



Growing
Together



GUIDE

DO'S AND DON'T OF INTELLECTUAL PROPERTY UNDER THE ACT

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PUERTO RICO TAX COMPLIANCE GUIDE

By Torres CPA Group
CifrasPR

Understanding the Puerto Rico tax system and its interrelation with United States is crucial for individuals and entities doing business in Puerto Rico. Puerto Rico is not a state; its's a territory, with its own Business and Payroll laws and regulations.

The following White Pater is designed to give an insight Tax Issues in Puerto Rico. It provides relevant background information, which will be of assistance to organizations considering establishing business in the Island. Nonetheless, it is highly recommended to seek advice and counsel from qualified professional sources before undertaking any business.

Certain exclusions and exemptions may apply and when specific problems occur in practice, it will often be necessary to refer to the laws and regulations of Puerto Rico, and to obtain appropriate accounting and legal advice.

It is understood that the following overview does not constitute any formal rendering of either legal, accounting, tax or professional services. If legal advice or other assistance is required, an attorney, CPA or tax adviser should be consulted.

Torres CPA Group is an Advice Certified Public Accounting Firm offering Audit, Tax, Consulting and Financial Outsourcing services for over 30 years. If you require any further information or help, please do not hesitate to contact us.

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Moving your Intellectual Related Business to Puerto Rico under an Act

Act offers a 4% tax rate on the net income of all services and exported goods provided by a Puerto Rico entity to entities outside of Puerto Rico. Also, income on a Capital gain, dividends and interest on owner-investors' personal transactions could be 100% tax-free under the Act 22 grant. To get more information on these Tax Incentives go to our web page at Tax Incentive, <https://torrescpa.com/pr-tax-incentives/> and White Papers on the subject at, <https://torrescpa.com/white-papers/>.

Act applies to any entity with a bona fide establishment in Puerto Rico that is engaged in the export of eligible and qualified services or goods. Qualified services and goods include but are not limited to, trading of products, investment banking, and other financial services, research and development, advertising and public relations, consulting, electronic programming development, call centers, professional services, and centralized management services.

Exports include qualified services and goods made by a Puerto Rico Act entity for a foreign entity (USA or Worldwide) or non-resident individual that does not relate to business activities within Puerto Rico.

There is a current misconception that USA extraterritorial business consists of evading taxes and hiding money from the government. There are 100% legitimate ways to structure your business in Puerto Rico and obtain significant benefits from asset protection and taxes.

Puerto Rico is a territorial possession of the USA. Under the US Internal Revenue Code, an American who becomes a resident of Puerto Rico begins a new tax rule, all the income the person earns from Puerto Rican sources is subject to Puerto Rican income tax only, not to US income tax. A Puerto Rico corporation is a resident and citizen of Puerto Rico, not a US resident or citizen.

Under the US Internal Revenue Code Section 933 and Section 861, if the person performing the service (whether an individual or a corporation) is a Puerto Rican resident working in Puerto Rico, the income is exempt from US tax.

Section 933 enables the government of Puerto Rico to offer Americans the same benefit that low-tax countries provide to anyone who is not an American on their locally generated income. The passing of Act, which reduces taxes for incoming investors and businesses respectively, is the exercising of that tax opportunity.

Many companies choose to move to Puerto Rico, mainly from the USA. USA taxes on capital gains and ordinary income is notoriously high. Managing your business through a Puerto Rico Act company can provide a variety of benefits, especially a lower 4% tax obligations.

You can do this too, SAVE A LOT IN TAXES

These are things to consider when moving your company to Puerto Rico:

- 1) Prepare a Strategic Business plan. Before doing anything to move your business to Puerto Rico, it is crucial to put together a complete business plan that covers objectives, goals, costs, and structure.
- 2) Any Business plan must take into account the comprehensive logistics in the financial forecast, where it anticipates that your business will be related to profits for at least the first six months, preferably for a larger time lapse of 12, 24 and 36 months.
- 3) Evaluating Critical areas to consider:
 - a) Functions and activities to relocate.
 - b) Validate the source of income, the nature, and location for compliance with Puerto Rico and USA IRS regulations.
 - c) Identify related party transactions that may be subject to IRS rulings on transfer pricing.
 - d) Identify Assets or Intellectual Property to be transferred that could be subject to IRS rulings on Fair Value Transfer.
 - e) Understand parties' ownership, to determine if the Control Foreign Corporation or GILTI minimum tax rulings apply.
- 4) Determine legal and operational structures that support the Tax advantages Strategy.
- 5) Seek specific advice from professionals that understand Puerto Rico and USA ruling and regulations during the planning process. This will enable you to make suitable amends if there are any logistical issues with your business plan or your tax position.

STRATEGIES NOT TO TRY WHEN MOVING TO PUERTO RICO

WHAT PEOPLE THINK

- People think that they can just run the revenues from their operations through a non-USA company formed in a low tax jurisdiction country and get paid through a location somewhere like Hong Kong, so that it results in zero taxes to the USA IRS.
- They also think that since the third party allows any non-USA company to register as a supplier, there is no problem with this strategy.

Wrong:

The issue here is not the non-USA third-party; it is the IRS.

- Perhaps you think that while the money remains abroad, taxes could be avoided indefinitely.

Wrong Again:

If the company is managed and controlled in the USA by a US Citizen or Resident, the IRS may consider that creating an international company for the sole purpose of avoiding US taxes. This strategy would not generate any tax savings and would probably throw you into hot water with an IRS auditor. In fact, your taxes can be significantly higher than if you just did the business through a US entity.

Follow USA IRS rulings, and Save A-lot of TAXES.

WHAT HAPPENS IF YOU DO NOT FOLLOW IRS RULES?

Follow the rules. We do not say this lightly.

The punishment can be severe and will interfere with double (or, in some cases, triple) taxes; in addition, the imposition of fines for delaying the payment of taxes to the IRS.

If your international company is reclassified as a US company, you may encounter the double taxation issue. This means:

- 1) US corporate taxes **plus**.
- 2) Branch Profit Tax (BPT): a flat tax of 30%: Branch income tax is an additional income tax imposed by the IRS on foreign companies that make profits from their business operations in the United States **plus**.
- 3) When paying the dividends, they will be taxable as nonqualified ordinary income, 100% taxable.

And this is so even if your company does not have to be physically present in the USA.

If you do not plan the non-USA structure carefully and appropriately, it would be much better to simply,

Tax-A-Lot.

Following the US IRS Regulations is a Good Pay Less Strategy

RULE OF INTELLECTUAL PROPERTY TRADE OR BUSINESS OF AN ENTITY IN PR WITH AN ENTITY OUTSIDE OF PR

RULE OF INTELLECTUAL OR VIRTUAL RELATED INCOME

Characterizing income as services income, a license of Intellectual assets, or sales of intellectual property is critical, in determining its source, consider the list of factors in distinguishing them from service, sales, lease or Royalty.

Services, Royalty or Lease income, is derived from permitting another person to use property with a share of the profits reserved by the owner, and that could result in royalty, rental, lease income or services Income.

Sales, Services vs. Lease or Royalty perspective

Let say you buy a limousine. The limousine can be sold, rented or provide delivery services.

- **Selling** a limousine that you **purchase** from another party, Income less cost, generates a **trading income**.
- **Selling** a limousine that you **built**, income less cost of production generates a **services income**,
- When **leasing** the limousine, it is merely renting a piece of equipment, operated by the lessee to get to a destination, **rental income**.

- When providing a Limo **delivery service**, delivering the client to a destination, the fare is calculated base on miles and time, and the entity provides personnel, equipment, fuel and maintenance, a **services income**.

Intellectual income would be a source, if services, were it is provided, if a Lease, were property is use, if Trading, were the transfer of title.

Services Income of Intellectual Property

The property used in connection to providing services income is considered to be owned and used by the service provider, not the service recipient. The service provider may use its Intellectual Assets in proving services income but keeping the assets.

Income factors indicating the existence of a services income, not a lease or royalty income include that the service provider (Eligible activity under Act), (Xerox V. IRS- 1981)

- Bears any risk of substantially diminished receipts or significantly increased expenditures if there is nonperformance or under-performance under the contract.
- Use the property concurrently to provide significant services to other entities.
- Provides maintenance service or upgrades the property.

- Has the right to remove and replace.

If the property is developed and or maintained by the PR entity, the source of income would be a PR source.

Sale of Intellectual Property- Trading

Factors indicating the existence of sales of property rather than a services contract include that the:

- Recipient Is in physical possession of the property.
- Recipient Controls the property.
- The recipient has a significant economic or possessory interest in the property.

Sale of Intellectual property will be sourced in Puerto Rico if the seller has a fixed place of business in Puerto Rico and transfers title in Puerto Rico to the Buyer.

Production or Creation of Intellectual Property

If intellectual property is produced for sale by rendering of services in its creation, the service provider typically will not own the newly created assets. In this regard, the rendition of services usually involves the employment of capital and labor for the benefit of another, without the retention by the service provider of ownership rights or interests in reward for the services provided, these would be considered Services Income, an Act activity.

When the buyer is the full owner of all the rights to change, resell, and has total control of use, it is critical the segregating between, service provided, gains on the sale of property, and royalties if any. Services income could qualify under Act, export of services; and Sales of Property could be eligible as Hub Trading activities, or under Act 27 or 73 for the development of products in PR (Microsoft operations in PR).

RULE OF VIRTUAL SERVICES INCOME

Activities such as cloud computing, data warehousing, database access, web-hosting transactions, and the like should be treated as income from services operations rather than from the use of Intellectual property. In all of these activities, the operating company providing the service owns, controls, operates and maintains the equipment on which the data or website is located. The operator gives customers access to the equipment and software, and the operator has the right to remove and replace equipment and software at will. Customers typically will not have possession of, control over, or any interest in, the hardware and software used. Moreover, customers use the equipment and software concurrently with other clients and pay a volume or time-based fee.

Although targeted online services entail the use of Intellectual property (e.g., search and matching algorithms, and valuable end-user data), the proper treatment of this income should be services income. A company that provides online internet service provides valuable sophisticated services that allow reaching a particular audience.

In the seminal case of Xerox, the court determined those copy machines/device were providing service income, not rental income or sales of property income. Xerox had full control over the property, had access and could freely substitute the property. The Court stated that, “In essence, therefore, the customer paid for a result, the number of copies made, and not the use of a machine for some duration. Service was identical to the produced in a darkroom”.

RULE OF DEVICE UTILIZATION

While the site of devices could be one factor, device location alone should not be a determining factor of source income. The device often can be located in different places which are not necessarily the location of the revenue that produces the activity. Device capacity also can be obtained from third parties and can be viewed as a commodity service that arguably does not add a significant amount of relative value. Further, device utilization can be switched from one device to another based on capacity, and possibly involves devices located in different countries.

In the context of a stand-alone computing device, the functional and factual analysis is likely to show that the device is performing only routine functions and relies on other parts of the enterprise to provide the Intellectual assets necessary for the device to perform if not all at least part of those functions. Accordingly, the activities of devices unlikely warrant they can be attributed to a substantial share of the profit.

The source of income can be determined by the location where the income producing activity occurs (i.e., the site of the services required under the contract), the location of the employees that provide the service, or the critical property used in the service. If the company’s whole staff and assets are located in Puerto Rico, it should be easy to conclude that the source of compensation for services should be in Puerto Rico and outside the US.

RULE OF NONHUMAN INTELLIGENT DEVICE VIRTUAL SERVICES

If a server/machine/device is performing primary service functions that replace employees in the business (intelligent nonhuman service), these could be characterized as a device providing nonhuman services; these can glean massive amounts of information instantly, replacing human staffers and cutting costs dramatically.

Some examples of Machines/device performing service include: Self-check in/out, Database, Cloud services, Booking, Document Management, Pay-bills and The Web Go to Meetings. These services could qualify as Act activities if the device is located in PR, since source of income would be where the services is provided.

RULES ON EFFECTIVELY CONECTED TRADE OR BUSINESS IN PUERTO RICO

Income on Trade or Business of a PR entity to an entity outside of PR through an Office or other fixed places of business in PR is considered the PR source. It also includes property for use, consumption or disposition outside of PR.

To consider the income from sources outside Puerto Rico to be treated as effectively connected with a trade or business in Puerto Rico, you must comply with the following:

- a) Have an office or other fixed places of business in Puerto Rico to which the income can be attributed; and that office or area of the company is a material factor in producing the income.

- b) The income is generated in the ordinary course of the trade or business carried on through that office or other fixed places of business.
- c) An office or other fixed places of business is a material factor if it significantly contributes to, and is an essential economic element in, the earning of the income.
- d) No other office or another fixed place of business outside of Puerto Rico has a material factor in the sale of the property for use, consumption, or disposition outside Puerto Rico.

RULES TO ENGAGE IN TRADE OR BUSINESS IN THE US

For a Puerto Rico entity to be engaged in a U.S. trade or Business in the USA, it is required that substantial, regular and continuous business activities be carried on by the Puerto Rico entity in the United States.

The degree of economic activities which will subject a Puerto Rico corporation to U.S. tax is substantially similar to the “permanent establishment” concept considered in many U.S. income tax treaties with foreign countries.

The 2017 updated Model Tax Treaty of the Organization for Economic Cooperation and Development (the “Model Treaty,” “Tax Convention”) provides guidance as to business profits of an enterprise of one country will be taxed only by that country unless the enterprise has a “permanent establishment” in another country.

The definition of “permanent establishment” for purposes of the treaty is a fixed place of business through which the business of an enterprise is wholly or partly carried on.

A “permanent establishment” does not include using facilities or maintaining a stock of goods or merchandise solely for storage, display, delivery, or processing by another enterprise. In particular, shall be deemed not to include:

- a) the use of facilities solely for storage, display or delivery of goods or merchandise belonging to the enterprise;
- b) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for storage, display or delivery;
- c) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for processing by another enterprise;
- d) the maintenance of a fixed place of business only to purchase goods or merchandise or of collecting information, for the enterprise;
- e) the maintenance of a fixed place of business solely to carry on, for the enterprise, any other activity of a preparatory or auxiliary character;
- f) the maintenance of a fixed place of business solely for any combination of activities mentioned in subparagraphs a) to e).

Provided that the overall operation of the fixed place of business resulting from this combination is of a preparatory or auxiliary character, provided that such action or, in the case of subparagraph f), the overall operation of the fixed place of business, is of a preparatory or auxiliary character.

An enterprise shall not be deemed to have a permanent establishment in the USA merely because it carries on business through a broker, general commission agent or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business.

PERMANENT ESTABLISHMENT COURT CASES

In the seminal case of Piedras Negras Broadcasting Co. v. Commissioner, in which 95 percent of their income came from American advertisers, and about 90 percent of the listener came from the US, the court ruled that the situs of the taxpayer's advertising activities be at the site of its broadcasting facilities in Mexico. The court's focus on the site of the broadcasting equipment and labor indicate that these activities should be characterized as services.

The location of broadcaster's audience (mainly in the US) was not a relevant consideration even though advertisers paid for access to that audience. Certain incidental activities were carried in the U.S. by employees crossing the border to collect mail and meet with advertisers to get paid and the solicitation of business in the US by either dependent (an employee) or independent agents, did not change these conclusions since the compensation under the contracts was for the services performed in Mexico.

The place where end users are using the product or services is also inconsequential in determining the entity's source of income.

In another formative case, a taxpayer sold advertising to US advertisers for publication in a magazine to be distributed only outside the United States. For purposes of determining the source of the advertising income, they only considered the sourcing rules for compensation for labor or personal services. They characterized the payments as remuneration for its activities in disseminating their advertisements in the magazine published and distributed outside the United States.

The source of advertising revenue to be received from US advertisers is the capital and labor employed in the publishing and distribution centers outside the United States that will carry out the activities to produce the advertising revenue. In other words, the employed capital and labor for publicity, resulting in income from services is a source from where they are rendered.

In other court cases, the judge stated:

“If an income be tax, the recipient thereof must have a domicile within the jurisdiction or property or activities within the jurisdiction so that the source of income may be said to have a situs in this country.” – Piedras Negras Broadcasting Co v. Commissioner

“Shipping goods into a state is not doing business therein,” Novelty Manufacturing v Connell.

“Nor is a sale by a solicitor, transportation of merchandise into a state, and collecting, therefore,” Brumer v Kansas Moline Plow Co

“Nor distributing a magazine by a foreign corporation”, Systems Co. v Advertiser’s Cyclopedia Co.

“Internal activities of a corporation, such as holding a stockholders’ meeting, do not constitute transacting business. Nor is a collection of debts, nor litigation to so collect, nor the place of signing a contract”, Equitable Credit Co. v Rogers

Regulations 94, article 231-1(b), “Whether a foreign corporation has an office or place of business within the United States depends upon the facts in a particular case. The term office or place of business, however, implies a place for the regular transactions of business and does not include a place where casual or incidental transactions might be, or are affected.”

RULE OF TRADE OR BUSINESS THROUGH OFFICES OR FIXED PLACES OF BUSINESS OUTSIDE PR

Having an Office in USA

A critical point: If the Puerto Rican entity that performs the service maintains an office or agent in the US that is involved in performing the service, the income will be taxable by the US. So, to benefit from Act, your business must avoid doing anything in the US that contributes to producing of the service. If any services are required to be done within US, they should be performed by a US entity.

A fixed site of business maintained by Puerto Rico entity in the United States is a source of income to the US. However, this rule does not apply to sales for use, disposition, or consumption outside the if your office or another fixed place of business outside Puerto Rico **WAS NOT** a material factor in generating the income.

A sales meeting in the US with a customer or potential customer would not drag the service income back into the US, the logic being that selling a service is not an element in performing the service. However fixing things or giving training related to the service from the US probably would make the income taxable in the US. Maintaining a sales office in the US is problematic unless it demonstrably restricts itself to selling only with no management discretion.

Owned Servers

Do not own a physical server in the United States. If you have your own (not third party) website as a sales platform, you should avoid having a physical web server in the US. If you have one, it could be considered a "permanent establishment" according to the US tax code. What makes your company responsible for US taxes.

It will be much better to use the service of the third-party web store, where you can host your website. The third-party web shop represents the most convenient and optimal sales channel that you can use today. The third-party web store does not require you to have your own sales platform or credit card processing solutions, etc. All you need is a bank account.

Collection Gateway Merchants Services

If you require using a US entity to process credit card payments, it may be necessary to establish separate Company, it would be in charge of setting a credit card line and processing account for a company located outside of the US.

The customer's processing payment and depositing in the Bank account of the US entity. The bank of the US entity would transfer from its bank account to the company of Puerto Rico. Note, it is necessary that the US company charge a fee to the Puerto Rican company for performing this credit card processing servicing. It would be preferable that it either be conducted from outside USA or by an independent third party.

In Spermacet Whaling & Shipping Co. v. Commissioner, (1958), a major shareholder of the taxpayer (a foreign corporation for federal income tax purpose) was a U.S. resident who received and dispersed certain funds of the taxpayer in the United States and received bank statements and correspondence addressed to the taxpayer. The Tax Court found that these activities of the taxpayer's agent did not constitute a U.S. business because they were "ministerial or clerical in nature, involving very little exercise of discretion or business judgment necessary to the production of the income in question."

RULE OF ACTING AGENT OR UNRELATED THIRD PARTIES PERFORMING SERVICES

An enterprise shall not be deemed to have a permanent establishment in the US merely because it carries on business in the US through a broker, general commission agent or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business.

However, a person that acts exclusively or almost exclusively on behalf of one or more enterprises to which it is closely related, that person shall not be considered to be an independent agent.

If the party is a material factor in providing the services and has direct contact with the client, this portion could be considered source outside of Puerto Rico, therefore taxable by country of the party. However, if the services are for back-office support services or does not add direct value to the services provided to clients, these would not change the source of income for the services, it would continue to be Puerto Rico source.

Complexities can arise when a PR entity contracts an independent, unrelated party to perform some, or all of the activities needed to provide the service. When an entity hires unrelated entities in different locations outside of Puerto Rico, it should be mindful of situations in which actions of these individual agent attributes as to the PR contractor for purposes of applying the source of income rules.

If a dependent agent conducts activities outside of PR on behalf of the PR contractor, income earned by the PR contractor but generated in part by that agent's actions could be deemed not PR source.

However, if an independent agent unrelated party conducts activities in the US on behalf of the PR contractor, income earned by the PR contractor but generated in part by that agent's actions could be deemed PR source if directly perform and delivered to the PR contractor with no client contact.

If a portion of the activity perform by an independent agent is a material factor in the revenue activities outside of Puerto Rico, that portion could be consider not Puerto Rico source, taxable in the country of the independent agent.

In *Piedras Negras Broadcasting Co. v. The United States*, 1942), a general advertisement was broadcasted to the United States by a foreign entity (a Mexican corporation), and mail responses were obtained from U.S. customers. The foreign entity maintained a mailing address at Eagle Pass,

Texas, and used a hotel room there in which it counted and allocated the funds received in the mails each day. Contracts with advertisers in the United States were handled through an advertising agent, an independent contractor. After analyzing these facts, the Court found no U.S. trade or business by the foreign entity. Using Piedras Negras, as a guideline (in particular, considering that the advertising agent, in that case, was an independent contractor), it could be argued that a foreign taxpayer's activities conducted through an independent contractor does not create a U.S. trade or business.

RULE OF RELATED PARTY CONTRACTS AND TRANSFER PRICING

Businesses should be mindful of how they contract with related parties to provide any activities that are necessary to generate the PR office's profits. The characterization of related party relationships, the corporate form, and the agreements are critical to effective planning of international tax planning, and the sourcing of income in particular.

The fact that a PR company and its US related Company contract with each other for the provision of services should not automatically create a relationship that would affect the source of income.

The Supreme Court has maintained that the corporate entity doctrine serves a useful purpose in business life and that a corporation will remain a separate taxable entity as long as the company carries on a business purpose. However, the Court noted that the corporate form might be disregarded when it is a mere sham or is not a real entity.

The courts have already ruled on services performed by a related company that did not create US source income for the foreign parent company in that the relationship between related companies was essentially no different from that of an independent contractor. In these cases, a foreign corporation was paid by US entities to perform research and development. Since the foreign corporation did not itself perform services in the United States, the court held that there could not be any US source income attributable to the foreign corporation, and that transactions between the related parties were being conducted at arm's length. Even though the U.S. company was a wholly owned subsidiary of the foreign corporation, it was doing business under its name as a separate, distinct entity, and thus the activities of the U.S. entity did not cause the foreign corporation to have U.S. source service income.

Pricing the amount charged in a controlled related party transaction must be determined arm's length. A controlled service transaction is defined as any activity by one member of a group of controlled taxpayers that results in a benefit to one or more other members of the controlled group. Controlled requires more than 50% ownership of a USA citizenship and USA residency.

THE ARM'S LENGTH PRINCIPLE, If two independent companies trade with each other, a market price for the transaction will result. It is known as "arms-length" trading because it is the product of a genuine negotiation in a market. This arm's length price is usually considered to be acceptable for tax purposes. But when two related companies trade with each other, they may wish to artificially distort the price at which the trade is recorded to minimize the overall tax bill. They might, for example, record the profit as much as possible in a tax haven with low or zero taxes.

Market Rate Transfer Price, the simplest and most elegant transfer rate is to use the market price. By doing so, the upstream and downstream revenue of related can sell or provide services either internally or externally and earn the same profit with either option.

Many US investors try to duplicate Big Companies strategy were the US company buy from the PR company, an up-stream revenue. That is for Big company that have a lot of funds for transfer pricing studies. Smaller entity should use the down stream approach, the PR company buys from the USA company, only those that it can not bring to PR. Getting prices from independent companies or entities would be a good base to determine fair value of services or products.

Strategies

Follow a Strategy to further emphasize the transparency of the structure in the eyes of the IRS. That will consolidate the legality of your business in the eyes of the IRS and still **SAVE A LOT OF TAXES.**

Critical things to consider when setting up your Business Strategy is that income from sources outside Puerto Rico will be treated as effectively connected with a trade or business in Puerto Rico. To do so, it must comply with the following:

- Have the intellectual property developed and or maintain done by the PR entity, source of income would be PR source, as results of services provided to develop and maintain it, direct relationship of services provided, qualified under Act.

- Bear any risk of substantially diminished receipts or substantially increased expenditures if there is nonperformance or underperformance under the contract.
- Use the property concurrently to provide significant services to any other entities.
- Provides maintenance service or upgrades the property.
- Retain the right to remove and replace.
- If you are selling intellectual property, where the buyer is the full owner of all right to change, resell, control total use, segregated revenue between any service provided and gain on sale of property, the royalties, if any.
- Services income would qualify under Act export of services and Sales of Property could qualify as Hub Trading activities, or under Act 27 or 73, development of products in PR (Microsoft operations in PR), make sure it is included within the scope of your Puerto Rico Act Grant.
- If have a server/machine/device that is performing primary service functions that replace employees in the business (intelligent nonhuman service), these could be characterized as a device providing nonhuman services, have the device located in Puerto Rico.
- In the context of a stand-alone computing device, the functional and factual analysis ascertain that the device is performing only routine functions and relies on other parts of the enterprise to provide the Intellectual assets necessary for the device to perform if not all at least part of those functions, have the support team in Puerto Rico.

- PR should be the location of the employees that provide the service thru devices, or the critical property used in the service. If the company's whole staff and assets are located in Puerto Rico, it should be easy to conclude that the source of compensation for services should be in Puerto Rico and outside the US.
- Sales of property|Goods is source where the transfer of title takes place, transfer title from the PR entity.
- Sales from PR company to the US resident (Individuals or Entities) or worldwide entity is considered PR income source, not US source, if the transfer of title is done from the PR entity, therefore pay only 4% Tax on net income.
- A corporation can only sell goods services revenue through its employees, hired Puerto Rico residents.
- Use third party websites.
- If you use your own sales platform have the server in Puerto Rico.
- If you store property (Inventory) in USA, use a USA independent warehouse to store and do not transfer title of property to the warehouse.
- Have delivering logistics thought an independent delivering entity.
- Performe all mayor critical functions of procurement, marketing, sales and logistic management in Puerto Rico.
- If you significantly contribute and are an essential economic element in the earning of the income, hire yourself as an employee of the Act entity.

- Have an office or other fixed places of business in Puerto Rico
- The revenue of the Puerto Rico location should be in the ordinary course of the trade or business carried through that office or other fixed places of business.
- The Puerto Rico office or other fixed places of business should be a material factor and it significantly contributes to, and is an essential economic element in, the earning of the income.
- Does not have another office or other fixed places of business in a foreign country or USA that has a material factor in the revenue of the property for use, consumption, or disposition outside of Puerto Rico.
- Relocate critical services to Puerto Rico and leave behind, in a separate US company, any activities that is not practical to move. That would mean billing clients separately for services from the US company and for services from the Puerto Rican company.
- Stay away from the strategy of a partial move, a US company to buy or sell from or to the Puerto Rican company. It takes the entities into the highly technical tax rules for “transfer pricing”. This approach is practical only for a large business.
- Smaller entity should use the down stream approach, the PR company buys from the USA company, only those that it can not bring to PR.
- Getting prices from independent companies or entities would be a good base to determine fair value of services or products between related entities.

- If you need to conduct activities in the US on behalf of the PR entity, use an independent agent or US Corporation, non related party, to conduct activities in the US on behalf of the PR contractor, income earned by the PR contractor but generated in part by that independent agent's or US Corporation from their activities could be deemed PR source if directly performed to the PR entity and delivered to the PR entity with no client contact.
- Effective risk identification and assessment crucial related parties transactions in the early stage of the planning.
- Transfer pricing risk requires assessment to sufficient, relevant, reliable information at an early stage and periodically updated.
- Pricing the amount charged in a controlled related party transaction must be determined as an arm's length transaction.
- Do not have more than 50% ownership of a USA entity.