



U.S.-Mexico Chamber of Commerce Mexico Tax, Legal, Fiscal and Supply Chain Update

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Mexico Subcontracting Reform

- Major change in the Mexican labor landscape, materially affecting:
 - Dual company structure (operating entity with no employees and separate related personnel entity)
 - Outsourcing companies (like Manpower, Kelly Services, etc.)
 - Profit Sharing

Mexico Subcontracting Reform

- The Reform amended various laws, including the Federal Labor Law, the Social Security and the Workers Housing Fund laws, the Tax Code, the Income Tax Law, and the Value Added Tax Law.
- Most of its provisions took effect on September 1, 2021, but many companies are still figuring out whether the Reform affects them, and, if so, how to comply with it. Sometimes contractual parties have opposite views on the subject.

Mexico Subcontracting Reform

Dual company structure

- For decades, multiple companies used dual company structures (operating entity with no employees and separate related personnel entity), primarily for profit sharing purposes.
- Many of these structures disappeared because the Reform prohibits the "subcontracting of personnel", defined as "one individual or entity providing to, or placing at the disposal of, someone else, the employees of the former for the benefit of someone else".

Mexico Subcontracting Reform

- However, the "subcontracting of specialized services or specialized works" is permitted, provided that the service provider registers with a new registry (REPSE) and complies with certain obligations to provide information evidencing compliance with employee-related labor and tax obligations on a periodic basis; and the specialized services are not included in the service recipient's corporate purpose or main economic activity.
- The service recipient is also required to verify that the service provider is complying with its relevant employee-related labor and tax obligations.

Mexico Subcontracting Reform

- The above required labor force restructurings in many companies because the personnel companies frequently performed the core activities of the service beneficiary, which is now prohibited. In many cases, the employees of the personnel entity were transferred to the operating entity, becoming entitled to receive profit sharing based on the profits of the operating entity.
- "Shared services" among related companies are considered specialized services, thus permitted if they comply with the above requirements.

Mexico Subcontracting Reform

Outsourcing companies (like Manpower, Kelly Services, etc.)

- Similarly to the case of companies with dual company structures, multiple companies outsourced various components of their labor force, sometimes including the employees that performed their core activities.
- These structures also had to be revisited because of the Reform's prohibition of the "subcontracting of personnel", resulting in the transfer of the employees that performed the core activities of the service recipient to that company. It also resulted in:

Mexico Subcontracting Reform

- The registration of the outsourcing companies with the REPSE;
- Amending the corporate purpose provision of the bylaws of many companies;
- Revising the contracts between service providers and service recipients; and
- Creating an internal infrastructure to ensure compliance with the new rules.

Mexico Subcontracting Reform

Profit sharing

- On the positive side, profit sharing is now capped at three months of salary, or the average profit sharing received by each employee during the preceding three years, whatever is more beneficial for the employee.
- It is still necessary to calculate profit sharing as usual, based on 10% of the taxable earnings of the employer. However, if the amounts to be distributed to each individual exceed the above caps, the caps will apply.

Mexico Subcontracting Reform

Potential consequences of not complying with the Reform

- Labor and tax fines
- Non-deductibility of payments for income tax purposes, and the inability to recover value added tax paid
- Criminal liability for tax fraud

Mexico Subcontracting Reform

Some issues that are still creating confusion

- Some companies take the position that practically all services need to meet the requirements applicable to specialized service providers (REPSE registration, etc.)
- The REPSE guidelines exacerbated the confusion adding to the statutory requirements.
- Characterizing something as specialized services results in joint liability for the service recipient if the service provider doesn't meet its labor and tax obligations with respect to its employees that provide the services to the service recipient.

Mexico Subcontracting Reform

- When the service provider or the service recipient is not a resident of Mexico.
- If the proper analysis is not performed, the conclusion might be that some companies may no longer do business in Mexico, or that it's necessary to radically change their business model.



Thank You!

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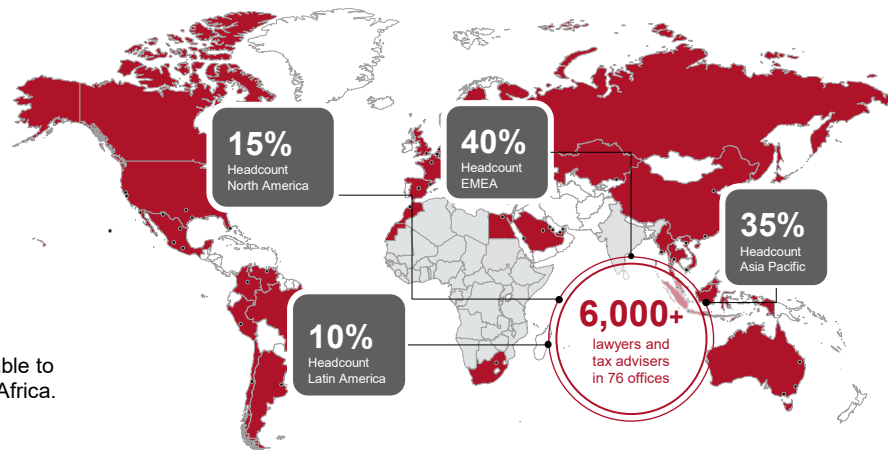
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Note: Headcount as of December 31, 2021

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Band 1 Ranking
COMMERCIAL CONTRACTS
2015-2020 CHAMBERS GLOBAL