

International Tax Puerto Rico Highlights 2018



Investment basics:

Currency – US dollar (USD)

Foreign exchange control – No

Accounting principles/financial statements – US GAAP. Financial statements generally are required annually, along with supplemental financial information.

Principal business entities – These are the corporation, limited liability company, partnership, joint venture, cooperative, closely held corporation and branch of a foreign company.

Entities operating in Puerto Rico generally must register with the Puerto Rico State Department, the Puerto Rico Treasury Department, the State Insurance Fund, the Puerto Rico Labor Department and any municipality where a fixed place of business is established.

Corporate taxation:

Residence – A company is resident in Puerto Rico if it is created or organized in Puerto Rico (i.e. a domestic corporation) or is a foreign corporation engaged in a trade or business in Puerto Rico.

Basis – Domestic corporations are taxed on their worldwide income. Nonresident corporations are taxed on their Puerto Rico-source income and income that is effectively connected with a Puerto Rico trade or business. For tax purposes, the US is considered a foreign jurisdiction.

Taxable income – Corporate tax is imposed on a company's net income, which consists of all income (less certain exclusions), reduced by ordinary and necessary business expenses. A portion of the expenses paid to a related party may be subject to disallowance.

Taxation of dividends – Dividends paid to eligible shareholders generally are taxed at a rate of 15%.

Capital gains – Capital gains are taxed at a rate of 20%.

Losses – Net operating losses (NOLs) incurred in tax years beginning after 31 December 2004 and before 1 January 2013 may be carried forward for 12 years; NOLs incurred in tax years beginning after 31 December 2012 may be carried forward for 10 years. The NOL deduction is limited to 80% of the net income for the year. NOLs may not be carried back.

Rate – The corporate tax rate in Puerto Rico comprises a base rate of 20%, plus a graduated surcharge.

Surtax – A graduated surcharge is levied in addition to the corporate income tax, at rates that range from 5% to 19%. The maximum surcharge rate is reached at levels exceeding USD 275,000 of net income. The first USD 25,000 of net income is not subject to the surcharge.

Alternative minimum tax – The alternative minimum tax (AMT) applies to "alternative minimum net income" at a 30% rate, and may be reduced by the alternative minimum tax credit for foreign taxes paid.

Foreign tax credit – Resident corporations may credit taxes paid to foreign governments, as well as to the US and other US possessions, against the corresponding Puerto Rico tax.

Participation exemption – No

Holding company regime – No

Incentives – Various incentives are available to the manufacturing and export services industries, among others, which can lower the income tax rate for these businesses to 4% or less.

Withholding tax:

Dividends – Dividends paid to nonresidents generally are subject to a 10% withholding tax.

Interest – Interest paid to related parties not engaged in a trade or business in Puerto Rico generally is subject to a 29% withholding tax.

Royalties – Royalties paid to nonresidents are subject to a 29% withholding tax.

Technical service fees – A special contribution of 1.5% of the total contract amount is imposed on a contract for professional services, consulting services or legal services concluded with the Commonwealth of Puerto Rico.

Branch remittance tax – A resident foreign corporation that derives less than 80% of its income from Puerto Rico activities is subject to branch profits tax at a rate of 10%, in lieu of the 10% withholding tax on dividends. This is an annual determination made at the time the income tax return is filed, and the tax is due even when an actual dividend has not been paid.

Other – Other items of fixed or determinable annual or periodic Puerto Rico-source income that are paid to nonresidents are subject to a 29% withholding tax (20% if paid to a US citizen).

Other taxes on corporations:

Capital duty – No

Payroll tax – Payroll tax consists of social security contributions and unemployment (federal and state) and disability insurance. Puerto Rico employers are subject to the “FICA” and “FUTA” provisions of the US Internal Revenue Code.

Real property tax – The tax rate varies by location, but most municipalities assess a tax of approximately 8.03% to 11.83% of the 1958 market value of real property.

Social security – Social security taxes are comprised of old age/survivor/disability taxes (OASDI) and Medicare/hospitalization insurance, both borne equally by the employer and the employee as a percentage of the employee's wages, with the employer responsible for remitting the tax to the federal government. The combined OASDI rate is 12.4% (i.e. 6.2% each for the employer and the employee) and the combined Medicare rate is 2.9% (i.e. 1.45% each for the employer and the employee). OASDI is levied on the first USD 128,400 of wages for 2018. Medicare is levied on total wages. The portion of social security taxes borne by the employer is tax deductible.

Stamp duty – See under “Transfer tax.”

Transfer tax – The transfer of real property is subject to a stamp tax. The transfer tax to be paid depends on the value of the property transferred.

Other – Personal property tax is imposed on certain personal property located in Puerto Rico (e.g. average

monthly inventory, furniture and fixtures and supplies). The rates range from 5.80% to 9.83%.

A municipal license tax is imposed on the gross receipts of a business. The rate imposed depends on the municipality (generally, the rate is 0.5%).

Anti-avoidance rules:

Transfer pricing – Puerto Rico's transfer pricing regulations are similar to those in the US.

Thin capitalization – While there are no specific thin capitalization rules in Puerto Rico, guidance is provided based on the US rules.

Controlled foreign companies – No

Disclosure requirements – No

Compliance for corporations:

Tax year – Taxpayers may elect to use a fiscal year or the calendar tax year.

Consolidated returns – Consolidated returns are not an option under the tax code. Each entity must file a separate return.

Filing requirements – All resident corporations are required to file a tax return by the 15th day of the fourth month after the close of the previous tax year. Resident partnerships are required to file a tax return by the 15th day of the third month after the close of the previous tax year. Extensions for three months may be requested.

Penalties – Monetary penalties may be imposed at rates up to 25%. Civil and criminal penalties apply in certain cases for failure to comply with the tax law.

Rulings – Private rulings are available from the treasury department for pending transactions. Closing agreements and voluntary disclosure agreements also may be negotiated with the tax authorities.

Personal taxation:

Basis – Residents of Puerto Rico are taxed on their worldwide income, regardless of their citizenship, while nonresidents are subject to tax on their Puerto Rico-source income. Nonresident individuals are taxed on gross income effectively connected with a trade or business in Puerto Rico.

Residence – An individual is resident if he/she is domiciled in Puerto Rico. For tax purposes, there is a presumption that an individual who is present in Puerto Rico for a period of 180 days or more in a calendar (tax) year is a resident. The facts and circumstances are critical in determining residence status.

Filing status – Depending on a taxpayer's civil status and personal circumstances, he/she may file as an

individual taxpayer, a married taxpayer or a married taxpayer filing separately from his/her spouse.

Taxable income – Individuals must include all forms of remuneration, less qualified exclusions, in taxable income. Adjustments may be made for deductions, personal exemptions and credits for dependents.

Capital gains – Capital gains are taxed at a rate of 15%.

Deductions and allowances – Residents of Puerto Rico are entitled to itemize certain allowable deductions.

Rates – Progressive rates are imposed up to 33%. An additional surtax of 5% is imposed on the tax liability if the net taxable income exceeds USD 500,000.

Other taxes on individuals:

Capital duty – No

Stamp duty – The transfer of real property is subject to a stamp tax. The transfer tax to be paid depends on the value of the property transferred.

Capital acquisitions tax – No

Real property tax – The tax rate varies by location, but most municipalities assess a tax of approximately 8.03% to 11.83% of the 1958 market value of the property.

Inheritance/estate tax – No, as from 1 January 2018.

Net wealth/net worth tax – No

Social security – Social security taxes are comprised of old age/survivor/disability taxes (OASDI) and Medicare/hospitalization insurance, both borne equally by the employer and the employee as a percentage of the employee's wages, with the employer responsible for remitting the tax to the federal government. The combined OASDI rate is 12.4% (i.e. 6.2% each for the employer and the employee) and the combined Medicare rate is 2.9% (i.e. 1.45% each for the employer and the employee). OASDI is levied on the first USD 128,400 of wages for 2018. Medicare is levied on total wages. The

portion of social security taxes borne by the employer is tax deductible.

Compliance for individuals:

Tax year – Calendar year

Filing and payment – Taxpayers are required to file their taxes by the 15th day of the month following the close of the previous tax year (15 April for calendar year taxpayers). An extension to file may be requested.

Penalties – Penalties may be imposed at rates of up to 25%. Other civil and criminal penalties also may apply.

Sales and use tax:

Taxable transactions – Puerto Rico levies a sales and use tax on taxable goods and services.

Rates – The standard rate is 11.5%. Services rendered to other merchants (B2B) and designated professional services are taxed at a 4% rate.

Registration – A taxpayer that sells or uses taxable items must register as a merchant with the Puerto Rico Treasury Department.

Filing and payment – Sales and use tax returns must be filed on a monthly basis.

Source of tax law: Internal Revenue Code for a New Puerto Rico (2011), as amended

Tax treaties: Puerto Rico does not have any tax treaties, nor is it a party to any agreement signed by the US.

Tax authorities: Puerto Rico Treasury Department

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