



Tax



Businesses



Taxpayers

# Tax advantage of preparing a Transfer Pricing Study

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Current tax provisions in Puerto Rico require that intercompany expenses incurred or paid during a taxable year be disallowed at a 51%. However, commencing on tax year 2019 the Puerto Rico Internal Revenue Code of 2011, as amended (“Code”) provides a tax advantage for entities that incur or pay expenses to related entities that are not engaged in trade or business in Puerto Rico. This option allows for such expenses to be fully deductible, provided the entity submits a transfer pricing study report.

## What is a Transfer Pricing Study report?

A transfer pricing study (“TPS”) 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. Its main purpose is to analyze specific transactions of goods, intangible property, or services and compare these with the industry’s standard in what is known as a “benchmark” to determine whether transactions held between related parties are performed at arm’s length.

In addition to this, the TPS report also analyzes the entity’s industry, its competitors, performance throughout the years, and potential risks. It is considered a comprehensive report that dives into the core business functions and compares it to similar operations within the industry. It also provides valuable insight of the company’s performance and, ultimately, dictates whether the transactions between related parties are within an acceptable range or not.

The Code establishes that for income tax purposes only 49% of the following expenses can be deducted:

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- expenses incurred or paid to a related person not engaged in trade or business in Puerto Rico, if such payments are attributable to the conduct of a trade or business in Puerto Rico and are not subject to withholding at source under the Code during the taxable year in which it occurs or
- expenses incurred or paid to a home office located outside of Puerto Rico, by a foreign corporation engaged in trade or business in Puerto Rico through a branch operation.

Taxpayers subject to the limitation explained above, have the option to claim 100% of intercompany expenses if a Transfer Pricing Study is performed following the United States transfer pricing rules established in Section 482 of the US Internal Revenue Code and its regulations thereunder. This TPS must be submitted along with the filing of the income tax return in order for taxpayers to be entitled to claim 100% of the expenses described above.

We are committed to keeping you up to date with all tax-related developments. Please contact our Tax Department should additional information be required regarding this or any other tax issue. We will be glad to assist you.



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