The Multilateral Instrument Becomes Effective in Mexico

By Edgar Klee, Fernanda Ruizesparza | June 29, 2023

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A decree promulgating the "Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting" (the "MLI" or "Multilateral Instrument") was published in the Official Federal Gazette ("*Diario Oficial de la Federación*") on June 19, 2023. The part of the MLI that applies to international tax treaties between Mexico and other nations that have acceded to the MLI will go into effect on July 1, 2023, whereas the part of the MLI that covers taxes withheld on payments to foreign residents will go into effect on January 1, 2024.

The MLI was signed by Mexico in June 2017. It was approved by the Chamber of Senators in October 2022 and the Senate's ratification was signed by the Executive Branch in December 2022. Mexico subsequently deposited the accession documents with the Organization for Economic Cooperation and Development ("OECD") in March 2023.

The MLI does not replace the existing double taxation treaties but complements them. Its main purpose is to enable OECD member countries (such as Mexico, Singapore, Canada, France, and Spain) to conform, align, and modify existing international tax treaties without the need to renegotiate each one of them, and thus avoid undue and abusive interpretations of international tax treaties. However, under the principle of "later law supersedes earlier law," the MLI prevails over earlier treaties on the subject matter.

The MLI includes several measures related to the Base Erosion and Profit Shifting Action Plan ("BEPS"), such as rules on (i) hybrid instruments, (ii) permanent establishment, (iii) dispute resolution, and (iv) anti-abuse of treaties; and significantly changes Mexico's taxation system on international matters and may significantly impact various taxpayer operations. Mexican tax authorities could question the use and application of international tax treaties under the MLI's mechanisms and minimum standards.

For example, Mexican tax authorities could deny benefits under international treaties by applying the MLI's principle purpose test ("PPT"), if they conclude that obtaining those benefits was one of the principal purposes of the arrangement or transaction. They could also use the MLI's limitation of benefits provision ("LOB"), which contains a series of putatively objective tests, to determine whether a person resident in one of the countries of an international tax treaty can access the benefits of that treaty.

For the above reasons (among others), one should review and analyze the operations, transactions, and structures that companies have with entities that form part of the MLI and use the benefits of international tax treaties.

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