of addressing previous limitations, thus transforming it into an attractive option to invest in Mexico. In general terms, these vehicles are considered as tax transparent, therefore allowing a pass-through treatment to be applied with respect to income derived through them. It is worth noting that as a consequence of its tax transparency, the corresponding treatment could greatly vary depending on several factors such as the tax residency of the investors, the income items that are earned (ie, capital gains, dividends, interests) or the existence of tax treaties that could provide relief.

10 Does your jurisdiction impose any distinctive taxes (eg, non-income taxes) that need to be specifically addressed when structuring and documenting cross-border deals?

Aside from income tax, value added tax and state taxes on the acquisition of real estate should be kept in mind when structuring cross-border deals. Such transfer taxes will be furtherly addressed hereunder.

11 Do withholding taxes apply to transactions either from or into your jurisdiction?

As previously mentioned, whilst Mexican tax residents are subject to income tax on a worldwide basis, non-residents could be liable for income tax in Mexico whenever they have a permanent establishment within national territory (income attributable thereto) or for any Mexican-sourced income they derive.

Bearing the foregoing in mind, Mexican tax residents or even permanent establishments of non-residents could be required to withholding the corresponding income tax on transactions entered into with non-residents.

Additionally, individuals and legal entities that sell goods, render independent services, lease goods or import goods or services on home territory would be subject to VAT in Mexico (certain exceptions set forth in the Mexican Value Added Tax Law apply).

What is more, in certain cases VAT ought to be withheld. For instance, whenever Mexican tax residents (individuals or legal entities) acquire or lease goods from a non-resident without a permanent establishment in Mexico, the relevant Mexican tax resident could be required to withhold, or whenever a legal entity receives services from an individual.

12 If withholding taxes apply to a transaction, what are the rates? Can they be reduced by treaty or are there structuring techniques or certification processes to avoid or mitigate the tax cost?

Concerning income tax withholdings, the corresponding rates can vary greatly depending on the transaction at hand or the concept for which the relevant payment is being made. Nonetheless, non-residents entering into transactions with a Mexican party should bear in mind that the broad range of tax treaties executed by Mexico could provide relief in the form of reduced tax rates, exemptions or tax credits.

Furthermore, in some cases and depending on the way the relevant transaction is structured, no Mexican source would be deemed to exist and consequently, no income tax would be due.

With respect to VAT, it is worth noting that the general tax rate is of 16 per cent. Additionally, certain operations could be subject to a zero per cent tax rate or even exempted thereof. Distinguishing between operations subject to a zero per cent tax rate and those exempted from such indirect tax is of paramount importance given that only the first would allow value added tax crediting.

13 Are VAT or transfer taxes significant? If so, in which types of transactions?

VAT is the most relevant federal transfer tax in pursuance of Mexican laws. It could be triggered whenever individuals or legal entities, within national territory, perform any of the following activities: sell or lease goods, render independent services or import goods or services. Nonetheless, depending on the goods or services, the relevant operation could be subject to a zero per cent tax rate or even exempted from value added tax. For instance, while the sale of patented medicines or specific nourishments, could be subject to a zero per cent tax rate, the sale of land or constructions that are to be used as dwellings or equity and certain securities could be exempted from the indirect tax in question.

It should be noted that between operations exempted from VAT and those subject to a zero per cent tax rate, only the latter could be used for tax crediting purposes. As previously mentioned, the general value added tax rate is of 16 per cent.

Moreover, non-residents should be aware of the fact that specific legal presumptions are set forth in the Mexican Value Added Tax Law in order to determine when a transaction should be deemed as performed within Mexican territory and thus, subject to taxation.

In this regard, goods could be presumed to have been sold within Mexican territory: (i) if the relevant goods are located therein at the time when they are shipped to the purchaser; (ii) whenever no shipment has been made, if the seller materially delivers the relevant goods to the purchaser within national territory; or (iii) goods subject to Mexican certifications or registrations sold by a Mexican resident seller or by a foreign resident with a permanent establishment in Mexico, could be deemed to have been sold on domestic territory in spite of them actually being sold abroad. Concerning intangible goods, the transaction would be deemed to have taken place within Mexican territory if both the seller and purchaser reside therein.

As for the rendering of services, and in general terms, they could be deemed to have been performed in Mexico if the relevant service is totally or partially rendered by a Mexican resident within national territory. However, in the case of

international transportation, the service could be deemed to have been performed in Mexico whenever the relevant journey initiates within Mexican territory (regardless of the shipping agent's residence). Concerning aerial international transportation, only 25 per cent of the relevant service could be deemed to have been rendered within Mexican territory.

Aside from VAT that is collected on a federal basis, certain state taxes could be triggered as consequence of the transfer of real estate.

14 Are there strategies to mitigate VAT or transfer taxes? What party typically bears the costs of VAT and transfer taxes?

As per mentioned above, stock deals tend to be considered as VAT-free transactions.

Additionally, and in general terms, cross-border transactions could only be subject to value added tax in Mexico if they are deemed to have been carried out therein (materially or in terms of the legal presumptions set forth in the Mexican Value Added Tax Law).

Therefore, any transaction that cannot be considered as performed within national territory would not be subject to value added tax in Mexico. Consequently, value added tax could be greatly mitigated or even avoided depending on the terms agreed upon by the parties. Relating to the sale of goods, no value added tax would be triggered if the relevant goods are not located within national territory when shipped to the corresponding purchaser or are not materially delivered to the purchaser therein. As for services rendered by a Mexican tax resident, they would not be subject to value added tax if they are rendered outside of Mexican territory.

Moreover, specific activities such as the Maquila industry could be subject to beneficial value added tax treatments.

Owing to its indirect nature, the economic cost of value added tax is usually absorbed by the purchaser or recipient of the taxed activity in a transaction.

15 What is the statute of limitations for tax claims in your jurisdiction?

The general statute of limitations for tax liabilities in Mexico is five years. However, if tax authorities consider that a taxpayer has deliberately failed to comply with certain formal tax obligations such as registering before the Federal Taxpayers Registry, duly keeping accounting records or giving notice of any change of tax domicile, the statute of limitations could be extended to 10 years.

16 In your jurisdiction, can a target be liable for taxes of other members of the consolidated group of which it was a member prior to an acquisition? Is the tax authority likely to assert such a liability against a target?

As of 2014, an optional tax regime for corporate groups was incorporated to the Mexican Income Tax Law. In general terms, the tax regime in question consists of an integrating company, that is, the holding company, and its integrated companies (subsidiaries or legal entities in which the holding company participates). Roughly speaking, the optional tax regime allows the integrating company to differ a portion of the income tax due by the group for up to three fiscal years.

However, if any of the companies that tribute under the optional regime fail to comply with the requirements set forth in order for them to be considered as integrating or integrated companies, if a company that meets the requirements in order for it to be considered as an integrated company is not integrated to the group, or any of the legal entities that conform the corporate group comes out of the optional tax regime, the differed income tax would immediately be due as of the moment in which it would have been triggered and payable had the relevant entity not been subject to the optional tax regime.

Moreover, it is important to mention that several formal tax obligations ought to be duly complied with both by the integrating and integrated companies. Failing to do so could result in the integrating company being held as jointly liable for the differed income tax due by the integrated companies as of the moment in which it would have been payable had the corporate group not opted to tribute under the optional tax regime.

The foregoing should be kept in mind when acquiring a legal entity that forms part of a corporate group that tributes under the optional regime (or that should have been integrated), and specifically, concerning the acquisition of an integrating company, given that the target company could likely be held as jointly liable for income tax due by any or all of the companies of its corporate group.

Because currently not many corporate groups operate under the optional tax regime, it is safe to presume that tax authorities would likely assess any tax liability triggered by the acquisition of a legal entity that formed part of such a corporate group.

17 Is there a typical approach to pre-closing tax indemnification in your jurisdiction?

Considering that an acquiring party could be exposed to tax liabilities of a target company, it is of paramount importance for adequate representations and warranties to be incorporated to the relevant agreement in order to mitigate such contingencies. In this regard, it is fairly common for acquiring parties to negotiate indemnity clauses and in some cases, for such indemnities to be backed up with collateral or guarantees by the seller.

Thorough due diligences should be conducted prior to the acquisition to ensure protection for the purchaser and to identify strategic vantage grounds in the negotiation of the relevant transaction.

18 Are indemnification payments under a purchase agreement taxable to the recipient? Is an indemnity obligation in your jurisdiction typically grossed up for taxes?

Indemnity payments received both by Mexican tax residents and permanent establishments of non-residents set up within national territory could be considered as taxable income. Concerning foreign entities that receive indemnity payments, income tax due would be determined in consideration of the total amount of indemnity payments made in their favour by Mexican residents or non-residents' permanent establishments located within national territory. It is also worth mentioning that indemnification payments are not deductible for income tax purposes.

Indemnity obligations should be grossed up for tax purposes considering that that payable tax claims ought to be calculated to present value and could be subject to surcharges and fines over the principal amount that would considerably increase the amount of the relevant tax credit.

19 Under what circumstances would an investor in a target in your jurisdiction have a tax filing obligation in your jurisdiction solely as a result of its equity interest in the target company?

Non-resident shareholders or partners are not required to register before the Federal Taxpayers Registry in so far as the Mexican entity in which they hold equity files before the competent authorities a schedule detailing its foreign shareholders or partners, their tax residency, tax identification number and domicile within the first three months following the closing of each fiscal year.

Additionally, it is worth noting that income tax due by foreign shareholders or partners is generally payed by means of withholding by the Mexican legal entity and only in cases where the corresponding withholding is not made, would the foreign investor be formally required to file a definitive income tax return before Mexican authorities.

Nonetheless, it is important to point out that other formal obligations could be applicable outside of the tax arena. For instance, Mexican legal entities with foreign capital are required to register before the National Register of Foreign Investment and to disclose before the competent authorities the identity and place of residence of their investors.

20 In your jurisdiction, are there techniques to efficiently push debt down into subsidiaries in jurisdictions with high tax rates?

Debt pushdowns tend not to be considered as convenient practices in Mexico given that they are often challenged by tax authorities. In such operations, it is common for tax authorities to argue that substance ought to prevail over the form thereof and, if such standard is not met, tax liabilities would likely arise.

21 Describe any limitations, such as earnings stripping or royalty stripping rules, that limit the ability to effectively shift taxable income when structuring M&A deals.

Mexican tax authorities have been addressing profit shifting in accordance with the OECD developments (ie, BEPS action plan). In this sense, more stringent requirements have gradually been incorporated into the local set of laws.

Consequently, thin capitalisation, back-to-back and transfer pricing rules ought to be abided by when entering into any transaction. Additionally, stringent requirements concerning interest payments have been incorporated. As a result, it is common for tax authorities to try and recharacterise interest payments as dividends (thus applying to such payments the tax treatment of the latter) if specific legal requirement are not met.

22 Is there transfer pricing legislation in your jurisdiction that could apply to transactions among a target and its subsidiaries or affiliates? If so, how restrictive is it?

Mexico is an active member of the OECD. Consequently, OECD guidelines are generally abided by. In this regard, transfer pricing rules are no exception. In fact, the rules applicable in Mexico on this particular subject follow the guidelines and valuation methods set forth by the OECD.

Furthermore, as a result of the BEPS action plan recently developed by the OECD, more stringent requirements have been incorporated to local regulations. In general terms, legal entities should always enter into arm's-length transactions with their related parties (such as subsidiaries or affiliates), given that tax authorities are vested with authority to initiate audit procedures in cases where said standard is not complied with and discrepancies are believed to exist between the fair market value and the considerations agreed upon by the parties involved in the relevant transaction.

23 Does your jurisdiction have anti-deferral regimes that apply to operations and income of subsidiaries (for example, a controlled foreign corporation regime, whereby a parent entity would be required to take into income undistributed income earned by a subsidiary)? Do these regimes affect cross-border planning?

Pursuant to the Mexican Income Tax Law, specific controlled foreign corporation rules should be kept in mind when structuring any cross-border transaction that involves both Mexican resident entities and non-resident entities. In general terms, Mexican residents or non-residents with permanent establishments in Mexico could be required to pay income tax in terms of Title VI of the Mexican Income Tax Law (preferential tax regimes and multinationals) over income derived by means of foreign legal entities in which they directly or indirectly participate, as well as over any income obtained through foreign legal vehicles deemed as tax transparent.

In this regard, the Mexican Income Tax Law establishes that a Mexican resident or non-resident with a permanent establishment set up in Mexico could be subject to the above-mentioned tax regime in cases they derive income from legal entities that reside within jurisdictions considered to be subject to preferential tax regimes. For purposes hereof, a jurisdiction could be considered to be subject to a preferential tax regime in cases where: (i) income deriving therefrom is not subject to taxation in the relevant jurisdiction; or (ii) the income tax to which said income is subject to in the relevant jurisdiction is less than 75 per cent of the income tax that would be due in Mexico.

Generally speaking, taxpayers that receive income considered as subject to a preferential tax regimes are bound to keep specific accounting records concerning each of the legal entities through which they derive income, and to pay income tax due separating it from the rest of their accruable income.

Moreover, such taxpayers could be required to file informative returns concerning income derived from preferential tax regimes, on February of each fiscal year. It should be noted that failing to lodge the aforesaid informative return for more than three months after the date in which it should have been filed, or filing it incompletely could eventually be considered by tax authorities as a criminal offense sanctioned with up to three years in prison.

24 Are there exit strategies, besides stock or asset sales, that are used in your jurisdiction to achieve tax benefits?

Capital decreases in a legal entity could prove to be effective disinvestment strategies given that, depending on the financial position of the relevant entity, its tax attributes could be used to provide relief in terms of the tax consequences triggered when reimbursing the relevant investor.

25 Discuss your tax treaty network and how that facilitates or impacts tax structuring for cross-border deals. Are any treaties being negotiated or renegotiated? Are any major changes in the structure of your treaties expected?

Mexico has an extensive tax treaty network and has been constantly broadening it. Asides from tax treaties concerning the exchange of information, Mexico has executed over 60 tax treaties for the avoidance of double taxation. Mexico's tax treaty network is of vital importance on a day-to-day basis considering that the existence of such treaties can greatly ease taxation on cross-border transactions and provide relief for the parties involved.

Mexico is currently engaged in negotiation proceedings with Egypt, Slovenia, Iran, Marshall Islands, Lebanon, Malaysia, Morocco, Monaco, Nicaragua, Oman, Pakistan, Thailand, Vanuatu and Vietnam. Likewise, the corresponding tax treaty between Mexico and Ireland is currently being renegotiated.

26 Does your jurisdiction identify certain jurisdictions as tax havens and subject them to adverse tax consequences when they are involved in M&A transactions? Give details.

As mentioned in question 23, specific controlled foreign corporation rules ought to be abided by whenever foreign legal entities or vehicles considered to be subject to preferential tax regimes are involved in a transaction.

In this regard, a Mexican tax resident or a non-resident with a permanent establishment within national territory could be deemed to derive income from preferential tax regimes in cases where such income is not subject to taxation in the foreign legal entity's jurisdiction or is subject to a tax rate lower than 75 per cent of the rate that would have been applicable for such transaction in Mexico. Additionally, said parties could be subject to this specific tax regime concerning their direct or indirect participation in foreign legal entities or vehicles as well as foreign vehicles treated as tax transparent in their jurisdiction.

Income tax caused by operations in which preferential tax regimes are involved would be due on a separate basis than the rest of the accruable income of the relevant taxpayer.

Furthermore, the Mexican Income Tax Law includes an extensive list of jurisdictions that are presumed to be preferential tax regimes and, whenever a Mexican tax resident or a non-resident with a permanent establishment in Mexico obtains income deriving from any of such jurisdictions, an informative return ought to be filed on February of each fiscal year.

27 Describe any material state, provincial or local taxes that may arise in an M&A deal involving a target, a buyer or a seller located in your jurisdiction.

Besides federal taxes, state taxes such as property tax or tax on the acquisition of real estate could be applicable to transactions in which a Mexican target, buyer or seller is involved.

28 Are there any proposed laws or regulations that could significantly change how transactions are structured in your jurisdiction?

Currently, no laws or regulations that could significantly alter the way in which transactions are normally structured in Mexico have been proposed.

29 What are the corporate tax rates applicable in your jurisdiction on ordinary income and capital gains? Are there any other categories of income subject to preferential rates that are relevant in M&A deals in your jurisdiction?

The corporate tax rate currently in force is of 30 per cent. In this sense, Mexican tax residents are required to accrue the totality of income derived during the relevant fiscal year (on a worldwide basis) and to apply thereto the corporate tax rate. However, assuming the corresponding legal requirements are met, certain deductions, tax credits or net operating losses could be reduced from the taxpayers' gross income.

For non-residents that receive income in the form of capital gains whose source is deemed to be located within national territory, income tax due would be calculated by applying a tax rate of 25 per cent without the possibility of reducing taxable income with any deduction. However, if the relevant non-resident were to have a legal representative within Mexico (and assuming certain conditions are met), the non-resident could be entitled to pay income tax by applying a tax rate of 35 per cent with the possibility of reducing its taxable income with allowed deductions.

30 Does your jurisdiction impose any taxes as a result of the indirect transfer of a company organised in your jurisdiction?

Generally speaking, federal taxes in Mexico are triggered in accordance with residency, source and territoriality principles. That is, income tax is triggered on a worldwide basis with respect to Mexican tax residents and non-residents could be liable for income tax in Mexico regarding Mexican-sourced income or income attributable to a permanent establishment of theirs set up within national territory.

As for value added tax, it is only triggered when goods are sold or leased, independent services are rendered or goods or services are imported within national territory.

Bearing the foregoing in mind, no tax would be triggered as a result of the indirect transfer of a Mexican legal entity in so far as the transaction does not fall under the scope of the residency, source or territoriality principles. On the other hand, if the parent entity that is being transferred were to be a Mexican tax resident as well as the subsidiary, a taxable source of income for the non-resident purchaser could be deemed to exist.

31 Are there significant tax issues relating to foreign currency matters in transactions in your jurisdiction involving buyers or sellers resident in other jurisdictions?

In pursuance of the Mexican Income Tax Law, profits or gains resulting from currency exchange rates could be considered as taxable income. However, exchange gains could be reduced by exchange losses for the purposes of assessing income tax due.

32 Discuss and describe any other relevant tax issues in cross-border M&A transactions in your jurisdiction that are not covered in the prior questions.

The most relevant tax issues with respect to cross-border transactions in Mexico have already been addressed herein. Nonetheless, interested parties should bear in mind that each transaction is likely to have its own particularities. Therefore, when planning a cross-border transaction in which Mexico is involved, tax advice should be given on a made-to-measure basis.

Ana Paula Pardo

SMPS Legal

Ana Paula joined SMPS Legal in 2015 as tax partner. Her main practice is taxation concerning domestic and international aspects and involves representing corporations and individuals. She regularly advises clients on matters involving commercial transactions, tax planning, start-up business, joint ventures, investments, acquisitions, mergers, spin-offs, dispositions, tax-free reorganisations and transfer pricing consulting.

Professional practice

Ana Paula has extensive experience in international transactions, in corporate law, including representation of multinationals groups and domestic groups, specific controversy and litigation, representing domestic and international clients in tax audits and negotiations skills.

Prior experience

Before joining SMPS Legal, Ana Paula was an associate at Hogan Lovells BSTL since 2010 and before that she was an associate at Basham Ringe y Correa. She also clerked at the tax boutique, Ortiz, Sainz y Erreguerena for two and a half years.

Education

Law degree, Universidad Panamericana, 2002 postgraduate degree, University of Salamanca, 2004.
LLM, University of Florida - Fredric G Levin College of Law, 2007, obtaining a certificate of academic excellence.

Languages

Ana Paula is fluent in Spanish and English.

Jorge San Martín

SMPS Legal

Jorge is both a lawyer and a certified public accountant. His practice is focused on tax and business planning, including mergers and acquisitions, as well as corporate reorganisations with particular focus on permanent establishments and other tax-related international matters. Jorge assists his clients in planning tax-efficient structures, including the tax treatment of acquisitions and investments. His practice includes the representation of clients before Mexican Tax Authorities in a broad range of national and international tax controversies as well as in litigation.

Professional practice

Jorge San Martín represents national and multinational clients in local and international tax matters regarding cross-border operations, investments and transactions. Jorge also provides advice involving structuring and planning of tax-efficient structures, including the tax treatment of acquisitions and investments.

Prior experience

Prior to founding SMPS, Jorge was partner at the Mexico office of Gardere Wynne Sewell, LLP, where he worked for more than 10 years, and prior to that, he was partner of the accounting firm Rocha, Pérez, San Martín, SC.

Education

Jorge obtained his JD from UNAM and his degree as certified public accountant from Universidad Anahuac del Norte, in Mexico City.

Professional associations

Jorge is a member of the Mexico's Public Accountants School and of the Mexican Institute of Public Accountants. He is also a member of the Canadian Chamber of Commerce and the American Chamber of Commerce, in Mexico City.

For over 20 years, the partners and lawyers of SMPS Legal have successfully counselled domestic and foreign investors in their activities in Latin America.

Specifically, SMPS Legal provides legal services and support in transactions and projects in Latin America in important industry sectors of the economy, such as energy and natural resources, including oil and gas (upstream and downstream), mining, electricity (power generation and transmission) and water, infrastructure, private equity, banking and finance, hospitality, insurance, capital markets, aeronautic, automotive, cultural, food, pharmaceutical, real estate, manufacturing and information technology.

Responding to the growth of emerging markets in Latin America, SMPS Legal specialises in cross-border transactions, acquisitions, spin-offs, joint ventures, strategic alliances and foreign investments in the region.

SMPS Legal currently has offices in Calgary, Dallas, Mexico City and Bogota and alliances with prominent firms in Brazil, Argentina, Costa Rica, Panama, Peru and other Latin American countries to best serve its clients.

From knowledge of the local commercial and corporate customs and practices, to evaluating the relevant sectors of the economy and obtaining specialised legal advice, SMPS Legal assists its clients to maximise the opportunities offered by the region, providing timely and cost-effective advice.

In addition to the fact that the members of SMPS Legal share a joint vision to apply a commercial approach and provide focused legal and business advice, the firm provides tangible added value to its clients by taking the time to understand their business and legal service needs.

SMPS Legal is a leader in the optimisation of tax structures and M&A tax-related issues. The tax practice is unique in that it is a fully integrated consulting and litigation tax practice whereby all members provide both consulting and litigation services, with a clear vision of the financial and legal aspects of every issue.

Andrés Bello N. 10, oficina 402,
Col. Polanco, 11560,
México, D.F.
Tel: +52 (55) 5282 9063

www.smpslegal.com

Ana Paula Pardo
apardo@smps.com.mx

Jorge San Martín
jsanmartin@smps.com.mx