DOING BUSINESS *IN MEXICO*

2020

VTZ

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ABOGADOS

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INTRODUCTION

As a result of Mexico's Trade and Investment Promotion Agency -PROMEXICO– extinguishment, ***Vázquez Tercero & Zepeda (VTZ)*** seeks to fill that void and promote Mexico as a business destination.

This is why **VTZ** has developed the guide **Doing Business in Mexico 2020,** which is divided into the following seven chapters:

1. *Why Invest in Mexico?*
2. *Foreign Investment.*
3. *International Trade Policy.*
4. *Trade Policy for the Manufacturing Industry.*
5. *Creating a Company in Mexico.*
6. *Taxation.*
7. *Labor & Migration.*

In line with our values, our chapters seek to provide relevant business and legal information in a practical and concise manner. This chapter, *Labor & Migration,* our member ***Rafael Alday*** will provide a general overview on the relevant labor law provisions on employment, from worker rights, dismissals to unions and collective bargaining, including a brief summary regarding the USMCA, the rapid response mechanism, as well as information on migration.

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7. Labor and Migration Environment

Mexico's labor framework is set forth in the Constitution and the Federal Labor Law (hereon "Labor Law"). Accordingly, a "job" or "working relation" is defined as *rendering of a subordinated personal service to another person in exchange for a wage.*[1] The job definition is quite broad because any person that renders a *subordinated* service to another, who in turn pays compensation, is deemed as an employee, regardless of the nature of the service performed, and he or she is entitled to labor rights.

Pursuant to the Labor Law, workers are entitled to numerous rights. Employees are entitled, for instance, to profit sharing, which can only be dismissed in a limited number of cases. If a worker is terminated without a justified cause, he or she is entitled to seek job reinstatement or severance pay. Indeed, foreign investors perceive Mexican Labor Law as "overprotective" and costly, as noted in WEF's Global Competitiveness Index 2019.

In addition to the Labor Law, Mexico has the following labor-related laws or regulations that complete its regulatory framework:

- Social Security Law,
- Retirement Savings System Law,
- Institute of the National Housing Fund for Workers Law (INFONAVIT Law),
- Federal Regulation on the Safety, Hygiene, and Environment at the Workplace,
- The Mandatory Standard NOM-035-STPS-2018 on Psychosocial Risk Factors at Work - Identification, Analysis and Prevention,[2] establishing the elements to identify, analyze and prevent psychosocial risk factors, as well as to promote an environment organizational support in the workplace.

The employers are required to register all of their employees before Mexican public institutions, namely the Mexican Social Security Institution (**IMSS**, acronym in Spanish), the National Housing Fund for Workers (**INFONAVIT**, acronym in Spanish) and the National Fund Institute for Workers' Expenditures (**FONACOT**, acronym in Spanish). As a result, an employer has to pay "social-taxes" to these agencies. Failing to register or make timely payments regarding these *social-taxes*, the employer is subject to penalties and surcharges.

[1] Article 20 of the Labor Law.
[2] Published on October 23, 2018, in the Official Gazette.

Also, the employer will have to register before the tax or treasury authority of the State (i.e. local authority). States collect a Payroll tax that is paid by the employer based on wages and other expenditures.

7.1 Individual Employment Agreements

As a general rule, the Labor Law establishes that an individual employment agreement duration is *indefinite* (i.e. permanent). Temporary contracts are permitted, however, only when there is a justified cause, such as probationary periods, initial training, among other situations.

7.2 Foreign Employees

Mexican employers may hire foreign employees. However, the Labor Law provides that employers must comply with the Mexican-foreign employees nine to one ratio. In other words, Mexican nationals must represent at least 90% of the business' workforce in Mexico.

The Labor Law provides some exceptions to the Mexican-foreign employees ratio rule. For example, the Mexican Labor Law provides that if there are no Mexican technicians or professionals, the company may temporally hire foreigners with the required expertise for the specific service; high-level foreign officers of Mexican entities are exempted at all times.

7.3 Outsourcing

Outsourcing labor legal schemes are carefully regulated to prevent their abusive use against employees and their labor rights. The 2012 labor reform[3] introduced the *"outsourcing or subcontracting regime"*, including two very relevant provisions. In essence, a labor-intensive service agreement, for instance, may have far reaching legal consequences to the extent of deeming service provider's workers as employees of the contracting company.

[3] Amendments to Labor Law published on November 30, 2012 and being effective as of December 1, 2012.

In essence, the Labor Law considers that outsourcing entails a "contractor" (i.e. outsourcing company) that performs work or provides services to a "beneficiary", an individual or enterprise. The beneficiary sets the tasks and supervises the development and execution of the contracted work. In turn, the outsourcing company will carry the services or work with his own employees.

An outsourcing company is responsible for all labor obligations, including social security and tax regarding, his employees. Needless to say, the beneficiary of the outsourcing services is jointly liable in the event that the outsourcing company fails to fulfill its labor obligations (including tax and social security).

The Labor Law considers, for instance, "human resources" companies (e.g. head-hunters) as intermediaries and not employers. However, if a "human resources" company provides a service that entails having the "employee" on its payroll, then said company is deemed as an outsourcing employer and, thus, it is responsible on labor law matter with the employee.

A valid outsourcing agreement must meet three requirements to avoid that service provider's workers are deemed employees of the beneficiary.

- First, the outsourcing agreement shall not cover all activities, whether identical or similar as a whole, carried out in the beneficiary's workplace. For instance, if the beneficiary's business is the production of auto-parts, the beneficiary cannot have 100% of his personnel under outsourcing; also, the outsourcing agreement cannot include technicians or workers that operate the machines to produce auto-parts.

- Second, the outsourcing agreement shall be justified by its *specialized* nature, say security or IT services. This means that, for instance, if the business is production of auto-parts, then the company can outsource security, cleaning, management, but not the main activity.

- Third, the outsourcing agreement cannot include identical or similar tasks performed by any of beneficiary's employees. For instance, a company cannot enter into an outsourcing agreement regarding cleaning activities when it has an employee that already carries out similar or identical cleaning tasks.

If any of the three requirements is not met, the beneficiary is considered the employer for all legal effects and he or she is even responsible of social security obligations.

7.4 Salary / Wages

The Labor Law provides the existence of a **general minimum daily wage**, which is defined as the minimum amount of money that a worker must receive for services rendered within a working day. Needless to say, jobs are normally subject to wages above the minimum wage, particularly in cities and the manufacturing sector.

The National Commission on Minimum Wages (CONASAMI), which is made up by government, workers and employers representatives, meets annually to establish a minimum wage. For instance, the minimum wage for 2020 is $123.22 Mexican pesos (about 5.50 USD) that is applicable mostly throughout the country. The Northern Border Strip is subject to a higher minimum wage, namely $185.56 Mexican pesos (about 8.25 USD) per workday during 2020.

The weekly work hours are determined by the work shift. The day, night, and mixed shifts entail **eight**, **seven**, and **seven and a half** working hours, respectively, and all shifts include a half-hour break.

7.4.1. Over-working hours

Mexican law allows over-working hours, but the following restrictions apply. Employees may carry out a maximum of 3 "extra" working hours per day, but an employee can only do extra working hours 3 times during a week; that is, a total of 9 "extra" working hours distributed in a week. The over-working hours are paid double the normal hour.

In the event that the employee exceeds the maximum of **3** "extra" working hours in a day or the **9** "extra" working hours in a week, the additional hour(s) are paid triple the normal hour.

7.4.2 Rest day

Wages are calculated on a seven-day week, but an employee is entitled to one day of rest, preferably Sunday, for every six-day work period with full pay. If the employee works on Sunday, a 25% bonus to his daily wage applies.

7.4.3 Labor Rights and Premiums

In addition to wages, employees are entitled to additional "payments" or rights, such as the year-end bonus (*aguinaldo*), vacations, vacation premium, among others. The Labor Law provides that these rights cannot be waived in the labor agreements.

When the employee has worked throughout the year with the employer, the year-end bonus (*aguinaldo*) shall be equivalent to 15 days of salary at least. The employer has to pay the year-end bonus the 20th of December at the latest.

Furthermore, an employee typically receives six days of vacation, which is the minimum required by Law, when he or she has worked for a year with the employer. As his or her seniority increases, the employee is entitled to more vacation days. At the beginning, the employee will increase two days of vacations each year of work during the first four years and, thus, having the right to enjoy 12 days of vacations. After his or her fourth year, the employee will continue collecting additional two additional days of vacations every five years of work.

When the employee enjoys his vacations days, the employer has to pay the regular daily wage for each day of accrued vacation, plus the vacation premium equivalent to 25% the daily wage.

7.5 Termination of Employment

Termination of employment relationship are justified under the following four possible scenarios:

1. The employee's voluntary resignation;
2. Employee dismissal with just cause;
3. Employee dismissal without just cause; or
4. Termination on behalf of the employee with just cause.[4]

[4] The employee may terminate the agreement under specific grounds as provided in article 51 of the Labor Law, for instance, wage reduction, misleading conditions of employment.

Regardless the applicable scenario, the employee is always entitled to receive a severance payment from the employer, commonly referred to as the "*finiquito*". The *finiquito* is composed of the following:

i) accrued and unpaid wages;

ii) proportional amount of the year-end bonus (*aguinaldo*);

iii) accrued vacations not taken by the employee;

iv) vacation premium; and

v) any other benefit accrued that has not been paid to the employee.

The *finiquito* payment is subject to specific rules that may vary depending on the termination scenarios. The employee is entitled to receive the following additional amounts beyond the *finiquito payment* under the following scenarios that we summarize as follows:[5]

i) **Voluntary Resignation:**[6] The employer shall pay: i) *finiquito payment,* and ii) a seniority bonus (*prima de antigüedad*) equivalent to 12 days of salary per year worked, provided that the employee has 15 or more years of seniority with the employer.[7]

ii) **Dismissal with Just Cause:**[8] The employer shall pay: i) the *finiquito,* and ii) the seniority bonus. These items that constitute "just cause" for termination of the employment relationship without liability for the employer.

[5] Disclaimer: This is a general summary and, thus, certain rules that may be applicable in a given situation are not mentioned. An Employer and/or employee must always review the severance payment with a licensed attorney.
Voluntarily resignation, of course, implies without undue pressure on behalf of the employer.

[6] Voluntarily resignation, of course, implies without undue pressure on behalf of the employer.

[7] The relevant daily wage of the seniority bonus, when applicable, is capped to the double of the minimum daily wage (246.44 pesos per day in 2020). In other words, the employee's daily salary level may be disregarded when his daily wage exceeds the double of the minimum daily wage.

[8] For instance, an employer is authorized to fire an employee that steals from the employer, an employee that performed a "violent" act against his colleagues or the employer, among other situations as indicated in the Labor Law.

iii) **Dismissal without Just Cause:** [9]The employer shall pay: i) the *finiquito*; ii) ninety (90) days of salary; iii) 20 days of salary per year worked; and iv) the seniority bonus.

iv) **Termination of the Employee with Just Cause:** The employer shall pay i) the *finiquito*; ii) ninety (90) days of salary when the employee claims compensation, or 20 days of salary per year worked when the employee claims reinstatement but the employer denies the reinstatement; and iv) the seniority bonus.

7.7 USMCA Labor Chapter

The US-Mexico-Canada Free Trade Agreement (USMCA) redefines what constitutes a modern free trade agreement because not only does it include non-trade disciplines, such as Chapter 23 – Labor (hereon "Labor Chapter"), but also novel "enforcement" mechanisms. USMCA entered into force on July 1st, 2020, and its Labor Chapter introduces binding commitments on the following internationally labor rights:

1. freedom of association and the effective recognition of the right to collective bargaining;
2. the elimination of all forms of forced labor;
3. the effective abolition of child labor;
4. the elimination of discrimination in respect of employment and occupation; and,
5. acceptable working conditions, i.e. minimum wage, working hours, and safety and health in the job.

In addition, the labor chapter includes provisions that USMCA parties must effectively address any incident of violence against workers when exercising their rights; to protect migrant workers under their local laws; as well as to protect workers against discrimination on the basis of gender, pregnancy, sexual orientation, gender identity, and caregiving responsibilities; provide job protected leave for birth or adoption of a child and care of family members; and protect against wage discrimination.

[9]A dismissal with just cause may become a dismissal without just cause if the employer fails to carry out the dismissal process as indicated in the Labor Law.

7.7.1 Labor Chapter and its Enforcement Mechanism

USMCA entails several mechanisms that allows the parties as well as private individuals to interact on labor matters.

7.7.1.1 Public Communications

Similar to the *OECD Guidelines for Multinational Enterprises*, USMCA also provides a public communication platform whereby a person may submit written queries to the "National Contact Point" of a Party, say Mexico, regarding any matter related to the Labor Chapter. In turn, Mexico will have to consider the raised matter and normally provide a written and public response.

The public communications mechanism is a two-edged sword. On the one hand, it allows a Party like Mexico to identify flaws in the application of its labor laws as well as to address labor matters before they further escalate into a possible international USMCA dispute. The public communications mechanism, on the other hand, may prove useful for foreign stakeholders (such as unions, NGOs) to collect evidence on possible denial of labor rights and submit a complaint before the relevant body to trigger an "enforcement" mechanism.

7.7.1.2 Enforcement Mechanism: State to State Disputes and Rapid Response Mechanism

The USMCA provides two "enforcement" mechanisms to demand compliance with substantive labor provisions. The first entails a "**general" mechanism** because any matter relating to a provision established in the Labor Chapter may be subject to a State-to-State dispute. After a series of mandatory consultations, the complainant party, say the USA, may request the establishment of a panel if no agreement is met. If the Panel determines that there has been a violation on behalf of the responding party, the USA may, for instance, suspend benefits, such as preferential tariffs.

The second enforcement mechanism is the ***facility-specific rapid response labor mechanism*** or **RRLM**, introduced in the USMCA Amendment Protocol signed in December 2019. The scope of the RRLM is, in principle, limited to matters relating to freedom of association and to effective collective bargaining in a specific facility within the so-called priority sectors. The enforcement of these rights in Mexico has been a major source of concern for unions in the USA and Canada.

It goes without saying that the RRLM's is available between US-Mexico or Canada-Mexico only, and the RRLM works, in essence, as follows:

- If a Party deems that a facility is denying labor rights to its workers, the US, for instance, may "trigger" the RRLM providing the relevant details of the case to Mexico. Mexico will have the opportunity to investigate and report back on whether there has been or not a denial of rights; if Mexico confirms that there has been a denial of rights, Mexico will also provide an "action plan" (i.e. remediation measures).

- Consequently, the US may either accept or reject Mexico's finding or, if applicable, remediation measures; if rejected, the US may, eventually, request the establishment of a RRLM panel.

- After reviewing the case and possibly visiting the facility, the RRLM panel will eventually make its determination. It is at this point where the US may be authorized to apply remedies against the products or services of the facility provided that the RRLM panel, of course, finds that there has been a denial of rights or the remediation plan is insufficient.

According to the rules, the process is designed so that the panel issues its determination about 115 days after the RRLM was activated. For a flow chart regarding how the RRLM, please visit our presentation in the following link: USMCA Labor & Trade.

7.7.2 Labor Mexican Amendment: Unions and Collective Bargaining

As a result of USMCA's Labor Chapter, in particular **Annex 23-A**, as well as the approval of Convention 98 of the International Labor Organization, Mexico carried out a Labor Law Reform seeking to comply with its international commitments. Published on May 1, 2019, the Labor Law Reform focuses on provisions related to the freedom of association, unions, collective bargaining, among other matters.

Protection contracts have been an issue for workers that have sought to enforce their collective labor rights in Mexico. A protection contract is a collective labor agreement executed between a company and a union, normally, before employees are hired. Foreign investors may find this situation quite strange:

Why should a company enter into collective labor agreement without having employees?

The answer, in fact, is quite simple. Companies cannot carry out their productive activities while facing a strike challenge, and a protection contract is a legal tool to prevent possible strikes on behalf of a "union", which is, of course, non-dominant.

In turn, the protection contracts posed a serious challenge to employees that sought worker representation. On the one hand, the law previously authorized only one union per company, and, on the other hand, the "union" may have no interest in representing the worker. Consequently, the worker or workers are forced to form a union, challenge the dominance of the other union in the Conciliation and Arbitration Board, and win the legal challenge to be recognized as the dominant union to enter into collective bargaining negotiations and agreements.

Notwithstanding the foregoing, the Labor Law Reform seeks to prevent the so-called "protection" contracts and transform the labor environment in Mexico. For instance, new companies or investments cannot enter into "protection contracts" as described above since the law now requires that a majority of the employees to approve the collective labor agreements; in turn, the majority of the workers must also approve a strike challenge. Thus, strikes on behalf of non-existent unions or group of workers is, in theory, prevented.

In essence, the 2019 Labor Law Reform seeks to empower workers in the life of union and the company, as well as reducing the employer's interference in union activity. Consequently, employees of a company must be introduced to the union leadership, and the labor authority has the power of review and sanction, if necessary, when a company or employer is not complying with these new provisions.

As of today, Mexico is carrying out the following actions in order to properly implement the Labor Law Reform and comply with USMCA's labor chapter:

1. the creation of the Coordination Council for the Implementation of the System Reform of Labor;
2. the creation of working groups at a State level to implement the Reform;
3. the publication of the Existing Collective Labor Agreement Legitimization Protocol;
4. the establishment of the Federal Center for Conciliation and Labor Registry, State Conciliation Centers, Federal Labor Courts, State Labor Courts;
5. The disappearance of the Conciliation Boards and Arbitration is still pending.

It is noteworthy that the Federal Center for Conciliation and Labor Registry, State Conciliation Centers, and courts will enter into operations through phases per the implementation of the so-called "New Labor Model".

The first 10 states, such as Guanajuato, San Luis, State of Mexico, will being the implementation of the New Labor Model by the end of 2020. The transition towards this new labor regime will conclude, in theory, in 2022, but this transition may, perhaps, change as a result of COVID-19.

7.8 Migration Matters

The Migration Law provides several ways through which a foreigner may eventually obtain a permanent residency migration status in Mexico. The investor visa, for instance, requires a foreigner to invest a certain amount either in an existing company or when incorporating a Mexican company. A foreigner with an investor visa may eventually have the permanent residency, but having such migratory status is a gradual process.

The law also introduces a resident visa for foreigners that have made a real estate investment. Similar to the investor visa, the foreigner would obtain first a temporary residence visa, and he or she may have access to the permanent visa after several years, provided the conditions are met.

A company that seeks to hire a foreigner as a worker must have a "permit" on behalf of the **National Institute of Migration** (INM, acronym in Spanish). Once authorized, the company can issue employment offers to foreigners, who will have to apply for the temporary residence visa or, if applicable, the permanent visa. Failure to comply with the Migration Law, the company may face harsh penalties.

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