U.S. - MEXICO FOUNDATION

RECOMMENDATIONS

ENHANCING MEXICO'S COMPETITIVENESS THROUGH FISCAL POLICY RECOMMENDATIONS

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PREPARED BY
ÚRSULA CARREÑO COLORADO
ANETTE RAMÍREZ VALENZUELA

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CONCLUSIONS AND RECOMMENDATIONS FOR MEXICO'S FISCAL POLICY

The document delves into three topics related to fiscal policy: nearshoring, tax regulation in Mexico, and comparative analysis in selected countries and regions. The first chapter, "Nearshoring: Firm's Decision-Making and Country Development," introduced a theoretical framework to provide a comprehensive understanding of nearshoring from both the private (firm) perspective – exploring when firms relocate processes closer to their headquarters – and the public or developmental approach. This approach delves into how nearshoring, as a private practice influencing FDI, can yield advantages for the host country. The discussion encompasses considerations for achieving desired outcomes such as heightened employment, accelerated technological transition, and improved productivity.

In examining the factors that facilitate or shape FDI attraction, an extensive body of literature highlights the diverse array of measures, policies, and country attributes that influence the fluctuations of FDI within host nations. This scrutiny reveals that taxes, encompassing their structure and rates, play a pivotal role in delineating the overall business environment of the host country. Nonetheless, beyond the realm of taxation, the importance of additional factors emerges, driven by their influence on bolstering the security of foreign investments and refining the precision of cost and profit projections.

Chapter 2 on tax regulation provided a broad perspective on the tax framework in Mexico, indicating that the country has aligned itself with international policies set forth by the OECD.

Furthermore, it described a detailed list of incentives that can help attract FDI, which we can summarize in the following:

- **Loss Carry Forward:** Mexico's Tax Law contemplates the possibility of reducing "tax losses." The mechanism to reduce them involves calculating the taxable income for the year, subtracting authorized deductions and employee profit-sharing, and then deducting the accumulated tax losses pending reduction. The result is the taxable profit. These tax losses can be carried forward and offset for up to the next ten years from the year they were generated, and this right is personal to each taxpayer.
- **Investment Deductions:** Investment deduction exists in Mexico with certain limits, and the rates vary depending on each asset or deferred expense and the activity it is used for. It can range from 3% to 100% of the investment. There are more than 40 maximum rates for these cases. It includes all types of

assets used for the company's operation and deferred charges such as software or intangible assets.

- **Investment Tax Credit:** In Mexico, there are tax incentives that, in specific sectors, allow for a reduction of up to 100% of the CIT to be paid. Additionally, these incentives also enable accelerated deductions of investments in assets. The main incentives include:
    - Tax incentives for the northern and southern border
    - Stimulus region welfare
- **Reduced Taxes on Dividends and Foreign-Source Interest:** In Mexico, there is no distinction in tax treatment between nationals and foreigners; however, there is the possibility of applying reduced rates through the observance of treaties to prevent double taxation.
- **Deductions for Qualified Expenses:** In Mexico, various deductions are available, each with specific limits in some cases. These deductions encompass returns received, discounts or bonuses granted, cost of goods sold, expenses, investments, uncollectible credits, losses due to unforeseen circumstances, social security contributions, accrued interest, and the deductible annual inflation adjustment.
- **Zero or Reduced Tariffs:** Mexico presently boasts a network of 14 Free Trade Agreements (FTAs) with 50 countries, 30 Bilateral Investment Treaties (BITs) with 31 countries or regional administrations, and nine limited-scope agreements (Economic Complementation Agreements and Partial Scope Agreements) within the framework of the Latin American Integration Association (ALADI). These trade agreements significantly reduce or exempt trade tariffs and facilitate international trade.
- **Value Added Tax (VAT) Credits:** Currently, in Mexico, there is a certification for VAT and Special Tax on Production and Services (IEPS), the main benefit of which is the ability to apply a tax credit equivalent to 100% of the VAT/IEPS that must be paid for the temporary importation of goods or inputs intended for the production, transformation, or repair of goods for export. This benefit applies to various schemes, including the maquiladora programs (IMMEX), fiscal deposit for the assembly and manufacturing of vehicles, production, transformation, or repair within a supervised facility, and strategic supervised facility.

In summary, chapter 2 has outlined the key considerations for foreign companies looking to establish themselves or enter into partnerships in Mexico. These include:

- **Compliance with Mexican Regulations:** It is crucial to thoroughly review Mexican regulations governing the incorporation of a company and ensure compliance with requirements related to foreign investment.
- **Financial Planning:** Foreign companies should develop well-defined financial projections for their ventures' initiation and ongoing operations in Mexico.
- **Taxation Rates:** Carefully examine the tax rates that apply to the services or merchandise offered in the Mexican market.
- **Tax Obligation:** Clearly define the tax obligations the company will be subject to while operating in Mexico.
- **Market-Value Transactions:** Ensure transactions with related companies adhere to market values.

The third chapter delivered a comprehensive overview of using tax incentives to attract FDI from wealthier economies to those with moderate or lower incomes, mainly through nearshoring practices. The case studies presented through a comparative analysis in selected countries and regions have highlighted the importance of various factors in shaping FDI attraction strategies.

The first case study emphasized the unique dynamics between the United States and Mexico, underlining the significance of their proximity, income disparity, and the role of individual Mexican and U.S. States in FDI competition. This case showcases the multifaceted nature of FDI attraction within a North American context.

The second case study explored the economic interactions between Baltic and Balkan countries and their Nordic counterparts in Eastern Europe. It drew attention to their geographical proximity to Western Europe, similar income characteristics to Mexico, and their successful embrace of IT and innovation-driven economic activities. These countries' experiences serve as valuable references for Mexico in diversifying FDI strategies.

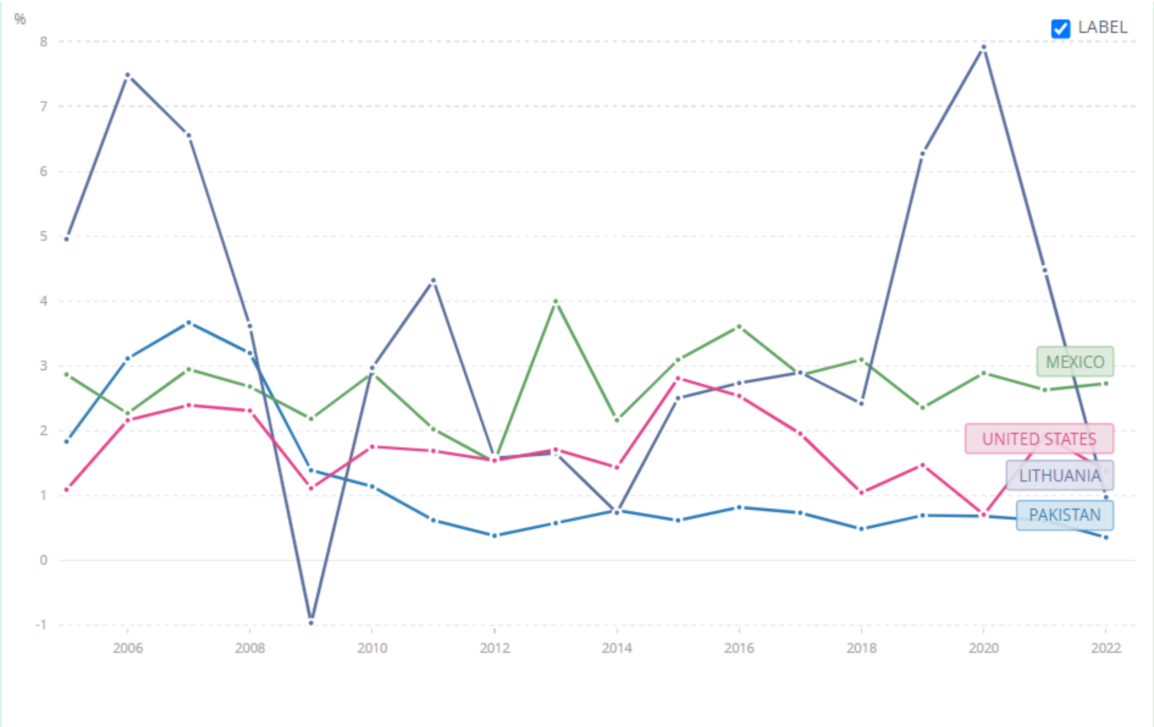
Finally, the third case study delved into Pakistan's FDI patterns and appeal, offering insights into nearshoring practices compared to Mexico. Pakistan's connections with the U.S., middle-income status, proximity to China, and favorable tax framework contribute to its relevance. This case highlights the importance of aligning industrial policies with high-income investment trends and prioritizing trade-oriented infrastructure complementary to tax incentives in attracting FDI.

In light of the above, we can conclude the following about Chapter 3:

Mexico's consistent and modestly increasing FDI as a percentage of GDP makes it a stable nearshoring destination.

The U.S. holds the highest attraction for foreign investment in millions of dollars. However, when examining FDI net inflows as a percentage of GDP, the U.S. demonstrates significant responsiveness to fluctuations in FDI, peaking in 2020 and dropping below Mexico's levels in 2022. Conversely, Mexico has maintained a relatively steady FDI share of GDP. However, it has yet to reach its peak in 2013 and is likely to exceed expectations by the end of 2023 after the investment announcement from several companies (i.e., Tesla). Notably, in 2022, Mexico's FDI share surpasses that of the U.S., Lithuania, and Pakistan, as demonstrated in Graph 16. This stability in retaining and even enhancing FDI during specific periods positions Mexico as a notable and growing nearshoring destination.

Graph 16. FDI, net inflows (% of GDP)

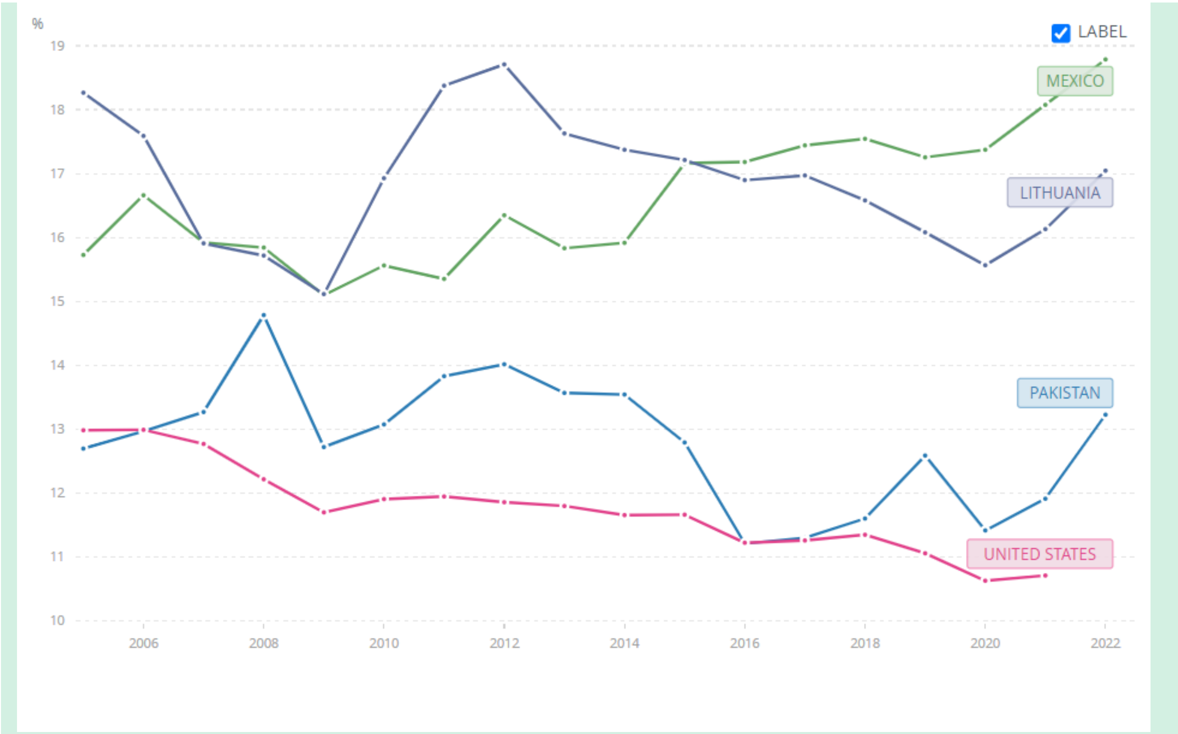


Source: World Bank Data. International Monetary Fund, International Financial Statistics and Balance of Payments databases, World Bank, International Debt Statistics, and World Bank and OECD GDP estimates.

Mexico's strong manufacturing position results from past liberalization tax and industrial policies demonstrating its economic prowess on the global stage.

The comparison of manufacturing value added as a percentage of GDP across countries reveals Mexico's economic strength as it maintains a significant nearly 6% advantage over the United States. Surprisingly, this places the U.S. below countries like Pakistan and Lithuania in this specific economic indicator. Notably, Lithuania's strategic efforts in liberalizing tax and industrial policies have enhanced its competitiveness in the manufacturing sector, as discussed in Chapter 3. Furthermore, the observed trend depicted in Graph 17 indicates a discernible level of specialization between Mexico and Lithuania, particularly evident in their respective automotive industries. Mexico appears to benefit from a strong presence of American and Japanese influences, while Lithuania likely draws from Swedish influence. This specialization is pivotal in both countries' prominence in this economic indicator.

Graph 17. Manufacturing, value added (% of GDP)

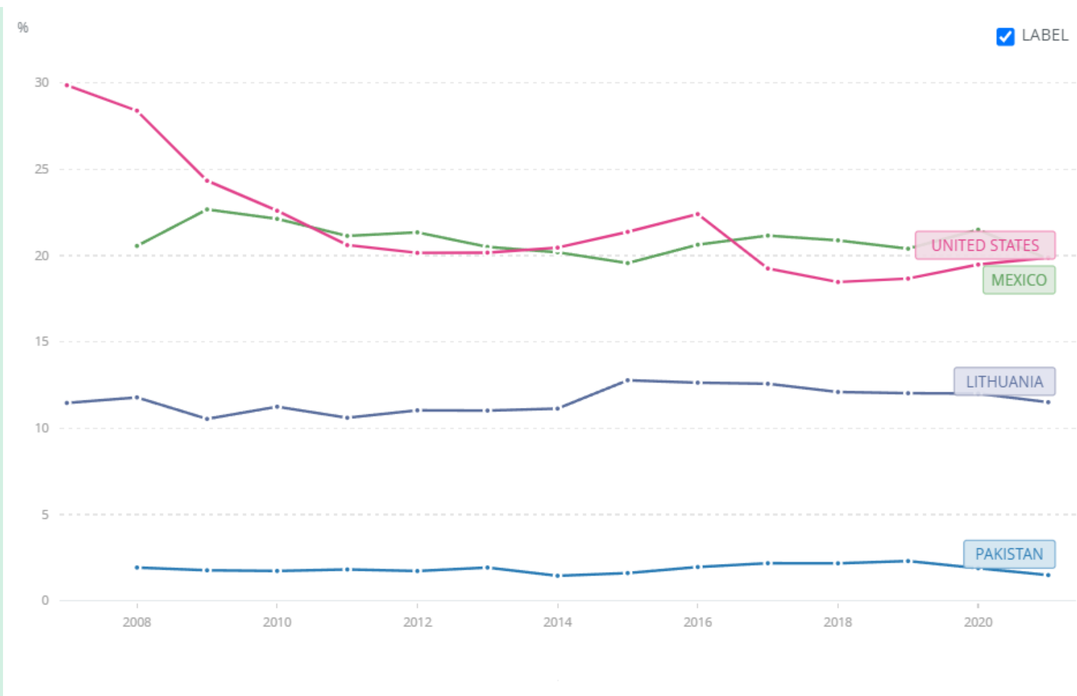


Source: World Bank Data. World Bank national accounts data, and OECD National Accounts data files.

The nearshoring potential is evident as the U.S. poses competition to Mexico in high-technology exports, as shown by a countercyclical trend between the two nations.

In the context of high-technology exports, the U.S. emerges as a strong competitor to Mexico. The data reveals an intriguing dynamic where the U.S. has experienced a fluctuating trajectory in high-technology exports, with a recent upward trend since 2018. In contrast, Mexico has displayed relative stability in high-technology export trends. Mainly noteworthy is the counter-cyclical pattern observed where an increase in the indicator for the U.S. corresponds with a decrease for Mexico and vice versa, warranting further investigation into the intricacies of their economic relationship.

Graph 18. High-technology exports (% of manufactured exports)

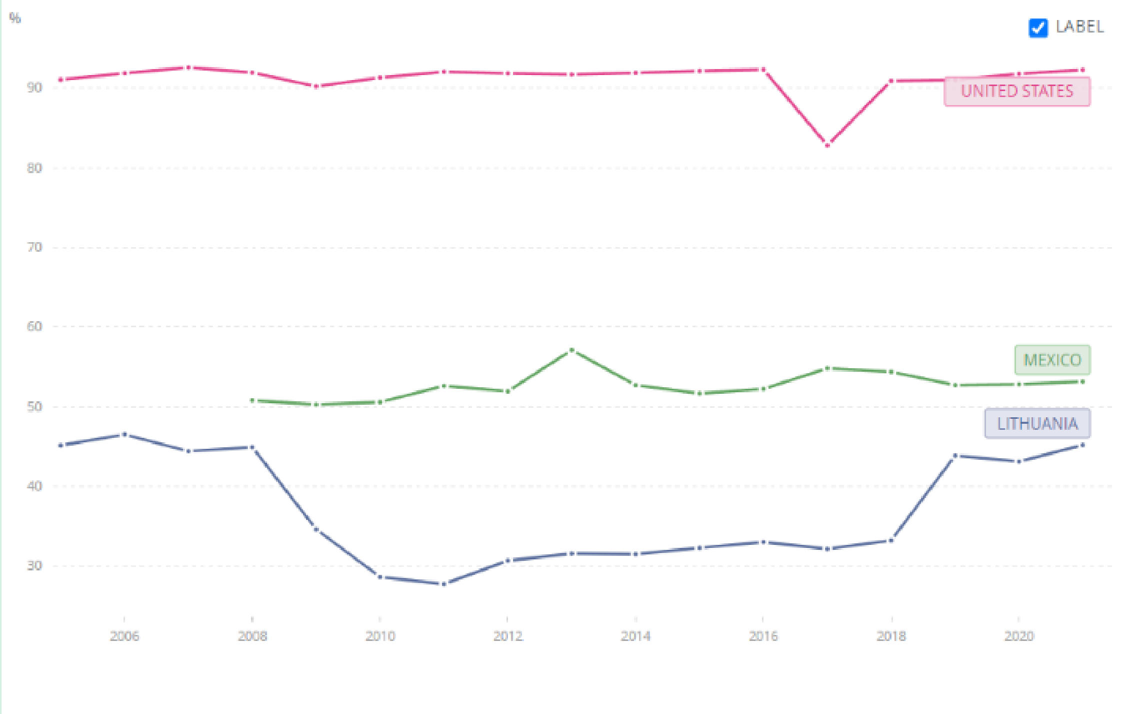


Source: World Bank Data. United Nations, *Comtrade* database through the WITS platform.

The variation in tax reliance suggests Mexico's potential to strengthen its attractiveness for nearshoring.

In summary, when considering income, profits, and capital gains taxes, the U.S. stands out as the country with the highest reliance on this tax category, followed by Mexico and Lithuania. Although Lithuania exhibited a period of decreased dependency on these taxes from 2009 to 2017, there was an upturn in 2018, possibly indicating increased corporate value and activity or a rise in CIT and capital tax rates. In contrast, Mexico positions itself moderately in terms of income, profit, and capital gains taxes, offering an opportunity for the country to enhance its appeal for nearshoring initiatives.

Graph 19. Taxes on income, profits, and capital gains (% of total taxes)



Source: International Monetary Fund, Government Finance Statistics Yearbook and data files.

Based on the comprehensive analysis presented in the preceding chapters, it is evident that Mexico holds a unique position in the landscape of FDI and nearshoring activities. Its stable and modestly increasing FDI as a percentage of GDP establishes it as a reliable nearshoring destination. Additionally, Mexico's consistent performance in retaining and even enhancing FDI during specific periods positions it as a notable and growing nearshoring hub. This stability, combined with its strong manufacturing sector, demonstrates Mexico's economic competence on the global stage.

To further bolster Mexico's attractiveness for nearshoring initiatives, it is recommended that the country also focus on enhancing its tax framework. While Mexico positions itself moderately in income, profit, and capital gains taxes, there is room for improvement to increase its competitiveness in attracting FDI. Streamlining tax processes, offering targeted incentives, and aligning tax policies with high-income investment trends can help Mexico solidify its position as a top nearshoring destination.

Moreover, considering the U.S. as a competitor and principal investor, Mexico should explore strategies to leverage its proximity to the U.S. market and foster synergies in technology-driven industries. Collaborative efforts and partnerships in research and development, innovation, and technology transfer can further enhance Mexico's appeal to companies seeking to nearshore their operations, especially when looking for a more high-skilled workforce.

Given the above, it is imperative to formulate specific recommendations considering the need for targeted improvements in Mexico's tax framework. By implementing these recommendations, Mexico could solidify its status as a top choice for companies seeking to relocate their operations and capitalize on its economic strengths, ultimately fostering sustainable economic growth and prosperity.

Recommendation 1. Review Interest Deduction Limit.

As a result of the efforts led by the OECD, Mexico has played a significant role in implementing the measures outlined in the BEPS Plan (Base Erosion and Profit Shifting). A concrete example of this commitment can be found in the 2020 Fiscal Reform. During that period, provisions related to the digital economy and the limitation of base erosion through interest operations were introduced. These provisions reflect Mexico's dedication to adhering to the directives and objectives outlined in the BEPS Plan.

One of the key provisions added to the Income Tax Law was the limitation on the deduction of interest payments made by taxpayers. This measure stemmed from the BEPS Plan, which identified that one of the most straightforward international tax planning techniques to shift profits involves making interest payments between related and independent parties. Furthermore, the BEPS Report indicated, based on academic studies, that multinational groups tend to accumulate higher levels of debt than their subsidiaries located in countries with higher tax rates. This practice has repercussions on developed and developing nations, with the latter facing even more significant risks.

For this reason, countries were advised to introduce a rule limiting the deduction of interest based on taxable profits before interest, depreciation, and amortization. As outlined in the Final Report, the recommended range for determining this ratio was between 10% and 30%. Mexico opted to set the maximum limit at 30% in its legislation. Simultaneously, regulatory harmonization was undertaken per the principles delineated in the BEPS Report. It was stated that these provisions should apply minimally to legal entities within multinational groups. Still, they could also be extended to domestic entities or those not affiliated with corporate groups.

As a result, this provision applies to all legal entities, establishing a minimum rule that applies uniformly to all taxpayers. Furthermore, it covers payments made to third parties, related parties, and members within the same corporate group, in line with the report's recommendations above. An alternative is provided, allowing countries to apply these rules to debts incurred before the tax year in which the provision takes effect, eliminating the need for transitional rules to address such situations. Consequently, this provision became effective for deductible interest starting from the 2020 tax year, irrespective of the origin of debts acquired in previous years. This decision was made considering the Mexican legal framework, ensuring that those with debts contracted before the implementation of this provision have a right of expectation, meaning that a law not in force at the time cannot be retroactively applied to them.

Additionally, the provision excludes debts acquired for financing public infrastructure projects, recognizing the typically high level of indebtedness associated with such initiatives. A non-exhaustive list of activities exempted under this exception is included. It is also specified that the provision does not apply to debts incurred for property development within the national territory to promote this sector.

On the other hand, the limitation on interest deductibility, as established in the adoption of the BEPS Plan, restricts the deductibility of interest to Tax EBITDA, which means that not all interest payments can be deducted in the current fiscal year. In the first year, this limitation can impact the annual adjustment calculation for inflation, as it does not consider the capital from which interest is derived as debt. This could result in an increase in the yearly deductible inflation adjustment (authorized deduction) or a decrease in the annual cumulative inflation adjustment (cumulative income). To mitigate the impact of inflation, in Mexico, companies can carry forward interest expenses that are not deductible for up to the following ten fiscal years.

Inflationary effects can influence the deductibility of interest because the actual value of the debt can change over time due to inflation. Since the deductibility limitation and the 'carry forward' are applied in nominal terms, high inflation rates can make the impact of non-deductible interest on the annual adjustment for inflation more significant in real terms.

In specific projects or businesses, the authorities acknowledge the necessity of exempting debts acquired for their operation or development from this limitation. **Establishing a business in Mexico often relies heavily on the initial investment, which is frequently facilitated through debt issuance, whether domestic or foreign.**

Consequently, it is crucial to reconsider the following aspects of this reform to promote schemes beneficial for FDI:

1. Introduce a **grace period for newly established companies** during their preoperative phase or while engaging in auxiliary activities related to their core operations, extending up to two tax years. During this period, the interest deduction limit would not apply if their interest expenses arise from debts acquired to finance projects within the national territory.
2. Establish **comprehensive rules** for applying the interest deduction limit when consolidated deductions are made (interests paid by a group). Despite the procedure being covered in the Law, it directly refers to regulations issued by the tax authority, which have yet to be published, resulting in uncertainty. One potential benefit of this approach could be applying a higher exemption limit for deductible interest expenses, mainly when debts are acquired directly by a consolidated group, potentially resulting in more significant interest expenses.
3. **Modify the rights granted by fiscal incentives** such as the North and South Border Area Decree and the Welfare Decree. The goal is to incentivize newly established companies in these designated areas to stimulate economic growth in the Welfare Area and enhance competitiveness in the Border Areas. The fiscal incentive would consist of a more substantial exception than what is currently provided by law (20 million pesos) for deducting interest expenses, potentially increasing it to 30 million pesos, provided these expenses result from debts intended to finance investment projects.
4. **Eliminate the inflationary effects** in determining deductible interests; companies may face a more significant financial burden in real terms as inflation increases the actual cost of non-deductible interest. This can affect the company's profitability, investment capacity, and financial decision-making. The company may need to allocate more resources to cover these non-deductible interests, which could limit its growth or investment capacity. Eliminating the inflationary effects on interest deductibility would promote business competitiveness in Mexico. Companies could make more efficient investments without worrying about the disproportionate tax impact of inflation on interest deduction.

Recommendation 2. Repeal Deduction Limits on Worker Payments.

Up to the tax year 2013, the Income Tax Law allowed people who have workers depending on them (employer) to make the deduction of the total amount of the different gainful concepts delivered to their employees, regardless of whether such elements were subject to taxation according to the Law, for the benefit of such workers. As a result, the tax authority considered that this taxation treatment resulted relatively asymmetric, as there were incomes that for the worker were completely exempt from income tax and, in turn, deductible for the employer, so it created damage for the federal tax authorities, as it did not collect it in a "symmetrical manner"[1] allowing taxpayers to deduct the total amount of payments that in turn were exempt income.

Consequently, according to the tax legislation, currently, the payments made by employers, which are also exempt income for the workers, will be non-deductible up to an amount that will result from applying a factor of 53 or 47%, as described in chapter 2 of the section of authorized deductions in Mexico.

In this context, it is paramount to consider a generalized fiscal reform focused on removing/ repealing the deduction limit of these payments for all taxpayers. This argument is supported by the fact that the current valid restriction can be considered detrimental and even contravenes fundamental principles outlined in the Constitution. These principles include fiscal proportionality, which rules that taxes must be proportional to the economic capacity of individuals, and tax equity, which is based on the premise that taxes are similar to those in equivalent situations and differently to those with different circumstances.

This can be exemplified as follows: The regulations, as they are currently, do not allow the complete deduction of payments made for social security contributions, even though this expenditure is essential for achieving the company's purpose of people. In other words, the dues paid regarding social security, as a benefit for workers, are included in the salary of the workforce. Consequently, this payment involves a strictly indispensable cost for attaining purposes and activities.

In this sense, this expenditure must be acknowledged and considered entirely deductible. This is because this expense is indispensable for developing the employers' activities.

For all that, the repealing of this deduction limit is suggested. This is made to safeguard the constitutional principles rooted in the legislation and promote investments by removing obstacles that prevent the complete deduction of payments corresponding to payrolls and benefits of workers.

It's important to mention that this initiative has been extensively discussed and presented to authorities by various technical groups, such as the Mexican Institute of Public Accountants.

[1] Tax symmetry is a taxation policy principle, non-legal but more dogmatic, that creates a link between taxpayers and the balance between income and expenses, so if a person must acknowledge an income that will be taxed, the counterparty making the payment must have a deduction.

Recommendation 3. Shorten the time frame for Returning Credit Balances of Contributions.

As stated in Chapter 2 of this study, in Mexico, according to legislation (Fiscal Code of the Federation, Tax Income Law, and VAT Law), the generation of credit balances in favor of taxpayers is allowed.

Usually, these credit balances are granted naturally by the calculation and determination of taxes. In the case of VAT, the credit balances are generated when the VAT transferred to the taxpayer is greater than the VAT transferred by him when the creditable VAT (the one generated by expenses) is greater than the VAT charged (generated by income).

By contrast, the Income Tax in favor is given naturally by an excess of provisional payments made compared to the yearly determination. This is, the provisional amount of income tax of one payment at the expense of the annual account can exceed the number determined for yearly income tax, thus generating a credit balance.

In this sense, it should be noted that fiscal authorities are obliged to return the credit balances within the following forty business days from the day after the contributions return request has been submitted before the fiscal authorities, which sometimes exceeds the term.

This can be unfavorable for the investment of companies in Mexico, as those who, due to the nature of their activity, generate credit balances both for VAT and income tax may find diminished their initial investment by having to wait for a considerable period for the return of excess contributions paid or credit balances generated from their activities.

In this context, it is proposed to reduce to a term of twenty days for the return of credit balances in favor of taxpayers or improper payments for those newly created companies in Mexico, as well as for those people who are in a preoperative period or carrying out auxiliary activities to its main operation, up to three tax years, or, as the case may be until the preoperative period has ended; as long as those credit balances obtained by the contributions are intended for reinvesting in the operation of entities.

Recommendation 4. Explicitly include the Research and Development (R&D) deduction within the authorized deductions.

Deductions on R&D play a crucial role in fiscal frameworks by encouraging innovation, boosting competitiveness, creating jobs, and contributing to long-term economic growth. They are vital for governments to support research and development activities that drive technological progress and enhance a nation's economic well-being.

As depicted in Chapter 3, the countries that have attracted foreign investment exhibit a concentration of highly skilled labor, particularly in the technological sector, substantial investments in R&D and infrastructure, as well as robust safeguards for IPR, which are critical factors for countries aspiring to host advanced manufacturing and domestic technological progress.

In particular, the deductions presented in Table 15 have been implemented in those countries.

Table 15. R&D tax incentives in selected countries

Country	Tax Incentives
United States	• Deductions on Research and experimental (R&E) expenditure: These expenses must be capitalized and amortized over five years from the midpoint of the tax year they were incurred, while R&E expenses related to foreign research are amortized over 15 years.[2]
Lithuania	• Deductions on R&D investments and profits**:** Since 2018, there has been an additional incentive for companies investing in R&D – a reduced 5% rate of the CIT for commercialization of inventions created in R&D activities, including investing in technological renewal.[3]
Balkan Countries[4]	• R&D allowances: Justifiable costs of R&D allow for additional deductions from the tax base by 100%, 125%, or 150% of the cost amount, depending on the character of the research (Croatia)

Mexico could use R&D tax deductions to support strategic sectors such as technology, healthcare, energy, and advanced manufacturing. This can drive specialization and growth in these industries.

[2] PwC Worldwide Tax Summaries.
[3] Ministry of Finance of the Republic of Lithuania. “Tax Incentives for Investment and Innovations”.
[4] Tax Incentives in Western Balkan Countries Article · January 2010

Implementing an R&D tax deduction in Mexico can promote innovation, attract investments, create high-quality jobs, and contribute to the country's long-term economic growth.

Therefore, it is recommended to implement a tax deduction for R&D activities that consider the following:

1. A percentage substantial and attractive to companies. This could range from 100% to 150% of qualified R&D expenses. A higher rate, such as 150%, can further incentivize investment in R&D.
2. Clear eligibility criteria and adequate oversight should also be in place to ensure that only genuine R&D activities qualify for the deduction. While a high deduction percentage is recommended, it's essential to establish reasonable limits to prevent abuse and ensure fiscal sustainability.
3. A periodic review of the deduction percentage and the results regarding R&D investment and economic growth should be conducted. This allows adjustments to the deduction as needed to meet fiscal and financial objectives.

In addition to the fiscal framework modifications described above, it is suggested that a comprehensive analysis of U.S. States, focusing mainly on those with significant FDI, such as California, Texas, and New York, be performed to assess their respective tax incentive programs.

Table 16. Tax Incentives, California, New York, and Texas.

California	New York	Texas
• California Competes Tax Credit • California Research and Development Tax Credit • Sales and Use Tax Exemption • California Alternative Energy and Advanced Transportation Financing Authority (CAEATFA) Programs	• Excelsior Jobs Program • Start-Up NY • Regional Economic Development Councils (REDCs) • New York State Research and Development Tax Credit • Green Energy Incentives • Qualified Emerging Technology Company (QETC) Credits	• Texas Enterprise Fund • Texas Emerging Technology Fund • Texas Enterprise Zone Program • Texas Economic Development Act • Texas Sales Tax Exemptions • Texas R&D Tax Credit

Source: California doing business, California State Treasurer, Official Website of New York State, Texas Economic Development.

Potential Benefits and Possible Impact of the Recommendations

The following impacts represent the potential outcomes of the recommendations in this document. These recommendations, addressing various aspects of fiscal policy and economic development in Mexico, can change the country's economic landscape. While some may lead to lower tax revenue in the short term, they are designed to generate substantial long-term benefits, including increased formal sector employment, the growth of domestic industries, and the transfer of environmental capabilities. In this overview, we explore how these potential impacts could contribute to Mexico's fiscal sustainability, economic prosperity, and the overall well-being of its populace.

Lower Tax Revenue in the Short Term, Higher Revenue in the Future: The proposed recommendations, such as a review of interest deduction limits, repeal of deduction limits on worker payments, and the introduction of an R&D tax deduction, might initially result in a reduction of tax revenue for the Mexican government. However, this short-term sacrifice can lead to long-term gains. For instance, the R&D tax deduction can incentivize local and foreign businesses to invest in research and development activities within Mexico. This, in turn, can spur innovation, attract multinational corporations, and ultimately boost economic growth. As these investments bear fruit, they can contribute to higher tax revenues in the future, expanding the tax base and potentially surpassing the short-term revenue decline.

Increased Formal Sector Employment: Removing deduction limits on worker payments can positively impact formal sector employment. By allowing businesses to deduct a broader range of payments related to their workers, companies are incentivized to provide more comprehensive employment packages, including benefits like health insurance, retirement plans, and bonuses. This, in turn, attracts talent to the formal job market, reducing informal labor and enhancing job security for workers and, thus, greater long-term revenue collection.

Fostering Local Industries: The recommendations encourage the growth of domestic industries by supporting research and development activities and making it more attractive for businesses to invest in Mexico. With an R&D tax deduction and less restrictive deduction limits, industries can develop new technologies, improve processes, and enhance product quality. This can boost the competitiveness of local industries, potentially leading to increased exports and reduced import reliance.

Transfer of Environmental Capabilities: The potential for a "pass of capabilities" in the environmental sector is a significant environmental and economic benefit. Mexico can accelerate its transition toward a more sustainable and eco-friendly economy by encouraging businesses to invest in environmental technologies and practices. This can lead to advancements in clean energy, waste reduction, and sustainable agriculture, contributing to environmental protection and long-term economic stability.

Increased Investment and Enhance Competitiveness: By introducing a grace period for newly established companies, comprehensive rules for applying interest deduction limits, and allowing newly created companies and those in preoperative periods to access credit balances promptly, the Mexican government can encourage more businesses to invest in the country. Also, as outlined in the recommendation proposal, eliminating the inflationary effects in interest determination could enhance the competitiveness of companies in Mexico, thereby attracting capital to the country through debt.

These benefits collectively contribute to Mexico's fiscal sustainability and economic prosperity. While there may be short-term challenges, the recommendations are designed to position Mexico for a more robust and sustainable financial future, aligning with international best practices and enhancing its competitiveness on the global stage.

Conclusively, conducting a dedicated study is imperative to accurately assess the long-term impact of Mexico's four fiscal policy recommendations. This study should rigorously follow the outlined steps, including gathering historical tax and employment data, defining key assumptions, calculating revenue changes unrestricted by limitations, contrasting them with current revenue, projecting long-term effects, and conducting sensitivity analyses for diverse scenarios. These meticulous steps are essential to comprehensively evaluate the recommendations' pivotal effects on tax revenue, job creation, and competitiveness.

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