Guide to develop and invest in the Mexican automotive sector.

PwC Mexico
September 2014

Doing Business in Mexico
Automotive Industry

www.pwc.com/mx/doing-business-automotive

Introduction

In 2014, Mexico's automotive industry will see its consolidation as one of the top countries in vehicle production and export, as a result of Nissan, Honda and Mazda's new facilities opening in Mexico's central region. Said facilities will be manufacturing several models at high volumes, that are targeted to high growth markets as well as those that are currently the biggest ones, without leaving behind those markets reflecting big improvements on its internal consumption. With this, during this year we might be close to 3.5 million produced vehicles, surpassing the Brazilian market, which is very dependent on its internal consumption; this, without considering the launch of Audi's plant scheduled for 2016, the announced investments of BMW, and Daimler/Nissan, together with the foreseeable arrival of new investment from the existing brands in our country, plus a couple of companies reassuring its investment this year.

Also, national vehicle production registered a maximum historic six-month growth of 7.4 percent, with one million 597 thousand manufactured units compared to the million 488 thousand of the same period of 2013. That number places Mexico 31 thousand units above the Brazilian vehicle manufacture, main competitor in Latin America.

In Mexico, internal vehicle sale continues to be a controversial matter, since we have not been able to establish the right mechanisms in order to achieve an internal sales growth above two digits. The introduction of used cars from the United States and the lack of automotive credits, are the two biggest concerns constraining a more dynamic vehicle internal consumption, besides Mexican market's sensitiveness to North American fluctuations.

Regarding supply, 2014 should also be one of the best years for Mexico since the quality of what is being produced keeps improving, and is being recognized worldwide. This situation has permitted not only to achieve growth on national production, but being able to provide other production lines in the United States, Europe and Asia, with which our TIER1 and TIER 2 suppliers have seen an increase on their business, whilst us being able to change the image of just being less expensive, to being one of the top countries competing in manufacture.

In 2013, global production grew 3.5% compared to what was registered a year before; with this increase, 3 more million cars were produced, a number that could have been higher, but the United States market was strongly contracted during the second part of the year, due to the delay of the Federal Government on the authorization of budget, creating a big uncertainty in car purchases. Also, the contraction faced by some European markets such as Spain or France, that have not been able to recover for some years, is still important; nevertheless, the upturn on emerging countries helped cushioning the fall of aforementioned markets.

GM brand, closed 2013 as the largest vehicle exporter followed by Ford and VW, being the United States, the main destination for said exports.

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A quick look at the Mexican automobile industry

Mexico as an automobile world power

Our country has recovered from the 2009 world recession, which significantly shook up the automobile industry. That crisis is now history, with only the statistics as a reminder. Nowadays, our country is on the path to become a leader in the manufacturing and exportation of light vehicles. Mexico is now the fourth exporter and holds the eighth position as a car producer; but, not for very long. Figures must increase in the next few months, thanks to the start-up of new operations from Nissan, Honda and Mazda, these will increase Mexico's production capacity by more than 650 thousand units per year (the equivalent to a 14% increase of the production); boosting exportations, since most of the cars are produced for the US market, where expected growth for 2014 is 4%. Other potential export markets are Central and South America, which have experienced significant growth, although production volumes are much lower. In addition, Europe: has shown a slight economic recovery, in countries such as Spain, France and Germany, which should favor exportations of light vehicles and auto-parts.

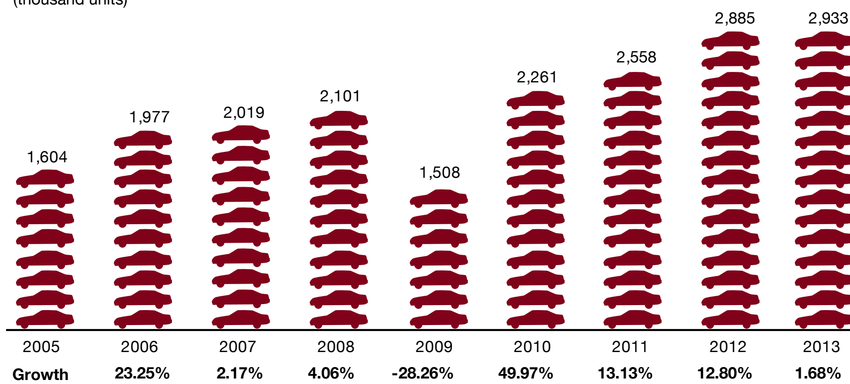
The start-up of new automobile industrial units and the increase in the production capacity of the existing facilities will result in an increase of supplies to meet the demand, as well as the increasing demand in the US, Europe and Japan. Therefore, growth in auto-parts production and exportation will be higher than expected for the light vehicles segment. The forecast is now a days, to achieve sales above 90 million USD by the end of 2015. To meet this goal, PROMEXICO has developed a number of investment projects, 100 of which are already underway, and many more under evaluation.

Consolidation as a producer

Mexico is increasingly consolidating its position as one of the world's top 10 car manufacturers. Last year, Mexico manufactured 2.9 million light vehicles, which represented 1.7% increase vs. 2012. Nonetheless, such figure could have been better; unfortunately Mexico's internal market only grew 7.7%, far from the potential market. On the other hand, the US - our main customer - went through a very harsh economic moments, such as the approval of the expense budget by Congress, which momentarily slowed down car sales and generated uncertainty in the market. At the same time, several European countries were under an economic crisis that affected the demand.

Mexican automotive production

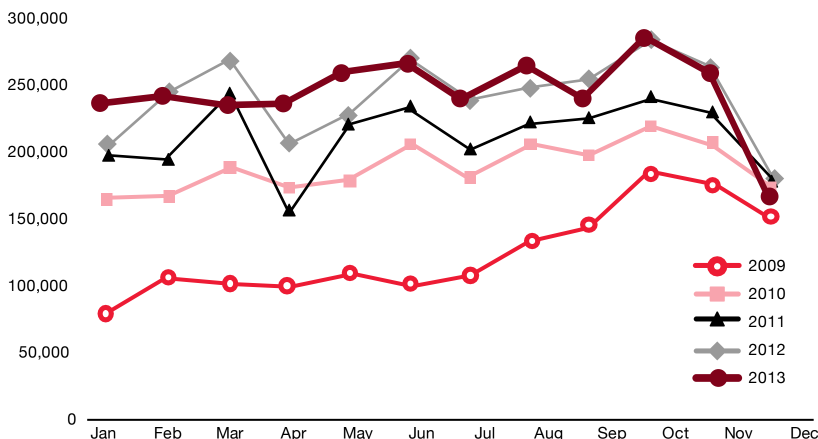
(thousand units)



Source: AMIA, AC. Monthly bulletin (several years).

Monthly production of cars and commercial vehicles

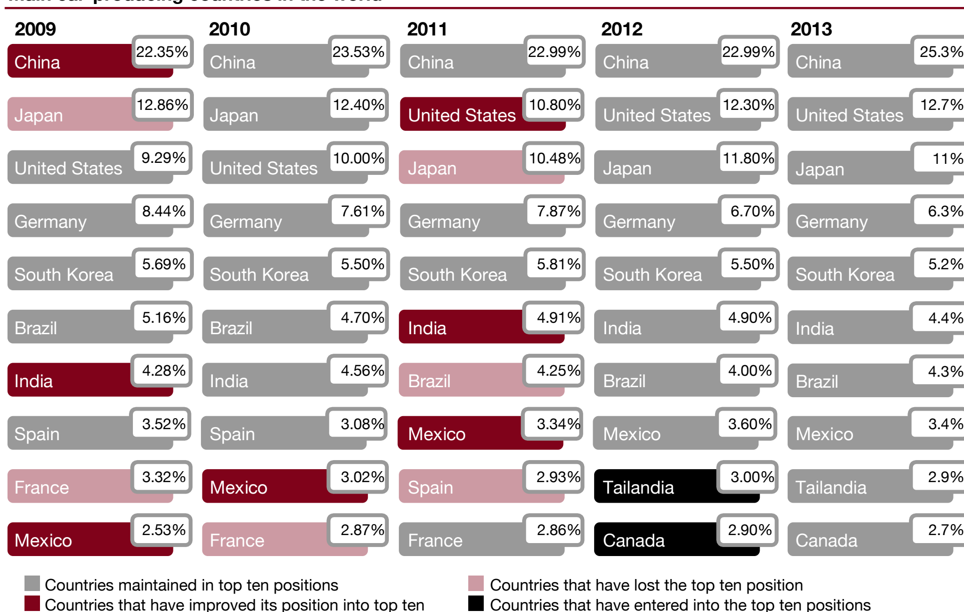
(units)



Source: AMIA, A.C. Monthly bulletin (several years).

Nonetheless, operations started this year at the Nissan II complex in Aguascalientes, Honda complex in Celaya and Mazda complex in Salamanca, aside from the new production line constructed by VW to manufacture the VII generation of the Golf. On the basis of the foregoing, the Mexican automobile industry will increase its production capacity by 650 thousand units, which means that by the end of 2014, or early 2015, we will match Brazil's position as the seventh light vehicle manufacturer, with production over 3.6 million cars.

Main car-producing countries in the world



Source: OICA (Organisation Internationale des Constructeurs d'Automobiles)

We have observed that production per car brand follows the trend of their participation in the internal market, where Nissan, with its Aguascalientes and Morelos complexes, reached 680,213 units in 2013, followed by GM's production of 645,823 units in 2013 at its central and northern Mexico complexes. Ford is third with a total of 525,200 units produced, followed very closely by VW with 516,146 units. However, VW achieves such production with a single facility in Puebla, which is the number one manufacturer of cars for the entire North America region, surpassing the Toyota, Honda and Nissan complexes in the US.

Total production of cars and trucks by company (units)

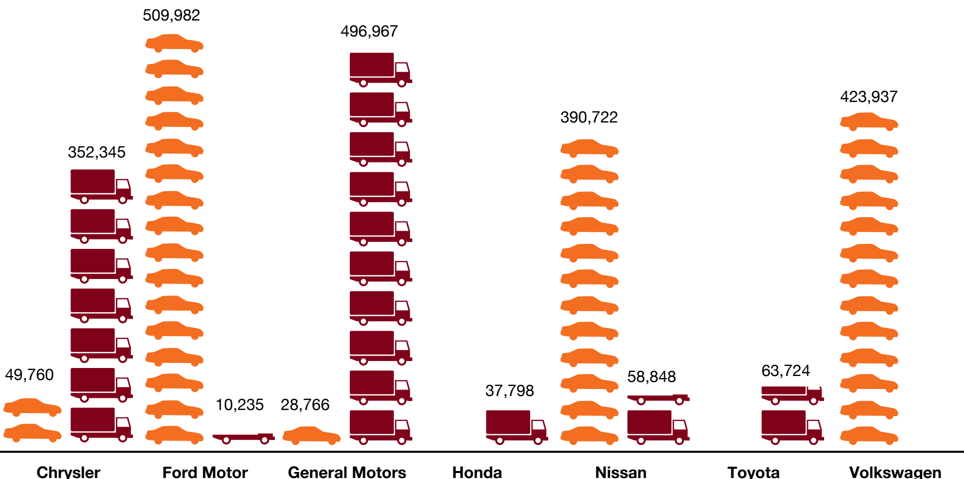
	2006	2007	2008	2009	2010	2011	2012	2013	Growth% 2013/12
Total	1,976,645	2,019,447	2,101,361	1,507,527	2,260,776	2,557,550	2,884,869	2,933,465	1.7%
General Motors	500,418	464,873	507,308	350,534	559,350	544,202	570,942	645,823	13.1%
Nissan	398,618	489,254	440,629	353,018	506,492	607,087	683,520	680,213	-0.5%
Volkswagen	347,020	409,566	449,096	319,743	434,685	510,041	604,508	516,146	-14.6%
Ford	349,910	304,137	314,231	234,330	393,649	462,462	451,648	525,220	16.3%
Chrysler-Fiat*	313,387	283,960	280,147	157,082	257,319	338,772	455,334	439,110	-3.6%
Honda	24,262	26,374	51,253	47,728	55,001	45,390	63,256	63,229	0.0%
Toyota	33,209	32,249	49,879	42,696	54,278	49,596	55,661	63,724	14.5%
Renault	9,821	9,034	8,818	2,396	0	0	0	0	NA

Source: AMIA, AC. Monthly bulletin (several years).
*AMIA, at the request of both companies concerned, it consolidates its figures since 2013 and for purposes of comparison, the same criteria was applied for 2012.

Export markets

One of Mexico's greatest challenges is to diversify light vehicle exports, to avoid dependence of the US market. In 2013, car exports totaled 2,423,084 units worldwide, a 2.9% increase vs the previous year, although 69% of such exportations were made directly to the US market, which increased purchases from Mexico by 9.5%, shipping 1.6 million cars. Canada received 8% of our exports, as a result of which, their purchases increased by 21.7%;, Brazil, which used to be one the main car buyers, currently only receives 5.7% of our exports, which represents a descent of 40% with respect to 2012.

Truck and automobile exports



Source: AMIA, AC. Monthly bulletin

Cars and trucks exports by company (units)

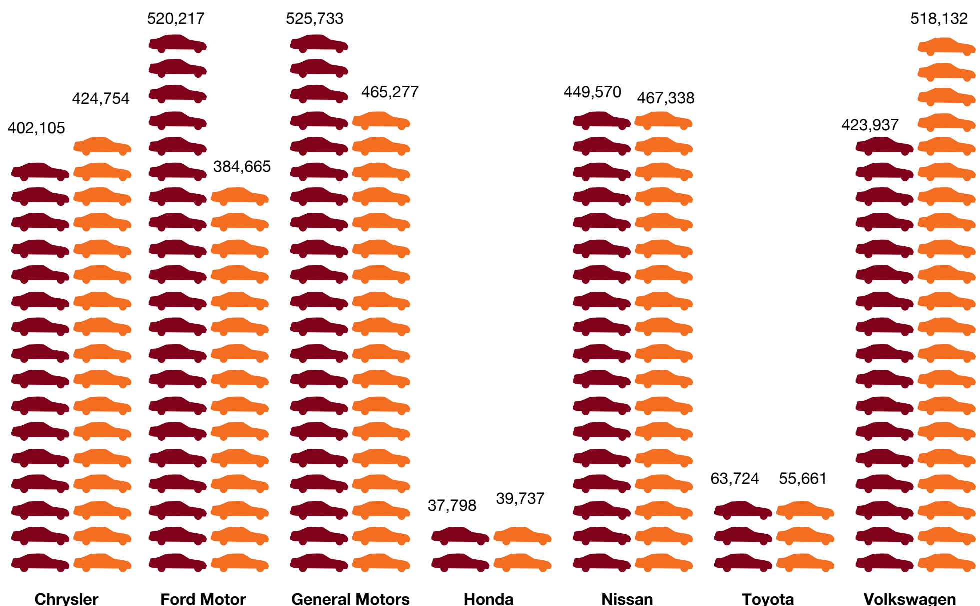
	2006	2007	2008	2009	2010	2011	2012	2013	Growth% 2013/12
Total	1,536,768	1,613,313	1,661,403	1,223,333	1,859,182	2,557,550	2,405,188	2,423,084	2.9%
General Motors	412,807	383,943	387,152	280,673	460,112	544,202	467,085	525,733	13.0%
Ford	302,780	263,452	272,924	231,003	384,629	607,087	435,080	520,217	35.2%
Volkswagen	283,564	331,453	382,755	271,391	350,721	510,041	520,438	423,937	-18.2%
Nissan	208,820	314,269	281,036	225,726	344,243	462,462	467,517	449,570	-3.8%
Chrysler-Fiat*	303,441	272,109	253,601	135,011	224,078	338,772	420,780	402,105	-5.3%
Toyota	10,111	32,249	49,879	42,696	54,278	45,390	55,661	63,724	14.5%
Honda	15,107	15,755	34,037	36,829	41,121	49,596	38,627	37,798	-4.9%
Renault	138	83	19	4	0	0	0	0	0%

Source: AMIA, AC. Monthly bulletin (several years).
*AMIA, at the request of both companies concerned, it consolidates its figures since 2013 and for purposes of comparison, the same criteria was applied for 2012.

The latter decrease is mainly due to the restructuring of the commercial balance between both countries performed two years ago. On the other hand, the recession in Germany resulted in a decrease on exportations, only 4.9% of the total, a drop of 59% in purchases made to Mexico by the end of 2013.

Exportations per brand are led by GM, which exported 525,733 units, followed by Ford with 520,217 units, Nissan with 449,570 units and VW with 423,937 units, reflecting a descent of 18.2% with respect to 2012 exports.

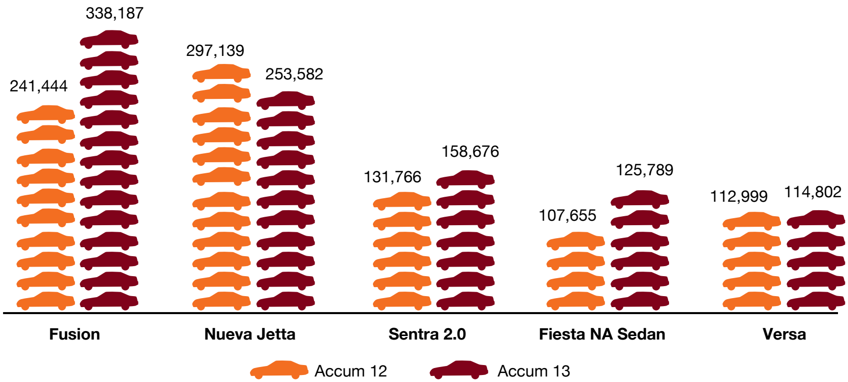
Automobile exports



Source: AMIA, AC. Monthly bulletin

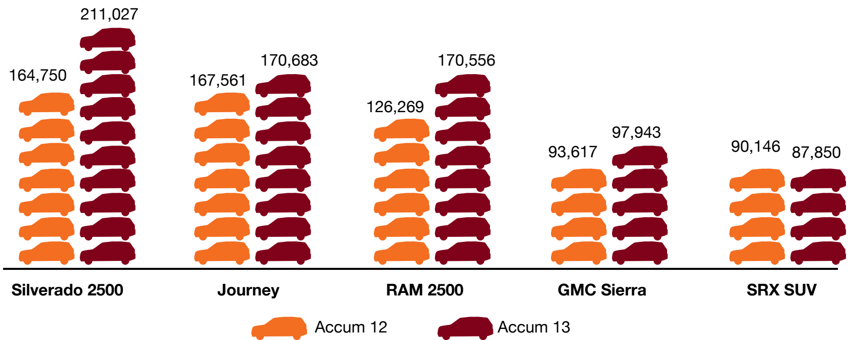
First two-month period of 2014, exportations had increased by 6.1%, due in part to the growth in the US market, plus an increase of purchases made by a number of European countries that are beginning to experiment a slight economic recovery.

Automobile models with higher export volume. January - December 2012 - 2013



Source: AMIA, AC. Monthly bulletin

Lightweight trucks with higher export volume. January - December 2012 - 2013



Source: AMIA, AC. Monthly bulletin

Pending items

Time keeps running and the automobile industry in Mexico still has several pending items that need to be resolved. For several years our attention has been drawn to the increasing importation of used vehicles from the US, situation that slows down the growth of internal market. By the end of 2013, approximately 7 million used vehicles have been introduced into Mexico. However, such figure becomes alarming, compared to the 8 million new cars that have been sold in Mexico during the same period. Aside from the negative effects on the environment, significantly damage is done to the auto-manufacturers, distributors and auto-parts companies.

Another important item in the agenda is the lack of a vehicle renewal program: the average age of the total cars running in Mexico is 16 years, twice the age of the total cars circulating in the US, affecting the environment due the high fuel consumption. Much of the foregoing also relates to the lack of competitive financing schemes that would allow increasing the potential for sales of new and semi-new cars.

The arrival of significant investments to increase the capacity for vehicle and auto-part production, has affected the generation of jobs in a positive manner. However, higher employment offer struggles to obtain an increasing number of qualified labor force, beginning to be a problem in some regions of Mexico, especially in central Mexico, since available labor does not meet the present demand of the production chain.

Uncertainty arising from the tax reform

The automobile industry in Mexico, for obvious reasons, is very sensitive to economic conditions and changes. The recent approval of the tax and financial amendments created a feeling of uncertainty that affected the automobile sector. This is partly due to the lack of information on the application of the new rules (for example the deduction factor) as well as the economic effects of such amendments on the taxpayer's pockets. However, it is only a question of time; doubts regarding the application of tax amendments are gradually resolved. It is important to remember that December, aside from being one of the best months of the year is also one of the shortest, due to the holidays is the month, sales are deferred to January of the following year.

Talking "green"

The use of alternative propulsion technologies for vehicles has opened a new chapter in the Mexican automobile industry, it has triggered the initiative of automobile brands to incorporate diesel, hybrid or electric technologies in their cars and it has broadened their product portfolios. The foregoing constitutes an innovative proposal to increase the autonomy of vehicles with minimum use of fuel and generation of pollutants. Nevertheless, those technologies pose great challenges, such as their adaptation to a society that has always been gasoline dependent and making technology prices accessible and competitive in the current vehicle market. The first challenge would seem easier, although the autonomy of electric cars continues to be one of the key factors to bear in mind, as well as the establishment of a reloading network in the main cities of Mexico. However, the foregoing is completely conditioned to the price of a car, which is the main element that people consider when purchasing a vehicle and that could bring such technology closer to consumers seeking greater efficiency, but not necessarily interested in paying much more for their vehicles. Fortunately, there are countries and cities that are committed to adopt "green" technology, which will gradually result in accessible prices.

In Mexico, sales of hybrid or diesel technology cars are few, mainly in the luxury car segment. By the end of 2014 the first electric cars will be on sale by Nissan, BMW and Renault. Unfortunately, support for that type of cars has not been defined as in other countries, situation that reduces the consumers interest in the use of such technology.

The new structure of the automobile market in Mexico

Market composition

In the late 90's the Mexican automobile industry was in a reconstruction phase, after a severe economic crisis resulting from a strong devaluation of the Mexican peso. However, at that time, one of the most interesting phases of Mexico's history started, due to the arrival of new automobile brands in the Mexican market; which aside from introducing new vehicles also opened our eyes to new business practices. With under one million units, it seemed complicated for some of those brands to prosper in Mexico. Fortunately, the reconfiguration of the Mexican market by new competitors and the growth in sales, made it possible for most of those brands to remain in Mexico. So far, only two brands were unable to continue operating in Mexico: MG-Rover and FAW.

There are only a handful of brands that have not reached Mexico. Although some of those brands have expressed their interest in setting up business in Mexico, sudden factors did not allow them to do so. Such was the case of the Japanese luxury car brand Lexus, which was ready to start operating in Mexico but which in the end could not reach a satisfactory agreement. In the last few months, Hyundai confirmed its arrival in Mexico after announcing its split from Chrysler and assessing the profitability of the Mexican market. Therefore, the arrival of the Korean brand opens the possibility for other brands to set their goals in Mexico: Tata Motors from India, Kia from Korea or other Chinese brands.

Results of the Mexican automobile market

The Mexican automobile market continues to be one of the markets with the most competition worldwide, given the number of car brands that operate here, aside from the vast offer of products offered by each brand. In most cases, automobile brands offer a full array of products, which means that there are up to 10 competitors in each of the market's segments.

In 2013, sales totaled 1,063,363 units, which represented an increase of 7.7% in relation to 2012. Nissan was market leader with annual sales of 263,477 units, i.e. a 7.6% increase, almost the same percentage of total market growth, with which it gained 25% of market participation. General Motors sold 201, 604 units, with the resulting growth of 8.2% and market participation of 19%. VW was one of last year's winners by achieving annual sales of 156,313 units, with growth of 16.7% and market participation of 15%.

Car and truck sales by company to dealers

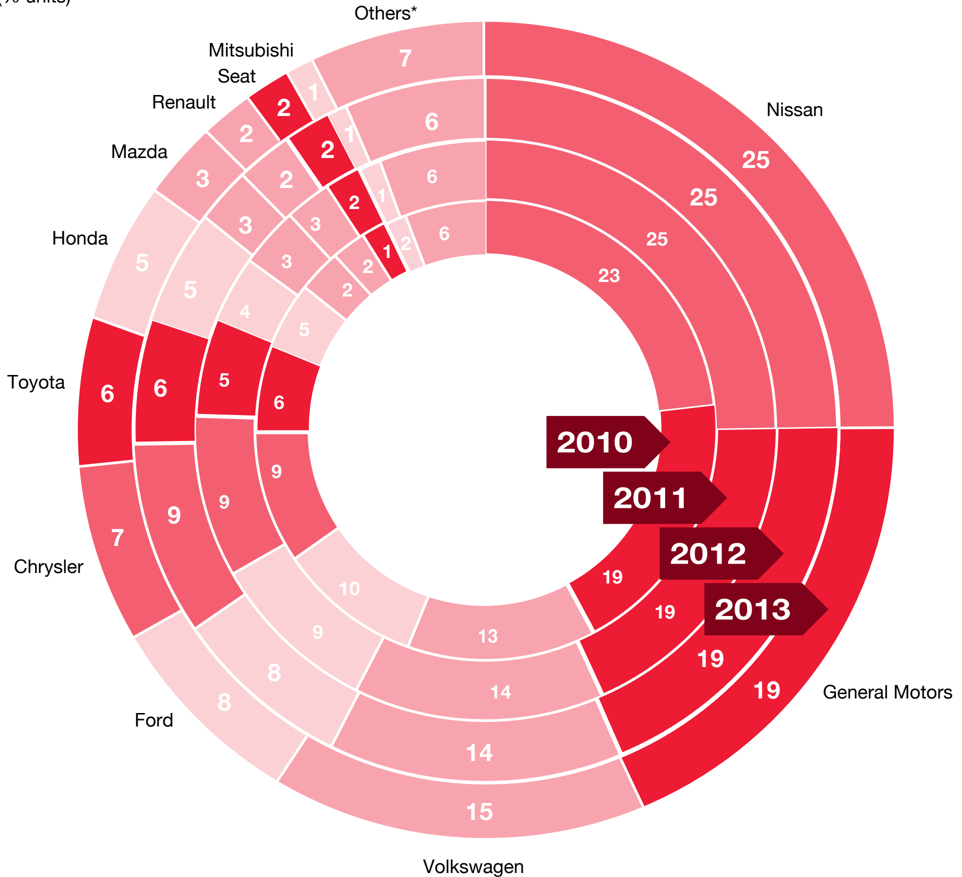
	2006	2007	2008	2009	2010	2011	2012	2013	Growth% 2013/12
Total	1,157,356	1,074,342	1,019,153	723,423	834,024	905,886	987,747	1,063,363	9.04%
Nissan	238,024	209,404	208,490	162,234	193,170	224,509	244,962	263,477	9.11%
General Motors	242,935	223,100	213,447	127,930	158,600	168,503	186,383	201,604	10.61%
Volkswagen	136,388	126,394	117,785	100,819	110,993	126,831	133,964	156,313	5.62%
Ford	184,432	134,299	130,106	78,262	85,092	85,988	82,328	85,721	-4.26%
Chrysler	130,864	125,050	113,666	77,775	78,061	82,072	88,023	78,974	7.25%
Toyota	58,244	75,736	61,186	45,268	49,945	48,589	56,278	60,740	15.82%
Honda	48,839	55,913	52,292	32,377	40,154	34,426	52,351	58,381	52.07%
Mazda	7,827	18,208	22,589	18,049	25,501	29,860	25,424	33,348	-14.86%
Renault	20,175	17,772	14,884	10,414	19,486	23,132	25,030	21,187	8.21%
Seat	19,498	13,409	12,590	15,753	14,251	18,115	21,114	21,189	16.56%
Mitsubishi	16,992	16,841	17,380	13,645	12,876	10,496	8,753	8,997	-16.61%
Suzuki	4,381	6,130	8,109	6,732	8,120	9,179	10,733	11,190	16.93%
Audi	4,451	4,796	5,452	4,559	5,416	8,058	9,482	11,712	17.67%
Mercedes Benz	6,222	7,791	7,443	5,166	6,258	7,823	8,966	8,871	14.61%
BMW	6,897	7,836	6,859	5,431	5,534	6,634	8,006	9,635	20.68%
Peugeot	15,474	13,023	8,871	6,818	6,113	5,796	5,204	6,941	-10.21%
Mini	1,768	2,073	2,089	1,710	2,124	3,003	3,821	4,357	27.24%
Fiat	1,447	3,549	3,165	3,169	2,614	2,580	5,038	8,228	95.27%
Lincoln	5,384	4,953	4,288	1,777	2,723	2,016	2,054	1,766	1.88%
Acura	1,715	1,852	2,106	1,846	1,960	1,783	2,164	2,570	21.37%
Isuzu	0	226	768	964	1,340	1,629	1,706	1,015	4.73%
Smart	589	596	749	679	990	1,470	1,634	1,676	11.16%
Volvo	2,708	2,690	1,823	608	1,262	1,334	1,513	1,568	13.42%
Land Rover	729	1,005	727	331	446	613	927	1,357	51.22%
Subaru	393	752	1,146	525	503	587	283	533	-51.79%
Infinity	n.d.	n.d.	n.d.	n.d.	0	231	736	989	218.61%
Porsche	676	740	859	465	413	539	650	765	20.59%
Alfa Romeo	n.d.	n.d.	n.d.	n.d.	0	30	93	104	210.00%
Jaguar	280	180	265	106	76	54	117	143	116.67%
Bentley	24	24	19	11	3	6	10	12	66.67%

Source: AMIA, AC. Monthly bulletin (several years).

[1] As of December

Companies' participation % on sale of cars and trucks to dealers

(% units)



Source: AMIA, AC. Monthly bulletin (several years).
*Includes the following companies (2012): Suzuki (1.09%), Audi (0.96%), Mercedes Benz (0.91%), BMW (0.81%), Peugeot (0.53%) , Mini (0.39%), Fiat (0.51%), Lincoln (0.21%), Acura (0.22%), Isuzu (0.17%), Smart (0.17%), Volvo (0.15%), Land Rover (0.09%), Subaru (0.03%), Infinity (0.07%), Porsche (0.07%), Alfa Romeo (0.001%), Jaguar (0.01%) y Bentley (0.0008%).

Toyota closed 2013 with only a sales increase of 7.9%, as opposed to the growth obtained by Peugeot of 33% and Mazda of 31%. Nevertheless, very few brands experienced a decrease in volume, such as Renault with a 15% drop compared with 2012.

As for the luxury car segment, Audi is growing in the Mexican market with total sales of 11,712 units, which is a 23% increase in relation to the previous year, resulting in market participation of 1.1%. BMW was slightly behind with sales of 9,635 units, which represents growth of 20.3% and a market participation of 0.91%. Mercedes-Benz sold 8,871 units and closed the year with a small decrease with respect to 2012 results.

On the other hand, the announced new plants for Nissan-Renault and Daimler in Aguascalientes will create 5 thousand 700 jobs. The announcement also implies the creation of 10 thousand indirect jobs for suppliers and distributors in Mexico.

Geographical distribution of plants of light vehicles

TOYOTA
Tijuana Plant
Hermosillo Plant
Chihuahua Plant
CHRYSLER
Ramos Arizpe Plant
GM
Ramos Arizpe Plant
CHRYSLER
Saltillo Plant
GM
SLP Plant
Puebla Plant
NISSAN
Aguascalientes Plant 1
Aguascalientes Plant 2
HONDA
El Salto Plant
HONDA
Celaya Plant
Guanajuato Inner Port
GM
Silao Plant
Salamanca Plant
CHRYSLER
Toluca Plant
GM
Toluca Plant
Cuautitlán Plant
NISSAN
Civac Plant
BCN
BCS
Son
Chih
Coah
NL
Sin
Dgo
Tamps
Zac
Ags
SLP
Nay
Jal
Gto
Qro
Hgo
Col
Mich
Méx
DF
Tlax
Mor
Pue
Ver
Gro
Oax
Yuc
QR
Camp
Tab
Chis

Geographical distribution of plants and heavy trucks

Geographical center of engineering and design

Mexico facing forward

Strengths

- Mexico is the country that has signed the most free trade agreements worldwide, which facilitates exportations of vehicles and autoparts.
- It has economic stability and tax certainty for the next five years.
- Mexico's geographic location favors exports of vehicles and autoparts to the main markets in the world.
- The Mexican automobile sector has the most modern and efficient installed capacity for vehicle production worldwide.
- Production capacity is highly technical and very flexible, which makes it possible to manufacture several types of models.
- The cost of Mexican labor is very competitive and it is rated as one of the best worldwide.
- New automobile clusters have been created and consolidated in central Mexico.
- Mexico's car industry has vast experience in manufacturing vehicle components and autoparts.
- Logistics costs of exportations are significantly reduced given the proximity to the US.
- There are public and private, colleges and universities, which teach undergraduate and postgraduate courses aimed at the automobile industry.

Weaknesses

- High dependence of the US market.
- Low internal market growth over the next few years.
- High levels of insecurity in some states and cities of Mexico.
- Entrance of used vehicles into Mexico from the US.
- Lack of programs to encourage car sales in Mexico.
- Lack of programs to develop qualified technical labor for the automobile industry.
- Lack of programs and financing to develop supply sources.
- High dependence on gasoline vehicles.
- Poor quality of fuels.
- Lack of government interest in developing programs to promote purchases of hybrid or electric cars.
- A large portion of electricity is generated with fossil fuels.

Opportunities

- Diversification of exportations to new markets of Central and South America, in order to avoid dependence on US market conditions.
- Growth in the segments of other countries in which we are currently producing vehicles and autoparts.
- Enactment of the new financial and energy reforms in Mexico.
- Eliminating the tax for new vehicles (ISAN) and car ownership taxes,
- Supporting and promoting purchases of cars with cleaner technology.
- Attracting new investments that will result in more direct and indirect jobs.
- Significantly reducing car thefts.
- Eliminating or reducing customs duties in South American countries.
- Creating a domestic program for vehicle renewal.
- Internal growth of the automobile market in the US.
- Improving the costs, services and quality of the distribution systems of the autorparts industry.

Threats

- New political and social conflicts in countries to which Mexico exports vehicles and autoparts.
- Slow recovery of the European markets.
- Lack of commitment by certain countries to preserve commercial agreements.
- Continuing to allow the entry of used cars from the US.
- An increase in the levels of insecurity due to the war against organized crime.

Main legislation applicable to the automotive industry

Legal Provisions

Foreign Investment

In Mexico, the legal framework that regulates investment by non-Mexican individuals or entities is the Foreign Investment Law (FIL), whose purpose is to establish and regulate the activities in which those individuals or entities are allowed to participate, assigning percentages, limits, restrictions or conditions for participation percentages.

The FIL specifies activities reserved exclusively for the Mexican State, those reserved for Mexican entities and individuals and those in which foreign investment is unrestricted or is limited to certain percentages of participation.

In the case of certain restricted activities, the FIL considers exceptions, which are ultimately subject to a resolution issued by the regulating authority, that in this matter is the Ministry of Economy.

There are also cases in which foreign investment participation is limited, those limits cannot be exceeded directly, or through trusts, agreements, social or statutory agreements, corporate restructuring, or any other means that provides control or a participation that exceeds what is established in the FIL, except for the case of foreign investment in the share capital of authorized Mexican companies or trusts.

According to the FIL, the companies should stipulate that foreign partners will be considered as Mexicans regarding their shares, partnership interests or rights acquired there under and regarding assets, rights, obligations, concessions, participations or interest of the holders, and therefore they agree not to appeal to the protection of their governments. Otherwise, they must add an exclusion clause clearly stating that the company will not allow foreign investment in its share capital.

In the particular case of the automotive sector, until 1999, companies dedicated to manufacture and assembly of parts, equipment and accessories for this industry, could have a participation of 49% of foreign investment, however, from that year, the FIL was amended to allow 100% participation of foreign investment without the need to secure any kind of permit or favorable resolution from the Mexican authorities.

Nevertheless the increased openness to foreign investment in the sector, companies are required to report to the authorities their financial situation and the changes in their shareholding structure, their share capital and their management (Board of Directors).

Investment in the Mexican Market

The automotive industry is one of the most important and productive value chains in the Mexican economy and although it has suffered the impact of the worldwide economic crisis over the last few years, since 2010 its recovery has been truly remarkable.

We, at PwC, realize that it is one of the industries with the greatest growth potential in Mexico, however, special attention should be paid to the following points and recommendations, to take full advantage of business opportunities offered by this sector and minimize the risks arising from the current regional and worldwide economic situation.

Following is a brief list of the main means for investing in the Mexican market and we will attempt to answer the most frequently asked questions by investors interested in investing in the automotive industry.

Incorporating a new company

The most frequent way of investing in the Mexican market is incorporating a new company. In our experience, we have noticed that foreign investment in Mexico usually participates through a Stock Corporation (S.A.[1]); or a Limited Liability Company (S. de R.L.[1]).

1 For its acronyms in Spanish

The main differences between those two types of organizations are the following:

Stock Corporation (S.A.)	Limited Liability Company (S. de R.L. de C.V.)
The liability of the shareholders is limited to the payment of their shares.	The partners are only required to pay their contributions.
There must be a minimum of two shareholders. The maximum is unlimited. Shareholders may hold more than one share. Different series and shares may be created.	There must be a minimum of two partners. The maximum is 50. No partner may hold more than one partnership interest, unless different rights and obligations are specified.
Company management must be ientrusted to a Sole Administrator or a Board of Directors. They may or may not be shareholders, and are temporary designated.	Company management must be entrusted to a manager or Board of Managers, who may be partners or third parties, temporarily designated or for an undetermined period.
The supreme organ of the company is the Shareholders' Meeting. Shareholders' Meetings may be held at the company's domicile, and may be general or special. Resolutions must be based on the majority established in the bylaws or in the General Corporation and Partnership Law.	The supreme organ of the company is the Partners' Meeting. Meetings may be held at the company's domicile. Resolutions must be based on majority votes of partners representing at least 50% of the share capital.

Common rules

- These companies may be of the Variable Capital type, and may increase or reduce their capital, as resolved at a Shareholders' or Partners' Meeting.

Considerations

- It is important to consider that the S. de R.L. de C.V. and the S.A. cannot quote on the stock exchange.
- If an S. de R.L. de C.V. or S.A. look forward to be positioned in the stock market, they may carry out a conversion process to become a Sociedad Anonima Bursatil (S.A.B.)
- Likewise, there is a subtype of an S.A., named Investment Promotion Corporation, (S.A.P.I.[1])
- The legal framework for a S.A.P.I. is contained both in the General Corporation and Partnership Law and in the Stock Market Law (SML), which was enacted to provide exceptions to the former, with the intent to attract risk capital investors by granting flexibility on covenants of shareholders.

Nonetheless, due to a recent reform of the General Corporation and Partnership Law (GCPL), now the S.A. has almost the same characteristics as the S.A.P.I., which consist of the following:

1. The shareholders may stipulate in the bylaws restrictions for shares transfers, including tag-along and drag-along clauses; establish the basis for excluding shareholders or for allowing them to withdraw.
2. S.A.s and S.A.P.I.s do not need to register or to be supervised by the National Banking and Securities Commission (NBSC).
3. S.A. and S.A.P.I.'s bylaws allow the issuance of several series of shares with different rights and obligations, in order to attract private and risk capital.

The main differences between the S.A. and the S.A.P.I. are the following:

- S.A.P.I.s may acquire their own shares, and are not subject to the prohibition established in the GCPL.
- S.A.P.I.s are not required to publish their financial statements, although such obligation is now an option for the S.A.s due to the recent reform.
- Their management is in charge of a Board of Directors, while the S.A.s may entrust their management to a Sole Director or a Board of Directors.
- The S.A.P.I. may: (a) adopt the management regime of an S.A. or (b) adopt the management regime of a Company Stock (S.A.B.[1])
- The S.A.P.I. may provide for in its bylaws limitations or extensions related to profit distribution or other special economic rights to its shareholders, while the S.A. expressly prohibits excluding one or more shareholders from the profit distribution.

The SML also provides for a subtype of S.A. named S.A.P.I.B.[1], which consists in a transitional entity in order to access the Mexican Stock Market.
S.A.P.I.B.s may list on the stock-market after adopting the S.A.B. regime within three years following the adoption of the S.A.P.I.B. regime.

- S.A.B.s are companies quoted on the stock market, and are therefore public to the business and investing community.
- S.A.B.s are subject to NBSC supervision.
- S.A.B.'s management is in charge of a Board of Directors and a General Director. They are also subject to corporate governance rules.

1 For its acronyms in Spanish

Mergers and acquisitions
Another way of investing is by means of a merger or acquisition of another company. This can be done by three main mechanisms:

a. By purchasing the shares or partnership interest quotas of an existing company.

b. By purchasing the assets of an existing company.

c. By merging two or more companies to create a new one, including the assets and liabilities of such companies.

Strategic alliances
A third option for investing in Mexico is to sign a contract with a company already established in Mexico. That way, a foreign individual or entity may use the infrastructure and/or rights previously acquired by its commercial allies.

Compliance with legislation
We should always take into account, that regardless of the way in which it is decided to invest, parties operating in this industry must comply with all applicable laws, before operations begin, and during business development. Primarily be taken into account, economic competition, environment, tax, labor and administrative rules, as well as obtaining licenses, permits and/or authorizations required for the proper operation.

Labor Reform
On December 1, 2012, the Labor Law was reformed, after extensive debate in the Chamber of Representatives and the Senate.

This reform requires changes in the way the labor relationship was documented, before its publication, in order to comply with the new law requirements and in order to avoid possible payment of substantial penalties.

Among the main changes in the Labor topics the following are considered as those which require special attention:

Harmonization of Law
- Standardization of principles from the International Labor Organization
- Adds the concept of decent and worthy job
- Prohibition of discriminatory practices
- Additions in rights of social interest
- Provisions related to labor harassment
- Principles relating to gender and equity

Subcontracting
With respect to the subcontracting regime, with both related and unrelated parties, new rules are set in order to prevent evasion and avoidance of compliance with obligations of the subcontractor (as an employer).

The legislation also included three important conditions that if all of these are breached, the contractor shall be deemed as the employer for purposes of labor and social security provisions. The conditions are:
a) The (subcontractor) activities may not cover all of the activities, the same or similar as a whole, taking place in the workplace (of the contractor).
b) The activity (of the subcontractor) must be justified by its specialized nature.
c) The activity (of the subcontractor) should not contemplate the same or similar tasks conducted by the rest of the workers of the contractor.
Failure to comply with these conditions, the contractor shall be considered as an employer, including its obligations on social security matters.

Individual Employment Relations
In addition to the common types of labor relationships, the Law now includes the following:
1. By season
2. Probation period
3. Initial training
4. Indefinite contract for fixed and periodic tasks
5. Home office work

Also, the Reform includes rules for the provision of international assignments with Mexican employees.

Obligations of employers (employers legal representatives are included)
- Compliance of safety, health and environment regulations and Mexican Official Rules (NOMs)
- Mandatory handicapped access for entities over 50 employees
- Obligation to make public for the employees a clearly full text of the Collective Bargaining Agreement (CBA)
- Inform employees of the risks and dangers associated to their activities in the workplace
- Paternity leave
- Establishment of policies avoiding harassment and discrimination

Employer's prohibitions
- Discriminatory practices
- No intervention in the internal affairs of the Union
- Prohibition to request certificates of pregnancy
- Prohibition to persuade the resignation, directly or indirectly, for being pregnant, change in marital status or having the care of children

Data Protection Law

Data protection acquired relevance in Mexico when according to the Federal Official Gazette dated June 1st, 2009, it was established as a constitutional guarantee granting every person the right to the protection, access, rectification, blocking, elimination and destruction of his/her personal data, as well as to oppose to its treatment in the terms stated in the Data Protection Law. Therefore, this law is a matter of public policy and is to be observed generally nationwide. Both, individuals and private legal entities processing personal data are regulated under this Law. This brings significant effects such as new obligations, new crimes, adverse publicity, legal actions against moral damages, loss of customers and employees' confidence.

Herein below are some of the general obligations to be complied with according to Law:

- To appoint a Data Protection Officer.
- Create an inventory of the personal data collected by the person/entity (Data Controller)
- Elaborate matrices of personal data processing occurring throughout the entity.
- To make readily available fair collection/privacy statements (considering the different purposes) to Data Subjects.
- Formalize the process to attend Subject Access Requests and the exercise of other Data Subject's rights such as rectification, blocking, erasure and destruction of his/her personal data (in Mexico referred as ARCO rights)
- Insert privacy clauses in contracts.
- To implement a privacy policy and the necessary proceedings and resources to enforce it.
- To enable technical and organizational measures to prevent unauthorized or unlawful processing of personal data.
- Develop business continuity and disaster recovery plans.
- Promote data protection and privacy culture among employees (Training)

Infringements to the Law will be punished by IFAI (Federal Institute for Access to Information and Data Protection) with fines from 100 to 320,000 days of the General Current Minimum Wage in Mexico. Regarding infringements committed in processing sensitive personal data, sanctions may be doubled.

It is noteworthy to consider the crimes related to unlawful processing of personal data:

- Three months to three years imprisonment, to any person who authorized to process personal data, for profit, causes a security breach affecting the databases under his/her custody.
- Six months to five years imprisonment, to any person who, with the aim of achieving unlawful profit, processes personal data deceitfully, taking advantage of an error of the data subject or the person authorized to transmit such data.

With regard to sensitive personal data, the penalties referred will be doubled.

Law to Prevent Money Laundering

The Law to Prevent Money Laundering is integrated by 65 articles scattered in eight chapters. Its main purpose is to impose the obligation to file a notice to the authority regarding certain commercial or professional transactions for the individuals who usually or professionally perform the following activities: the commercialization or distribution of vehicles; armor-plating vehicles services; the loan or guarantees offer by non-financial entities.

Also, the Law includes gambling, competitions or raffles; the issuance or marketing of services, credit or prepaid cards, as well as any cards that are considered an instrument to store the monetary value when issued or commercialized by non-financial entities; the issuance or commercialization of travel checks by non-financial entities; the construction services or the development of real estate; the commercialization of precious metals and stones, jewelry or watches; the auction or commercialization of works of art; the service of transfer and custody money; certain operations in the rendering of independent professional services; certain operations in the rendering of attestation services; the reception of donations; certain operations in the rendering of foreign trade services by agents or customs brokers, as well as the establishment of rights to use real estate.

The Law states that in the case that a commercial transaction reaches a certain amount (calculated based on the legal minimum wage) the natural person or entity shall identify its client and in some cases, file a notice of the transaction before the authority; the Rules for the Law to Prevent Money Laundering establish that the notice shall be sent to the Tax Administration Service (SAT).

Moreover, the Law states that non-compliance with the filing of the notice shall be administratively penalized; which means, that penalties have been established and may consist of pecuniary fines or even in the revocation of the Notary Publics' registration or the cancelation of the authorization granted to customs brokers.

It is important to point out that the filing of notices is not the unique obligation established in the Law to Prevent Money Laundering, as the individuals obliged by the Law (in accordance with the amount of the transaction) shall comply, among other things, with training their personnel, with their registration before the SAT in order to be able to file the notices, with the establishment of systems for the custody of information and with the drafting of internal manuals whereby it is detailed the manner in which the business is in compliance with the Law.

An issue to highlight is that for the first time in a federal legislation the use of cash is restricted in certain transactions connected with assets considered of great value, with the purpose of obstructing the high volume of cash entering into the formal economy. In this sense, for example, it has been prohibited to pay off in cash for real estate, vehicles or watches, jewelry, precious metals and stones when they overflow certain amounts.

It is important to point out that the compliance of this Law will have as a consequence that a wide commercial sector will have in its possession personal private information regarding their clients, since they are obliged to identify them, they must know their information. Thus, whoever is obliged to file notices to the authority shall comply with the Federal Law on the Protection of Personal Data in order to avoid any penalty in the terms established in said Law.

The last chapter of the Law named "Regarding Crimes" establishes several activities constituting crimes which may be committed by individuals or bureaucrats and could be punished with up to 10 years of prison; for instance, to provide fake or modified information to be incorporated into a notice or to amend or to modify the information contained in a notice. On the other hand, the bureaucrats who have access to the information contained in the notices and make public the information without this being required for the compliance of their functions, could be sanctioned with up to 10 years imprisonment.

Tax Obligations

Corporate taxpayers in Mexico are required to:

- File, no later than March of the following year, an annual tax return[1] showing the result or taxable profit for the period and the basis for Employees' Statutory Profit Sharing (PTU).
- File, no later than February, a number of informative returns reporting on specific points such as wages and salaries, taxes withholding, payments made to foreign residents, uncollectible accounts, donations made, tax withheld from third parties, dividends paid, payments made to related parties, etc.
- Prepare a statement of financial position and conduct an inventory count of stock at the year-end closing.
- Taxpayers subject to the provisions of Title II of the Income Tax Law (ITL) which have declared taxable income of $644,599,005 or more in the immediately preceding tax period; taxpayers whose shares have been placed among the general investing public and on stock exchanges; business entities operating under the optional tax regime for groups of companies; State owned entities (Paraestatal) of the Federal Public Administration; foreign entities with permanent establishments located in Mexico (only for the activities carried out in such permanent establishments); and Mexican business entities regarding the operations carried out with foreign business entities, must file an informative return reporting on their tax situation by June 30 of the year immediately following the close of the period in question.
- In 2014, individuals engaged in business operations and business entities which in the immediately preceding period have received taxable income exceeding $100 million, whose assets value exceeds $79 million or which have employed at least 300 employees in each of the months of the immediately preceding period may opt to have their financial statements audited by an authorized public accountant. Said option is not available to State owned entities of the Federal Public Administration.

In order to exercise this option, the income tax return filed in the terms established in the law must specify that the option is to be taken.

1 A report is issued on value added tax (VAT) for each month of the year.

The audit report issued by the registered public accountant must be filed no later than June 15 of the year immediately following the end of the year in question.

In those cases, the requirement to file an informative return reporting on the tax situation is considered to be complied with:

- An authorized public accountant must issue a report on compliance with Social Security and Workers Housing Fund obligations, when certain assumptions apply.
- Have an authorized public accountant report issued on compliance with local tax obligations, i.e. the average number of employees, the cadastral value of real property or bi-yearly water consumption.
- Have a transfer pricing study made to demonstrate that operations with local and foreign related parties were conducted at fair market value.
- Companies engaging in foreign trade must submit certain specific information to the Department of the Economy.

Certain additional tax obligations must be complied with, depending on the operations conducted by each company. Those operations must therefore be analyzed separately.

Income tax - IT

IT is payable in Mexico by parties resident in the country (on all income received in the period) and by parties resident abroad with a permanent establishment in Mexico or parties receiving income from a source of wealth located in Mexico.

In general terms, IT is calculated by applying the 30% rate to the tax result for the period.

The tax result is determined by subtracting authorized deductions (such as cost of sales, investments in fixed assets and financial costs and expenses) from taxable revenue for the period, then subtracting PTU paid. Unamortized tax losses[1] not amortized in preceding periods are subtracted from the tax profit, when applicable.

The Mexican tax system is very strict when compliance with obligations such as filing informative returns and issuing invoices is required in order to be entitled to apply authorized deductions. Special care should therefore be taken to ensure the tax compliance.

Additionally, only electronic invoices (CFDI) are accepted; all other types of invoices have been eliminated.

1 It results when taxable income is less than the authorized deductions and PTU

Certain advantages

The after-tax earnings account (CUFIN)

The ITL requires entities to keep a CUFIN to have the track of its profits on which tax has been paid. Dividends paid from that account are not subject to income tax as of December 31, 2013.

A transitory provision establishes that for periods from 2001 to 2013, after-tax earnings must be determined as per the ITL in effect at such tax period.

The provision does not specify the mechanism for determining CUFIN for periods from 1975 to 2000.

The capital contributions account (CUCA)

Companies are required to keep an account called the CUCA to record capital contributions, which should not give rise to income tax when reduced, reimbursed or amortized.

It should be remembered that it is necessary to apply controls, keep records and ensure that there is documentation supporting the CUCA and the CUFIN, such as annual tax returns and tax reports, which must be kept throughout the lifetime of the company.

Tax losses

The ITL explains the treatment applicable to a company's tax losses, when, in the period, deductions declared exceed income. Those losses can be subtracted from tax profits in a ten year carry forward, until they are exhausted.

Reduction of provisional tax payments

Taxpayers are required to make provisional income tax payments on account of annual income tax, based on a profit factor determined on tax figures for the preceding period. When that profit factor is considered to exceed the factor actually corresponding to those payments, the tax authorities can be requested to authorize a reduction in said payments as from the second half of the period.

Maquiladora industry

The maquiladora industry is born from the need to reduce operating costs of large transnational corporations, through low cost labor. In Mexico, the industry is a creative source of jobs, so the building on the premises of this industry has proliferated since the 60s. In fact, it started in 1965, and its history of international outsourcing (maquila process) through the so-called Border Industrialization Program, which aimed to solve the same problem of unemployment in the north border of our country, and reduce the flow of migrants to United States of America. Later analysis is presented regarding current foreign trade programs Mexican authorities which provide.

The maquila principal resident in a country with which Mexico has signed a double taxation treaty will not be considered to have a permanent establishment in Mexico as concerns maquila operations when maquiladoras determine their profits as per the “Safe Harbor” rules (6.9% of assets or 6.5% of costs and expenses).

The taxpayer may arrange an advance pricing agreement (APA) with the tax authorities. However, it is not entirely clear whether or not this prevents the party resident abroad from being considered to have a permanent establishment in Mexico.

The new Income Tax Law defines the “maquila operation” concept and establishes the condition that income associated with production operations must arise entirely from maquila operations in the terms of the Decree for the Promotion of the Manufacturing, Maquiladora and Exportation of Services Industry (the IMMEX Decree). It is understood that all goods processed, repaired and sold in Mexico must be exported (including virtual exports).

Parties resident abroad with shelter maquila operations in Mexico will continue to be entitled to protection from being considered to have a permanent establishment, for a maximum period of four years.

International treaties

Mexico has signed a number of international treaties for the avoidance of double taxation with numerous countries, including the following:

Argentina[1]	Finland	Latvia	South Africa
Australia	France	Lithuania	South Korea
Austria	Germany	Luxembourg	Spain
Bahrain	Greece	New Zealand	Sweden
Barbados	Hong Kong	Norway	Switzerland
Belgium	Hungary	Panama	The Czech Republic
Brazil	Iceland	Peru	The Netherlands
Canada	India	Poland	Ukraine
Chile	Indonesia	Portugal	United Kingdom
China	Ireland	Qatar	United States
Colombia	Israel	Romania	Uruguay
Denmark	Italy	Russia	
Ecuador	Japan	Singapore	
Estonia	Kuwait	Slovakia	

In order to apply the benefits contained in the tax treaties as concerns operations carried out between or among related parties, the authorities may request the party resident abroad to demonstrate the existence of juridical double taxation in the form of a sworn statement.

Tax incentives

Promotion of the national economic development (PROMEXICO)

The Promexico fund was created by Presidential Decree on June of 2007, and focuses on contributing for the attraction of direct foreign investment, through the granting of support to projects that promote the national economical development.

The fund is operated through a trust fund which is operated by the National Bank of Foreign Commerce (BANCOMEXT) and is integrated by resources provided within the Federal Budget for the Ministry of Economy.

The fund supports Companies that provide within its business activities, the following:

a) Infrastructure
   (i) Physical (Civil engineer works and equipment).
   (ii) Technological (Installation of laboratories, design and test centers).
b) Buildings and constructions.

1 Applicable for International Transport

c) Equipment (purchase and installation of machinery and equipment).
d) Innovation and Technological Development (payment of royalties, licenses and intellectual property).
e) Technological transfer (expenses involved for the transfer of technology required for the development of the project).
f) Development of Human Capital (Training employees in Mexico and abroad).

Companies contracting persons 65 and over

The ITL provides individuals and business entities subject to income tax with an incentive consisting of deducting (from taxable income) an additional 25% of salaries actually paid to persons of 65 years old or over.

Incentive for employing special needs or blind persons

Employers may deduct IT withheld from employees with physical disabilities, such tax will be refund.

The December 11, 2013 decree provides individuals and business entities subject to income tax with an incentive consisting of deducting (from taxable income) an additional 25% of salaries actually paid to persons with motor incapacity requiring the permanent use of prosthesis, crutches or wheelchairs; mental incapacity; hearing incapacity or speech impediments with 80% or more of normal capacity; and blind persons.

Tax incentive for investments in Mexican motion picture production (FIDECINE)

Taxpayers may apply a tax credit of the amount contributed to investments in Mexican motion picture productions, against IT for the period.

That credit is not subject to IT, and may not exceed 10% of IT payable in the period immediately preceding that in which it is applied.

Investments in Mexican motion picture projects are considered to be only those made in Mexico, as well as the human, material and financial resources necessary for the project.

Tax incentive for investments in Mexican theater production

A tax incentive is provided to IT taxpayer equivalent to the amount contributed to investments in Mexican theater production projects; that incentive is applied to IT for the period and provisional payments for that same period.

That credit is not subject to IT and may not exceed 10% of the taxpayer’s IT for the immediate preceding period.

Program for the Development of High-Technology Industries (Prodiat)

Prodiat rules were published on July 21, 2009. The objective is to promote the preservation and improvement of human capital developed by companies, as well as to provide temporary assistance for the transfer and adoption of technologies, based on market deficiencies in those industries.

Prodiat support consists of subsidies contemplated in the Federal Disbursement Budget, and are provided to beneficiaries under certain operating rules and other legal provisions based on objectivity, fairness and transparency criteria, as well as on the feasibility and social economic impact of the project.

New truck and bus tax incentive

Another tax incentive makes it possible to replace vehicles used to provide federal freight and passenger transportation service with new vehicles.

That incentive is applicable to authorized manufacturers, assemblers or distributors resident in Mexico that sell:

- Tractor-trailers
- Unit buses
- Buses

The tax incentive consists of a credit equivalent to the lowest of the price paid for used vehicles, 15% of the price of a new vehicle and the amount specified in the Decree; the ceiling is $161,000 Mexican pesos for fifth-wheel trucks, $103,000 Mexican pesos for three-axle minibuses, $69,000 Mexican pesos for two-axle minibuses and $138,000 Mexican pesos for full size-buses factory- outfitted with more than 30 seats.

The Decree establishes that the tax incentive determined may be credited against IT, against IT withheld from third parties, and against Value Added Tax (VAT) payable in provisional payments, definitive payments or in the annual return, as the case may be.

New vehicles tax (ISAN)

This tax is payable when a car is acquired by the final consumer. Depending on how the car is acquired, tax would be due as follows:

- Tax must be paid when new cars are acquired in Mexico by individuals or legal entities if they are final consumers.
- For new cars imported into Mexico by individuals or legal entities, it must be paid by customs declaration.

Taxable person
Individuals or legal entities acquiring cars provided they are the final consumer.

Tax due
The tax is calculated by applying rates and tariffs corresponding to the price of the car, including optional equipment, regular or luxury, with no discounts, reductions or rebates.

Cars seating up to 15 passengers are subject to rates depending on the car's price, from 2% to 17%.

Rate

Lower limit (MXN)	Upper limit (MXN)	Fixed rate (MXN)	Rate applicable to amounts exceeding the lower limit
0.01	223,744.75	0.00	2.0%
223,744.76	268,493.64	4,474.82	5.0%
268,493.65	313,242.72	6,712.37	10.0%
313,242.73	402,740.38	11,187.26	15.0%
402,740.39	onwards	24,611.88	17.0%

Certain rules apply to tax payment on imported cars, based on the type of car and other factors.

However, consumers are exempted of this tax when the sales price (including optional equipment, regular or luxury) does not exceed 208,555.47 MXN. Furthermore, when the price goes from 208,555.47 MXN to 264,170.27 MXN, the exemption would apply to 50% on tax payment.

Tax period
It is paid only once when final consumer, an individual person or entity, acquires the new car.

Annual circulation tax (ACT)

Taxable event
Tax is due for cars circulating in Mexico.

As of 2012, this tax ceased to be a federal tax and it is now up to each state to impose it, on the basis of the foregoing. For the most part, Mexican states have exempted the ACT when taxpayers have properly complied with previous payments and if they have already paid for the annual plates.

Taxable person
Individuals owning vehicles circulating in Mexico

Tax due
ACT is calculated on the basis of the features of the vehicle – such as the model, car brand, year, version and price – by using tables and percentages, which are updated annually. The percentage of ACT would depend on the Mexican state in which the vehicle is to be registered and on the type of vehicle in question.

It is important to point out that the tax is gradually reduced according to the vehicle ages, and no tax is payable on vehicles when ten years or more have passed since they were manufactured.

Tax period
Payment must be made on a yearly basis starting when the car was acquired by final consumer.

Circulation dues

Vehicular circulation card
The federal government requires all states to update its vehicle fleet registry every three years, which usually takes place through the change of number plates; this situation could be a long process with high costs, so recently the Mexican government requested that, rather than plate replacement, there should be a renewal of the vehicular registration card.

It should be mentioned that the objective is to contribute to the updating of the vehicular register; this new instrument allows for legal certainty of the corresponding car.

The vehicular circulation card is valid for a three-year period and the cost is related to the type of car and use.

Plate Number
Number plates are part of the registration dues and are calculated on the basis of the features of the vehicle and characteristics of users: model, make, year, version, type of user, vehicles driven by the handicapped etc.

Payments are made when the new or used vehicle is registered or any change to the situation occurs (user, type of license etc.).

Vehicular emissions test
There is a mandatory program for all internal combustion motor vehicles registered in Mexico which consists of verifying all emissions issued by such vehicles during the year; motorcycles and hybrid vehicles (gas/electricity) are not subject to this program.

All owners, keepers and drivers of motor vehicles registered in Mexico and circulating with metropolitan plates are obligated to comply with this program.

The cost of the vehicle inspection services would depend on the type of certificate that is delivered to the user, which could consist on the following:

Certificate 00: Allows free circulation on all days and the emissions inspection must be performed every two years.

Certificate 0: Allows free circulation on all days and the emissions inspection must be performed every year.

Certificate 1: Emissions inspection must be performed every year and vehicles are not allowed to circulate one day a week.

Certificate 2: Emissions inspection must be performed every year and vehicles are not allowed to circulate two days a week.

2014 Tax Reform

Overview

In October 31, 2013, the Mexican Congress approved a number of tax amendments for the 2014 period, which were published in the Official Gazette. Most of those amendments went into effect on January 1, 2014.

As a result of the different measures approved, the federal government expects to receive revenue of $4.4 trillion pesos, which is 12.82% above the 2013 revenue budget.

The 2014 Federal Revenue Law estimates an average peso/dollar exchange rate of $12.90, inflation of 3%, and average price of $85 per barrel of crude oil, 3.9% growth in the Gross National Product (GNP), internal and external indebtedness of up to $570,000 million of pesos and $10,000 million dollars, respectively, accounting for the equivalent of 16% of total budgeted revenue.

Estimated revenue arising from taxes, Social Security dues and government fees rose 6.25, 4.76 and 2.5% respectively over 2013. The principal increases are seen in a hike of 153% in excise tax and 23% in income tax.

The tax amendments are aimed at boosting tax revenue, focused mainly on strengthening the income tax base, which had been eroded over the last few years by a number of incentives for investment, savings and support for specific sectors.

The result of the tax amendments coincides with the commitments signed by the Federal Executive in December 2013 in the Pact for Mexico as concerns strengthening the State's financial capacity and conducting a comprehensive revision of the policy for subsidies and special regimes with a view to establishing an efficient, transparent and progressive system.

Following is a summary of the main amendments:

ITL

A new ITL has been approved, which eliminates the judicial and administrative resolutions pertaining to the law in effect up to 2013. The Regulations to the ITL will remain in effect to the extent that they do not conflict with the new law.

The new ITL eliminates and limits, among others, the following tax regimes and deductions:

Tax regimes eliminated:

1. The tax consolidation regime, although a new regime has been created for corporate groups wishing to defer income tax over a maximum of three years.
2. The special regime for Real Estate Investment Companies

Tax deductions limited:

1. The maximum amount deductible for restaurant expenses is 8.5%, $200 daily for leases, $130,000 for investments in automobiles, and 53% and 47% for contributions to pension and retirement funds and exempt salaries paid to workers.
2. Interest, royalty or technical assistance payments made to a party resident abroad that controls or is controlled by the taxpayer, when:
   a) The company receiving the payment is considered to be transparent, except when the operation is carried out at market value and its stockholders or associates are subject to income tax on income received through the company located abroad.
   b) The payment is considered to be nonexistent for tax purposes in the country in which the foreign party is located.
   c) The foreign company receiving the payment does not consider it to qualify as taxable income.
3. Payments that are also deductible for a related party resident in Mexico or abroad, unless the related party includes income generated by the taxpayer in its own taxable income, in that period or in the following period.
4. The immediate deduction of fixed asset investments.

In relation with the foregoing, there are current tax provisions regarding the deductions mentioned which are unclear, for this reason it is necessary to analyze them in every specific case.

It is important to mention that those limitations in the deductions pointed out are going to impact directly in the determination of the effective tax rate and also in the calculations of the deferred IT provision.

Tax consolidation

The new ITL eliminates the tax consolidation regime under the following scenarios:

1. The regime remains in place for groups that opted to consolidate as from 2010 and have therefore been consolidating for less than five years.
2. Groups that have been consolidating for more than five years must deconsolidate and have three options for determining and paying deferred tax.
3. Opt for a new regime

Following are the features of each of the aforementioned scenarios:

Continuation of the tax consolidation regime

The new ITL establishes that groups authorized at December 31, 2013 to determine a consolidated tax result in the terms of the ITL in effect up to December 31, 2013 and are within the term of five years mentioned it article 64 of that law, may continue to determine tax as per the provisions contained in Chapter VI of Title II of the repealed law during the years remaining of that five-year period.

Year in which consolidation began	2010	2011	2012	2013
Last year of consolidation	2014	2015	2016	2017

Until they complete the aforementioned term, those groups will continue to be entitled to the following benefits:

1. Immediate application (in the year in which they arise) of the tax losses of the controlling and the controlled companies of the group against the tax profits of other companies of the group, thus streamlining cash flows as a result of deferring the payment of income tax at the group level.
2. Deferral, over a period of five years, of income tax on dividends not arising from the CUFIN, paid among the companies of the consolidating group.
3. Calculating the tax cost of shares of the controlling company considering consolidated tax results, which generally means an increase in the cost of shares.

Once the five-year period established in article 64 of the ITL has elapsed, the controlling company must determine deferred tax as per either of the two provisions contained in section XV of the ninth transitory article of the new ITL, and pay income tax by the following deadlines as from conclusion of the five-year period:

1. 25% in May of the first tax period
2. 25% in April of the second tax period
3. 20% in April of the third tax period
4. 15% in April of the fourth tax period
5. 15% in April of the fifth tax period

The tax to be paid (with the exception of the first 25% of deferred tax) must be restated.

Procedures for determining the tax arising from deconsolidation

The transitory provisions contemplate the following optional procedures for calculating tax on group deconsolidation:

1. Applying the deconsolidation rules contained in article 71 of the 2013 ITL.
2. Applying the optional procedure established in section XV of the ninth transitory article of the new ITL.
3. Calculating, for the periods from 2008 to 2013, tax deferred in the terms of article 71-A of the ITL in effect up to 2013 and paying that tax by the deadlines established in that law.

Alternatives 1 and 2 for determining tax resulting from deconsolidation consist of recognizing the effects in the 2013 period by filing an amended return, considering the following items:

1. Special consolidating items
2. The unamortized tax losses of the controlled company and the unamortized individual tax losses of the controlling company.
3. Losses on the sale of shares
4. Dividends distributed among companies of the group, not arising from the CUFIN
5. The difference between the consolidated CUFIN and the individual CUFINs of the controlled and controlling companies.
6. Recoverable asset tax

The procedures for calculating deferred tax as per alternatives 1 and 2 above differ in that under alternative 1, all the above items are included in the 2013 tax result, while under alternative 2, only the first three items are included and the tax on dividends and CUFIN differences are calculated separately.

Special consolidating items
A controlling company with special consolidating items prior to 2002 arising from the sale of shares, land and fixed assets among the companies of the group may pay the respective deferred tax when the items giving rise to those items are sold to parties outside the group.

Dividends not paid from the CUFIN
The controlling company need pay no tax on dividends paid among companies of the group prior to January 1, 1999, even when not arising from the CUFIN.

Furthermore, the group may opt for tax on CUFIN dividends not paid from 2002 to 2013 to be paid by the controlling company that distributed the dividends or profits, no later than the fifth month following the month in which deconsolidation occurs (May 2013).

In the latter case, a controlled company may credit dividend tax against income tax payable for the period and the two following periods, in the terms of section I of article 10 of the Income Tax Law in effect as from January 1, 2014 and must recognize the effect in the balance of the CUFIN at January 1, 2014. On the other hand, the company receiving the dividend may increase its CUFIN balance by the restated amount of the dividends or profits on which tax has been paid.

In order to take that option, the controlling company must notify the SAT by the last day of February 2014 in a free-form statement containing the name of each of the companies that will be making the tax payment, the amount of the dividend or profit and the respective tax on each, as well as the name of the company or companies that have received the dividend or profit in question and will be increasing the balance of their CUFIN as a result of taking that option.

CUFIN differences
For the purpose of the CUFIN differences, only the individual balances of the controlling and controlled companies are considered, as well as the consolidated CUFIN, arising from January 1, 2008 to December 31, 2013.

The aforementioned items need not be included in the deconsolidation calculation when the controlling company has already paid deferred tax on those items or when that tax is still pending because it is subject to the payment schedule established in article 4 of the transitory provisions of the 2010 ITL or article 70-A of the ITL.

Lastly, the controlling company must add (to income tax determined on the deconsolidation) deferred tax arising from comparing the CUFIN and reinvested CUFIN balances for the periods from 2004 to 2007 on which it has opted to defer determination and payment of the respective tax.

Deadlines for paying the tax
The tax resulting from deconsolidation must be paid to the tax authorities as follows:
1. 25% no later than the last day of May 2014
2. 25% no later than the last day of April 2015
3. 20% no later than the last day of April 2016
4. 15% no later than the last day of April 2017
5. 15% no later than the last day of April 2018

That tax (with the exception of the first 25%) must be restated for inflation.

Additionally, taxpayers which at December 31, 2013 are subject to the payment schedules contained in the fourth transitory provision for 2010 or article 70-A of the ITL in effect up to December 31, 2013 must continue paying tax deferred under consolidation in 2007 and preceding years, as per the aforementioned provisions, until completing payment according to the specified schedule.

Groups opting to determine deferred income tax as per article 71-A of the repealed ITL
Controlling companies which in 2013 have opted to determine deferred income tax as per the procedure contemplated in article 71-A of the repealed ITL may opt to determine the effect of deconsolidation considering income tax deferred from 2008 to 2013 as per the schedule of partial payments, as follows:

Period	Year of option	Year in which payment concludes
2008	2014	2018
2009	2015	2019
2010	2016	2020
2011	2017	2021
2012	2018	2022
2013	2019	2023

Asset tax
The following is applicable to both the controlling and controlled companies as concerns asset tax payable by the controlling company as a result of deconsolidation and recoverable tax:
1. The controlling company must determine asset tax payable by subtracting asset tax paid by its controlled companies (recoverable) from consolidated asset tax paid in prior periods (recoverable). The tax payable is the amount by which the controlled companies' recoverable tax exceeds consolidated recoverable tax.
2. The tax may be paid in installments as specified in article 70-A in effect in 2013, rather than the month following deconsolidation.
3. The controlling company must provide the controlled companies with a certificate that will allow them to recover the respective asset tax.

A new optional regime for groups of companies
The tax consolidation regime will be replaced by a new optional regime under which tax payment is partially deferred over a three-year period.

Each company will determine its tax on the basis of a consolidated tax result factor. That factor is determined by dividing the consolidated tax result by the sum of the consolidating portion of the positive tax results of the companies of the group.

The consolidated tax result for the period is determined by adding the tax results of the companies of the group and subtracting the tax losses of the remaining companies of the group (all in the consolidating portion).

The consolidating portion is determined as follows:

1. The consolidating portion of the controlled companies is the average daily direct or indirect shareholding of the controlling company in the controlled companies during the period.
2. For the controlling company, the consolidating portion is 100%.

The controlling and controlled companies must pay restated deferred income tax on the same date on which they are required to file the return for the period following that in which the three-year period concludes.

It is important to mention that after the procedures publication pointed out for deconsolidation, the tax authorities have issued specific rules in order to clarify these procedures.

The additional tax on dividends:
Residents abroad will be subject to an additional 10% tax on dividends paid from profits generated as from 2014, payable via withholding by the paying entity; considered a definitive payment.

Changes to special regimes and authorized deductions:
Value Added Tax Law
Operations conducted in the border zones are subject to the general 16% rate, instead of 11%. Temporary imports, exempt of VAT, will pay VAT as of 2015, unless a "VAT Certification" is obtain, such certification will allow obtaining and automatic tax credit for the VAT trigger when importing goods.

Federal Tax Code
Among others

Tax mail box:
Entities registered at the tax office will be assigned a tax mail box on the SAT webpage which the tax authorities can use to notify the taxpayer of any action or resolution, including those with recourse, and on which taxpayers are required to file requests or notifications and to comply with official requests for information.

That provision will go into effect for business entities on June 30, 2014 and for individuals on January 1, 2015.

Accounting
Taxpayers must provide the tax authorities with documentation attesting to loans made or received. Taxpayers must also enter their accounting records into the SAT webpage on monthly basis from July 1st, 2014.

Digital Receipts
Issuance of digital receipts over the Internet (CFDI for its acronym in Spanish).

According to the approved tax reform to go into effect on January 1, 2014, taxpayers must now issue CFDI (digital receipts over the Internet), which must be issued by generating an XML file and be certified by a third party known as an Authorized Certification Supplier (PAC). All provisions allowing the use of other types of receipts have now been repealed.

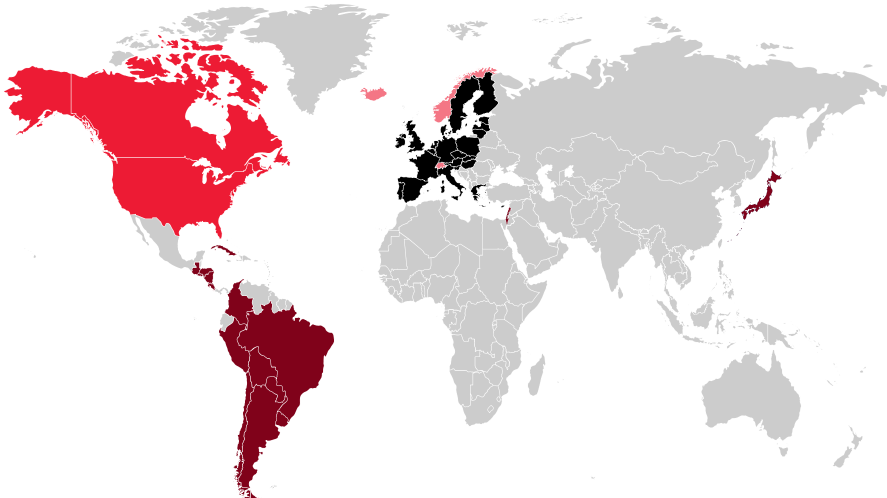
Taxpayers must now issue a CFDI for the payments made to their employees, which means that taxpayers must obtain this information from their current payroll systems and adapt it to the new requirements.

Printout with no tax effects
A printout of a CFDI merely represents the existence of the underlying XML file. Therefore, as concerns tax deductions and credits, taxpayers must validate their authenticity as per the requirements established in the general rules issued by the tax authorities, and then store them for a period of five years.

Flat Tax Law and Cash Deposit Law
Both the flat tax and the cash deposit tax have been repealed. However, entities belonging to the financial system must report annually on cash deposits received by taxpayers in accounts opened in their name when the total amount exceeds $15,000 per month.

Foreign trade

Mexico has diverse programs to support the automotive industry, given the importance of this sector in the Mexican economy.



European Union (EU)*

European Free Trade Association:
- Iceland
- Norway
- Switzerland
- Liechtenstein

North America:
- United States
- Canada

Other countries:
- Argentina
- Bolivia
- Brazil
- Chile
- Colombia
- Costa Rica
- El Salvador
- Guatemala
- Honduras
- Israel
- Japan
- Nicaragua
- Perú
- Uruguay

Notwithstanding the above, it is worth mentioning that Mexico has an extended treaty network such as Free Trade Agreements which allow to import goods under preferential duty rates. Nowadays this network includes 10 treaties with 45 different countries around the world.

* Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden, UK.

Temporary imports (IMMEX) previously known as Maquilas

The Ministry of Economy (SE) created The Decree to Promote Manufacturing, Maquila and Export Services Companies (IMMEX) published in November 2006. This Decree consolidates the Maquila and PITEX programs (the previous temporary import programs), nullifying the PITEX program. Entities exporting at least US$500,000 or 10 percent of their production may enter into a IMMEX program authorized by SE and rewarded with the following benefits:

- Temporary (duty-free) imports (raw materials):
  For up to 18 months for raw materials, supplies and packing materials used on the exported production.
- Exemption from import duties:
  On raw materials, fuels, lubricants, spare parts, and other consumables used in the production of export goods.
- VAT will be returned within 20 days if there is a credit balance.
- Permanent Establishment protection, as long as regulations are complies.

Temporary imports are exempt from customs duties (except for fixed assets) and will pay VAT as of January 2015. Although, if certain requirements are met, is possible to obtain an automatic tax credit for such VAT, throughout a “VAT Certification”.

The life of an IMMEX program is indefinite as long as the company complies with the provisions, including:

- Generate a foreign trade operations annual report according to the program;
- Keep an automated inventory record to control the merchandise imported and exported during the life of the program.
- Export merchandise in 18 months, at the latest.
- Zero rate of VAT is applicable to exports, even when they are physically exported by a third party, provided they remain under the temporary importation regime.

IMMEX includes the services authorized in the Maquila programs, as well as the additional services of repairing, cleaning, quality control testing, packing, painting, greasing activities and technological support services (software).

On December 2012, the Mexican ITL, was amended, to include modifications set in the 2010 IMMEX decree, and include a definition for Maquila operations (toll manufacturer):

a. As of July 2014, all revenues associated with productive activities must derive solely from Maquila activities.
b. Raw materials are supplied by a foreign resident (with whom the Maquila has a maquila contract) are temporarily imported to be processed, transformed or repaired and returned abroad, in accordance with the Mexican Customs Law and the IMMEX decree, including virtual import-export customs declarations. For this purpose it would not be necessary to export scrap or waste.
c. The Maquila would also be permitted to have goods imported under the permanent regime and local purchases can be made, as long as such goods are consumed in production or are exported with the temporarily imported inventory under the IMMEX program.

d. Process, transformation or repair of goods would be required to be performed with temporarily imported Machinery & Equipment (M&E) and property of the foreign resident. For this purpose, at least 30% of the M&E used for Maquila operations must be property of the foreign resident and temporarily imported under the IMMEX. Such M&E cannot be previously owned by the Maquila or a Mexican related party.
   - M&E used in Maquila operations could be complemented with fixed assets that are property of the Maquila, or another Mexican unrelated party which provides those goods in a lease agreement.
   - Note that specific rules for determining the percentage of M&E would be applicable according to the specific rules of the tax authorities, which would be published.
   - The limits for M&E was not applicable to companies that were operating under an IMMEX program as of December 31, 2009. Nonetheless, such provision will be void on January 2016.

e. Companies must fulfill all requirements established in articles 2 and 216bis of the ITL, and it is not considered a Maquila activity when goods transformed or repaired are sold in Mexico, unless such sale is documented with an export customs declaration (i.e. virtual exportations). Therefore, local sales would not ordinarily be deemed to be operations described in ITL articles 2 and 216-bis.

Sectorial Relief Programs (SRP)

The SRP provides companies a preferential tariff rate to import goods intended for production, regardless of the country of origin, and charges preferential rates (foreign trade taxes from 0% to 5%) to export the resulting products.

The authorized sectors in which companies are able to charge preferential rates in the importation of goods are the following:
- Vehicle and auto-parts industry
- Electronic industry
- Capital goods industry
- Chemical industry
- Rubber and plastic manufacturing industry
- Steel industry
- Leather and fur industry

The program lifecycle is indefinite as long as the company complies with the law provisions, such as the production of other imported goods and the filing of an annual report.

Bonded Warehouse

Bonded Warehouse regime consists of introducing for a limited period of time, foreign, national or nationalized goods into authorized warehouses, with the purpose of being stored for safekeeping, exhibition, distribution, transformation or to be repaired, as long as such goods are strictly controlled.

The main benefits of said regime are as follows:

Neither import duties nor countervailing duties will be paid, except for those cases contemplated within the Free Trade Agreements Rules prevailing accordingly.

Non-tariff restrictions and regulations do not have to be complied with, except for those regarding animal and vegetable sanitation, public health, environmental and national security.

Duties and VAT will be triggered only if goods are extracted into domestic market, bonded via a definitive import.

Import duty drawback

Under import duty drawback, all exporters (including indirect exporter suppliers) are entitled to the refund of import duties paid up to one year before on imported merchandise integrated into exported goods or sold to other entities that physically transport the exported assets.

This document contains the road-signs necessary to navigate safely through a sector opening up to world and national dynamics full of surprises. Throughout the different sections, by analyzing the figures and indicators provided, the reader will find areas of opportunity, as well as unforeseen situations.

As it can be seen throughout this document, the road-signs showing the way (expanding markets and speedily recovered competitiveness) are not unmovable; they sometimes shift in a positive manner and sometimes towards areas of uncertainty, such as the frequent changes in Mexican legislation. But those areas have to be dealt with and imply changes in strategy.

However, if the details contained herein are taken into account, the players in this industry will feel more confident in charting their way, with the aid of this PwC report, which has been designed to assist in planning future strategy. What is important to us is that this update will be instrumental in working out the best strategies for your company within the worldwide dynamics of the Mexican automotive industry.

The many changes in Mexican legislation and in the international regulations affected by it must be efficiently dealt with in order to mitigate contingencies and risks and provide practical and innovative solutions making it possible to streamline resources and avoid cutting into a company's financial capacity. Therefore, before setting out on the road to recovery, we recommend talking to the PwC automotive industry specialists and taking advantage of their expertise in dealing with all the challenges posed by globalization.

PwC offers overall support in designing, deciding or adjusting the best strategy for your company, as well as maximizing or transforming your business competitiveness.

We will be pleased to advise you in this regard.

Pulverized market

Mexico is one of the most competed countries worldwide; if we analyze the size of the market which is right above one million units, and compare it to the more than 40 brands with presence in our country plus one of them having a 25% market share, we have as a result, a fierce competition in order to attract new clients and achieve a bigger market growth. Also, it is important to mention that before the end of the first semester of 2014, Korean brand, Hyundai, will be arriving to Mexico. The brand has a wide product portfolio that without hesitation, will look forward to take a market share, increasing internal competition even more on a market that hardly will reach a growth close to the expected 4.5% for 2014.

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