THE POWER OF BEING UNDERSTOOD

THE GOVERNOR OF PUERTO RICO HAS SIGNED ACT 72 OF 2015

Year 2015 Issue #8

The Governor of Puerto Rico has signed into law Act 72-2015. As highlighted previously, this Law changes several tax rules in Puerto Rico for individual income tax, partnership tax, corporate income tax and sales & use tax. Here are a few excerpts of these changes:

Individual Income Tax

- Individual Income Tax Rates will continue to remain at the rates used for the 2014 returns; No reduction in individual income tax rates was approved.
- 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.
- The 2% special tax for individuals with $200,000 or more of self-employment income will no longer be in effect for years starting after 2014.

Corporate Income Tax

The following tables summarize some of the new rules:

INTERCOMPANY EXPENSES		
	Before Act 72-2015	*After Act 72-2015*
Intercompany Expenses paid to Related Parties Outside of Puerto Rico – Regular Tax	Subject to 51% Limitation, full waiver from this rule allowed.	Subject to 51% Limitation, waiver will only be allowed for up to 60% of intercompany Expenses
Intercompany Expenses paid to Related Parties Outside of Puerto Rico – AMT	20% AMT on intercompany expenses not subject to withholding, full waiver from this rule allowed	20% AMT on intercompany expenses not subject to withholding, waiver only allowed up to 60% of intercompany expenses
Intercompany Purchases from Related Parties Outside of Puerto Rico (only for businesses with $10 million or more of gross revenues)	2% AMT on intercompany purchases. Partial waiver allowed.	2.5% through 6.5% AMT on intercompany purchases. No new waivers after 2014. Rate depends on level of gross revenues.

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NET OPERATING LOSSES		
	Before Act 72-2015	*After Act 72-2015*
Regular Net Operating Losses	Limited to 90% of Current Year Taxable Income	Limited to 80% of Current Year Taxable Income
Alternative Minimum Tax Losses	Limited to 80% of Current Year AMT Income	Limited to 70% of Current Year AMT Income
Intercompany Expenses	All deductible portion is allowed as part of NOL.	Not allowed as part of the NOL to be carried forward.

In addition to these changes, the new rules also state that any portion of services provided by a non-resident service provider will only be deductible to the extent that the recipient of these services duly pay any applicable sales & use tax or value added tax, which we will describe later on in this Tax Alert. This will also apply to the depreciation of assets purchased from non-resident vendors. If the business in Puerto Rico that purchases the fixed assets fails to pay the sales & use tax or value added tax on the purchase, as applicable, then no deduction for depreciation will be allowed.

Also, Net Capital Loss carry-overs for corporations will now be limited to 80% of current year net long term capital gains.

This Act also creates a new type of taxpayer named "Large Taxpayers" that will be required to file their respective income tax returns in a separate office and in the manner that the Secretary of the Treasury will soon determine. "Large Taxpayers" include:

- Commercial Banks or Trust Company
- Private Bank
- Brokerage Houses
- Insurance Companies
- Businesses dedicated to Telecommunications; or
- Any business with $50,000,000 or more of gross revenues in the previous tax year.

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Sales & Use Tax

This Act has also changed several rules regarding sales & use tax (SUT) in Puerto Rico. These changes, for the most part, begin on July 1, 2015 and principally entail an increase in the current rate from the current 7% to an 11.5%. The following table summarizes how these changes will be implemented, since there are several relevant dates in which these rules will begin.

SALES & USE TAX (SUT)			
	Before Act 72-2015	*Starting July 1, 2015*	*Starting October 1, 2015*
Designated Professional Services (Lawyers, Architects, CPAs, etc.)	Exempt	Exempt	4% state tax
Business to Business Services - General Rule	Exempt	Exempt	4% state tax
Bank Charges, collection services, security services, cleaning services, laundry services, repairs and maintenance, waste disposal services, telecommunications and vehicle leases	Subject to 7% SUT	Subject to 11.5% SUT	Subject to 11.5%
Medical Services	Exempt	Exempt	Exempt
Educational Services	Exempt	Exempt	Exempt

There will be temporary provisions for merchants with gross sales of $1,000,000 or less that will allow these businesses to pay the SUT for the month of July 2015 in four separate installments, the last one being in November of 2015. Also, the credit available for resellers of use tax paid on imports against SUT collected on sales will be increased from the current 75% to 100%. Furthermore, the buyer of services from a non-resident vendor will be principally responsible for self-assessing and paying the 4% or 11.5%, as applicable.

For businesses with pending contracts or bids awarded before July 1, 2015 there will be a 12 month period where purchases under this contract or bid will be subject to the rules and rates prior to July 1, 2015. The Secretary of the Treasury will issue rules to establish the manner in which this temporary rule will be implemented.

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

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Value Added Tax

Starting in April 1, 2016, a new Value Added Tax (VAT) will be enacted as part of the progressive changes that this Act introduces. The VAT will be 10.5% and Act 72-2015 states that Municipalities will still collect a 1% SUT based on the rules and regulations currently in effect. This means that in the aggregate both the VAT and SUT will represent an 11.5% tax rate on many goods and services.

Under the VAT, some rules will differ when compared to the rules for SUT. This includes Designated Professional Services such as Lawyers, Architects and CPAs, among others, that will be subject to the full 10.5% VAT. Services provided between one registered business and another registered business will be subject to the 10.5% VAT as well. Other services such as bank charges, collection services, security services, laundry services, cleaning services, repairs & maintenance, waste disposal services, telecommunication services and vehicle leases will also be subject to the 10.5% VAT and seem to continue subject to the 1% municipal SUT since they are currently subject to the 1% municipal SUT.

In addition, VAT paid on goods and services will be available to businesses as a credit, subject to certain limitations. Businesses that contract services to be provided by non-resident vendors will be principally responsible for self-assessing the VAT on the value of these services.

Some transactions will be considered 0% sales which although no tax is applicable, they will not be considered exempt transactions. This includes the sale of goods for export, the export of services and the sale of certain eligible items to manufacturing plants. Small businesses that will not be required to charge VAT on sales will be those with yearly gross revenues of less than $125,000.

Also, businesses will be required to generate certain fiscal receipts that must be furnished to clients, upon request under the time limits established, stating the amount of tax paid on each transaction. The buyer will have to require these fiscal receipts in order to be allowed to credit the amounts paid on the monthly VAT return. This credit will have certain limitations for those business that have exempt sales (not including 0% sales).

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