AMENDMENT REGARDING OUTSOURCING

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On April 23, the outsourcing amendment has been approved by the Chambers of the Mexican Congress.

Such amendment has been in controversy among the three main actors that are taking part in such bill (the government -including the members of the Chambers- the employees -mainly represented by the Unions- and businessmen -mainly represented by the bodies of the "business groups").

Such process has passed different instances, from the corresponding amendment project by the federal executive power to the Mexican Congress, until it was approved, passing by an "open parliament", the analysis of different scholars and intense negotiations between the government, unions, and the businessmen, until such process was completed with the approval of this law, which is described throughout this document in which we have highlighted the most relevant parts of this law.

We start emphasizing that this initiative affects the following laws with different provisions, which makes of it an amendment that must be fully analyzed through different sections, as we will discuss, it will affect the labor, corporate, social security scope (including the right to the workers' dwelling), and tax matters, as the following laws are amended:

a) The Federal Labor Law;
b) The Social Security Law;
c) The Mexican Fund Institute for Workers' Dwelling;
d) The Federal Tax Code;
e) The Income Tax Law; and,
f) The Value-Added Tax Law.

Before starting the analysis of each highlighted element of this amendment, it is worth mentioning that the effective date is within a short term, which will make that companies should accelerate their response with the need to adapt or change several scopes of such companies, such as: corporate purposes of companies, different budget and payroll control systems of the companies, carry out several processes before different authorities, review of the of the different agreements, adapt systems to obtain information from the specialized service providers, determine financial impacts of affected companies, negotiation with unions, among others.

Due to the foregoing, we will start with the analysis of such amendment by each one of the Laws that were affected:

The Federal Labor Law

(referred to as the "LFT" due to its acronym in Spanish)

Express prohibition of outsourcing, except for specialized services

We think that one of the most relevant amendments done in this initiative, is the express prohibition included in the LFT[1] of the outsourcing of personnel under general terms, specifically excluding from such term (the outsourcing) the provision of specialized services or the performance of specialized works not part of the corporate purpose or main economic activity of the beneficiary, with the condition that the contractor of such services should be registered before the Ministry of Labor and Social Welfare for such purposes (Ministry of Labor or "STPS" due to its acronym in Spanish).[2]

Due to the foregoing, only in very specific conditions with respect to the specialization of the services, the outsourcing of third parties is allowed (which we previously knew as outsourcing), provided that the supplier complies with the aforementioned terms.

It is worth mentioning that such registry shall be effective 30 days following the publication of the decree giving rise to such amendments, for the Ministry of Labor to issue the applicable general rules to such respect. Even when such rules are issued within such period, the contractors are given a term to obtain such registry of 3 months as from the date that such rules are issued.

To this respect, the Unified Commissions of the Chamber of Deputies giving rise to the approval of such amendment, state the following: "We should solve the issues without damaging companies that due to their needs they want to hire specialized services or works not part of the corporate purpose or the economic activities, maintaining and protecting the labor rights and avoiding labor exploitation and misuse of taxes".

In particular, we think that the diagnosis is exemplary, however, the way it was amended differs from the stated purpose, as in real terms, the origin of the services providers (part of business groups or independent parties) was the need that such companies focused their efforts on the compliance with the corporate purpose and, mainly, to avoid the excessive payment of the profit sharing of employees in Employee Profit Sharing (PTU) as originally stated, it diminishes the competitiveness of Mexican companies, as it is determined as a tax without a real incentive for productivity. Unfortunately, in many cases this structure was abused to the extreme of creating structures regarding labor, social and tax responsibilities of certain companies.

Notwithstanding, it is worth mentioning that the outsourcing of specialized services or works provided by companies of the same business group is allowed, under the applicable conditions for companies providing services independent from a business group, abovementioned.

Brokers

The broker figure continues in force, but only as a person (individual or legal entity) taking part in the recruitment process and appointment of personnel, as well as the training of such employees, among other services; however, it is specified that the employer will be the individual benefited from such services.

1 Article 12 of the LFT
2 Article 13 of the LFT

Legalities and requirements to contract specialized services

As we stated in the previous paragraph, outsourcing is prohibited, but the outsourcing of specialized services or specialized works is allowed, provided certain requirements are complied with, such as the legalization of such relations (we refer to the provider-beneficiary relation) through an agreement setting forth the purpose of the services and the estimated number of employees involved in such benefit.

In this sense, prior to the execution of such services agreement, it is essential to guarantee that the specialization of the services and the compliance of the labor, tax and social security obligations of the provider must be complied with as stated below.

In addition, in this sense, as we mentioned before, it is included the creation of a registry of specialized services providers by the Ministry of Labor, which must be permanently published. Such registry must be renewed each three years.

Thus, with respect to such registry, the STPS must have an opinion within a term of 20 days as from the date such request was received; failing this, the requester may request to such Ministry of Labor to render the corresponding resolution, which must be issued within a term of 3 days following the request. After such term, it shall be considered affirmative with respect to such registry for all the purposes that may arise.

On the other hand, the Ministry of Labor will reject or cancel at any time such registry if in its opinion it fails to comply with the requirements set forth in the law for such purposes. A point of criticism that we make here is that there is no procedure guaranteeing a right of hearing of the affected party for a resolution in this sense (rejection or cancellation) in order for it to provide evidences in its benefit correcting the omission giving rise to the rejection or cancellation of such registry, which is very important not only for the service provider but for the beneficiary.

Employer replacement

With respect to the employer replacement, a paragraph to Article 41 of the LFT was added to set forth that the purposes of the company or the establishment of the replacement employer must be transmitted for such figure to be effective.

It is worth mentioning that such provision will be effective three months following the effective date of the executive order giving rise to this amendment, therefore, if derived from such amendments, an employer replacement process must be performed in order to comply with these obligations. The corresponding term should be indicated in order not to transfer the assets of the provider to the beneficiary.

New method to calculate the payment of the Employee Profit Sharing

As you know, the Employee Profit Sharing corresponds to the 10% of the taxable profit of the taxpayer (determined according to Article 9 of the Income Tax Law) and it must be shared among the employees according to the following criteria: 50% should be shared equally among all the employees, taking into consideration the number of days worked per each year, regardless the amount of the salaries. The second should be shared proportionally to the amount of the salaries accrued for the work provided during such year. [3]

This method does not change at all, but the change is regarding a limitation set forth in Fraction VIII of Article 127 of the LFT, which sets forth two potential methodologies to determine such limit, to wit: a) three months of salary of the employee; or b) the average of the Employee Profit Sharing received in the last 3 years; whatever is more favorable for the employees' interest.

There is a doubt with respect how would be the interaction between this method and the method set forth in Fraction II of such Article 127, which textually states the following: the non-union employees shall participate in the profits of the companies, but if the salary received is higher than the salary corresponding to the unionized employee with the highest salary in the company, or failing this the regular employee with the same characteristic, this salary shall be increased in a 20% as a maximum salary.

A potential interpretation is that in the case of non-union employees, if their salary is higher than the unionized employees or regular employees, the limit of the three months of salary aforementioned will be determined by increasing the highest salary of the unionized employee
in a 20% and if there are no unionized employees, the regular employees with such characteristic. The foregoing as the fractions of Article 127 were not amended and, accordingly, Fraction II abovementioned continues in force.

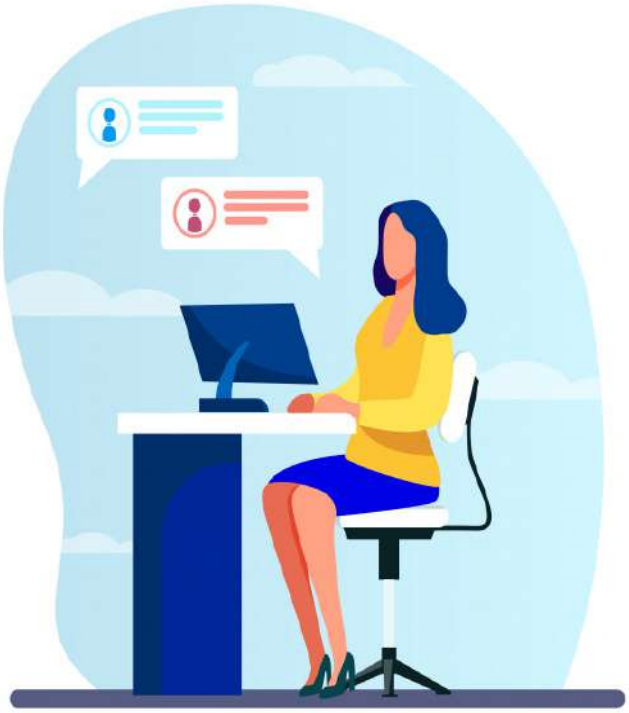
3 As stated in Article 123 of the LFT.

As stated above, with respect to the non-union employees, there may be three scenarios with respect to the limit above referred:

1) if there is a union, the measurement must be made considering the highest salary of the unionized employees, added in a 20%;

2) if there are no unionized employees, but there are regular employees, it must be taken into consideration this type of employees' salary, of higher amount and it shall be added with the 20%; or else,

3) if there are only management employees, no limit of 20% will exist from the salary of higher amount regardless they are unionized or regular employees. [4]



It is worth mentioning that if there is an amount to be shared as the Employee Profit Sharing and it is not enough to be shared due to the limits above referred, they shall not be part of the Employee Profit Sharing that must be added the next year.

Penalties

There are penalties for the parties taking part in the outsourcing of specialized services that does not comply with the formal requirements above mentioned (for both, the provider, and the beneficiary).

One of these penalties is that, in the event the services provider fails to comply with the labor obligations derived from the relations of this nature with its employees, the contractor shall be jointly responsible regarding such relation with respect to the employees used in the provision of such services.

On the other hand, two new penalties are introduced that must be taken into consideration:

a. The employer not allowing the inspection by the labor authorities will receive a penalty between 250 and 5,000 Measurement and Update Units (UMA). [5]

b. On the other hand, there is a new penalty for those outsourcing personnel (as now, as previously stated, is prohibited) and for those subcontractors without a corresponding registry mentioned in the following paragraphs. The penalty for such conducts is between 2,000 and 50,000 UMAS.[6]

Therefore, the noncompliance with this matter may derive in different penalties for the provider and the beneficiary of the services, thus, a special emphasis must be made to comply with all the sections we have defined here and those stated in the following paragraphs.

4 There is no definition of regular employees, as there is no definition as such in the LFT. Notwithstanding, the general terms of such definition are made by exclusion in the sense that are those employees who do not perform activities developed by the management employees and do not belong to a union.

5 Represents a value between $22,405.00 and $448,100 Mexican pesos, considering that the UMA for year 2021 amounts to $89.62 Mexican pesos.

6 It means that the range of the penalty is between $179,240.00 Mexican pesos and $4,481,000.00 Mexican pesos.

Social Security Law

We previously mentioned that this reform included amendments to different laws, among others the Social Security Law, which will be mentioned in this section.

In this sense, the amendment derives mainly in the contracting of specialized services or works that must comply with the provisions for such proses of the labor law above analyzed.

Thus, if the service provider fails to comply with its social security obligations, the contractor must be jointly responsible in connection with the employees used for the performance of such services and works.

New obligations for the specialized services provider or specialized work supplier

There is a new obligation for the specialized services providers and specialized work suppliers in the sense that, on a four-month basis, they must report their agreements not later than the 7th day of January, May and September. The following information must be provided:

I. The parties to the agreements: name, corporate name, tax ID, corporate address or conventional address if other than the tax address, e-mail and contact telephone number.

II. From each agreement: purpose, term, relation of employees and other individuals to provide specialized services or to perform specialized works in favor of the beneficiary, indicating name, personal number, social security number and base quote salary, as well as the federal name and registry of taxpayers of the beneficiary of the services per each agreement.[7]

III. Simple copy of the registry issued by the Ministry of Labor to provide specialized services or to perform specialized works. [8]

We must wait that the Technical Committee of the IMSS issues the general rules to duly comply with these new obligations.

Penalties

Failing to comply with the obligations mentioned in the subsection immediately above derives in penalties between 500 and 2,000 UMAS, which amounts in Mexican pesos arise to $44,810.00 to $179,240.00.

7 The information mentioned in this item and in the immediately previous number (I.) must start as from three months from the effective date of the executive order giving rise to this amendment.
8 The document must be obtained once the STPS provides the users the device to obtain such document. We think that this transience must be congruent with that determined for such purposes in Article 15 of the LFT above referred (that is to say, 30 days following the effective date in order for the STPS to inform the device and 3 months following to obtain such document).

Mexican Fund Institute for Workers' Dwelling

Other law with relevant changes in this amendment was that of the Mexican Fund Institute for Workers' Dwelling (INFONAVIT), which we describe in this section.

New obligations for the specialized services provider or specialized work supplier

As in the IMSS, there is an obligation imposed on the services providers or work suppliers considered as specialized services that must be reported on a four-month basis in the same months and days as in the IMSS, information with respect to the agreements executed according to the information required by the IMSS in this sense.[9] [10]

The only additional data different from those mentioned above that must be reported according to the INFONAVIT are the following:

- The amounts of the contributions and amortizations (it is not clear if this obligation refers to contributions to such institute and amortizations to the credit of the employees or other elements referred to in this obligation, we think that this must be clarified).

As in the IMSS, we must pay attention to the publication of the applicable rules in order to comply with these obligations; likewise, in the event of noncompliance with obligations for INFONAVIT, with respect to the services provider employees, the beneficiary shall be jointly responsible for such omissions with respect to the employers used to execute such contracting. [11]

Unlike the IMSS Law, this law fails to state specific penalties regarding the noncompliance with these obligations.

9 We suggest you to read the corresponding section of the IMSS in order to avoid unnecessary repetitions.
10 The document proving the registry of the services provider before the STPS must be obtained once the STPS provides the users the device to obtain such document. We think that this transience must be congruent with that determined for such purpose in Article 15 of the LFT above referred (that is to say, 30 days after the effective date of the STPS to know the device and 3 months following to obtain such document).
11 The INFONAVIT shall have two months as from the publication date of this amendment to issue the rules determining the applicable procedures to comply with this obligation.

Federal Tax Code

The Federal Tax Code ("CFF" due to its initials acronyms in Spanish) was also amended to state the following.

No deductibility or claim of tax credits

No deductibility or credit of the considerations paid with respect to the execution of outsourcing agreements will be made, if the purpose of such agreements are services related to the corporate purpose and the main economic activity of the contracting party. That is to say, if the consideration derives from an agreement not complying with the provisions of Articles 12, 13 and 14, mainly, of the LFT, above analyzed.

The considerations derived from the services agreement will not be deducted or credited in the following assumptions:

I. If the employees provided by the supplier were originally employees of the beneficiary and they were transferred to the supplier by any legal structure; or else,

II. When employees provided by the supplier to the beneficiary perform services that are considered under the scope of the main economic activity of the beneficiary.

Deductibility of payments for specialized services and works

It is included the possibility to deduct and credit the tax to be paid for considerations related to specialized services and works, if any, by the contractor, with the registry before the STPS we mentioned above, in addition to the compliance with other obligations included in the Income Tax Law (LISR) and the Value-Added Tax Law (LIVA), which will be detailed below in the corresponding sections.

Thus, with respect to Article 15-D of the CFF being analyzed, it is determined a definition of specialized services or works named "complementary or shared", provided between companies of the same business group, although these must be different from the corporate purpose or the main economic activity of the beneficiary; therefore, mainly, it may be construed for tax purposes, although there is no registry before the Ministry of Labor of such companies, the considerations may be deductible and the tax may be claimed, provided they differ from the main activity of the beneficiary.

Penalties

Penalties due to the omission of the new obligations of the contracting parties and the services providers included in the LISR and LIVA are included to be analyzed below in the corresponding sections. As we may distinguish, such obligations refer to the delivery of certain information by the provider to the service beneficiary and the penalty by such omission derives in an amount between $150,000 and $300,000 Mexican pesos per each failure of delivery of such information.

Likewise, as prevention, the qualified fraud crime is included when it derives from using simulated programs of services or works provision considered as specialized in the events they refer to complementary services or works, or else, if personnel under such definitions is subcontracted which is now prohibited by the LFT.

Income Tax Law

Requirements to be complied with by the service beneficiary to deduct the consideration

The obligation of the beneficiaries of the specialized services or works is based on the sense to obtain from the services provider certain information, which is summarized as follows; it is worth mentioning that the services rendered must provide this information to the contracting party:

- Copy of the current authorization under the terms of Article 15 of the above referred LFT;
- Payment receipts of salaries of the contractor to its employees;
- Copy of the payment statement of the tax withheld to employees;
- Copy of the payment of worker-employees fees for the employees performing a service before the IMSS; and,
- Copy of the payment of the contributions to the INFONAVIT for the same employees.

Non-deductible payment

As above referred in the corresponding CFF section, the considerations made for outsourcing services prohibited under the LFT, must be considered as nondeductible for determining the base of the income tax.

Value-Added Tax Law

The tax derived from the considerations due to outsourcing should not be credited

As mentioned above in the section corresponding to CFF, the transferred VAT for considerations made derived from the outsourcing services prohibited according to LFT must considered as not creditable for the purposes of determining the payable VAT of the contracting party.

Requirements that must be complied with by the beneficiary of the service to credit the transferred VAT derived from the consideration

The obligation of the beneficiaries of specialized services or works must be in the sense that the services provider must obtain certain information, which is summarized as follows, it is worth mentioning that the services provider must provide this information to the contracting party:

- Copy of the current authorization under the terms of Article 15 of the LFT above referred;
- Return of the VAT and acknowledgment of receipt of the corresponding payment to the period in which the contracting party made the payment of the consideration.

Such information must be provided not later than the last day of the month following in which the contractor has made the payment of the consideration of the received service. In the event the contractor fails to obtain such information in the required time, it must submit a complementary return subtracting such claim.

6% Withholding is eliminated

Also the section IV of Article 1-A is repealed, to eliminate the 6% withholding.

OTHER RELEVANT TOPICS

Term to be effective

All the other amendments related to this amendment having an impact on the tax matters (amendments to CFF, LISR and LIVA) shall be effective in August 2021; however, except as stated in each section, this amendment shall be effective as from the day following its publication, therefore, the companies must be adapted to this amendment immediately.

Likewise, the Ministry of Labor must issue the general provisions regarding the obtaining of the registry within 30 natural days following the effective date of the executive order.

Likewise, the individuals or legal entities providing outsourcing services must obtain the registry before the Ministry of Labor and Social Welfare within a term of 90 natural days following the publication of such general provisions mentioned in the previous paragraph.

It is worth mentioning that the obligation included in the CFF, LISR and LIVA, with respect to the obtaining of the registry of contractors before the Ministry of Labor, shall be demanded, in these events, until the registry of service providers is available at the Internet site, we think that it will be of the Ministry of Labor, as it is not clear in the transitory article in this sense.

Actions to be followed

As mentioned above, the complexity of this amendment transversally affects different aspects of the company, from the labor matters to the tax matters, and also the corporate, financial matters and that corresponding to internal systems, just to mention some.

Of course, our experts in each of the corresponding areas are prepared to assist you in the implementation of this amendment since if you do not appropriately attend this matter, you may have monetary consequences such as fines, or even, tax issues classified as crime.

We hope that you find this information useful.

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