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ASSESSING THE IMPACT  
OF THE FISCAL REFORM  
AGENDA FOR MEXICAN  
CIVIL SOCIETY  
ORGANIZATIONS



The International Center for  
Not-for-Profit Law

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## ACRONYMS

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CBO	Community-based organization
Cemefi	Centro Mexicano para la Filantropía (Mexican Center for Philanthropy)
CLUNI	Clave Única de Inscripción (Unique Registration Key or Identification Number)
CSO	Civil society organization
CSR	Corporate Social Responsibility
ENAFI	Encuesta Nacional sobre Filantropía y Sociedad Civil (National Survey of Philanthropy and Civil Society)
FPA	Federal Public Administration
GDP	Gross Domestic Product
GNI	Gross National Income
GoM	Government of Mexico
INDESOL	Instituto Nacional de Desarrollo Social (National Institute for Social Development)
ICNL	International Center for Not-for-Profit Law
IETU	Impuesto Empresarial a Tasa Única (Flat Rate Business Tax)
ITAM	Autonomous Technical Institute of Mexico
JHU	Johns Hopkins University
LISR	Ley del Impuesto sobre de la Renta (Federal Income Tax Law)
LIVA	Ley del Impuesto al Valor Agregado (Law on Value Added Tax)
PAN	Partido Acción Nacional (National Action Party)
PRI	Partido Revolucionario Institucional (Institutional Revolutionary Party)
PILAP	Partners for Improving Laws Affecting Philanthropy
RISR	Reglamento de la Ley del Impuesto Sobre la Renta (Income Tax Law Regulations)
SAT	Servicio de Administración Tributaria (Tax Administration Service)
SEDESOL	Secretaría de Desarrollo Social (Ministry of Social Development)
SHCP	Secretaría de Hacienda y Crédito Público (Ministry of Finance and Public Credit)
VAT	Value-Added Tax

## EXECUTIVE SUMMARY

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In 2010-2011, the International Center for Not-for-Profit Law (ICNL) undertook a study of the fiscal framework governing civil society in Mexico to analyze the impact of recent reforms. The study is part of the Partners for Improving Laws Affecting Philanthropy (PILAP) project funded by the William and Flora Hewlett Foundation. Since 2005, the PILAP project has undertaken activities in Mexico to improve fiscal laws and regulations affecting civil society organizations (CSOs) and their donors and increase capacity among civil society representatives and government officials to work together to create a more enabling environment for civil society. This report provides a snapshot of the current fiscal framework governing CSOs and analyzes the impact of recent reforms. The report also identifies remaining obstacles and recommends steps to improve the fiscal framework further so that it fosters the development of a strong, independent, and financially sustainable civil society sector in Mexico.

The starting point of this report is *Defining a Fiscal Agenda for the Development of Civil Society Organizations in Mexico (Fiscal Agenda)*, a paper prepared in 2007 by a working group of civil society stakeholders, including a number of PILAP grantees.<sup>1</sup> One of the chief findings of the *Fiscal Agenda* was that Mexican CSOs and their donors operate under a legal system that hinders, rather than facilitates, a vibrant sector.

The *Fiscal Agenda* found that complicated laws and expensive bureaucratic procedures prevented many organizations from seeking recognition as legal persons and obtaining public benefit status.<sup>2</sup> Obtaining formal legal status and, in many instances, public benefit status under either the Federal Law for the Promotion of Activities Undertaken by CSOs (Promotion Law) or the Federal Income Tax Law (Ley del Impuesto sobre de la Renta or LISR) are prerequisites for accessing funds from many institutions, such as the government, international aid agencies, and corporate philanthropy programs, as well as other domestic and foreign donor institutions. The *Fiscal Agenda* also demonstrated how the weak relationship among the government, the public, and civil society limited the growth and sustainability of the sector. The report included concrete proposals for legal reform.

In response to the calls for reform presented in the *Fiscal Agenda*, the government of Mexico (GoM) has taken many steps to strengthen civil society over the past five years. Specifically:

1. Eligibility to receive tax-deductible donations (authorized donee status) and other tax benefits under the LISR has been expanded to include additional categories of CSOs, including civic activist organizations, legal aid providers that serve a broader cross-section of the Mexican community, organizations that serve the migrant and refugee communities, and gender equity groups.

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<sup>1</sup> Sergio Garcia et al., *Defining a Fiscal Agenda for the Development of Civil Society Organizations in Mexico* (Incid Social, Cemefi, ITAM, and ICNL, 2007).

<sup>2</sup> Public benefit status is not a universal term under Mexican laws. CSOs may obtain “public benefit status” in accordance with a number of laws from several different government agencies; the benefits bestowed upon these different types of organizations vary greatly.

2. The application process for becoming an authorized donee was streamlined. For example, applicants may now submit some documents to the Tax Administrative Service (the Servicio de Administración Tributaria or SAT) online using electronic signature technology. In addition, the SAT has improved and expanded the information available about the process for becoming an authorized donee.
3. In an effort to make professional support more readily available to CSOs attempting to become authorized donees, the SAT developed a registry of legal and accounting professionals and offers continuing education courses for such professionals on issues pertinent to authorized donees.
4. CSO transparency has been improved through the introduction of an online reporting mechanism for authorized donees; reports are available to the public to view.
5. In an effort to reduce some of the reporting requirements for authorized donees, the SAT raised the threshold annual income for mandatory audits from 400,000 pesos to 2 million pesos in 2011.
6. The SAT published an opinion letter clarifying the provisions of the LISR affecting cross-border donations with the United States. Through this letter, the Mexican government provides assurance to US donors and potential donors that authorized donees are eligible to receive tax-deductible donations under the 1994 United States - Mexico Income Tax Convention. This step facilitates the ability of US donors to obtain tax deductions for their donations to Mexican authorized donees, making such donations more attractive.
7. CSOs worked with a member of the Mexican Congress to produce and publish a bilingual manual that explains the requirements for donors and recipients of cross-border in-kind donations between Mexico and the United States.
8. In order to make government funding more available to CSOs, some ministries have adopted uniform criteria for funding applications, streamlined systems to process applications, and improved the information made available about the process to receive funding.

These reforms have been a move in the right direction. Other legislative changes, however, have had a more ambiguous impact on CSO financial sustainability. This study was undertaken in response to the need to better understand the impact of these reforms and to identify the remaining obstacles in the current fiscal framework. The study finds that there are still a number of obstacles to more robust development of the sector and makes recommendations to address them:

1. The lack of harmonization between the LISR and the Promotion Law, as well as other laws affecting CSOs, results in gaps and inconsistencies that prevent some classes of CSOs from applying for public benefit status and leave other CSOs vulnerable to

unintended missteps and selective enforcement. A comprehensive effort to reform the LISR is needed to resolve this problem.

2. Complex and onerous administrative procedures for authorized donees limit CSOs' interest in pursuing authorized donee status. First, the law imposes a 5 percent cap on the amount of tax-deductible donations and any interest income derived from these donations that can be used for administrative expenses. The low cap, combined with the complexity of determining whether an expense should be treated as administrative, imposes a tremendous burden on authorized donees. The government and CSOs would both be well-served by re-examining the need for this requirement.

Second, CSOs find the process for obtaining an accreditation letter from a qualifying government agency - a requirement for authorized donee status - to be ambiguous, varying greatly from agency to agency. The process of applying for authorized donee status could be simplified by either eliminating the need for the accreditation letter entirely or identifying agencies with good practices and promoting adoption of similar processes among all qualifying agencies.

3. Stakeholder capacity to comply with the laws and regulations that promote CSO financial sustainability needs to be increased.

First, CSOs operate with limited staff, which hampers their ability to pursue fundraising initiatives and to understand the regulations to which they are subject. Many organizations remain unclear about the process to gain authorized donee status and many organizations are unable to comply with the requirements to maintain authorized donee status. Developing or expanding training programs for CSOs on legal issues, management, accounting, and evaluation may help address some of these weaknesses. The SAT might also consider organizing regional workshops for CSOs across the country to explain the fiscal reforms for authorized donees and encourage organizations to take advantage of them.

Second, government regulators, particularly at the SAT, need additional capacity - in terms of personnel, resources, and employees' knowledge - to implement laws and educate CSOs about the laws that affect them.

Finally, an insufficient number of lawyers and accountants have the knowledge needed to provide CSOs with competent advice about navigating the legal and fiscal framework. The SAT should continue to take steps to educate notaries, lawyers, and accountants in order to ensure that they have the appropriate knowledge to assist CSOs in applying for and maintaining authorized donee status. New training efforts focusing on authorized donee status could build on existing programs that encourage lawyers to offer pro bono services to CSOs with the aim of ensuring that volunteer lawyers are well-prepared to address this issue.



4. Although the dialogue between government and CSOs has increased, there is still much to be done in terms of improving the relationship. In order to improve CSO-government engagement, leaders from both sectors should use existing mechanisms while also creating new avenues. Such efforts should seek to engage a broad number of CSOs and government officials.
5. The sector suffers from a weak public image that makes it difficult for CSOs to recruit volunteers, attract donations, and influence public policy. CSOs must collect and disseminate data that shows the substantial impact they have on Mexico's development in order to counter the sector's negative image in society.
6. Mexico suffers from a weak culture of philanthropy. According to the Johns Hopkins University (JHU) Comparative Nonprofit Sector Project, Mexico devotes just 0.04 percent of its GDP to charitable giving – the lowest percentage of any country studied.<sup>3</sup> In order to promote a culture of giving among Mexican citizens and corporations, tax incentives need to be expanded, donors must be educated about incentives that exist, and trust in the sector must be developed to increase understanding of the sector's role and impact in society.

This report is based on information gathered through a number of diagnostic tools, including (1) desktop research and analysis of the laws, regulations, and policies making up the fiscal framework governing CSOs in Mexico; (2) a survey of close to 900 CSO representatives about the practical effects of the laws and regulations on the sector; (3) a survey of lawyers and accountants serving Mexican CSOs; (4) interviews with key government, academic, and CSO stakeholders; and (5) focus groups that gave stakeholders an opportunity to share recommendations for future action.

This report is divided into four parts. The first section provides historical background and context. The next section contains an overview of the legal framework. This is followed by a presentation of the study's findings of the impact of the legal reforms undertaken so far. Finally, the paper concludes with a number of recommendations for future action.

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<sup>3</sup> Volunteering and giving as a share of GDP by country, 1995-2002, (data includes only charitable giving; it does not include gifts to religious worship organizations), available at [http://ccss.jhu.edu/wp-content/uploads/downloads/2011/10/Comparative-Data\\_2004\\_FINAL.pdf](http://ccss.jhu.edu/wp-content/uploads/downloads/2011/10/Comparative-Data_2004_FINAL.pdf).

# I. INTRODUCTION

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## A. BACKGROUND AND CONTEXT

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Over the past decade, Mexico's political and economic landscape has changed dramatically. After more than seventy years of one-party rule, opposition party candidate Vicente Fox was elected as President in 2000 in the freest and fairest elections in Mexican history to date.<sup>4</sup> Since 2000, the Mexican economy has grown significantly, nearly doubling its Gross National Income (GNI) from 2002 to 2010.<sup>5</sup>

Progress in the area of legal reform, however, has not kept pace with these political and economic advances. Instead of engaging in comprehensive legal reform, the government has adopted piecemeal amendments to existing laws, creating a vast web of legislation that is extremely difficult for citizens to navigate and nearly as difficult for regulators to enforce consistently. This is particularly true with regard to the legal framework governing civil society organizations (CSOs).<sup>6</sup> The lack of a comprehensive CSO framework law and consistent guiding regulations creates a number of challenges for CSOs, the government, donors, and other stakeholders.

The legal framework governing Mexican CSOs explicitly recognizes the importance of the sector in promoting the development of the country. However, CSOs struggle to determine their rights and obligations under the many federal, state, and local laws that make up the CSO legal framework.<sup>7</sup> In particular, the legal framework lacks a consistent definition of what constitutes a CSO or a public benefit organization – a CSO that pursues objectives that are desirable and beneficial for society and therefore deserves access to state funding and preferential tax treatment.<sup>8</sup> This complicated – and often contradictory – legal framework inhibits rather than encourages CSO growth and sustainability.<sup>9</sup>

In 2004, the Johns Hopkins University (JHU) Comparative Nonprofit Sector Project published comparative data about the civil society sectors in thirty-six countries.<sup>10</sup> The data showed that the size of the formal civil society sector in Mexico was extremely small relative to its population and

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<sup>4</sup> U.S. Department of State Bureau of Western Hemisphere Affairs Background Notes: Mexico, November 16, 2011, available at: <http://www.state.gov/outofdate/bgn/mexico/191338.htm> (accessed November 12, 2012).

<sup>5</sup> World Bank GNI per capita, Atlas method (US\$9,240 in 2011, available at:

<http://data.worldbank.org/indicator/NY.GNP.PCAP.CD/countries/1W-MX?display=graph>.

<sup>6</sup> The Federal Law for the Promotion of Activities Undertaken by CSOs (the Promotion Law) - a key law governing CSOs - was passed in 2004. Since then, the Promotion Law has not been substantially improved or harmonized with the LISR; instead, the government has made a series of small legislative fixes and administrative interpretations that have complicated rather than clarified the framework.

<sup>7</sup> For an in depth discussion on the various ways that CSOs are defined throughout the Mexican legal framework, see Ireri Ablanado, *Las organizaciones de la sociedad civil en la legislación mexicana* (Washington, D.C., 2009).

<sup>8</sup> *Id.*, p. 25.

<sup>9</sup> See, for example, *Fiscal Agenda* and *El marco fiscal y legal de las organizaciones de la sociedad civil: una guía breve de los trámites legales y obligaciones fiscales* (ITAM and Alternativas y Capacidades A.C., 2005).

<sup>10</sup> See Lester M. Salamon and S. Wojciech Sokolowski (ed.), *Global Civil Society: Dimensions of the Nonprofit Sector, Volume Two*, (Kumarian Press, 2004); and Lester M. Salamon, Helmut K. Anheier, Regina List, Stefan Toepler, S. Wojciech Sokolowski (ed), *Global Civil Society: Dimensions of the Nonprofit Sector, Volume One* (1999).

economy.<sup>11</sup> The study also found that the level of domestic philanthropy in Mexico was exceptionally low, with Mexico devoting just 0.04 percent of its GDP to charitable giving.<sup>12</sup>

In response to these findings, a group of CSOs and academics came together in 2005 to identify and analyze the obstacles to CSO development in Mexico. The working group convened six expert forums involving 150 representatives of CSOs and government to present information, solicit input on the challenges that CSOs face, and collectively develop recommendations.

This group's findings were published as *Defining a Fiscal Agenda for the Development of Civil Society Organizations in Mexico (Fiscal Agenda)* in 2007. The *Fiscal Agenda* identified a number of key obstacles to CSO development and proposed changes and initiatives to support an effective and self-sustaining Mexican civil society. Most significantly, the *Fiscal Agenda* found that the legal framework that regulates CSOs in Mexico hinders rather than supports the growth of the sector. In particular, the *Fiscal Agenda* concluded that the legal framework does not support the financial stability of the sector, noting that domestic sources of funding for Mexican CSOs have not increased to fill the gap left by a steady decrease in foreign funding. Furthermore, the *Fiscal Agenda* found that the relationship between government, civil society, and citizens is in need of serious repair.

The *Fiscal Agenda* considered how the tax laws affect three basic categories of CSOs:

1. Authorized donees - those organizations authorized by the Ministry of Finance and Public Credit (SHCP) to receive tax-deductible donations;
2. Formally constituted organizations that are not authorized donees; and
3. Informal groups without legal status.<sup>13</sup>

The *Fiscal Agenda* also compared the benefits of being an authorized donee with the benefits of registering under the Federal Law for the Promotion of Activities Undertaken by CSOs (Promotion Law); organizations registered under the Promotion Law are sometimes referred to by the acronym for the Promotion Law registration number, or CLUNI.

The authors ultimately focused on identifying the challenges related to authorized donees, as they determined that this status offers the greatest financial benefits for CSOs within the Mexican legal framework. Most importantly, authorized donees can receive tax-deductible donations.

In recent years, the government of Mexico (GoM) has taken several steps to address some of the obstacles identified in the *Fiscal Agenda*. Through a process of consultation with CSO representatives, the GoM has made the following reforms:

- Expanded eligibility for authorized donee status under the Federal Income Tax Law (Ley del Impuesto sobre de la Renta or LISR) to include several additional categories of

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<sup>11</sup> Id., p. 430.

<sup>12</sup> Volunteering and giving as a share of GDP by country, 1995-2002, (data includes only giving ; it does not include gifts to religious worship organizations), available at: <http://ccss.jhu.edu/wp-content/uploads/downloads/2011/10/Comparative-Data-2004-FINAL.pdf>.

<sup>13</sup> *Fiscal Agenda*, p. 38.

organizations identified as public benefit organizations under other laws (e.g., the Promotion Law);

- Streamlined the application process to become an authorized donee, including making the application available online, thereby reducing the time needed to complete the process to a few weeks instead of several months or even longer;
- Launched a new online reporting system that has helped to increase the transparency of authorized donees;
- Improved the availability of information regarding the process for becoming an authorized donee, by, e.g., revising a comprehensive manual that describes the process and including additional materials on its website that explain the process in greater detail;
- Issued a determination letter that confirms that authorized donees qualify for tax-deductible donations from US donors under the terms of the 1994 United States - Mexico Income Tax Convention, making such donations more attractive;<sup>14</sup> and
- Amended the LISR in 2010 to permit authorized donees to earn income from economic activities unrelated to the activities for which they were granted preferential status.<sup>15</sup> The income from unrelated activities will not be taxed unless it exceeds 10 percent of the organization's total income; income from unrelated economic activity that exceeds 10 percent of the organization's total income will be taxed at the current corporate rate.<sup>16</sup>

However, significant challenges remain. This study was undertaken, in part, in response to the need to understand better the impact of these reforms and to identify the remaining obstacles presented by the current fiscal framework.

## B. METHODOLOGY

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This report is based on information gathered through a study involving a number of diagnostic tools. In an effort to obtain a broad assessment of the fiscal framework for CSOs in Mexico, the study sought participation from diverse stakeholders including CSO representatives, government regulators, legislators, and academics. ICNL conducted a literature review and held consultations with stakeholders to develop the themes and specific issues on which to focus the study. ICNL then organized focus groups, interviews with key stakeholders, and surveys of CSO representatives, lawyers, and accountants about their knowledge of and experience under the current legal framework. Through this process, over 900 stakeholders were able to identify constraints and opportunities in the legal and regulatory framework for CSOs, and to prioritize focus areas for policy and legal reforms. The survey respondents were from all thirty-one Mexican states, plus the federal district.

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<sup>14</sup> See, for example, SAT letter 600-04-05-2008-74888, Exp. 243, Reg. 13818/08 to the Instituto Tecnológico Autónomo de México, July 4, 2008. The United States - Mexico Income Tax Convention entered into force December 28, 1993 and most provisions became effective January 1, 1994. See Article 22: Exempt Organizations, p. 23 available at: <http://www.irs.gov/pub/irs-trty/mexico.pdf>.

<sup>15</sup> This reform has proven unwelcome to some Mexican authorized donees, who argue that as a practical matter, identifying and taxing unrelated income has placed new administrative and financial burdens on them.

<sup>16</sup> The corporate tax rate for 2012 is 30 percent.

ICNL aimed to make this study as comprehensive as possible, but faced a few limitations. First, the study focuses on the current legal and fiscal framework and some of the major issues this framework presents for CSOs; it does not cover all issues affecting the CSO sector. Second, this study focuses on issues pertinent to groups registered as legal entities, while recognizing that much of Mexican civil society consists of unregistered organizations. As a practical matter, the laws governing authorized donees, financial benefits for authorized donees and other CSOs, and related issues only affect organizations that are legally registered.

## II. OVERVIEW OF THE LEGAL FRAMEWORK

According to the 2011 CIVICUS report, which cites statistics from the Mexican Center for Philanthropy (Cemefi), the Ministry of Interior, and the Federal and State Electoral Institutes, as well as other academic research, there are approximately 35,000 to 40,000 non-governmental, not-for-profit CSOs in Mexico.<sup>17</sup>

Mexican CSOs are generally relatively young. As reflected in the chart below, nearly all of the CSOs surveyed for this study were legally established after 1970, with a sharp rise in the numbers established in the late 1990s and early 2000s, followed by a sharp drop starting in the late 2000s. This pattern may be related to a number of historical events, such as the 1985 Mexico City earthquake, the country's economic crisis in 1995, and events related to Mexico's democratic transition, including local elections in 1991 and 1993 and federal elections in 1994 and 1997.<sup>18</sup> In 2000, the National Action Party (PAN) ended the Institutional Revolutionary Party's (PRI) decades-long hold on power. The surge in security threats from drug cartels, criminal violence, and reports of government human rights abuses in recent years have sparked the emergence of new CSOs to address these issues.



While the number of CSOs has increased over the past several years, the vast majority of organizations remain concentrated in the Federal District and in or around other densely populated

<sup>17</sup> *A Snapshot of Civil Society in Mexico: Analytical Report on the CIVICUS Civil Society Index* (Mexican Center for Philanthropy (Cemefi), Citizens' Initiative for the Promotion of a Culture of Dialogue, and Social Administration and Cooperation: 2011), p. 29; Michael D. Layton, "Focos rojos en las cifras sobre sociedad civil organizada", *Este País* 247 (November 1, 2011), available at <http://estepais.com/site/?p=35835>. There is disagreement, however, on the size of the sector – perhaps attributable in part to the lack of a consistent definition for CSOs. Some governmental sources reportedly rely on figures of up to 250,000 not-for-profit entities.

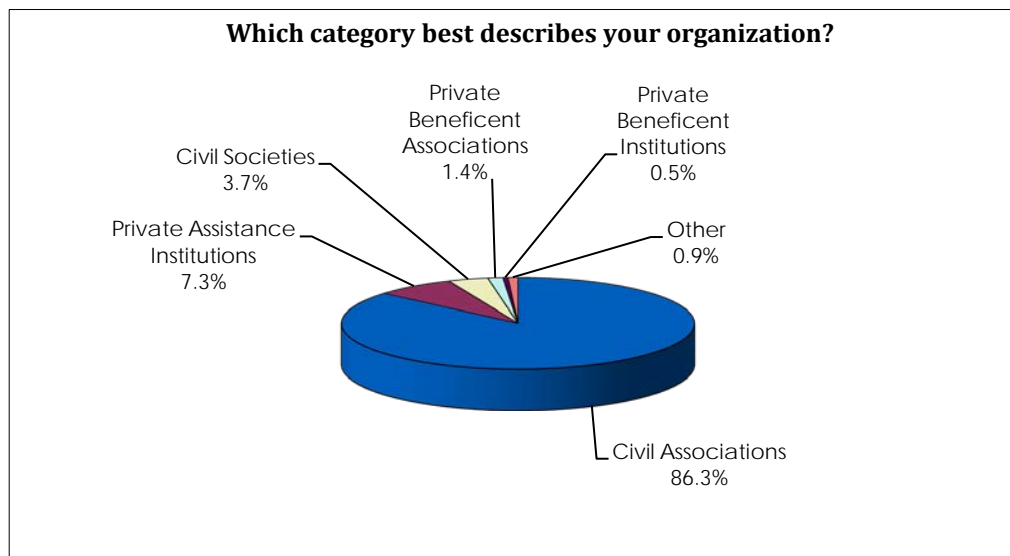
<sup>18</sup> See, e.g., *A Snapshot of Civil Society in Mexico: Analytical Report on the CIVICUS Civil Society Index*, p. 9.

cities.<sup>19</sup> According to the 2011 CIVICUS Index, 74.5 percent of authorized donees and 47.3 percent of CLUNIs are located in the twenty most populous cities.<sup>20</sup>

## A. LEGAL FORMS

Mexico's legal framework allows CSOs to be created in different forms to pursue legitimate aims, including both mutual benefit and public benefit interests. In order to obtain legal status, Mexican CSOs must register at the state or federal level. Several guides describe in detail the required steps to gain legal status in Mexico.<sup>21</sup>

Most CSOs in Mexico are organized under one of four legal forms: civil associations, private assistance institutions or private beneficent institutions/associations, civil societies, or trusts. Among the 881 CSOs that responded to the survey implemented for this study, over 85 percent are organized as civil associations, as reflected in the chart below.



<sup>19</sup> For more information on the geographic concentration of organizations in 2007, see *Fiscal Agenda*, p. 21-23.

<sup>20</sup> *A Snapshot of Civil Society in Mexico: Analytical Report on the CIVICUS Civil Society Index*, p. 29.

<sup>21</sup> See *Building your organization in 16 steps (Construyendo tu organización en 16 pasos)*, a comprehensive guide to the legal registration process (focusing on legal formation as a civil association) in Spanish from Alternativas y Capacidades, at: <http://www.alternativasycapacidades.org/sites/default/files/16%20pasos%202a.edici%C3%B3n.pdf>; and *Beyond Borders: Observations for US organizations considering nonprofit incorporation in Mexico* (Border Partnership, 2010), available at: [http://borderpartnership.hostcentric.com/BPP%20Beyond Borders Study.pdf](http://borderpartnership.hostcentric.com/BPP%20Beyond%20Borders%20Study.pdf).

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## CIVIL ASSOCIATIONS

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A civil association<sup>22</sup> is a group of individuals who have come together voluntarily for a definite time to realize a common purpose that is not prohibited by law and that is not predominantly economic in character.<sup>23</sup> Each state's Civil Code regulates civil associations, outlines the purposes for which they may operate, and establishes minimal governance requirements. The very broad definition allows organizations to carry out a multitude of purposes, and is less restrictive than rules governing other organizational forms. For example, civil associations are subject to fewer restrictions on how they may earn income. Civil associations also have greater flexibility to determine their own internal governance matters.

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## PRIVATE ASSISTANCE INSTITUTIONS, PRIVATE BENEFICENT INSTITUTIONS, AND PRIVATE BENEFICENT ASSOCIATIONS

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Private assistance institutions and private beneficent institutions and associations are formed in accordance with state Laws on Private Assistance/Beneficent Institutions or Associations to provide social and humanitarian assistance, such as food or medical services to the needy. These organizations are closely regulated by state Private Assistance Boards or Institutes. The Boards or Institutes coordinate activities, provide legal advice, and provide oversight to ensure that funds devoted specifically to private assistance are used for the purposes defined in each organization's bylaws. In addition, the Boards or Institutes often serve as conduits for their member institutions to receive additional benefits, such as exemption from Value Added Tax (VAT), authorization to receive tax-deductible donations, and exemptions from some state and local taxes. Private assistance institutions and private beneficent institutions/associations automatically qualify for tax-exempt status because of both the nature of their public benefit activities and the continuous government oversight to which they are subject.

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## CIVIL SOCIETIES (PARTNERSHIPS)

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A civil society (or partnership) is established in accordance with state civil codes by a contract in which the founders mutually obligate themselves to combine their resources or efforts in order to realize a common purpose of a predominantly economic character that does not constitute commercial speculation. Relatively few CSOs are formed as civil societies, in part because the provisions offer less flexibility to members.<sup>24</sup> For example, the establishing contract for a partnership may only be modified by unanimous agreement among its members.<sup>25</sup> This legal form may be appropriate for a CSO that carries out regular economic activities for its own sustainability as well as the sustainability of other not-for-profit entities.

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<sup>22</sup> For more on the process and requirements for establishing a civil association, see *Construyendo tu organización en 16 pasos*.

<sup>23</sup> United States International Grantmaking (USIG) project of the Council on Foundations in partnership with the International Center for Not-For-Profit Law, available at <http://usig.org/countryinfo/mexico.asp>.

<sup>24</sup> Many professional organizations such as law firms are civil societies because they are organized as partnerships.

<sup>25</sup> See Article 2698 of the Civil Code for the Federal District available at: [http://www.icnl.org/research/library/files/Mexico/DF\\_Codigo\\_Civil\\_2011.pdf](http://www.icnl.org/research/library/files/Mexico/DF_Codigo_Civil_2011.pdf).



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## TRUSTS

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Trusts are governed by the General Law of Titles and Operations of Credit (LGTOC). A trust is created when a donor dedicates property to a particular lawful purpose, which may be either for private or public benefit.<sup>26</sup> A trust may be created during the life of the donor (through a trust instrument) or upon the death of the donor (through a will). The donor must designate a fiduciary institution authorized under the LGTOC to carry out the obligations of the trustee.<sup>27</sup>

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## B. FISCAL FRAMEWORK

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The fiscal framework for CSOs in Mexico is part of a complex general legal framework that bestows different benefits and obligations on different groups. Once a CSO has been registered, it may apply for preferential status as an organization that provides some benefit to the public under either or both the Promotion Law and the LISR. Each of those laws has its own eligibility criteria, application procedures, programmatic or financial incentives, and regulatory burdens.<sup>28</sup>

While CSOs are governed by a combination of federal, state, and local laws, the scope of this study is limited to the federal laws, regulations, and policies that most directly affect CSOs' sustainability.<sup>29</sup> This section examines the laws, regulations, and provisions that establish tax-exempt status and public benefit status, as well as those that provide for the tax treatment of CSO income and donations.

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## INCOME TAX-EXEMPT STATUS

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Article 93 of the LISR generally exempts not-for-profit organizations from paying taxes on income from most sources.<sup>30</sup> After obtaining legal recognition at the state or federal district level, a CSO seeking tax-exempt status must register as a "Persona Moral con Fines no Lucrativos" (a not-for-profit entity) with the federal tax authority (Servicio de Administración Tributaria or SAT in Spanish). Articles 95 and 102 of the LISR recognize organizations that fall into the following consolidated list of categories as not-for-profit entities:

- Private assistance institutions or private beneficent institutions, and not-for-profit civil associations or civil societies incorporated for the benefit of low-income individuals, sectors, or regions and engaged in activities to improve the subsistence conditions and development of indigenous communities and vulnerable groups by virtue of age, gender, or disability;

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<sup>26</sup> See LGTOC §381.

<sup>27</sup> LGTOC §385.

<sup>28</sup> CSOs may also choose to apply for preferential status under a parallel system of state laws promoting civil society organizations.

<sup>29</sup> For more information on some individual state laws and regulations governing the CSO sector, see USIG Country Report: Mexico, available at: <http://www.usig.org/countryinfo/mexico.asp>.

<sup>30</sup> Not-for-profit entities in Mexico do not have to pay income tax on membership dues, donations, or income generated from activities related to carrying out their missions, among other sources of revenue.



- Organizations engaged in scientific or technological investigation and registered in the Scientific and Technological Institution's National Register;
- Civil associations and societies engaged in cultural activities, environmental preservation activities, and grant making;
- Organizations authorized to teach in accordance with the General Education Law (Ley General de Educación), as well as Parent Associations;
- Institutions incorporated by a presidential decree or law;
- Consumer cooperative associations;
- Mutual insurance companies as well as agricultural and rural insurance funds, which do not operate with third parties;
- Investment companies specialized in retirement funds (except for investment companies specialized in equity);
- Civil societies and limited liability companies organized for public purposes engaged in the decentralized management of irrigation units and districts;
- Political parties; and
- Agencies of the federal, state, and local governments.

Notwithstanding the aforementioned, not-for-profit entities (except political parties, federal, state and local governments, authorized donees, and investment companies specializing in retirement funds) are obligated to pay income tax on revenues obtained from: (i) property transfers; (ii) interest; and (iii) awards.<sup>31</sup>

Although the above list seems fairly comprehensive, several categories of organizations are still ineligible for income tax exemptions and other preferential tax treatment, even though they are not-for-profit and recognized as public benefit organizations under other Mexican laws.<sup>32</sup>

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## PUBLIC BENEFIT STATUS

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Not all tax-exempt organizations in Mexico have public benefit status. In most countries, the state does not extend all benefits to all CSOs, instead extending certain benefits to a subset of these organizations based on their purposes and activities.<sup>33</sup> By providing benefits, the state seeks to promote certain designated activities, usually those related to the common good. CSOs pursuing such activities are given various labels in different countries, including charities and public benefit organizations. Charitable or public benefit status is fundamentally an issue of fiscal regulation.<sup>34</sup> To promote public benefit activity, the legal framework links public benefit status to preferential tax treatment or other forms of government support. In exchange for these benefits, organizations are

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<sup>31</sup> LISR Article 93 and Chapter IV.

<sup>32</sup> See discussion under Remaining Obstacles.

<sup>33</sup> For a more extensive discussion of international good practice in the granting of tax benefits and the role of such benefits in improving the enabling environment for NGOs, see Open Society Institute and ICNL, *Guidelines for Laws Affecting Civic Organizations* 2<sup>nd</sup> Ed. (New York, NY: 2004), p. 77.

<sup>34</sup> Id.

generally subjected to more stringent supervision to ensure that they are using their assets for the public good.<sup>35</sup>

The Mexican legal framework does not provide a single definition of a public benefit organization. Instead, Mexican legislation contains a myriad of references to “social groups” and “civic organizations” and refers to a number of categories of organizations and activities that are “in the public interest.” These lists are not always congruent.

For the purposes of this study, we compare two federal laws - the Federal Income Tax Law (LISR) and the Federal Law for the Promotion of Activities Undertaken by CSOs (Promotion Law) - that set forth specific criteria to obtain public benefit status. Both laws recognize a number of activities that are considered for the public’s benefit, bestowing certain benefits on CSOs that undertake these activities and comply with specific rules and regulations. However, the list of public benefit activities recognized by the two laws only partially overlap. Most significantly, recognition under one law as a public benefit organization does not provide recognition under the other law.<sup>36</sup>

### AUTHORIZED DONEES

In addition to establishing the criteria for tax-exempt status, the LISR identifies the types of public benefit activities and/or organizations that are eligible to apply for authorized donee status. Authorized donees enjoy a number of benefits. For example:

- Individual and corporate donors to authorized donees may deduct some or all of those donations from their taxes. By reducing tax liability, these tax deductions can be a powerful incentive for taxpayers to donate to authorized donees.
- Authorized donees generally do not pay federal income tax except on income derived from unrelated business income that exceeds 10 percent of a CSO’s total income. This exemption saves an organization from paying the corporate tax on its income.<sup>37</sup>
- In most instances, authorized donees do not pay state income tax. The availability of state tax exemptions varies by state.
- Authorized donees automatically qualify for tax-exempt donations from US donors under the bilateral treaty.<sup>38</sup>
- The SAT publishes a list of authorized donees every year. This list provides authorized donees with greater public visibility, making it easier for potential donors to identify them as possible recipients.

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<sup>35</sup> Id., p. 65

<sup>36</sup> Ablanado, *Las organizaciones de la sociedad civil en la legislación mexicana*, p. 44-45.

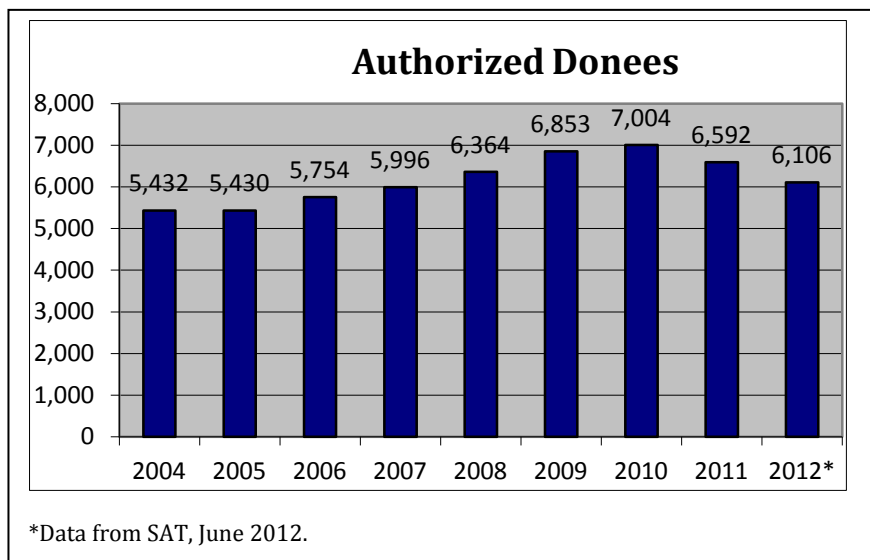
<sup>37</sup> Other not-for-profit CSOs pay income taxes on unrelated income or income from providing services to non-members if that income exceeds 5 percent of the CSO’s total income. See LISR Article 93.

<sup>38</sup> See discussion on page 26.

To be eligible to receive authorized donee status, an organization must engage in one of the following activities:

- provide aid to the needy;<sup>39</sup>
- engage in educational activities as defined by the General Education Act;
- undertake scientific or technological research;
- engage in activities to protect the environment;
- support or promote culture or the arts;
- preserve national treasures;
- defend and promote human rights;
- grant scholarships; or
- make grants to other authorized donees.

An authorized donee, regardless of its particular legal form, must comply with a number of operational and financial rules as set forth in LISR and enforced by the SAT. Specifically, an authorized donee must first obtain a letter of accreditation from another government agency stating that the organization does in fact pursue the goals for which it was organized and



devote its assets exclusively to the pursuit of these goals.<sup>40</sup> It may not distribute assets to any individual or entity except for payment of services rendered or transfers to other authorized donees. It may not participate in political activities.<sup>41</sup> Authorized donees must also limit administrative expenditures to 5 percent of tax-deductible donations and any interest income derived from these donations. Upon the organization's dissolution, any remaining assets must be transferred to another authorized donee as set forth in a mandatory irrevocable provision in the organization's statutes.

<sup>39</sup> Providing aid to the needy includes the following support: subsistence, medical, psychological, education and training for employment, prevention and attention in disasters, intra-family violence, legal, disasters, and funeral assistance, those working with refugees and migrants, and on gender equity issues. See LISR Article 95.

<sup>40</sup> The SAT grants authorized donee applicants temporary status, providing them with a six-month window to obtain the accreditation letter.

<sup>41</sup> According to LISR Article 97 II, CSOs with authorized donee status "shall not be entitled to intervene in political campaigns or to become involved in activities of propaganda or intended to influence legislation." The same article carves out an exception for CSO publications or analyses that do not have a proselytizing nature, as well as for technical assistance provided to government entities at their written request.

An authorized donee must adhere to the SAT's administrative oversight and transparency rules. Pursuant to amendments to the tax code made in 2007, an authorized donee must inform the SAT about any transactions with related parties, and about services provided and goods acquired from donors.<sup>42</sup> An authorized donee is generally required to undergo an annual audit, although the SAT has exempted organizations with annual income less than two million pesos from this requirement.<sup>43</sup> Authorized donees must renew their status every year. Authorized donee status may be revoked by the SAT if an organization fails to meet its compliance obligations. In the first half of 2012 alone, the SAT stripped 756 authorized donees of their status because they failed to comply with reporting requirements.<sup>44</sup>

Notwithstanding this reduction in the total number of authorized donees, organizational applications for authorized donee status have increased tremendously over the last several years. From January to July 2011, the SAT received almost 700 applications for authorized donee status, a 12 percent increase in applications.<sup>45</sup> This may be a result of the SAT introducing a more streamlined online application system; amendments to the tax regulations that expanded the universe of organizations eligible for authorized donee status; or the reduction in the time that it takes to process applications from an average of nine months to three.

### CSOS REGISTERED UNDER THE PROMOTION LAW (CLUNIS)

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The Federal Law for the Promotion of Activities Undertaken by CSOs (Promotion Law) of 2004 recognized the importance of CSO activities for Mexico's development and created the Federal Registry of Civil Society Organizations. Each organization listed in the registry is assigned a Unique Registry Code (CLUNI) number, which is a prerequisite to obtain government funding. The Promotion Law is intended to encourage civic activity, not to regulate the sector. The Promotion Law establishes a general mandate for governmental ministries to facilitate greater CSO participation in public policy development and encourages government funding for the sector. It also recognizes a number of activities as being for the public benefit, including:

- social assistance
- nutritional programs
- civic participation
- legal assistance
- rural and indigenous development
- promotion of gender equality
- support for services for the disabled
- community development
- defense and promotion of human rights
- promotion of sports

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<sup>42</sup> See LISR §97(VII).

<sup>43</sup> At the time of publication, two million pesos equaled approximately US\$151,400. See Secretaría de Hacienda y Crédito Público, *Resolución Miscelánea Fiscal para 2012*, sec. I.2.15.1 (December 2011).

<sup>44</sup> SAT Statistics as of June 2012, available at:

[ftp://ftp2.sat.gob.mx/asistencia\\_servicio\\_ftp/publicaciones/donatarias/Estadisticas\\_180612.xls](ftp://ftp2.sat.gob.mx/asistencia_servicio_ftp/publicaciones/donatarias/Estadisticas_180612.xls).

<sup>45</sup> Interview with SAT official.

- health and sanitation
- environmental protection
- environmentally sustainable urban and rural development
- promotion of education, culture, the arts, science and technology
- improving the economy
- civil protection
- support for the creation and strengthening of civil society

CSOs with CLUNIs are prohibited from partisan politicking and religious proselytizing. Although CSOs with CLUNIs are eligible to apply for government funding for certain activities, the receipt of government funding is not guaranteed. For example, only CSOs with CLUNIs are eligible to compete for funding to provide social services such as job training or medical services under the *Co-investment Development Program* offered by SEDESOL, but just like any competitive award process, applicants are not assured funding.

Besides being eligible to apply for government funding, CSOs with CLUNIs are entitled to:

- Engage with the Technical Council, a consultative body established under the Promotion Law to facilitate better CSO-government relations and to foster greater participation in policy development; and
- Participate in planning, executing, and monitoring politics, programs, projects, and processes undertaken by the Federal Public Administration (FPA).<sup>46</sup>

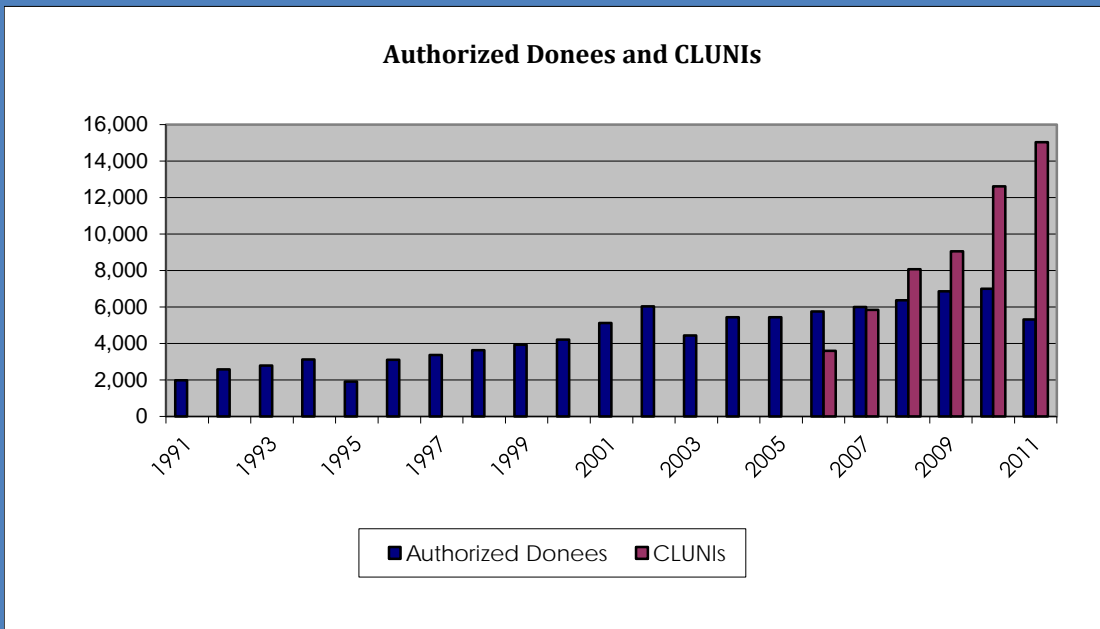
CSOs with CLUNIs must observe the operational, accounting, and reporting rules set forth in the Promotion Law. These include having an accounting system consistent with generally accepted accounting rules, and submitting annual reports to the Commission on the Promotion of Activities for CSOs that state accomplishments, financial information, and how public support and benefits were utilized. In the case of dissolution, a CSO with a CLUNI is required to direct the remainder of its assets to another CSO with a CLUNI.

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<sup>46</sup> The FPA encompasses all ministries and agencies of the Mexican federal government.

### Authorized Donees vs. CLUNIs

Of the approximately 40,000 private, not-for-profit organizations in Mexico, as of December 2011, over 15,000 organizations were registered as CLUNIs and just under 6,000 organizations held authorized donee status. Approximately 2,500 organizations have both designations. The number of CLUNIs has increased significantly since 2006, when there were just under 4,000. At the same time, the number of authorized donees has remained almost the same. Among survey respondents, 95.2 percent (820 organizations) have CLUNI status, while just 5 percent (45 organizations) reported having authorized donee status.



Experts and CSO representatives point to a number of reasons why the number of CLUNIs nearly quadrupled from 2006 to 2011 while the number of authorized donees remained stagnant. The most often cited reason, as discussed below, is the lack of understanding about the process to become an authorized donee. In addition, the compliance obligations for authorized donees are more difficult to meet.

\* Chart from Michael D. Layton, "Focos rojos en las cifras sobre sociedad civil organizada", Este País 247 (November 1, 2011), available at <http://estepais.com/site/?p=35835>. Data from SAT, INDESOL, and INEGI.

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## C. EXEMPTIONS FROM VAT, CUSTOMS DUTIES, AND OTHER TAXES

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### VAT

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All Mexican individuals and legally constituted organizations that engage in the transfer of goods, provision of services, grant of temporal use or enjoyment of goods, or importation of goods or services within the national territory of Mexico are obligated to pay value-added tax (VAT) at the rate of 16 percent.<sup>47</sup> Not-for-profit CSOs are exempt from paying VAT on the services they provide if the services fall within the following categories:

- educational services;
- health services;
- public shows;
- publishing books, magazines, newspapers;
- lotteries and raffles; and
- the importation of goods donated by foreign residents to organizations with authorized donee status as authorized by the SAT.

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### CUSTOM DUTIES

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Organizations with authorized donee status that receive goods donated from abroad may apply for exemptions from import taxes for certain in-kind donations.<sup>48</sup>

Some types of exempt in-kind donations of particular relevance to CSOs include:

- ambulances and mobile clinics,
- school buses and computers for educational institutions,
- fire engines,
- garbage trucks,
- medical equipment and laboratory instruments, and
- wheel chairs and orthopedic equipment.

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### FLAT BUSINESS TAX

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In January 2008, the new Flat Rate Business Tax Law (Impuesto Empresarial a Tasa Única, or IETU in Spanish) went into effect in Mexico. The IETU was the key component of a major tax reform undertaken by President Calderón. According to the Flat Tax Law, Mexican individuals, legal

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<sup>47</sup> Tax Law (Ley del Impuesto al Valor Agregado (LIVA)) §1. Please note that the VAT rate for the transfer of goods or services in the Mexico-US border region is 11 percent. Id. §2.

<sup>48</sup> See *Guía para Donativos en Especie a México*, International Community Foundation (2008), available at [http://ficbaja.org/portal/images/documentos/guia\\_donativos\\_pdf.pdf](http://ficbaja.org/portal/images/documentos/guia_donativos_pdf.pdf).

entities, and non-residents with “a permanent establishment in Mexico” are obligated to pay the flat business tax on income earned from the following activities:

- Transfer of goods;
- Provision of independent services; and
- The grant of temporary use or benefit of goods.

Revenue earned by authorized donees is exempt from the flat tax if it is also exempt under LISR.<sup>49</sup>

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### III. IMPACT OF REFORMS: STUDY FINDINGS

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The *Fiscal Agenda* identified several problems in the legal environment for CSOs and offered a number of suggestions on how to eliminate or reduce the burdens they posed. Since the publication of the *Fiscal Agenda* and in consultation with CSOs, the government has instituted a series of regulatory reforms and policy changes in an attempt to improve the environment for CSOs. Some of the changes directly addressed the obstacles identified in the *Fiscal Agenda*, while others have indirectly addressed these issues. Here we offer an analysis of the impact of these changes on the major obstacles identified in the *Fiscal Agenda*, and other important issues as identified by survey respondents, interviewees, and focus group participants of this study.

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#### A. AUTHORIZED DONEES

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##### BECOMING AN AUTHORIZED DONEE

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##### ELIGIBILITY

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**ISSUE:** The *Fiscal Agenda* noted that eligibility criteria to receive tax-deductible donations (authorized donee status) were too restrictive. The eligibility criteria prescribed in the LISR did not include all of the categories of activities recognized as “in the public’s interest” as set forth in other Mexican laws, including the Promotion Law and the Social Assistance Law.<sup>50</sup> These narrow eligibility criteria were one factor keeping the number of authorized donees relatively small, and many CSOs undertaking public interest work were not able to access important financial benefits that could help sustain their activities.

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<sup>49</sup> Flat Tax Law, § 4.

<sup>50</sup> See Ablanedo, *Las organizaciones de la sociedad civil en la legislación mexicana*, p. 28-36.



## Obstacles to Becoming an Authorized Donee Identified in the *Fiscal Agenda*

The *Fiscal Agenda* identified the difficulties CSOs faced in obtaining authorized donee status, complying with regulatory requirements, and becoming financially sustainable as obstacles to a stronger civil society. In particular:

- The confusing and often contradictory laws that govern the sector made it difficult for CSOs and donors to understand their rights and obligations.
- For many organizations, the high financial and human resources costs of acquiring and maintaining authorized donee status outweighed the benefits.
- Many organizations were not eligible for authorized donee status because the LISR only recognized limited categories of activities as being eligible for tax benefits.
- The government and the public had a negative view of the sector as a whole.

**REFORM:** Eligibility for authorized donee status has been expanded to include additional CSO activities. Since 2007, the SAT expanded the universe of CSOs eligible to apply for authorized donee status to include the following:

- gender equity groups;
- organizations that support immigrant rights;
- legal aid providers that serve a broader cross section of Mexican citizens;<sup>51</sup> and
- organizations that promote civic participation.<sup>52</sup>

The expansion of eligibility for authorized donee status is a step in the right direction. One SAT official highlighted the expansion of categories of CSOs eligible for authorized donee status to include those promoting civic participation as having a “tremendous impact”:

*I'm talking about those organizations that are in charge of auditing the authorities or evaluating State transparency, human rights, and neighborhood improvements: paving, trash collection, and even animal rights... All these examples are included within the Public Services and Works category, so there is now diversity among the types of organizations eligible to receive authorized donee status.<sup>53</sup>*

Despite the position taken by the SAT, there continues to be disagreement among CSOs regarding the reach of the reforms and a sentiment that the categories still need to be further expanded. According to a press release issued in July 2012 by Fortaleciendo Causas Ciudadanas, a coalition of CSOs:

*Despite the important contributions that CSOs make to Mexican society, many [CSOs] cannot access the authorized donee regime. Many, even, cannot be considered as non-profit legal entities, in accordance with Title III of the Income Tax Law, including social*

<sup>51</sup> *Resolución miscelánea fiscal para 2008*, Sección 1.3.9.6.

<sup>52</sup> See *Resolución miscelánea fiscal para 2008*, Sección 1.3.9.3.

<sup>53</sup> ICNL interview with key SAT official, September 2011.

*organizations that aim to promote civic engagement, defend consumer rights or freedom of speech and press, strengthen other CSOs or promote education. This outdated tax system does not encourage philanthropy and denies the right to enjoy tax incentives to most CSOs.<sup>54</sup>*

This issue was also raised by several focus group participants:

*Article 5 of the Promotion Law [Ley de Fomento] describes all activities that are recognized by the Mexican State as matters of public interest and should be supported by government agencies, including fiscal stimulus.*

*We have not yet been authorized to issue tax deductible receipts. We had some problems because our social purpose is not recognized by Article 95 of the Income Tax Law...We have truly tried to expand the social purposes [of the organization] in order to access the donee registry.*

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#### APPLICATION PROCESS

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**ISSUE:** According to the *Fiscal Agenda*, CSOs found the procedure for becoming an authorized donee to be bureaucratic and expensive. In addition, information about the process was not adequately accessible to stakeholders.

**REFORMS:** The SAT has adopted a number of new technologies in an effort to streamline the application and reporting processes for authorized donee status. For example, applicants may submit some documents required for authorization online using electronic signature technology.

While the increased use of technology may have helped to reduce some of the costs associated with applying for authorized donee status and helped to speed up the SAT's response time, the process remains cumbersome. For example, one focus group participant complained that technical glitches in the on-line system left her organization unable to access the SAT website for extended periods.

The SAT has had a guide about the process for becoming an authorized donee for a number of years. In August 2008 and again in February 2012, the SAT revised the language in its handbook *Authorized Donees: Requirements, Benefits, and Tax Obligations*,<sup>55</sup> supplementing this general manual with more detailed descriptions of each step of the authorization process on its website. The SAT now provides applicants with written instructions about the procedures that must be followed throughout the authorization process, and has included the estimated amount of time each step should take.

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<sup>54</sup> See July 13, 2012 Press Release, *Organizaciones de la sociedad civil reiteramos al SAT nuestra demanda para que amplié el régimen de donatarias autorizadas*, available at: <http://www.causasciudadanas.org/2012/07/comunicado-de-oscs-para-el-sat-sobre.html>.

<sup>55</sup> *Donatarias Autorizadas: Requisitos, ventajas, obligaciones fiscales* (SAT: 28/02/12), available at: [ftp://ftp2.sat.gob.mx/asistencia\\_ftp/publicaciones/folleto12/donautoriz\\_03052012.pdf](ftp://ftp2.sat.gob.mx/asistencia_ftp/publicaciones/folleto12/donautoriz_03052012.pdf).

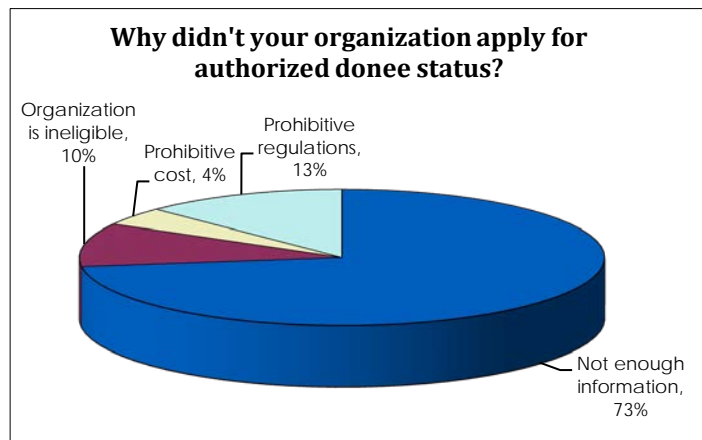
These changes have helped to provide better information to stakeholders about the application process, likely contributing to the increasing number of applications for authorized donee status over the last two years.

Although there are now a number of resources explaining the process to obtain authorized donee status, the CSO survey respondents and focus group participants point to the need for additional information about the process. According to one focus group participant:

*One of the greatest difficulties at the beginning was discovering where we could find information about the right path to processing the application to be able to issue tax-deductible receipts.*

The lack of information available about the process was chief among the issues that have frustrated respondents in their efforts to obtain authorized donee status, as shown on the following chart. The majority of survey respondents reported that their organizations have not ever pursued authorized donee status because they did not have enough information about the process.

Survey responses reflect the difficulties CSOs experience when applying for authorized donee status. When asked whether they had ever applied for authorized donee status, 59 percent of the 829 respondents to the question answered affirmatively. In response to a follow-up question that asked whether the SAT eventually approved the application for authorized donee status, just 45 CSOs surveyed responded affirmatively; the majority of the remaining CSOs that participated in the survey did not respond to this follow-up question.



Notwithstanding recent efforts by the SAT to educate various ministries and standardize their processes for issuing accreditation letters, CSOs participating in this survey identify the accreditation letter as a particularly significant source of confusion and delay. Of the 422 CSOs that answered the survey question about obstacles encountered in soliciting the accreditation letter, 26 percent reported difficulties figuring out how to apply and 27 percent stated that the government office took over 90 days to respond to the request for an accreditation letter.

Among those CSOs whose applications for authorized donee status were rejected, 60 percent reported that the SAT required specific technical corrections; 20 percent stated that the SAT provided no explanation at all for rejecting the application; and another 20 percent asserted that the SAT's reasons for rejecting the application were misguided.

Some SAT officials agree that they should do more to make their guides and materials about the application process for becoming an authorized donee more accessible to CSOs; however, a lack of

resources - both financial and human - prevents the agency from undertaking additional activities. In contrast, INDESOL, the agency that governs CLUNIs, has undertaken an active campaign to educate CSOs about the process to become a CLUNI. In part, this may be explained by the different objectives of the two agencies. INDESOL views the promotion of CSOs as an integral part of its mission. The SAT, on the other hand, is focused on administration of the tax system; expanding the number of authorized donees who can receive tax-deductible donations is not a principal goal of the agency.

#### PROFESSIONAL SUPPORT

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**ISSUE:** When the *Fiscal Agenda* was drafted, many CSOs found it difficult to navigate the process to become an authorized donee without the assistance of legal or accounting professionals. This problem was compounded by the fact that there were not enough lawyers and accountants with knowledge of the fiscal framework for CSOs. Recognizing this problem, the *Fiscal Agenda* recommended training for such professionals to ensure that they have the appropriate knowledge to assist CSOs in this process.

**REFORM:** To address this problem, the SAT developed a registry of legal and accounting professionals to support authorized donees. In addition, the SAT offers continuing education classes for legal and accounting professionals on issues pertinent to authorized donees.

Despite these efforts, CSOs may still experience difficulties locating or affording a knowledgeable professional. Overall, close to 47 percent of respondents claimed that they changed legal or accounting advisors because they lacked necessary expertise. One focus group participant described the down side of free legal assistance in navigating the authorized donee application process:

*We tried [to apply for authorized donee status] over the course of three years without accomplishing anything. We were lucky to find a legal firm with a pro bono department that took on our case and resolved the application process in nine months. But some things happened that seemed illogical to me. What absolutely caught our attention is that in order to receive authorized donee status they eliminated some of the activities that appeared in our Charter, like cultural and recreational activities, despite the fact that Mexico has signed an international treaty in which it clearly states that disabled persons have the right to this type of activity. These disappeared from our Charter, although we continue to do them.*

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## REPORTING REQUIREMENTS

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**ISSUE:** The Promotion Law and the LISR require organizations subject to them to provide reports. However, the *Fiscal Agenda* noted that organizations are primarily required to report to the government. Organizations had limited obligations to provide information to the public. Making programmatic and financial information more accessible to the public could improve sectoral transparency and accountability.

**REFORM:** In 2007, the SAT introduced an online reporting mechanism for authorized donees in an effort to increase transparency. Authorized donees must submit reports in order to renew their authorized donee status. Reports submitted through this system are available to the public.

The online reporting system increases the accountability and transparency of authorized donees and provides useful information to the public. Many Mexicans, however, do not know about the website or are unable to access this type of technology. Moreover, at least one focus group participant complained that the on-line reporting system has proven to be unreliable in practice:

*We had always [submitted required reports] and never had a problem, but they [the SAT] told the accountant that everything was now on the Internet and that she had to do it on-line. She tried to do it on the Internet, and the system was always down. She returned to [the SAT] and they told her there was nothing they could do; that it had to be via Internet. And then the time for renewal ran out and they told her that there was no way to renew the status; that she had to apply all over again. And that's what we're doing now.*

**ISSUE:** Authorized donees with annual income above a certain amount are required to undergo an annual audit. The *Fiscal Agenda* noted that the limit should be higher, as the audit requirement placed an unreasonable burden on smaller CSOs.

**REFORM:** In an effort to reduce the administrative and financial burdens on authorized donees, the SAT substantially raised the threshold annual income for mandatory, and costly, external audits from 400,000 pesos to 2 million pesos in 2011.<sup>56</sup> This reform provides real relief for small and medium-sized authorized donees<sup>57</sup>, and removes one disincentive for CSOs that wish to apply for authorized donee status but are uncertain whether the potential to receive tax-deductible donations is sufficient to justify the associated costs.

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<sup>56</sup> *Resolución Miscelánea Fiscal para 2012*, Sec. I.2.15.1 (Dic. 2011)

<sup>57</sup> While ICNL's survey did not ask about the number of CSOs that would qualify for this relief, over 70 percent of survey respondents reported annual budgets less than 500,000 pesos.

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## FISCAL FRAMEWORK GOVERNING AUTHORIZED DONEES

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The fiscal framework governing authorized donees is very complex, leading to confusion among CSOs, donors, and other stakeholders about their rights and obligations.

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### TAX TREATMENT OF DONATIONS

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**ISSUE:** According to the *Fiscal Agenda*, many CSOs felt that greater tax incentives would encourage greater Mexican philanthropy.<sup>58</sup> At the same time, however, the GoM believed that tax exemptions for donations were too generous.

**REFORM:** Prior to 2007, an individual or corporation in Mexico could deduct 100 percent of the donations made to an authorized donee from gross taxable income. In 2007, however, Mexico introduced fiscal reforms, including the introduction of a flat tax (IETU) for both individuals and corporations. The IETU limits deductions for donations to organizations with authorized donee status to 7 percent of the donor's taxable income (utilidad fiscal) as set forth in the LISR.<sup>59</sup>

The charitable deduction was preserved in the flat tax only as a result of civil society representatives' efforts to educate the legislature about the importance of maintaining this incentive to donate. The GoM argued that the introduction of a flat tax necessarily brings with it the elimination of nearly all previously available exemptions and deductions. However, the legislature was persuaded by the evidence presented by civil society groups about both the need to preserve the tax deduction for donations to authorized donees and international examples of similar flat tax rates with deductions.

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### CROSS-BORDER DONATIONS

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**ISSUE:** According to the *Fiscal Agenda*, "The provisions regarding cross-border in-kind and cash donations are unclear, a situation which fosters arbitrary application of the related provisions and causes delays and complications, ultimately discouraging these donations." The situation regarding cross-border donations was complicated in 2002 when Mexico significantly restructured its Tax Code. Among the provisions that were relocated and renumbered was the LISR provision cited in the United States - Mexico Income Tax Convention to identify the category of CSOs eligible to receive cross-border, tax-deductible donations. Because the provision cited in the Convention no longer referred to authorized donees, US donors were unsure of their ability to claim a deduction for donations to such organizations.

**REFORM:** The Border Philanthropy Partnership, the International Community Foundation (ICF), and Fundación Internacional de la Comunidad (FIC) worked with a member of the Mexican Congress, Lic. Carlos Torres Torres from Baja California, to produce and publish a bilingual guide that explains the tax treatment of cross-border in-kind donations to authorized donees.

In addition to this guide, the SAT published an opinion letter in 2008 clarifying the provisions of the LISR affecting cross-border donations with the United States. With this letter, the SAT confirms that

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<sup>58</sup> See *Fiscal Agenda*, p. 55.

<sup>59</sup> See Flat Tax Law § 5(VIII), LISR § 31.

Mexican authorized donees are equivalent to the class of CSO identified in the United States - Mexico Income Tax Convention.<sup>60</sup> This means that US donors can make tax-deductible donations to such organizations, thereby reestablishing a useful incentive for US donors to support Mexican authorized donees.

Despite the reforms related to both the tax treatment of donations and cross-border donations, some stakeholders still struggle to understand the fiscal framework. Of the CSOs surveyed, 39.6 percent reported that their organizations' staff had little knowledge of the tax laws governing CSOs, and 6.8 percent reported that they have no knowledge at all about the tax laws governing CSOs in Mexico.

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## B. PUBLIC FUNDING

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**ISSUE:** The criteria for accessing public funds vary dramatically from ministry to ministry. According to the *Fiscal Agenda*, "creating uniformity of criteria for access and operating rules for public funds available to CSOs from a variety of ministries and public institutions is necessary in order to ensure equity in distribution of such funds."<sup>61</sup> Very few organizations receive public funding.

**REFORM:** Some ministries, including the Ministry of Social Development, SEDESOL, have adopted uniform criteria for funding applications. These ministries have also adopted a streamlined system to process applications from CSOs seeking eligibility to receive government funding and have extensively overhauled their websites to provide applicants and the public with much more information about the process to receive funding, among other improvements. For example, CSOs with CLUNIs are able to apply for funding entirely through the INDESOL website.

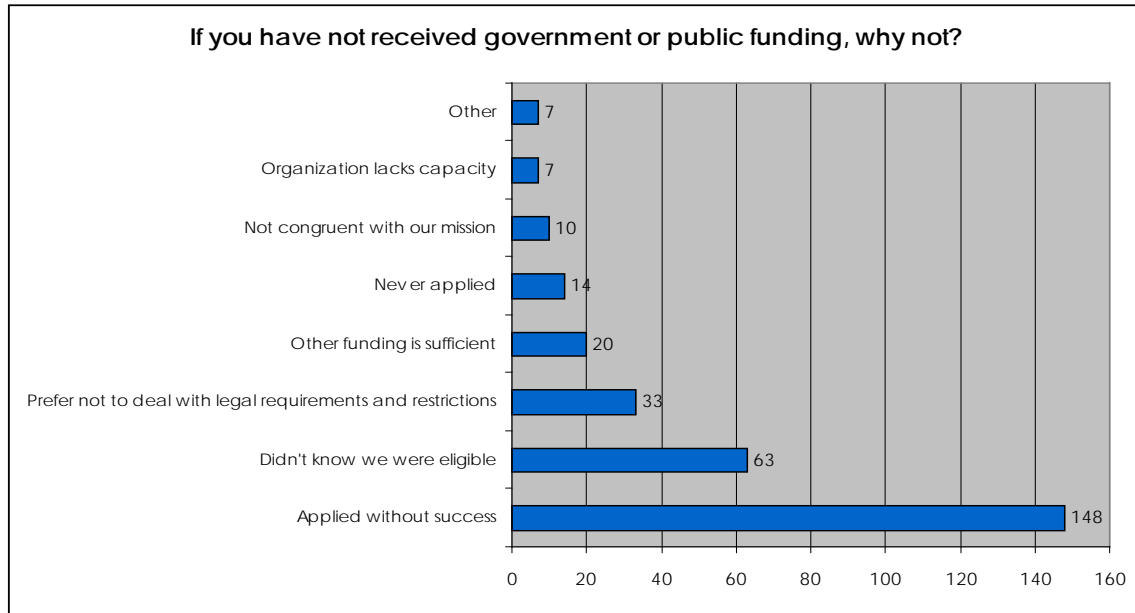
Even with these improvements, over 40 percent of respondents stated that they do not receive government funding. As the chart below indicates, of the respondents that have not received public funding, 57.8 percent reported that they had attempted to receive public funds without success, 25 percent said that they did not know that they were eligible, and 13 percent said they did not want to have to deal with the legal requirements and restrictions that come with public funding.

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<sup>60</sup> See, for example, SAT letter 600-04-05-2008-74888, Exp. 243, Reg. 13818/08 to the Instituto Tecnológico Autónomo de México, July 4, 2008.

<sup>61</sup> *Fiscal Agenda*, p. 56.





### C. ECONOMIC ACTIVITY

**ISSUE:** As the *Fiscal Agenda* stressed, the creation of a strong, independent, and vibrant CSO sector depends in part on the ability of CSOs to access diversified funding sources. In addition to grants and donations, these include membership dues, investment income, and income from economic activities. Economic activities can be defined as “regularly pursued trade or business involving the sale of goods or services.”<sup>62</sup>

According to international best practices, CSOs should be allowed to engage in and earn income from economic activities as a means of supporting their missions. Of course, the law usually sets limits on the extent to which a CSO may engage in economic activity. The most basic restriction included in most laws governing CSOs around the world is the non-distribution provision, which states that CSOs may earn a profit, but are prohibited from distributing that profit to any individuals, including members, founders, officers, and employees. Thus, all profits must be used to support the CSO’s operations. In some cases, the laws permitting CSOs to engage in economic activities may also impose an express limitation that a CSO only use the income to support its statutory goals. Further limitations may include, for example, that the economic activities be related to a CSO’s mission, or that the economic activities be incidental or accessory to the mission.

The income derived from economic activities is a critical source of income for Mexican CSOs.<sup>63</sup>

<sup>62</sup> *Survey of Tax Laws Affecting Non-Governmental Organizations in Central and Eastern Europe, 2nd edition*, p. 16 (ICNL: 2003).. Note that what constitutes economic activity is frequently undefined in countries’ laws.

<sup>63</sup> See Michael Layton, “Philanthropy and the Third Sector in Mexico: The Enabling Environment and Its Limitations,” *NORTEAMÉRICA*. Year 4, number 1, January-June 2009, p. 99; see also JHU study and *Fiscal Agenda*.



### Sources of Income for Mexican CSOs

The majority of CSOs surveyed for this study, 57.2 percent, reported that they sell products or charge fees for services. Of those CSOs that do not sell products or charge fees for their services:

- 42.5 percent believed that such economic activities would be inconsistent with their missions;
- 32.3 percent reported that they did not have the organizational capacity to do so; and
- 16.3 percent reported that they did not want to deal with the tax consequences related to selling products or charging fees for services.

**REFORM:** A 2010 amendment to the tax law permits authorized donees to earn income from economic activities unrelated to the purpose for which they are authorized to receive tax-deductible donations.<sup>64</sup> This income will not be taxed unless it exceeds 10 percent of the organization's total income. Income from unrelated economic activity that exceeds 10 percent of the organization's total income will be taxed at the current corporate rate.<sup>65</sup>

Passage of this amendment was controversial. Many in the CSO community interpreted the law before amendment to permit an authorized donee to earn income from unrelated economic activities so long as it did not constitute "a substantial part of its income,"<sup>66</sup> which some CSOs interpreted to mean up to 49.9 percent of their income. They thus perceived the amendment as a new limitation on the amount of tax-free income they could earn from unrelated economic activity. The amended law has also been criticized because it does not clearly define what is considered related and unrelated business activities. The law is also silent on how to calculate the 10 percent limit. For these reasons, some Mexican authorized donees argue that identifying and taxing unrelated income has placed new administrative and financial burdens on them.

As a result of an advocacy campaign by civil society groups, the office of the President granted a two-year tax holiday on the amount earned above the 10 percent limit until December 2013.<sup>67</sup> It is not yet clear what impact this amendment will have once implemented.

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<sup>64</sup> LISR Art. 93. LISR Article 93 also provides that authorized donees are not required to pay income tax on economic activities that are related to the objectives for which they were granted authorized donee status. Distinguishing between related and unrelated activities, however, can be complicated for both CSOs and the SAT.

<sup>65</sup> Corporate tax rate for 2012 is 30 percent. See LISR regulations 2012.

<sup>66</sup> Interviews with M. Layton and C. Castro (September and November 2011).

<sup>67</sup> Presidential Decree of May 2010 extending stimulus tax holiday until December 2013, available at:

[http://dof.gob.mx/nota\\_detalle.php?codigo=5213835&fecha=12/10/2011](http://dof.gob.mx/nota_detalle.php?codigo=5213835&fecha=12/10/2011).

## IV. REMAINING OBSTACLES AND RECOMMENDATIONS

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Although a number of reforms have been implemented to strengthen civil society since 2007 when the *Fiscal Agenda* was published, several obstacles remain to fostering a strong, independent, and financially sustainable civil society sector in Mexico.

### A. HARMONIZATION OF THE LAWS AND POLICIES OF THE FISCAL FRAMEWORK

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The fiscal framework in Mexico is made up of complicated laws and policies that are often contradictory, making it very difficult for stakeholders to identify their rights and obligations under the law and to take advantage of existing benefits. In addition, the fiscal framework is not consistently applied. In particular, the lack of harmonization between the LISR and the Promotion Law, as well as other laws affecting CSOs, results in gaps and overlaps that leave CSOs vulnerable to unintended missteps and selective enforcement. For example, the Promotion Law recognizes CSOs that foster economic development as in the public interest; however, these same groups are not eligible for authorized donee status under the LISR. A coalition of CSOs called Fortaleciendo Causas Ciudadanas (Strengthening Citizens' Causes) contends that CSOs dedicated to the promotion of civic participation, consumer rights, freedom of expression and the press, strengthening other CSOs, or promoting education fall outside of the definition of not-for-profit legal entities set forth in Title III of the LISR and are therefore not eligible for fiscal incentives, including authorized donee status.<sup>68</sup>

Piecemeal legislative reform efforts designed to address the lack of consistent treatment of categories of CSOs across these separate laws have unfortunately compounded the confusion. For example, the Mexican legislature adopted a provision in the 2012 Revenue/Budget Act that allows organizations eligible to receive benefits under the Promotion Law also to receive tax-exempt status temporarily under the LISR.<sup>69</sup> In effect, this provision harmonizes the two eligibility regimes for the purposes of income tax exemptions during fiscal year 2012 only. Some organizations argued that, in addition to extending tax-exempt status to CSOs eligible under the Promotion Law, this temporary provision also permits Promotion Law-eligible organizations to apply for authorized donee status, with the corresponding tax incentives for donations. During the implementation of this study, ICNL spoke with one of the drafters of the temporary provision, Roberto Cantu. Mr.

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<sup>68</sup> See July 13, 2012 Press Release, *Organizaciones de la sociedad civil reiteramos al SAT nuestra demanda para que amplié el régimen de donatarias autorizadas* (available at: <http://www.causasciudadanas.org/2012/07/comunicado-de-oscs-para-el-sat-sobre.html>). Some of these assertions are not easily reconciled with the *letter* of recent reforms. For example, CSOs promoting civic participation are eligible to apply for authorized donee status, though they are required to first enter into an agreement with a government agency to carry out a particular activity. (See *Resolución Miscelánea Fiscal para 2012*, Sec. 1.2.15.1 (Dic. 2011).) Similarly, CSOs dedicated to human rights are eligible for authorized donee status, and freedom of expression and the press are fundamental human rights that would seemingly fall within that category. It may be that the SAT is interpreting the authorized donee eligibility provisions strictly, and that *in practice*, CSO statutes are deemed ineligible if they specify promotion or defense of a particular right rather than human rights in general. It is also possible that CSOs are not aware of the recent reforms regarding eligible activities.

<sup>69</sup> The 2012 Revenue/Budget Act includes a provision that says that all organizations that undertake activities listed under Article 5 of the Promotion Law will be considered Public Assistance Institutions for purposes of Article 95 of the Income Tax law for fiscal year 2012. See *Causas Ciudadana: Promueven ampliar regimen de donatarias autorizadas en Ley de Ingresos de la Federación 2012* available at: <http://www.causasciudadanas.org/2011/10/dictamen-ley-de-ingresos-de-la.html>.

Cantu said that the legislative intent was only to extend tax-exempt status to the additional organizations – not to make them eligible to become authorized donees.<sup>70</sup> As a practical matter, observers have noted that this expansive interpretation of the recent reform has not been pursued; as of May 2012, only one CSO has reportedly applied for authorized donee status citing the law.<sup>71</sup>

Without a clear legal framework, stakeholders do not have a clear understanding of their rights and obligations under the law. Consistency and certainty are needed in all areas of the legal framework to ensure greater acceptance of the rule of law by citizens. Clear and simple laws and policies agreed to and known by all parties could dramatically improve the fiscal framework and the overall legal environment for CSOs by making the application of the law less arbitrary. Therefore, a comprehensive reform effort to amend the LISR is needed to resolve this problem, as the temporary efforts taken so far only act to compound the problem.

## B. STANDARDIZATION AND SIMPLIFICATION OF ADMINISTRATIVE PROCEDURES

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While much has been done to simplify administrative procedures related to the process of becoming and remaining an authorized donee, additional obstacles remain. Two significant issues that were identified in the *Fiscal Agenda* have not yet been addressed: the extremely low 5 percent cap on administrative expenditures and the nebulous accreditation process necessary to obtain authorized donee status.

*Administrative Cap:* Article 110 of the Income Tax Law Regulations (RISR) establishes that in no case may an authorized donee cover administrative costs using more than 5 percent of its tax-deductible donations and any interest income derived from these donations. An authorized donee may cover administrative costs without limitation using income from sources other than donations (for example, income from economic activity or public funding). In essence, the administrative cap unfairly penalizes authorized donees that are successful in raising a significant portion of their income from tax-deductible donations.<sup>72</sup>

An additional problem stems from the fact that the definition of administrative expenses is awkwardly drafted and contains a lengthy and non-exclusive list including rental fees, office products, utilities, taxes, and legal fees, while also noting that payments necessary to fulfill the authorized donee's social objectives fall outside of the definition.<sup>73</sup> This vague definition has led to a great deal of confusion among CSOs about what they should classify as administrative expenses. It

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<sup>70</sup> ICNL interview with Roberto Cantu, November 2011 (Mexico City).

<sup>71</sup> ICNL interview with SAT officials, June 2012 (Mexico City).

<sup>72</sup> Although only 5 percent of survey respondents are authorized donees and therefore affected by this restriction, over a third (35.5 percent) of respondents listed donations from individuals as a primary source of funding.

<sup>73</sup> For the purposes of this provision, administrative costs considered to fall within this non-exclusive list are those related to office and administrative expenses: remuneration of personnel; renting property and furniture; telephone; electricity; paper products; maintenance and conservation; federal and local taxes and rights; and legal contributions and fees. Payments that the authorized donee must make to fulfill its social objectives directly fall outside of the definition of administrative expenses.

is not clear, for example, whether payments to administrative personnel, external auditors, institutional capacity building consultants, or other expenses that might help strengthen an authorized donee would fall within the definition of administrative expenses. Some CSOs find it difficult to cover such costs, along with other listed administrative expenses, while respecting the 5 percent cap.

The authorities argue that the 5 percent limit was established to prevent abuses by CSOs. However, the low ceiling on administrative expenses, combined with the complexity of deciding whether to categorize expenses as administrative, imposes a tremendous burden on CSOs. Some CSOs argue that decisions about limits on expenditures devoted to administrative activities should be made by individual organizations' management and donors. Ultimately, insistence on this unrealistic limit serves to undermine CSO compliance with the letter of the law. The government and CSOs would both be well-served by re-examining the need for this requirement. If they choose to retain a cap on administrative spending, those costs should be clearly defined, and the limit should be compatible with sound CSO administrative practices.

*Accreditation Letter:* To verify that a CSO does in fact undertake the activities for which it seeks authorized donee status, the SAT requires CSOs to obtain a letter of accreditation from a qualifying government agency, in which the agency affirms that the CSO conducts the activities. This system was put in place because the SAT lacks the expertise and resources to investigate applicants that assert statutory objectives corresponding to a broad range of eligible activities. However, there is no universal criterion for the issuance of the accreditation letter; thus, the process – along with costs and delays – varies from agency to agency.

There may be alternatives to the accreditation letter that more efficiently accomplish the goal of preventing tax-deductible donations to ineligible CSOs. The tax authorities of many countries rely on periodic reporting regarding programs, activities, and expenditures to ensure that public benefit organizations continue to carry out public benefit activities.

The SAT could thus consider eliminating the accreditation letter requirement altogether. Rather than devoting scarce resources to attending to accreditation requests, agencies could inform the SAT if, during their routine oversight activities, they learn that an authorized donee is not carrying out eligible activities.

If the accreditation letter requirement is maintained, then the government and CSOs could identify agencies with good practices in handling the accreditation process, and promote adoption of similar processes among all issuing agencies.

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### C. STAKEHOLDER CAPACITY BUILDING

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Study participants pointed to the lack of stakeholder capacity – particularly among CSOs and the government – as the source of a number of obstacles.

- Many CSOs operating in Mexico do not have the tools or resources needed to operate a successful organization, and operate with very limited staff. Under-resourced organizations

may find it difficult to learn about the regulations that govern their rights and obligations, develop appropriate administrative structures, and implement effective institutional assessments and evaluations of their work, among other things.

CSO survey respondents cited a lack of institutional capacity as the primary reason for not developing fundraising initiatives that target the public. Of the CSO respondents that reported no fundraising activities, the main reasons for failing to pursue such initiatives included a disinclination to deal with the associated legal requirements (42 percent) and a lack of fundraising capacity within their organizations (33 percent).

Investing in the capacities of CSOs could benefit donors as well as CSOs and beneficiaries. While donors benefit from more capable and reliable partners on the ground, CSOs benefit from needed capacity and institution building. Longer-term donor commitments to CSOs could also translate into longer-term engagement between CSOs and their beneficiaries.

CSOs have need for training on legal issues, management, accounting, and evaluation. This could include joint training and capacity building events, establishment of forums for consultation and dialogue, and scaling up partnerships between local governments and CSOs. There are already a number of CSOs that have implemented training programs, including Fortalece Legal, a CSO dedicated to training CSOs and law students in the laws governing the sector. Other CSOs, including Alternativas y Capacidades, as well as universities, including Universidad Iberoamericana and the Instituto Tecnológico y de Estudios Superiores de Monterrey (ITESM), have introduced similar courses covering the laws governing CSOs. Such efforts could be expanded. The SAT might also consider organizing regional workshops to explain the fiscal reforms for authorized donees to CSOs across the country and encourage organizations to participate in them.

- At the same time, government regulators, including the SAT, lack adequate resources to effectively implement and enforce the laws. Several stakeholders, including focus group participants, pointed to the lack of capacity among government regulators - the SAT specifically - as a reason for the widespread confusion among CSOs and other stakeholders about the fiscal framework. Although the SAT has taken important steps to improve its capacity to effectively regulate authorized donees, the agency is not adequately equipped with personnel or resources to ensure compliance with its own rules.<sup>74</sup> As an example, the SAT made a number of improvements to the authorization process, as previously discussed, which reduced its response time to applications for authorized donee status dramatically. However, as noted above, the number of applicants for authorized donee status has increased in recent years. This trend is continuing, suggesting that the SAT's capacity may soon face strains. The SAT's capacity must be expanded so it can implement the laws governing authorized donees more effectively.
- Another obstacle that stakeholders have consistently identified is the lack of lawyers and accountants knowledgeable about issues affecting the sector and available to provide advice

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<sup>74</sup> Interview with SAT officials.

about navigating the fiscal framework. Nearly half - 46.7 percent - of CSOs surveyed reported that they have had to change their legal or accounting advisors because of their lack of knowledge.

Although the SAT has instituted continuing education workshops for these professionals, the number of qualified professionals willing to support CSOs is still too small. A number of professionals who participated in the focus group cited the lack of knowledge of CSO-related issues as one reason why there are so few professionals that assist CSOs; however, they also noted their belief that professionals are not able to make a sustainable living working in this area.

The SAT should continue to take steps to educate experts like notaries about the process for becoming an authorized donee in order to ensure that they have the appropriate knowledge to assist CSOs. Several CSOs, including the Appleseed Foundation and the Cyrus Vance Center for International Justice, independently support programs to encourage lawyers to offer pro bono services to CSOs in Mexico.<sup>75</sup> New training efforts focusing on authorized donee status could build on existing programs that encourage lawyers to offer pro bono services to CSOs with the aim of ensuring that volunteer lawyers are well-prepared to address this issue.

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#### D. GOVERNMENT-CSO ENGAGEMENT

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Some groups of CSOs collaborate effectively with policy makers and positive steps have been taken to improve engagement between CSOs and the government. For example, there are some institutionalized mechanisms to foster communication between CSOs and the government, like the Technical Council established under the Promotion Law. However, both the government and CSOs agree that there should be more frequent and constructive dialogue between the two sectors. In addition, the number of CSOs engaged in such dialogue should be expanded. As a result of long-held opinions, government and some CSOs have a weak understanding about each other's objectives and activities. The absence of a consistent government policy towards civil society, reflected in the inconsistent definitions of public benefit organizations in the Promotion Law and the LISR, compounds misunderstandings between CSOs and government officials. One focus group participant remarked on the sometimes tense relationship:

*People in the Third Sector often feel persecuted or as tax delinquents because they start with good intentions, wanting to help, and the government accuses them of tax crimes...*

While full consensus between government officials and civil society is an unrealistic goal, misunderstandings rooted in lack of communication could be overcome. In order to improve CSO-government engagement, leaders from both sectors could explore creative options for dialogue. Existing mechanisms, such as the Technical Council and the Private Assistance Boards, should be

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<sup>75</sup> See, for example, Red Pro Bono Mexico at: <http://probono.org.mx>.



strengthened to promote dialogue between the sectors, but other avenues should also be created to increase engagement. CSO and government representatives might build on the experience of multi-sector working groups to address discrete issues, for example, how best to address the requirement of an accreditation letter for authorized donee applicants – a requirement that has been administered differently by various government agencies.<sup>76</sup> The working groups could identify best agency practices and document the costs and benefits of the requirement for CSOs, the SAT, and the accrediting agencies. The dialogue might not lead to elimination of the requirement, but it could contribute to a more accurate understanding of its impact across the CSO sector. Such efforts should seek to engage a broad number of CSOs and government officials.

## E. WEAK PUBLIC IMAGE OF CSOS

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As a sector, CSOs in Mexico suffer from a weak public image. In a CIVICUS/Cemefi study, 54.6 percent of CSOs surveyed said that cases of corruption among civil society are “frequent,” or “very frequent.”<sup>77</sup> Half of the CSOs surveyed for this study cited the public’s negative perception of CSOs as a reason for the relatively low level of donations made to civil society in the country. In addition, there is “a limited understanding of what civil society organizations do, what their aspirations are, and what impact they can have in the promotion of equitable development in Mexico and in the world.”<sup>78</sup> As a result of this negative public image, many potential Mexican donors – both individuals and institutions – do not support CSOs.

Further exacerbating the problem, CSOs are not recognized for the valuable work they do. The 2008 ENAFI survey found that 92 percent of Mexicans said that neither they nor anyone in their families “received support from a foundation or charity or any nonprofit institution.” In fact, CSOs channel more than 1.4 billion pesos a year to social projects.<sup>79</sup> In some fields, such as assisted living facilities for the elderly, CSO representatives argue that services provided by the sector far surpass those provided by the federal government. It appears, then, that many Mexican citizens fail to associate particular service providers with the civil society sector. This weak public image makes it difficult for CSOs to recruit volunteers, attract donations, and influence public policy.

CSOs must improve the reputation of the sector, as well as of individual organizations, by disseminating information about the value and impact of the sector’s work. CSOs have started to analyze data that shows the tremendous impact they have on Mexico’s development. However, this data has not been disseminated widely. To improve the sector’s public image, CSOs must conduct research and disseminate data and information to donors, policy makers, and the public about the positive impact they have on Mexican society.<sup>80</sup>

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<sup>76</sup> See discussion on page 32.

<sup>77</sup> CIVICUS Civil Society Index Analytical Report for Mexico, p. 49.

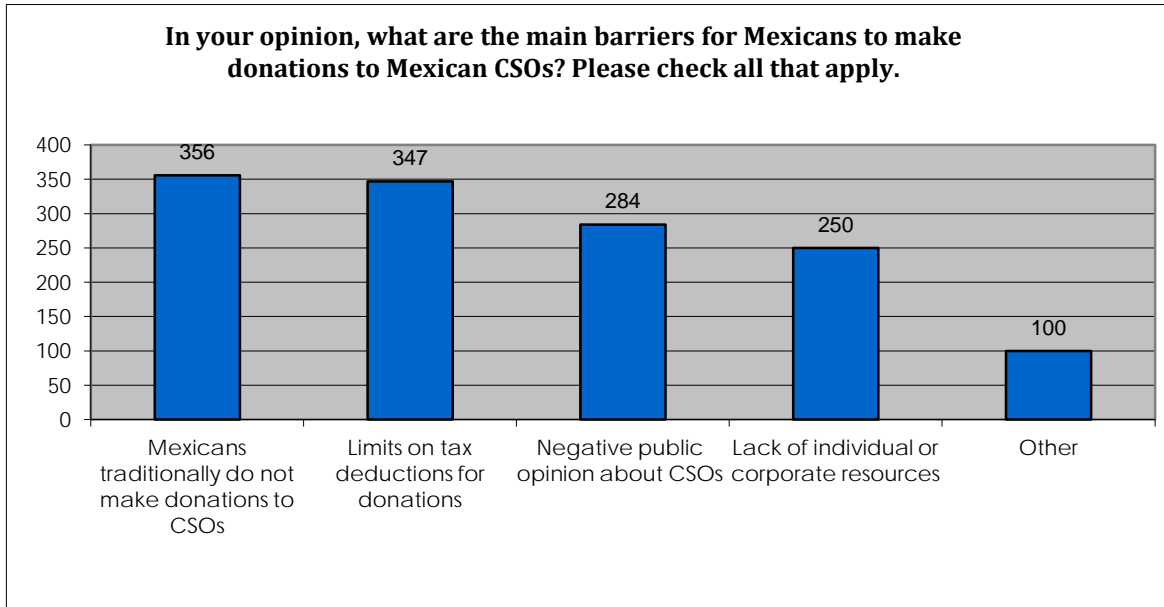
<sup>78</sup> Michael Layton, “Flat Taxes, Santa Claus, and Charity: The Need to Strengthen Civil Society in Mexico,” *International Journal for Not-for-Profit Law* Volume 9, Issue 4, August 2007.

<sup>79</sup> *Fiscal Agenda*, p. 17. See also *Las organizaciones de la sociedad civil en la legislación mexicana*.

<sup>80</sup> See Michael Layton, “Philanthropy and the Third Sector in Mexico: The Enabling Environment and Its Limitations,” *NORTEAMÉRICA*. Year 4, number 1, January-June 2009.

## F. PHILANTHROPIC CULTURE IN MEXICO

Throughout this study, stakeholders have identified the lack of a formal philanthropic tradition in Mexico as one of the principal barriers to CSO financial sustainability.<sup>81</sup> The Johns Hopkins University (JHU) Comparative Nonprofit Sector Project study found that the level of domestic philanthropy in Mexico was exceptionally low compared to other countries studied. At just 0.04 percent, Mexico dedicated the lowest percentages of GDP to philanthropy of all countries studied.<sup>82</sup> Among the close to 570 respondents to a question in ICNL's survey, over 60 percent claimed that Mexicans do not traditionally donate to CSOs, as seen in the following chart.



Even at the highest levels of government and society, the effectiveness of philanthropy is often questioned. President Calderón has said that “Social justice must come before charity as a cardinal virtue and philanthropic actions are not sufficient to meet the challenge of reducing poverty and inequality in Mexico.”<sup>83</sup> Carlos Slim, the richest man in Mexico and the world (according to Forbes Magazine), has said about his philanthropic vision:

*“Our concept is more to accomplish and solve things, rather than giving; that is, not going around like Santa Claus.... Poverty isn't solved with donations.”<sup>84</sup>*

The nature of Mexico's philanthropic culture is likely shaped by the pervasive distrust that exists at a societal level in the country. The recent spike in violence associated with drug trafficking has only

<sup>81</sup> Id., p. 103-105.

<sup>82</sup> Volunteering and giving as a share of GDP by country, 1995-2002, (Data includes charitable giving only; it does not include gifts to religious worship organizations), available at: [http://ccss.jhu.edu/wp-content/uploads/downloads/2011/10/Comparative-Data\\_2004\\_FINAL.pdf](http://ccss.jhu.edu/wp-content/uploads/downloads/2011/10/Comparative-Data_2004_FINAL.pdf).

<sup>83</sup> Michael Layton, “Flat Taxes, Santa Claus, and Charity: The Need to Strengthen Civil Society in Mexico” citing “Inconforma a FCH queja de filántropos,” Reforma (Mexico City), July 6, 2007.

<sup>84</sup> Id., citing “Billionaire Pokes Fun at Philanthropy,” Mexico City, March 13, 2007 (Associated Press), <http://www.cbsnews.com/stories/2007/03/13/business/printable2563316.shtml>.



made the situation worse. Mexicans have been “left increasingly unsure [about] who among their neighbors, co-workers and other fellow citizens might have criminal ties.”<sup>85</sup> The 2008 ENAFI study found that just 14 percent of respondents had high levels of trust in their co-workers, while 30 percent reported “little” or “none.”<sup>86</sup> According to surveys conducted in 2008 in the 34 nations of the Organization for Economic Cooperation and Development, a group that includes most of the world’s biggest economies, Mexico ranked near the bottom in the percentage of citizens who “express high levels of trust in others.”<sup>87</sup> This low level of trust applies to the CSO sector as well. The 2008 ENAFI study shows that 57 percent of respondents had little or no confidence in CSOs.<sup>88</sup>

In addition, some donors continue to provide charitable contributions to groups that are not authorized donees. A recent study about Corporate Social Responsibility (CSR) practices by Alternativas y Capacidades and ITAM found that only half of surveyed companies require CSOs to be authorized donees as a condition for granting donations, and many corporate donors do not even require grantees to be legally formed entities, implying that current tax incentives do not seem to figure prominently into the practices of roughly half of surveyed donors.<sup>89</sup>

Finally, it is clear that many donors are simply unaware of the incentives available to them. According to the ENAFI study, only a third of respondents knew of available incentives, and only 4 percent actually took advantage of them.<sup>90</sup> Given the above, CSOs may not have the necessary incentives to undertake the extra work to become a legal entity or to apply for authorized donee status, especially considering the burden of complying with the laws and regulations.

In order to promote a culture of giving among Mexican citizens and corporations, a three-pronged approach is necessary. First, incentives for donors should be expanded. Although only half of corporate donors currently take advantage of tax incentives for donations to authorized donees, limits on tax deductions for donations are seen by many as an important barrier to donations, as the chart on page 37 indicates. Second, donors and potential donors must be educated to increase awareness of fiscal incentives. In particular, understanding of the authorized donee system must be increased among both CSOs and donors in order to increase its perceived value. In addition, it is likely that US-based donors and potential donors are uninformed about the 1994 United States - Mexico Income Tax Convention. They might shift their giving practices to donate – or donate more – to Mexican authorized donees if they knew of the tax benefits available to them. CSOs should make

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<sup>85</sup> Nick Miroff, “For Mexico’s Middle Class, Drug War Deepens Trust Deficit”, Washington Post, June 1, 2012. [http://www.washingtonpost.com/world/the\\_americas/for-mexicos-middle-class-drug-war-deepens-trust-deficit/2012/06/01/gIQAePtU7U\\_print.html](http://www.washingtonpost.com/world/the_americas/for-mexicos-middle-class-drug-war-deepens-trust-deficit/2012/06/01/gIQAePtU7U_print.html).

<sup>86</sup> 2008 ENAFI survey, question 33.

<sup>87</sup> ESS (European Social Survey); ISSP (International Social Survey Programme); OECD (2008), Growing Unequal? Income Distribution and Poverty in OECD Countries ([www.oecd.org/els/social/inequality](http://www.oecd.org/els/social/inequality)), available at [http://www.oecd-ilibrary.org/sites/soc\\_glance-2011-en/08/01/g8\\_co1-01.html?contentType=&itemId=/content/chapter/soc\\_glance-2011-26-en&containerItemid=/content/serial/19991290&accessItemIds=/content/book/soc\\_glance-2011-en&mimeType=text/html](http://www.oecd-ilibrary.org/sites/soc_glance-2011-en/08/01/g8_co1-01.html?contentType=&itemId=/content/chapter/soc_glance-2011-26-en&containerItemid=/content/serial/19991290&accessItemIds=/content/book/soc_glance-2011-en&mimeType=text/html).

<sup>88</sup> 2008 ENAFI survey, question 43k.

<sup>89</sup> Michael Layton, “Philanthropy and the Third Sector in Mexico: The Enabling Environment and Its Limitations”, p. 101,” <http://www.cisan.unam.mx/Norteamerica/pdfs/n07/n0704.pdf> citing Carrillo Collard, Patricia, Michael D. Layton, and Monica Tapia, 2008, “Filantropía Corporativa ‘a la mexicana’,” *Foreign Affairs en Español*, vol. 8, no. 2.

<sup>90</sup> 2008 ENAFI survey, question 39.

an effort to educate current and potential donors about the benefits provided to them by the treaty. Third, it is critical to increase understanding of the impact and diversity of the sector in order to build trust. Without this social capital, organizations will continue to struggle for financial sustainability.

## V. CONCLUSION

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ICNL hopes that this assessment will be helpful to stakeholders evaluating the impact of Mexico's fiscal reform agenda. We further hope that it will inform continued fiscal reforms to improve the sustainability of CSOs and promote increased philanthropy.

