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Many countries in LATAM, such as Mexico, Argentina, Chile, Colombia, Costa Rica, Uruguay, Paraguay and Ecuador, have taken full advantage of the digital economy's growth by taxing digital services. The result has been not only prodigious increases in tax revenues, but also significant increases of tax compliance on those digital platforms that sell goods and services.

For example, Mexico, Chile and Ecuador as previously did Uruguay and Colombia,

electronic and digital services on Sept. 16, 2020. Now, non-resident digital services providers must register with the tax authority or have payment providers withhold VAT.

The overall result of these changes was that Mexico, which began taxing digital services in mid-2020, increased its tax revenues by $304 million – a 915% jump compared to 2019. Meanwhile, from June 2020 to June 2021, Chile has secured more than 194 million of VAT from digital services. Ecuador is expected to collect more than 19 million dollars for the same services during 2021.

So, as Mexico, Chile and Ecuador experienced tax revenue gains durings the COVID-19 pandemic, some other LATAM counties' tax revenues plummeted. So, how were these countries able to secure such high revenue increases during the COVID-19 lockdown?

The secret has been to mandate the collection of VAT on direct supplies of digital products and services such as Website and data hosting, E-learning, Online membership clubs Auction, gig and sharing economy services, Data processing services, Automated technical and administrative support, and other sales of audio visual media, apps and software. The second part of the secret has been to impose collection and other reporting obligations on digital platforms that act as intermediaries between suppliers and consumers of goods and services.

But is that all for foreign suppliers of digital services?

To collect taxes on B2B supplies of digital services LatAm has relied traditionally on the consumer, that is required to apply the corresponding reverse charge. However, the big bulk of digital services revenues nowadays come from services and products sold directly to final consumers. Therefore, the tax administrations have taken two venues to collect the VAT and other taxes on those sales: The first one is to require the credit and debit card companies used by the purchaser to withhold and submit

Tax administrations want to know in real time everything about the transactions that are carried out in their jurisdictions. For that, they have imposed continuous transaction control mandates (CTCs) that require suppliers of services and products to issue electronic invoices that are pre cleared with the tax authorities. Based on the information obtained from the CTC mandates, the authorities prepare the periodic VAT return of taxpayers.

In fact, in some countries like Mexico, Digital platforms providing intermediation car riding or temporary lodging services such as UBER and AirBnB, are required not only to comply with electronic invoicing obligations but also with many other tax collection and reporting mandates.

In short CTC mandates are becoming the nervous central system of tax compliance in most LatAm, not only for VAT, but also income, excise and social security tax obligations. This system is fully in place for local taxpayers, and sooner rather than later, will reach foreign suppliers of digital services.

LATAM's digitization precedent

First, we have to rewind about 10 years. Beginning in 2010, LATAM countries were some of the first to adopt ambitious programs to digitize the taxation process. In fact, LATAM countries were the first in the world to implement CTCs. These cloud managed services allow tax administrations to collect data in real-time or near-real time from business management systems. LATAM countries' implementation of CTCs have since inspired Turkey, Italy, Poland, France, Hungary and the UK to begin their journeys towards adopting the technology.

CTCs hold multiple benefits. First, they minimize value-added tax (VAT) gaps. But moreover, CTCs also offer a trove of real-time economic data, which has also allowed these countries to keep a real-time pulse of their performance.

CTCs' real-time insights are valuable in any context, but they've been doubly helpful

jumped from 14% in 2019 to 17% in 2020. Daily sales on Mercado Libre, an online marketplace operating in LATAM countries, were twice as high in Q2 2020 as they were in Q2 2019.

Not being physically located in a country, may give a foreign supplier a false sense of immunity from the local tax requirements of the countries where they sell goods or services.

But as most countries know that a significant share of their tax revenues should come from the digital market, they are not only relying on the traditional fines and other sanctions that they impose on local taxpayers. Some countries like Mexico are also mandating the telecommunication companies to suspend any electronic transmission coming from the servers of those foreign suppliers of digital services that do not register and comply with their tax obligations in the country. In addition to that, tax administrations are aware of the reputational damage that may carry being labeled as "Tax Evader". Therefore, they are publishing the lists of those that are in compliance to eventually do the same with those that are not. They are also examining the way of using inter country tax information and collection agreements to enforce compliance of those located in their jurisdictions and selling to other countries.

Therefore, compliance with the local tax obligations is no longer something that can be ignored by foreign suppliers of digital services and products. These services collectively generate vast amounts of revenue each day – numbers that have accelerated due to the pandemic's impact on consumer behavior.

Learning From the Pros

So, what can other countries learn from Mexico, Chile and Ecuador when implementing similar regulations?

At a base level, digitizing the tax reporting process is essential. Digitizing tax

administrators. It can take a country 1-2 years to implement a new e-invoicing mandate from a data exchange perspective. But countries can take over a decade to be able to fully harness taxpayer data through analytics, alongside a fully trained workforce of tax administrators.

While Mexico may be reaping the benefits of CTCs now, it started its journey towards them in 2010. Even now, the country is planning additional steps to fine-tune its analytics abilities.

Still, a 915% increase in tax revenue in one year is worth the footwork.

If there's one lesson that tax administrators can learn from Mexico, Chile and Ecuador, it's that harnessing the digital world for tax reporting holds many benefits. Implementing VAT on digital services can drive up tax revenue. For the foreign suppliers of digital services, keeping up with the numerous compliance obligations of the countries where they sell, is indeed a cumbersome and challenging task, but the economic and reputational damage that non-compliance can carry out is a risk that cannot be ignored. Getting to that point, however, requires bringing your tax reporting into the digital age.

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