



Tax



Business



Transactions

Who needs a Transfer Pricing Study?

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For various years we have been talking about transfer pricing in Puerto Rico. What is transfer pricing? In a simple way we could define it as the price that an entity charges to a related entity for goods and services when they are each in different jurisdictions. Then, why is this subject gaining more importance now than ever? Why do we have to take immediate action?

Because starting with the tax returns for taxable year 2019 some taxpayers will be required to file a transfer pricing study together with their income tax return. A transfer pricing study is an analysis of the transactions among related entities and a comparison of those transactions with the results of similar transactions among unrelated parties to determine if the charges are arm's length.

Taxpayers that require a transfer pricing study are those corporations or partnerships that deduct expenses incurred or pay to related entities that are not engaged in business in Puerto Rico. Also, those entities that receive allocations of expenses from their Parent Company, Home Office or other related entity outside Puerto Rico.

Originally, these types of expenses were deductible up to 49% of the amount incurred and the remaining 51% resulted in a non-deductible tax adjustment. Before 2019, Puerto Rico Treasury allowed the request of a waiver from the application of this provision. Such waiver required the filing of a formal request, an Agreed Upon Procedures Report and a Transfer Pricing Study. This process was long and costly, and also, Puerto Rico Treasury was slow in responding to these requests. For these reasons many taxpayers decided against requesting such waivers.

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When Act 257 was signed on December 2018 it simplified the process by establishing that in order to deduct the total amount of such expenses the taxpayer must file with the income tax return a Transfer Pricing Study including the Puerto Rico operations. This requirement is effective for years beginning after December 31, 2018. It is important to note that operations covered under a tax exemption grant are not subject to this requirement. Puerto Rico law establishes that such study must be performed following the United States transfer pricing rules established in Section 482 of the US Internal Revenue Code and its related regulations. Also, for groups of related entities that do not have any member in the United States the study will be accepted if prepared following the Transfer Pricing Guidelines issued by the Organization for Economic Cooperation and Development (OECD).

The most important matter at this moment is to identify if your business incurs in the type of expenses mentioned above, because it could benefit greatly from the preparation of a Transfer Pricing Study, which takes time and planning.

We will continue with our commitment to keep you up to date with these tax-related developments. Please contact our Tax Department should you require additional information regarding this or any other tax issue. We will be glad to assist you.



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