

# **Simplified Tax Regime named «monotributo» as labor formalization instrument in the Southern Cone of Latin America**

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coverage in ASEAN**

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# TOPICS OF DISCUSSION

Introduction: Informality in Latin America

The tax response: simplified regimes in the region

“Monotributo” as formalization instrument

Three cases: Argentina, Brazil and Uruguay: Distinctive features

Final remarks and future challenges

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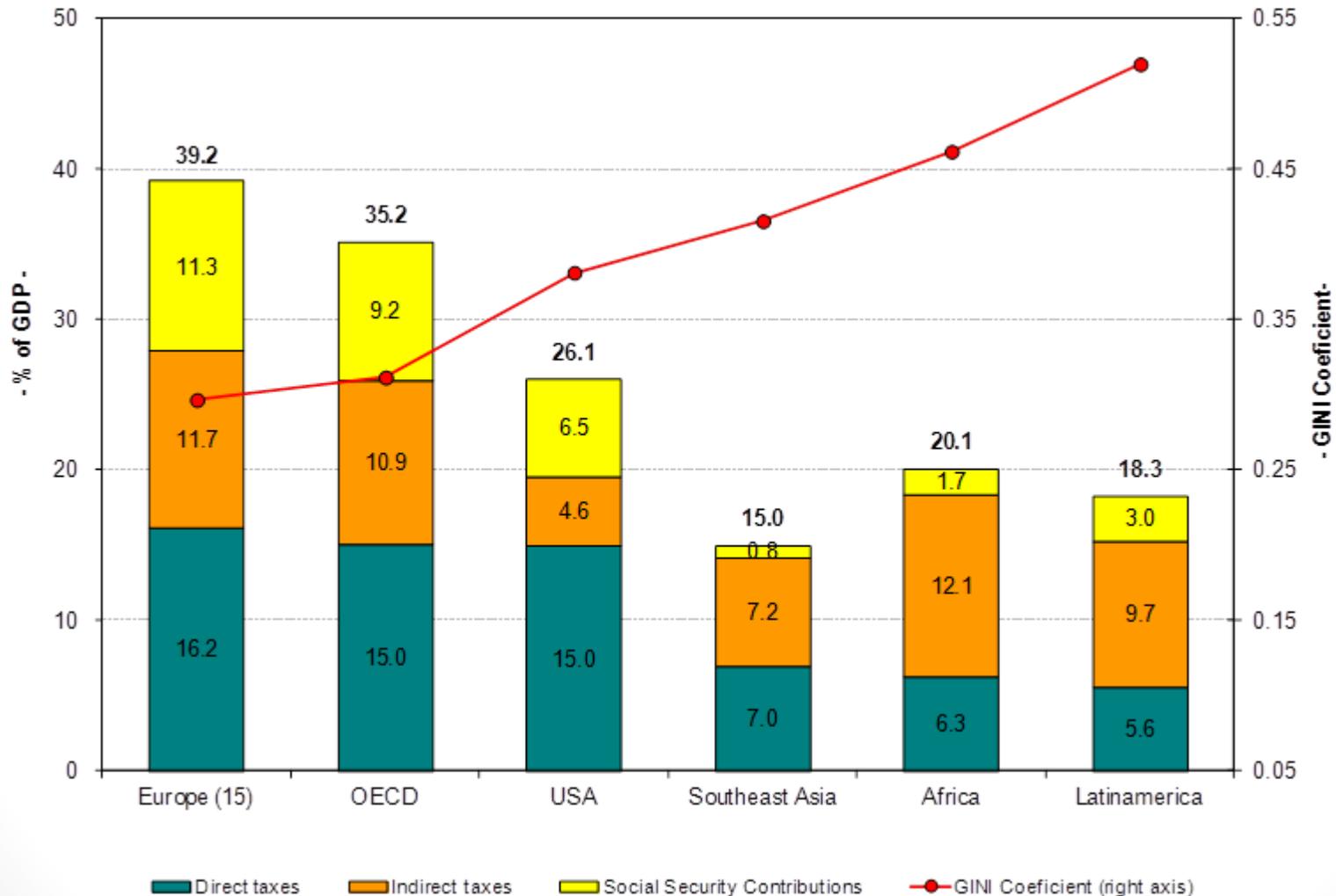
Final remarks and future challenges

# Introduction

Latin America is characterized for:

- Highest inequality
- Informal economy
- Inadequacy of contributory social protection
- Low tax burden

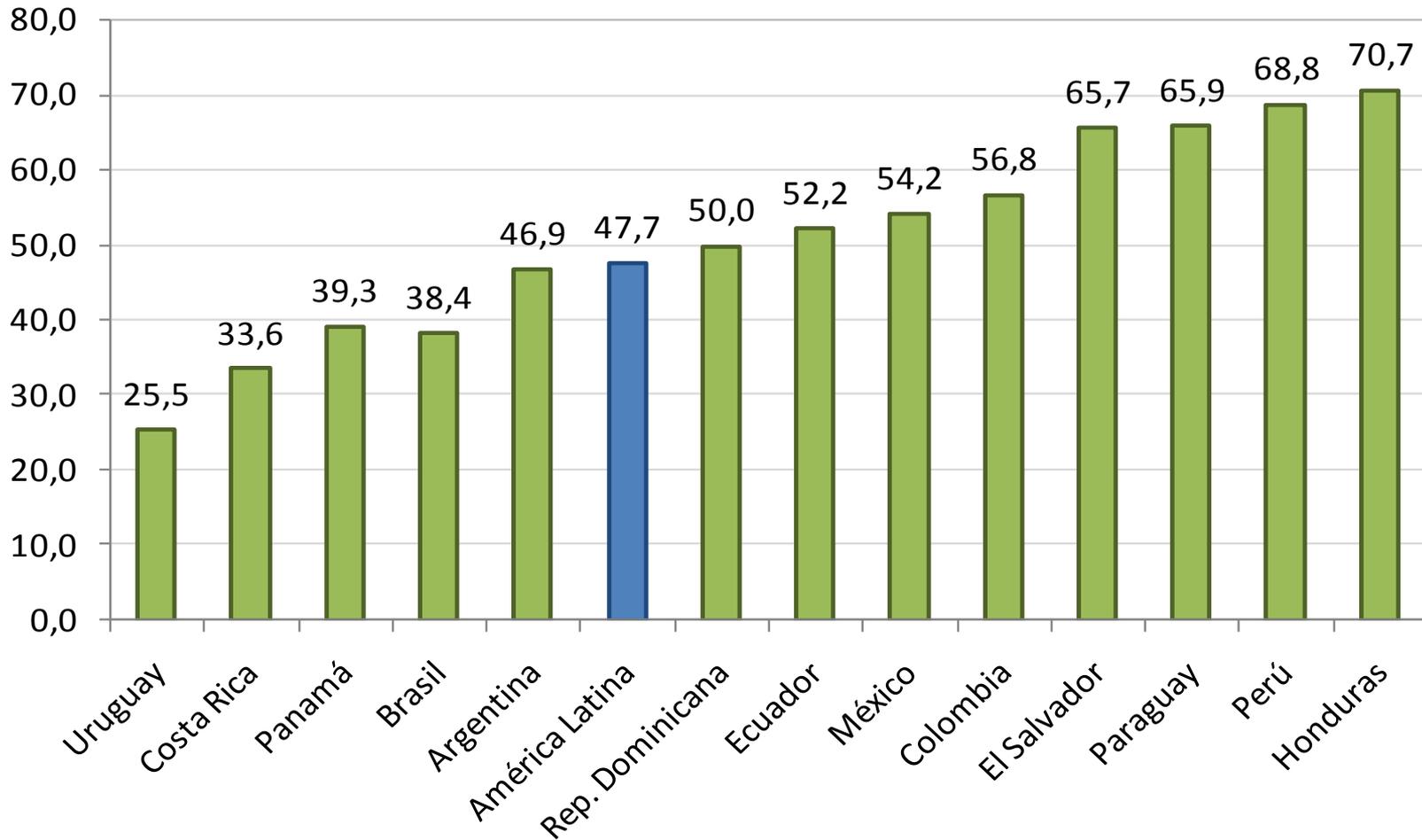
# Tax revenues and Gini Coefficient, by region



# Persistent informality as one of the main obstacles to reducing inequality

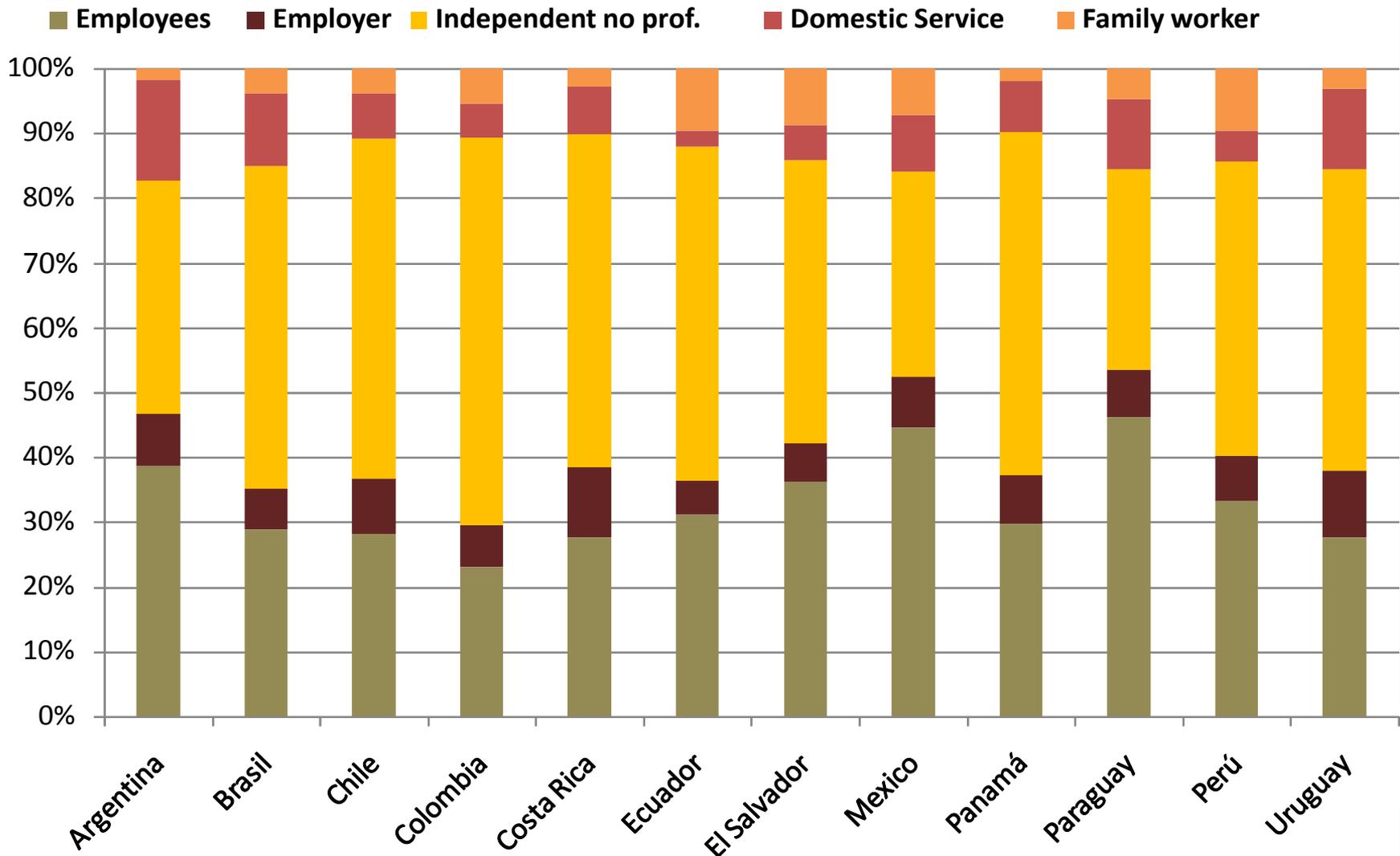
- Negative effects on the labor market
- Informality limits the scope of social security contributions and subtracts resources for the financing of new social protection systems that are being developed in many countries
- Concentration of informality in some sectors of activity, in certain groups of the population, in certain establishments and in certain age groups.
- Although there were improvements, the levels are still far from being comparable to those of developed countries.

# Informality rates (non agricultural sector) in Latin America. 2011



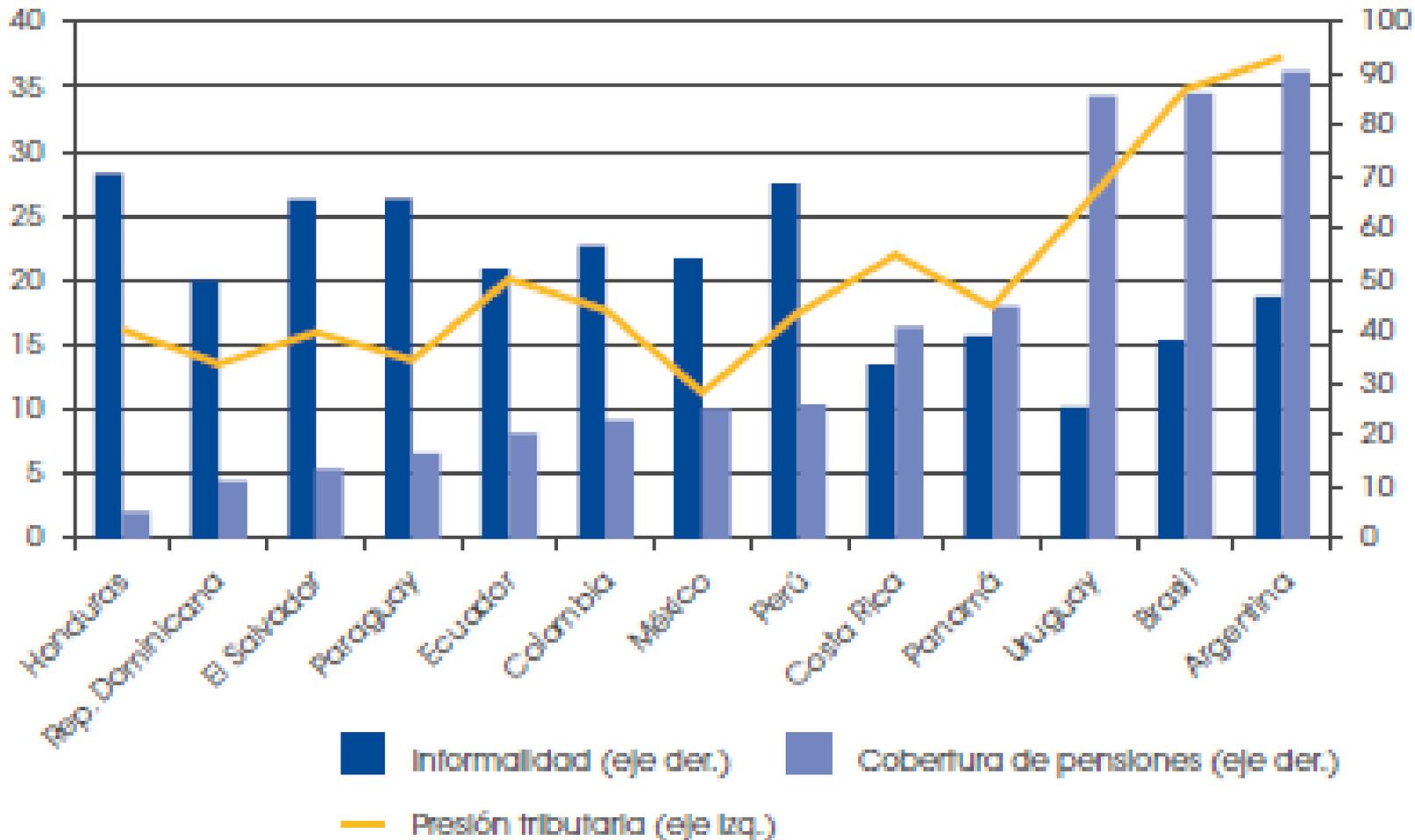
Source: Based on OIT (2012).

# Structure of informal work according to occupational category in Latin America - Year 2011



Fuente: Based on OIT (2012).

# Social security coverage (light blue, right axis), informality (blue) and tax burden (yellow line, left axis) in Latin America



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# Simplified regimes in Latin America

- At the end of the 1990s, some countries in the region began to develop simplified tax regimes for self-employed and small companies to get them incorporated into tax registers.
- Their objective has been to facilitate taxpayers “compliance” with the following characteristics:
  - ✓ Low income,
  - ✓ High number of cases that hinders official control,
  - ✓ Mostly informal,
  - ✓ Poor organizational structure and
  - ✓ High volatility.
- The primary objective of its implementation for Tax Administration Offices in Latin America has not been the collection of taxes, but to solve a problem of tax administration in the face of persistent informality among small taxpayers.

# Some information on existing simplified regimes in Latin America

- Broad dissemination (16 countries), in some countries coexist several simultaneous schemes (Argentina, Brazil, Chile, Mexico, among others)
- Generally apply to individuals, although in some cases extend to small firms.
- Most of the cases envisage voluntary adherence and self-categorization, and are targeted at the sectors of trade, service provision, agriculture, etc.
- The main presumptive technique is the "fixed fee", replacing one or more taxes (VAT, ISR and others).
- Thresholds (gross income) are set to differentiate taxpayers and limit the application of Simplified Regimes

# Tax collection of simplified regimes - in selected Latin American countries - 2010

Countries	% of Total Tax Revenues	% of GDP
Argentina	1,16	0,34
Bolivia	0,10	0,02
Brasil	2,86	0,94
Chile	0,02	0,01
Costa Rica	0,08	0,02
Ecuador	0,05	0,01
Guatemala	0,59	0,07
México	0,05	0,02
Paraguay	0,07	0,01
Perú	0,09	0,05
Rep. Dominicana	0,05	0,01
Uruguay	0,40	0,10

Source: Pecho Trigueros (2012); "Regímenes Simplificados de Tributación para Pequeños Contribuyentes en América Latina", CIAT.

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# Monotributo: simplified regime for taxes and social security contributions

- Based on the idea of a simplified tax regime which, in addition to facilitating the payment of one or more taxes, ensures a minimum level of social protection (pensions for old age and health) to a large number of small taxpayers.
- In Latin America there are three relevant cases: Argentina, Brazil and Uruguay.
- A Tax Incorporation Regime (RIF) was recently approved in Mexico, which also includes Social Security, but has different characteristics
- In January 2017 a Monotributo was introduced in Colombia as part of a broader tax reform.

# Fundamentals of monotributo

## *Taxes (coincident with other simplified rules):*

- ✓ Guarantee tax compliance of small taxpayers, ensuring their incorporation after formal registration.
- ✓ Reduce the regressive effect of compliance costs according to the size of the taxpayer.
- ✓ Avoid overburdening the Tax Administrations with a large number of small taxpayers whose revenue collection is very limited..

## *Social security (distinctive feature):*

- ✓ Avoid fragmentation derived from the contributory schemes of the formal labor market.
- ✓ Promote universal coverage of the population in health and pensions dimensions of social protection.
- ✓ Provide incentives to the taxpayer through a minimum payment (which usually implies a subsidy) that ensures access to health and social security coverage.

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# Argentina

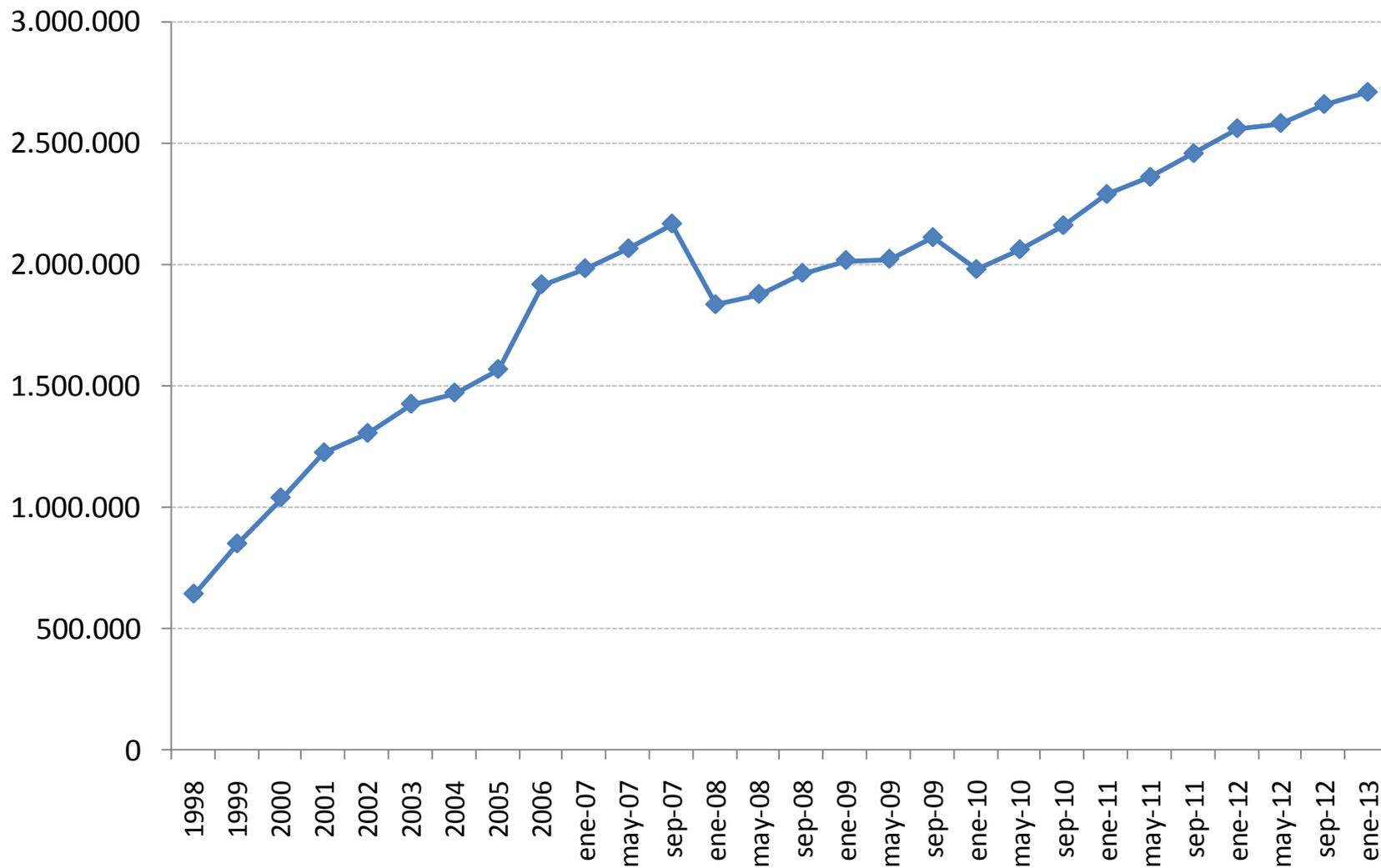
- The Monotributo was introduced in October 1998 as a replacement for the previous simplified VAT scheme
- It has undergone numerous modifications throughout its history, both structural and parametric.
- It coexists with other simplified regimes (domestic service, agricultural workers, first job).
- The monthly fixed fee consists of 2 components:
  - ✓ Tax: Replaces VAT, Revenue and all national taxes. A fixed monthly amount is imposed based on 11 categories by gross income level.
  - ✓ Social Security: composed of two fixed contributions intended to finance the pension system and health insurance.

# Supplementary schemes to the monotributo in Argentina

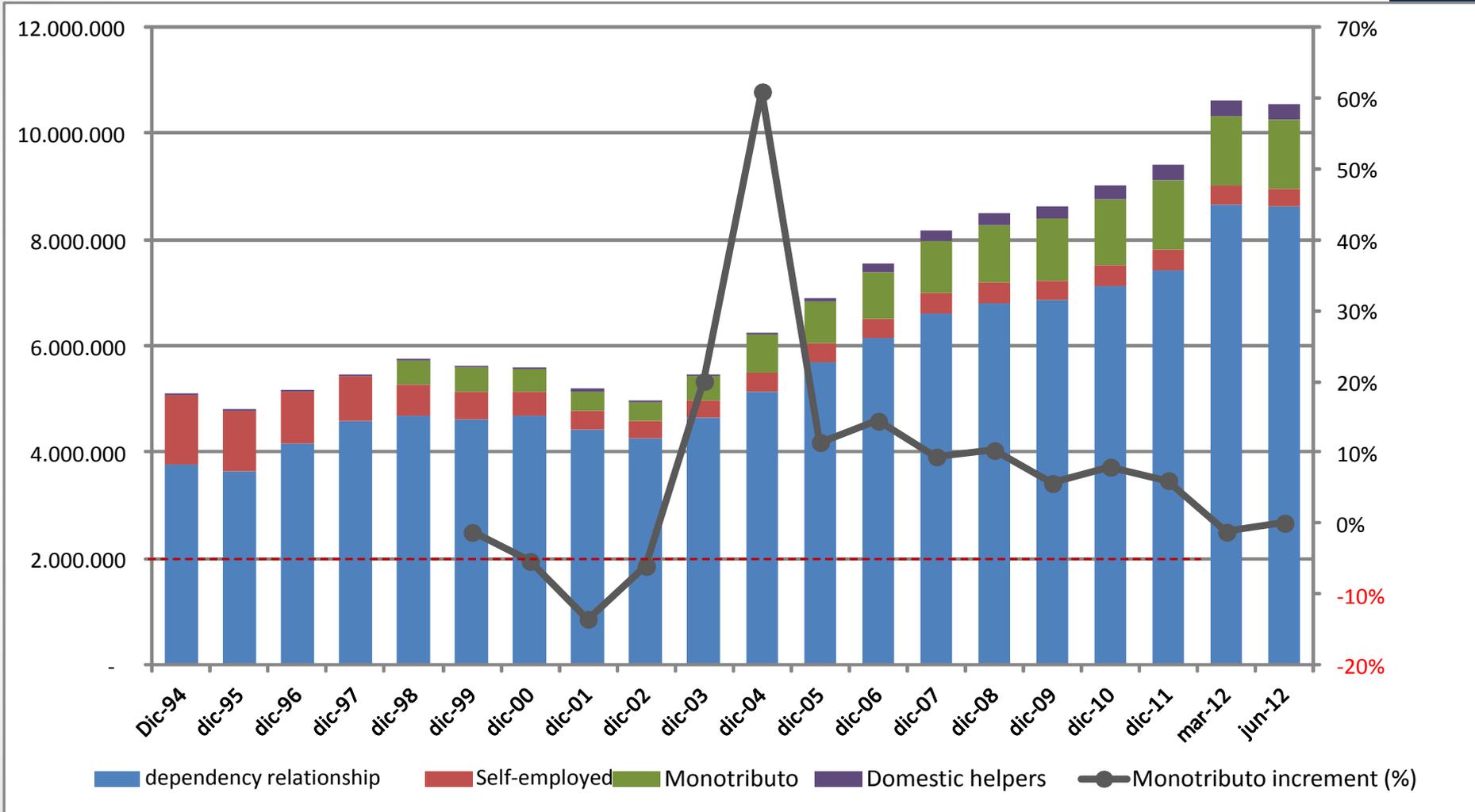
1. Social inclusion and independent work promotion regime. They pay a minimum fee
2. Social Monotributo. For informal workers.
3. Special regime for cooperatives. They only pay social security but not the tax contribution.
4. Domestic helpers.

In all cases the subjects have access to health insurance programs under more advantageous conditions, as well as to the pension system.

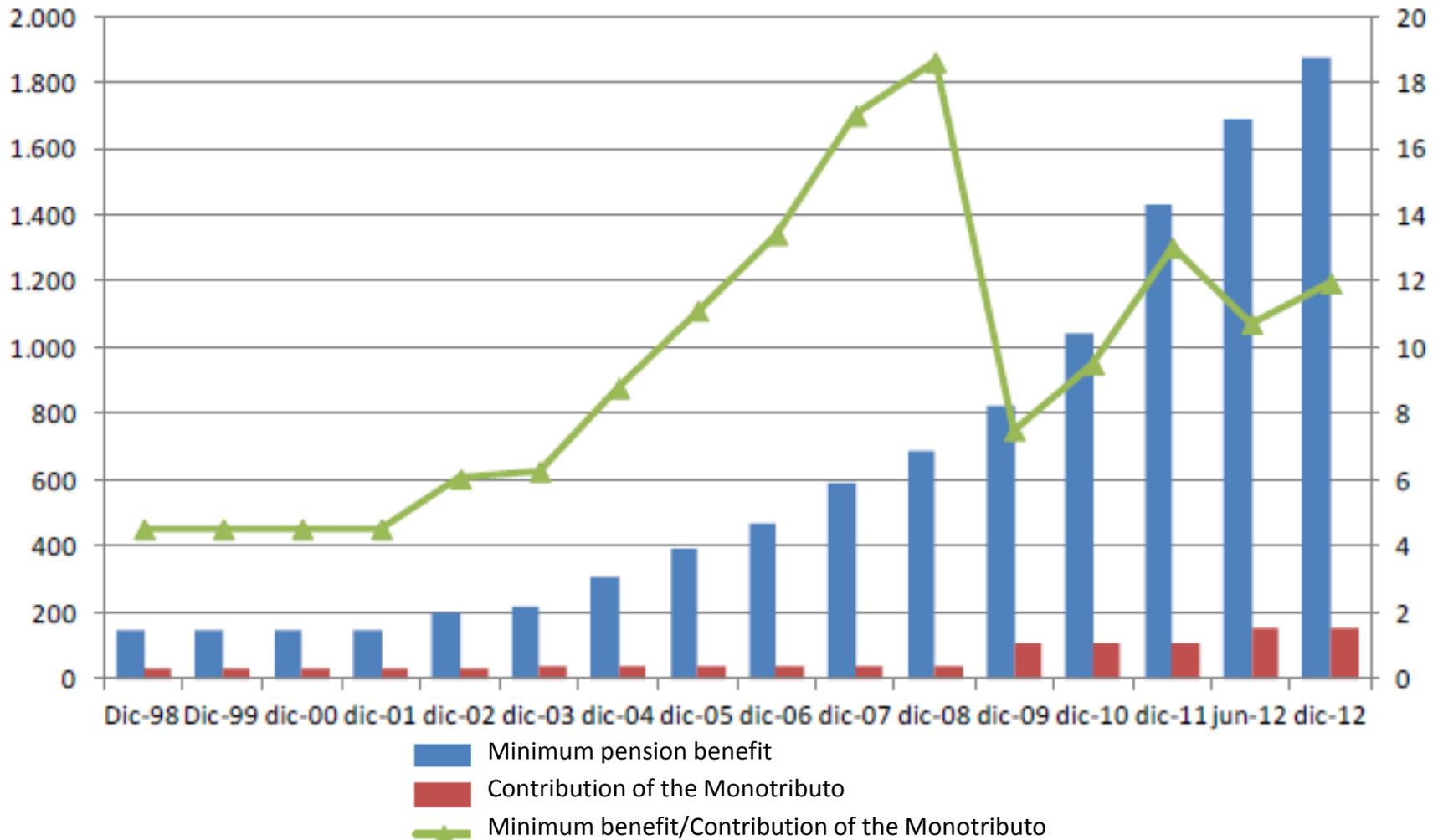
# Evolution of the number of taxpayers registered in the Monotributo - 1998/2013



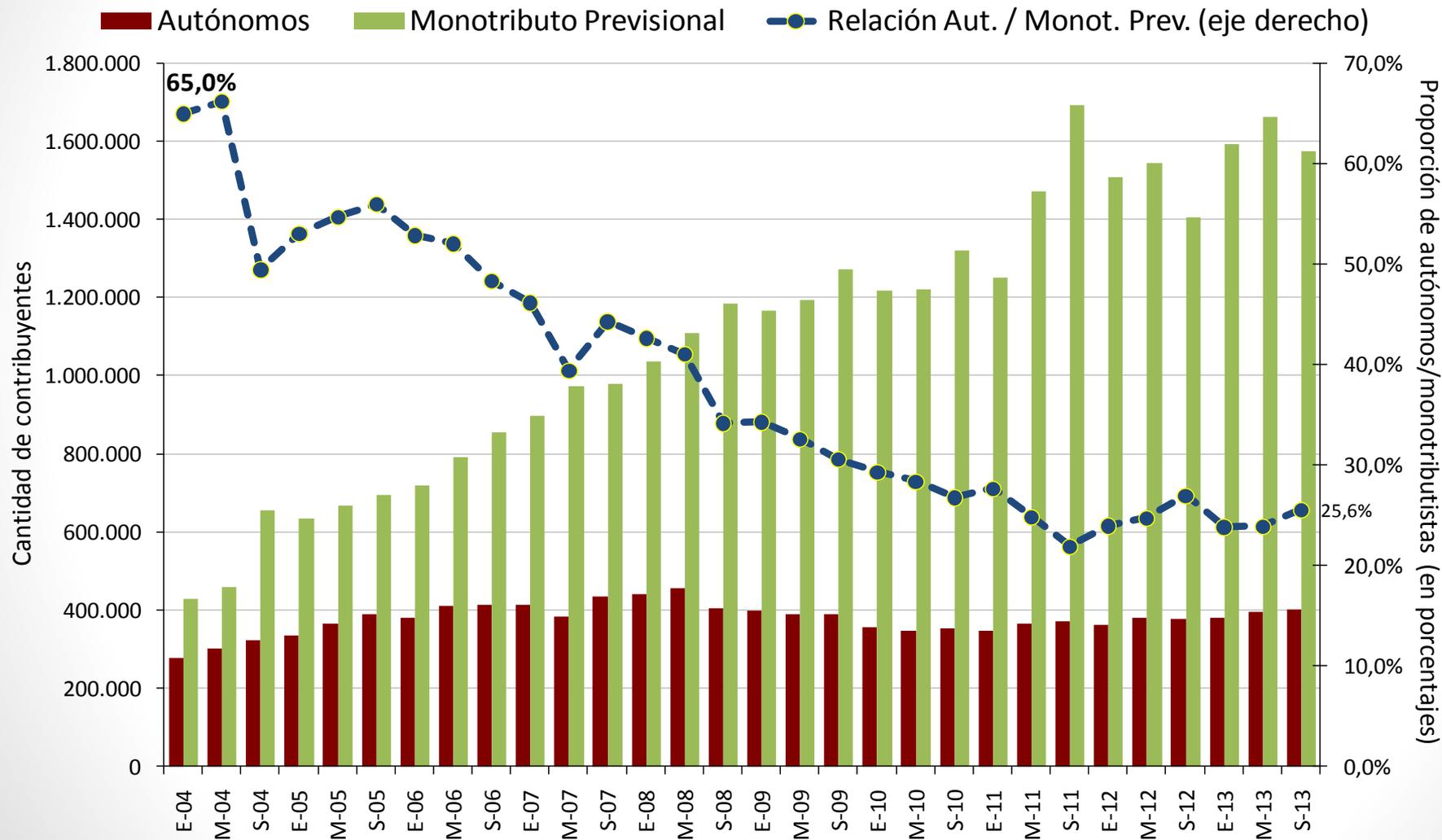
# Number of workers contributing to each pension scheme



# Comparison between the minimum pension benefit for employees and the contribution of the Monotributo



# Contributing workers in the Regime of Autonomous (general) and in the Monotributo previsional (simplified)



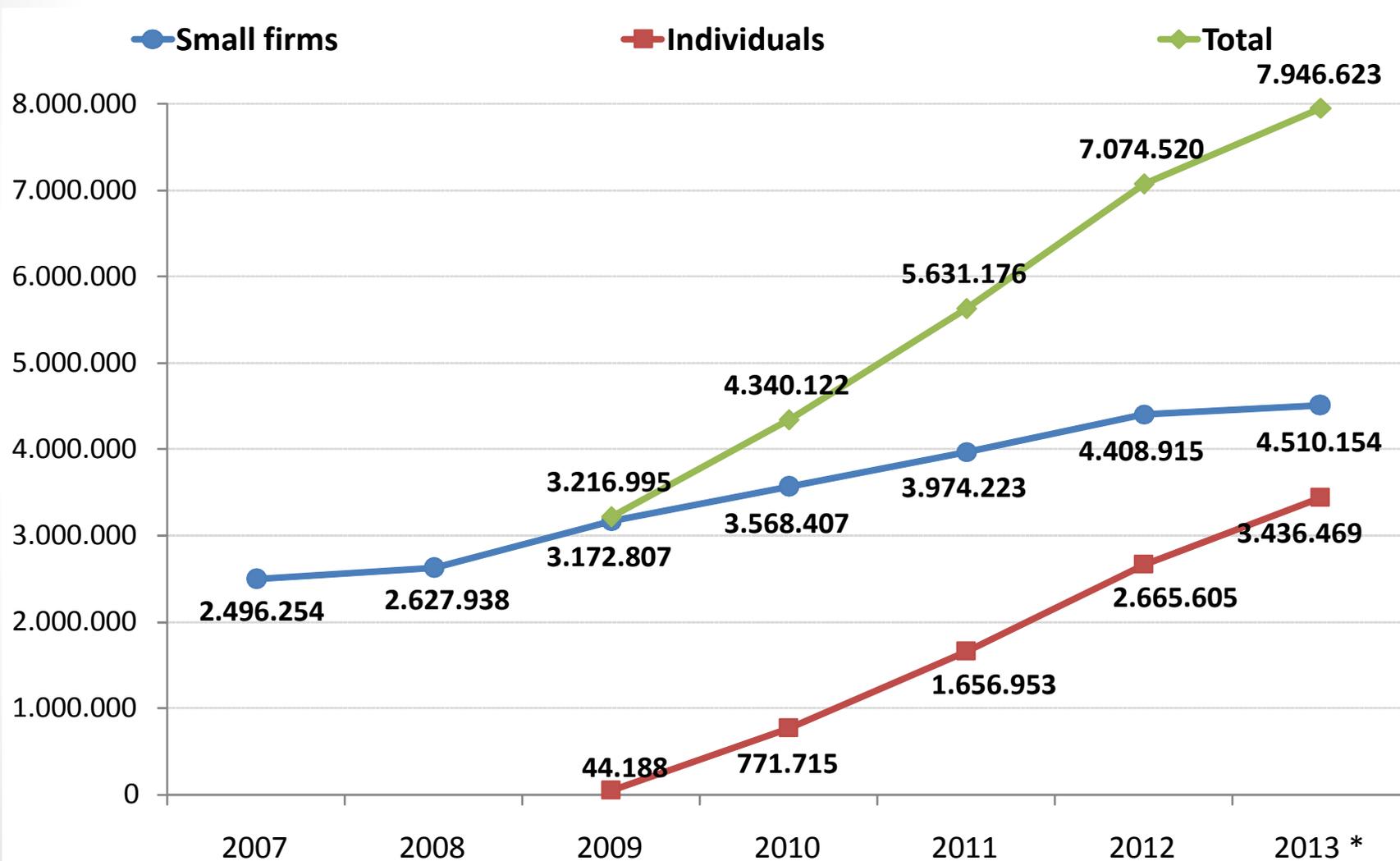
# Brazil (SIMPLES-SIMEI)

- In 1996 the Federal Government created the SIMPLES, which coexisted with different subnational schemes until it was unified in the National SIMPLES from 2007.
- Intended for small enterprises (micro and SMEs, with exceptions), it has increasing rates by level of turnover and type of activity (trade, industry, services, construction and professionals).
- Replaces in a single payment:
  - Several federal taxes and contributions (IRPJ, PIS / PASEP, CSLL, COFINS, IPI, CPP)
  - The main state tax (ICMS)
  - The main municipal tax (ISS).

# Brazil (SIMPLES-SIMEI)

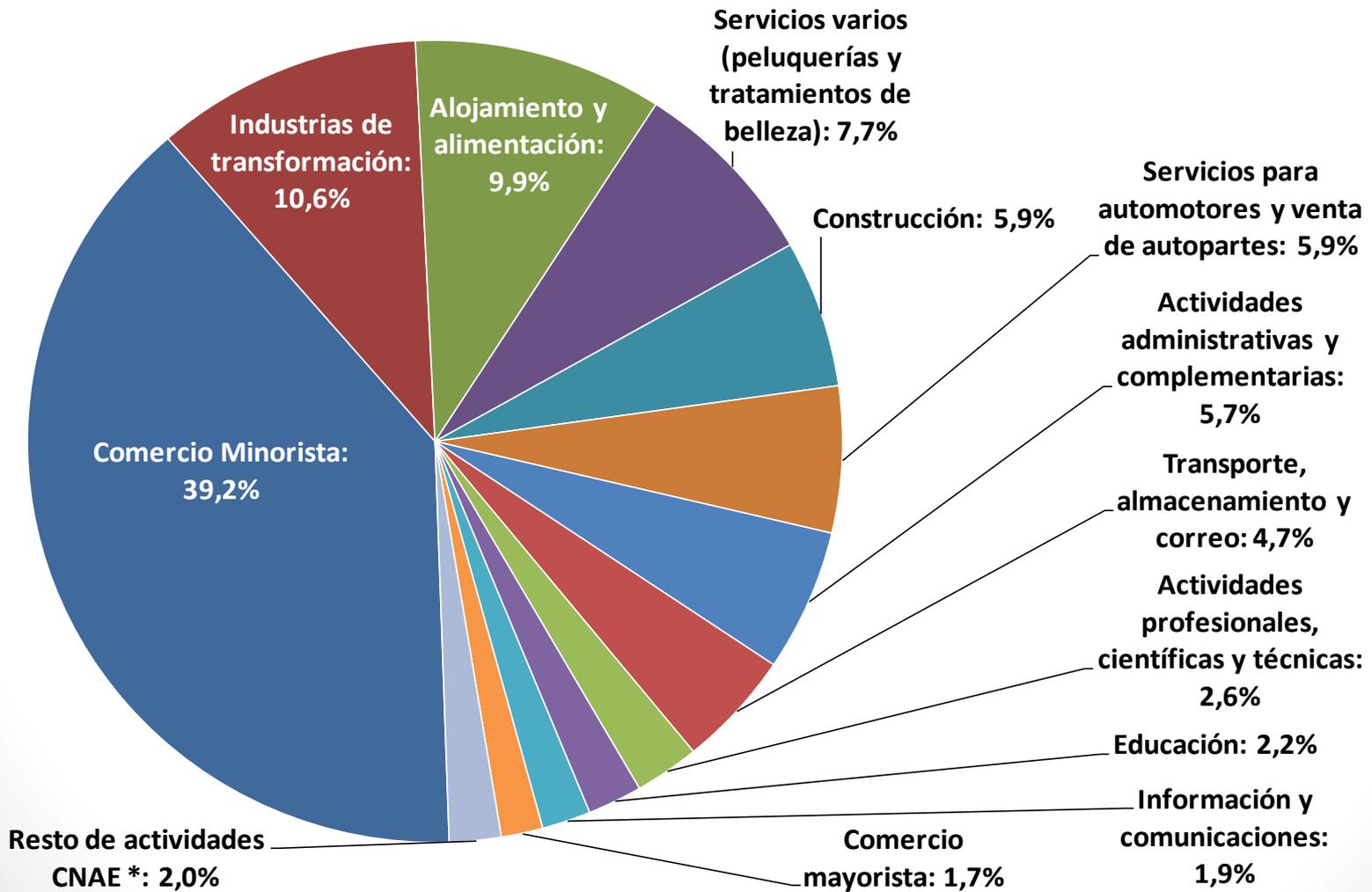
- In 2009 SIMEI is implemented for individual micro-entrepreneurs up to an annual turnover cap (R \$ 60,000).
- Replaces federal income tax from SIMPLES for a fixed monthly fee compounded by the social security contribution (5% average minimum wage) and an additional taxpayer when the state ICMS (R \$ 5) and / or municipal ISS (R \$ 1 ).
- Allows registration in the National Registry of Legal Entities (facilitates opening of bank accounts, loan application and bill issuance).
- Both SIMPLES and SIMEI provide access to benefits such as support for maternity, illness, retirement, among others.
- They do not include health insurance, since in Brazil it is Universal (SUSS).

# Evolution of the number of taxpaying workers registered in the National SIMPLES (including SIMEI) – 2007-2013



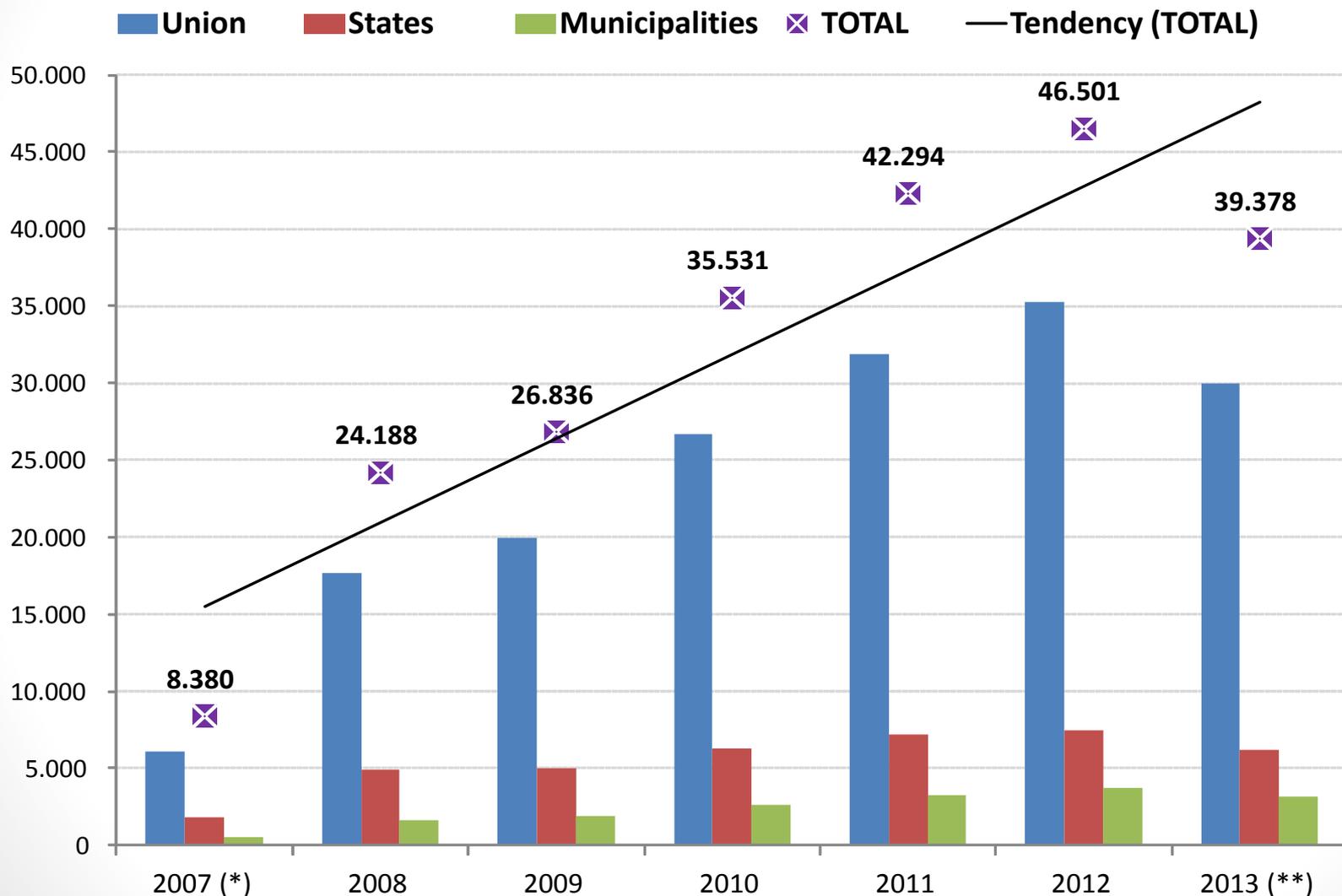
Source: Based on data from Receita Federal – SINAC Statistics.

# Taxpayers registered in SIMPLES+SIMEI. Perceptual Structure by activity



Spource: Based on Receita Federal data – Estadísticas SINAC.

# Annual tax collection of National SIMPLES (In millions of current Reales)



Source: Based on data from Receita Federal do Brasil

# Uruguay

- There are 3 schemes: Monotributo, Social Monotributo MIDES and Small Business Scheme (ex VAT MINIMUM).
- ***Monotributo:***
  - ✓ It was created in 2001 and was reformed at the end of 2006, directed to single-member companies and de facto partnerships up to TWO partners, with a maximum turnover determined by indexed units (U.I.).
  - ✓ It involves the substitution of social security contributions and all national taxes (except on importation).
  - ✓ The monthly quota arises from applying the sum of aliquots (30.625%) of the taxes collected by the Social Security Bank on a fictitious salary equivalent to FIVE Basic Taxes (BFC).
  - ✓ Includes optional health insurance (difference with Argentine case). If the coverage of the National Integrated Health System (SNIS) is not opted for, it is obliged to contribute 8% on the Benefit and Contributions Base (PCB) for Health Insurance.

# Uruguay

## ➤ **MIDES Social Monotributo:**

- ✓ Effective since June 2012 and aimed at personal or associative enterprises (up to 4 or 5 partners) of vulnerable sectors, with evaluation and qualification by the Ministry of Social Development (MIDES).
- ✓ Structure similar to Monotributo (ceilings and quotas), but with reduction of the quota during the first 3 years (25%, 50% and 75% of the corresponding value in each year) and with option of health coverage through FONASA.

## ➤ **Small Business Scheme:**

- ✓ Established as Minimum VAT in 2001 and reformed in mid-2007, aimed at commercial or industrial SMEs up to annual turnover (U.I.).
- ✓ It requires minimum monthly payment for VAT, exempts from IRAE and IPE (assets), provides for a reduced and gradual application of VAT and Employers' Contributions to the BPS for 2 years (25% 1st and 50% 2nd).

## Number of contributors:

Monotributo: 3,256 (Dec-2006) -26,315 (Apr-2013)

Small Business: 20,223 (Dec-09) - 26,628 (Apr-13)

Monotributo MIDES: 22 (jun-12) - 492 (apr-13)

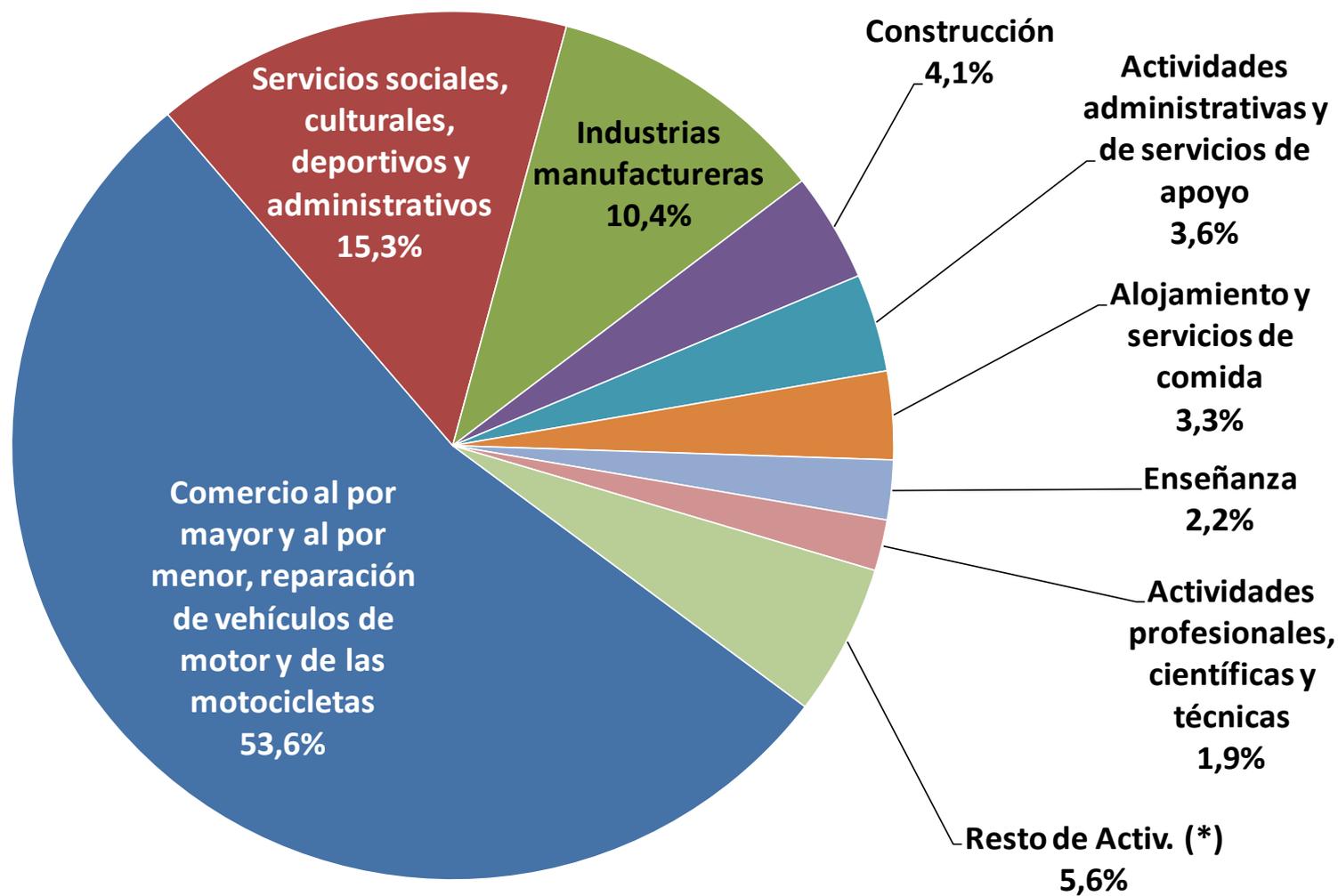
## Revenues:

*% del GDP*

<b>Year</b>	<b>Monotributo</b>	<b>Minimum VAT</b>	<b>TOTAL</b>
<b>2007</b>	<b>0,01%</b>	<b>0,10%</b>	<b>0,11%</b>
<b>2008</b>	<b>0,02%</b>	<b>0,09%</b>	<b>0,11%</b>
<b>2009</b>	<b>0,02%</b>	<b>0,09%</b>	<b>0,11%</b>
<b>2010</b>	<b>0,03%</b>	<b>0,08%</b>	<b>0,10%</b>
<b>2011</b>	<b>0,03%</b>	<b>0,07%</b>	<b>0,10%</b>
<b>2012</b>	<b>0,03%</b>	<b>0,06%</b>	<b>0,10%</b>

Note: The "Monotributo" column includes the figures corresponding to the Social Monotributo MIDES.

# Taxpayers registered in the Monotributo. Perceptual Structure by activity (ISIC). 2013



Source: Based on data from BPS.. Taxpayers registered in Social Monotributo MIDES are not included.

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# Strengths and weaknesses

- All three systems seek to ensure minimum social security coverage for small taxpayers and help reduce informality.
- Technical characteristics vary in each country, although Simples Nacional (Brazil) would reduce the "leap" from simplified regimes to the general regime.
- Argentina generates incentives to remain indefinitely in the monotributo regime by concentrating taxpayers on low incomes.

# Recent reform in Mexico

- New Tax Incorporation Regime (RIF) that, upon the departure of the previous Small Taxpayers Regime (REPECOS), encourages formalization
- To facilitate transit establishes the possibility of joining the Social Security Incorporation Regime (RISS), consisting of a subsidy of social charges of small companies that is decreasing for 10 years
- Workers incorporated into the RISS will be entitled to all social security benefits (including mortgage loans), and employers will be able to contribute and will be entitled to a pension.
- It is a transitory regime that generates a "bridge" to formality, but it has the characteristics closest to the employment policies known in several countries, rather than of tax simplification.

# Recent reform in Colombia

- In January 2017 a Monotributo was introduced in Colombia as part of a broader tax reform.
- The Monotributo in Colombia is optional and only for small firms (traders) who are already paying income tax.
- It is an alternative to the existing Simplified VAT Regime.
- When paying the Monotributo, the payer automatically acquires the right to:
  - ✓ Join a Family Compensation Fund.
  - ✓ Automatic registration of the BEPS, that are a voluntary savings program that is part of the new model of protection for ageing population, promoted by the National Government

# Final Remarks and Future Challenges

- These instruments should be considered as a "transitional bridge" to the tax general regime and social protection, since the indefinite permanence in them affects the fiscal revenues and generates inequities and economic distortions.
- The challenge is to design a system that, at the same time, stimulates the economic and labor formalization and avoid generating a permanent segmentation of the taxpayers in general.
- This is particularly important for pension systems

**Thank you very much!**

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