

Mexican President Signs Decree

to Lower Taxes and Increase Salaries on the Northern Border

1. The prospect of tax reduction on the US-Mexico border is looking promising. On 31 December 2018, the Mexican Official Gazette published a Decree whereby President Andres Manuel Lopez Obrador (a/k/a AMLO) granted a tax stimulus to legal and natural persons residing in one of the 43 designated municipalities bordering the United States (Decree).
2. These tax benefits, coupled with the National Minimum Wage Commission's determination to double the minimum daily wage in the same 43 designated municipalities, are part of AMLO's strategy to strengthen the economy on the northern border.
3. The Decree, which entered into force on 1 January 2019, consists of two main parts: (I) a preamble announcing the justification and purpose of the Decree, and (II) substantive provisions setting forth the tax benefits, the requirements for their application and implementation, and exclusions to same.

I. Objective and Purpose of the Decree

4. The preamble to the Decree explains the motivation behind the introduction of tax stimulus in the border zone. It notes that low levels of economic activity and investment in the border zone has directly contributed to high levels of violence and criminal activity, resulting in a Catch 22 situation for Mexico: lower levels of economic activity due to China's strong competition in the manufacturing sector, combined with close proximity to the US, resulting in increased living costs due to the prominence of the US dollar in local transactions.
5. The public policy behind these tax measures is to reactivate the economy of the border area by attracting both Mexican and foreign investment while increasing individuals' income to generate jobs and reduce violence and crime.

II. Tax Stimulus Introduced

6. The decree introduces two main tax measures: fiscal credits for income tax and a value added tax (VAT).

II.1 Income Tax Fiscal Credit

7. Article II of the Decree provides that taxpayers, whether legal or natural persons, who generate most of their income from activities performed or services rendered in the border

area, will be entitled to a fiscal credit equivalent to one-third of the relevant proportion of the income tax paid and generated in the previous fiscal year.

II.1.1 Requirements

8. In order to benefit from the income tax fiscal credit, the Decree sets forth certain requirements: First, taxpayers interested in the tax stimulus must register with a special registry (*Padrón de Beneficiarios del Estímulo para la Región Fronteriza*) no later than 31 March of the corresponding fiscal year, which will be subject to the tax authority's approval. Second, for the registration to be effective, the taxpayer must evidence that no less than 90 percent of the taxpayer's total income of the previous fiscal year was generated in the border area. Third, a taxpayer's fiscal domicile, including its main domicile, branch or office, must be registered in one of the municipalities set forth in Article I no less than 18 months prior to the registration for obtaining the tax stimulus.
9. Additionally, the Decree provides that the tax stimulus cannot be combined with other tax benefits. It therefore excludes the application of the tax stimulus whenever the taxpayer is already entitled to other tax benefits, unless the taxpayer renounces the latter.

II.1.2 Exceptions

10. Article VI of the Decree sets forth a long list of activities excluded from the application of the tax stimulus. For example, income generated by intangible assets and independent professional services is not covered by the tax benefit.

II.2 *VAT Fiscal Credit*

11. Article XI of the Decree provides that taxpayers, either legal or natural persons, who perform activities that essentially amount to a transfer of property, independently provide services, or temporarily lease assets within the border area, will be entitled to a tax credit equivalent to 50 percent of the VAT tax rate indicated in Article I of the Value Added Tax Law, i.e. 16 percent.

II.2.1 Requirements

12. The Decree also sets forth requirements that the taxpayers must fulfill to benefit from the tax stimulus. First, the delivery of goods or the provision of services must be made within the border area. Second, the taxpayer must submit a notice of its intention to apply for the tax stimulus within 30 days following the entry into force of the Decree. If the taxpayer commences activities thereafter, this notice must be submitted together with the documents for registration at the Federal Taxpayers Registry. Other requirements may be added in the future.

II.2.2 Exceptions

13. The exceptions for the application of the VAT tax stimulus are indicated in Article 13 of the Decree. Among others, the Decree provides that VAT arising from real property and intangible assets are excluded. Also, goods or services relating to digital content do not benefit from the tax benefit.

III. Analysis

14. This Decree was issued during a tense moment in US-Mexico relations and shortly after the renegotiation of NAFTA (the USMCA) [[see our joint bulletin of 4 October 2018 on that development](#)]. According to news reports published in 2018, AMLO's candidacy for the Mexican presidency stressed that southern Mexico should be prioritized for economic stimulus, on the basis that northern Mexico has traditionally received disproportionate government assistance due to its proximity to the US and its free trade manufacturing zones (maquiladoras). Notwithstanding AMLO's previous position during the campaign, this recent Decree seemingly reflects an emphasis on continued economic development along Mexico's northern border.
15. In light of the considerable uncertainty with respect to President Trump's border wall and the ongoing domestic political debate in the U.S. over immigration and trade, AMLO's recent Decree coupled with the border zone minimum wage hike should not be read in a vacuum, but ought to be considered within the present political context. One thing is for certain – the border region will continue to attract significant political and media attention in both Mexico and the US for the considerable future. If the Decree yields results for President Trump's a agenda, such as decreased immigration from Mexico and Central America and restructured trade balances, the Decree and its tax breaks could be a significant factor with respect to the presently fluid U.S.-Mexico relationship.

This article is not legal advice and is generic in nature. If you would like to discuss any aspect of this commentary, please contact:

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