



The Legal 500 & The In-House Lawyer
Comparative Legal Guide
Mexico: Private Client (3rd edition)

This country-specific Q&A provides an overview of the legal framework and key issues surrounding Private Client law in Mexico.

This Q&A is part of the global guide to Private Client.

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Country Author: SMPS Legal

The Legal 500



Jorge San Martín (Partner)

jsanmartin@smps.com.mx

The Legal 500



Ana Paula Pardo (Partner)

apardo@smps.com.mx

The Legal 500



Iván Pérez Correa (Partner)

iperez@smps.com.mx

The Legal 500



Luis Roberto Moreno (Associate)

lmoreno@smps.com.mx

1. **Which factors bring an individual within the scope of tax on**

income and capital gains?

In Mexico, there is no distinction between income tax and capital gains tax, since capital gains are considered as ordinary income for income tax purposes.

Individuals are obliged to pay income tax over all their income, regardless it is obtained in cash, goods, credits or services. In this context, capital gains are considered as an additional cumulative income for individuals and integrate the taxable base to which the income tax progressive rate will be applied (that can go from 1.92% up to 35% on the total individual's income, depending on its amount).

None of the factors for which a person is obliged to pay income tax include citizenship, the location of its assets, or the location of its economic activity, so these factors don't bring an individual within the scope of income tax.

The factors that subject an individual to pay income tax are the following:

- Tax Residence in Mexico. Residents in Mexico are obliged to pay income tax with respect to all their income, regardless the location of the source of wealth they come from.
- Permanent Establishment in the country. Residents abroad who have a permanent establishment in the country are obliged to pay income tax regarding all the income attributable to said permanent establishment.
- Source of wealth in Mexico. Residents abroad are also obliged to pay income tax regarding income which sources of wealth are located in national territory, when they do not have a permanent establishment in the country, or when having it, such income is not attributable to it.

It is important to note that an individual is deemed as a resident in Mexico when he has established his home within national territory. When the individual in question also has a domicile in another country, he will be deemed as a resident in Mexico if his center of vital interests is in the national territory.

For these purposes, it is considered that the center of vital interests is in national territory when, among other cases, the individual updates any of the following assumptions:

- When more than 50% of the total income obtained by the individual in the calendar year has a source of wealth in Mexico.
- When the main center of their professional activities is located in the country.

2. What are the taxes and rates of tax to which an individual is subject in respect of income and capital gains and, in relation to those taxes, when does the tax year start and end, and when must tax returns be submitted and tax paid?

Individuals are obliged to pay income tax over all their income, regardless it is obtained in cash, goods, credits or services.

The income tax of individuals is calculated in a schedular way, separating the different kinds of income that an individual can receive. Each of the regulated taxable income has its own calculation and deduction system, and each individual has to calculate the income obtained by each of the regimes and has to add the result to the general total income.

The Mexican Income Tax Law establishes special regimes for the income that comes from: (i) salaries; (ii) business and professional activities; (iii) leases; (iv) sale of goods; (v) acquisition of assets; (vi) interest; (vii) prizes; and (viii) dividends and profits distributed by a legal entity.

Once the individual calculates the tax base in accordance with the particular regime of each income (with their own deductions, if applicable), all income obtained during the year shall be added, regardless of their source of origin. The resulting amount can be reduced by personal deductions (deductions that can be made by all individuals), and the total amount will be the general tax base.

The rate imposed to the income of individuals is a progressive fee, that goes from the 1.92% up to the 35% on the individual's total income, depending on its amount.

Tax year equals the calendar year, so it starts on January 1 and ends on December 31. The annual tax return shall be presented before April 30 of the immediately following calendar year to the year in which such incomes were obtained.

Notwithstanding the foregoing, throughout the tax year individuals shall execute advance payments over the income tax. Such payments shall be credited by the tax payer from the annual income tax calculation at the end of the tax year.

3. Are withholding taxes relevant to individuals and, if so, how, in what circumstances and at what rates do they apply?

Withholding is relevant for income tax purposes, since the payor could be obliged to withhold taxes in certain cases. Among the main cases, we can enlist the following:

- Employers (whether entities or individuals) shall withhold and pay income tax for the payments made to their employees. This income tax shall be withheld and paid in a monthly basis applying a progressive tax rate of up to 35%, being this an advance payment of the individual's annual tax. Furthermore, the law establishes several assumptions where an income is deemed as a salary, and, therefore, is subject to a withholding made by the person making the payment.
- Entities that receive professional services from individuals are obliged to withhold, as advance payment, the amount resulting of applying a rate of 10% over the payments made to the individual.
- Entities that lease real state from individuals are obliged to withhold the 10% of the total amount paid to the individual, as an advance payment of income tax, and without the possibility to make any tax deductions.
- Public notaries that register transactions where individuals sell goods shall withhold and pay the income tax resulting from the transaction. Tax could be up to 35% of the profit received by the individual.
- When the sale do not involve the participation of a public notary, the buyer is obliged to withhold, as advance payment, the amount resulting of applying a rate of 20% over the total amount of the transaction. Some alternatives may apply when shares are being sold, in which the advance payment could be up to 35% on the profit.
- Financial institutions that pay interest to individuals are obliged to withhold, as advance payment, the amount resulting of applying an annual withholding rate of 1.04% on the

capital invested by the individual. In the event that the payor is not a financial institution, the withholding rate could increase up to 35%.

- Entities that pay prizes earned in lotteries, raffles, bets and contests to individuals are obliged to withhold income tax in the amount resulting from applying a rate of 1% over the prize amount, without any deduction, as long as such income is not taxed for local purposes or such tax is below the rate of 6%. The tax rate shall be 21% if the income is taxed locally in a rate greater than 6%.
- Mexican entities that pay dividends to individuals are obliged to withhold income tax in the amount resulting from applying a rate of 10% over the dividend being distributed to the individual.

Regarding Value Added Tax, individuals are obliged to withhold value added tax regarding the acquisition or temporary use of tangible goods, alienating or granting residents abroad without permanent establishment in Mexico.

Finally, entities shall withhold value added tax to individuals when individuals render personal services or when they give the entity the temporary use or enjoy of goods.

4. Is there a wealth tax and, if so, which factors bring an individual within the scope of that tax, at what rate or rates is it charged, and when must tax returns be submitted and tax paid?

Mexican law does not distinguish income tax and wealth tax, as wealth is contemplated as an ordinary income for tax purposes.

5. Is tax charged on death or on gifts by individuals and, if so, which factors cause the tax to apply, when must a tax return be submitted, and at what rate, by whom and when must the tax be paid?

According to Mexican Law, income derived from death is exempted for income tax purposes.



Nevertheless, individuals that have obtained income that exceeds the amount of \$500,000 Mexican pesos during a tax year are obliged to declare all their income in their tax return, including income deriving from successions.

Lack of compliance could cause that the tax authorities deem all the undeclared income as cumulative income for income tax purposes, regardless of whether it was originally exempt.

An individual's death might cause other taxes, such as Real Estate Acquisition Tax, which is a local tax that shall be paid by the individual that is inheriting a real state.

In Mexico City, this tax has a progressive rate that goes from 3.163% to 4.565% on the total value of the property, and shall be paid by the person who is inheriting the real state by means of a withholding made by the notary public at the time the acquisition takes place.

Regarding gifts, Mexican Law states that gifts received by individuals are exempt from paying income tax in certain cases, including the following:

- Gifts between spouses or those who receive the descendants of their ascendants in a straight line, whatever the amount.
- Those who receive the ascendants of their descendants in a straight line, provided that the goods received are not disposed of or donated by the ascendant to another offspring in a straight line without limitation of degree.
- All other gifts, provided that the total value of those received in a calendar year does not exceed three times the general minimum salary raised per year. For the surplus, tax will be paid in the terms of the Mexican Income Tax Law.

Regardless of whether the donation is taxed or not, individuals residing in Mexico are obliged to report in their annual tax return about the loans, donations and prizes obtained therein, provided that these, individually or as a whole, exceed \$600,000.00 Mexican pesos.

Again, lack of compliance could cause that the tax authorities deem all the undeclared income as cumulative income for income tax purposes, regardless of whether it was

originally exempt.

If the donation is not exempt for income tax purposes, the individual shall pay the corresponding tax at the progressive rate that corresponds to him as explained before (see question 2). Said tax shall be paid through the annual tax return, no later than April 30 the following year.

In addition, individuals that obtain income from taxed donations shall cover, as an advance payment, the amount that results from applying the 20% rate on the income received, without any deduction. The advance payment shall be made through a tax return that shall be filed within 15 days after obtaining the income.

6. Are tax reliefs available on gifts (either during the donor's lifetime or on death) to a spouse, civil partner, or to any other relation, or of particular kinds of assets (e.g. business or agricultural assets), and how do any such reliefs apply?

As stated in question 5, Mexican Law establishes that gifts received by individuals are exempt from paying income tax in the cases explained before.

7. Do the tax laws encourage gifts (either during the donor's lifetime or on death) to a charity, public foundation or similar entity, and how do the relevant tax rules apply?

Mexican Income Tax Law authorizes taxpayers to deduct donations made to the entities deemed as "tax-exempt institutions" or "grantee institutions" ("*donatarias autorizadas*"), as well as those donations made to the federation or to the federative entities.

In order to be deemed as a *donataria autorizada*, entities shall have altruistic purposes and shall obtain an authorization from the Mexican tax authorities.

Donations made to this kind of institutions are deductible up to a total amount that does not exceeds the 7% of the taxable income obtained by the taxpayer in the immediately preceding year that in which the tax deductions are being made.

8. How is real property situated in the jurisdiction taxed, in particular where it is owned by an individual who has no connection with the jurisdiction other than ownership of property there?

Real estate located in Mexican territory is taxed by a local tax called “Predial”.

This tax shall be paid annually, and it is calculated by applying the rate foreseen in each state on the catastral value of the real estate, calculated in accordance with the procedure stated in each local law. In Mexico City, the tax rate can go from 1.5% to 20% on the value, depending on the catastral value of the property.

Foreign residents that own real state in Mexico can also be taxed with income tax or value added tax, depending on the activities to which such real estate is being subject in Mexican territory.

Regarding income tax, foreign residents that obtain an income from the sell of real state located in Mexico shall pay income tax in the amount resulting from applying a rate of 25% over the total income obtained, without any deduction. The tax shall be paid by means of a withholding made by the purchaser if he is a resident in Mexico or a resident abroad with a permanent establishment in the country; otherwise, the foreign individual shall pay the corresponding tax by means of a tax return that he shall present within fifteen days after obtaining the income.

In addition, individuals who own real estate in the national territory shall pay income tax in the event they receive any income from the leasing of such property. Tax will be determined by applying the rate of 25% over the income obtained, without any deduction. By general rule, the tax is paid by means of a withholding made by the person making the payments. In the event that the person making the payments is a

resident abroad, the tax shall be paid by means of a tax return within fifteen days of obtaining the income.

It is important to mention that in both cases tax treaties could provide relief regarding the applicable rate.

The alienation of the real estate shall also cause value added tax, at a rate of 16% on the sale value of the construction. The leasing of such real estate shall also be taxed by Value Added Tax, unless the real estate is destined or used exclusively for house-room.

9. Are taxes other than those described above imposed on individuals and, if so, how do they apply?

In addition to Income Tax in the terms explained before, other taxes may apply depending on the activities performed by the individual. Among the main taxes, individuals are obliged to pay consumption taxes, which affect the entire population. We will not enter into more details since we consider those taxes exceed the purpose of this document.

10. Is there an advantageous tax regime for individuals who have recently arrived in or are only partially connected with the jurisdiction?

No, it does not exist an advantageous tax regime for individuals who have recently arrived in or are only partially connected with the jurisdiction, they will be taxed as any other tax resident or a foreign resident with a source of wealth located in Mexico.

11. What steps might an individual be advised to consider before

establishing residence in (or becoming otherwise connected for tax purposes with) the jurisdiction?

Before establishing their tax residence in Mexico, individuals shall take into consideration the following aspects:

- Once they establish their tax residence in Mexico, individuals shall pay income tax on all of their worldwide income, regardless of the origin of said income. In this virtue, individuals shall pay taxes in Mexico with respect to all income that is received abroad (including any income derived from the alienation of goods located abroad), which may lead to a double taxation event if the country in which the income is received does not have a tax treaty with Mexico.
- The individual shall consider which activities are performed abroad, since activities that are exempted abroad may not be exempted in Mexico. Likewise, it should be considered that the income received from activities held abroad will also be taxed in Mexico.
- Individuals shall consider the tax base of the property owned by them, since once they are considered as tax residents in Mexico it will be necessary to determine the tax value of said assets in the event of a possible transfer.

12. What are the main rules of succession, and what are the scope and effect of any rules of forced heirship?

In accordance with current legislation, people in Mexico can inherit through two different regimes: testamentary succession and legitimate succession.

Through testamentary succession, a capable person can freely dispose of his assets and rights and declares or fulfils duties for after his death. The general rules for granting a will are regulated in each of the state legislations, to the extent that successions are governed under state jurisdiction.

On the other hand, the legitimate succession occurs when the author of the inheritance did not grant a will before his death, or the one he granted does not include all his assets or is invalid, so his assets and rights are distributed in accordance with the provisions set forth by the law.

Each state has its own rules regarding the order and form of inheriting through legitimate succession. However, and as an example, we enlist the following general rules of legitimate succession in Mexico City:

- Only descendants, ascendants, collaterals up to the fourth degree, spouse or surviving concubine, and in the absence of all of them, the System for the Integral Development of the Family from Mexico City can inherit through legitimate succession.
- As a general rule, the closest relatives exclude the most distant, except in those cases where ascendants or descendants concur, since the descendants, even being of the same degree or farther degree, exclude the ancestors, who will only be entitled to support payments.
- As a general rule, relatives who are in the same degree will inherit equally.
- Kinship by affinity does not give the right to inherit.
- The straight line excludes collateral. In a straight line, descendants exclude ascendants.

Finally, it is important to note that in Mexico there is no rule of forced succession, so everyone is free to dispose of their assets in the way they deem appropriate.

13. Is there a special regime for matrimonial property or the property of a civil partnership, and how does that regime affect succession?

Mexican Law establishes a special regime for matrimonial property, under the name of marital partnership.

The general rules for marital partnership are regulated in each of the state legislations, to the extent that this matter is governed under state jurisdiction.

In Mexico City, marital partnership shall be ruled by the prenuptial agreement, which establishes the patrimonial regime to which the property acquired during the marriage will be subject to.

Additionally, in the event a spouse dies, the one who remains alive shall continue with

the possession and management of the goods that constitute the marital partnership, until the verification of the partition of the goods in accordance with the succession procedure.

Regarding civil partnerships (understood as civil entities governed by the Mexico City Civil Code), one of the causes of dissolution involves the death of a partner with unlimited responsibility for the social compromises, except if the incorporation deed bylaws state that the partnership shall continue with its inheritors. Likewise, civil partnership shall also be extinguished by the death of the industrial partner, provided that his industry has originated the partnership.

14. What factors cause the succession law of the jurisdiction to apply on the death of an individual?

Mexican law does not expressly indicate in which cases it may apply to successions that have an international vocation (that is, those that have factors or points of connection with the outside), when the deceased did not grant a will to the date of his death.

However, the Mexican Federal Civil Code provides the rules for determining the applicable law should the specific act not be otherwise expressly regulated.

In accordance to it, the status and capacity of individuals is governed by the Law of the place of his domicile, while the constitution, regime and termination of rights in rem over real estate, as well as leases and temporary use of such property and personal property, will be governed by the law of the place of their location, even if their owners are foreigners.

Based on the foregoing, the Mexican succession Law would be applicable to a foreigner provided that at the time of death he has its domicile in national territory, or when the real or personal property of that person is located in national territory at the time of death (in which case Mexican Law will only apply with respect to said assets).

It should be noted that in accordance to the Mexican Federal Civil Code, the domicile of an individual is deemed to be: (i) the place where he habitually resides; in the absence of this, (ii) the place of the main center of its business; in the absence of these (iii) the place where they simply reside; and in the absence of all these (iv) the place where they are. It is presumed that a person habitually resides in a place when he remains in the place for more than six months.

Finally, regarding the competent courts to hear the hereditary trial (if necessary), the Mexican Code of Civil Procedures provides that it is competent judge: (i) the one of the place where the author of the succession was domiciled at the time of his death; (ii) in the absence of domicile, the one of the place of the location of the estate assets; (iii) and in the absence of both, the place of death of the author of the inheritance.

15. **How does the jurisdiction deal with conflict between its succession laws and those of another jurisdiction with which the deceased was connected or in which the deceased owned property?**

According to the Mexican Federal Civil Code, Mexican Law governs everyone who is located in Mexican territory, as well as the acts or events occurred inside it and those that are subject to Mexican laws, except when said laws provide for the application of a foreign law and except as provided in international treaties to which Mexico is party.

When applying foreign law, substantive foreign law shall be applied, without considering conflict provisions that would make Mexican law applicable. Exceptionally, attending to the special circumstances of the case, such conflict law provisions may be applied.

Furthermore, foreign law shall not be applicable in cases of fraud of law and when the foreign laws are contrary to Mexican public interest institutions and principles.

Finally, it is important to mention that as of the date Mexico has not concluded any international treaties to avoid conflict of succession laws with other countries.

16. In what circumstances should an individual make a Will, what are the consequences of dying without having made a Will, and what are the formal requirements for making a Will?

An individual should make a will always he has assets, rights or obligations that are susceptible to be transmitted because of death.

The consequence of dying without a will is that all assets, rights and obligations of the deceased are transmitted through the legitimate succession. For purposes of determining the order in which the family members of the deceased would inherit, the legislation of the domicile of the deceased shall be considered.

The special requirements depend on the type of will and the place of its grant. In Mexico City, the open public will is the only valid will and has the following requirements:

- It may be granted by any individual over 16 years old who enjoy their full capacity, except that in the event an individual does not enjoys their rightful judgement the individual is in a state of lucidity.
- It must be granted before a public notary.
- Testator must express his will clearly and strictly, having the notary to write it down.
- Once drafted, the notary must read it out loud for the testator to indicate if he agrees, if so, both proceed to sign it.
- The notary must record the day, month, year and time in which it was granted.
- The will must be granted in a single act, which will begin with the reading of the will and end with the signing of the will.
- The notary shall attest that all the beforementioned formalities have been complied.

Finally, it is important to highlight that, to our consideration, a foreigner whose only connection with Mexico is a real estate located in the country does not necessarily have to grant a will in Mexico regarding such property, since as noted in previous answers, it is sufficient that said individual has granted a will in his country of

residence that is valid according to the laws of such jurisdiction.

17. How is the estate of a deceased individual administered and who is responsible for collecting in assets, paying debts, and distributing to beneficiaries?

The estate of a deceased person is administered by the executor (“albacea”), which is the person in charge of liquidating the assets that constitute the estate of a deceased person (hereditary wealth), and that is empowered by the law to perform all the acts necessary to guarantee such liquidation.

Only people who have legal age (more than eighteen years) and those who are not disabled can be executors. The executor may be appointed by the following persons: (i) by the testator; (ii) by the heirs; (iii) in certain cases by the legatees; and (iv) a lack of the previous ones, by the judge.

The executor is in charge of formulating the corresponding inventory, collecting the assets, paying the debts, legally defending the succession and carrying out the project of inheritance and asset allocation.

The administration of assets shall be done under the fundamental principle that the estate of the deceased is an estate in liquidation, so that although the executor is allowed to perform new operations, these operations shall be transitory and with the shortest possible duration (thus, if the deceased had immovable property, the executor can lease said assets, but only for a maximum period of one year).

Finally, it should be noted that the executor has powers for lawsuits and collections and administrative acts in relation to hereditary property by legal provision, without implying that he is directly someone's representative, but that he is an executor with powers to perform legal acts.

18. Do the laws of your jurisdiction allow individuals to create trusts, private foundations, family companies, family partnerships or similar structures to hold, administer and regulate succession to private family wealth and, if so, which structures are most commonly or advantageously used?

In Mexico, people who intend to maintain, manage and regulate the succession of private family wealth can do so through two legal structures: through a "family" company or through the constitution of a fideicomiso.

The first of these options would involve the constitution of a "family entity", or a company whose partners or shareholders are only members of that family, being able to condition the alienation of the company's shares only among the members of that particular family.

Nevertheless, the most commonly used structures are fideicomisos, since they allow individuals to establish a purpose and a regulatory framework that best suits the needs of each specific case, to the extent that the fideicomiso is a structure through which any purpose can be achieved (as long as it is legal and possible).

19. How is any such structure constituted, what are the main rules that govern it, is there any requirement for registration with or disclosure to any authority or regulator, and what information about the structure is available to the public?

For Mexican legal purposes, the fideicomiso is a contract through which the trustor conveys to a fiduciary institution the ownership of one or more assets or rights, as the case may be, to be used for lawful and determined purposes, entrusting the execution of said purposes to the fiduciary institution itself.

As a general rule, there are three different parties in the fideicomiso:

- Settlor: Is the one who constitutes the *fideicomiso* and transmits ownership of the assets to the trustee. Anyone with the capacity to transmit ownership of the assets or rights subject to the *fideicomiso* can be settlors.
- Trustee: Is the person ordered by the settlor to carry out the purpose of the *fideicomiso*. He becomes the owner of the assets destined to the realization of such purpose. In accordance with the General Law of Credit Institutions, only institutions that are expressly authorized to do so may be trustees (including credit institutions, insurance institutions, surety institutions, brokerage firms, etc.).
- Beneficiary: Is the one in whose favor the administration of the assets is exercised. People who have the necessary capacity to receive the benefit that the *fideicomiso* implies can be beneficiaries. The Settlor can designate more than one beneficiary or even substitute beneficiaries.

It is important to mention that it is possible to create a *fideicomiso* without an initial beneficiary, as long as the purpose is legal and determined and the fiduciary institution accepts the assignment.

All kinds of assets and rights can be object of a *fideicomiso*, except those that are strictly personal in accordance to the law. The assets that are given in *fideicomiso* can only be used for its purpose, so the Trustee cannot exercise rights and actions that are not related with such purpose.

Finally, it is important to mention that the constitution of the *fideicomiso* shall always be in writing and if the settlor provides any real state the contract shall be granted before a notary public.

The steps for its constitution are the following: (i) determine what is the purpose to be done and select the goods to be disposed of to achieve it (the purpose must be legal and determined); (ii) select who will be the beneficiary; (iii) choose a fiduciary institution to be in charge of the administration and agree with it the conditions of the administration; (iv) define the duration period (taking into account the limitations that will be analyzed later); and (v) sign the contract with the fiduciary institution.

Regarding the main rules governing its operation, we can enlist the following:

- The *fideicomiso* constituted in fraud of third parties, can at all times be attacked for nullity

by the interested parties.

- The *fideicomiso* whose purpose is real estate shall be registered before the Property Section of the Public Registry of the place where the assets are located. The *fideicomiso* will take effect against a third party from the date of registration in the Registry.
- The *fideicomiso* whose purpose is movable property, will take effect against third parties from the date of its registration in the Sole Section of the Sole Registry of Secured Transactions of the Public Registry of Commerce.
- The beneficiary has, in addition to the rights granted to him by virtue of the constitutive act of the *fideicomiso*, that of enforcing compliance with the fiduciary institution; and that of attacking the validity of the acts that it commits in its detriment, in bad faith or in excess of the faculties that by virtue of the constitutive act or of the law corresponds to it.
- The fiduciary institution will have all the rights and actions that are required for the fulfillment of the *fideicomiso*, except for the limitations established when it is constituted. Among the main obligations, it is obliged to fulfill the *fideicomiso* according to the constitutive act; it cannot excuse or renounce his assignment except for serious reasons in the judgment of a judge, and is always responsible for the losses or impairments that the goods suffer because of it.
- The fiduciary institution shall register the assets or rights attached to the *fideicomiso* in a special account and keep them separately from their freely available assets.
- Secret *fideicomiso* and those in which the benefit is granted to successive persons who must be replaced by death of the previous one are prohibited, except in the case that the substitution is made in favor of people who are alive or conceived already, at the death of the trustor.
- *Fideicomisos* with duration of 50 or more years are prohibited, although some exceptions may apply.

It is important to mention that the fiduciary institutions have their own regulation issued by the Bank of Mexico through general circulars, which indicate their powers, prohibitions, transparency measures and the obligations they shall comply with before the Mexican authorities.

With respect to the information that the trustees are obliged to share, in accordance with the general rules issued by the Bank of Mexico, they shall provide the information on the *fideicomisos* that they celebrate or administer in the form and terms set forth by the special regulations.

Notwithstanding the foregoing, as a general rule, the information related to a *fideicomiso* agreement has the character of confidentiality under the fiduciary secret regulated in the Mexican Credit Institutions Act, according to which, the information and documentation related to the *fideicomiso* operations will be confidential, so that the credit institutions, in protection of the right to privacy of their clients and users, in no case may give news or information of these operations or services, but the beneficiaries, their legal representatives or those who have granted power to intervene in the operation or service.

20. **How are such structures and their settlors, founders, trustees, directors and beneficiaries treated for tax purposes?**

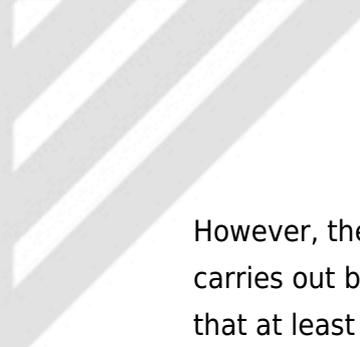
As a starting point, it is important to mention that as indicated before, for Mexican legal purposes the *Fideicomiso* is a contract that lacks legal personality, so it is never considered as a taxpayer. Instead, Mexican law attributes the tax burden to either the beneficiary or the trustor, as the case may be, and even in some specific cases assigns different obligations to the fiduciary institutions.

In order to know who the taxpayer in each *fideicomiso* is and in what cases the fiduciary institution has different obligations, it is important to distinguish whether the *fideicomiso* carries out or not business activities.

- *Fideicomiso* with business activities

It is considered that a *fideicomiso* carries out business activities whenever it carries out commercial, industrial, agricultural, livestock, fishing or forestry activities.

In accordance with Mexican Laws, when business activities are carried out through a *Fideicomiso*, the fiduciary institution shall determine in the terms of the legal entities, the result or the tax loss of said activities in each tax year and shall perform on behalf of the set of beneficiaries the obligations indicated in the Law, including the one of making the advance payments.



However, there is a regulated exception in our legal order, since a *fideicomiso* that carries out business activities can be exempted from the previous obligations provided that at least ninety percent of the total income obtained through the *fideicomiso*, during the tax year in question, comes from passive income.

In the case of *fideicomisos* that carry out business activities, the tax is attributed to the beneficiaries, except in cases where there is no beneficiary, or they cannot be identified, in which case it will be understood that the business activities carried out through the *fideicomiso* are performed by the trustor.

In these cases, the beneficiaries (or the trustor, if applicable) shall accumulate to their other income for the year, the part of the tax result derived from the business activities carried out through the *fideicomiso* that corresponds to them, and they can credit in that proportion the amount of the advance payments made by the fiduciary institution.

- *Fideicomiso* without business activities

If the *fideicomiso* does not carry out business activities, it is considered as a transparent structure for tax purposes, and the fiduciary institution has no obligation other than calculate the percentage of participation that each of the settlors or beneficiaries (depending on whatever it is a revocable or irrevocable *fideicomiso*, as explained below) have in both the profits and the losses (or, if applicable, deductions) of the *fideicomiso*, for the purpose of each individual accruing said income in accordance to their corresponding schedular regime and calculate its general tax base for the year.

For purposes of knowing who the taxpayer in this type of trust is, it is important to determine if it is a revocable or irrevocable trust, since from this will depend to whom the generated income is attributed.

For tax purposes, the *fideicomiso* will be revocable when the trustor reserves the right to reacquire ownership of the assets that were contributed to the *fideicomiso* (right of reversion).

For its part, the *fideicomiso* will be irrevocable when the trustor does not have the right to reacquire ownership of the assets that were contributed to the *fideicomiso*.

The above distinction is of great importance, since it will condition that the constitution of a *fideicomiso* is considered as an assumption of alienation in favor of the beneficiary (there will be alienation if the trust is irrevocable, either from the moment of its constitution or when the trustor loses the right of reversion) and will determine to whom the tax burden of the *fideicomiso* will be attributed.

If the *fideicomiso* is revocable, it is considered that the income generated through it is received by the trustor, for which reason he is the one liable to pay the tax. Otherwise, if the *fideicomiso* is irrevocable, it is considered that the income is received by the beneficiary, so the tax burden is transferred.

As an example of this, Mexican Law establishes that in the *fideicomiso* operations for which the temporary use or enjoyment of real estate is granted, the income is attributed to the trustor even if the beneficiary is a different person, except in the cases of irrevocable trusts, in which case the income is attributed to the beneficiary from the moment the trustor loses the right to reacquire the real estate.

21. **Are foreign trusts, private foundations etc recognised?**

Mexican Federal Civil Code establishes that legal situations validly created in a foreign State in accordance with their law shall be recognized.

Consequently, foreign structures validly created under foreign law are recognized for Mexican legal purposes, so in principle, foreign trusts and private foundations are recognized in Mexico (as long as they have been validly created in their country of incorporation), and will receive the legal treatment that corresponds to them depending on the nature that they have in their place of incorporation.

Thus, if the trust is considered as a legal entity with legal personality and its own assets in the place of its incorporation, it will also be considered as a legal entity in

Mexico, receiving the corresponding legal treatment.

On the other hand, if the trust is considered in its place of incorporation as a contract, that same nature will be respected in Mexico. In this case, it is important to mention that the legal effects of the contracts will be governed by the law of the place where they should be executed, so if the effects of such foreign trusts will be executed in Mexico, they shall be subject to Mexican legislation.

Similarly, private foundations are recognized in Mexican law, having the corresponding effects depending on their legal nature according to their place of incorporation.

22. **How are such foreign structures and their settlors, founders, trustees, directors and beneficiaries treated for tax purposes?**

As a starting point, it is important to briefly explain the general tax regime applicable to individuals who have some participation in a foreign entity or trust, so we can be able to explain each particular case.

As a general rule, individuals residents in Mexico that have any participation in a foreign entity or trust are obliged to consider the income they obtain from these entities or trusts as a cumulative income of the year, until the moment in which said income is distributed to them by the foreign entity or structure. Under this context, individuals shall accumulate the income until the moment they have any increase in his assets, which occurs when the entity or foreign trust materially distributes their profits to them.

Notwithstanding the foregoing, our law regulates an exception to this regime, in the event that the income comes from a jurisdiction considered by Mexican law as a preferential tax regime.

For Mexican purposes, a jurisdiction will be deemed as a preferential tax regime when the income received by an individual is taxed at a tax rate lower than 22.5%, or when the entity or trust through which the income is generated is not considered as a

taxpayer in the country of its incorporation or creation, and the income is attributed by that jurisdiction directly to its members, shareholders or beneficiaries (in these cases, the foreign entity or trust is denominated by Mexican law as a transparent entity or structure).

If the company or the foreign trust from which the income derives is in any of the above cases, the general rule changes, and the individuals that have any participation in them are obliged to recognize the income that comes from those entities or trusts in advance, from the moment in which the income is received by the foreign figure and without being able to wait for the profits to be materially distributed.

Having explained the general regime, we can enlist the following particular cases.

- Foreign entities deemed as taxpayers. Individuals who are considered as shareholders of a foreign entity that is deemed as a taxpayer in the country of its incorporation shall recognize as cumulative income any income that they receive from the entity. Individuals shall accumulate the income until the moment in which the entity distributes the profits or dividends.
- Foreign entities that are not deemed as taxpayers. If the foreign entity is not deemed as a taxpayer in the country of its incorporation (and therefore, is considered by Mexican law as a transparent entity in the terms explained before), individuals shall recognize the income based on the rules of the preferential tax regimes, which has the consequence that the individuals shall recognize such income in advance since the moment the entity receives it, without waiting for the moment in which the entity distributes them the profits or dividends.
- Foreign trusts. In the case of foreign trusts, it is important to mention that for tax purposes, the Law considers them as foreign legal structures, understood as any trust, association, investment fund or any other similar legal form incorporated under the foreign law that does not have legal personality.

If the trust is considered as a transparent foreign legal structure (again, assumption that is updated when the trust is not considered as a taxpayer in its country of creation), the income derived from the trust shall be accumulated in advance by the individuals participating in such trust, since the moment in which the income is received by the trust and without waiting for the moment in which such profits are distributed.

Otherwise, if the trust is not considered as a transparent foreign legal structure and is a taxpayer in its country, the income received by the trust shall be accumulated by the individuals participating in it until the time of its distribution, without having to accumulate them in advance.

Regarding the person considered as a taxpayer in these cases, we must distinguish if the trust is revocable or irrevocable (in the terms explained in question 20).

If the trust is revocable, the income must be accumulated by the settlor. On the other hand, if the trust is irrevocable, the income must be accumulated by the beneficiary, which normally occurs at the moment of the profits distribution.

23. To what extent can trusts, private foundations etc be used to shelter assets from the creditors of a settlor or beneficiary of the structure?

For Mexican legal purposes, a trust (understood as a *Fideicomiso* in the terms of Mexican Law) cannot be used to protect the assets of any of the trustors from a creditor if the trustors are the beneficiaries, since now the assets to be claimed are the rights on the trust.

In accordance with the Mexican Federal Civil Code, the debtor responds of the fulfillment of its obligations with all its assets (including his rights under a trust), except those that are inalienable and indefeasible, independently that these had been or not cause of the debt.

With the foregoing, Mexican legislation guarantees creditors the fulfillment of their obligations, since it constitutes a kind of guarantee in favor of the creditor with all the assets and rights of the debtor, except those that are inalienable or unattachable according to the law.

As indicated before, in a trust agreement, the trustor transmits to a fiduciary institution the ownership of one or more assets or rights, as the case may be, to be used for

lawful and specific purposes, entrusting the realization of said purposes to the fiduciary institution itself.

In this regard, when a person establishes a trust in Mexico, ownership of the assets that are affected by the trust is transferred to the fiduciary institution, so that it can be used to fulfill the purposes of the trust.

In this context, if any of the trustors is sued by a creditor after having contributed the assets to the trust, said assets would no longer form part of his own assets, so they could not be seized for the purpose of paying off the outstanding debt.

Notwithstanding this, and in accordance with the regime explained in previous paragraphs, if said trustor has any right derived from the trust (such as the right of reversion or the right to receive any return, product or proceeds of the trust assets), the right would be considered part of the assets of that trustor, so its creditors could affect it for the purpose of liquidating their respective debts.

On the other hand, it should be noted that if the debtor decides to affect his assets in trust knowing that he can be sued by his creditors, this act can be considered as an act in fraud of creditors under the terms of the Mexican Federal Civil Code. Pursuant to its provisions, the acts entered into by a debtor to the detriment of his creditor may be annulled, at his request, if the insolvency of the debtor results from those acts, and the credit under which the action is sought is earlier to them.

24. **What provision can be made to hold and manage assets for minor children and grandchildren?**

Other than a Tutor, that is the person in charge of a minor, the typical structure regulated by Mexican law to be able to maintain and manage the assets of minor children and grandchildren is the *fideicomiso*, which, as noted, is a structure that can have any purpose as long as it is licit and determined.

Based on the foregoing, nothing would prevent a person from establishing a

fideicomiso for a fiduciary institution to administer the assets of their minor children and grandchildren, provided that said assets are lawful and determined. This would have the tax consequences that were explained in previous answers.

25. **Are individuals advised to create documents or take other steps in view of their possible mental incapacity and, if so, what are the main features of the advisable arrangements?**

Mexican law regulates two different figures to address the mental disability of a person: guardianship and conservatorship.

In accordance with the Mexican Federal Civil Code, the object of the guardianship is the protection of the person and property of those who not being subject to parental authority have natural and legal incapacity to govern themselves.

In the other hand, conservatorship is planned to monitor the conduct of the guardian and to inform the judge of anything that he or she considers may be harmful to the incapacitated person.

Mexican law does not allow any of the previous positions to be appointed by the person that is incapable, nor that a person can decide who will be their guardian or curator in view of an imminent disability, since the appointment of these positions is previously established in the Law.

Given this circumstance, people who are in Mexico cannot take any previous step or preventive measure against an eventual mental disability.

26. **What forms of charitable trust, charitable company, or philanthropic foundation are commonly established by**

individuals, and how is this done?

In Mexico, two types of moral persons can be constituted for charitable or philanthropic purposes: the civil association ("A.C.") and the private assistance institution ("I.A.P.").

A civil association is a non-profit private entity with full juridical personality made up of individuals for the fulfillment of cultural, educational, dissemination, sports or similar purposes, in order to promote among its members and / or third parties any social activity.

The steps to constitute a civil association are the same as those regulated to constitute any entity in Mexico and basically consist of the following:

- The association must be made up of at least two people, who must be natural persons in accordance with the Mexican Federal Civil Code.
- The corporate name or name of the association must be chosen, which must be registered before the Ministry of Economy of the Mexican federal government.
- The statutes of the association must be drawn up, where the corporate purpose must be indicated. The corporate purpose cannot pursue lucrative purposes.
- These statutes must be notarized before a notary public.

Regarding their administration, these associations may have an individual or collegiate administrative body, which shall be called Director or Directors, without having any additional requirements for their appointment.

Finally, it should be noted as to the heritage of these associations that unless they are authorized as an authorized grantee ("*donatarias autorizadas*"), they may freely acquire, dispose of and / or tax their assets, without requiring any prior authorization or have to give some notice or notification in this regard.

For their part, people who want to perform philanthropic or welfare work in Mexico can also do so through a private assistance institution.

Like public associations, private assistance institutions are also legal entities intended for assistance, with the following differences:

- Social object, it is important to distinguish that private welfare institutions, unlike a civil association, which may have other purposes, comply solely welfare purposes.
- As for its form of constitution, the A.C. do not require authorization or special permission to be constituted, instead the I.A.P. needs to obtain the prior approval of their bylaws by the Private Assistance Board, a work plan must be added, and they must be subsequently notarized and registered in the Public Registry of Legal Entities of its City.
- Regarding its Social Reason, in the constitution of the A.C. the corresponding authorization must be requested from the Ministry of Economy, unlike the I.A.P. where the request is made directly before the Private Assistance Board, who will give a reply within 15 working days.
- Regarding its Heritage, in the I.A.P., the members cannot alienate immovable property of the institution without prior authorization from the Board of Private Assistance.

Finally, it is important to mention that both types of companies can obtain authorization from the tax authorities to receive tax-deductible donations for the persons who perform them, provided that they process their authorization to be an authorized grantee (“Donataria Autorizada”) before the tax administration service.

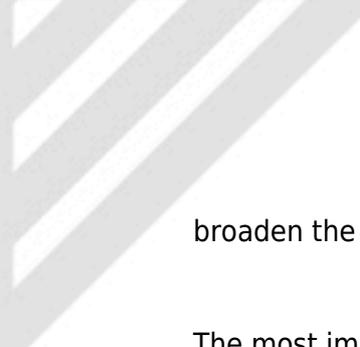
27. **What important legislative changes do you anticipate so far as they affect your advice to private clients?**

On October 30, 2019, Mexican Congress approved the new tax reform for 2020, making important modifications to the current Mexican tax regime. This modifications will enter in force as of tax year 2020, and should be considered by all taxpayers. Some of the most relevant changes are explained below.

- Income Tax Law

1. Update of the concept of permanent establishment.

In order to reflect in the Mexican legislation the recent changes to the definition of permanent establishment included on the Organization for Economic Cooperation and Development (OCDE) Base Erosion and Profit Shifting (BEPS) project, it is proposed to



broaden the concept that is currently included in the Mexican Income Tax Law.

The most important additions to the permanent establishment definition refers to activities carried out by non-residents through a person different from an agent of an independent status; also, a new provision was included aimed at preventing a group of related parties from fragmenting a business operation into minor operations in order to avoid having a permanent establishment in the country.

2. Combat hybrid mechanisms (or hybrid mismatches).

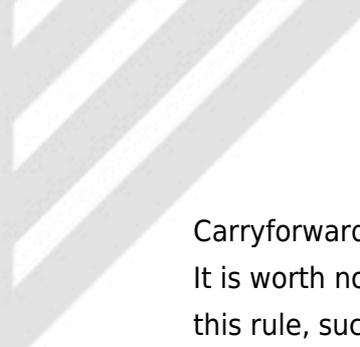
Although the Mexican tax legislation already contains measures against hybrid mechanisms or mismatches (i.e. cases where an expense deduction is authorized by the Mexican tax legislation and the corresponding income is tax exempted or not subject to tax abroad), the Mexican government has acknowledged that these measures have not been effective, and that the most recent recommendations of the OECD to combat this practice need to be included in our tax legislation.

Based on the above, payments made by a Mexican tax resident to a related party directly or through a “structured agreement” (under which the consideration to be paid involves payments to entities subject to preferential tax regimes which benefits the Mexican taxpayer or its related parties) will not be considered as deductible for Mexican tax purposes.

3. Limits for interest payment deductions.

Although Mexican law already contains measures which limit the deduction of interest between related parties, such as thin capitalization rules, the Mexican government deems necessary to include new rules regarding interest payments made not only to related parties but also to independent parties.

Under the new rule, any amounts exceeding 30% of the adjusted tax ebidta of a legal entity will not be deductible for tax purposes. This limitation is only applicable when the amount of the interest payments made by a Mexican resident entity and its Mexican-resident related parties exceeds in the aggregate MXN 20 million.



Carryforward on non-deductible interest is permitted for the following ten fiscal years. It is worth noting that certain interest payments are excluded from the application of this rule, such as interests on loans obtained to finance public infrastructure works, real estate developments located in Mexico, as well as interest paid on loans taken to finance projects in the extractive industries, and those derived from public debt instruments

Corporate groups are allowed to calculate the adjusted tax profit on a consolidated basis, in the terms that will be later established.

4. Tax treatment of provision of services and sale of goods through the internet, technological platforms, computer applications and similar means.

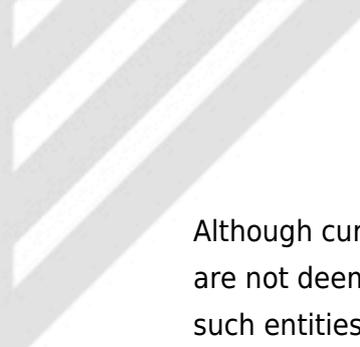
Following the administrative rules that had been published earlier in the year, and confirming the intention of the Mexican government to implement new mechanisms that ensure that Mexican resident individuals that participate in the business models of the digital economy comply with their tax obligations, new withholding rules are included.

Under the new regime, companies providing digital platform services (regardless of whether they are residents in Mexico or residents abroad) would be obliged to withhold income tax from Mexican resident individuals who obtain income through such digital platforms. Formal obligations are established both for the taxpayers (individuals) and for the legal entities obliged to make the tax withholding, including non-residents who do not have a permanent establishment in Mexico.

5. Elimination of private Infrastructure and Real Estate Trusts (private 'Fibras').

Given that the Mexican government considers that taxpayers have taken abusive advantage of the tax regime applicable to private Infrastructure and Real Estate Trusts, this regime was eliminated from the Mexican legal system.

6. Payments made to tax transparent foreign entities and vehicles.



Although current Mexican legislation recognizes the tax transparency of entities that are not deemed as taxpayers in other countries, allocating income to the members of such entities and vehicles, it has been considered necessary to establish a new rule that simplifies the collection of taxes that ultimately correspond to the members of transparent entities and vehicles, either Mexican tax residents or non-residents.

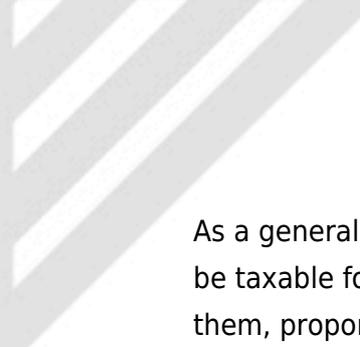
For these purposes, a new provision is included in the Mexican Income Tax Law applicable to foreign fiscally transparent legal entities and vehicles (such as trusts and partnerships) who obtain Mexican sourced income, in order to disregard their tax transparent status thus being subject to tax under the rules applicable to resident legal entities or to non-resident legal entities, as the case may be.

An exception to the above has been proposed regarding tax transparent vehicles that manage private equity funds invested in Mexican legal entities, subject to the compliance of certain requirements, i.e. that the transparent vehicle and its members are tax residents in a jurisdiction with which Mexico has entered into an exchange of information agreement considered as a “broad” by the Mexican tax authorities.

7. Income obtained by Mexican tax-residents through fiscally transparent foreign entities and vehicles and through controlled foreign entities whose income is subject to a preferential tax regime.

Under the current tax regime, Mexican tax residents who obtain income through fiscally transparent foreign entities and vehicles or through legal entities whose income is subject to preferential tax regimes, as a general rule, shall pay income tax on the income derived by the foreign entities or vehicles, even if the corresponding income has not been distributed by the same. This tax treatment has certain exceptions under which tax deferral is authorized, i.e. lack of control over the entity’s management.

Under the new rules, a differentiated tax treatment is established between income obtained through fiscally transparent entities, and income obtained through controlled foreign entities who do not have a transparent status abroad and whose income is subject to a preferential tax regime.



As a general rule, in both cases, income derived by the foreign entity or vehicle shall be taxable for the Mexican taxpayers, even if the same has not been distributed to them, proportionally to their participation in the entity or vehicle. Tax deferral may be applicable in certain cases where the taxpayers lack significant control regarding income obtained through controlled foreign entities; no tax deferral is allowed regarding income obtained through tax transparent vehicles.

- Value Added Tax Law

1. Provision of digital services by non-tax residents.

The reform also includes several changes and additions to the Value Added Tax Law in the area of digital economy, in order to comply with the recommendations issued by the OECD and increase revenue from indirect taxes.

Among the most relevant changes, the reform establishes that in the cases of digital services provided by non-residents who do not have an establishment in Mexico, the service shall be deemed to be provided within national territory and thus will be taxable for value added tax purposes when the recipient of the service is located in Mexico. In these cases, the non-resident who provides the service through a digital platform shall charge the corresponding value added tax to the service recipient, and shall pay such tax before the Mexican authorities, regardless of whether the non-resident has a permanent establishment in Mexico or not.

- Federal tax code

1. Measures against companies that issue, sell and use tax invoices for non-existent transactions.

Although the current legislation already includes measures against the sale of tax invoices connected to non-existent operations, the current Administration has considered necessary to include more severe measures against these operations.

Among the most important changes, the reform enables the tax authority to deny the



use of the electronic signature (used for purposes of complying with tax obligations) in some specific cases, and to increase the number of cases in which the authority may render digital seal certificates (which enable taxpayers to issue tax invoices) null and void.

These measures are complemented with the criminal-tax reform that was approved by the Mexican Congress during earlier days, intended to increase the penalties imposed to those who sell or use tax invoices in connection with non-existent operations.

2. General anti-abuse rule

Although Mexican legislation currently contains measures against tax simulation, it has been deemed necessary to include a new general anti-abuse rule to combat this problem more effectively and comply with the recommendations made by the OECD.

Under the new rule, legal acts that lack a business reason but generate a direct or indirect tax benefit will have a recharacterization of the tax effects corresponding to the acts that would have been performed to obtain the economic benefit reasonably expected by the taxpayer.

3. Disclosure of reportable schemes

In order to increase fiscal transparency, and following the recommendations made by the OECD, Mexican government deems necessary to include a new reporting obligation applicable to tax advisors and taxpayers.

In accordance with the new rule, tax advisors are required to register before the tax authorities and disclose general and personalized schemes designed for their clients as defined under Mexican law.

For these purposes, a “reportable scheme” is deemed as any scheme that generates or may generate, directly or indirectly, a tax benefit in Mexico as long as it complies with any of the features established by law, while “tax advisor” includes any individual or corporation resident in Mexico or resident abroad with a permanent establishment in



Mexico that in the ordinary course of their activities are responsible for or involved in the design, marketing, organization, implementation or administration of a reportable scheme, or the person who makes available a reportable scheme for implementation by a third party.