



# TAX EXPENDITURES COUNTRY REPORT

**Mexico**

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## List of abbreviations

|                |   |
|----------------|---|
| <b>ASF</b>     | Auditoría Superior de la Federación [Mexico's supreme audit institution]  |
| <b>Banxico</b> | Banco de México [Mexico's central bank]   |
| <b>CEFP</b>    | Centro de Estudios de las Finanzas Públicas [Center for Public Finance Studies]   |
| <b>CIEP</b>    | Centro de Investigación Económica y Presupuestaria [Center for Economic and Budgetary Research]                           |
| <b>CIT</b>     | Corporate income tax  |
| <b>CSS</b>     | Contribuciones a la Seguridad Social [Social security contributions]  |
| <b>DOF</b>     | Diario Oficial de la Federación [Official Gazette of the Federation – the main official government publication in Mexico] |
| <b>GDP</b>     | Gross domestic product  |
| <b>GTETI</b>   | Global Tax Expenditures Transparency Index  |
| <b>IEPS</b>    | Impuesto Especial Sobre Producción y Servicios [Special Tax on Production and Services – Mexico's excise tax]             |
| <b>LIF</b>     | Ley de Ingresos de la Federación [Federal Revenue Act]  |
| <b>MXN</b>     | Mexican peso(s)   |
| <b>OECD</b>    | Organisation for Economic Co-operation and Development  |
| <b>PIT</b>     | Personal income tax   |
| <b>RESICO</b>  | Régimen Simplificado de Confianza [Simplified Trust Regime – a tax framework]   |
| <b>RIF</b>     | Régimen de Incorporación Fiscal [Fiscal Incorporation Regime – a tax framework]   |
| <b>SHCP</b>    | Secretaría de Hacienda y Crédito Público [Mexican Ministry of Finance and Public Credit]                                  |
| <b>USD</b>     | US dollar(s)  |
| <b>VAT</b>     | Value added tax   |

### Executive summary

In Mexico, tax expenditures refer to all fiscal measures that reduce public revenue by granting preferential tax treatment relative to the benchmark system. These include deductions, exemptions, tax credits, differentiated rates and tax incentives (SHCP, 2024b).

While tax incentives are conceptually equivalent to tax expenditures, in Mexico the former are a component of the latter, as per the structure of the SHCP's tax expenditures document. As such, **tax incentives constitute a specific subset of tax expenditures and are typically created by presidential decree**, unlike other benefits which are incorporated directly into tax legislation (SHCP, 2024b).

**Transparency:** Mexico fell from 42nd to 51st place in the Global Tax Expenditures Transparency Index (GTETI)'s 2024 ranking, reflecting a decline in the availability, quality and clarity of information pertaining to tax expenditures. While the country still meets the minimum standards for publication of tax expenditure information (as regards such things as estimates, methodology, legal basis and beneficiary analysis), there is still significant room for improvement, particularly when it comes to defining the benchmark, incorporating assessments and strengthening the role of Mexico's parliament, the Congress of the Union. With publication of the tax expenditures document (*Documento de Renuncias Recaudatorias*) having resumed in 2024, there is now an opportunity to make up lost ground in terms of tax transparency and promote more proactive oversight by the legislative branch and civil society.

**Complex fiscal landscape:** tax expenditures amounted to some MXN 1.42 trillion in 2024, which equates to 4.2% of gross domestic product (GDP) and 19.4% of tax revenue. The primary tax expenditures pertain to the 0% value added tax (VAT) rate and the income tax system. Additionally, tax incentives, most of which are granted by presidential decree, account for approximately 25% of total tax expenditure. These measures have different objectives, legal foundations and timeframes, reflecting a Mexican tax expenditure system that is fragmented and inconsistent in design.

**Evaluation challenges:** despite advances in incidence analysis and disaggregation by tax type, there is no systematic model in place to evaluate compliance with the objectives of this public policy. In the absence of ex-ante and ex-post evaluations and performance indicators, it is difficult to determine the effectiveness and relevance of the different tax expenditures. At the same time, a time lag between publication of tax decrees and the tax expenditures document limits assessment of the impact of these expenditures.

**Fiscal sustainability:** tax expenditures account for almost 20% of tax revenue. Their scale poses a challenge to the sustainability of public finances. Against the backdrop of the energy transition, demographic transition and structural pressure on welfare spending and public investment, it is essential to review the permanence and effectiveness of these tax expenditures to prevent them from becoming a structural source of inefficiency and regression.



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### Areas for improvement:

1. **Enhance the design** of tax expenditures with time (including sunset clauses), transparency and accountability criteria.
2. **Establish assessment standards**, including interim assessments of tax incentives.
3. **Integrate performance indicators** into budgetary programmes related to tax expenditures.
4. **Strengthen the technical capacities of the Congress of the Union**, and more specifically the Center for Public Finance Studies (CEFP), to assess the relevance of tax expenditures and their impact on the economy and public revenue.
5. **Promote a strategic vision** that brings tax expenditures into line with the objectives of the National Development Plan (*Plan Nacional de Desarrollo*) and ensures their long-term fiscal sustainability.

A tax reform process that incorporates an assessment of tax expenditures will make the tax system more progressive and effective.





## Mexico at a glance (2024)



Population  
**132.3**  
(million)

GDP

**MXN 25.41**  
**trillion**  
USD 1.388 trillion

GDP/capita

**MXN 192,100**  
USD 10,500

**8.6%**  
(of GDP)

Total national taxes and  
contributions

**52.1%**  
(of GDP)

Public debt

### TAX STRUCTURE

Tax revenue comprises taxes collected by central government and social security contributions (CSS). There are three components to CSS: contributions made by employees in the formal sector, employer contributions and contributions made by the federal government (CIEP, 2021).

#### Revenue from taxes, 2022

| Category                             | MXN million      | % total | % GDP       | USD million    |
|--------------------------------------|------------------|---------|-------------|----------------|
| <b>Direct taxes</b>                  | 1,236.392        | 58%     | 5.0%        | 61,428         |
| Corporate income tax                 | 1,201.888        | 57%     | 4.9%        | 59,714         |
| Personal income tax                  | 34,504           | 2%      | 0.1%        | 1,714          |
| <b>Indirect taxes</b>                | 726,602          | 34%     | 2.9%        | 36,100         |
| Special taxes                        | 172,004          | 8%      | 0.7%        | 8,546          |
| VAT                                  | 554,598          | 26%     | 2.2%        | 27,554         |
| CSS                                  | 159,456          | 8%      | 0.6%        | 7,922          |
| <b>Total taxes and contributions</b> | <b>2,122.450</b> |         | <b>8.6%</b> | <b>105,451</b> |

Source: Organisation for Economic Co-operation and Development (OECD) (2024), SHCP (2024a), Banco de México (Banxico) (2024), International Monetary Fund (IMF) (2024). World Bank (2025), MXN/USD exchange rate (2024) = 18.30 and (2022) = 20.13.





## Tax expenditures key figures (2024)

**Annual  
reporting**  
since  
**2002**

**125**  
Reported provisions

**MXN 1.42  
trillion**  
USD 77.5 billion

**4.2%**  
Total TEs as % of GDP

**19.4%**  
Total TEs as % of tax revenue

Source: SHCP (2024b) and Banxico (2024). World Bank (2025), MXN/USD exchange rate (2024) = 18.30.

Tax expenditures in Mexico are reported in the tax expenditures document (*Documento de Renuncias Recaudatorias*). This document must be published before 30 June each year and must include the following:

1. An estimate of the total revenue that will be foregone
2. The methodology used for the estimate
3. Legal basis
4. Beneficiary sectors or activities for each provision
5. Social and economic benefits associated with the tax expenditures



## Key governance and institutional features

*In Mexico, **tax expenditures** comprise the full range of fiscal measures that reduce public revenue. They consist of: **a) exemptions, b) deductions, c) differentiated rates, c) tax incentives and d) other preferential treatments**, and can be created through tax legislation or by presidential decree. They are designed and implemented with the involvement of the executive and the legislative branches.*

The Federal Executive (*Ejecutivo Federal*) is authorised, via the Ministry of Finance and Public Credit (SHCP), to introduce tax incentives by presidential decree. These incentives constitute a significant proportion of the tax expenditures and are designed to address temporary situations or promote particular economic activities. At the same time, the Legislative Power (*Poder Legislativo*) plays a part in the definition of permanent tax treatments by means of approving tax legislation and the annual economic package (*Paquete Económico*). Other institutions with a key role in this process include the Center for Public Finance Studies (CEFP)<sup>1</sup>, which conducts technical analyses of revenue and public expenditure, and Mexico's supreme audit institution (*Auditoría Superior de la Federación* – ASF), which monitors regulatory compliance and assesses aspects of public resource efficiency.

The tax expenditures document is published regularly, as stipulated in Article 26 of the Federal Revenue Act (*Ley de Ingresos de la Federación* – LIF). This document provides an estimate of the revenue foregone by the federal government as a result of preferential tax treatments, grouping the information into five categories: two for direct taxes (natural persons and legal entities), two for indirect taxes (VAT and Special Tax on Production and Services (IEPS)) and one for tax incentives. Each provision is reported for the current and the following year in a document broken down into four sections: I) Introduction, II) Function, definition and methodology of the tax expenditures, III) Results, and IV) Description of the concepts and legal basis. For each provision, tax expenditure

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<sup>1</sup> The CEFP is an institution of the Legislative Power. One of its roles is to conduct legislative research into budgetary topics for members of the Congress of the Union.

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is estimated for the reporting year and the following year. Employing time series analysis enables the creation of one's own database in which estimates are aggregated for each year.<sup>2</sup>

A significant proportion of tax incentive measures are established by presidential decree (Table 1). Presidential authority to issue decrees is anchored in Article 71 of the Political Constitution of the United Mexican States (commonly referred to as the Mexican Constitution). Presidential decrees must be published in the Official Gazette of the Federation (*Diario Oficial de la Federación* – DOF), Mexico's main official government publication, and be signed by the relevant Secretary of State, in accordance with Article 92 of the Mexican Constitution. The nature and duration of presidential decrees can vary. Some are temporary and others permanent, depending on their purpose and legal basis.

**Table 1. Classification of Presidential Decrees in Mexico**

| Category                                   | Description  |
|--|--|
| <b>Administrative or executive decrees</b> | Decisions that are translated into administrative acts, such as the creation of decentralised agencies.  |
| <b>Legislative or delegated decrees</b>    | Confer upon the President legislative powers to issue decrees or participate in the legislative process. Can be subdivided into several categories, including decrees issued on the grounds of necessity or emergency and decrees in the health or commercial sectors. |
| <b>Non-delegated decrees</b>               | Do not require legislative authorisation and are linked to the Mexican Constitution in terms of purpose, incorporation or divestiture of public property, and expropriation.   |
| <b>Collaborative legislative decrees</b>   | Include initiative and veto decrees.   |

Source: own compilation, based on Martínez, R. (2021).

Recent examples of tax decrees include the tax incentive for motor vehicle fuel (1.1% of GDP in 2022 and 0.07% of GDP in 2024) (SHCP, 2022; SHCP, 2024) and the incentive for the relocation of companies in Mexico (0.01% of GDP in 2024), both of which illustrate the use of decrees to introduce fiscal measures during the current tax year. Article 25 of the Federal Revenue Act (LIF) stipulates that tax incentives must be assessed in relation to any direct expenditure policies pursuing the same objectives. Additionally, the tax expenditures document must be shared with the Legislative Power and the CEFPP and made available to the general public ahead of the debate on the annual economic package.

In 2018, Mexico's supreme audit institution (the ASF) conducted a performance audit of the tax expenditures budget (the *Presupuesto de Gastos Fiscales*, which has since been renamed the *Presupuesto Renuncias Recaudatorias*). This analysis identified the regulatory framework for the document, the actors responsible for its creation and the degree to which it complied with applicable legislation, and proposed areas for improvement. The ASF identified the Ministry of Finance and Public Credit (SHCP), via the administrative unit running the budgetary programme entitled 'Revenue policy design' (*Diseño de la Política de Ingresos*), as the authority responsible for drafting the document. At the same time, the ASF proposed that indicators for tax expenditures be integrated into the relevant budgetary programme. Reference was also made to the fact that it may not be possible to capture the total effect of the measures within one tax year given the time lag between publication of presidential decrees and the drafting of the document.

<sup>2</sup> Official documents only contain information for the year of publication and the following year. As such, there is no official source of open data that presents all the information in aggregated form.

# 46.1/100

The overall GTETI score



## Tax expenditures transparency

The quality and scope of TE reporting in Mexico is reflected in the GTETI where it ranks 51st out of 105 assessed countries.



8/20

### Dimension 1 – Public Availability

This dimension captures the extent to which TE reports are made available to the general public. It considers the regularity of reporting, the timeliness of data, the online accessibility, and the reader-friendliness of the document.



8/20

### Dimension 2 – Institutional Framework

This dimension evaluates how well the institutional framework promotes transparency and accountability in TE policy-making. It assesses the legal basis for TE reporting, the requirement to submit reports to Parliament, the assignment of the responsibility to report to a specific public authority, and the consideration of TEs in the country's budget cycle and medium-term strategy.



11.7/20

### Dimension 3 – Methodology and Scope

This dimension analyses the extent to which TE reports cover all TEs applied at the national level, the level of specification of the reference benchmark system against which TEs are assessed, and the method(s) used to calculate revenue foregone.



10/20

### Dimension 4 – Descriptive TE Data

This dimension assesses the information available in the report to identify and explain the nature of different TEs. It evaluates the extent to which the report specifies the policy objective(s) of TEs. Also, it analyses the availability of TE data with regard to the type of TE (tax credit, deduction etc.), beneficiaries, time frames, and the legal basis under which TEs are granted.



8.4/20

### Dimension 5 – TE Assessments

This dimension analyses the extent to which revenue foregone estimates are provided in the report, including levels of (dis)aggregation choices, and the time span of revenue foregone estimates (previous years and forecasts). Further, it assesses the availability of information on TE evaluations, considering both the existence of ex-ante and ex-post evaluation frameworks, and the scope of publicly available evaluations.



### Transparency

Mexico occupies 51st place in the GTETI ranking (Redonda et al., 2024). One of the areas identified for improvement in terms of methodology concerns the lack of clarity and consistency in defining the benchmark. This limits the inclusion of certain measures that could be considered tax expenditures if broader or more internationally comparable definitions were adopted. For example, the Fiscal Incorporation Regime (RIF), which grants reduced rates, was considered a tax expenditure, yet its replacement, the Simplified Trust Regime (RESICO), which also offers preferential rates of between 1.0% and 2.5%, was not. This points not only to a potential lack of provisions in official estimates, but also to an absence of technical explanations to justify the exclusion of certain measures.

While the 2024 tax expenditures document does meet the requirements for reporting the total amount, methodology, legal basis and beneficiary sectors or activities, analysis of the economic and social effects of the tax expenditures is still limited. In this context, the ASF considers that the *sectoral and incidence analysis* section of the document makes a partial contribution to identifying these effects by providing evidence pertaining to the distribution of tax expenditures by economic sector and income level. Nonetheless, this analysis does not constitute a comprehensive assessment of the impact of the tax expenditures, nor does it permit evaluation of whether each measure meets its public policy objectives.

In the same vein, the recent update to the GTETI has recognised the incorporation of the incidence analysis under the ‘TE Assessments’ dimension, which has contributed to Mexico’s improvement in this dimension. Notwithstanding, it is important to point out that this analysis does not equate to a cost-benefit analysis (or other type of impact analysis) that would permit assessment of the effectiveness of each differential treatment. Its focus is limited to showing the distribution of tax expenditures across different economic sectors and taxpayer groups. While it represents progress in terms of transparency, there is still room to extend its scope by employing more robust methodologies that would enable a more comprehensive assessment.

Finally, Section IV of the document identifies the regulatory framework applicable to the tax expenditures, along with the sources of information used for their estimation. It should be noted that some information sources are public (surveys, public reports, etc.), while others are private for reasons of privacy and security (tax data from the Tax Administration Service (Servicio de Administración Tributaria – SAT)). Furthermore, the document clarifies that certain reduced rates are not considered to be tax expenditures. This applies, for example, to the 0% VAT rate on exports, which, as a generally and automatically applicable provision, is not classified as a tax expenditure (SHCP, 2024b).

### Limitations of the document

Two methodological characteristics were identified that are relevant to the public debate. First, because the estimates do not take account of changes in economic behaviour in response to changes in tax policy, it is not sufficient to assume that eliminating a particular administrative benefit or differential treatment will yield the revenue presented in the document. As such, despite serving an illustrative purpose, the total tax expenditure amount is not technically correct (SHCP, 2024b). However, this limitation is acknowledged in the document itself.

Second, the methodology establishes a tax expenditure as a deviation from the norm, which means that some special regimes could be considered the norm and thus not classified as tax expenditures (see “RIF and RESICO” section below). While this characteristic is intrinsic to the methodology, it should not be excluded from public



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debate, as it is possible to employ regulatory strategies to reduce the tax expenditures budget without considering the impact this will have on revenue or on efficiency in the achievement of the objectives.

The incidence analysis within the 2024 tax expenditures document seeks to estimate the impact of these fiscal measures on different economic sectors and taxpayer groups by breaking down the distribution of the expenditures by tax type and income level. It draws on data from the National Household Income and Expenditure Survey (*Encuesta Nacional de Ingresos y Gastos de los Hogares (ENIGH)*) 2022, making it possible to estimate the distributive impact of these measures on households by income level. However, given that ENIGH 2022 does not reflect recent changes in the economic landscape, estimates may differ from reality, affecting the accuracy of the analysis.

While this analysis represents significant progress in terms of understanding the distribution of tax expenditures in Mexico, there is still room for improvement when it comes to its quality. Updating the methodologies used and incorporating newer data and more dynamic models would permit more precise and useful analysis for designing more equitable and efficient tax policies.



@Image by Freepik

## Benchmark and revenue foregone

*Tax expenditure provisions are defined as tax treatments that deviate from the normal tax structure and generate lower revenue or no revenue as a direct result. These amounts are measured based on the understanding that no account is taken of changes in economic behaviour in response to modifications to tax policy. This does not imply that this total amount would be collected if the treatment in question did not exist, as the behaviour of the economic agents could vary. Additionally, the totals are presented as a proportion of the size of the economy (% GDP) (SHCP, 2024b).*

A restructuring of tax expenditures has been observed since they were first published<sup>3</sup>. The following points are worthy of particular mention:

- The largest volumes of tax expenditures pertain to indirect taxes, especially the application of the 0% rate to food products.
- For 2024, tax expenditures associated with direct taxes (income tax system) exceed those derived from temporary tax incentives issued by presidential decree. This contrasts with the situation observed in 2023, when total tax expenditures were higher due to the tax incentive offered on motor vehicle fuel. These incentives were issued under the Special Tax on Production and Services (IEPS) in response to the geopolitical situation resulting from the Russia-Ukraine conflict.
- It is important to note that tax incentives issued by decree can apply to indirect and direct taxes alike. The main difference is found in their temporal nature and in the instrument used to establish them, unlike permanent tax expenditures, which are prescribed in legislation.
- Finally, a downward trend was observed in tax expenditures applicable to direct taxes between 2005 and 2010.

In 2008, tax expenditures reached a record 6.0% of GDP, primarily due to the impact of the negative rate on fuels observed during that year.

**Table 2. Fiscal structure of tax expenditures, 2024**

| Category                      | No. of provisions | MXN million      | USD million   | % GDP      | % tax revenue | % tax expenditure |
|-------------------------------|-------------------|------------------|---------------|------------|---------------|-------------------|
| Direct taxes                  | 62                | 450,264          | 22,921        | 1.3        | 6.1           | 31.7              |
| Indirect taxes                | 16                | 630,617          | 32,102        | 1.9        | 8.6           | 44.4              |
| <b>Total: tax legislation</b> | <b>78</b>         | <b>1,080.881</b> | <b>55,023</b> | <b>3.2</b> | <b>14.7</b>   | <b>76.1</b>       |
| Tax incentives                | 47                | 338,621          | 17,238        | 1.0        | 4.6           | 23.9              |
| <b>Total: tax expenditure</b> | <b>125</b>        | <b>1,419.502</b> | <b>72,261</b> | <b>4.2</b> | <b>19.4</b>   |                   |

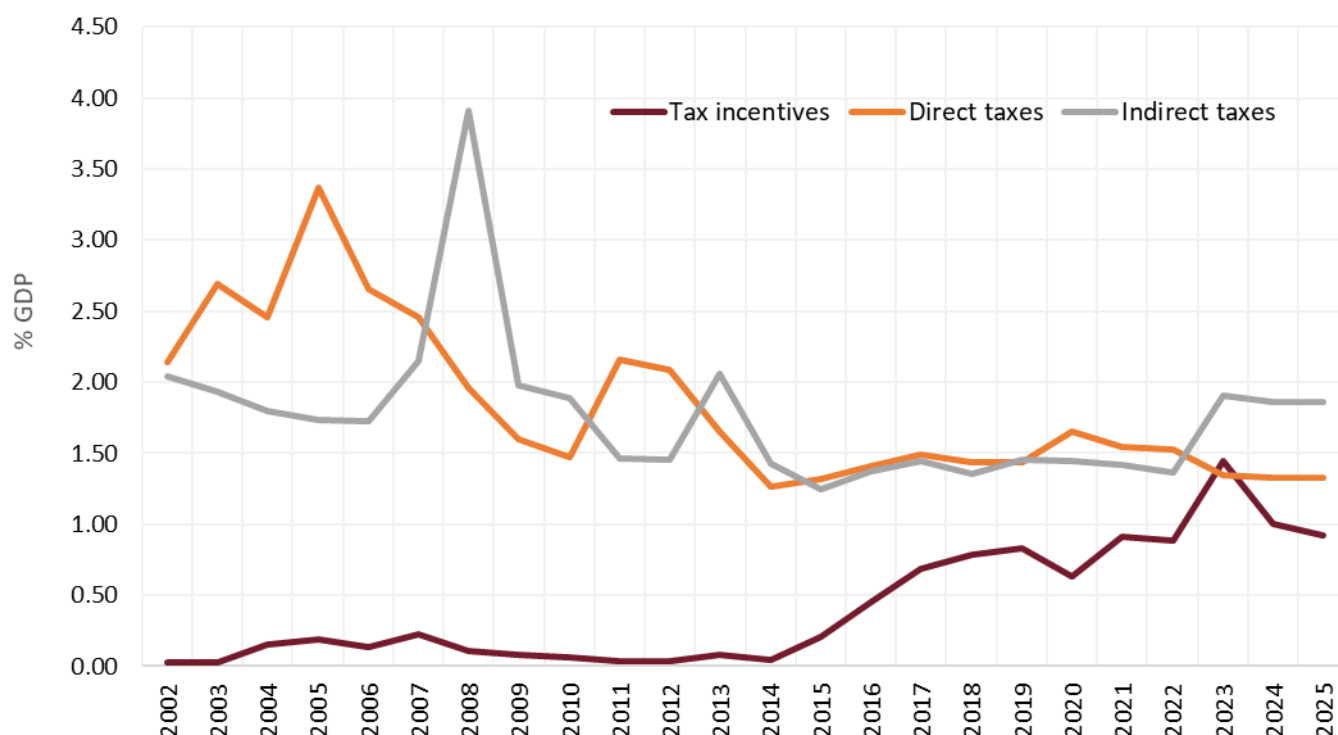
Source: SHCP (2024), Banco de México (Banxico) (2024).

Note: \*Based on an exchange rate of MXN 19.6440 to USD 1, as at 2 October 2024. \*\* Budgetary revenues correspond to the scheduled total in the LIF 2024.

<sup>3</sup> First published in 2002.

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**Figure 1. Trend in tax expenditures**



Source: own compilation, based on SHCP (2020; 2022; 2024b).

125 provisions classified as tax expenditures were reported for 2024, with an estimated total value of MXN 1.42 trillion or 4.2% of GDP (Table 2). It should be noted that this total is equivalent to 19.4% of the tax revenue approved in the LIF for 2024. The tax expenditures consist primarily of indirect taxes, including the 0% reduced rate of VAT on food and medicines. Next come direct taxes and, finally, tax incentives.

Tax incentives accounted for 23.9% of total tax expenditures and were issued primarily in response to presidential decrees which, since they generally relate to temporary situations, tend to lack monitoring and evaluation processes (CEPAL, 2019).

It should be noted that 75% of total tax expenditures in 2024 come from the 10 most relevant provisions: three from VAT, three from tax incentives, two from personal income tax (PIT) and two from corporate income tax (CIT).

### The 10 provisions with greatest revenue foregone

Table 3 presents the 10 main tax expenditure provisions in order of revenue foregone. Each provision listed in the table is analysed in greater detail below.

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**Table 3. Provisions incurring greatest tax expenditure**

| Tax            | Description   | % GDP 2024 | % tax expenditures 2024 |
|----------------|---|------------|-------------------------|
| VAT            | 0% rate on food products  | 1.3        | 31.8                    |
| PIT            | Income-based exemptions   | 0.7        | 16.6                    |
| Tax incentives | Tax incentives in the Fronteriza Norte region   | 0.4        | 9.0                     |
| Tax incentives | Special Tax on Production and Services (IEPS) applicable to motor vehicle fuel  | 0.3        | 6.6                     |
| VAT            | Exemption for teaching services   | 0.1        | 3.4                     |
| VAT            | 0% rate on medicines  | 0.1        | 2.7                     |
| Tax incentives | For creators of real estate investment trusts primarily intended for the construction and purchase of real estate (FIBRAS) who transfer real estate to those trusts, enabling them to defer their tax payments* | 0.1        | 2.6                     |
| CIT            | Employment subsidy  | 0.1        | 2.3                     |
| PIT            | Other income exemptions   | 0.1        | 2.1                     |
| CIT            | Deduction on motor vehicle purchases  | 0.1        | 1.8                     |
| Total          |   | 3.1        | 75.0                    |

Source: own compilation, based on SHCP (2024b).

Note: \* This incentive applies to income tax and enables payment of tax generated by the sale of the asset to be deferred until the sale of the trust certificates or the transferred real estate.

**0% rate on food and medicines:** the reduction of the VAT rate on food to 0% is the most important tax expenditure, accounting for 31.8% of total expenditure, while medicines account for 2.7%.

**PIT exemption based on income:** includes incomes from retirement and other pensions, social service benefits, savings banks and funds and other income tax-exempted income related to employment. It accounted for 16.6% of total tax expenditure in 2024, making it the largest provision after the 0% rate on food products.

**VAT exemption for teaching services:** unlike food and medicines, personal expenditure on teaching services is VAT exempted. It accounted for 3.4% of tax expenditure in 2024.

**Tax incentive in the Fronteriza Norte region:** this incentive is designed to strengthen the regional economy, counteracting the negative impact of violence and organised crime. To this end, 50% tax credits are applied on VAT and on one third of income tax levied on the region's revenue. It accounted for 9.0% of total tax expenditure for 2024.

**Tax incentive on motor vehicle fuel:** this tax incentive is implemented via the Special Tax on Production and Services (IEPS) applicable to motor vehicle fuel and accounted for 0.02% of total<sup>4</sup> tax expenditure in 2024. This is due to a greater accreditation of IEPS owing to a reduction in the price of petroleum and fuel globally. However, this expenditure does not take account of the fact that the presidential decree made it possible to establish a

<sup>4</sup> Unlike in 2022, when the IEPS tax incentives applicable to motor vehicle fuel equated to approximately 18.8% of total tax expenditure.

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potential credit balance in the payment of IEPS relative to other taxes such as VAT and IEPS, which means that the total impact on revenue is unknown.

**VAT exemption for teaching services:** unlike food and medicine, personal expenditure on teaching services is VAT exempted. It accounted for 3.4% of tax expenditure in 2024.

**Tax incentive for FIBRAS:** deferral of VAT payment on revenue generated from the transfer of real estate to investment trusts primarily intended for the construction and purchase of real estate (FIBRAS). While this incentive has already been abolished, it still has an impact on tax expenditure. It accounted for 2.6% of total tax expenditure for 2024.

**Employment subsidy (CIT):** a justified tax expenditure if the total subsidy provided per worker is greater than the tax incurred by the same income. This phenomenon is observable for low incomes, for which there tends to be an increased labour supply. This subsidy was designed to improve wage levels for low-income families. However, it has been observed that the elasticity in labour supply has translated into lower payroll costs for companies. The employment subsidy accounted for 2.3% of total tax expenditure in 2024.

**Other PIT-exempted incomes:** the main income tax-exempted incomes not related to wages are the interest generated by the investment funds managing individual retirement accounts with defined contributions (known as SIEFORES in Mexico) and the income from the sale of real estate for residence purposes (*casa-habitación*). These PIT-exempted incomes accounted for 2.1% of tax expenditure in 2024.

**CIT deduction on motor vehicle purchases:** expenditure on motor vehicle purchases can be deducted in the case of internal combustion vehicles worth less than MXN 175,000 and battery-driven, electric, hybrid or hydrogen-powered vehicles. This provision accounted for 1.8% of total tax expenditure in 2024.

### Tax expenditure by tax type

#### *Corporate income tax (CIT)*

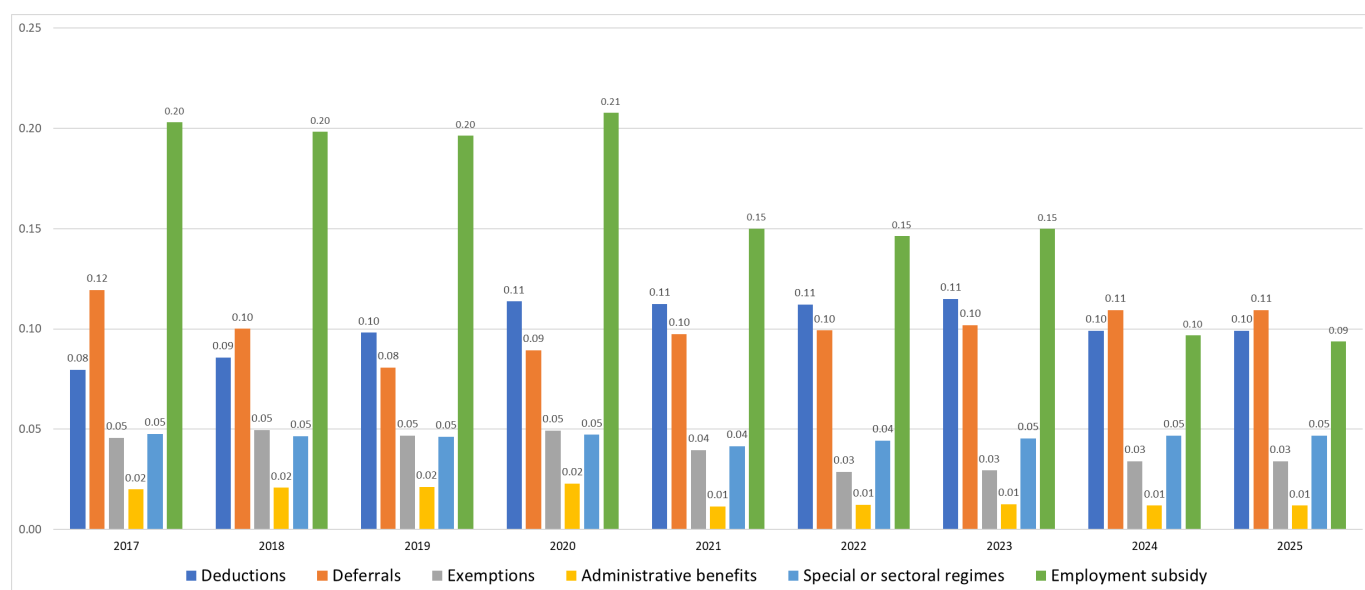
Analysis of tax expenditure on corporate income tax (CIT, known in Mexico as *Impuesto sobre la renta empresarial*) in Mexico is based on a structure in which companies pay tax on their total net revenue, which is defined as the difference between revenue and costs strictly necessary for generating a profit. Within such an ideal structure, there would be no exemptions, special deductions, sectoral regimes or tax incentives that alter the tax liability or the effective tax rate. However, the applicable legislation allows for different preferential treatments, such as accelerated deductions, differentiated tax regimes for specific sectors (agricultural, maquiladora, etc.) and tax incentives (such as the employment subsidy). These systems modify the effective tax burden and can create economic distortions that benefit particular sectors or activities to the detriment of tax neutrality.

Tax expenditures on CIT were estimated at 0.40% of GDP for 2024. The main expenditure is on the employment subsidy, which equates to MXN 32,841,000,000 (0.1% of GDP), and deductions<sup>5</sup> (0.09% GDP), which increased by 0.02 percentage points of GDP between 2017 and 2024.

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<sup>5</sup>These comprise motor vehicle purchases, non-onerous and non-remunerative donations to authorised recipients, car leasing, restaurant expenditure, purchases of conventional bicycles and rechargeable electric battery-powered bicycles and motorcycles, and an additional deduction for employment of workers 65 years old and above and with disabilities (SHCP, 2024b).



**Figure 2. Tax expenditure on CIT**

Source: own compilation, based on SHCP (2020; 2022; 2024b)

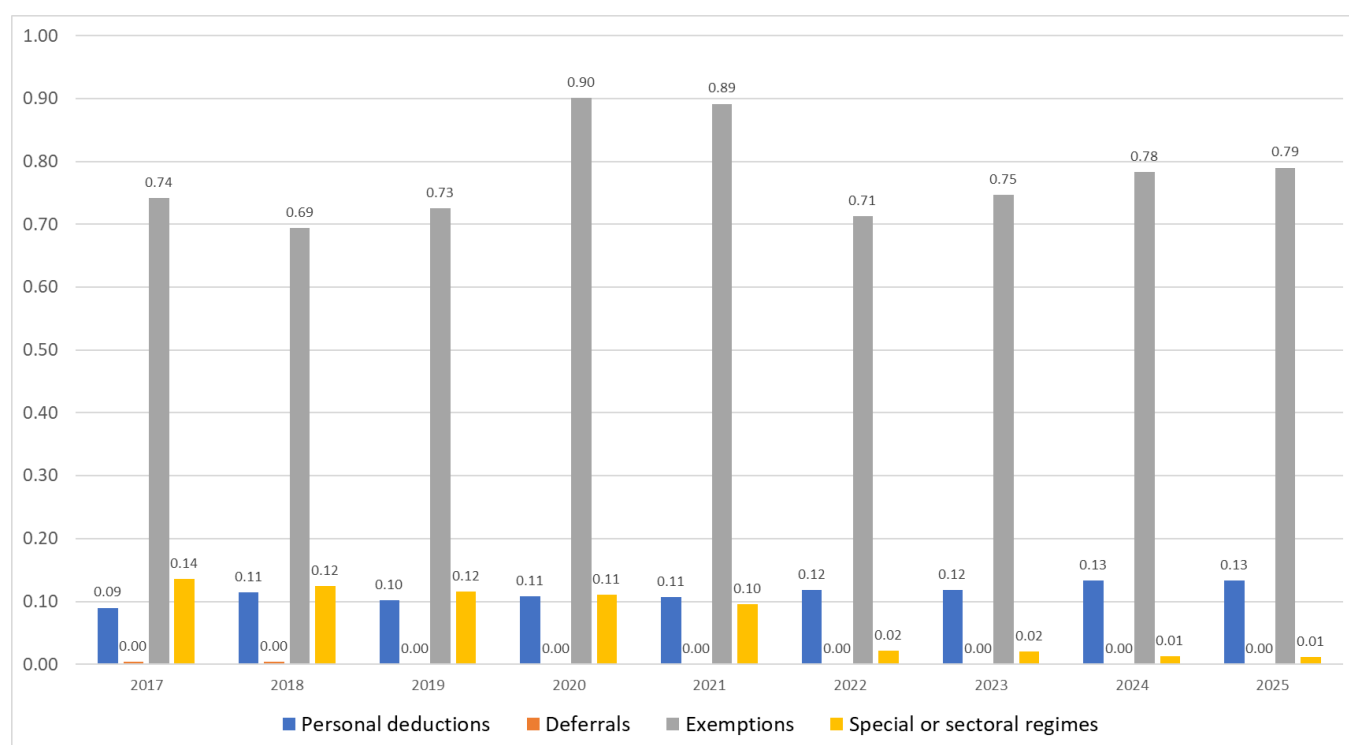
### Personal income tax (PIT)

Analysis of tax expenditure on personal income tax (PIT, known in Mexico as *Impuesto sobre la Renta de Personas Físicas*) is based on a system in which all natural persons pay tax on their overall income within a progressive marginal rate structure. In its most pure form, this tax would be applied without deductions, exemptions or differentiated treatments, meaning that all incomes would be subject to a uniform application, proportional to the economic capacity of the taxpayer in question. In practice, however, PIT includes a series of personal deductions, exemptions and special regimes, such as the Fiscal Incorporation Regime (RIF) and the exemptions for certain employment income and pensions. These provisions reduce the tax base and generate tax expenditures, affecting the progressivity of the tax system and the distribution of the tax burden among different segments of the population.

For PIT, the main tax expenditures are estimated to account for 0.94% of GDP, compared with 0.97% in 2017 and 0.88% in 2023. These tax expenditures are concentrated around income tax-exempted incomes (0.78% of GDP). At the same time, there has been an observable reduction in tax expenditures associated with special regimes due to the replacement of RIF and other regimes with RESICO for natural persons.

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**Figure 3. Tax expenditure on PIT**



Source: own compilation, based on SHCP (2020; 2022; 2024b).

**Incidence:** most PIT exemptions are focused on higher-income families (Table 4). Income exemptions with a greater concentration of benefits are employers' social security contributions (CSS), medical, dental and hospital expense reimbursements, and severance payments.

**Table 4. Incidence of PIT-exempted incomes**

| Distribution by income decile of income-based exemptions during the 2024 tax year |                         |                     |                              |              |                    |                |                |   |  |              |  |                                   |
|---|-------------------------|---------------------|------------------------------|--------------|--------------------|----------------|----------------|---|--|--------------|--|-----------------------------------|
| Decile  | Social service benefits | Other earned income | From savings banks and funds | Annual bonus | Severance payments | Overtime hours | Vacation bonus | Employer participation in company units | Employers' social security contributions | Sunday bonus | Reimbursement of medical, dental and hospital expenses | Reimbursement of funeral expenses |
| I   | 0.1                     | 0.1                 | 0.1                          | 0.4          | 0.1                | 0.1            | 0.5            | 6.3                                     | 0.1                                      | 0.2          | 0.1  | 0.2                               |
| II  | 0.3                     | 0.2                 | 0.1                          | 0.9          | 0.2                | 0.2            | 0.8            | 4.0                                     | 0.1                                      | 0.7          | 0.1  | 0.5                               |
| III   | 0.6                     | 0.4                 | 0.3                          | 2.4          | 0.4                | 0.7            | 1.7            | 3.6                                     | 0.1                                      | 1.9          | 0.3  | 0.9                               |
| IV  | 0.9                     | 0.8                 | 0.4                          | 8.1          | 0.6                | 1.2            | 3.9            | 4.6                                     | 0.3                                      | 5.0          | 0.5  | 1.4                               |
| V   | 3.6                     | 2.3                 | 1.6                          | 10.8         | 1.5                | 4.1            | 6.8            | 9.2                                     | 0.7                                      | 11.3         | 1.5  | 3.5                               |
| VI  | 8.3                     | 5.1                 | 4.6                          | 13.4         | 2.9                | 9.4            | 10.3           | 13.0                                    | 1.7                                      | 17.0         | 3.1  | 11.5                              |
| VII   | 14.1                    | 10.1                | 10.4                         | 15.6         | 5.5                | 17.2           | 15.3           | 16.8                                    | 4.7                                      | 19.4         | 6.6  | 16.0                              |
| VIII  | 18.5                    | 18.5                | 15.2                         | 16.7         | 9.1                | 25.0           | 19.7           | 15.9                                    | 11.4                                     | 17.9         | 10.1   | 19.5                              |
| IX  | 21.7                    | 25.5                | 22.1                         | 17.4         | 16.7               | 27.4           | 21.7           | 13.8                                    | 23.6                                     | 16.3         | 12.8   | 20.2                              |
| X   | 32.0                    | 37.0                | 45.2                         | 14.4         | 63.0               | 14.8           | 19.3           | 12.9                                    | 57.5                                     | 10.3         | 65.0   | 26.5                              |
| Total   | 100.0                   | 100.0               | 100.0                        | 100.0        | 100.0              | 100.0          | 100.0          | 100.0                                   | 100.0                                    | 100.0        | 100.0  | 100.0                             |

Source: own compilation, based on SHCP (2024b).

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### *RIF and RESICO for natural persons*

One of the inherent limitations of the analysis is that, because it measures deviations from the norm, it omits the impact on norms with lower rates than a normal structure within the income system. One example in the Mexican context is the replacement of RIF by RESICO. Both regimes sought to simplify the tax process and strengthen the taxpayer base, but with different benefits.

RIF offered tax credits on income tax, starting with 100% in the first year and a 10% reduction until loss of the benefit over a 10-year period, in addition to VAT benefits (Congreso de la Unión, 2014). RESICO requires taxpayers to pay between 1% and 2.5% on total income, without the right to make deductions (Congreso de la Unión, 2021). For RIF, tax credits represented a tax expenditure, while for RESICO, they do not. In other words, RIF was considered a tax expenditure due to being a reduced rate on the regular income tax structure. RESICO, on the other hand, is a regime with lower rates stipulated in law, which means it is not a deviation from the norm and thus is not considered a tax expenditure.

After having 1.05 million taxpayers at year end 2022, RIF had just 958,656 taxpayers in 2023 and a mere 618,117 for 2024<sup>6</sup>. At the same time, RESICO has registered 3.46 million taxpayers in total over the last three years after registering just 2.98 million in 2023. In the last year, RESICO has registered a 16.2% growth rate in registrations, while RIF has seen a 35.5% drop.<sup>7</sup>

In terms of revenue, RESICO collected 5.5% more in its first year of operation than RIF did at its peak. It should be noted that RESICO also absorbed other special regimes such as agricultural products, leaseholders, etc. The difference of taxpayer and revenue results casts doubt on how special regimes impact the population and how they can meet objectives for taxpayer incorporation and federal revenue.

As such, the difference between regimes is one area that is not currently assessed. It does, however, lead to a reduction in tax expenditure on RIF, as the reduced rates under RESICO are not considered to be deviations from the norm. Assessments or more disaggregated data concerning taxpayers and their contributions are required to measure the efficiency and impact of these benefits.

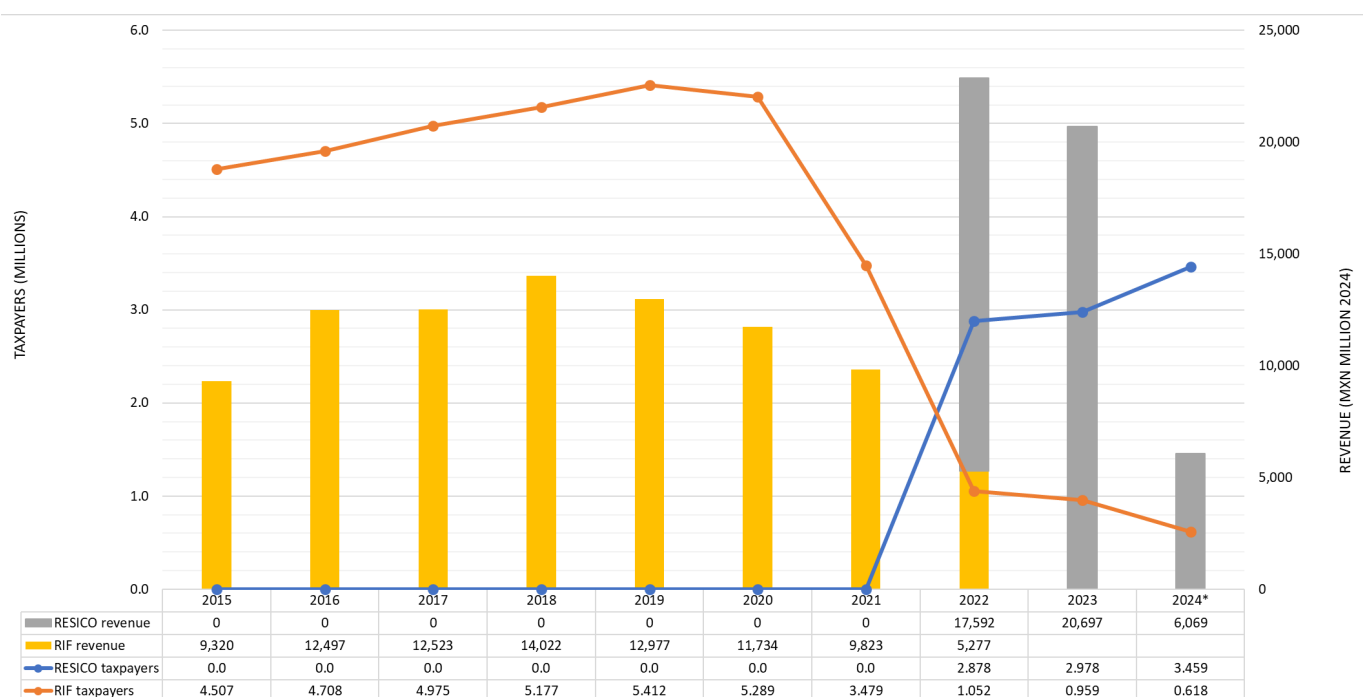
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<sup>6</sup> While the Fiscal Incorporation Regime (RIF) was replaced as a registration system by the Simplified Trust Regime (RESICO) in 2022, the gradual transition process means that there are still active taxpayers within RIF. It is not possible for new taxpayers to register with RIF, but those already in the system can remain within it until they have used up the established benefits or until they decide to migrate. Consequently, taxpayers were still registered under RIF in 2023 and 2024, even though the corresponding revenue has not been updated or reported in the same detail in the most recent documents. This transition phase explains the sustained reduction in registrations, along with the apparent lack of revenue data in several reports.

<sup>7</sup> Data up to August 2024.

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**Figure 4. Revenue and taxpayers within RIF and RESICO**



Source: own compilation, based on SAT (2024<sup>a</sup>; 2024b)

Note: \*Data up to August 2024. While the Fiscal Incorporation Regime (RIF) was replaced by the Simplified Trust Regime (RESICO) in 2022 for new registrations, the gradual transition process means that there are still some active taxpayers within RIF. For this reason, data is still reported for RIF in past years, though this does not always include disaggregated information on revenue collection.

### *Value added tax (VAT)<sup>8</sup>*

In its most neutral configuration, the benchmark for value added tax (VAT) in Mexico would be based on the application of a single rate to the consumption of all goods and services, with no distinction made between essential and non-essential products and no exemption or reduced-rate treatments. This model would make it possible to record the total added value within the economy, guaranteeing efficient tax collection and minimising distortions in consumption patterns. Nevertheless, Mexican legislation provides for a 0% rate on certain goods (such as food and medicines) and exemptions for specific services (such as education and housing), which generates significant tax expenditures and affects tax revenue. While these treatments are designed to reduce the fiscal impact on low-income households, a number of studies have indicated that the benefits are also concentrated in higher-income deciles, given the greater purchasing power of those deciles.

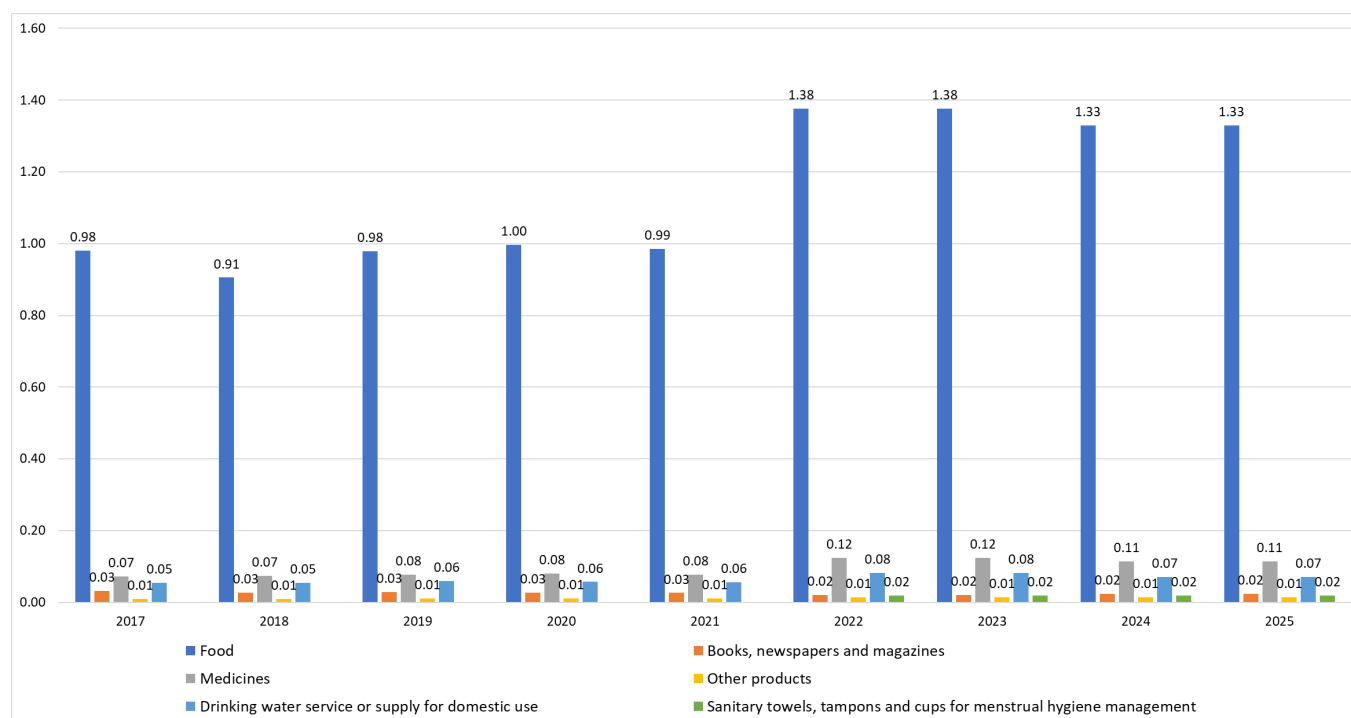
The higher tax expenditures are those linked to VAT (1.82% of GDP), primarily the 0% rate on various goods and services (1.33% of GDP). In terms of progression, tax expenditures associated with VAT grew by 0.30 percentage points of GDP between 2017 and 2024.

<sup>8</sup> Does not include exports.

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**Incidence:** unlike in 2022, in 2024 the fiscal transfer to exemptions and reduced rates was used in a similar way by households with different income levels, namely for exemption provisions for teaching services, housing and medical services. However, relative to household income or expenditure, the incidence of tax expenditures tends to benefit lower-income deciles to a greater extent (CIEP, 2023). This is due primarily to a disparity in purchasing power, as higher-income families tend to spend more money on food, yet food accounts for a greater proportion of income/expenditure among lower-income families. An example of the former is the 0% VAT rate on food, a fiscal transfer that is greater for households in decile I.

**Figure 5. Tax expenditure on 0% VAT rate**



Source: own compilation, based on SHCP (2020; 2022; 2024b).

### Special taxes (IEPS and ISAN)

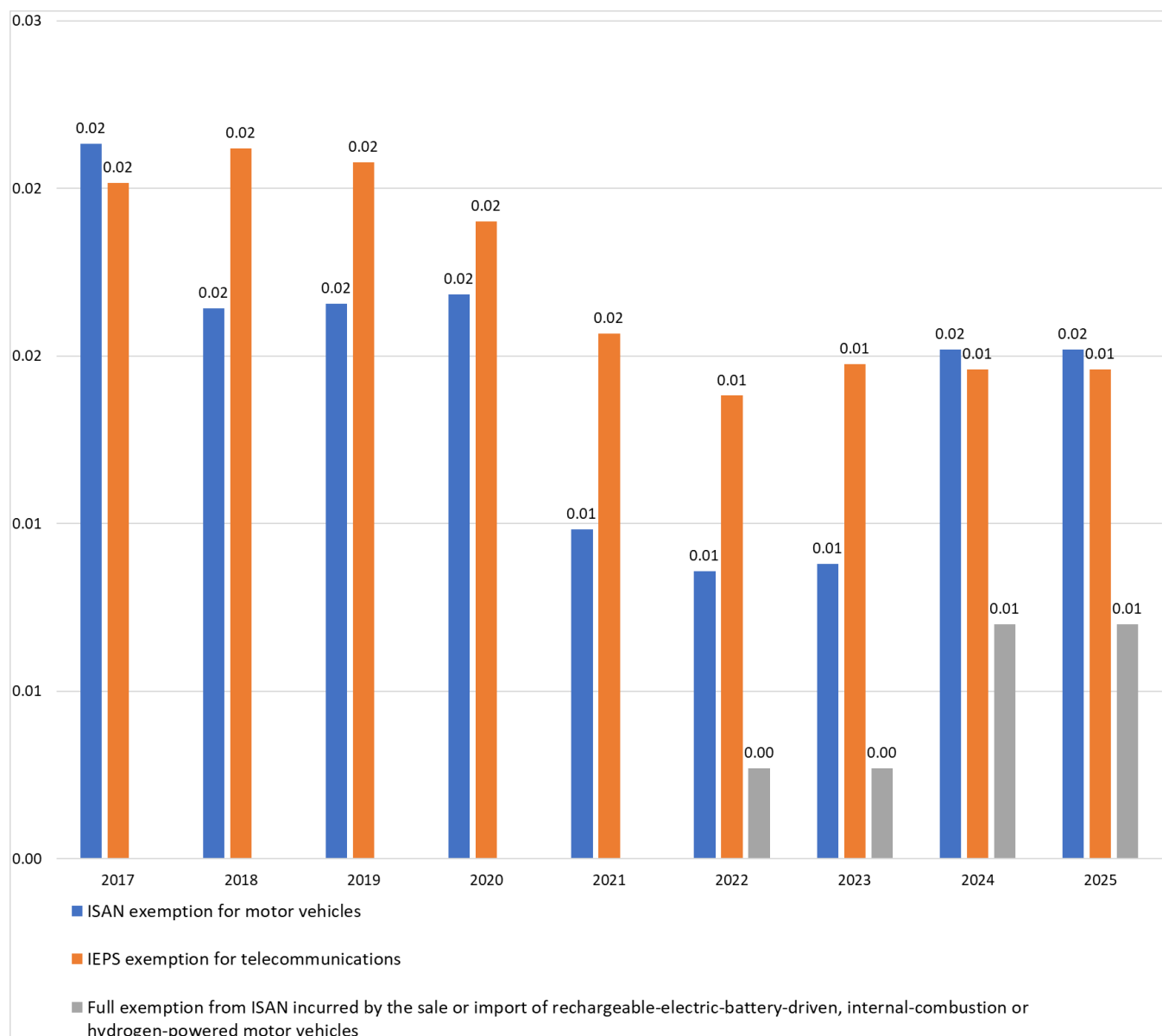
The Special Tax on Production and Services (IEPS) and the Tax on New Motor Vehicles (ISAN) operate on the principle of internalising negative externalities, for which they tax the consumption of goods and services that have an adverse impact on public health, the environment and mobility. Under a reference system, these taxes must be applied consistently to all products within each category, regardless of rate or exemption, to ensure that they reflect the social costs associated with their consumption. In practice, however, IEPS in Mexico presents differentiated rates based on the type of fuel, sweetened products and alcoholic beverages, along with exemptions for telecommunications and tax incentives for certain sectors (for example, reimbursement of IEPS on diesel for transport companies and farmers). In the case of ISAN, value thresholds are established for determining how the tax should be applied. This generates tax expenditures associated with low-priced vehicles and exemptions for electric vehicles. These treatments create incentives that could modify consumption patterns, reducing the revenue collection effect and the efficacy of these taxes as public policy instruments.



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The lowest concentration of tax expenditures pertains to special taxes (0.04% of GDP). The main expenditures relate to exemptions to the Tax on New Motor Vehicles (ISAN), based on their value and whether they are powered by non-gasoline energy sources, and to the IEPS-exemption for telecommunications involving public internet services.

**Figure 6. Tax expenditure on special taxes**



Source: own compilation, based on SHCP (2020; 2022; 2024b).

### Tax incentives

Tax incentives may not be required within a neutral tax structure that is applied consistently to all taxpayers. Nonetheless, in Mexico, tax incentives have been used as tools to incentivise economically strategic activities, correct market failures and promote investment in specific regions. The main incentives include tax credits in the Fronteriza Norte y Sur region, the immediate deduction of renewable energy investments, the accreditation

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of IEPS to diesel for specific sectors and tax incentives for export manufacturing, film production and scientific research. While these incentives can have a positive impact on economic growth and employment creation, they also reduce public revenue and, in some cases, they have not undergone comprehensive assessment in relation to their effectiveness in meeting public policy objectives.

Tax expenditures on tax incentives reached their peak of 1.64% in 2022. This was due principally to growth in tax incentives, issued by presidential decree, for the sale of gasoline, which were intended to mitigate the inflationary effects on fuel observed globally. These incentives equated to 0.92% of GDP for 2024.

**Temporary omissions:** 2 September 2024 saw the approval of tax incentives for the use of electronic payment methods to encourage the use of bank cards and improve the country's payment infrastructure. These incentives involve crediting against income tax, whether one's own or withholdings made to third parties, the amount corresponding to the costs levied by those entities, by the federal government. This is done for particular financial institutions than can identify the cardholder and comply with the relevant regulations. Given that the tax expenditure report was published on 28 June 2024, the deductions for this incentive are not available in the document.

### Evaluation

*Given the relevance of tax expenditures (4.2% of GDP) and their concentration within the 10 main provisions representing 75% of total tax expenditure, it is fundamental to include in public debate assessment processes that evaluate compliance with the objectives of the provisions and tax incentives.*

Assessment of tax expenditures should revisit the specific objectives of those expenditures. Mexico has gained experience of assessing public expenditure through its budgetary programmes. Nonetheless, this methodology has not been applied to tax expenditures. One option for employing an assessment method is to refer back to the definition in the terms of reference for evaluating the design of the budgetary programmes (*Términos de referencia para la evaluación en materia de diseño de los Programas Presupuestarios*). To this end, the objectives associated with tax expenditures must comply with the stipulations of the performance assessment system (*Sistema de Evaluación de Desempeño*) (Transparencia Presupuestaria, 2023):

- Analyse the public issue or need that justifies the creation of or significant change to the fiscal framework.
- Analyse the relevance of the tax expenditure's design with regard to the public issue or need that it seeks to address.
- Analyse the consistency between the design of the tax expenditure and the applicable regulations.
- Analyse the tax expenditure's contribution to achievement of the objectives of national plans and strategies.
- Identify potential complementarities or similarities, as well as the risk of overlaps with other budgetary programmes or existing tax expenditures.
- Analyse the consistency of the performance assessment instrument (*Instrumento de Seguimiento del Desempeño*) in terms of the tax expenditure's design.
- Include other specific objectives in case they are required.

Once the political objective of each provision has been identified, taking account of the regulatory framework and experience of assessing the budgetary programme, it would be possible to review experiences of tax expenditure monitoring and evaluation and the budgetary programmes for current expenditure. This would enable compliance with the requirements of Article 25 of the LIF, which stipulates that tax incentives must be assessed with regard to a possible expenditure policy that meets the same objectives.

#### Monitoring and evaluation

It is crucial to measure the impact of tax expenditures on revenue collection, the economy and society in general in order to facilitate informed decision-making on tax policy. This would allow comparison of tax measures that goes beyond estimating the total revenue, as in the case of RIF and RESICO, and compensates for the intrinsic limitations in the analysis of each system.

Current analysis of tax expenditures, based on measuring deviation from the taxation benchmark, is limited in its ability to capture total impact. Consequently, it is necessary to consider other assessment methods that permit analysis of the degree to which each measure complies with its specific objectives and of its effect on income distribution and the reduction of inequality.

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To this end, there is a need to adapt the recommendations of the ASF (2019) and the monitoring and evaluation experience of Mexico and implement the stipulations of the National Council for the Evaluation of Social Development Policy (*Consejo Nacional de Evaluación de la Política de Desarrollo Social* – CONEVAL):

- Diagnose the problem and create a matrix of indicators to measure changes that the tax expenditure seeks to bring about.
- Evaluate the design and theory behind the proposed change and, if necessary, improve the indicator matrix.
- Quantify the indicators to assess their consistency and potential results.
- Implement a system for monitoring the indicators that includes impact assessment.

This would permit evaluation of the degree to which the tax expenditures are meeting the objectives for which they were adopted and of their effectiveness. Combined with measurement of tax expenditures, this would allow cost-benefit analyses to be conducted.



## Political economy and reform

*Mexico has taken important steps in recent years towards greater transparency in the treatment of tax expenditures, most notably through regular publication of the tax expenditures document (Documento de Renuncias Recaudatorias), produced by the Ministry of Finance and Public Credit (SHCP). This instrument estimates income losses derived from preferential tax treatments and has made it possible to visualise the magnitude of the expenditures, as well as their high concentration within a few provisions, creating opportunities to advance towards a more efficient tax policy.*

Nonetheless, the country still faces structural limitations when it comes to the assessment, design and reform of these mechanisms. While the current methodological framework is based on identifying deviations from a benchmark system, it does not incorporate ex-ante and ex-post evaluations that would make it possible to determine whether the measures are properly compliant with public policy objectives. Additionally, the lack of a clear and consistent definition of the benchmark has resulted in some preferential treatments, such as the Simplified Trust Regime (RESICO), not being classified as tax expenditures, despite their impact on public revenue. One additional factor complicating the planning and assessment of tax expenditures is the publication of presidential decrees throughout the year. Given the inability to fully predict their number, content and fiscal impact at the time the tax expenditures document is created, there is structural uncertainty concerning the total revenue effectively foregone by the state and this limits transparency and accountability.

In this context, systematic assessment of tax expenditures must become a key component of any future tax reforms, especially where the objective is to increase the progressivity of the tax system without having to raise nominal rates. Raising effective rates by means of revising exemptions, deductions and tax incentives is a strategic approach for reducing inequalities and strengthening tax fairness, both vertically (higher earners pay more) and horizontally (equal earners pay equally). For Mexico, this approach would enable it to boost revenue and improve the efficiency of the system without intensifying distortions or affecting lower-income sectors.



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