Auto parts companies could pay more income tax for their *maquila* operation in Mexico

Although the approved Economic Package for Fiscal Year 2022 did not increase the Income Tax rate (ISR) to be paid by legal entities, it does contain a modification whose practical effect will be that many Mexican auto parts companies pay more ISR for the *maquila* operation they carry out.

In Mexico, a large number of companies operate whose activity consists of temporarily importing inputs and consumables to make, or "*maquilar*", auto parts on behalf of their "principal" abroad. These *maquiladora* companies only receive income taxed in Mexico for providing the *maquila* service, while the income from the sale of the auto parts they produce is taxed in the jurisdiction of the principal abroad, a situation that does not satisfy the Mexican tax authorities.

For 2021, the *maquiladoras* will be able to determine their ISR under one of the following two methods: (i) the minimum tax profit or "Safe harbor" or (ii) according to the specific profit margin agreed with the tax authorities in a particular resolution known as "Advance Pricing Agreement" (APA). While "safe harbor" is a rigid method, the APA seeks to reflect the specific situation, characteristics and conditions of each *maquiladora*.

However, as of fiscal year 2022, the APA is eliminated as a method to determine the amount of the ISR to be paid (art. 182 of the LISR). Therefore, all the maquiladora companies in the country will have to determine and pay their ISR under "Safe harbor", i.e., using as the taxable base the bigger amount resulting from applying 6.9% on the total value of the assets used or 6.5% on the amount of the operating costs and expenses. In capital-intensive companies, the common denominator of auto parts companies, the application of this method usually results in the payment of ISR much higher than would be paid under an APA.

This is a very relevant modification that will surely affect auto parts companies, and those in other sectors that had been taxed under an APA. Therefore, we suggest immediately evaluating the impact of this modification on the operation of the company and identifying the corresponding mitigation mechanisms, including the validity and destination of the particular resolutions in progress.

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S I N C E R E L Y

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