WEALTH MANAGEMENT
Tax

A taxing issue

Managing withholding taxes can be a cumbersome task for corporations. This is particularly true in Latin America, where navigating the complexities requires local expertise, according to ***Ana Paula Maciel****, Principal Tax Research Analyst at Vertex, and* ***Ernesto Levy****, Senior Leader of Global Indirect Tax at Intuit*

Understanding tax regulation can be challenging at the best of times. In much of Latin America, rules around withholding taxes on B2B transactions vary so greatly it can dramatically hinder efficient business.

This fact is especially concerning when it comes to the consequences of non-compliance. For example, in Argentina, failure to pay taxes can result in hefty fines of up to 10 times the amount not paid. Effectively managing B2B transactions, therefore, is of the essence.

Doing so, however, requires an in-depth understanding of the individual, country-specific regulations that govern each jurisdiction. *World Finance* spoke to Ana Paula Maciel, Principal Tax Research Analyst at leading tax solutions firm Vertex, and Ernesto Levy, Senior Leader of Global Indirect Tax at Intuit, to find out more about how Argentina, Brazil and Mexico differ in regulations, and what businesses can do to streamline their processes.

Navigating the complexities

In Maciel's words: "Withholding tax is a government requirement for the buyer of goods or services to deduct a specific amount from the payment made to the supplier." However, what sounds simple in theory is far more complex in reality, especially when various external factors – such as the various levels of government at play (federal, provincial and municipal) and frequently changing rules – are taken into consideration.

"Several common challenges crop up when tax functions address withholding tax requirements in Argentina, Brazil and Mexico, not least because each country has multiple forms of withholding taxes, rates and procedures", said Maciel. "Rules, rates and calculations are subject to frequent adjustments and legislative changes, especially during periods of economic stress, in which governments are hungry for faster ways to collect revenue. Tax managers grappling to manage withholding taxes in these countries may feel that the rules, scattered throughout government layers, change at least every 100 days."

When it comes to withholding, Brazil and Argentina are two of the most complex countries in the world. This is not helped by the fact that, in the latter country, a collection regime also applies, whereby the seller is mandated by the government to collect an advanced payment of taxes from the buyer at the time of invoicing.

The issue with Argentina

Both of these regimes are used heavily in Argentina; they can be found at the federal, provincial and municipal levels of government (*see Fig 1*) and are applied within almost all tax categories, including income tax, VAT and turnover tax. According to Levy: "This approach complicates business and tax compliance in the country. Tax departments must collaborate closely with finance and accounting teams, investing significant time in tax management and compliance activities."

Then there are the various regulations within each government level: on the federal side, almost all goods and services are subject to withholding income tax, and the majority of registered taxpayers are required to act as withholding tax agents. There are, however, some exemptions, including chargebacks, currency exchange transactions and payments made to government institutions.

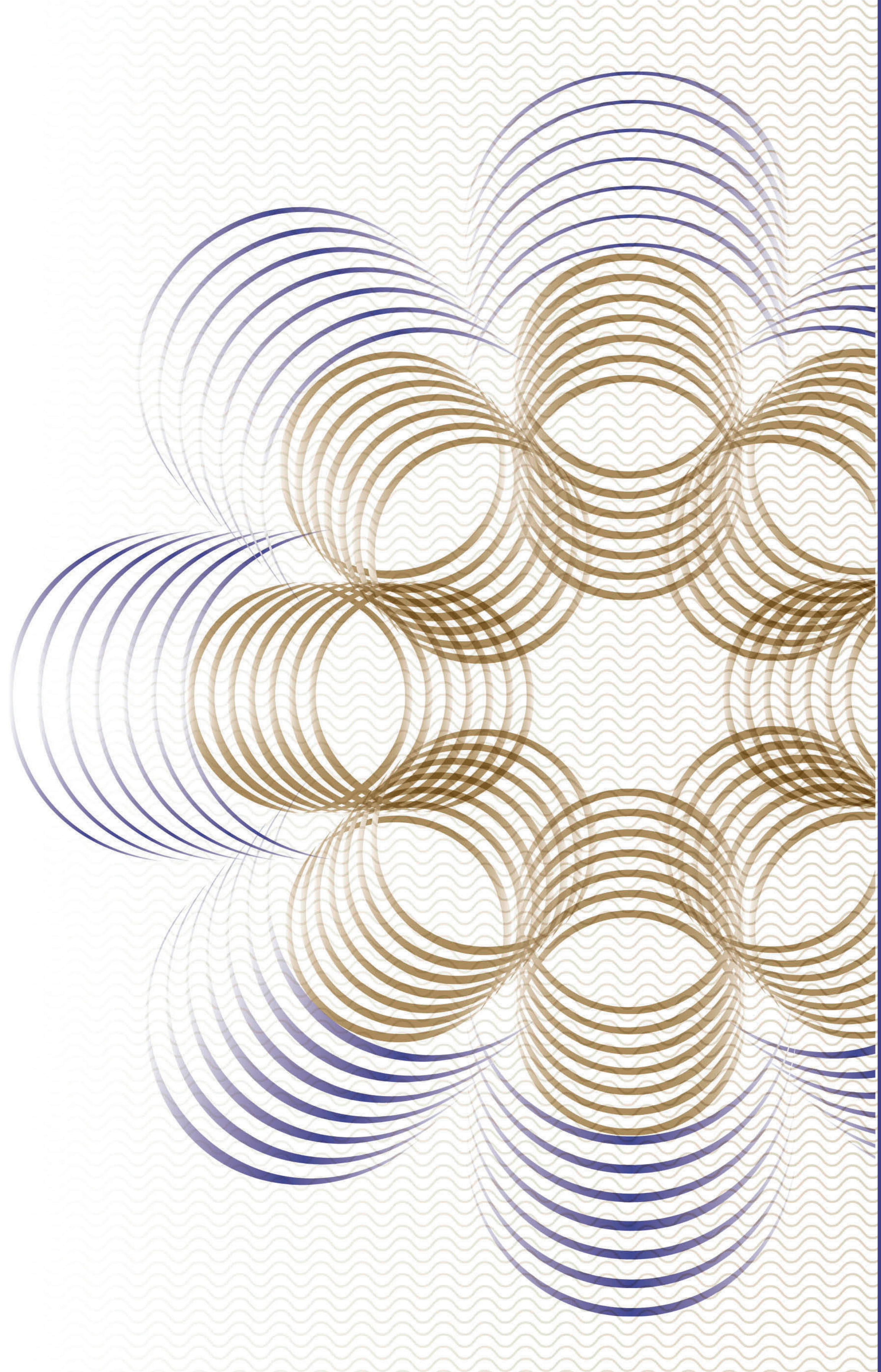
"The calculation is highly complex, in part because it requires the buyer to track all payments made to each taxpayer within a specific category throughout the month", said Levy. "The total payments for each category must then be compared to each threshold."

When it comes to VAT withholding, rates in Argentina vary depending on the type of goods or services being supplied – ranging from 50 percent on the sale of goods and certain construction services, up to 100 percent for 'blacklisted' taxpayers identified as high risk by the authority.

Fig 1 **Argentina's withholding taxes**

Federal level	
Income tax	General withholding tax
	Specific withholding tax
VAT	General withholding/collection tax
	Specific withholding/collection tax
Provincial level	
Turnover tax	General withholding/collection tax
	Specific withholding/collection tax

SOURCE: Vertex and Intuit



"In much of Latin America, differences in rules around withholding taxes vary so greatly that it can dramatically hinder efficient business"

While this sounds confusing, things get even trickier at the provincial level. According to Maciel: "At this level, Argentina's approach to withholding and collection taxes applied to turnover tax qualifies as complex." There are 24 autonomous tax jurisdictions, and each one handles withholding and collection taxes based on a unique set of regulations. There are then various exemptions to consider; certain transactions may be excluded under different provincial tax regimes. In some cases, sales of capital goods are excluded from withholding and collection taxes, for example.

"As a result, there are numerous different withholding and collection tax rules, procedures and calculations that buyers and sellers of goods and services need to follow", added Levy. "Usually, in order to be designated as either a withholding or collection agent, a taxpayer must have activities in the jurisdiction. Some provinces might also make the determination based on the company's revenue; under this approach, larger companies tend to bear more of the brunt of withholding taxes."

The Brazilian system

Over in Brazil, things are almost as complicated, with a system that can at times be unpredictable. "The Brazilian tax environment remains one of the most complex and fast-changing in the world", Maciel said. "It's important to recognise this condition in a country where indirect taxes and VAT withholding taxes apply only to services."

The country is home to more than 80 different taxes. Those on VAT include: IPI, a federal tax on manufactured goods; PIS, a federal contribution applied to corporate gross revenues and used for the government's social integration programme; COFINS, which funds social security and is applied to monthly invoicing; and ISS, a municipal service tax applied on services provided to a third party. Those on the corporate tax side include: IRPJ, a corporate income tax calculated on a company's gross income; CSSL, a social contribution tax on net profit; and INSS, or National Institute of Social Security contributions, calculated on employees' monthly salaries.

"It is important to keep in mind that some of these taxes apply differently, or do not apply at all, depending upon whether a transaction involves a good or a service", said Maciel. "For example, at the federal level, IPI applies to goods but not to services. At the state level, ICMS applies to goods and some transportation and communications services, but no other services."

The location of the transaction and its participants can also affect the status. And, as in the case of Argentina, it's the buyer that is responsible for calculating and deducting the tax, rather than, as with most standard taxes, the seller.

A straightforward approach

Fortunately, Mexico has simplified things a little: it's primarily income tax and VAT transactions that are subject to a withholding regime, making its regulations at least a little easier to navigate than the country's South American counterparts. Here, income tax withholding generally applies to payments made from entities to individuals for professional service. These local entities operate as the withholding tax agent and, as with Argentina and Brazil, withholding is triggered upon payment. The withholding tax rate is 10 percent, and it's applied to the net amount of the transaction.

There are nevertheless still a few niggling details that companies need to navigate around. Transactions between local entities aren't usually subject to VAT withholding, but for those that are, the rates vary – for example, from four percent for ground transportation of goods, to 16 percent for scrap to be used as raw material or sold. Independent personal and commission services, meanwhile, demand a payment of 10.67 percent. All of these rates are normally applied to the net amount, but in some circumstances come off the VAT amount.

There are further complications that apply to all three countries, however. If the value of individual goods and/or services isn't itemised on an invoice, for example, withholding tax calculations becomes more difficult. "Chargebacks, payments in kind and instalment payments also tend to create additional layers of difficulty in the determination and management of withholding taxes," added Levy. "Finally, some tax authorities provide software that taxpayers are required to use for reporting – and compliance – purposes."

Fortunately, there are solutions to these issues – namely drawing on exterior knowledge and using technologies to streamline complex, tax-related data. "Withholding taxes in Argentina, Brazil and Mexico can be managed", said Levy. "The leading approaches to doing so typically feature a blend of overall tax expertise, local knowledge, leading tax data management practices and supporting tax automation."

Software platforms such as those offered by Vertex can help simplify systems and take the pressure off the companies themselves. Although the platforms can't control the changes themselves, they can help organisations react to them. That's well worth noting during a period of flux, when regulations are, according to Maciel, likely to undergo a series of rapid changes. This is expected to be the case over the coming years – but whether that's for better or for worse remains to be seen. ■