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HOUSE BILL 2482 WITH PROPOSED CHANGES TO THE PUERTO RICO INTERNAL REVENUE CODE OF 2011, AS AMMENDED

Year 2015 Issue #7

In a new attempt to enact tax measures that create higher sources of revenue for the Government after a failed attempt to approve a complete Tax Reform, House Bill 2482 was submitted this week. This Bill maintains in effect the current Puerto Rico Internal Revenue Code of 2011, as amended (herein "PRIRC"), but brings significant changes to certain aspects. We will highlight some of these changes throughout this Tax Alert.

Individual Income Tax

- Individual Income Tax Rates will continue to remain at the rates used for the 2014 returns.
- The Gradual Adjustment, that consisted of an additional tax calculation for certain high income individuals, will be enacted once again for all individuals with income subject to tax of $500,000 or more.
- Deduction for charitable contributions made after December 31, 2014 will only be allowed if the charity or non-profit organization is authorized by the Puerto Rico Treasury Department as a charity.
- Net Capital Losses carried forward to a future period will only be allowed as a deduction up to 80% of the current year capital gains.

Corporate Income Tax

- Companies with intercompany expenses incurred and paid to related party located outside of Puerto Rico will be allowed to obtain a waiver from calculating the 20% alternative minimum tax on these expenses. However, the rules would limit this waiver to 60% of these expenses. This limitation also applies for the deductibility of these expenses for regular income tax purposes.
- Intercompany purchases from related parties located outside of Puerto Rico will be subject to alternative minimum tax on these purchases on a rate that increases progressively depending on the company's gross revenue. The tax will begin at a 2.5% rate once gross revenue is $10,000,000 or more, and can increase up to 6.5% for companies with $2,750,000,000 or more of gross revenue.
- For purposes of the alternative minimum tax on intercompany purchases, no waiver will be approved for periods beginning after December 31, 2014. Any waiver already in effect for any period beginning after December 31, 2014 will be subject to certain limitations.
- Net Operating Losses available for alternative minimum tax purposes will be limited to 70% of income subject to alternative minimum tax for periods ending after December 31, 2014.
- Net Operating Losses available for regular income tax purposes will be limited to 80% of income subject to regular tax for periods commencing after December 31, 2014.
- For purposes of Net Operating Losses, no deduction will be allowed in a future period for the portion of the net operating loss that consists of intercompany expenses paid to a related party located outside of Puerto Rico.

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HOUSE BILL 2482 WITH PROPOSED CHANGES TO THE PUERTO RICO INTERNAL REVENUE CODE OF 2011, AS AMENDED (CONTINUED)

- No deduction will be allowed for services contracted and paid to a non-resident taxpayer if the taxpayer engaging these services did not pay the sales tax and/or value added tax described later on in this Tax Alert. This will also apply to the deduction of depreciation on the purchase of any other taxable item purchased from a non-resident taxpayer.
- Net Capital Losses carried forward will only be allowed up to 80% of current year capital gains for periods commencing after December 31, 2014.
- There will be new rules for certain taxpayers considered as "Large Taxpayers" by definition of the PRIRC. These taxpayers include, among certain types of industries, any taxpayer with gross revenues in excess of $50,000,000 yearly.

Partnership Income Tax

- Partners of Corporation of Individuals, Special Partnerships and Partnerships will now have a limit on the deductibility of prior year net operating losses. For year commencing after December 31, 2014, the loss deduction will be 80% of the current year aggregate distributable share of net income.

Sales & Use Tax (Until March 31, 2016)

- Sales & Use Tax ("SUT") rate from July 1, 2015 through March 31, 2016 will be increased from the current 6% (currently 7% including the municipal portion) state SUT to a 10.5% (11.5% including the municipal portion) state SUT on most taxable items and combined transactions.
- From October 1, 2015 through March 30, 2016, services rendered from one registered business to another, also known as B2B transactions, and designated professional services will be subject to a 4% state SUT.
- The taxpayer responsible for the SUT in Puerto Rico on taxable services, B2B services and designated professional services rendered by a non-resident service provider will be the recipient of these services.
- Duly Registered Resellers will be allowed 100% credit on their monthly sales & use tax returns for the amount of tax paid on the purchase of inventory.
- There will be transition rules for contractors that had pending contracts or bids on contracts so that they can purchase goods estimated under the pending contract or bid at the previous rate.

Value Added Tax (Starting April 1, 2016)

- A new Value Added Tax ("VAT") would also be enacted under this Bill. The rate would be 10.5% state VAT (11.5% VAT assuming that the 1% Municipal Portion is not repealed) and goods sold for export and services exported will be subject to a 0% state VAT. Goods imported into Puerto Rico will not be subject to the VAT if the seller of the goods charged the VAT on the sale.
- Under the VAT, designated professional services and B2B transactions will be taxable. However, the lease of commercial space by a registered business will be exempt.
- In cases where the seller of a good or service is required to collect the VAT as a withholding agent, the seller will be principally responsible but the buyer could also be subject to the tax if the seller did not comply with the withholding requirement.

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HOUSE BILL 2482 WITH PROPOSED CHANGES TO THE PUERTO RICO INTERNAL REVENUE CODE OF 2011, AS AMENDED (CONTINUED)

- Any business that sales goods and services, except "Small Businesses" discussed above, will be required to charge the VAT as a withholding agent.
- Businesses that buy goods and services can request a Fiscal Receipt from the seller within 30 days of receiving the goods or services only if those goods and services were taxable and that the sale was not retail.
- The Fiscal Receipt will indicate, among other things, certain information including the name of the seller and buyer, the value of the purchase, the amount of tax attributable to the sale, the amount of the value plus the tax and any other information that the Secretary of the Treasury deems necessary.
- There will be additional requirements when a Fiscal Receipt is issued and afterwards there are returns or other types of adjustment to the transaction's value.
- The price of goods and services and the VAT will be presented separately, unless the seller requests that the VAT be included as part of the price and the Secretary of the Treasury approves it.
- Goods imported by air carrier or postal services will be allowed to report and pay the VAT on or before the 10th day of the month following the import.
- Businesses will be allowed to credit the VAT paid on the purchase of goods and services to their monthly VAT returns. Any portion of VAT paid that is proportionate to exempt sales will not be allowed as a credit.

Please contact us here at RSM where we are prepared and committed to answer all your inquiries related to these new rules.

- Telephone: 787-751-6164
- Fax: 787-751-6865
- Email: tax@rsm.pr
- Webpage: www.rsm.pr