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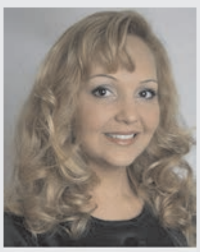
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In this article, the authors discuss the reasons U.S. companies still look south for business opportunities in Latin America despite economic challenges and the complexity of that market's ever-changing tax rules.

As more executive teams of U.S.-based companies look south to consider business opportunities in Latin America, they may experience double vision. The extremely valuable business opportunities in the region look clear, but the overall tax environment looks blurry thanks to complex and dynamic transactional tax management challenges.

To fully benefit from those business opportunities in Argentina, Brazil, Mexico, and other Central and South American countries, companies must be able to address that tax complexity. Doing so requires deep tax knowledge, familiarity with country-specific tax intricacies, and an overall tax management approach that leverages tax automation when possible.

Tax managers must carve out time for following and understanding the quickly changing, multilayered indirect tax rate topics for companies doing business in Latin America.

Lionel Nobre, the Latin America tax director for Dell Inc. and the founding member of Tax Executives Institute Latin America, understands the skill sets tax professionals need to thrive in the region's complex tax environment. He has said that to be truly successful, ''future in-house tax professionals in Latin America will not only need accounting but also informatics and systems skills.''[1]

Looking South Is Lucrative

The U.S. Commerce Department believes Latin American markets can help make U.S. companies more successful. In 2014 the department launched its ''Look South'' initiative to help more U.S.-based companies of all sizes understand why expanding into Latin American markets can improve their bottom lines. The initiative focuses on the growing business opportunities in Mexico, as well as 10 other economies that participate in several U.S. free trade agreements in the region.[2]

''Our Latin American trade agreements, which cover over 70 percent of our regional trade, do more than just eliminate tariffs,'' said Francisco J. Sánchez, former U.S. undersecretary for international trade.[3] ''Companies in the United States and Latin America benefit from commitments that facilitate transparent rulemaking, predictable legal frameworks, strong intellectual

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[1]Michael Levin-Epstein, ''Latin America: Many Trading Partners, Diverse Tax Implications,'' *Tax Executive* (May 29, 2015).

[2]U.S. Commerce Department, ''Fact Sheet: Look South Initiative'' (Jan. 9, 2014)

[3]John Larsen, ''Look South: Mexico Is a Springboard to Attractive New Markets in Latin America,'' 7 *TradeSource* (July 2013).

property rights protections, and regulatory certainty at home, as well as in global markets.'' Exporting U.S. goods to Latin America represents one of the largest and fastest-growing components of U.S. global exports. Mexico in particular is booming, according to year-over-year increases in its economic growth as measured by the IMF.

One article noted that ''Mexico stands out as an excellent place for U.S. Companies to look for new opportunities.''[4] Despite a recent downturn, Brazil's long-term economic prospects, propelled by its fast-growing middle-income consumers, also look promising. And the U.S. figures as the third largest trading partner of Argentina, which is one of the largest economies in Latin America thanks to its population of more than 41 million.[5]

Sánchez also pointed out that the trade agreements that apply to several countries in Latin America serve as a ''playbook'' for succeeding in those markets by removing tariff and non-tariff trade barriers and providing transparency, predictability, and recourse. While that's certainly the case, those playbooks would be incomplete without information and expertise on the tax environments.

II. Country Close-Up

Companies and their tax functions must be careful when looking south. Because of the complexities of the Latin American tax environment, there is almost always more to the tax picture than initially meets the eye. That is certainly the case when analyzing indirect tax rate trends in recent years. For example, an initial look at indirect tax rate trends by global region shows that Latin American rates are higher than those in other regions but relatively similar to those in Asia. In 2014 the average indirect tax rate was 12.5 percent in Asia and about 13.6 percent in Latin America, according to KPMG LLP.[6]

However, focusing more closely on Latin America provides a slightly different picture. In 2014 four countries had notably higher reported average indirect tax rates than the regional average: Argentina, at 21 percent; Brazil, at 19 percent; Mexico, at 16 percent; and Colombia, at 16 percent.[7] An even deeper look amplified by more information and local expertise shows a much different picture, with Brazil as a vivid example. A high-level summary of the tax environments in Brazil, Argentina, and Mexico follows.

A. Brazil

The Brazilian tax environment is one of the most complex and dynamic in the world. Many daily newspapers are dedicated to reporting on new laws, most of which relate to taxation on the federal, state, and municipal levels.[8] Brazil has more than 85 taxes, including:

- IOF (tax on financial transactions), levied on financial operations and assessed on different types of events, including credit, foreign exchange, international transactions, securities, and insurance;
- CIDE (economic domain intervention contribution), applied to contracts connected to royalty payments and technology transfers;
- IRPJ (corporate income tax), calculated on a company's income;
- CSSL (social contribution tax on net profit), an additional income tax imposed on a company's income before taxes; and
- INSS (national institute of social security contributions), a percentage charged monthly on employers and employees calculated on employees' monthly salaries.

The country's standard indirect tax, Imposto Sobre Operações Relativas à Circulação de Mercadorias e Serviços de Transporte Interestadual de Intermunicipal e de Comunicações (ICMS), is a VAT ''on sales and services that applies to the movement of goods, transportation and communication services, and to the supplying of any goods.''[9]

Although Brazil's average indirect tax rate was 19 percent in 2014, many factors figure into a company's tax burdens, such as the location — that is, federal, state, and municipal taxes — and industries in which a company operates. It is common for a company to be subject to the ICMS as well as:

- IPI (federal tax on manufactured goods), calculated on transactions with goods produced or imported;
- PIS (federal contribution for social integration program), applied to corporate gross revenues;
- COFINS (federal contribution for financing of social security), applied to monthly invoicing; and
- ISS (municipal service tax), applied to services a company provides to a third party.

If each of those taxes were applied, ICMS would represent less than half (44 percent) of the total indirect tax rate a company is subject to.

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[4]Joe Matthews, ''One Year Later, Look South Looking Brighter,'' Tradeology (blog), Jan. 9, 2015.

[5]*Id.*

[6]See KPMG, Tax Tools and Resources: Tax Rates Online (undated).

[7]*Id.*

[8]Andréa Novais, ''The 16 Most Common Brazilian Taxes,'' *The Brazil Business*, Sept. 11, 2012.

[9]Novais, ''Understanding ICMS,'' *The Brazil Business*, Sept. 10, 2012.

It is useful to look at Brazil's most notable forms of indirect tax at the federal, state, and municipal levels. At the federal level, PIS, COFINS, and IPI are important. PIS and COFINS both apply to a company's operational gross revenue. The calculation method varies depending on several factors. Under a noncumulative regime, companies would have a PIS rate of 1.65 percent, a COFINS rate of 7.6 percent, and would be entitled to input tax credits. Under a cumulative regime, companies would have a lower PIS rate of 0.65 percent, a COFINS rate of 3 percent, and would not be entitled to input tax credits.

Under a monophasic or tax substitution regime, rates vary more, and companies are not entitled to input tax credits. IPI marks an important federal VAT charged on transactions involving manufacturing or imported goods. The rates for that noncumulative tax vary widely, from 0 to 330 percent, depending on the item.

The Brazilian Superior Court of Justice recently considered the IPI in a case (STJ — REsp: 1403532 SC) with high stakes for the Brazilian Treasury and possibly many importers.[10] The court found that importers should not be required to pay the IPI on the resale of imported goods that are not subject to a manufacturing process in Brazil. Although very relevant to Brazilian taxpayers in general, the decision does not apply to all importers, but only on the importers that filed the lawsuits.[11] It reflects both the complexity and fast-changing nature of the indirect tax environment in Latin America's largest economy.

B. Argentina

Argentina's standard indirect tax rate ranks among the highest in Latin America. The VAT, known as the IVA (*impuesto al valor agregado*), and an excise tax (*impuestos internos*) are the most notable federal taxes.

The IVA is a multiphase, noncumulative tax levied on all stages of transactions. Companies cannot deduct input VAT on exempt transactions, except those involving exports. While the standard IVA rate is 21 percent, it can vary. For example, there is a luxury rate of 27 percent on utilities supplied to registered taxpayers and a reduced 10.5 percent rate for some construction activities, financial transactions, and transactions involving capital goods.

The excise tax is levied on specific goods and services, including alcohol and tobacco, soft drinks, automobiles, mobile phone services, insurance premiums, and luxury items. It is generally levied on the production or importing stage — that is, the first stage — but not on exports. It is also levied on the sale price, which includes this excise tax itself and other taxes but excludes VAT. The rate varies depending on the item.

At the provincial level, Argentina's turnover tax is called *impuesto sobre los ingresos brutos*, a gross income tax imposed on gross revenues from the sale of goods and services. Rates and regulations are determined individually among the country's 24 tax jurisdictions. Further, rates of this multiphase, cumulative tax (input tax from the preceding stage is not deductible) vary depending on whether the seller is a manufacturer, wholesaler, retailer, or services company; by type of activity; and by turnover. In most cases, exports of goods and services are exempt. Also, a multilateral agreement among all provinces and the federal district in Argentina is intended to deter multiple taxation while distributing the taxable base.

Numerous other taxes apply in Argentina. At the federal level, those include a corporate income tax, a tax on minimum notional income, and a tax on bank account debits and credits. At the provincial level, there is a stamp tax (*impuesto de sellos*), and at the municipal level, a safety inspection fee often applies.

C. Mexico

Mexico, the United States' second largest export market, is the destination for more U.S. exports than Brazil, China, India, and Russia combined.[12] Mexico's tax environment has some commonalities with Argentina's: a VAT regime imposed by the federal government and an excise tax on production and services.

Mexico's standard IVA (VAT) rate is 16 percent. The IVA is a multiphase, noncumulative tax levied on all stages of transactions. Unlike other tax regimes in Latin America, Mexico's uses a cash flow system under which a seller pays the tax when consideration for a supply is paid (output VAT) and a buyer is entitled to an input credit when a payment is made to the supplier (input VAT).

A special tax on production and services marks another crucial federal tax in Mexico. This special excise tax, part of tax reforms implemented in Mexico in the past two years, is levied on specific goods and services such as alcohol and tobacco, sugar-added beverages, gasoline, and calorie-dense food. It is generally levied on the production or importing stage — again, the first stage — but not on exports.

The tax is applied using rates that depend on the sale price or a fixed amount established in the law depending on the good or service sold. Other important federal taxes and duties are a corporate income tax (*impuesto sobre la renta*), a compulsory profit-sharing tax, and import/export duties (*aranceles de importación/exportación*).

III. Complexity, Change, and Technology

The complexity of Latin American taxes is evident, even from a relatively high-level perspective. Focus on

[10] EY, ''TradeWatch'' (Mar. 2015).

[11] *Id.*

[12] Larsen, *supra* note 3.

a specific country's tax challenges, and the difficulty of managing that complexity quickly becomes apparent. In Brazil, for example, interactions among various indirect taxes, gross-up effects, application conflicts (for example, ICMS versus ISS), contentious relations between taxpayers and tax authorities, and quickly changing rules pose significant challenges to tax functions.

Nobre said he thinks that environment presents tax professionals with risk and opportunities, saying that ''Latin America has very complex and always-changing tax systems with increasing foreign investment, which provides major opportunities for tax professionals in this region.''[13] He also pointed out the increasingly important role tax automation and related technology play.

More Latin American tax regimes are embracing automation to support key tax processes, with some requiring that taxpayers use specific applications for reporting and compliance. The more tax processes that companies can automate, the more time and energy they can devote to keeping pace with the challenges they face.

The volume, specificity, and interaction of tax rules in Latin America create intricacies that must be managed. The complexity stems from taxes often being levied by three administrative levels (federal, provincial or state, and municipal or city); the sheer number of taxes and rates; and numerous withholding and collection regimes. The lack of a unified approach to VAT in Latin America also poses difficulties.

Tax rate increases and policy changes occur with greater frequency in many Latin American countries. This year, for example, Brazil introduced a series of tax increases designed to raise government revenue at a time when the Brazilian economy faces head winds.[14] Frequent legislative changes, as well as court rulings on major tax topics, also complicate tax compliance throughout Latin America.

As more Latin American countries move to electronic invoicing, auditing, and reporting, tax departments must bring in technical tax skills to adapt. More tax authorities are also requiring taxpayers to use new software for compliance and reporting purposes, which also increases the need for internal tax-automation expertise.

Conclusion

As more companies enter Latin America or expand their activities there, they must master the complex challenges of transactional tax management. Addressing those challenges begins with a high-level understanding of the nature of Latin American tax regimes, followed by a more detailed, country-by-country understanding of unique tax challenges. When looking south, it pays to look closely at tax. ◆

[13]Levin-Epstein, *supra* note 1.

[14]Jeff Lewis, ''Brazil Announces Tax Increases for 2015,'' *The Wall Street Journal*, Jan. 19, 2015.