

Original Article

# The Regime of Fiscal Incorporation A Measure Against Informality in Mexico

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**Abstract** - This research is based on the new scheme of taxation for individuals earning less than two million pesos to develop business and nonprofessional services. The inclusion of this scheme aims to establish itself as an entry point to the formality through the granting of discounts decreasing taxes during the first years of participation. The aim of this study is to identify the financial, administrative, and tax damages caused in Baja California by the entry of the new tax for micro-entrepreneurs and to know whether the benefits in favor of formality are reality or mere myth. A longitudinal descriptive study with data from micro-entrepreneurs in Baja California. Sampling was stratified probabilistic applied, integrating different sectors and strata with a confidence level of 95%.

**Keywords** - New scheme of taxation, Micro-entrepreneurs, Negative effects.

## I. INTRODUCTION

Article 31, section IV of the Political Constitution of the United Mexican States, declares that they are obligations of Mexicans, to contribute to the public expenses of the Federation, as of the Federal District or of the State or Municipality in which they reside, in a proportional manner and equitable as provided by the Laws. Based on this constitutional precedent, the Ministry of Finance and Public Credit (SHCP) has created countless taxes to control a part of society that has sometimes been informal. Since 2014, a new Fiscal Regime has been created, the Tax Incorporation Regime (RIF), which in turn has eliminated the Small Taxpayers Regime and the intermediate regime, which allowed in a simple way to pay the tax and contribute with the State, when paying an integrated quota, however, were unsuccessful, as they were mostly used as figures for tax avoidance, and they failed to convince informal taxpayers of tax payment.

According to the document "Tax statics at Latin America 1990-2000" carried out by the OECD, the national commission from Latin America and the Caribbean (ECLAC), and the Inter-American Center of Tax Administrations (CIAT), the Mexican tax is located just above Nicaragua, where the rate is 19.5%; Panama 18.5%; Peru 18.5%; Paraguay 17.6%; Honduras 17.5% and Salvador rates 15.7%, according to Milenio magazine.

These statistics lead Mexico to undertake one of the most important tax reforms for the country, as Corbachosays (2012), there is no more important reform for the sustainable and inclusive growth of Latin America and the Caribbean that it has to produce in the Tax and Tax Systems of the Region.

As part of this reform is born a tax regime whose tax subjects are micro-entrepreneurs is a new scheme of optional taxation introduced in the Tax Reform approved in 2013 for individuals who perform business activities with incomes of less than two million pesos. This new regime replaces the Small Taxpayers Regime (REPECOS) and the Intermediate Regime, which made that from January 1st, 2014, the REPECOS migrated automatically to the RIF.

This tax regime is aimed at individuals with a business activity that provides public services in general and does not require a professional title. The legal basis of the RIF is found in the Income Tax Law (LISR) in force as of 2014, in Title IV "On Physical Persons", Chapter II "On Income from Business and Professional Activities", Section II "Tax Incorporation Regime", in articles 111 to 113 of the aforementioned Law. On April 8, 2014, the first "Decree by which they are published" was published on April 8 2014. The second, "Disclosed on September 10, 2014; and the third, "Is published on March 11, 2013."

As Cardenas said (2014), the main benefit of this new regime is to be able to gradually incorporate the tax over a period of ten years. However, this does not



guarantee that collection will increase in the short term, since during this incorporation period, the authority will have to sacrifice collection and invest in administrative, technological, human resource infrastructure, etc., to ensure the control and permanence of taxpayers from the informal sector who are incorporated into the formality.

The fiscal reform that came into effect in January 2014 has implied important changes, which have impacted the functioning of small businesses and translate, in some cases, into the choice of adapting or not surviving. It is interesting to note, then, that what Mexico seeks is growth and greater tax collection, based largely on microenterprises since it is known that for this type of business is very easy to live in the informal or to provide a lower collection to the Federation by the low income they receive. In this regard, Corbacho states that tax reforms must respect five basic principles: First, the reforms must include taxes that favor the poor; this implies establishing an income tax with fewer exemptions that have real redistributive capacity but that protects the income of the poorest households.

Second, reforms should establish simpler tax systems with broader tax bases. Most of the tax systems in the region are too complex due to a multitude of exemptions and privileges for certain activities, sectors, or groups of taxpayers. The result is taxes that often severely distort the allocation of resources and generate narrow and fragile tax bases.

Third, tax administrations must be strengthened so that all citizens and businesses comply with their tax obligations. Reduce the high tax evasion and create institutions that guarantee that all economic agents and citizens contribute their part to the collective effort that is an essential element of social legitimization and, as such, a requirement for the sustainability of any tax system designed to promote the development.

Fourth, institutional agreements and consensus are needed to ensure that local governments have the necessary resources to act as agents of development. For the decentralization of public spending to be sustainable, the sources of own resources of local governments must be strengthened, and, fifthly, tax reforms for development should create fiscal systems that look to the future.

The present investigation analyzes some comments on the Fiscal Incorporation Regime, the importance of micro-entrepreneurs in Mexico, and the fight against the informality that the tax authorities have undertaken when implementing this regime.

## II. LITERATURE REVIEW

A significant percentage of the companies in the country are microenterprises that do not exceed two

million pesos in their income in the year. These small businesses generate a considerable number of jobs, both formal and informal, providing support to many Mexican families.

However, it's common knowledge that these companies have traditionally been tax evaders due to the fact that they carry out operations almost exclusively for the general public, that is to say, with clients that do not require tax receipts for production and crediting purposes. Therefore, and in response to the claim of traditionally captive taxpayers, the Federal Executive in 2013 published a decree for the creation of the new law on income tax, which requires tax-payers micro-entrepreneurs to register in the regime of fiscal incorporation and learn about its medium-term fiscal collection.

Informality represents an important barrier for the accelerated growth of productivity, so it will always be an objective on the part of the tax authorities to promote formality. In Mexico between 2000 and 2010, the regime of small taxpayers (REPECOS) registered an evasion higher than 96%, this based on the Tax Evasion Study in the Small Taxpayers Regime, prepared by the Monterrey Institute of Technology and Higher Education City Campus of Mexico, Unit of Strategic Studies Center, coordinated by the Investigator Hugo Javier Fuentes Castro and his team, dated October 4, 2011. On the other hand, according to the Procurator of the Defense of the Taxpayer (PRO DECON), this new regime also seeks to promote more accelerated growth of productivity with the purpose of preparing taxpayers for an eventual insertion in the General Regime of taxation. In addition, it is said that this regime will allow the tax authority to complete the chain of verification and tax information by having records about the operations of the participants with their suppliers and customers.

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records about the operations of the participants with their suppliers and customers.

It's important to emphasize that the effectiveness and compliance with the goals of this regime are not immediate; in principle, the benefits should be reflected in an increase in the tax-payer register and, therefore, in the collection. Therefore, the questions arise as to whether the taxpayers operating in the informal sector were indeed convinced to join.

**III. OBJECTIVES**

The present investigation has as a general objective to identify the effectiveness of the regime, as well as the financial, administrative, and fiscal effects that it caused to the micro-entrepreneurs of Baja California, the entry into force of the RIF.

The specific objectives derived from the general objective of the research are:

First, identify the items where the taxpayers required greater monetary resources with the arrival of the RIF

Second, analyze the tax burden of the new regime for taxpayers.

Third, identify the collection statistics according to the tax authorities.

**IV. METHODOLOGY**

In this study, the method used to carry out the investigation was the longitudinal descriptive one, by virtue of the fact that information was collected from the micro-enterprises domiciled in the Baja California state, regarding the affectations suffered in the administrative, financial and fiscal scope, become a RIF the population subject to study is composed the micro-companies established in Baja California area, which were selected by means of stratified probabilistic sampling, integrating the different sectors and strata into the sample, achieving results with a confidence level of 95%.

In the first phase of the research, bibliographic information related to the subject was collected and analyzed. Subsequently, the databases of microenterprises located in the cities of Tijuana, Mexicali, and Ensenada, in the Baja California state, were identified in order to select the most reliable and complete. In the second phase, the questionnaire was designed and applied to the selected sample. Subsequently, the information obtained in the SPSS statistical program was captured.

Finally, in the third phase, the statistical analysis of the information obtained was carried out, and the research report was obtained.

**V. RESULTS**

In Baja, California, there are currently 7027 microenterprises; questionnaires were applied in

Mexicali to Commerce in 56%, 40% Services, and 4% of other activities. In Tijuana, the application of questionnaires was 62.7% Services, 36% Commerce, and 1.3% others. While in Ensenada, the sample consisted mainly of the Trade Sector in 65.7% and of the Services Sector in 34.3%.

Table 1 indicates the main results obtained from the application of the questionnaire are the following: first, of the surveys applied, data was obtained on the regime to which the taxpayers were assigned before the arrival of the RIF, leaving the data as follows:

**Table 1. Results of the instrument**

CITY	REGIME			TAXPAYER
	REPOS	INTERMEDIATE	General	NOT REGISTERED
Mexicali	62.7	14.7	9.3	13.3
Tijuana	64	14.7	8	13.3
Ensenada	51.5	30.9	10.3	7.3

Own preparation, figures expressed as a percentage.

In order to comply with the new fiscal obligations of the Tax Incorporation Regime, the Tax Administration Service (SAT), which is the body responsible for applying tax and customs legislation in our country, has designed the necessary tools to facilitate compliance with tax payment. This virtual platform allows, among other things, the small business owner to issue invoices, capture his income and expenses in a virtual platform called my accounts, and then use that information in his monthly statements. In this respect, the Forbes magazine cited above mentions, compared to not keeping accounts, the incorporation regime if it implies a greater administrative burden for micro-entrepreneurs. In addition, the Chamber of Commerce, Services and Tourism in Small in Mexico City (CANACOPE) states that between 40 and 42% of small businesses are adults over 60, who are not familiar with the new electronic programs, therefore the resistance to join the RIF.

Taking as a basis the new tools that the authorities have made available to taxpayers, the micro-entrepreneurs were asked who generates the accounting and financial information of the business, whether an accounting firm or an internal accountant, finding that in Mexicali 65.3% the accounting information is generated in an accounting firm, in Tijuana in 62.7% and in Ensenada in 76.5%. While only 34.7% have an Internal Accountant in the city of Mexicali, in Tijuana only 33.3% and in Ensenada 22.1%.

Another important question was to identify the contributions that cause a greater expense for the taxpayer, the options that were provided were the Income Tax (ISR), Value Added Tax (IVA), Special Tax on Production and Services (IEPS) ) and Social Security Contributions, finding IVA as one of the taxes that cause the smallest businesses in the cities of

Mexicali and Tijuana with a proportion of 57.3% and 69.3% respectively, however it is interesting to note that in the case of Ensenada, the causation of this tax is relegated to a second place with 29.4%, while the ISR represents 48.5% of the causation, while for the cities of Mexicali and Tijuana it represents 32% and 22.7% respectively.

On the other hand, it was observed that both the IEPS and the social security contributions, such as the payment of fees to the IMSS and INFONAVIT, do not generate a large outlay for micro-entrepreneurs, since, in the case of the IMSS and INFONAVIT, Mexicali responded in a 45.3% that are contributions are not the most important for your company, Tijuana had a similar response with 52% and Ensenada 47.1% said not to be affected by these contributions.

From the answers obtained by the taxpayers, we find first of all that strategy of the tax authorities to create a new regime that allows the incorporation of businesses that were in informality and that contribute to public spending by paying their taxes, in the first instance if it is working, but slowly because it was observed that there are few businesses so far that have regularized their fiscal situation.

Now let's analyze the data provided by the collecting entities; according to data from the Center for Public Finance Studies, in 2015, the Ministry of Finance and Public Credit (SHCP) presented hard data in its Report on the Economic Situation, Public Finance, and the Public Debt, where it is observed that the use of the application of "My accounts" was 5,396,438 of operations, on the other hand, the number of taxpayers registered in the RIF in the same period was 4,356,478, of the figures it is concluded that each subject registered in the registry carried out 1.23 operations in the period from January to March 2015. Likewise, it was observed that the collection obtained by the RIF in the first quarter of 2015 was 1.191 million pesos (MDP), a figure that represents 0.18% of the Non-Oil Tax Revenue registered for the same period, amounting to \$ 664,018.3 million pesos. Another interesting fact contained in the quarterly report is that the rate of collection of Income Tax (ISR) as well as the Special Tax on Production and Services (IEPS) are minimal since the first tax was obtained a total of 3 MDP; In the same order of ideas, the tax that collected the most in the multisided regime was the Value Added Tax (IVA), since its collection was for 1,179 million pesos. Undoubtedly, this date coincides with the response of the surveyed taxpayers who assert that their higher expense is due to IVA tax.

Since its inception, the collection of the RIF has been good; however, as shown by the SHCP in the aforementioned report when evaluating the results obtained by the RIF, in comparison with the income obtained by the Extinction of Small Taxpayers Regime

( REPECOS), the following was obtained, according to what was published by the SHCP, the REPECOS in the first quarter of 2013, obtained revenues of \$ 897 mdp8, while the revenue reached by the RIF in the first quarter of 2015 was 1,191 MDP, a figure that increased by 23.7 percent in real terms. On the other hand, the standard that integrated the REPECOS according to data from the SAT was 3, 886,294 taxpayers, compared to the standard of 4,356,478 made up of the RIF during the first quarter of 2015, which means an increase of 12.09 per hundred since its creation; that is, in the first 15 months of birth, the RIF increased the taxpayer base, growing by 470,184, at an average rate of 31,346 monthly contributors.

As you can see, the entry of this regime was rapacious, but the question arises about whether it continues to collect in the same way, according to the tax and management report of the second quarter of 2018 issued by the SHCP, during the first quarter of 2018, non-oil tax revenues were located in 1 trillion 558 thousand 76.6 million pesos, this is 92 thousand 231.6 million pesos more than budgeted in the Law of Income of the Federation (LIF), 6.3% higher. With respect to the same semester of 2017, revenues grew 1.1% in real terms.

Another important fact highlighted in the aforementioned report is the dynamism shown by the taxpayers' register, since by June 2018, this pattern was made up of 68.4 million taxpayers, which means an increase of 6.9 million taxpayers (11.2%). With respect to the same month of the previous year. The Income Tax (ISR) presented an increase of 0.4% in real terms with respect to the same period of 2017, and it was 60 thousand 413.4 million pesos above the LIF. The VAT, for its part, showed a growth of 9.8% in real terms with respect to the previous year and exceeded the goal of the LIF in 49 thousand 314.5 million pesos.

The collection obtained during the first semester of 2018 was 3 thousand 918 million pesos, this is an increase of 15.4% real compared to the first semester of 2017, and the number of registered taxpayers in the RIF is 5 million 76 thousand 244 For its part, the incentives of this regime were 13 thousand 635.7 million pesos, 10.4% less than those registered in the same period of the previous year.

The taxpayers of the RIF use the application "My Accounts" to record their operations of income, expenses and issue invoices. In the second quarter of 2018, there were 14 million transactions in that tool, 14.9% more operations than in the same period of the previous year.

## VI. CONCLUSION

The year 2015 was a year full of challenges for small entrepreneurs who faced not only a change in

their tax regime but also a greater tax burden since the modification of their obligations under the new regime redesigned the way of presenting the information. This taxpayer is currently obliged to keep accounts, file returns, invoice, and other formal obligations that previously did not have.

Therefore, after having made the present investigation, the following conclusions are presented: First. That the establishment of the new RIF regime, if it establishes administrative burdens for taxpayers with incomes less than two million pesos and that although most of the respondents have hired an accounting firm to keep the accounts, many taxpayers have observed an increase in the administrative burden of your business, because now you have to invoice, keep an adequate record of your deductions and present your bi-monthly payments in the virtual tools that for this purpose have prepared the authority.

Second. That according to data from the Ministry of Finance and Public Credit, this tax has increased the collection and also the taxpayer register, which implies an advance for informality, comparing the first quarter of 2015 with the base of taxpayers registered in the RIF was 4, 356,478, while the data reported by the same Secretariat in June 2018, show how this pattern was made up of 68.4 million taxpayers. Undoubtedly, then, the RIF as a tax regime has been successful in incorporating various taxpayers into the formality. However, the question remains if these new captive taxpayers are satisfied with their new obligations because, to date, the fiscal stimuli that were planned for. This regime has been decreasing, which implies a higher payment on your taxes. On the other hand, taxpayers who were already registered and automatically went to the RIF underwent major administrative changes because of not keeping formal accounts and paying their taxes based on estimates. Currently, they are forced by the former small taxpayers and intermediate regime, not only to be formal but to keep electronic accounting, to invoice and bear an administrative burden to comply with these obligations.

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