



Foreign corporations with operations in Mexico under the so called “shelter” (albergue) program, might face a double cost of income tax applicable to a single manufacturing service, unless the operational terms with the contractor are restructured.

The Mexican Income Tax Law, as of 2014, established that residents abroad shall not be deemed to have a permanent establishment in Mexico for the following 4 years, or four years after contracting the “shelter” company, whenever they directly or indirectly supply raw materials, machinery or equipment, to carry out the

manufacturing activities through companies with a current maquila program under the shelter (albergue) scheme authorized by the Ministry of Economy, provided that said residents abroad are not related parties of the company holding the approved shelter program, nor of a related party of said company.

In some cases, the 4 year period might be considered as a brief period to define the continuity of their manufacturing investment in Mexico. Considering the above, the Maquila Association mediate with the Tax Administration Service, achieving the publication of rule 3.20.6 in the Miscellaneous Resolution for 2017.

Tax and Legal Services

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Rule 3.20.6, grants foreign corporations an administrative benefit to keep their manufacturing process in Mexico for an additional four year period with the "shelter" company. In this case, it will not be deemed that the foreigner has a permanent establishment in Mexico and it will not be required to incorporate its own company in Mexico. The foreign resident, will have to notify the tax authorities its desire to extend their agreement with the shelter company for an additional four years period. In case that the foreign resident extends for a second term their "shelter" agreement, the following must be considered:

- They might be able to comply with their tax obligations through the IMMEX "shelter" scheme company, once that the first 4 year contract term has concluded.
- For this purpose, the "shelter" company must fill a notice to the tax authorities, on behalf of the residents abroad, where they state their intention to extend the agreement with the "shelter" company for up to another 4 year period, which will start once that the first period concludes.
- Residents abroad will have to pay the income tax through the "shelter" company. The tax computation shall be done either through Safe Harbor or an Advanced Pricing Agreement (APA) with the Tax Administration Service.
- Residents abroad shall request a federal taxpayer registration, with no tax obligations.

As a preliminary analysis, we have found that through this administrative benefit granted by tax authorities, the foreign resident will have a double disbursement for income tax applicable to the same manufacturing

activity, according to the following:

The first disbursement would be the income tax amount that would be paid by the shelter entity with IMMEX program and that is charged to the resident abroad as part of the fees paid due to the shelter agreement, which it is a hidden cost that the resident abroad is paying through the shelter manufacturing agreement. The second disbursement would be the income tax amount that it would pay the shelter entity on behalf of the resident abroad (the Principal) for the manufacturing maquila activity through either the safe harbor calculation and/or through the APA methodology as established in the miscellaneous rules before mentioned.

The shelter Company who operates under an IMMEX shelter program shall expressly state, through a notice, their willingness to take responsibility in the tax computation and payment on behalf of the resident abroad and agreeing to become jointly liable regarding the income taxes in Mexico that it is obligated to pay the resident abroad.

The benefit established in rule 3.20.6, will not be used by residents abroad that already have constitute a permanent establishment in Mexico, nor, those who had been previously sheltered by a different company with IMMEX shelter program and had applied the 3.20.6 rule.

The rule mentioned above, could only be applied if the "shelter" company earns revenue only through their maquila services to residents abroad. In any case, the "shelter" company will not be able to obtain revenue for sale or distribution of finished products in Mexico.

For all of the above, foreign corporations that have their maquiladora operation through a shelter scheme contracted on January 1, 2014 or before, 2017 will become a crucial year for their operations, due to the decision of extending for an additional 4 year period with the shelter company, or wants to constitute a permanent establishment, or establish a subsidiary company in Mexico keeping their manufacturing operations as an independent maquiladora.

Please be advised that this document is applicable for shelter companies operating under the "Albergue" program.

This issue, will demand an evaluation of the possible advantages and disadvantages of keeping its manufacturing operations through a maquiladora with a shelter operator, however, we can already confirm that extending the shelter contract, will represent an additional income tax expense for the foreign company as we explained before. A possible solution will require the establishment of a Mexican subsidiary to do the manufacturing operation directly, then, obtaining its own IMMEX Maquila program through the mentioned maquila, in order to avoid a double disbursement of income tax over a single manufacturing operation.

In order to properly analyze and bring value solutions to each maquila manufacturing operation according to their own specific situation and help define alternatives more ad hoc to your economic and operational interest, please reach out to any of our Business Tax team members which will gladly support your query.

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