Employer Substitution in Mexico's Subcontracting Reform Bill.

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By means of the Reform Bill submitted by President Andres Manuel Lopez Obrador on November 12, 2020, his Administration intends to amend certain provisions of the subcontracting regime (insourcing and outsourcing) from the Mexican Federal Labor Law and the Mexican Social Security Law, among other laws (the "Reform Bill").

Key Change

In essence, the Reform Bill seeks to prohibit the subcontracting of workers in its current state, only allowing for the rendering of specialized services under certain conditions, therefore, if approved as submitted, the companies currently employing outsourcing or insourcing schemes shall regularize their situation in order to comply with the new regulations through a transfer of employees from the "services" company to the "operative" company. Such transfer of employees is formalized through an employer substitution.

The New Enforceability Requirement

Among other things, the Reform Bill adds a new essential requirement for the enforceability of employer substitutions to be carried out once this bill comes into force, by proposing the the addition of a paragraph to Article 41 of the Mexican Federal Labor Law, establishing that in order for employer substitutions to be valid and enforceable, a transfer of the substituted company's assets shall be carried out in favor of the substitute employer. Until now, court precedents and the Mexican Social Security Law merely assumed the existence of an employer substitution upon: (i) the transfer of business essential assets with the intent of continuing their exploitation, and (ii) a shared presence of a majority of partners or shareholders between the companies; however, the validity of the employer substitution was not conditioned to the formalization of such transfer of assets, nor was required to evidence it in the substitution process.

Future

Upon hard lobbying from Mexican business groups, on December 8, 2020, the Federal Executive Branch requested the Federal Legislative Branch to delay until February, 2021 the discussion of the Reform Bill, intended to be appointed as a preferential bill, which would in turn mean that it could be discussed, and approved, within a 30 days-period. If approved as it is, the mandatory regularization that shall be carried out by the companies using insourcing or outsourcing services, shall also include the formalization of the legal documents related to the transfer of the company's assets by the "services" company in favor of the "operative" company. This additional requirement does not exist at this moment.

Actions and Compliance

Taking into consideration the particularities of each case, we recommend that the companies currently using insourcing or outsourcing schemes to first analyze the preventive plans that could be employed to avoid falling, once the Reform Bill is enacted, under the situation requiring such condition to be met. Once the Reform Bill comes into force, we would recommend to evaluate a compliance plan for this new obligation to consequently avoid any of the penalty fees considered in the bill. For current outsourcing schemes, the execution of assets purchase and sale, or assignment agreements shall be primarily explored, taking into consideration the assets that would be effectively transferred to the substitute employer;

meanwhile, for insourcing schemes, corporate restructures through the aforementioned type of agreements, as well as through the merger of the companies participating in these schemes, could be formalized, thus transferring the substituted employer's assets.

There are multiple compliance options, and in every case with different labor, tax, social security and corporate impacts, which must be carefully examined.

Please send any question or comment to info@jata.mx. JATA is a Mexican law firm with offices in Monterrey, Mexico and Houston, Texas.

December 11, 2020.

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