
CHAMBERS GLOBAL PRACTICE GUIDES

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**Mexico: Law and Practice
& Trends and Developments**

Ángel Escalante, Gabriel Rojas,
Daniel Colunga and Brenda Favela
Escalante & Asociados



MEXICO



Law and Practice

Contributed by:

Ángel Escalante, Gabriel Rojas, Daniel Colunga and Brenda Favela
Escalante & Asociados

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Escalante & Asociados (E&A Legal) is a boutique tax law firm with a team of highly specialised practitioners, focused on tax controversy and non-contentious tax matters. Established in 2015 by its managing partner, Ángel Escalante Carpio, the firm operates from offices in Mexico City and Houston, Texas, providing strategic advice on complex domestic and cross-border tax matters, particularly in the Mexico-US corridor. The firm is recognised for its expertise in tax audits, administrative proceedings, and high-stakes tax litigation, as well as in international tax planning, restructuring, compliance, and AML matters, offer-

ing an integrated approach that combines technical sophistication with a strong business-oriented perspective. Its practice also covers foreign trade, real estate tax structuring, estate planning for HNWI individuals, and double taxation issues. E&A Legal regularly represents clients in disputes before Mexican tax authorities and advises multinational and domestic companies on the design and implementation of robust tax structures to mitigate risks and support their long-term business objectives, including cross-border operations and intercompany transactions.

Authors



Ángel Escalante is the founding partner of E&A Legal, with more than 20 years of experience in tax controversy, including administrative proceedings, tax audits and litigation before Mexican authorities. His

practice focuses on complex tax disputes, international taxation and matters involving foreign trade and anti-money laundering compliance. He holds law and accounting degrees, as well as a master's degree in tax law, and has completed advanced studies in international taxation. He is a member of the World Compliance Association, under which he co-ordinates the Tax Committee in Mexico, and the International Fiscal Association.



Gabriel Rojas is a partner at E&A Legal with more than ten years of experience in corporate tax and controversy, focusing on administrative proceedings, audits and disputes before Mexican

authorities. His practice focuses on domestic and international tax matters, including cross-border structuring, foreign trade and tax incentive programmes such as IMMEX and PROSEC, as well as VAT and excise tax certifications. He regularly represents clients before the Mexican Tax Administration Service (SAT) and other regulatory bodies. Gabriel has completed a law degree and postgraduate studies in international tax law, including an Advanced LLM from the University of Amsterdam, and is a member of the International Fiscal Association.



Daniel Colunga is an associate at E&A Legal, focusing on tax controversy, including administrative and constitutional tax litigation. He advises and represents clients in audits, investigations and disputes

before Mexican authorities, including the Mexican Tax Administration Service (SAT), PRODECON and other regulatory bodies, as well as before administrative and constitutional courts. His practice centres on complex tax disputes and enforcement-related matters. Prior to joining E&A Legal, he worked at specialised tax law firms, where he gained experience in taxpayer defence. Daniel holds a law degree from Escuela Libre de Derecho and is a member of the International Fiscal Association.



Brenda Favela is an associate at E&A Legal, focusing on tax controversy, including administrative and constitutional tax litigation. She advises and represents domestic and international clients in audits,

assessments and disputes before Mexican authorities and courts, participating in the preparation of administrative appeals, annulment claims and constitutional (amparo) actions. Her practice focuses on complex tax disputes and enforcement-related matters. She also has experience in foreign trade and anti-money laundering compliance, supporting a multidisciplinary approach to regulatory issues. Brenda holds a law degree from Universidad Anahuac México.

Escalante & Asociados

Torre Altiva/Blvd Manuel Avila Camacho 138 Piso 8
Lomas de Chapultepec
Miguel Hidalgo
11000, Mexico City
Mexico

Tel: (+52) 55 8854 9587
Email: dmariscal@eyalegal.com
Web: www.eyalegal.com



1. Sources and Principles

1.1 Domestic Sources of International Tax Law

The Mexican tax legal system is primarily grounded in the Political Constitution of the United Mexican States (the “Federal Constitution”), particularly in Article 31, section IV, which establishes the obligation of individuals to contribute to public expenditure in a proportional and equitable manner. These constitutional principles operate as substantive limits on the taxing power of the state and apply equally in the context of international taxation.

In addition, Article 133 of the Federal Constitution establishes the hierarchy of legal norms within the Mexican legal system, providing that international treaties concluded by the executive and approved by the senate form part of the supreme law of the union.

The principal legislative source governing international taxation is the Mexican Income Tax Law (MITL), which regulates, among other things:

- the taxation of non-residents on Mexican-source income;
- the concept and taxation of permanent establishments (PEs);
- transfer pricing rules applicable to related party transactions; and
- preferential tax regimes.

The Federal Fiscal Code (FFC) complements this framework by establishing general procedural provisions, including the audit powers of the tax authorities and interpretative rules applicable to tax legislation.

Administrative interpretation is primarily issued by the Mexican Tax Administration Service (*Servicio de Administración Tributaria* or SAT), particularly through: (i) the annual Miscellaneous Tax Resolution and its annexes; and (ii) non-binding interpretative criteria.

Judicial precedents issued by the federal judiciary as well as decisions of the Federal Administrative Justice Court constitute another important source of international tax rules in Mexico.

Finally, Mexico maintains an extensive network of double taxation treaties (currently exceeding 60 agreements). These treaties aim not only to eliminate double taxation but also to prevent tax evasion and allocate taxing rights between contracting states.

1.2 Hierarchy of Sources

From a theoretical perspective, Mexico is generally regarded as following a monist approach, since international treaties become part of domestic legal order upon their approval by the senate and do not require further legislative transformation. This is expressly recognised in Article 133 of the Federal Constitution, which establishes that treaties concluded by the executive and approved by the senate form part of the supreme law of the union.

However, the hierarchy position of treaties within the national legal system has been clarified through Supreme Court of Justice jurisprudence which has established that: (i) international treaties on human rights have a constitutional hierarchy; and (ii) other international treaties, including tax treaties, are hierarchically below the Federal Constitution but above federal legislation.

This constitutional framework must be read together with the principle of tax legality, derived from Article 31, section IV of the Federal Constitution, which requires that taxes be established by law. Under this principle, only a formal legislative act may determine the essential elements of taxation, including the taxable event, the tax base and the applicable rate.

As a result, tax treaties cannot create taxes or establish new taxable events, since this would exceed the limits imposed by the principle of legality. Instead, they operate as instruments that allocate and limit taxing rights between jurisdictions, thereby preventing double taxation and reducing instances of double non-taxation.

Accordingly, in the national legal system, the interaction between domestic law and tax treaties follows a structured approach:

- domestic tax law determines the existence of a taxable event and the applicable tax liability;
- tax treaties subsequently operate to restrict or allocate taxing rights between contracting states; and
- where applicable, treaties may provide relief mechanisms, such as reduced withholding tax rates or exemption methods.

This reflects the dual function of tax treaties in the Mexican system: they form part of domestic law but operate primarily as co-ordination instruments rather than independent sources of taxation.

1.3 OECD Model/United Nations Influence on Treaty Practice

Mexico generally follows the OECD Model Tax Convention, although its treaty practice also incorporates elements of the United Nations Model Double Taxation Convention, particularly in areas where source-based taxation is emphasised.

This is reflected, for example, in provisions relating to to: (i) PE definition; (ii) taxation of services; and (iii) certain categories of income where broader source taxing rights are preserved.

Mexican courts have also recognised that the OECD Model Commentary constitutes soft law. While it is not

legally binding, it is frequently used as an interpretative tool when applying tax treaties, particularly where treaty language aligns with the OECD Model.

1.4 Multilateral Instrument

Mexico is a signatory to the Multilateral Instrument (MLI), adopted as part of the OECD/G20 BEPS Project, which was designed to simultaneously modify multiple bilateral tax treaties, incorporating provisions intended to combat base erosion and profit shifting (BEPS).

The MLI was approved by the Mexican Senate on 12 October 2022 and published in the Official Gazette on 22 November 2022. Mexico deposited its instrument of ratification before the OECD on 15 March 2023 and the MLI came into force in Mexico on 1 July 2023.

However, its provisions only became effective as of 1 January 2024.

2. Territoriality, Residence and Permanent Establishment

2.1 General Principle of Territorial Taxation

The Mexican tax system is based on a combination of residence and source principles, which determine the territorial scope of the state's taxing power.

Mexican tax residents are subject to taxation on a worldwide income basis, meaning that all income is taxable regardless of where it is generated. This principle is established in Article 1 of the MITL.

To mitigate potential situations of international double taxation, Article 5 of the MITL allows taxpayers to credit foreign taxes paid against their domestic income tax liability, subject to certain limitations.

By contrast, non-residents are taxed only on Mexican-source income, in accordance with Title V of the MITL. In this context, the existence of a PE in Mexico is a key factor in determining the applicable tax regime.

2.2 Tax Residence of Individuals

According to Article 9 of the FFC, an individual is considered tax resident when: (i) they have a permanent

home in Mexico; or (ii) their centre of vital interests is located in Mexico.

The concept of centre of vital interests is determined through objective economic criteria. An individual is deemed to have their centre of vital interests in Mexico when: (i) more than 50% of their total income during the calendar year is derived from Mexican sources; or (ii) their principal professional activities are carried out in Mexico.

In practice, Mexican law relies primarily on these economic indicators, rather than on broader personal or family ties.

In addition, Mexican nationals are generally presumed to remain tax resident in Mexico, unless they formally notify the tax authorities of a change of tax residence. Accordingly, the loss of Mexican tax residence requires not only a change in factual circumstances but also compliance with formal administrative requirements, including the filing of a notice before the tax authority.

2.3 Taxation of Resident Individuals

As mentioned above, individuals who are tax resident are subject to income tax on their worldwide income, which is calculated by applying a progressive rate schedule established in Article 152 of the MITL, under which the applicable tax rate increases according to the level of income earned.

The taxable base is determined by subtracting allowable deductions from gross taxable income. These deductions may include certain personal expenses, contributions, and other deductions expressly authorised under domestic tax law, such as medical expenses, transportation expenses, and similar items.

In the international context, the principal mechanism used to avoid double taxation is the foreign tax credit, which allows taxpayers to credit foreign taxes paid against domestic income tax liabilities, within the limits established by Mexican legislation.

2.4 Taxation of Non-Resident Individuals

Non-residents deriving income from Mexican sources are subject to income tax in accordance with Title V of the MITL provisions. In general terms, such income is

taxed through withholding at source, applying specific rates depending on the income, including: (i) employment income; (ii) interest; (iii) dividends; (iv) royalties; and (v) capital gains.

The applicable withholding rates will depend on the type of income and the specific conditions established under domestic law. However, when an applicable double taxation treaty exists, the taxpayer may benefit from reduced withholding rates or alternative allocation of taxing rights provided under the treaty.

2.5 Tax Residence of Legal Entities

Pursuant to Article 9 of the FFC, a legal entity is considered tax resident when its principal place of business administration or place of effective management is located within Mexican territory.

This criterion is complemented by Article 4-A of the MITL, which provides that foreign transparent legal entities may also be treated as Mexican tax residents when their place of effective management is located in Mexico.

This criterion aims to identify the jurisdiction where key strategic and managerial decisions are effectively made, reflecting the approach generally adopted in international tax law for determining the residence of legal entities.

2.6 Definition of Permanent Establishment

Under Article 2 of the MITL, a permanent establishment is defined as any place of business through which business activities are wholly or partially carried out, or through which independent personal services are rendered.

Examples of PEs include branches, agencies, offices, factories, workshops, installations, mines, quarries and any place where natural resources are explored, extracted or exploited.

The MITL also recognises the existence of a dependent agent PE in cases where a person in Mexico habitually acts on behalf of a foreign resident and performs activities leading to the conclusion of agreements that:

- are concluded in the name of the foreign resident;

- involve the transfer of ownership rights or the granting of the use or enjoyment of property owned by the foreign resident; or
- require the foreign resident to provide services.

PE domestic definition is aligned with the OECD Model Tax Convention definition, particularly regarding the existence of a fixed place of business through which the enterprise carries on its activities.

However, Mexico introduced some reservations and observations with respect to the OECD Model, particularly concerning:

- the recognition of a PE in construction or supervision projects exceeding certain time thresholds;
- taxation of services performed in the source state for extended periods; and
- the interpretation of preparatory or auxiliary activities.

These positions reflect Mexican policy stance as a source-oriented jurisdiction seeking to preserve broader taxing rights over income generated within its territory.

3. Taxation of Cross-Border Income

3.1 Income From Immovable Property

Taxation of Residents

Resident legal entities

Resident legal entities are taxed on their worldwide income under the general corporate income tax regime. Accordingly, income derived from immovable property, whether through transfer or leasing, is included in the taxable base and is subject to the general corporate income tax rate of 30%.

Capital gains are determined on a net basis, by subtracting the tax basis and allowable deductions from the sale price. This gain is tax at the corporate income tax rate of 30%.

Resident individuals

Resident individuals are also taxed on a worldwide income basis, but subject to a progressive rate schedule under Article 152 of the MITL.

In the case of real estate leasing, individuals can choose between: (i) deduction of the proven expenses like maintenance, insurance and property tax; or (ii) a so called “blind deduction” under which a statutory 35% deduction of the gross income plus property tax applies.

In the case of capital gains from the transfer of real estate, the taxable gain is calculated by subtracting the cost of acquisition and authorised deductions from the sale price. Capital gains derived from the transfer of real estate are determined by subtracting the tax basis (cost of acquisition) and certain allowable deductions from the sale price. The corresponding tax is calculated using the progressive rate schedule established in Article 152 of the MITL.

Additionally, the MITL provides that if the real estate is the taxpayer's primary residence, the sale may be exempt up to 700,000 UDIs or investment units (approximately USD320,000).

Taxation of Non-Residents

For non-residents, Article 160 of the MITL provides that the tax is determined by applying a 25% withholding tax on the gross proceeds, without allowing deductions.

However, non-residents may elect to be taxed on a net basis (ie, on the actual capital gain) applying the general tax rate, provided certain formal requirements are met. These include the requirement that the transaction be formalised through a public deed before a notary public and that the relevant reporting obligations be satisfied.

In addition, certain state-level taxes on the acquisition of real estate may apply depending on the jurisdiction where the property is located.

Rental income from real estate located in Mexico

For non-residents, withholding tax at source is applied, typically at a 25% rate on the gross income, without allowing deductions.

3.2 Business Profits

Pursuant to Article 9 of the MITL, business profits earned by resident legal entities are subject to corporate income tax at a rate of 30%.

Resident legal entities are taxed on a worldwide income basis, meaning that all income must be included in the tax base regardless of the jurisdiction in which it arises. Income tax is paid through monthly advance payments calculated based on accumulated profits during the fiscal year.

For non-residents, business profits are generally taxable only if they are attributable to a PE located in Mexican territory, according to Article 2 of the MITL and applicable tax treaties.

Rule 2.1.33 of the Miscellaneous Tax Resolution establishes that, for the purpose of applying tax treaties, the term “business profits” refers to income derived from business activities, which pursuant to Article 16 of the FFC, are defined as those of a commercial, industrial, agricultural, livestock, fishing or forestry nature; thereby providing a functional domestic reference for the interpretation of the treaty concept of business profits.

3.3 Passive Income

Passive income (eg, dividends, interest and royalties) is generally taxed through withholding at source.

Dividends

Dividends distributed by Mexican companies to resident individuals are subject to an additional withholding tax of 10% in accordance with Article 140 of the MITL.

Dividends paid to non-residents are also subject to a 10% withholding tax, subject to potential reductions under an applicable tax treaty.

Interest

Interest income is subject to different withholding rates depending on the nature of the lender and the financial instrument involved. In general terms, withholding rates range approximately between 4.9% and 35%, pursuant to Title V of the MITL provisions.

For tax residents, interest income is treated as taxable income and included in the taxpayer’s taxable base.

Royalties

Royalties paid to non-residents are subject to withholding taxes that may range between 1% and 25%, depending on the nature of the underlying rights involved (eg, copyrights, patents, trade marks or technical assistance) (Article 167 of the MITL).

Withholding Tax

The withholding tax rates established under domestic legislation may be reduced or eliminated under an applicable double taxation treaty.

In practice, treaty benefits are generally applied directly at the withholding stage by the payer (withholding agent), who is responsible for applying the appropriate reduced rate, provided that the recipient demonstrates tax residence in the relevant contracting state and complies with the applicable procedural requirements under national law.

In this context, the withholding agent assumes a position of joint liability for the correct application of the treaty provisions. Accordingly, if treaty benefits are applied incorrectly, the withholding agent may be held liable.

3.4 Capital Gains

Capital gains are generally treated as taxable income for income tax purposes.

Residents

For resident individuals, capital gains are taxed under the progressive rates established in Article 152 of the MITL, while resident legal entities are taxed at the corporate income tax rate of 30%.

Non-Residents

For non-residents, capital gains derived from the disposal of assets located in Mexico or shares issued by Mexican companies may be subject to withholding taxes under Title V of the MITL, unless an applicable tax treaty provides otherwise.

3.5 Employment Income

Employment income is taxed in Mexico under the progressive rate schedule established in Article 152 of the MITL. The tax is withheld and remitted by the employer, who acts as the withholding agent.

Pursuant to Article 154 of the MITL, for non-resident employees, income is considered to have a Mexican source when the services are performed within Mexican territory. However, when: (i) the salary is paid by a foreign employer without a PE in Mexico; and (ii) the employee remains in Mexico for less than 183 days within a 12-month period, the income may be exempt from Mexican taxation, provided that the statutory conditions are satisfied.

Currently, Mexican tax legislation does not contain specific rules addressing cross-border remote work, and therefore the tax treatment generally depends on the physical location where the services are effectively performed.

3.6 Other Income

There are other categories of income subject to specific rules under Mexican law, such as: (i) independent personal services; and (ii) technical assistance. In certain cases, the tax treatment may differ from that contemplated in the OECD Model Tax Convention, particularly with respect to the definition and taxation of royalties and technical assistance, in relation to which, Mexico has applied reservations in its treaty practice.

4. OECD/G20 Global Tax Reform

4.1 Pillar One – Amount B

Amount B of Pillar One was developed by the OECD as a mechanism designed to simplify the application of the arm's length principle in certain baseline marketing and distribution activities.

Specifically, Amount B proposes a standardised return for routine marketing and distribution functions considered low risk, with the objective of reducing transfer pricing disputes and enhancing tax certainty.

To date, Mexico has not formally adopted a specific domestic regime implementing Amount B within its tax legislation. Consequently, distribution activities carried out by multinational enterprises continue to be analysed under the general transfer pricing rules under the MITL, as well as under the OECD Transfer Pricing Guidelines.

4.2 Pillar One – Amount A

Amount A of Pillar One represents a structural shift from the traditional international tax framework based on the PE concept.

Under this approach, a portion of the residual profits of certain multinational enterprise groups would be reallocated to market jurisdictions where consumers or users are located, even in the absence of physical presence.

The purpose of this mechanism is to adapt the international tax system to highly digitalised business models capable of generating significant revenues in a jurisdiction without substantial physical presence.

Mexico has participated actively in the development of Pillar One as a member of the OECD/G20 Inclusive Framework and has generally supported the objective of partially reallocating taxing rights to market jurisdictions.

Nevertheless, the effective implementation of Amount A depends on the entry into force of a multilateral convention, which would subsequently need to be incorporated into domestic law following the constitutional procedure applicable to international treaties.

4.3 Pillar Two

Pillar Two introduces a global minimum tax system designed to ensure that multinational enterprises pay a minimum level of taxation regardless of where they operate.

The system is based on the Global Anti-Base Erosion Rules (GloBE), which establish a minimum effective tax rate of 15% for multinational enterprise groups with consolidated revenues exceeding approximately EUR750 million.

The mechanism operates by determining the effective tax rate (ETR) in each jurisdiction where the multinational group operates. When the ETR in each jurisdiction falls below the 15% minimum rate, a top-up tax is triggered in order to increase the effective tax burden to the agreed minimum level.

At the time of writing, Mexico has not formally implemented Pillar Two rules in its domestic legislation, and therefore the global minimum tax does not currently apply within the Mexican tax system.

4.4 Specific Features or Deviations of Pillar Two

See 4.3 Pillar Two.

4.5 Digital Services Tax

Mexico has not adopted a specific digital services tax (DST) comparable to those implemented in certain jurisdictions within the European Union. However, in 2020, domestic legislation introduced a special value added tax (VAT) regime applicable to digital services supplied by non-resident providers without a PE in Mexico.

Under this regime, foreign digital service providers supplying services to users located in Mexico (ie, streaming platforms, digital intermediation platforms or online services) must:

- register before SAT;
- charge and remit VAT on the services provided; and
- comply with reporting and information obligations.

The objective of this regime is to ensure tax neutrality between domestic and foreign digital service providers and secure VAT collection within the digital economy.

5. Anti-Avoidance and Anti-Evasion Measures

5.1 Definition and Identification of Tax Fraud, Evasion, Tax Avoidance and Abusive Schemes

Under Article 108 of the FFC, a person commits tax fraud when, through deceit or by taking advantage

of errors, they wholly or partially omit the payment of taxes or obtain an undue benefit to the detriment of the federal treasury. In addition, Article 109 of the FFC establishes a series of conducts treated as equivalent to tax fraud, which are punishable with the same penalties.

By contrast, the concepts of tax evasion and tax avoidance are not expressly defined in domestic tax legislation. However, under a doctrinal perspective, a distinction is typically made between:

- tax evasion, which involves the unlawful failure to comply with tax obligations through concealment, misrepresentation or falsification; and
- tax avoidance, which refers to the reduction or deferral of tax liabilities through formally lawful arrangements that exploit gaps or inconsistencies in the law, for the primary purpose of obtaining a tax advantage.

The latter category is addressed primarily through the General Anti-Avoidance Rule (GAAR) established in Article 5-A of the FFC, which provides that legal acts lacking a valid business purpose and generating a direct or indirect tax benefit may be recharacterised for tax purposes, assigning them the tax effects that would reasonably correspond to the transactions that would have been carried out to obtain the expected economic benefit.

The provision also establishes a rebuttable presumption that a transaction lacks a business purpose when the quantifiable economic benefit is lower than the tax benefit obtained.

Cross-Border Transactions

In cross-border transactions, the identification of abusive arrangements is further supported by several specific anti-avoidance mechanisms. First, Articles 179 and 180 of the MITL require that transactions between related parties be conducted in accordance with the arm's length principle, meaning that a deviation from arm's length pricing may constitute an indicator of base erosion or artificial profit shifting.

Second, preferential tax regime rules established in Articles 176 to 178 of the MITL aim to prevent the

artificial deferral or diversion of profits to low-tax jurisdictions.

Finally, Article 28, section XXIII of the MITL denies the deductibility of certain payments made to related parties or under structured arrangements when the corresponding income received by the related party is subject to a preferential tax regime, including situations involving hybrid structures.

Principal Legal Indicators of Tax Abuse

In summary, the principal legal indicators used to identify abusive tax arrangements include:

- the absence of a valid business purpose under Article 5-A of the FFC;
- the lack of economic substance or material capacity in documented transactions;
- non-compliance with the arm's length principle in related-party transactions; and
- the use of structures involving low-tax jurisdictions or hybrid arrangements.

5.2 Anti-Avoidance Mechanisms

The Mexican legal framework includes both general and specific anti-avoidance mechanisms aimed at addressing tax fraud, evasion and aggressive tax planning, provisions primarily established in the FFC and the MITL.

General Anti-Avoidance Rule (GAAR)

The GAAR, contained in Article 5-A of the FFC, allows the tax authorities, within the exercise of their audit powers, to presume that certain legal acts lack a business purpose and their tax consequences can therefore be recharacterised according to the economic benefit reasonably expected by the taxpayer.

Importantly, this provision does not invalidate the legal act itself, but rather allows the tax authorities to redefine its tax effects for the purpose of determining the appropriate tax treatment.

Specific Anti-Avoidance Rules (SAARs)

In addition to the GAAR, Mexican tax law includes specific anti-avoidance rules (SAARs) designed to address types of tax planning structures, especially in a cross-border context.

For example, in interest payments the following SAARs apply:

Interest deduction limitation (earnings-stripping rule)

Pursuant to Article 28, section XXXII of the MITL, the deductibility of net interest expense is limited to 30% of the taxpayer's adjusted taxable profit (tax EBITDA). Net interest exceeding this threshold is non-deductible in the relevant fiscal year, although it may generally carry forward for up to ten years, subject to certain conditions.

Thin capitalisation rules

Under Article 28, section XXVII of the MITL, interest paid on debt contracted with foreign related parties is non-deductible to the extent that the taxpayer's debt-to-equity ratio exceeds 3:1.

Non-deductibility of payments to low-tax jurisdictions and hybrid structures

In accordance with Article 28, section XXIII of the MITL, payments made to related parties, or under structured arrangements, are non-deductible when:

- such income is subject to a preferential tax regime;
- the payment gives rise to a hybrid mismatch, resulting in non-taxation or double deduction; or
- the income is not effectively subject to taxation abroad.

The Transfer Pricing Regime

The transfer pricing regime, primarily set forth in Articles 179 and 180 of the MITL, requires taxpayers engaged in transactions with related parties to determine their taxable income and allowable deductions based on the arm's length principle (prices or consideration that would have been agreed upon by independent parties in comparable transactions).

These rules represent the primary mechanism for preventing artificial profit shifting in cross-border related-party transactions.

Preferential Tax Regime Rules

Under Article 176 of the MITL, income obtained through foreign entities or legal arrangements subject

to low taxation may be treated as income derived from preferential tax regimes.

Income is considered subject to a preferential tax regime when it is either not taxed abroad or taxed at an effective rate lower than 75% of the tax that would have been payable in Mexico. In such cases, the tax-resident taxpayer must recognise the income in the fiscal year in which it is generated, in proportion to its direct or indirect participation in the foreign entity, even if the income has not been distributed.

Additionally, Article 178 of the MITL establishes specific reporting obligations, including the submission of an annual informative return regarding income derived from preferential tax regimes.

This regime is complemented by Article 28, section XXIII of the MITL, which denies the deductibility of certain payments made to related parties or under structured arrangements when the corresponding income is subject to a preferential tax regime. This rule operates as a specific anti-hybrid and anti-base-erosion mechanism in international tax structures.

Presumed Non-Existence of Transactions

Another significant anti-avoidance mechanism is contained in Article 69-B of the FFC, which allows the tax authorities to presume the non-existence of transactions documented through tax invoices when the issuer lacks the assets, personnel, infrastructure or material capacity necessary to perform the activities or services described.

Taxpayers identified under this procedure may be included in a public list of entities issuing simulated invoices, published by the SAT and in the Official Gazette, making this provision one of the most visible tools used to combat invoice-based tax evasion schemes.

Reportable Tax Schemes (Mandatory Disclosure Rules)

Mexico also operates a mandatory disclosure regime for reportable tax schemes, established in Articles 197 to 202 of the FFC.

Article 197 identifies tax advisers who are required to disclose reportable arrangements, while Article 198 provides that in certain circumstances the disclosure obligation falls on the taxpayer itself.

These provisions require the disclosure of tax arrangements that may generate a tax benefit in Mexico and that have certain characteristics associated with potential tax avoidance risks.

5.3 Blacklists and Non-Cooperative Jurisdictions

Mexico does not maintain a formal blacklist of non-cooperative jurisdictions comparable to those adopted by certain international organisations.

Instead, it relies primarily on the preferential tax regime (*regímenes fiscales preferentes*, or REFIPRES) framework, provided by Articles 176 to 178 of the MITL, which identifies income derived from low-tax jurisdictions and operates through a substance-based, case-by-case analysis of foreign income.

Under such framework, income obtained through foreign entities or legal arrangements is considered subject to a preferential tax regime when it is: (i) not subject to taxation abroad; or (ii) subject to an income tax rate lower than 75% of the tax that would have been payable in Mexico on the same income.

This determination is made on a case-by-case analysis, requiring a comparison between: (i) the effective tax burden in the foreign jurisdiction; and (ii) the Mexican income tax that would have been due under domestic rules.

In such cases, a taxpayer must include the income in its taxable base in the year in which it is generated, proportional to its direct or indirect participation in the foreign entity receiving the income, regardless of whether the income has been distributed.

For this purpose, the taxpayer must determine the taxable result of the foreign entity under domestic tax rules, to determine the taxable base and calculate the corresponding tax liability.

In addition, taxpayers must comply with specific reporting obligations, including the filing of an informative return in February of each year reporting income obtained from preferential tax regimes during the preceding fiscal year.

This approach is aligned with an effective taxation test rather than a jurisdictional blacklist.

5.4 Reporting Obligations and Disclosure Regimes

National law combines traditional reporting obligations with mandatory disclosure regimes designed to detect and prevent tax evasion and tax avoidance.

Related-Party Reporting

Under Article 76 of the MITL, taxpayers must maintain and submit information regarding transactions carried out with foreign related parties.

Furthermore, Article 76-A of the MITL introduced the obligation to complete master file, local file and country-by-country reports for certain multinational groups, in line with Action 13 of the OECD BEPS Project.

Preferential Tax Regime Reporting

As previously discussed, Article 178 of the MITL requires taxpayers to file an informative return in February of each year reporting income generated through preferential tax regimes during the preceding fiscal year, whether obtained directly or through foreign entities.

Reportable Tax Schemes (Mandatory Disclosure Rules)

Mexico also operates a mandatory disclosure regime for reportable tax schemes, established in Articles 197 to 202 of the FFC.

Under this regime, certain tax arrangements must be disclosed to the tax authorities when they generate, or are expected to generate, a tax benefit in Mexico and exhibit specific characteristics associated with potential tax avoidance risks.

Pursuant to Article 199 of the FFC, a reportable tax scheme is defined as any arrangement that produces or may produce a tax benefit in Mexico, and that

falls within a set of predefined characteristics, which among other things includes:

- arrangements that avoid the exchange of financial information;
- mechanisms to prevent the identification of the ultimate beneficiary of income or assets;
- transactions involving loss transfers or the use of tax attributes to reduce the tax base;
- hybrid or cross-border structures that generate double non-taxation; and
- arrangements that recharacterise income or exploit mismatches in tax treatments between jurisdictions.

Pursuant to Article 197 of the FFC, the obligation to disclose generally falls on tax advisers who design, promote, organise or implement the reportable scheme. However, pursuant to Article 198 of the FFC, the obligation may shift to the taxpayer in certain circumstances, including when:

- the adviser is not required to disclose;
- the adviser is located abroad; or
- legal privilege or confidentiality rules apply.

Reportable schemes must be disclosed generally within 30 days from the date on which the scheme is made available or implemented, depending on the nature of the arrangement.

5.5 Role of Tax Authorities and Enforcement Measures

Audit Powers

Tax authorities may exercise audit powers to verify taxpayers' compliance with tax obligations. These powers include:

- on-site tax audits conducted at the taxpayer's registered tax domicile;
- desk audits requiring the taxpayer to provide documentation and information at the tax authority's offices; and
- electronic audits carried out based on information contained in the tax authority's electronic databases.

Recharacterisation of Transactions

Tax authorities may also apply Article 5-A of the FFC to recharacterise transactions lacking a business purpose and Article 69-B of the FFC to presume the non-existence of transactions supported by tax invoices when the issuer lacks sufficient economic substance.

Furthermore, the tax authorities may determine the simulation of legal acts for tax purposes and reclassify them accordingly, particularly in the context of related-party transactions and transfer pricing adjustments. In such cases, the authorities may recharacterise transactions according to their true economic substance, assigning the tax consequences that would reasonably correspond to the transaction capable of generating the expected economic benefit.

Under Article 69-B of the FFC, the tax authorities may presume the non-existence of transactions documented through electronic tax invoices when the issuing taxpayer lacks the assets, personnel, infrastructure or material capacity required to carry out the activities or services described in such invoices.

6. Penalties and Sanctions

6.1 Tax Penalties

Penalties are primarily established in the FFC and the MITL.

The FFC

Under the FFC, several administrative penalties are established, including monetary fines for the failure to comply with formal tax obligations, for example failure to:

- file informative returns concerning related-party transactions;
- report payments made to foreign entities; or
- comply with reporting obligations related to preferential tax regimes.

The FFC also provides fines in cases of late payment or omission of taxes, and in certain circumstances the tax authorities may impose administrative measures such as the restriction or cancellation of the digital certificate required to issue electronic tax invoices. In

addition, it establishes tax crimes, including tax fraud and equivalent tax fraud offences, which may result in criminal sanctions including imprisonment and monetary penalties.

The MITL

The MITL also provides specific consequences in the context of international transactions. For example, if transactions between related parties are not conducted at arm's length, the tax authorities may recharacterise the transactions according to their economic substance and determine the taxable profits that would reasonably have been obtained between independent parties.

Similarly, under the preferential tax regime, income obtained through foreign entities subject to low taxation must be recognised in the fiscal year in which it is generated, in proportion to the taxpayer's direct or indirect participation, even if such income has not been distributed.

For these purposes, the taxable result of the foreign entity must be determined in accordance with domestic tax rules, calculating the corresponding tax using the applicable domestic tax rate.

Finally, national tax law also allows the tax authorities to deny treaty benefits under double taxation agreements when substantive requirements are not satisfied, such as the existence of a valid business purpose or beneficial ownership of the income.

Sanctions

Administrative sanctions are imposed and enforced by SAT, while criminal offences are investigated by the Federal Public Prosecutor's Office and adjudicated by the criminal courts.

6.2 Criminal Penalties

Article 108 of the FFC establishes tax fraud offence, which is committed when a person, through deception or by taking advantage of errors, wholly or partially omits the payment of a tax or obtains an undue benefit to the detriment of the federal treasury.

The applicable penalties vary depending on the amount of tax evaded but may include:

- imprisonment (three months to nine years); and
- monetary fines.

These penalties may be increased in the presence of aggravating circumstances such as:

- failure to withhold or remit taxes that were collected on behalf of third parties;
- the simulation of legal acts or transactions for tax purposes; and
- the use of false invoices to reduce taxable income.

In addition, Article 109 of the FFC regulates equivalent tax fraud offence, through which the same penalties applicable to tax fraud may be imposed on individuals who, for example:

- report false deductions or reduce taxable income in tax returns;
- improperly benefit from a tax subsidy or incentive; or
- fail to file mandatory tax returns for more than 12 months when such returns are required to be filed on a final basis.

6.3 Interaction Between Tax and Criminal Procedures

Pursuant to Article 93 of the FFC, when tax authorities become aware of facts that may constitute a criminal tax offence, they are required to notify the Federal Public Prosecutor's Office and provide the documentation and evidence collected during the administrative proceedings.

The investigation and prosecution of tax crimes therefore fall within the jurisdiction of the Federal Public Prosecutor's Office, while criminal penalties are imposed by the competent criminal courts. Importantly, the Mexican legal system follows a principle of independence between administrative and criminal proceedings. Accordingly, tax audits and administrative determinations of tax liabilities are conducted independently from criminal investigations and prosecutions; therefore, one does not necessarily depend on the outcome of the other.

7. Administrative Co-Operation

7.1 Legal Framework for Administrative Co-Operation

Mexico participates in a broad range of international legal instruments aimed at facilitating administrative co-operation in tax matters, including mechanisms for exchange of information, mutual assistance and co-ordinated efforts to prevent base erosion and profit shifting.

Most Relevant Instruments

Multilateral Instrument (MLI)

This aims to:

- prevent the abuse of tax treaties;
- eliminate tax avoidance through treaty structures;
- introduce measures designed to discourage BEPS practices; and
- improve the efficiency of dispute resolution mechanisms.

Double taxation treaties

Most of these include provisions on exchange of information and administrative co-operation.

The relationship between the MLI and bilateral tax treaties can be summarised as follows: (i) both instruments co-exist and share the same legal nature under international law; and (ii) where potential conflicts arise, they must be resolved through the interpretative mechanisms and conflict clauses established under treaty law.

In practice, the application of international tax rules generally follows a three-step approach:

- analysis under domestic tax law;
- analysis under the relevant double taxation treaty; and
- analysis under the MLI, where applicable.

The Supreme Court of Justice has also clarified that the taxable events and tax rates applicable within the national legal system are established in domestic tax law, particularly the MITL. Accordingly, tax treaties do not create tax obligations, but rather determine which contracting state has the right to tax a given category

of income and establish limitations on domestic taxation.

Therefore, when applying a tax treaty in conjunction with domestic law, the following steps generally apply:

- the taxpayer must demonstrate tax residence in one of the contracting states;
- the taxable event must first be determined under domestic law;
- the applicable treaty provision must then be identified; and
- if the treaty provides a maximum withholding tax rate lower than the domestic rate, the treaty rate may be applied directly by the withholding agent.

Country-by-Country Reporting Multilateral Competent Authority Agreement

On 27 January 2016, Mexico signed the Multilateral Competent Authority Agreement on the Exchange of Country-by-Country Reports (CbCR).

This agreement facilitates international tax transparency and the exchange of information between tax authorities, and its implementation within domestic law is aligned with OECD BEPS Action 13, which concerns transfer pricing documentation and country-by-country reporting.

7.2 Exchange of Information Clauses in Tax Agreements

Mexico participates in the Common Reporting Standard (CRS) developed by the OECD for the automatic exchange of financial account information between tax administrations.

Under the CRS framework, financial institutions annually report information regarding financial accounts held by foreign tax residents, which is automatically exchanged with the tax authorities of participating jurisdictions.

Mexico also exchanges information through the CbCR framework.

In addition, domestic legislation and international agreements also allow for spontaneous exchange of information, where relevant information discovered

during a tax audit may affect taxation in another jurisdiction, as well as the exchange of information upon request.

These exchanges are conducted in accordance with international agreements such as tax treaties (in particular Article 26) and the Multilateral Convention on Mutual Administrative Assistance in Tax Matters.

In particular, exchange of information upon request (EOIR) operates through a formal procedure whereby the competent authority of a foreign jurisdiction submits a specific and justified request to the competent Mexican authority, demonstrating that the requested information is foreseeably relevant for the administration or enforcement of its domestic tax laws, in line with the standard set forth in Article 26 of the OECD Model Tax Convention.

Upon receipt of such request, SAT is empowered to obtain the requested information by exercising its domestic audit and information-gathering powers, including those provided under Article 42 of the FFC, which allow the authority to request information from taxpayers, financial institutions and third parties.

At the domestic level, the exchange of taxpayer information is further supported by Article 69 of the FFC, which, while establishing the general principle of tax secrecy, expressly permits the disclosure of such information when required under international agreements to which Mexico is a party.

The entire process is subject to strict confidentiality and use limitations, ensuring that the exchanged information is used exclusively for tax purposes and in accordance with the applicable treaty provisions.

7.3 Other Forms of International Tax Collaboration

Although Mexico does not currently participate in the OECD's International Compliance Assurance Programme (ICAP), it does participate in other forms of multilateral tax co-operation.

In particular, tax authorities may conduct simultaneous or joint tax audits with other jurisdictions in cases involving multinational enterprises or cross-border

transactions. These activities are typically supported by international legal instruments such as the Multilateral Convention on Mutual Administrative Assistance in Tax Matters and bilateral tax treaties containing provisions on exchange of information and administrative co-operation.

Also, as a member of the OECD, Mexico also actively participates in international working groups and forums on tax administration, exchange of information and the development of international tax standards.

8. Mutual Agreement Procedures and Arbitration

8.1 Availability and Legal Basis

Mexico operates a mutual agreement procedure (MAP) framework under its tax treaties. Therefore, the national tax administration has issued a specific administrative procedure for requesting the initiation of a MAP under a double taxation treaty. This procedure is described in administrative form 102/CFF, which is included in Annex 2 of the Miscellaneous Tax Resolution for 2026.

The procedural requirements and legal basis for the MAP are provided in both the FFC and the MITL, as well as in the relevant tax treaties.

8.2 Application Deadlines

The deadline for submitting a MAP request is primarily determined by the provisions of the relevant double taxation treaty, which typically follow Article 25 of the OECD Model Tax Convention and provide a time limit generally three years from the first notification of the action that resulted in taxation not in accordance with the treaty.

This treaty based time limit is expressly recognised in domestic administrative provisions, particularly in Rule 2.1.29 of the Miscellaneous Tax Resolution and the corresponding Form 102/CFF contained in its Annex 2.

8.3 Mandatory Binding Arbitration

From an international tax perspective, mandatory arbitration is not generally available in Mexico.

Mexico has not adopted arbitration clauses as a standard feature in its double taxation treaties, and therefore disputes arising under the MAP are typically resolved through negotiations between competent authorities, without recourses to binding arbitration mechanisms.

At a domestic level, however, Mexican law provides several alternative dispute resolution mechanisms, which, while not equivalent to arbitration, aim to facilitate the resolution of tax controversies and include:

- Administrative Conclusive Agreements – an ADR mechanism that allows taxpayers to reach an agreement with the tax authorities, during a tax audit, in order to regularise their tax situation before a final determination is issued.
- The General Law on Alternative Dispute Resolution Mechanisms (*Los Mecanismos Alternativos de Solución de Controversias* or MASC) – enacted in Mexico in 2024, this introduces mechanisms such as negotiation, mediation and conciliation in administrative matters.

9. Dispute Prevention

9.1 Advance Pricing Agreements

Under Article 34 of the FFC, tax authorities may issue binding rulings regarding the methodology used to determine transfer prices or the amount of consideration in transactions between related parties, provided that the taxpayer submits the information and documentation necessary for the authorities to evaluate the request.

These rulings may be made conditional upon the taxpayer demonstrating that the transactions covered by the agreement are conducted at arm's length, consistent with the prices or margins that would have been agreed upon by independent parties in comparable transactions.

Such ruling may have effect:

- in the tax year in which the request is filed;
- in the immediately preceding tax year; and
- for up to three subsequent tax years.

Following a 2022 tax reform, legal entities operating under an IMMEX tax incentive programme are no longer allowed to request or renew advance pricing agreements (APAs) as a transfer pricing compliance mechanism. Instead, they must comply with Safe Harbour rules, which have become the exclusive compliance framework for maquilas (foreign-owned manufacturing plants in Mexico).

9.2 Other Mechanisms

From an international tax perspective, Mexico does not currently offer formal programmes aimed at obtaining tax certainty that are comparable to the co-operative compliance frameworks or enhanced engagement models implemented in other jurisdictions.

However, at the domestic level, Mexican law provides certain mechanisms that may contribute to tax certainty, particularly through the possibility of obtaining advance rulings from the tax authorities.

Taxpayers may submit binding consultations to SAT regarding the interpretation and application of tax provisions to specific factual situations. These rulings are generally binding on the tax authorities with respect to the requesting taxpayer, provided that the facts presented are accurate and complete.

Notably, such rulings are not subject to appeal, meaning that taxpayers cannot challenge their content through administrative or judicial means. As a result, while they may provide a degree of certainty, they do not constitute a negotiated or co-operative compliance mechanism, nor do they involve ongoing engagement between taxpayers and the tax authorities.

Accordingly, Mexico's approach to tax certainty in international matters remains primarily rule-based and transactional, rather than based on continuous or co-operative relationships between taxpayers and the tax administration.

Trends and Developments

Contributed by:

Ángel Escalante, Gabriel Rojas, Uzziel Rodríguez and Daniel Colunga
Escalante & Asociados

Escalante & Asociados (E&A Legal) is a boutique tax law firm with a team of highly specialised practitioners, focused on tax controversy and non-contentious tax matters. Established in 2015 by its managing partner, Ángel Escalante Carpio, the firm operates from offices in Mexico City and Houston, Texas, providing strategic advice on complex domestic and cross-border tax matters, particularly in the Mexico–US corridor. The firm is recognised for its expertise in tax audits, administrative proceedings, and high-stakes tax litigation, as well as in international tax planning, restructuring, compliance, and AML matters, offer-

ing an integrated approach that combines technical sophistication with a strong business-oriented perspective. Its practice also covers foreign trade, real estate tax structuring, estate planning for HNW individuals, and double taxation issues. E&A Legal regularly represents clients in disputes before Mexican tax authorities and advises multinational and domestic companies on the design and implementation of robust tax structures to mitigate risks and support their long-term business objectives, including cross-border operations and intercompany transactions.

Authors



Ángel Escalante is the founding partner of E&A Legal, with more than 20 years of experience in tax controversy, including administrative proceedings, tax audits and litigation before Mexican authorities. His

practice focuses on complex tax disputes, international taxation and matters involving foreign trade and anti-money laundering compliance. He holds law and accounting degrees, as well as a master's degree in tax law, and has completed advanced studies in international taxation. He is a member of the World Compliance Association, under which he co-ordinates the Tax Committee in Mexico, and the International Fiscal Association.



Gabriel Rojas is a partner at E&A Legal with more than ten years of experience in corporate tax and controversy, focusing on administrative proceedings, audits and disputes before Mexican

authorities. His practice focuses on domestic and international tax matters, including cross-border structuring, foreign trade and tax incentive programmes such as IMMEX and PROSEC, as well as VAT and excise tax certifications. He regularly represents clients before the Mexican Tax Administration Service (SAT) and other regulatory bodies. Gabriel has completed a law degree and postgraduate studies in international tax law, including an Advanced LLM from the University of Amsterdam, and is a member of the International Fiscal Association.



Uzziel Rodríguez is a senior attorney with more than 20 years of experience in tax controversy and dispute resolution, particularly in matters linked to large-scale real estate, corporate and expansion projects. His

practice at E&A Legal focuses on complex tax disputes, including matters involving regulatory scrutiny and multi-jurisdictional elements, and this is complemented by his experience in corporate law and compliance. He has worked in-house at organisations such as Walmart and Fibra Uno, where he led legal and contractual strategies and managed tax-related controversies. Uzziel holds a law degree from Escuela Libre de Derecho and has completed postgraduate studies in corporate and real estate law.



Daniel Colunga is an associate at E&A Legal, focusing on tax controversy, including administrative and constitutional tax litigation. He advises and represents clients in audits, investigations and disputes

before Mexican authorities, including the Mexican Tax Administration Service (SAT), PRODECON and other regulatory bodies, as well as before administrative and constitutional courts. His practice centres on complex tax disputes and enforcement-related matters. Prior to joining E&A Legal, he worked at specialised tax law firms, where he gained experience in taxpayer defence. Daniel holds a law degree from Escuela Libre de Derecho and is a member of the International Fiscal Association.

Escalante & Asociados

Torre Altiva/Blvd Manuel Avila Camacho 138 Piso 8
Lomas de Chapultepec
Miguel Hidalgo
11000, Mexico City
Mexico

Tel: (+52) 55 8854 9587
Email: dmariscal@eyalegal.com
Web: www.eyalegal.com



In recent years, Mexico's international tax landscape has undergone a significant transformation, driven by a combination of OECD-led reforms (particularly the base erosion and profit shifting (BEPS) Project), increased audit activity by tax authorities, and structural economic developments such as nearshoring and supply chain reconfiguration.

These developments have resulted in a more substance-oriented, enforcement-driven and internationally aligned tax environment, in which traditional tax planning structures are subject to increasing scrutiny.

The following trends reflect the most relevant developments currently shaping tax practice in Mexico, particularly in cross-border scenarios.

Interest Deduction Limitations and Financial Structuring

One of the most significant developments in Mexican tax practice has been the strengthening of interest deduction limitation rules, reflecting Mexico's alignment with BEPS Action 4 (limiting base erosion involving interest deductions and other financial payments).

As a starting point, interest expenses must comply with general deductibility requirements under Mexican tax law, which requires that expenses be strictly indispensable for the taxpayer's business activity, duly supported by tax invoices, properly recorded in the accounting records, and effectively paid through authorised means.

Earnings-stripping rule

The most relevant provision is contained in Article 28, section XXXII of the Mexican Income Tax Law (MITL), which establishes an earnings-stripping rule. Under this rule, net interest expense is deductible only up to 30% of the taxpayer's adjusted taxable profit (tax EBITDA). Any excess interest is disallowed in the relevant fiscal year but may generally be carried forward for up to ten fiscal years, subject to certain limitations.

This rule applies broadly to both domestic and cross-border financing. It represents a shift from transactional analysis to a global limitation approach, as it considers the taxpayer's overall financial position rather than individual transactions.

Thin capitalisation rule

In parallel, Mexico maintains a thin capitalisation rule under Article 28, section XXVII of the MITL, which specifically targets related-party debt. This provision limits the deductibility of interest when the taxpayer's debt-to-equity ratio exceeds 3:1, effectively disallowing interest attributable to excess leverage. This rule is particularly relevant in multinational group structures where debt is concentrated in Mexican entities.

Limitations on deductions

Additionally, Article 28, section XXIII of the MITL introduces limitations on deductions in cases involving: (i) hybrid mismatch arrangements, where differences in tax treatment between jurisdictions result in double non-taxation; and (ii) payments to entities subject to preferential tax regimes.

Importantly, these rules do not operate in isolation but rather apply cumulatively, creating a complex framework in which multiple limitations may simultaneously restrict the deductibility of a single financing arrangement.

Layered limitation framework

From a practical perspective, these rules operate cumulatively, creating a layered limitation framework. Taxpayers must therefore analyse interest deductibility from several angles simultaneously, including:

- quantitative limitations (EBITDA test);
- structural limitations (thin capitalisation); and
- anti-avoidance provisions (hybrids and low-tax jurisdictions).

Mexican tax authorities have increasingly focused on intra-group financing arrangements, particularly in audits involving multinational groups. Areas of scrutiny include:

- whether the borrower has the capacity to assume and service the debt;
- whether the financing structure reflects a genuine business need; and
- whether the interest rate complies with the arm's length principle.

In many cases, the authorities have challenged financing arrangements on the basis that they lack economic substance or business purpose, particularly where debt appears to be artificially introduced to generate tax deductions.

As a result, taxpayers have begun to restructure financing models, moving towards:

- increased use of equity funding;
- more conservative leverage ratios; and
- enhanced documentation to support the commercial rationale of financing transactions.

In practice, this reflects a broader shift towards a substance-over-form approach, where legal structuring alone is no longer sufficient to sustain tax benefits.

Real Estate Investment and Nearshoring Dynamics

Mexico has emerged as a key destination for foreign direct investment in real estate, largely driven by nearshoring trends and the strategic relocation of manufacturing and logistics operations closer to North American markets.

This shift has resulted in a significant increase in demand including industrial and logistics infrastructure, particularly in northern and central regions, warehousing and distribution facilities; and commercial and hospitality developments linked to industrial expansion.

From a tax perspective, Mexico offers a relatively attractive framework for real estate investment, combining structural flexibility with specific tax incentives.

One of the most important features of the Mexican system is the widespread use of trusts (*fideicomisos*) as investment vehicles. Trusts are generally treated as tax transparent, meaning that income is attributed directly to the beneficiaries rather than taxed at the trust level. This allows investors to structure investments in a flexible manner while maintaining tax efficiency.

In addition, Mexico has developed a sophisticated market for real estate investment trusts (*Fideicomisos de Infraestructura y Bienes Raíces* or FIBRAs), which

are publicly traded vehicles designed to facilitate investment in income-generating real estate.

FIBRAs offer several tax advantages, including:

- deferral of taxation upon contribution of assets;
- access to capital markets; and
- a single level of taxation at the investor level.

Recent government initiatives, particularly the “Infrastructure Investment Plan for Development with Well-being 2026–2030” programme, have further enhanced the attractiveness of real estate and infrastructure investment by introducing tax regimes for certain types of assets, including construction and infrastructure investments. The programme also outlines potential use of specialised funds and structures aimed at attracting institutional capital, reducing financing costs, and enhancing transparency standards.

Despite these advantages, real estate investments in Mexico involve a high degree of complexity due to the interaction between: (i) federal taxes (income tax and VAT); and (ii) local taxes, including property taxes and transfer taxes, which vary significantly across states and municipalities.

VAT treatment can be complex in cases involving mixed-use properties, where some activities are taxable, and others are exempt. This may result in non-creditable VAT, which can significantly impact project profitability.

Furthermore, real estate structures must carefully consider the potential creation of a permanent establishment (PE), particularly where foreign investors are involved in active management or development activities.

Under domestic law, a PE is deemed to exist when construction, installation, or related activities exceed a period of 183 days within a 12-month period. Notably, this threshold is broadened by rules that require the aggregation of time spent by subcontractors, significantly increasing the likelihood of triggering a PE.

Overall, while Mexico presents significant opportunities for real estate investment, it also requires a highly

structured and multidisciplinary approach, integrating tax, legal and operational considerations.

Substance, Materiality and Related-Party Transactions

A defining feature of the current Mexican tax environment is the increasing emphasis on economic substance and materiality, particularly in relation to related-party transactions.

General Anti-Avoidance Rule (GAAR)

This approach is anchored in the introduction of the General Anti-Avoidance Rule (GAAR) under Article 5-A of the Federal Fiscal Code (FFC), which allows tax authorities to disregard or recharacterise transactions that lack a valid business purpose and generate a tax benefit.

Transfer pricing rules

In addition, transfer pricing rules under Articles 179 and 180 of the MITL require that transactions between related parties be conducted in accordance with the arm's length principle, consistent with OECD standards.

Scrutiny of intercompany transactions

In practice, Mexican tax authorities have significantly increased their scrutiny of intercompany transactions, particularly those involving:

- place of effective management (POEM) and administrative services, where the benefit to the recipient is often questioned;
- royalties and licensing arrangements, especially in cases involving intangible assets with unclear ownership or value creation; and
- financial transactions, including loans and guarantees.

A key aspect is the concept of materiality, which requires taxpayers to demonstrate that transactions have a real economic impact and are not merely formal arrangements designed to achieve tax benefits.

This has led to a more substance-driven analysis, where tax authorities evaluate:

- whether the transaction would have been entered into by independent parties;
- whether it generates a measurable economic benefit; and
- whether it aligns with the functions, assets and risks (FAR analysis) of the entities involved.

This approach is closely aligned with OECD transfer pricing guidelines, particularly the emphasis on value creation and DEMPE functions (development, enhancement, maintenance, protection and exploitation) in relation to intangible assets.

In cross-border contexts, this has resulted in increased challenges to structures involving:

- low-substance entities in foreign jurisdictions;
- back-to-back arrangements; and
- centralised service or IP holding structures.

As a result, taxpayers are increasingly required to maintain adequate documentation and functional analyses, and to ensure that their structures reflect genuine economic activity.

Evolving Interpretation of “Business Activities”

Another important development in Mexican tax practice is the evolving interpretation of “business activities”, which plays a central role in determining the tax treatment of cross-border income.

Under Articles 14 and 16 of the FFC, business activities are broadly defined to include commercial, industrial, financial and service activities, among others. This broad definition has allowed tax authorities to adopt an increasingly expansive interpretation of what constitutes business activity.

This concept is particularly relevant in the context of:

- the determination of business profits under tax treaties;
- the identification of a PE; and
- the classification of income as active or passive.

In recent years, Mexican tax authorities have adopted a more substance-oriented approach, focusing on the actual conduct of the taxpayer rather than formal

legal structures. This has led to the recharacterisation of passive income as business income, particularly where the taxpayer is actively involved in generating such income; a broader interpretation of dependent agent permanent establishments, particularly where local agents play a key role in contract negotiation or conclusion; and increased scrutiny of digital and remote business models, where economic presence may exist without a traditional physical footprint.

In practice, this is consistent with broader international developments, including the OECD's work on the digital economy and nexus rules, although Mexico has not fully implemented all aspects of these initiatives.

In practice, foreign investors must carefully assess:

- their level of activity in Mexico;
- the role of local personnel or intermediaries; and
- the risk of being deemed to carry out business activities in Mexico, thereby triggering tax liability.

Failure to properly assess these factors may result in the unexpected recognition of a taxable presence (PE) and the recharacterisation of income, with significant tax implications.

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