



México changes Maquiladora refund operations in (VAT) per 2019

Background.

Maquiladoras or IMMEX (Manufacturing, Maquila And Export Service Industry) are manufacturing plants that import raw material from the US in to México, transform the raw material with a manufacturing process, and export a finished product, such as electronic, automotive or aerospace consumer product mostly to the US utilizing cost benefits from manufacturing in México.

In order to stimulate foreign investment, the Maquila operation is subject to a 0% (Sales tax or commonly referred to as Value added Tax, “VAT” hereinafter) this benefit translates into the ability to request a refund for all of the VAT that the Maquila spend in Mexico on their vendors related to the Maquila operation on a monthly basis.

This right usually gives them the ability to have a favorable balance of VAT tax on a monthly basis. Before 2019, Federal tax code permitted that any taxpayer may offset this favorable balance of VAT, against any taxes there are owed to the federal government, this presented a great advantage to the Maquila operation because, it could offset its favorable balance of VAT tax, against the withholding tax for their employees or any other federal obligation related to the Maquila process, this gives the operation more cash flow on a monthly and yearly basis, because the obligations between the parties was automatically settled out.

Up until 2019 the VAT tax rate was 16%, so the favorable balance of VAT was usually compensated or offset against the companies own obligations and withholdings.

New regulations per 2019

As a positive move the VAT tax rate has been lowered for the border area to 8%, however Federal legislators have revised a yearly law (Ley de Ingresos de la Federación 2019 or Yearly Income law 2019) and not the Federal tax code or VAT law and have changed¹ to indicate that taxpayers *may no longer offset favorable balance* of VAT tax against any obligations or withholdings that they have with the federal government.

This means that for January 2019 *going forward* they will have separate obligations per each tax, (VAT, Income Tax, Withholdings, etc.) and may not offset or compensate favorable balance of each other on a monthly or yearly basis.

¹ This has generated some amount of confusion because the revision was made to the yearly law, and not to federal tax code and or VAT law, hence lawsuits and arguments about the revision are still moving forward to this date. It is clear that the Mexican Government’s intentions are that Maquilas must request refund of any Favorable VAT tax going forward on a monthly basis and not compensate such favorable balances.



As a consequence, the Maquila operation will have to file a monthly VAT refund on a timely basis in order to try to receive as much cash flow from their operation expenditure, because they may no longer compensate the favorable balance of VAT against their employees withholdings, income tax or other obligations, and the refund must now be filled per the *total amount of the favorable balance*. This monthly refund will be answered and approved or denied, depending on the criteria of the tax authority, where it must evaluate that all invoices requested per the return meet all requirements.

In the past because the compensation or offset notice was performed automatically, the process was subject to much less analysis by the tax authority and usually authorized the compensation notices without much issue, because they did not review each invoice per operation.

In our experience the refund process is much longer and sometimes difficult because the tax auditors frequently request additional information that may, or *may not* be exactly applicable to the refund request, however this process must now be performed on a monthly basis in order to recuperate the cash flow expenditure from vendors, because the operation may not offset this balance against other taxes.

For starters, we consider that this legislative change will bring more refund returns to the tax authority, however it is clear that the refund process, will now analyze *in more detail* the right to claim the return, and as such, if any portion of the return is denied, legal advice per any denial or balance that is not fully recovered, is not only recommended, almost mandatory².

Any favorable balance of taxes that was generated previous to 2018 may only be compensated against obligations of those years and not 2019 going forward, hence this favorable balance must be requested, and if denied must be litigated within 30 days of the notification of the denied invoice and expenditure. As such it is important to have legal advice to review any final balances of VAT tax up until 2018 and to present the filing accordingly.

Because the favorable balances of VAT are now capped or limited to 2018, it is very important to identify the invoices associated with this expense and file the refund accordingly because the statutes of limitations are 5 years on those expenditures to claim the refund.

In some occasions the tax auditors do not agree to certain invoices or expenditures, and they have a tendency to condition the total return to the taxpayer from desisting or not requesting some invoices. Our law firm has experience in these cases so we can review and help the company recuperate those VAT tax expenses in the Maquila operation for 5 years going back.

² We recommend that we help the Maquila operation review all resolutions that authorize or resolve the VAT refund request, in almost all cases they do not pay the full amount.



Our recommendations.

It is important to have a *dedicated accounting staff* that process the IVA returns on a monthly basis, this must be performed like clockwork in order to recuperate the VAT tax as quickly as possible. Depending on the number of documents involved in the return this may take from 2 to 6 or more months from filing to reimbursement and deposit in the bank, even for certified Maquiladoras.

In most cases the tax authority does not pay interest on this return even though they are obligated to do so, and in order to recuperate the interest, legal action must be taken on the refund return, no later than 30 days after the refund was notified, hence legal review on all returns is recommended.

Legal advice to recuperate any favorable VAT balances will now be more important than ever, please contact us to advise, so that we can review and recuperate any pending and all expenditures going forward.

March 2019

Best Regards

Adrian Ocampo, Esq

adrian@ocampo.biz

(619) 666 94 65

Independent Tax attorney that specializes in Maquiladora Legal and Tax issues in Mexico.