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The maquiladora industry, which enjoyed a nearly tax-free status for the past five years, is scheduled to lose its exemptions at the beginning of 2000. In mid-August, the Secretaria de Hacienda y Credito Publico (SHCP) announced that maquiladora plants will have to begin paying taxes on income related to machinery and inventory. The plants had been exempt from these taxes since 1995, but were required to pay taxes on income for payroll and services. The policy change will affect the nearly 3,300 maquiladora plants operating in Mexico, most of which are located near the US-Mexico border. The majority of maquiladoras are subsidiaries of US companies, although a growing percentage are affiliated with companies based in Taiwan, South Korea, and Japan.

Mexico negotiating treaty with US to avoid double taxation

The new tax would reverse exemptions enacted in 1995, which were intended to prevent double-taxation. Mario Gabriel Budebo, the SHCP's coordinator of income policy, said the new tax is based on the assumption that maquiladora branches are established for business on a permanent basis. Article 5 of the current US-Mexico tax treaty states that a US company is considered to have a permanent establishment in Mexico if it owns goods in the country that are processed by a dependent agency using assets supplied by the US company. "The change would tax the profits generated in Mexico, because that is really where we are ceding to the US tax collectors," said Budebo. "We are exporting taxes."

The possibility of having to pay the same tax in two countries initially caused the Consejo Nacional de la Industria Maquiladora de Exportacion (CNIME) to oppose the new tax on machinery and inventory. "This measure would raise production costs of manufacturing and cause us to lose competitiveness to other countries," CNIME president Humberto Inzunza Fonseca told Reuters news service in early August. The CNIME president said the 40% corporate tax imposed by Mexico added to the corporate tax on revenues by the US Internal Revenue Service (IRS) could force maquiladora plants to pay taxes totaling 75%.

But Inzunza said the CNIME has decided to keep an open mind regarding the new tax because of government assurances that a new taxation treaty with the US would be in place before the new tax becomes effective. The two countries have been negotiating the treaty since February of this year. "We were assured by President Ernesto Zedillo, the SHCP, and the Secretaria de Comercio y Fomento Industrial (SECOFI) that the government is holding intense talks with the US to reconcile both countries' tax systems," Inzunza told the daily newspaper The News in late August.

Maquiladora plants also face other taxes

The tax on inventory and machinery is the second change in Mexico's tax code affecting the maquiladora industry. In January of this year, the SHCP began charging value-added tax (impuesto al valor agregado, IVA) on all components brought into Mexico. The government granted a special

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waiver allowing maquiladora plants to petition the government to recover the IVA on those imports. However, maquiladora executives have complained that the petition process has become cumbersome because of the extensive work required to recover IVA payments. The two new taxes are only the first changes in the fiscal transformation of the maquila industry.

Beginning in November 2000, maquiladoras will no longer be exempt from import tariffs for products originating in countries that do not have a trade agreement with Mexico. President Zedillo proposed the new policy in combination with reductions in income tax (Impuesto Sobre la Renta, ISR) and IVA as an incentive for maquiladoras to begin seeking Mexican suppliers for some their components. But the new policy is unlikely to promote any significant increase in domestic-component usage, since most parts are already imported duty-free from the US under terms of the North American Free Trade Agreement (NAFTA).

Maquila industry criticized for domestic practices

Many critics say the maquiladora sector has failed to respond to complaints about its inability to incorporate more Mexican parts in its final product. "Between 1988 and 1998, Mexican products comprised only 2% of the parts used by maquiladoras," said Laura Juarez, a researcher at Universidad Obrera de Mexico (UOM). Juarez said the maquiladora sector also fails to promote development in Mexico because its operations involve only assembly and light manufacturing. "These facilities have only a limited impact on the domestic market because they are so closely linked to the productive process in the US," said Juarez.

While the maquiladora industry is losing some tax protections, federal and local authorities continue to provide other benefits to the industry. Some benefits come in the form of labor laws that are weaker for maquiladora than for other Mexican plants under the federal labor code (Ley Federal del Trabajo, LFT). Weak labor laws allow maquiladora managers to pay employees low wages and reduced benefits while discouraging the formation of unions, Juarez said at a recent forum in Mexico City. Juarez said real wages for employees at maquiladora plants have fallen by 23% in the past five years. (Sources: Novedades, 08/11/99; La Jornada, 08/11/99, 08/12/99; El Economista, 08/11/99, 08/20/99; El Universal, 08/11/99, 08/20/99; Reuters, 08/19/99; The News, 08/20/99)

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