

TAX REFORM INITIATIVE FOR 2020

On September 8, 2019, the Executive Branch submitted to Congress the Economic Package for Fiscal Year 2020 (the "Economic Package"). Such package includes, among others, the Federal Revenue Law initiative, the initiative that reforms several tax provisions ("Tax Miscellaneous") and the Federal Expenditure Budget. The modifications included in the Economic Package are not final, since they will be subject to discussion, modification and approval by the Chamber of Representatives and the Senate, for its subsequent approval by the Federal Branch and its publication in the Federal Official Gazette.

Listed below are the topics that we consider most relevant in the proposal of the Economic Package:

FEDERAL REVENUE LAW FOR FISCAL YEAR 2020

With respect to the Federal Revenue Law for Fiscal Year 2020, among others, the following changes are proposed:

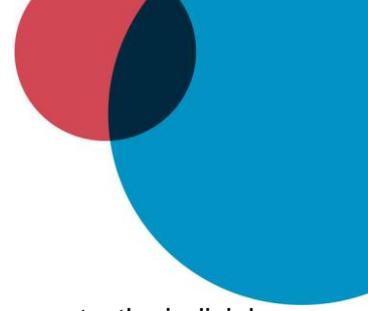
1. The annual withholding rate on interest paid by institutions that belong to the financial system during fiscal year 2020 is increased from 1.04% to 1.45% on the amount of the principal from which interest derives.
2. The tax incentives granted yearly through this regulation are maintained.

TAX MISCELLANEOUS

MEXICAN INCOME TAX LAW

With respect to the Mexican Income Tax Law ("MITL"), the following is proposed:

1. Update of the assumptions in which a foreign resident constitutes a permanent establishment, in accordance with the recommendations of the Project to tackle Base Erosion and Profit Shifting (the "BEPS Project") of the OECD.
2. Incorporation of rules for foreign transparent fiscal entities and foreign legal figures to be taxed as legal entities, regardless of whether their members, partners, shareholders or beneficiaries are taxed in their country or jurisdiction of residence.
3. The obligation of legal entities and foreign residents with a permanent establishment in Mexico to recognize the revenue obtained through foreign transparent fiscal entities and foreign legal figures, regardless of the tax treatment they have overseas, when they have direct participation in them, or when they have indirect participation that involves other foreign transparent fiscal entities and foreign legal figures.
4. Limitation of the foreign tax credit to prevent that such credit generates benefits in multiple jurisdictions.
5. Elimination of the obligations regarding labor subcontracting, so that the deductibility of payments made to a contractor for the provision of such services is limited to compliance with the obligation to withhold the value added tax ("VAT") of said payments.
6. Limitation of the deductibility of payments made to related parties or through structured agreements when the recipient's income is subject to a preferred tax regime ("REFIPRE", as per its acronym in Spanish), or when a payment is also deductible for a member of the same group, or for the same taxpayer in a country or jurisdiction where said taxpayer is also a tax resident.
7. Limitation of the deductibility of net interest of the fiscal year that exceeds 30% of the adjusted net income, in accordance with the recommendations of the BEPS Project, in addition to the existing thin capitalization rules.
8. Incorporation of a regime applicable to individuals who sell goods or provide services through the digital economy in which the legal entities that provide the electronic platform withhold the corresponding tax.



9. In the case of real estate lease lawsuits in which the lessee is obliged to pay overdue rents, the judicial authorities will require the creditor evidence of the issuance of the corresponding tax invoices and will inform the tax authorities if such invoices were not issued.
10. Substantial modifications to the REFIPRE regime, including the elimination of the exception of the regime to revenue derived from royalties that met certain requirements.
11. Modification to the existing requirements to qualify under the treatment applicable to a real estate investment trust (“FIBRA”, as per its acronym in Spanish) to exclude from such treatment trusts whose certificates are not placed among the general investment public (private FIBRAS).

VALUE ADDED TAX LAW

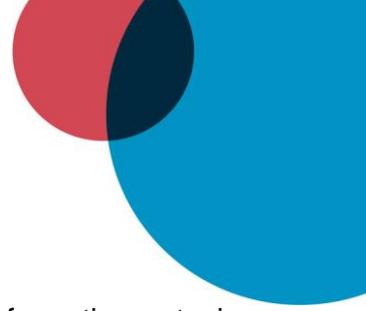
With respect to the Value Added Tax Law (“VATL”), the following is proposed:

1. Establish regulation to the digital economy, including the following amendments:
 - a. Establishment of the assumption under which digital services are provided in Mexico, the criteria under which the recipient of said services is considered to be in Mexico, obligations for the providers of the aforementioned services and applicable penalties for non-compliance of these provisions.
 - b. Incorporation of the nexus criterion that will allow the taxation of services provided by foreign residents without a permanent establishment in Mexico, in accordance with the model by which they provide digital services.
 - c. Establishment of the obligation to provide information to the tax authorities regarding operations carried out through platforms that function as intermediaries between third parties.
 - d. VAT credit by the receiver of digital services located in Mexico.
2. Addition of the VAT withholding obligation for payments made for contracting labor outsourcing services by the taxpayers hiring these services.
3. Restriction of the VAT credit derived from expenses incurred to carry out activities which are “not subject” to this tax, as defined in the VATL.
4. Elimination of the offset against other taxes of balances in favor in the provisions of the VATL.
5. Establishment of the obligation so that in real estate lease lawsuits in which the lessee is obliged to pay overdue rents, the judicial authorities require the creditor to prove the issuance of the tax invoices corresponding to said income.

FEDERAL FISCAL CODE

With respect to the Federal Fiscal Code (“FFC”), the following is proposed:

1. Inclusion of a general anti-abuse rule that grants the tax authorities the ability to presume that legal acts performed by taxpayers’ lack of a valid business reason based on their particular facts and circumstances.
2. Elimination of the joint liability exceptions that currently apply to liquidators, general directors, sole administrators, partners and shareholders.
3. Incorporation of more stringent measures to taxpayers who issue, commercialize and use tax invoices from non-existent operations, including the following:
 - a. Cancellation of certificates of digital stamps.
 - b. Requirements for obtaining the electronic signature, also known as *e.firma*.
 - c. Enablement of the tax mailbox on the tax authorities’ website and the registration of valid means of contact.
 - d. Inclusion of the figure of the third-party contributor (i.e., whistle blower) who provides data to identify taxpayers to substantiate the procedure described in article 69-B of the FFC.
 - e. Inclusion of the assumption of “not found” in the lists of taxpayers with allegedly non-existent operations, or of the presumption of improper transmission of tax losses for the granting of subsidies or incentives.



4. Establishment of a regime for the disclosure of reportable schemes that provides information on topics identified as areas of risk by the tax authorities, in which tax advisors would be, in most cases, obligated to disclose the aforementioned schemes.
5. Elimination of the tax secrecy regarding the name, denomination or legal name and Federal Taxpayer Identification number (“RFC”, as per its acronym in Spanish) in the case of taxpayers who receive and exercise federal public resources, and corporations that place shares in the stock market and the over-the-counter securities market, which do not comply with certain obligations, and individuals or legal entities who have used for tax purposes invoices that cover non-existent operations, without having demonstrated the materialization of said operations and corrected their tax situation.
6. Elimination of the “universal offset” of taxes.
7. Addition of a provision that states that the expiration and statute of limitations will not affect the implementation of the dispute resolution procedures provided in treaties to avoid double taxation.

Some other modifications are proposed regarding the Excise Tax Law, the Federal Duties Law and the Hydrocarbons Revenue Law.

We will issue a complete summary of the modifications made to the tax provisions for fiscal year 2020 once they are in their final version.

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We remain at your service for any questions or comments regarding the information contained herein.

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