Mexico subcontracting reform 2021

Labor, Social Security and Tax Laws

Mexico published legislation on April 23 that modifies the tax and labor treatment of subcontracted services. The new rules could significantly impact Mexican investments, and could disrupt current approaches to human resources. Failure to comply with the new rules could result in significant penalties or charges of tax fraud.

Labor, social security and tax reform – Subcontracting

Allowed:
Subcontracting of specialized services

Disallowed:
Outsourcing of workforce supply

The reform impacts:

Labor	Business restructuring
Social security	Corporate legal
Workers housing fund	HR
Unions	Finance
Profit sharing	Processes
Income tax	Compliance & risk
VAT	Technology
TP	Governance
Electronic invoicing	

- Subcontracting of specialized services or works not forming part of the purpose or predominant economic activity, if provided by a registered contractor, is allowed.
- Subcontracting of the workforce is illegal when it consists of providing or putting personnel at disposal for the benefit of others.

Subcontracting framework

Background

- Labor reform effective **April 24** and related tax reform effective **August 1**.
- Labor regulations will be published soon.
- Reform prohibits subcontracting of workforce and allows subcontracting of specialized services, including specialized insourcing services (within a group that has a controlling entity).

Qualification requirements

- Services shall not be related to the beneficiary's corporate purpose or predominant economic activity.
- Must be a registered contractor before the labor authorities (Public Register).
- Contracts shall be made in writing and must satisfy specific requirements.

Obligations

- Registration and renewal every three years.
- Contractors shall regularly provide information to beneficiaries, social security, and tax authorities.
- Beneficiaries have joint liability with the contractor for labor, social security, and tax purposes in case of non-compliance.
- Confirmation to the beneficiary of contractor's compliance obligations (labor, social security, income tax, VAT, and social security contributions).

Enforcement

- Significant sanctions (labor), up to US $200K for contractor and beneficiary, per violation and per contract.
- Non deductibility, VAT not creditable, tax fraud for subcontracting workforce and sham situations.
- Transfer of employees through an employer substitution allowed for three months without needing to transfer assets.

Profit sharing

- Capped to three months of salary or average of the profit sharing paid the last three years.

Next steps for subcontracting

Holistic risk assessments and mitigation actions

- Review all services relationships with third parties and related parties.
- Consider restructuring and transfer pricing issues resulting from potential transfer of functions, assets, and risks.
- Review company's bylaws (corporate purpose and predominant activity) from different angles (e.g., tax perspective).
- Review bylaws of contractors, elaborate contracts and evaluate new terms and conditions (e.g., indemnities).
- Implement tax compliance and other processes and controls.
- Consider how technology could enable assessments and mitigation.
- Consider potential changes to governance to ensure compliance and mitigate risks with relevant stakeholders: workers, providers, clients, labor, tax, and other authorities.
- Determine whether any potential restructuring required to comply with the new rules falls into the reportable disclosure obligations.

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