

Tax update...

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After six months of uncertainty about the special income tax rate applicable to long-term capital gain transactions, the Governor of Puerto Rico signed on December 10, 2007 Act No. 181 (“Act 181”). In general terms, Act 181 reduces the special tax rate applicable to individuals, estates and trusts from 12.5% to 10%. It is important to mention that this special tax rate also applies to lump sum payments made under a variable annuity contract issued by an eligible insurance company. In the case of the sale of real property or stock by nonresident individuals the applicable rate will be 25%. However, if the individual is a US citizen, the rate will be 10%. The special tax rate on long term capital gains for corporations and partnerships was reduced from 20% to 15%. The special tax rates established by Act 181 will apply to transactions occurred on July 1, 2007 and after.

In addition, the special tax of 10% will apply to distributions made by a qualified trust to any participant or beneficiary only if the plan complies with the following requirements:

1. the trust is organized under the laws of the Commonwealth of Puerto Rico or has a Puerto Rico resident trustee and uses such trustee as payment agent; and
2. ten percent of the total assets of the plan attributable to the participants residents of Puerto Rico has been invested in property located in Puerto Rico during the year of the distribution and for the two years previous to the date of the distribution. However, this requirement will not apply to distributions made between January 30, 2006 and December 31, 2007.

Keep in mind that if the trust does not comply with these requirements the special tax will be 20% instead of 10%.

In addition to Act 181, during the month of December the Governor has signed 4 additional Laws which provide certain income tax benefits to taxpayers. Below you will find a summary of each one.

Act No. 172 of December 3, 2007 increases the maximum amount allowed as deduction for expenses incurred in the purchase, manufacture and installation of any solar equipment from \$750 to \$1,500. In the case of married taxpayers filing a separate return, the maximum deduction was increased from \$375 to \$750. This increase will be applicable for taxable years commenced after December 31, 2006. This Act also establishes that this deduction will be taken into consideration when computing the adjusted gross income for purposes of the alternative minimum tax for individuals. However, in this case, the deduction will be applicable for taxable years commenced after December 31, 2006 and ending not later that December 31, 2008.

Act No. 177 of December 4, 2007 establishes an exemption from the excise tax up to \$5,000 to vehicles acquired by disabled veterans. This exemption also is extended to blind persons or to any person who can not drive a vehicle due to a permanent physical impairment, but uses the services of an authorized chauffer to drive to his/her work place. This Act will be effective immediately after its approval.

Act No. 178 of December 4, 2007 provides a special and temporary deduction of 100% of the contributions made to the “Museo de Arte de Ponce” during the years 2008 and 2009. It is important to note that the contributions should be specified as being made only for purposes of the renovation and expansion of the museum.

Act No. 182 of December 10, 2007 establishes a credit of \$2,000 against the income tax imposed by the Subtitle A of the Puerto Rico Internal Revenue Code of 1994, as amended for the purchase of an automobile powered by alternate or combined energy sources. The Secretary of the Treasury will determine which automobiles will be eligible for purposes of this credit, taking into consideration the list provided by the US Internal Revenue Service. The provisions of this Act will be applicable for years commencing after December 31, 2007.

Should you have any questions or comments regarding the aforesaid, please do not hesitate to contact personnel in our Tax Department at 787-754-1915.

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