

# “Tax digital invitations” the new form of tax reviews initiated by the Mexican tax authorities

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## **Background**

The Mexican Tax Authorities (SAT) have very actively pursued the digitization of tax compliance in Mexico. Examples of this are the implementation of electronic tax invoices (CFDIs) to document all economic transactions, the pre-population of individual income tax and VAT returns, the tax electronic audit program and new monthly tax electronic accounting obligations that include: i) chart of accounts; ii) trial balance; and iii) journal entries.

The use in real time of data obtained from the implementation of these programs has increasingly allowed the tax authorities to have unprecedented insight into the behavior and planning of taxpayers. This, in turn, has contributed to a substantial increase in the tax collection.

## **“Tax digital invitations”, the new form of tax reviews initiated by the Mexican tax authorities**

The Mexican tax authorities have, in the last months, started to review the tax position of taxpayers by sending “Tax digital invitations”. In said invitations, the SAT requests for the company's legal representative to attend a live meeting to discuss inconsistencies or omissions detected by cross referencing the information sent by the taxpayer against universe of data available to the tax authorities through the tax compliance programs in place.

Taxpayers are encouraged to clarify or self-correct these inconsistencies in a very short period of time. If no corrections are made, the SAT will very likely initiate a formal audit process, in which case the payment of penalties will apply by law if tax is due.

Tax invitations mainly derive from inconsistencies obtained by the tax authorities upon carrying out the following tests:

- a. Comparison of payroll withholding income taxes (WHT) reported in the CFDIs issued by the taxpayer and WHT effectively paid;
- b. Comparison of payroll WHT reported in the monthly payroll returns filed by taxpayers against the calculation made by the tax authorities based on information contained in CFDIs;
- c. Comparison of the revenue included in the CFDI against the monthly and annual income tax returns filed by the taxpayers;
- d. Detection of operations with blacklisted providers that are not complying with their own tax obligations;
- e. Comparison of the VAT reported in CFDIs against the VAT reported by taxpayers in the monthly tax returns;
- f. Detection of unusual tax payment fluctuations when compared to past cycles.

In many cases, these inconsistencies are not fully analyzed by the tax authorities under the income tax rules as they only limit their observations through cross-checks and validations across different data points.

#### **Legal perspective involving “tax invitations”. What to do.**

From a legal perspective these Tax Invitations do not constitute formal tax audits since they do not follow the formalities required under the Mexican Federal Tax Code for such audits.

Any preliminary conclusion shared by the tax authorities with taxpayers during these meetings can't be taken as the initial formal procedure of a tax audit.

In practice however, when a taxpayer receives a Tax Invitation, the tax authorities usually provide a very short period of time (e.g., 6 to 10 days) to respond. This, in turn, causes significant stress in terms of human resources and systems required to respond appropriately.

In general, taxpayers are interested in responding and addressing information inconsistencies, as most likely an appropriate response will stop the initiation of a formal audit procedure. For this reason, it is increasingly critical for taxpayers to have systems and automated processes that can rapidly assist them generating information and monitor regularly their own tax profile.

Further, in an ideal world, taxpayers should consider cross referencing the information sent monthly or annually in their tax returns with the CFDIs available in the infrastructure of the tax authorities **before** the tax returns are filed. For example, before filing monthly provisional income tax returns, taxpayers could cross-reference in an automated way the information about to be submitted with the CFDIs available to the tax authorities. This will anticipate the detection of issues that would likely be brought up by the tax authorities in a tax invitation, with the possibility of solving them before the actual filing or at a minimum, be ready to address them up-front in a tax invitation.

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