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Puerto Rico will lose federal tax credits that suppo 18% of revenue

BY SOURCEMEDIA | MUNICIPAL | 09/12/19 04:23 PM EDT

By Robert Slavin

Puerto Rico, already restructuring its billions in bond debt, now needs to look for an alternative to a provided 17.6% of its net revenues in fiscal 2019.

U.S. Treasury Secretary Steve Mnuchin told Gov. Wanda Vázquez that the government would take end the tax credit that supports Puerto Rico's Act 154 tax on foreign corporations. Passed in 2010, is a 4% excise tax on the revenues of foreign corporate subsidiaries based in Puerto Rico.

Act 154 revenues go to Puerto Rico's General Fund, which will be used to pay general obligation a other central government bonds, once the current stay on payments is lifted.

While Puerto Rico is part of the U.S., for tax purposes it is considered a foreign land.

In 2011 U.S. Treasury agreed to a tax credit for the Act 154 payments on a temporary basis. The cr since been extended beyond its original sunset. On Tuesday Mnuchin said that the credit would ha phased out, though he didn't specify a deadline.

Observers have worried that the loss of the federal tax credit would lead corporations to remove th operations from Puerto Rico. Many of the "foreign corporations" affected by Act 154 are companies in the U.S.

According to Puerto Rico, 10 corporations and partnerships paid 90% of all Act 154 taxes in fiscal y 2016. The law mainly affects corporations manufacturing pharmaceuticals and other high-tech proc the island.

Attorney John Mudd said that if Puerto Rico tried to continue the Law 154 tax after the federal tax c was withdrawn, the subject companies would probably successfully challenge it in court.

There has been talk of substituting an income tax on the subsidiaries for the excise tax. Mudd said would probably also be legally challenged, but would probably survive any such challenge.

If Puerto Rico were to put an income tax on the subsidiaries, the parent companies would have to p another tax on the income in their federal taxes. However, under current federal tax law it would be deductible.

Under the phase-out plan, the parent companies based in the 50 states with Puerto Rico subsidiar would have increased tax bills. Under the new tax conditions, some may choose to move the subsi operations to other locations.

Vicente Feliciano, president of Advantage Business Consulting, was optimistic. "Puerto Rico needs come up with a reasonable income tax structure that provides these companies with a competitive environment but maintaining the present level of tax revenues. Done carefully and with a transition it should not be a major issue."

The Puerto Rico Oversight Board certified fiscal plan, based on a variety of factors excluding a fed decision to revoke tax credits, projected that Act 154 revenues would decline by 37% from fiscal ye to fiscal year 2024.

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