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VAT – CREDIT CALCULATION, REFUND AND RETURNS

Year 2016 Issue #5

As part of our VAT series, this tax alert will briefly explain the credit system and the documentation requirements to claim the corresponding credits as well as the tax returns that will be required under the value added tax (“VAT”) regime. In order to make it more easy to explain and follow, we have decided to prepare this tax alert on a frequently asked questions format, based on the questions and/or concerns we have been receiving so far from our clients.

It is important to note that this tax alert does not include all calculations and/or possible different application of the credit determination that may be appropriate to your particular situation. This publication is meant as a broad guideline to present the general rules applicable in certain situations.

Credit calculation

Who can claim the credit in the VAT return?

- Every merchant registered as such that does not possess a Small Merchant’s Registration Certificate

How do I determine the amount of VAT available for credit?

A merchant will be entitled to claim a credit for the amount of VAT that results from the sum of:

- VAT paid on the introduction of articles imported to Puerto Rico and reported on the Tax on Imports Monthly Return
- VAT paid on the purchase goods and services, as shown on the fiscal voucher; and
- VAT amount self-assessed by a merchant for receiving a service from a nonresident person, as shown on the Monthly Value Added Tax Return.

Direct or Indirect VAT?

In those cases where it cannot be determined whether the VAT corresponds directly to a particular sale of goods or rendering of taxable services, then it will be considered that it could be indirectly related with the sale of goods that are exempt and therefore not completely creditable.

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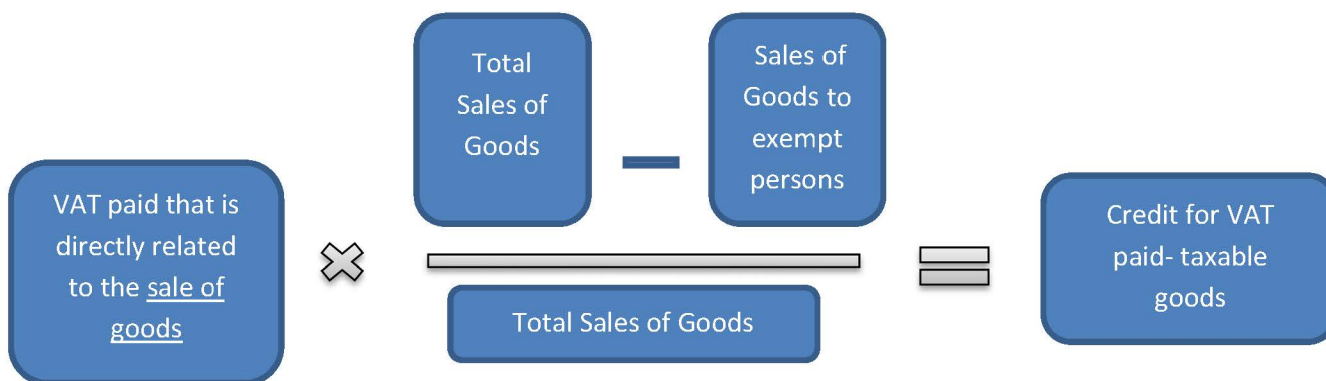
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Direct VAT

The recently issued proposed regulations establish that a merchant that reports taxable sales of goods and services has to separately identify and calculate:

- The credit for VAT paid directly attributable to the sale of taxable goods and,
- The credit for the VAT paid directly attributable with the taxable services rendered.

It further states that a merchant will determine the credit for VAT paid related to taxable goods using exclusively the gross sales of goods (excluding services) generated during the month. To calculate the VAT credit directly related with the sale of taxable goods the following formula must be used:



In order to calculate the credit for VAT paid directly attributable to the sale of taxable services, the following formula must be used:



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The credit directly attributable to sale of taxable services may be claimed exclusively in cases where the merchant uses a subcontractor to provide taxable services to its clients.

After these separate computations are made, then the results will equal the amount of credit for VAT paid that is directly attributable to taxable transactions.



There is a monthly reconciliation of the direct credit that is required and it applies to merchants that report taxable sales and sales to exempt persons during a particular month. This reconciliation will allow or disallow the excess direct credit limited by the above calculations and may increase or decrease the VAT credit amount for a certain month.

Indirect VAT

The following formula must be used to calculate the VAT paid that is indirectly attributable to sale of goods or services:



The excess indirect credit attributable to exempt sales will not be allowed as a credit in the current and future returns.

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What are indirect costs that could generate indirect VAT?

Examples of indirect costs:

- Acquisition of office supplies
- Accounting services
- Telecommunication services
- Maintenance/Repairs
- Security services

Important exceptions:

- VAT paid regarding the acquisition of goods that are sold to beneficiaries of the Federal Nutrition Assistance Program ("PAN") or under the Special Supplemental Nutrition Program for Pregnant Women, Nursing and New Mothers, Infants and Children (known as "WIC") will be considered VAT paid directly related to the sale of goods or the rendering of taxable services. Also, PAN and WIC sales will be considered taxable sales **only** for purposes of the credit calculation.
- Merchants *principally engaged* in the following activities may elect to claim a credit on the Monthly VAT Return for the VAT paid *up to the total amount of the tax paid or accumulated during the month*.
 - the sale of unprepared food or provisions, detail or wholesale;
 - in the sale of prescription medicines, medicines or articles for the treatment of health conditions; and
 - in the wholesale or retail sales of goods that are subject to excise taxes under the following categories:
 - Gasoline
 - Crude oil, unfinished oils and end products derived from oil and other hydrocarbons mixture.
 - Vehicles

Am I principally engaged in one of the activities described above?

The term "principally" means that during the three (3) taxable previous years, the merchant had an average of seventy (70) percent or more of his retail sales from any of the activities listed above.

What kind of documentation will I need to claim the credit?

- VAT reported on a Fiscal Voucher
- VAT reported on the monthly tax on imports return
- VAT reported due to self-assessment on the monthly VAT return

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VAT – CREDIT CALCULATION, REFUND AND RETURNS (CONTINUED)

Is the VAT paid on the acquisition of fixed assets creditable?

A new concept introduced by the proposed regulations recently issued by the Puerto Rico Treasury Department, is the treatment of the VAT paid on the purchase or construction of fixed assets that exceeds \$100,000 dollars in cost. The VAT paid in these cases will be:

- Considered as indirect VAT;
- Has to be transferred to subsequent VAT returns until is used as a credit in its entirety; or
- May be claimed as a refund once a 12 month period has lapsed

Can the excess VAT be refunded?

The excess of the creditable VAT over VAT withheld and due has to be reported on the next months' return. Once this excess is \$10,000 dollars or more, a refund of the amount may be claimed:

- immediately if it is an Eligible Merchant; or
- if it is the third consecutive month showing an overpayment, regardless of the amount

VAT returns

Under the VAT regime, the returns required for sales and use tax purposes will still be required. Therefore, the following returns need to be filed:

- Import Declaration – due each time an article is introduced into Puerto Rico
- Monthly import value added tax return – due the 10th of each month and:
 - Report a summary of all the import declarations that occurred during a particular month; and
 - required to claim the VAT credit
- Monthly VAT return – due the 20th of each month
 - Reports all sales generated during a particular month to determine the amount of VAT withheld, credit available and payment due.

Small Merchants' Annual Informative Declaration – every Small Merchant must present a declaration that is due 60 days after the due date of filing for the income tax returns of such small merchant, including extensions. The declaration will reflect the total amount of sales generated during the previous taxable year and any other information required by the Puerto Rico Treasury Department.

Here at RSM Puerto Rico, we are prepared to answer your concerns or inquiries regarding these new rules. If you would like more information regarding this matter, please contact your tax advisor at RSM Puerto Rico.

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