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The Secretaria de Hacienda y Credito Publico (SHCP) has launched a series of fiscal reforms to expand the country's tax base, including programs that affect maquiladora plants and street vendors. President Ernesto Zedillo's proposed reforms are intended to reverse Mexico's extremely low tax- collection rate. Tax revenues have been falling steadily during the past decade. In 1998, income from taxes, excluding those paid by the state-run oil company PEMEX, amounted to only about 10.7% of GDP, a full percentage point below the 11.7% rate recorded in 1989.

So far this year, tax evasion and loopholes have cost the government at least 50 billion pesos (US $5.24 billion) in revenue, the equivalent of 1.25% of Mexico's GDP, the government's tax collection agency (Servicio de Administracion Tributaria, SAT) reported in early October.

The SHCP estimates that tax revenues will decline by another 40 billion pesos (US$4.19 billion), roughly 0.1% of Mexico's GDP, in 2000 because of scheduled reductions in income taxes (impuesto sobre la renta, ISR) and the elimination of some import tariffs under the North American Free Trade Agreement (NAFTA).

But low tax collections are also tied to the high poverty rate. The SHCP estimates that roughly 70% of Mexican workers do not earn enough to pay taxes. A recent survey by the government's statistics agency (Instituto Nacional de Estadisticas, Geografia e Informatica, INEGI) showed that 44% of Mexico's urban population earn the equivalent of two or less minimum wages per day, roughly 64 pesos (US$6.71).

Reducing reliance on oil-export revenues

The Zedillo administration's efforts to boost tax payments are part of a strategy to reduce reliance on oil exports to increase government revenues. Income from oil exports accounts for one-third of the government's total revenues. In years when oil prices fall sharply, as in 1998, the government is forced to reduce its budget (see SourceMex, 1998-07-15, 1998-03-25, 1998-01-21). Efforts to boost tax revenue will require major changes to the tax code. However, the president and Congress are not likely to enact any major changes in 2000 because it is an election year.

Meanwhile, the administration is seeking new avenues for tax revenues, such as the undertaxed maquiladora sector and the informal economy. Changes for the maquiladora sector, announced in late October, will require maquiladora plants to pay a higher rate on either their fixed assets or their operational costs. Maquiladoras will either have to pay 6.9% on their fixed assets or 6.5% on their operational costs. Since 1995, maquiladoras have paid only 5% on either their fixed assets or their operational costs. The new plan is a compromise from the original proposal announced in mid-August to begin charging income taxes to maquiladora plants (see SourceMex, 1999-09-01).

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The government planned to change the designation of maquiladoras to "permanent Mexican companies," rather than temporary enterprises dependent on a parent company in another country, which would have required maquiladoras to pay the same taxes as any other Mexican company.

The maquiladora industry protested the original plan, since this would have forced subsidiaries of US companies to pay income taxes to both Mexico's SAT and the US Internal Revenue Service (IRS). This concern prompted officials from the SHCP and the US Treasury Department to develop a temporary compromise, which was the tax plan announced in October.

The plan, which will be in effect from 2000 through 2002, will be replaced by a more comprehensive system to tax maquiladoras. US and Mexican officials are expected to meet during the next several months to draft the longer-term plan.

Tax increase for maquiladoras to raise 1.5 billion pesos

Deputy finance secretary Tomas Ruiz Gonzalez said the agreement with the US Treasury boosting the tax rates on fixed assets and/or operational costs will add as much as 1.5 billion pesos (US$157 million) each of the next three years to the Mexican Treasury.

Conversely, the US Treasury will lose this amount, since parent companies of maquiladora plants will receive US tax credits for any increased payments to the Mexican Treasury. "The agreement allows for a more equitable distribution of tax revenue between the two countries without increasing a company's total tax burden," Ruiz said at a maquiladora- industry convention in Cancun.

The Consejo Nacional de la Industria de la Maquiladora de Exportacion (CNIME), which strongly opposed the original income-tax plan, offered a guarded endorsement of the latest proposal. It said the positive aspect of the plan is that the overall tax burden would not change for the industry because any increased taxes paid in Mexico would be compensated by a tax reduction in the US.

But CNIME president Humberto Inzunza Fonseca said the industry was hoping for a longer-term solution to the tax situation. "We still only have a clear situation for the next three years," said Inzunza. "And this will still be somewhat risky for companies considering long-term investments." Still, other industry insiders praised the accord, which allows for gradual transition to a new plan.

"This is a good agreement for Mexico, the maquiladora industry, and the US government because it removes the prospect of unacceptable taxation on the US companies and creates a framework for discussing how the Mexican companies should be taxed in the future," CNIME tax adviser John McLees told The Christian Science Monitor.

Researchers David Eaton and Javier Alberto Reyes of the Instituto Tecnologico de Estudios Superiores de Monterrey (ITESM) said the proposed tax changes are a "clear signal" to the maquiladora sector to expand its role beyond simple assembly operations into value-added manufacturing. Government seeks to tax street vendors The SHCP, meanwhile, has also announced an ambitious program to incorporate Mexico's street vendors onto the government's taxpayer rolls.

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SAT director Alma Rosa Moreno said the Programa Nacional de Regulacion de la Economia Informal will require all 12 million to 16 million street vendors to register with the government. However, the government expects only a fraction of the vendors to earn enough from street sales to pay income taxes. The effort should initially boost the government's tax collections by about 8 billion pesos (US$840 million), said Moreno.

The government's program will initially be implemented in the five metropolitan areas of Mexico City, Guadalajara, Monterrey, Puebla, and Veracruz, and eventually extended to the rest of the country. Moreno dismissed criticisms that the program amounts to persecution and harassment of street vendors. She said the government is primarily targeting the street vendors' suppliers, which in many cases are large companies that distribute shoes, toys, and other illegally imported products. But the efforts to bring street vendors onto the tax rolls has already been strongly criticized by debtors-rights groups, economists, and the two major opposition parties.

Legislators from the center-left Partido de la Revolucion Democratica (PRD) and the conservative Partido Accion Nacional (PAN) will introduce a bill to halt the "fiscal terrorism." Among other things, the bill would remove some of the SHCP's powers to unilaterally adopt tax-related measures. The governors of six states led by opposition parties said they will refuse to comply with the program to collect taxes from street vendors during 2000.

In a letter to Finance Secretary Jose Angel Gurria Trevino, the governors of Baja California Sur, Nuevo Leon, Jalisco, Queretaro, Tlaxcala, Guanajuato, and Nayarit said the crackdown on street vendors is not supported by most Mexicans. "We are not going to go through this extra effort during an election year," the governors said.

PRD Sen. Hector Sanchez Lopez acknowledged the government's need to expand its sources of tax revenue, but he said this can be done without harassing average citizens. "We cannot continue supporting a government that collects the income of an increasingly impoverished population to rescue rich bankers," Sanchez said, referring to the government's controversial bank-rescue program (Fondo Bancario de Proteccion al Ahorro, FOBAPROA).

The PRD delegation in the finance committee (Comision de Hacienda) in the Chamber of Deputies has proposed that the government increase tax revenues by raising taxes on the "exorbitant earnings" from speculative investments on Mexico's stock exchange, the Bolsa Mexicana de Valores (BMV).

Economist urges government to focus on job creation

Pedro Venegas, an economist with the Centro de Analysis Proyecciones Economicas de Mexico (CAPEM), said the government could address the tax deficiencies by creating more jobs in the formal economy. CAPEM reports that Mexico will face a deficit of 16 million jobs next year, which will force even more Mexicans to earn a living from street sales, the black market, and other areas of the informal economy. The growth of Mexico's informal economy has attracted the attention of the International Labor Organization (ILO).

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At a recent conference in Monterrey, ILO director Jean Maniat said six of every 10 new jobs created in Mexico during the past decade were in the informal economy. "It's going to be extremely difficult to reverse this trend in the short term," said Maniat. "This is going to be a problem because 1.5 million persons enter the work force in Mexico every year."

Venegas said the government is wrong to view the informal economy as merely a byproduct of trade expansion, which has allowed easier entry of smuggled goods into the country. He said the increase is caused by a severe slump in sectors that have traditionally provided employment for Mexicans. He pointed in particular to agriculture, which provided 30% of the total jobs in Mexico in 1970. This percentage fell to 18% in 1998, he said. Venegas said the growth in the informal economy is also the result of a decline in the purchasing power of most Mexicans. He said current wages in real terms are only worth 29% of what they were in 1980.

Laura Juarez, a researcher at Universidad Obrera, has proposed that unions negotiate an increase in the minimum wage of no less than 154%, which is the only raise that will allow workers to recover their purchasing power. But the independent labor organization Consejo Nacional de los Trabajadores (CNT) has taken a more realistic stance, seeking an increase of no less than 25% in 2000.

However, the Zedillo administration and business organizations like the Centro de Estudios Economicos del Sector Privado (CEESP) have recommended that increases in the minimum wage be limited to 10% next year, to match the projected rate of inflation. [Note: Peso-dollar conversions in this article are based on the Interbank rate in effect on Nov. 3, reported at 9.53 pesos per US$1.00] (Sources: Knight Ridder news service, 10/26/99; La Jornada, 10/06/99, 10/12/99, 10/13/99, 10/22/99, 10/29/99; Los Angeles Times, Associated Press, 10/30/99; Reuters, 09/30/99, 10/29/99, 10/31/99; The Dallas Morning News, 10/19/99, 10/31/99; Proceso, 10/24/99, 10/31/99; El Financiero International, 10/25/99, 11/01/99; The Christian Science Monitor, 11/01/99; El Economista, 10/09/99, 10/12/99, 10/20/99, 11/01/99, 11/02/99; El Universal, 09/23/99, 10/18/99, 11/02/99; Excelsior, 10/13/99, 10/18/99, 10/30/99, 11/02/99, 11/03/99; Reforma, 10/27/99, 10/29/99, 10/30/99, 11/01-03/99)

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