

House Bill 741 sets to 4% the Excise Tax of Act 154-2010 for 2013 through 2017

In our October 2010 Monthly Bulletin of The Tax Advisor we discussed the most important aspects of Act 154-2010 (the "Act"). In general terms, a nonresident foreign entity ("Nonresident entity") not otherwise considered engaged in a trade or business in Puerto Rico, will be considered as such if it has manufacturing or service transactions with an affiliate Puerto Rico manufacturing resident entity ("Resident entity").

The Act imposed a tax depending on the sales level of the Resident entity. If the sales level exceeds \$75 million for any of the three preceding tax years of the Resident entity from purchases by the Nonresident entity, the latter will be subject to an excise tax withholding (such tax must be withheld from the acquisition of tangible personal property manufactured or produced in whole or in part in Puerto Rico and from the services performed in Puerto Rico). Otherwise, if the sales threshold is not met or if no excise tax is due, a four factor test will need to be calculated to determine if some portion of the Nonresident entity's income considered non Puerto Rico source income will be characterized as Puerto Rico source income. The four factor tests are: Sales, purchases, commissions and facilitator tests. For a brief explanation of these tests, please refer to our Monthly Bulletin dated October 2010.

Regarding the excise tax withholding, it phases out over a six-year period as follows:

1. 4.00% for periods commencing after December 31, 2010;
2. 3.75% for periods commencing after December 31, 2011;
3. 2.75% for periods commencing after December 31, 2012;
4. 2.50% for periods commencing after December 31, 2013;
5. 2.25% for periods commencing after December 31, 2014;
6. 1.00% for periods commencing after December 31, 2015 and ending on or before December 31, 2016.

Notwithstanding, House Bill 741 (Senate Bill 351) ("House Bill") proposes to amend the excise tax percentages withholdings and sets it to 4% for periods commencing after June 30, 2013 through periods ending on or before December 31, 2017.

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In addition, the House Bill proposes to amend the payment due date, changing it from the 15th to the 13th day following the month in which the transaction occurs. As it is written, the effective date of the House Bill will be immediately after its approval.

Z&A comments

The Puerto Rico Manufacturers Association, the Pharmaceutical Industry Association and

manufacturers subject to the House Bill have been meeting with the Puerto Rico Treasury Department trying to find ways to reduce its impact. They have been able to postpone the commencement of the 4% excise tax from January 1, 2013, the date established in the original bill, to July 1, 2013. Those efforts continue, and it seems that the House Bill as it stands will be signed into law. We will keep track of the House Bill and inform you of any changes of importance that may occur during the

legislative process. We also encourage you to examine your current situation to determine the effect the House Bill may have in your total taxes. We may assist you in this process and with any negotiation you require with the Puerto Rico Treasury Department or the Puerto Rico Industrial Development Company.

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