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## MEXICAN SENATE APPROVES TAX TREATIES WITH SAUDI ARABIA AND THE PHILIPPINES

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On October 3, the Senado de la República (the “Mexican Senate”) approved a pending tax treaty between the United Mexican States and the Kingdom of Saudi Arabia that avoids double taxation and prevents fiscal evasion of income taxes. The treaty was originally signed in Riyadh on January 17, 2016. The Mexican Senate also approved a similar tax treaty with the Republic of the Philippines, originally signed in Manila on November 17, 2015.

One of the distinctive features of these tax treaties are provisions relating to permanent establishment (“PE”) status (or taxable presence), likely inspired by both the Base Erosion and Profit Shifting (“BEPS”) project of the Organisation for Economic Co-operation and Development (“OECD”) and Mexico’s new policy of opening the oil and gas sectors to private parties. Some of the more significant aspects of these tax treaties with regard to the PE status are as follows:

- **Oil & Gas Activities PE.** The treaty with Saudi Arabia provides that the activities in Contracting State A of an enterprise resident of Contracting State B related to hydrocarbon exploration, production, refining, processing, transportation, distribution, storage, and trading will result in the creation of a PE in Contracting State A if such activities continue for more than 30 days in any 12-month period. Although this provision is not expressly included in the tax treaty with the Philippines, the treaty permits Contracting State A to apply its domestic law with regard to income from the production of hydrocarbons by an enterprise resident of Contracting State B. Mexico’s domestic law has a similar 30-day provision, so the result should be the same for activities conducted in Mexico by enterprises resident of the Philippines.
- **Services PE.** The provision of services, including consulting services, in Contracting State A by an enterprise resident of Contracting State B will result in the creation of a PE in Contracting State A if such activities continue for more than 183 days in any 12-month period.
- **Taxable Profits of a PE.** The profits of an enterprise resident of Contracting State A that may be subject to tax in Contracting State B where a PE of such enterprise is deemed to exist include not only profits attributable to such PE, but also those attributable to sales or other entrepreneurial activities of such enterprise performed anywhere in Contracting State B that are identical or similar to those it carries on through the PE.

Another interesting element of the tax treaty with the Philippines, which is not included in the treaty with Saudi Arabia, is that it applies a “Principle Purpose Test” (“PPT”). A PPT is also proposed in the OECD’s new Multilateral Instrument (“MLI”). Under the treaty’s PPT, treaty benefits may be denied

to an enterprise if it is reasonable to conclude that one of the principal reasons it entered into a given transaction was to claim a benefit under the treaty.

These tax treaties are not yet in force. However, the Mexican Senate's approval is certainly a significant step toward their full adoption, and may be indicative of Mexico's future approach to the scope of treaty benefits.

If you have any questions concerning these treaties, please do not hesitate to contact the Thompson & Knight attorney with whom you regularly work or the attorney listed below.

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