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# CLE Week

December 5-16, 2022



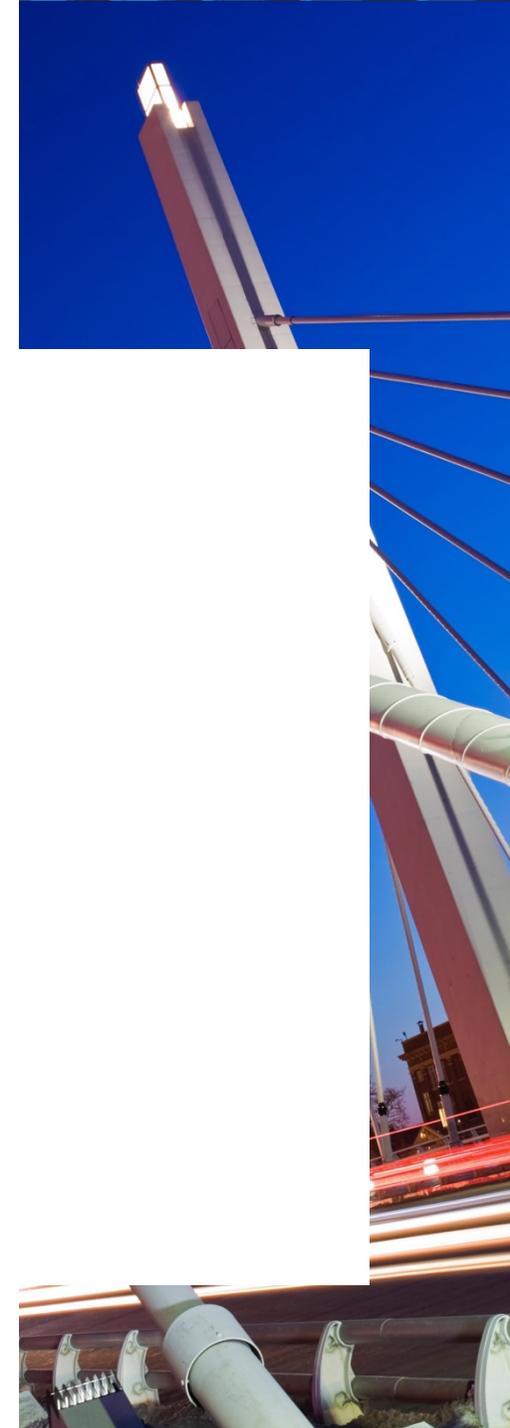


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# Relevant Legal Challenges for U.S. Companies Doing Business in Mexico

# Agenda

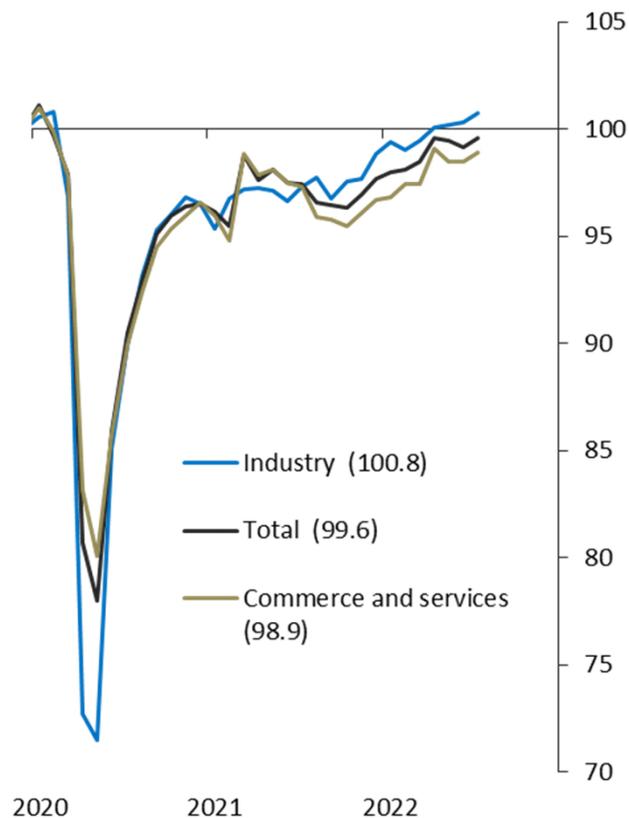
1. Nearshoring
2. USMCA's (Automobile) Rules of Origin Panel
3. Identification of the Ultimate Beneficial Owner
4. USMCA-Driven Labor Reforms in Mexico
5. Outsourcing in Mexico: Recent Developments
6. Are Mexico's TROs an Option?



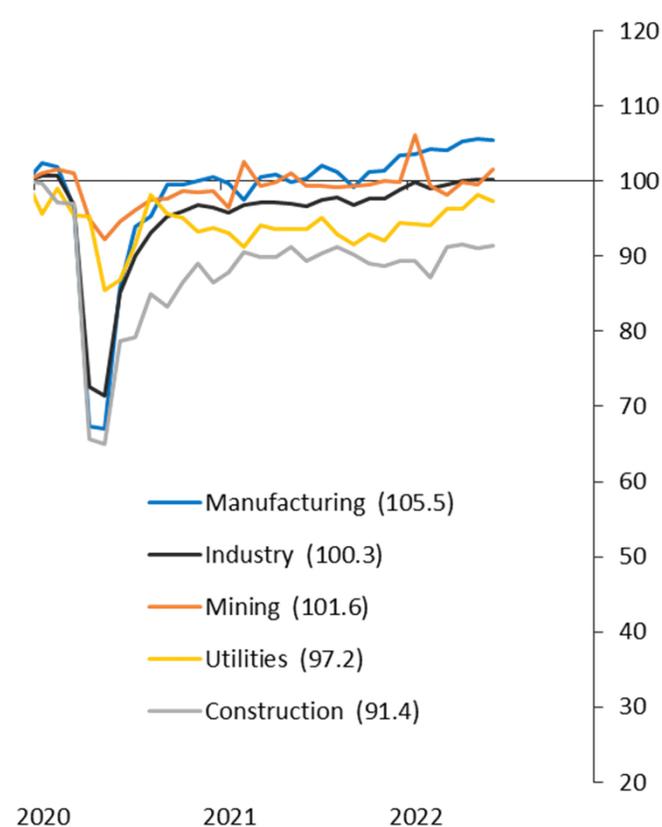
# Nearshoring

## After the pandemic, the recovery process of the economy has been diverse

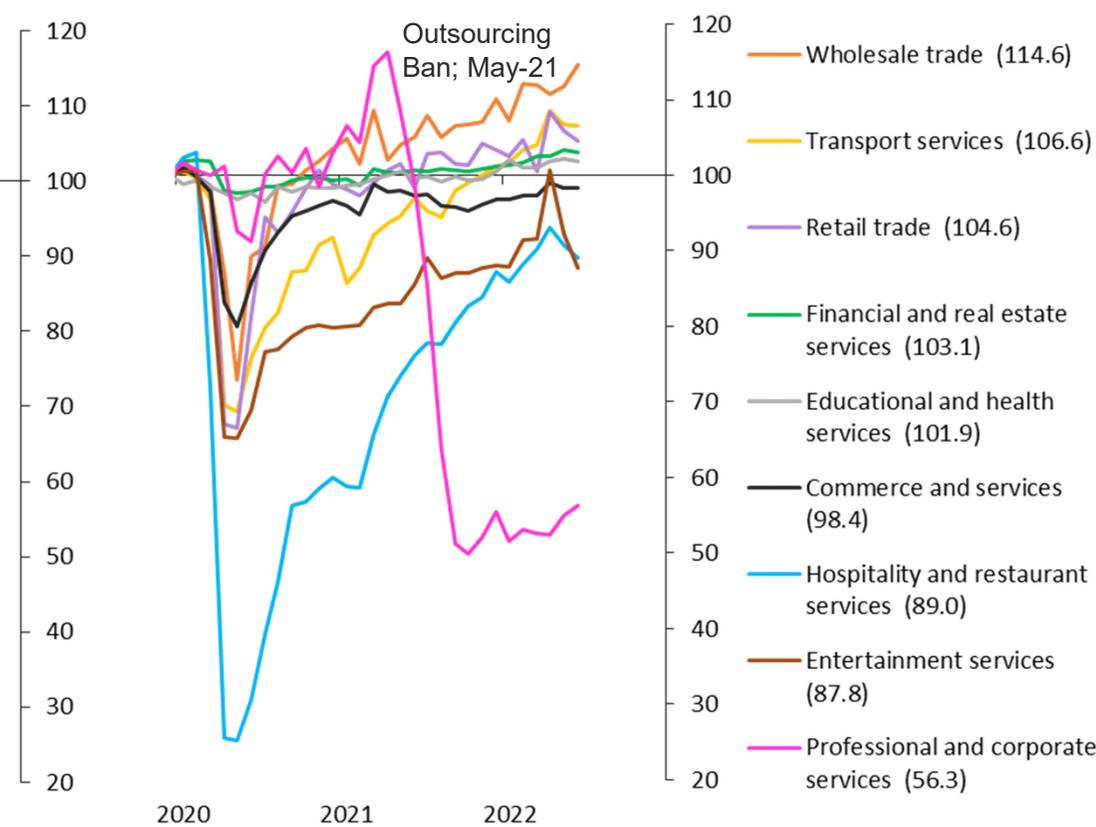
**Economic Activity**  
(Dec-19=100); Jul-22



**Industrial Activities**  
(Dec-19=100); Jul-22



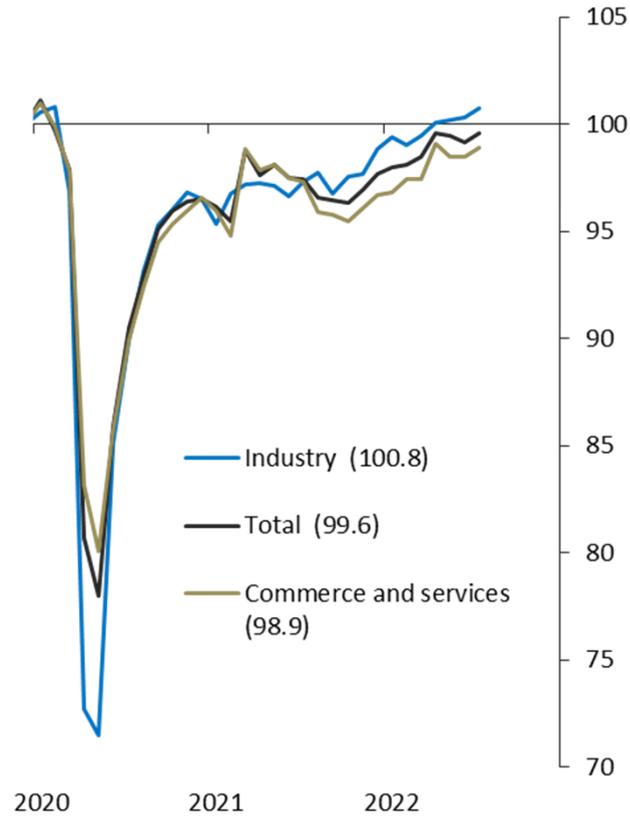
**Commerce and Services**  
(Dec-19=100); Jul-22



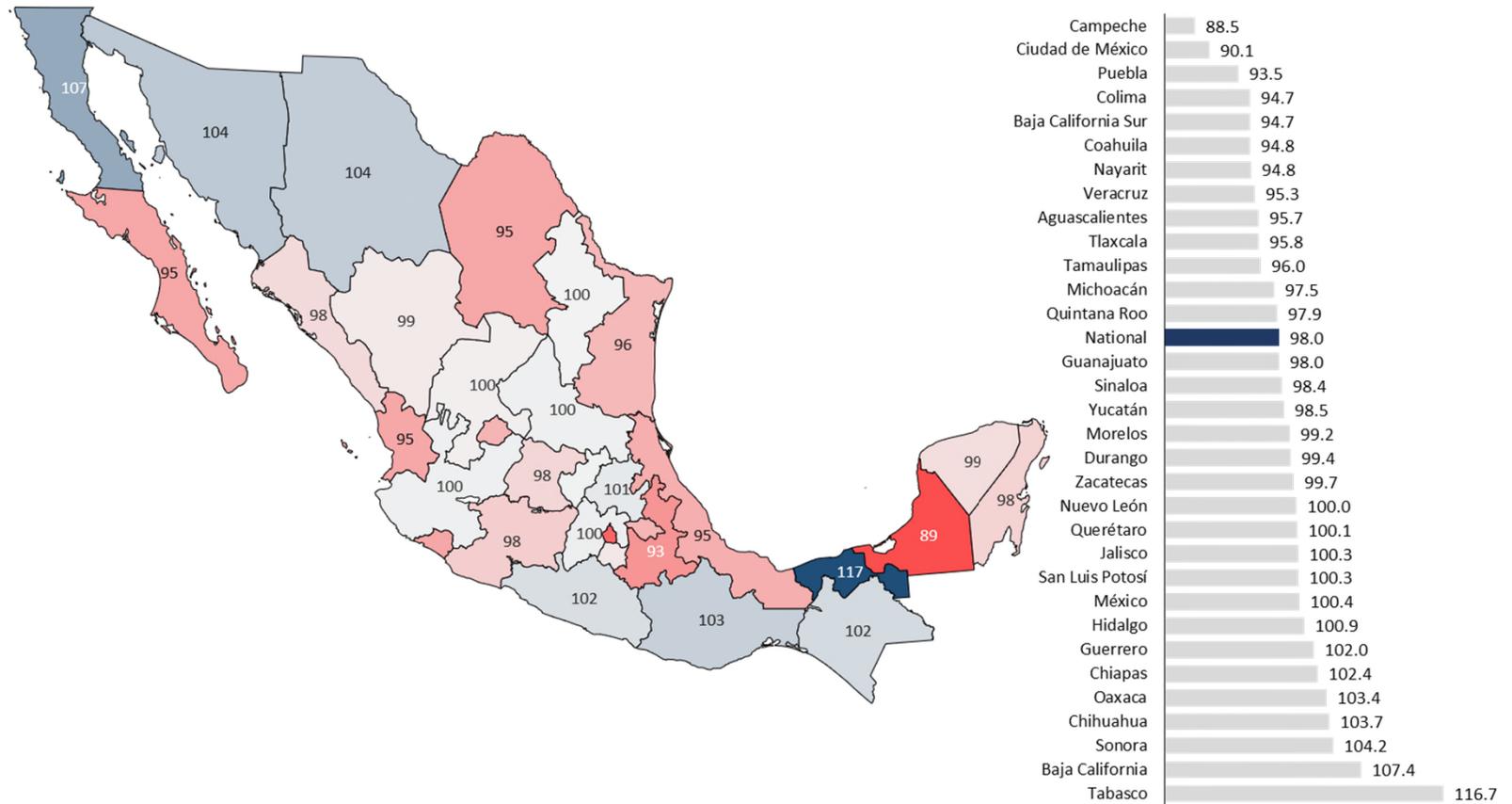
# Nearshoring

At the regional level, thirteen states are above pre-pandemic levels. Within them, different stories explain their dynamics

**Economic Activity**  
(Dec-19=100); Jul-22



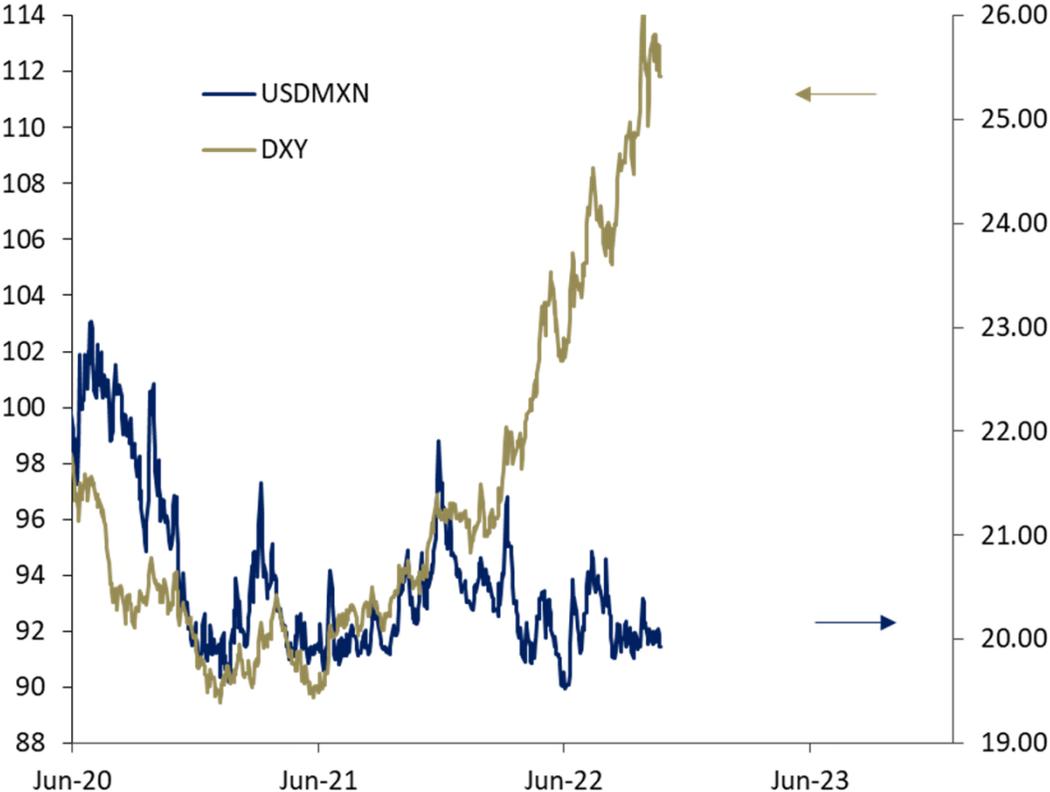
**GDP by State**  
(Dec-19=100); 1Q-22



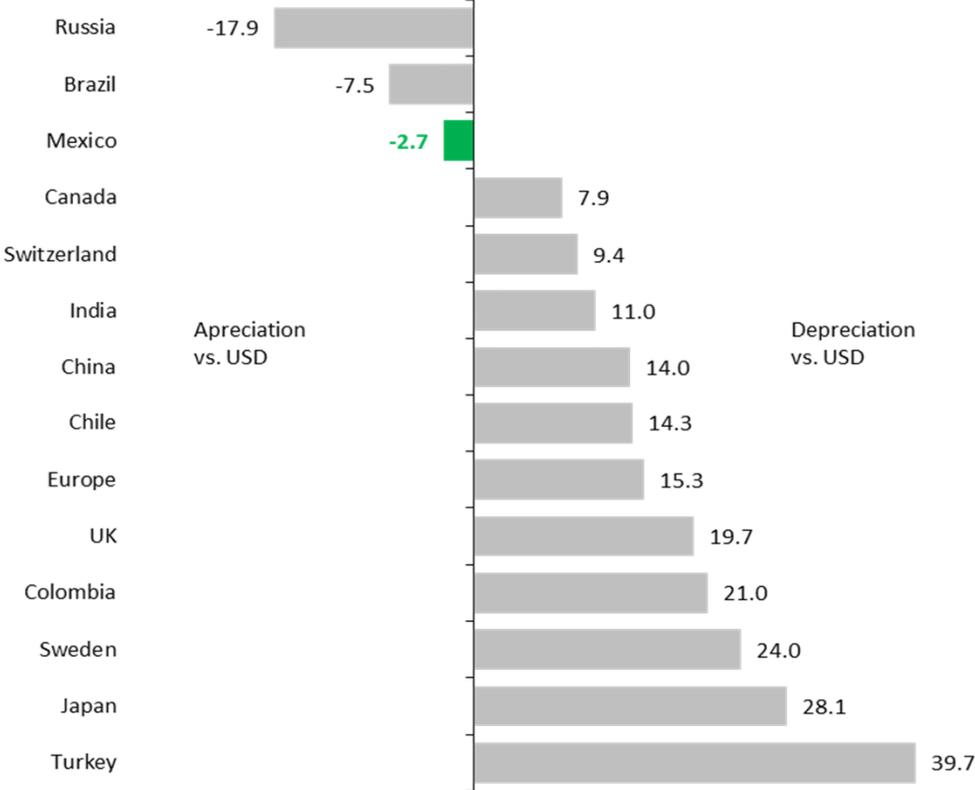
# Nearshoring

## Inflation has benefited the Mexican Peso, which has been resilient in the face of a stronger Dollar

US Dollar Index (DXY) and (USD/MXN) Exchange Rate  
(Points and pesos per dollar); 21-Oct-22



Currencies vs. USD  
(Cumulative % in the year); 21-Oct-22

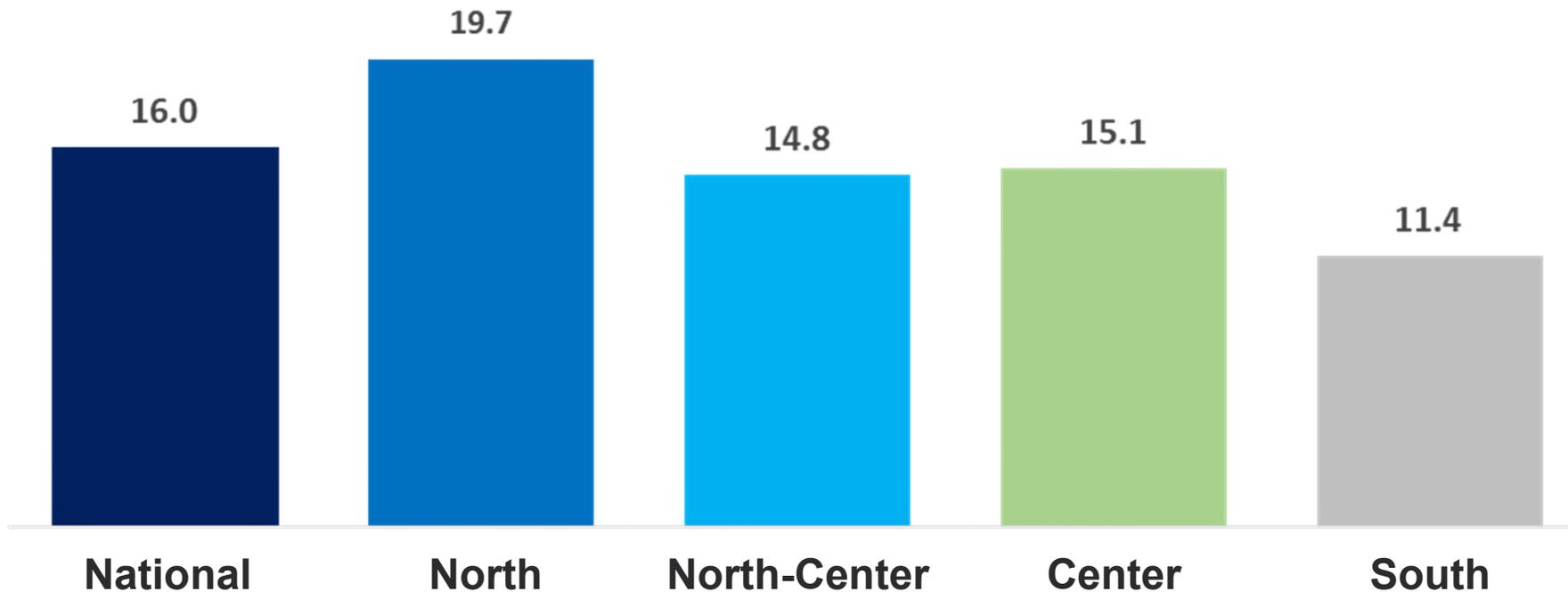


# Nearshoring

## Entrepreneurs across the country report that Nearshoring has had a positive impact on their industries

Entrepreneurs who have seen increased demand for their products or increased investment in their industry as a result of Nearshoring

(% of total businessmen surveyed); 2Q-22

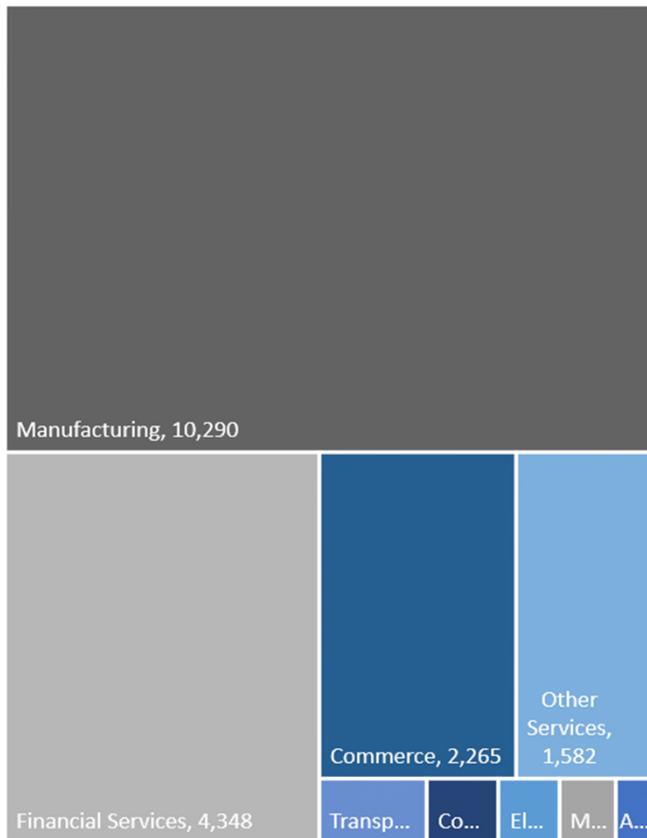


# Nearshoring

Since the pandemic, investment has increased Manufacturing, and has been redirected to Transportation & Logistics, and Mass Media.

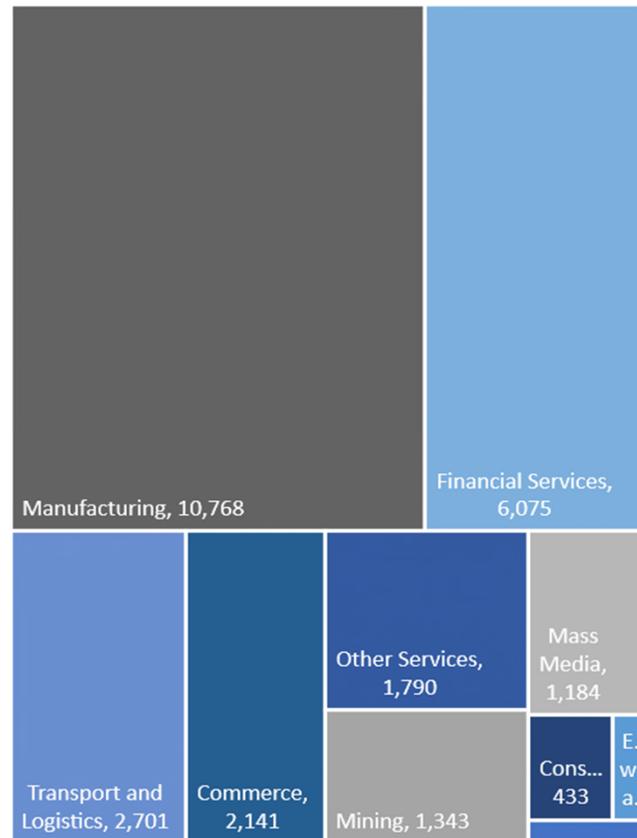
## FDI 2000

(Total = USD 19,253 million, annual flow)



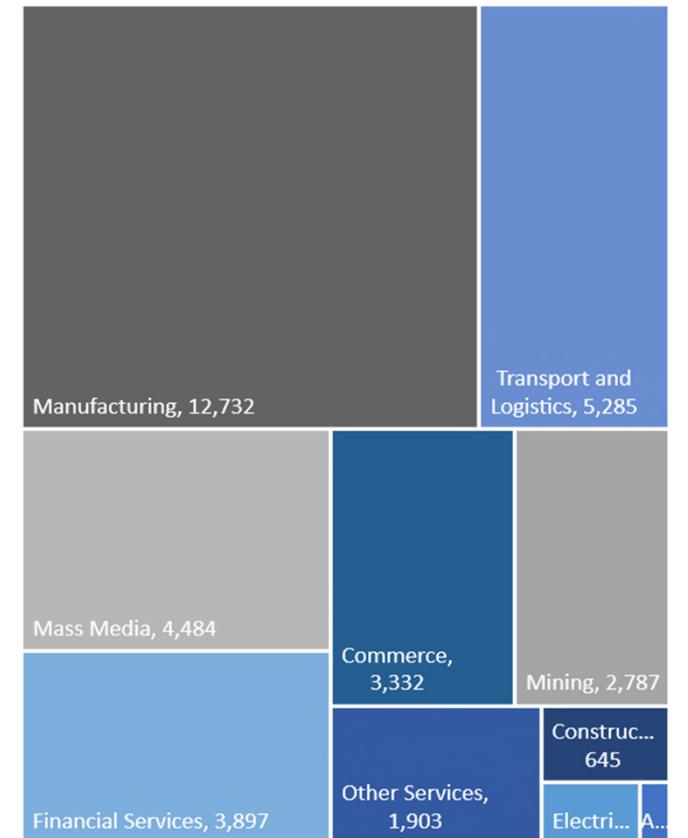
## FDI 2020

(Total = 26,829 USD million, annual flow)



## FDI 2Q-2022

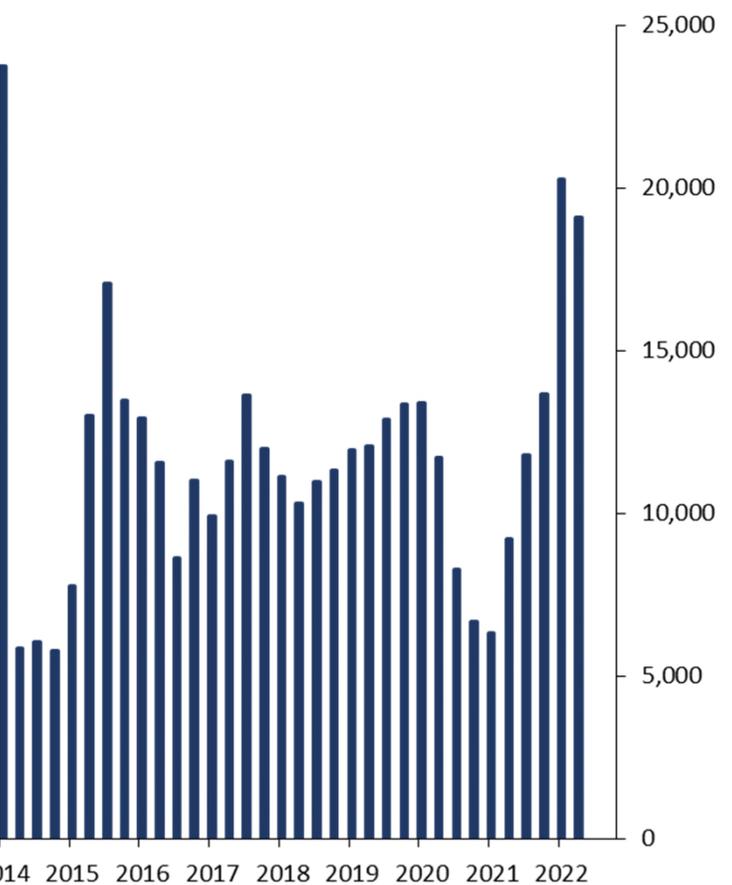
(Total = 36,936 USD million, annual flow)



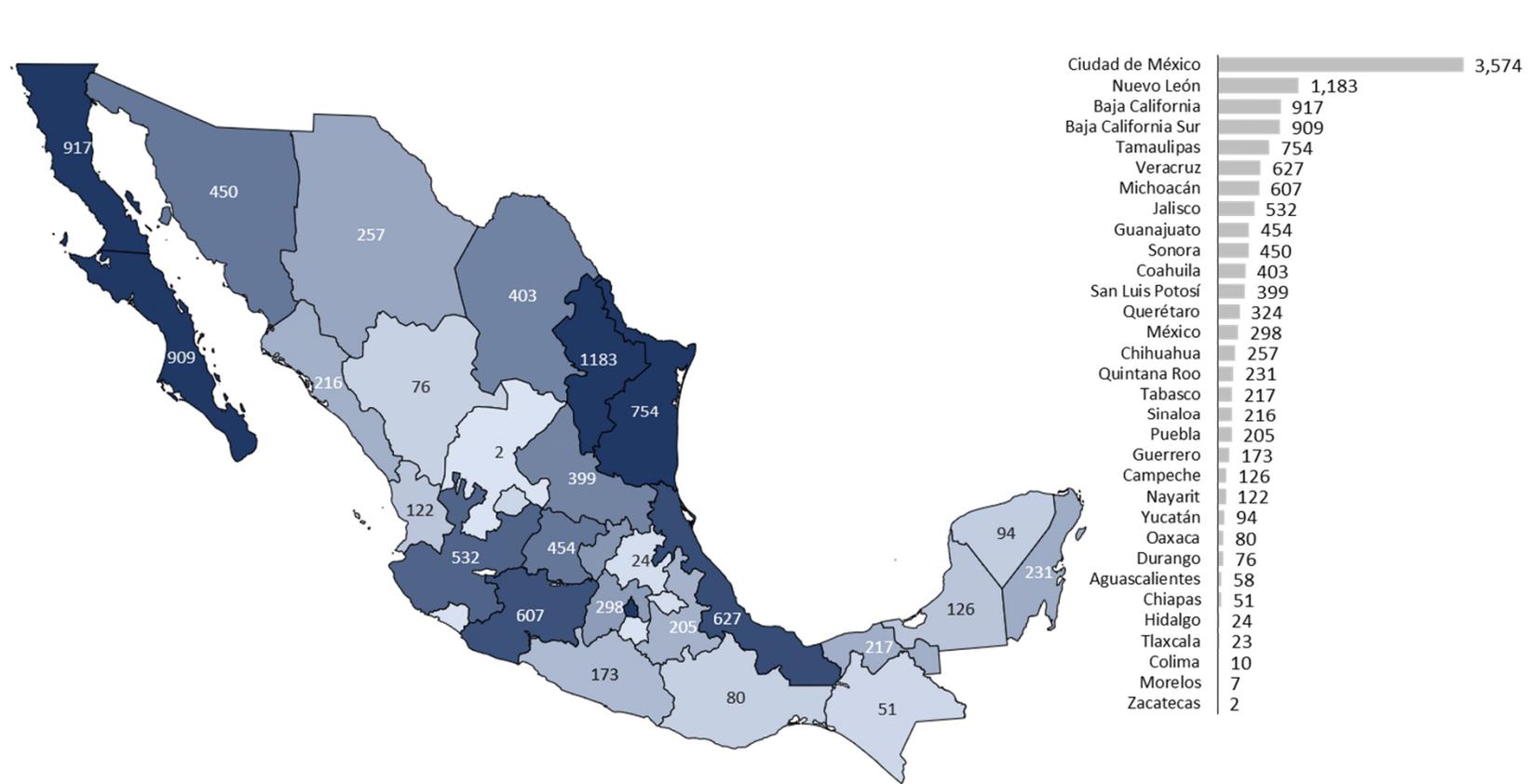
# Nearshoring

## Nearshoring has triggered the arrival of new investment

New Foreign Direct Investment  
(USD million, 12-month flow); 2Q-22



New Foreign Direct Investment  
(USD million); 2Q-22

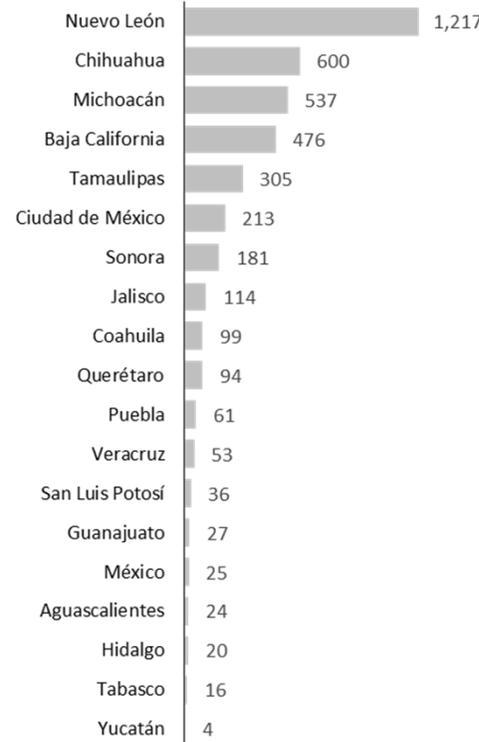
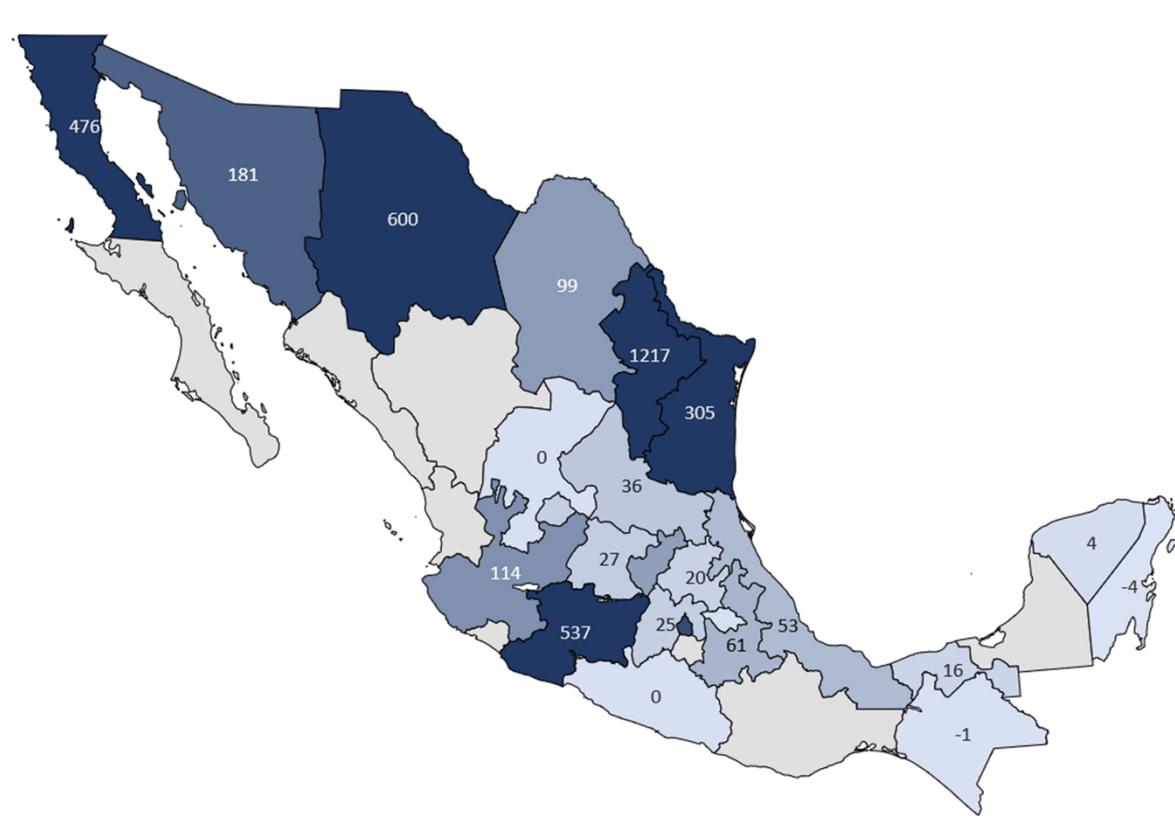
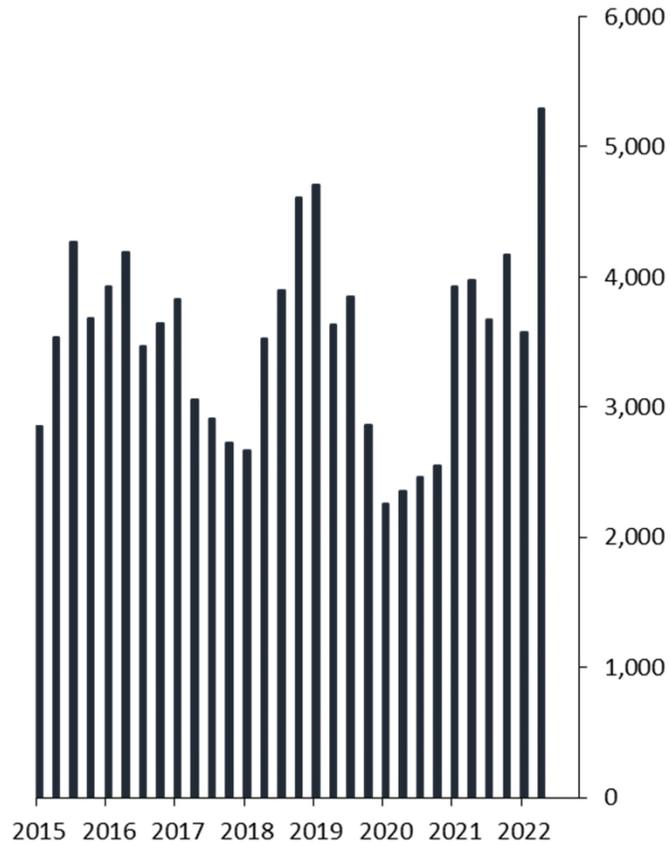


# Nearshoring

## Nuevo León, Chihuahua, Baja California, and Tamaulipas are the States most benefitting from investment in electronics and machinery

**FDI: Manufacturing Electronics and Machines**  
(USD million, 12-month flow); 2Q-22

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(USD million, 12-month flow); 2Q-22

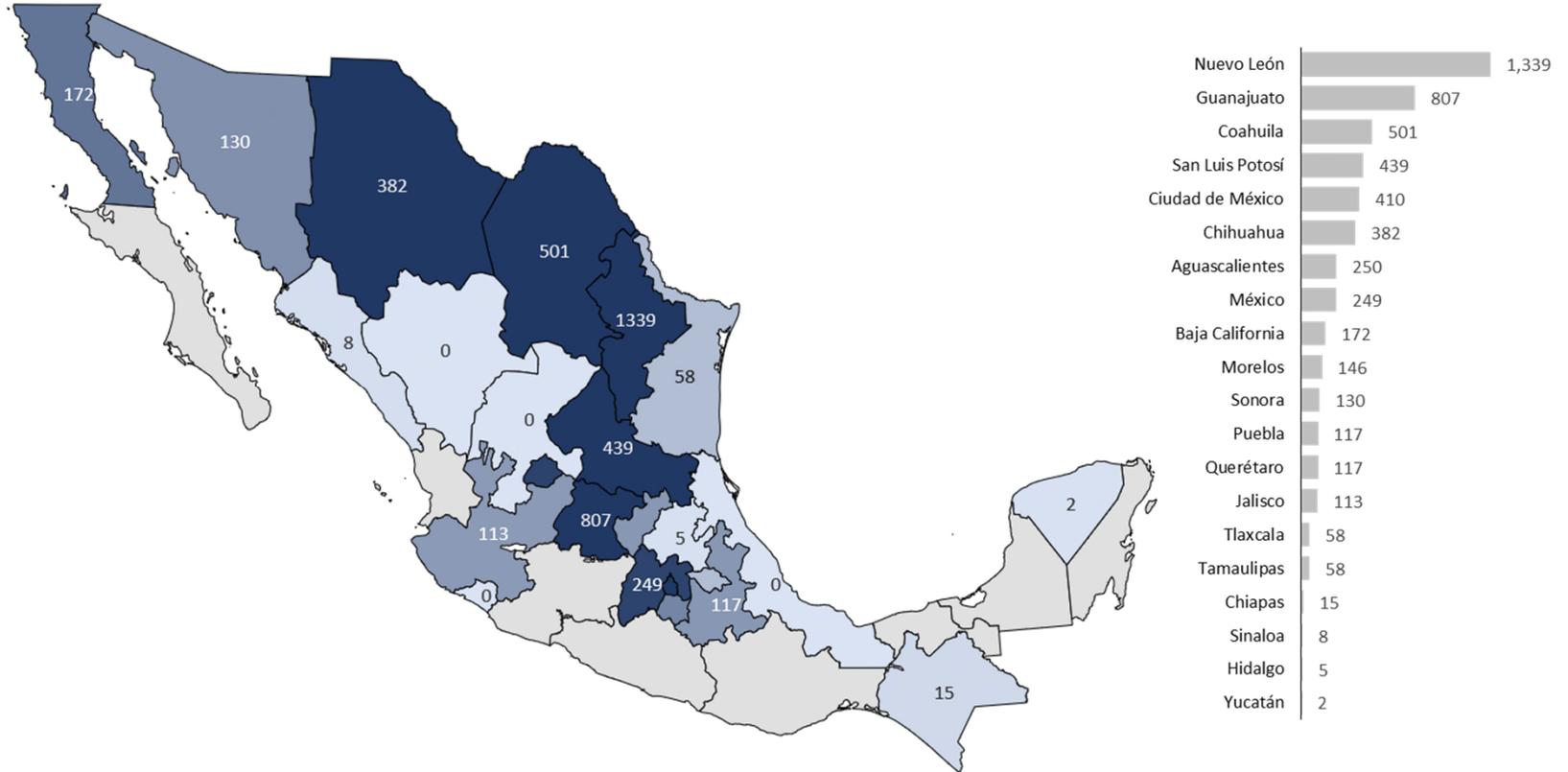
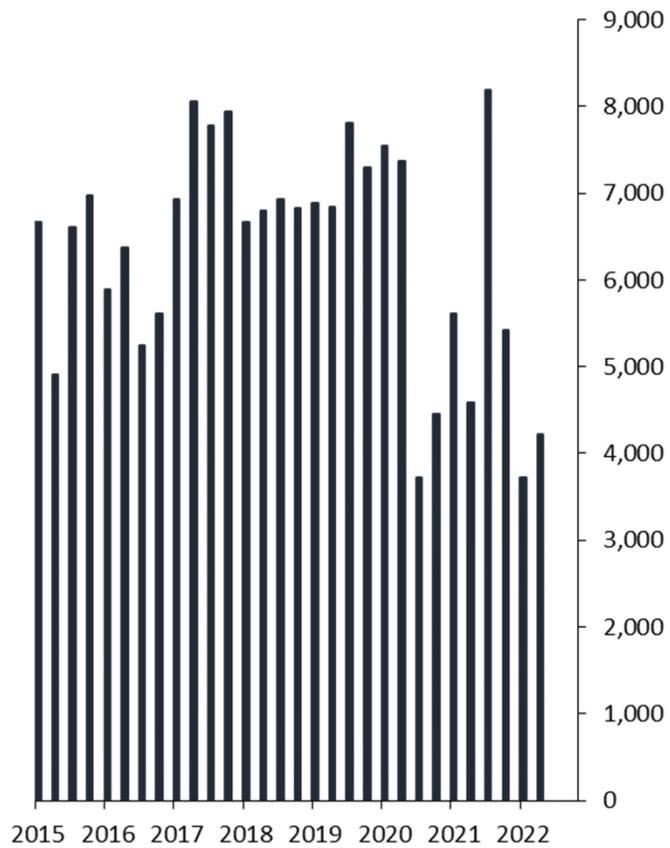


# Nearshoring

## Nuevo León, Guanajuato, Coahuila, and San Luis Potosí are the States most affected by the contraction of investment in the automotive sector

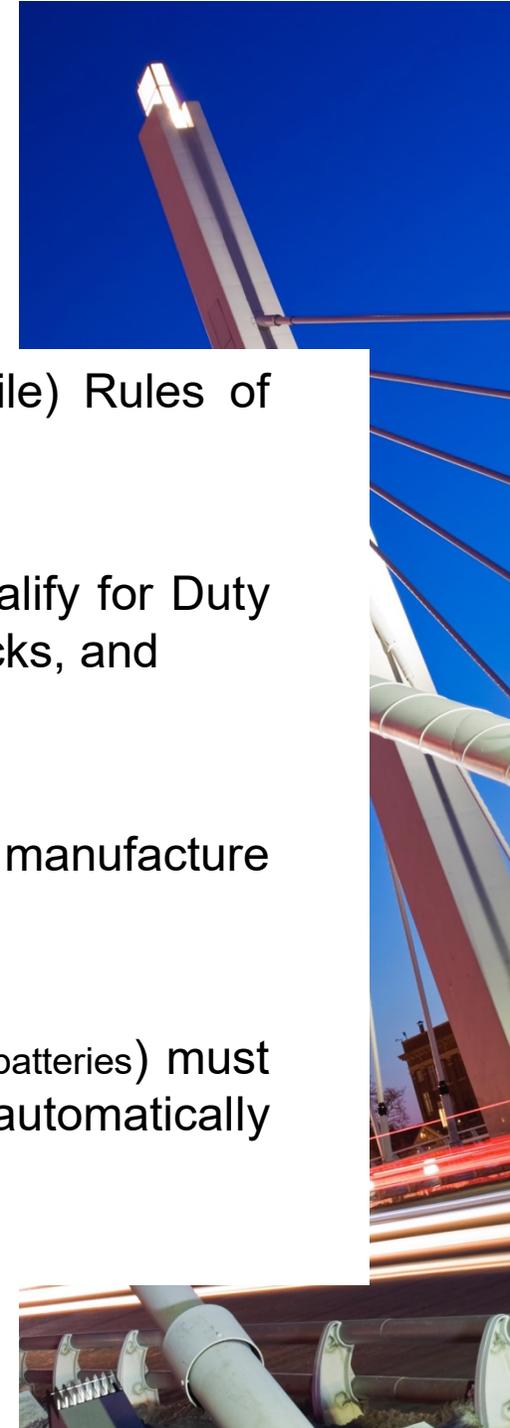
**FDI: Manufacturing Automotive**  
(USD million, 12-month flow); 2Q-22

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(USD million, 12-month flow); 2Q-22



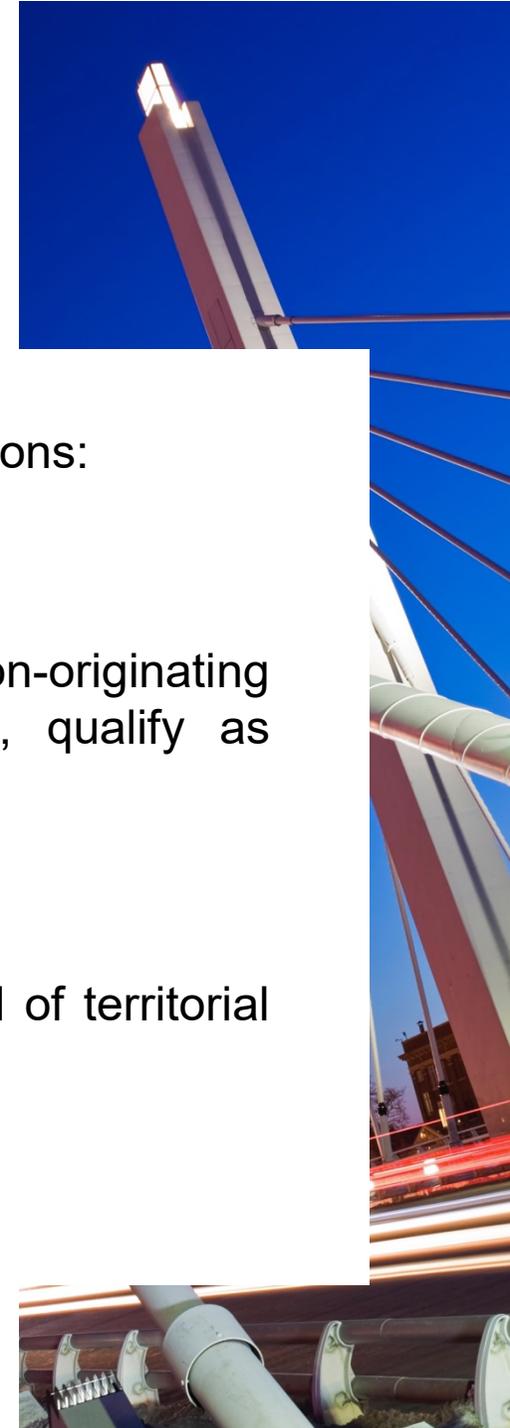
# USMCA's (Automobile) Rules of Origin Panel

- In early 2022, Mexico and Canada challenged the U.S. interpretation of (Automobile) Rules of Origin (ROO) calculation. Panel decision expected early 2023.
- Dispute: How to calculate USMCA's 75% Regional Value Content (**RVC**) to qualify for Duty Free treatment for North-American made passenger vehicles, lights trucks, and certain auto parts.
- Even in a region as interconnected and developed as North America, it is difficult to manufacture complex goods without components from other countries.
- Core parts (engines, chassis and body, axles, transmissions, suspension systems, steering, and advanced batteries) **must** have a 75% RVC and, as long as this percentage is met, 100% of such core parts automatically qualify as having USMCA origination. (Detroit Athletic Club / Auto Dealership examples)



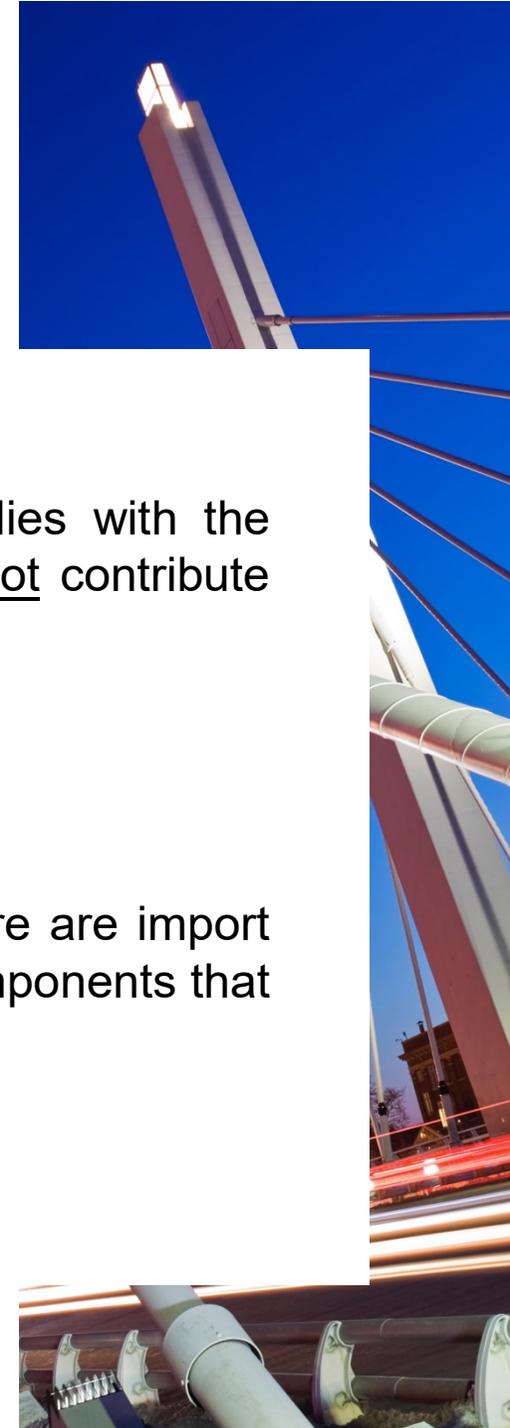
# USMCA's (Automobile) Rules of Origin Panel

- Mexico and Canada contend that the U.S. interpretation violates certain USMCA provisions:
  - ✓ In general, goods produced in the territory of an Agreement Party using non-originating materials, provided that they satisfy the relevant product-specific ROO, qualify as originating
  - ✓ In particular, that a core part (except for an advanced battery) is considered of territorial origin as long as it satisfies the 75% RVC requirement.



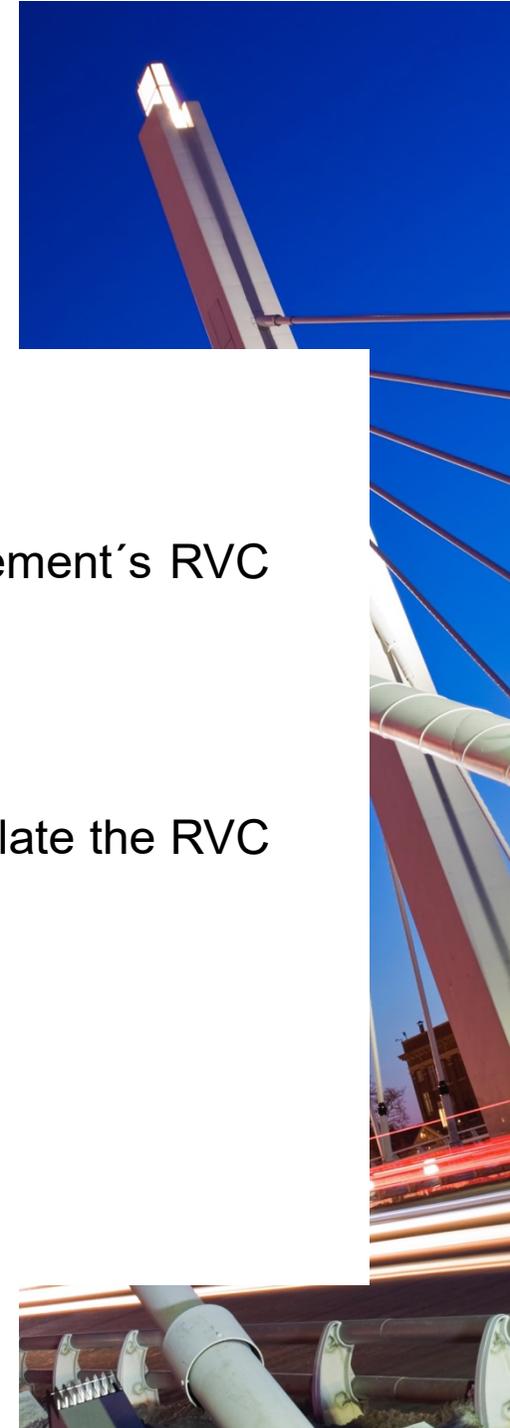
# USMCA's (Automobile) Rules of Origin Panel

- If the USMCA Panel affirms the U.S. interpretation, even if a manufacturer complies with the relevant ROO and observes all of its additional obligations, that producer still may not contribute with a 100% of its qualifying manufacturing to the region's automotive production.
- Such scenario could create the incentive for parts to be source abroad – even if there are import duties – as cheaper imports may be more attractive than costlier, wholly originating components that do not fully contribute to a motor vehicle's Regional Value Content.



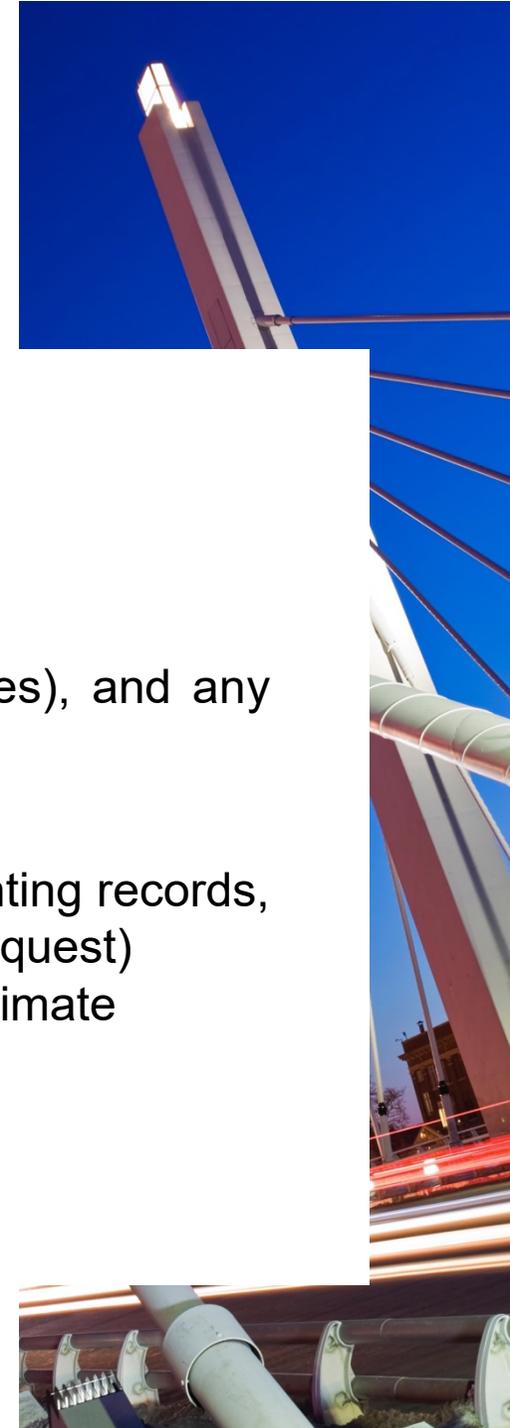
# USMCA's (Automobile) Rules of Origin Panel

- Nothing to signal that this could not become the U.S. systemic approach to the Agreement's RVC calculations for all manufactured goods.
- Particularly worrisome is the US Government's understanding that the manner to calculate the RVC is to be consistent with USMCA's text, the Uniform Regulations:
  - ✓ “ *and [the] direction from USTR and U.S. Customs and Border Protection.*”



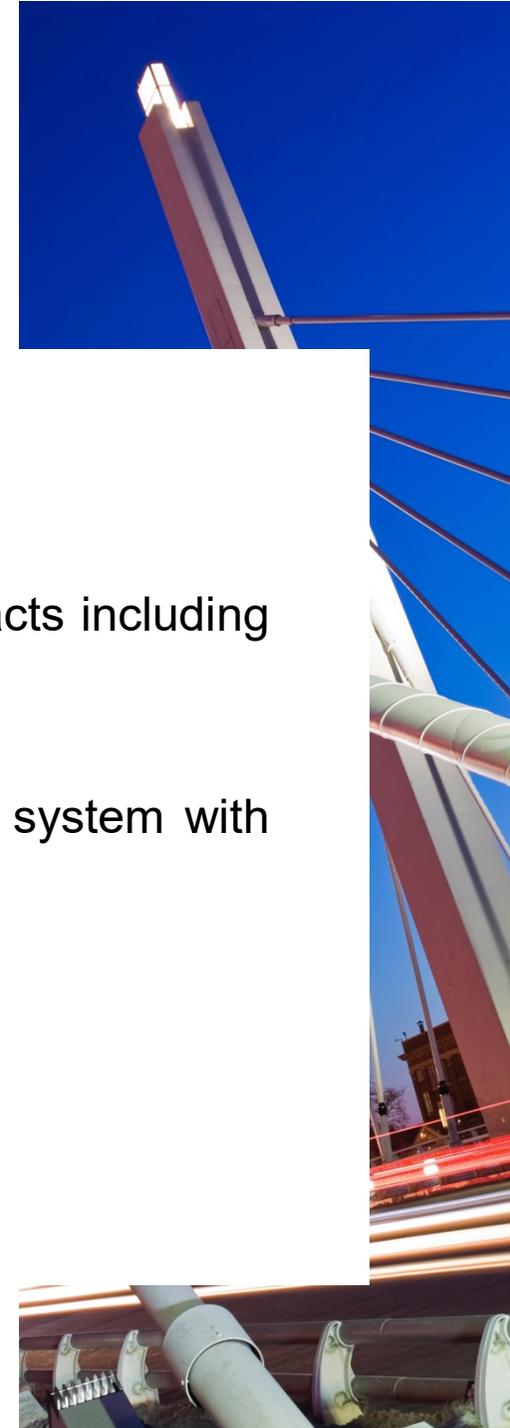
# Identification of the Ultimate Beneficial Owner

- New tax requirement that became effective as of January 1, 2022.
- Applicable to: any legal entity, all parties to a trust (settlor, trustees, and beneficiaries), and any other party with respect to contracts of any legal arrangement (JV).
- What is the requirement about: To identify, obtain and maintain, as part of the accounting records, and to provide to the Mexican tax authorities (upon request) accurate, complete and updated information of the ultimate beneficial owner.



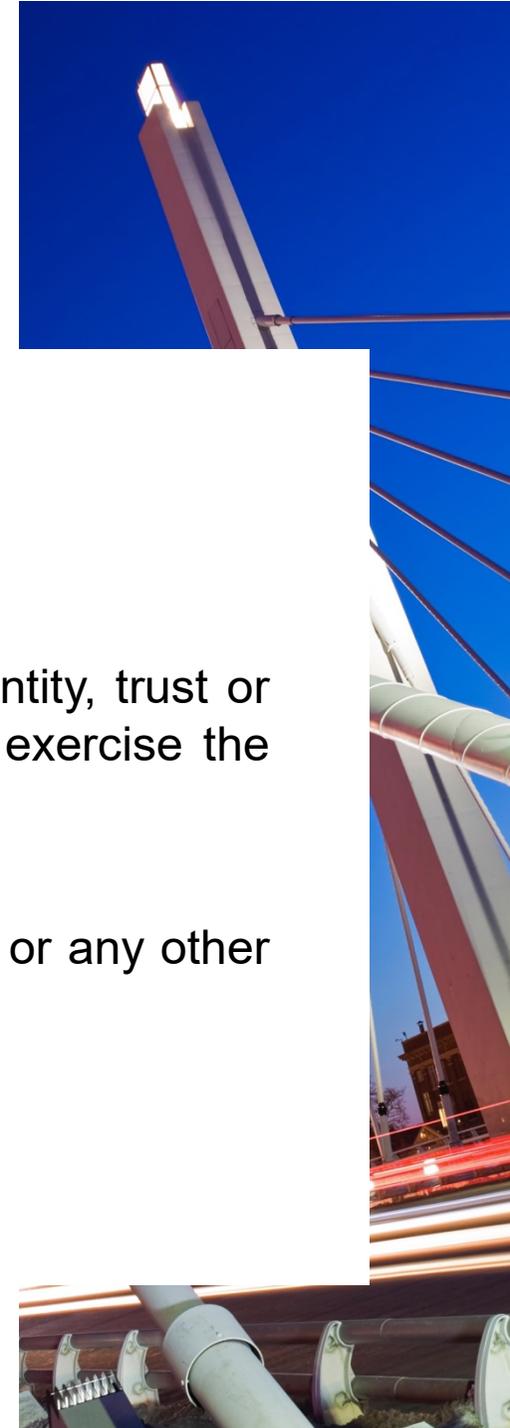
# Identification of the Ultimate Beneficial Owner

- In addition, notary publics that incorporate entities or that intervene in any other contracts including trust agreements, must request information to identify the ultimate beneficial owner.
- Also, this obligation applies to financial entities or members of the Mexican financial system with respect to financial accounts.



# Identification of the Ultimate Beneficial Owner

- Who is the ultimate beneficial owner: individual or group of individuals that:
  - ✓ Directly or indirectly obtain a benefit resulting from their participation in an entity, trust or any other legal arrangement, or that individual or individuals that ultimately exercise the rights of use, benefit, or disposal of an asset or service.
  - ✓ Directly or indirectly (even in a contingent way) has control of an entity, trust, or any other legal arrangement.

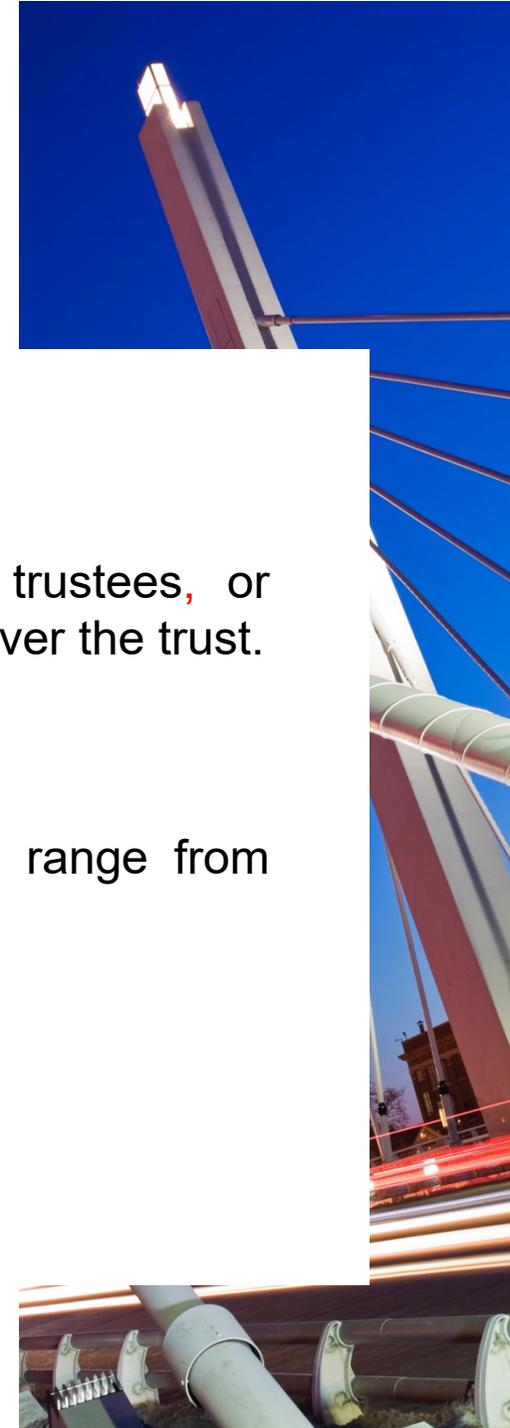


# Identification of the Ultimate Beneficial Owner

- An individual or group of individuals shall be deemed to have control, through ownership of equity, or by contract, or any other legal act when such individual or group of individuals can:
  - ✓ Impose, directly or indirectly, decisions in the shareholders' or partners' meetings (or similar) or to designate or remove most of the members of the board of directors (or their equivalents)
  - ✓ Maintain ownership of the rights that allow them, directly or indirectly, to exercise the voting rights with respect to more than 15% of the capital stock
  - ✓ Manage, directly or indirectly, the administration, strategy, or main policies of the legal entity, trust, or any other legal arrangement or body.

# Identification of the Ultimate Beneficial Owner

- In the case of trusts, the ultimate beneficial owner shall be either the settlor, trustees, or beneficiaries or any other person that has the effective control, even if it is contingent, over the trust.
- Failure to comply with the aforementioned new requirements could generate fines range from US\$20,000 to US\$100,000 (in addition to other potential sanctions).



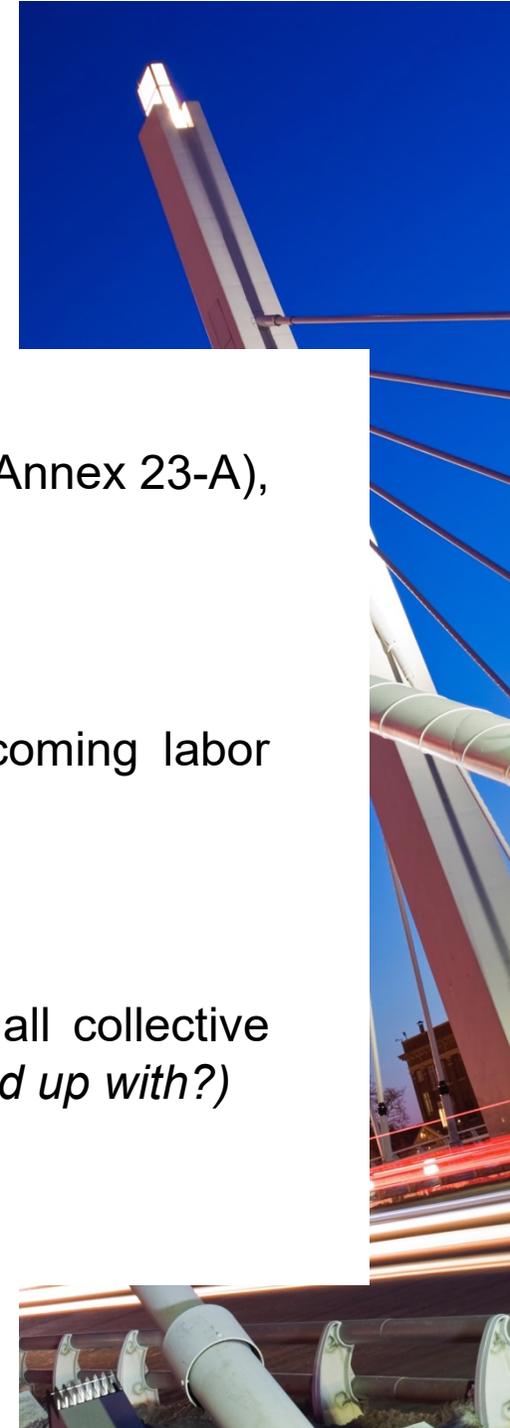
# USMCA-Driven Labor Reforms in Mexico

- A new labor ball game in Mexico?
  - ✓ There will be real, working unions
  - ✓ Collective contracts signed with employer-friendly unions (commonly known as “protection” contracts / “white unions” contracts) will be out the door
  - ✓ This will likely bring new leadership and more than one union to a company.



# USMCA-Driven Labor Reforms in Mexico

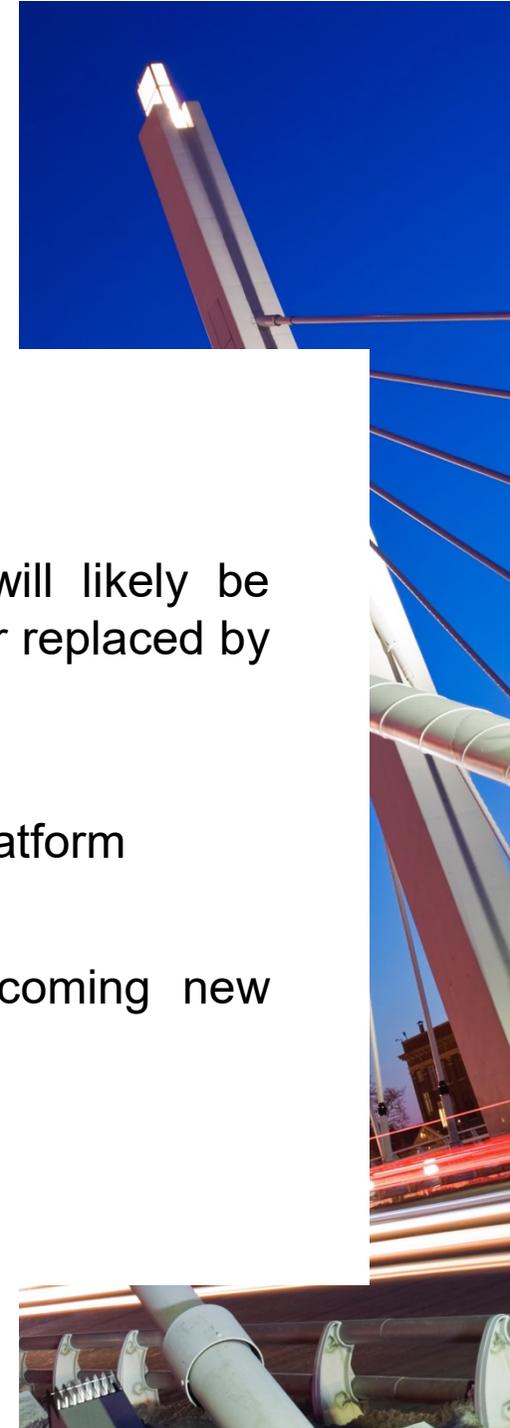
- USMCA entered into effect July 2020 and, as part of its commitments (Chapter 23 and Annex 23-A), Mexico obliged itself to reform its labor laws
- On May 1, 2019, Mexico issued its final legal amendment to support the then incoming labor provisions
- By May 1, 2023, all collective bargaining agreements should be legitimized; if not, all collective bargaining agreements will be automatically terminated. (*What will your local facility end up with?*)



# USMCA-Driven Labor Reforms in Mexico

## ■ Possible Impacts to Employers

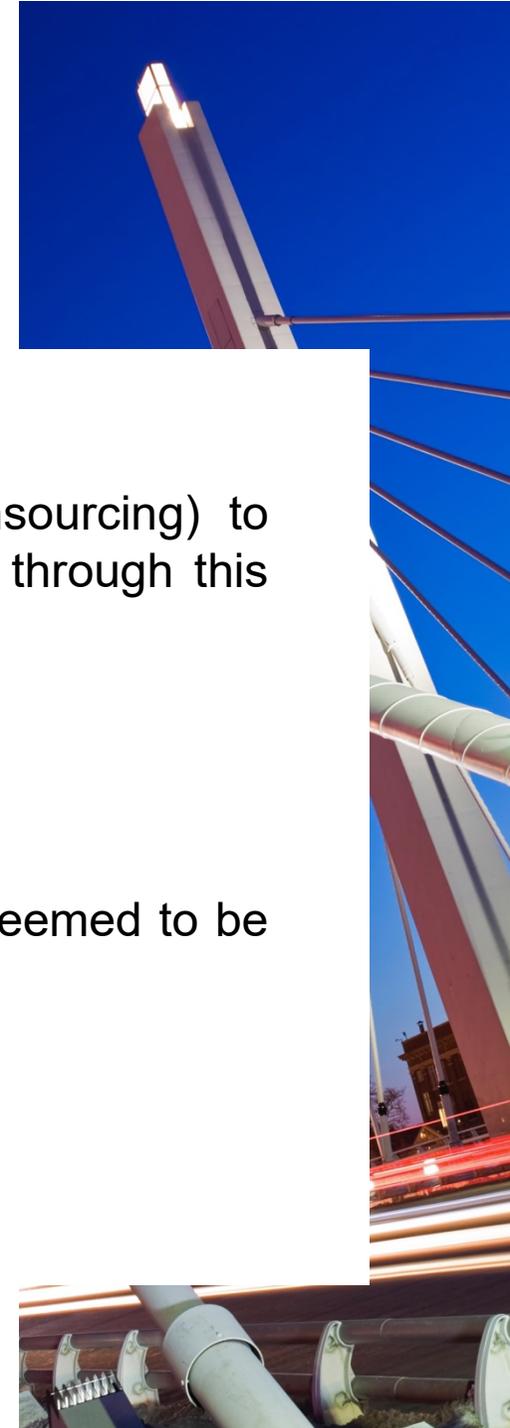
- ✓ “Protection” labor contracts (i.e., those signed with employer-friendly union) will likely be challenged and, depending on company-by-company negotiations, either ratified or replaced by other contracts
- ✓ Younger union leaders will likely be elected under a perceived more-progressive platform
- ✓ Time to strengthen the Mexican Human Resources departments, identify incoming new leadership, and know what may be bringing restlessness to your work force.



# Outsourcing in Mexico: Recent Developments

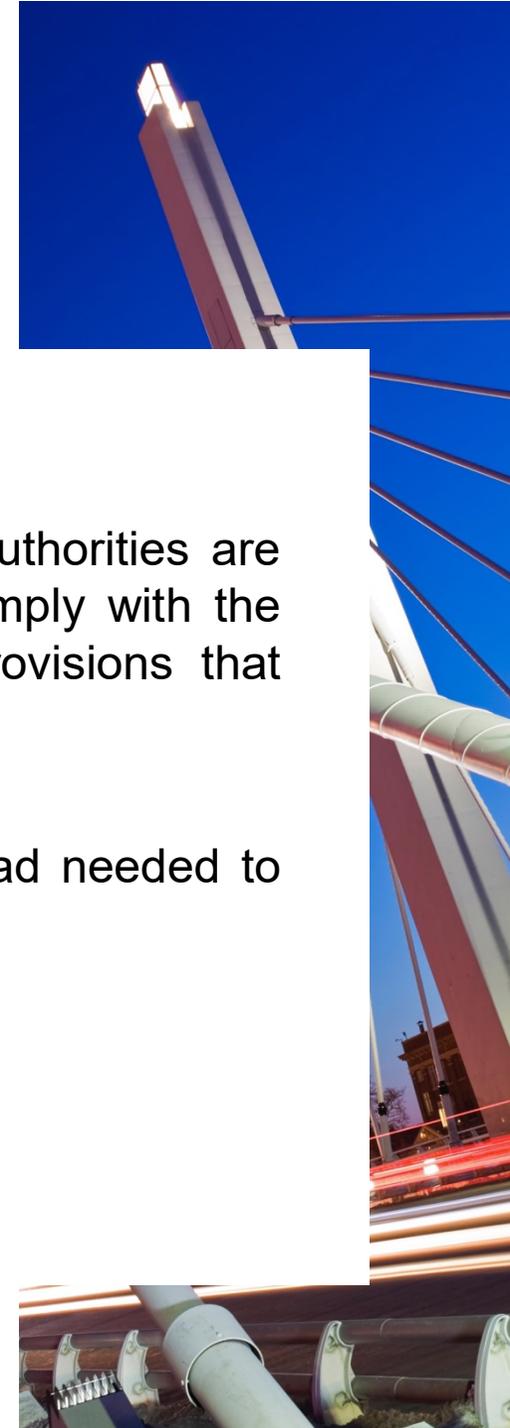
- Background

- ✓ Mexican companies commonly used payroll companies (outsourcing and insourcing) to indirectly hire employees. Many of those companies reduced their tax burden through this structure.
- ✓ On September 1, 2021 the use of payroll companies was prohibited.
- ✓ The use of outsourcing structures can continue to be used if the services are deemed to be specialized and a governmental authorization called “REPSE” is obtained
- ✓ Failure to comply with these prohibitions could result in consequences.



# Outsourcing in Mexico: Recent Developments

- Latest Developments
  - ✓ Many companies were able to obtain the REPSE. However, Mexican labor authorities are currently auditing companies that obtained the REPSE to verify that they comply with the applicable requirements. This was enhanced by an amendment to legal provisions that became effective on August 24, 2022.
  - ✓ It was not clear if Mexican shared services companies assisting entities abroad needed to obtain the REPSE.
  - ✓ Still many doubts on the application of the outsourcing provisions exist.



# Are Mexico's TROs (Temporary Restraining Orders) an option?

- Should consider State vs Federal statutes provisions
  - ✓ Mexico City has historically considered *Force Majeure* and Unforeseeability of Events Doctrine; other States still working around them
  - ✓ In Federal Civil Procedures, judges can grant all appropriate injunctions to maintain *status quo*, even without prior notice to Defendant. Requesting party should guarantee possible damages and loss of profits that Defendant may suffer.
- Do you know what is considered in your current T&Cs? [*Have you checked the children, When a Stranger Calls* (2006) situation?]



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