CARIBBEAN BUSINESS

caribbeanbusinesspr.com | THURSDAY, JANUARY 20, 2011 | WEEKLY $2.00

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Treasury Secretary-designate

Taxes to be cut in half for salaried workers, 30% for businesses

Reform will boost economic growth and increase fairness of tax system

By John Marino

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Tax Reform rewards salaried workers, local businesses

New tax rules aim to boost nonprofits, low-income workers and tax compliance

Treasury Secretary-designate Jesús Méndez

BY JOHN MARINO
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The Tax Reform, expected to be signed into law in the coming days by Gov. Luis Fortuño, is the centerpiece of a host of reforms launched by the administration aimed at reshaping the island's investment landscape and reigniting its slumbering economy.

The largest and most sweeping tax reform implemented in recent memory, it delivers three times the tax relief given to taxpayers in the 1994 reform. Designed to reward hard work and investment, its big winners are salaried workers and local businesses, which officials say have borne more than their fair share of the island's tax burden over the past several decades.

Moreover, officials say such "unprecedented relief" has long been promised to both individual and corporate taxpayers, at least since the enactment of the sales & use tax (IVU by its Spanish acronym) in November 2006, but those promises remain unfulfilled, even as island residents and businesses have been increasingly squeezed in recent years by rising utility costs, tolls and other fees, just as the years-long island recession and depression were eroding island wealth and earning power.

"The days of the government looking to take more money from you are over," Fortuño said when he announced the reform in a special joint session of the Legislature last year. "The time has come for the government to put more money in your pockets.

"Today, we responsibly comply with the pledge we made to all Puerto Rican workers: the most sweeping, equitable and just tax reform ever adopted in Puerto Rico. This reform is based on our commitment to bring relief to Puerto Ricans through lower tax rates combined with better control of government spending that will be the formula for our economic development."

While the reform is expected to undergo some changes in the Legislature, where it is still under consideration (proposals to increase the withholding on professional-service payments were among those under review), the major outline of the administration plan is expected to be passed intact. Approval by the House and Senate was expected as early as next week, which would clear the way for Fortuño to sign the measure into law. Lawmakers, however, said "technical" amendments could be made subsequent to its passage.

The tax relief will average a 50% cut for individual taxpayers and a 30% cut for businesses in Puerto Rico. It adds up to an average annual $1.2 billion for individual taxpayers over the next six years. That translates into $1,500 in yearly average savings for the average taxpayer. Corporate tax relief, meanwhile, will average $260 million annually over the next six years.

The new tax package will also incentivize charitable giving, simplify the tax code and contain new tools for fighting tax evasion, which dovetail with larger administration efforts to improve efficiency in government and work in greater partnership with the private sector to move the island economy forward and improve the quality of life here.

It also offers elderly retirees on a fixed income a tax credit to help

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them cope with the rising prices of basic necessities.

While the reform offers no immediate benefit to the unemployed, it provides work incentives for the poor and lower middle class through an expansion of the earned-income tax credit (EITC), which proponents say will begin to address the island's dismally low worker-participation rate by encouraging more workers to enter the formal workforce.

And while the reform won't help cash-strapped businesses struggling to remain afloat during the current five-year economic downturn, government planners insist that it will establish the basis for a return to economic growth, especially in conjunction with its other efforts over the past two years.

"There is not a single solution to our economic situation, but tax reform is a huge step in the right direction," Treasury Secretary-designate Jesús Méndez told CARIBBEAN BUSINESS in an exclusive interview. "This is the most aggressive reform ever undertaken and its benefits are very broad. The reform is pro-growth because it not only provides immediate relief, but is also designed to foster economic development. It rewards hard work and capital investment."

Méndez, the former Public Buildings Authority executive director and Government Development Bank (GDB) vice president who was tapped last month to be Treasury secretary, pledged to make implementation of the reform and increased tax-compliance priorities.

The administration dealt with the fiscal crisis in its first year in office, including saving the island's credit rating, and set the stage for a return to economic growth by cutting costs in all government agencies in its second year. In 2011, the administration's third year, economic recuperation is expected to start to take hold, Méndez said. Tax reform, with relief already flowing into the economy, will provide another big economic push.

The substantially reduced rates under tax reform are effective in 2011, which means taxpayers will begin to feel the relief with taxes due April 15, 2012. The rates will be phased in through 2016, with taxpayers experiencing additional cuts every year. Additionally, tax relief for the 2010 tax year, for which the filing date is this April 15, has been granted through tax credits ranging from 7% to 15% for individuals, and 7% for businesses that pay Christmas bonuses to workers.

Government Development Bank Chairman of the Board & President Carlos M. García

Government officials are hopeful they can achieve 3% growth by 2014, when the second part of the reform is slated to kick in, if government revenue, spending and economic-growth targets are met.

Economic Development & Commerce Secretary José Ramón Pérez-Riera added that the administration's record over the past two years on taking action to spur economic development, private-sector growth and job creation is "unquestionable."

"Fiscal discipline toward a balanced budget, a restored and improved credit rating, permitting reform, energy reform, government reform, the public-private-partnership [PPP] initiative and, now, a sweeping tax reform to cut taxes on individuals by half and taxes on companies by 30% are all part of what we are doing precisely to be more competitive at attracting outside investment, as well as encouraging local private-sector growth," he added.

Financing the reform

The reform will initially be financed through Law 154, which levies a controversial, six-year excise tax on the offshore affiliates of island manufacturing operations, as well as through continuing efforts to clamp down on public spending and increase efficiency in tax collection. The manufacturing operations have tax-exemption decrees that cover most of their island-based profits.

The excise tax is levied on the offshore purchases of locally produced goods and services between affiliated companies when such transactions surpass $75 million annually and certain other conditions are met.

Law 154 took effect this month, with the excise tax set at 4%. It will be cut to 3.75% in 2012, 2.75% in 2013, 2.5% in 2014, 2.25% in 2015 and 1% in 2016, the final year the tax will apply. The Fortuño administration estimates the excise tax this year will bring in from $1.4 billion to $2 billion, with the amount declining over the life of the tax to $360 million in 2016. Economist Ramón Cao told lawmakers the new tax would likely bring in $1.9 billion in its first year of implementation.

In addition to the excise tax, under amendments to the tax code's Source Rule, the Puerto Rico government also has the ability to permanently levy the normal 39% corporate income tax on offshore affiliates' portion of their income determined to stem from Puerto Rico.

That means those firms with sales below $75 million will be exposed to the corporate income tax under the new regulation, which will also apply to the larger firms once the excise tax expires, tax experts said.

Government officials, however, insist that the temporary excise tax is the "main means of revenue collection" being considered by the administration and that the amended Source Rule is really aimed at targeting the offshore affiliate for the new excise tax, which is a tax paid "in lieu of an income tax."

Manufacturing and business groups have railed against the plan, saying it would inflict particular damage on the island's pharmaceutical and life-sciences manufacturing sectors, which despite years of downsizing, still comprise Puerto Rico's most productive and profitable economic sectors. They have also criticized the way the tax was imposed, having been passed by the Legislature in a secretive weekend session without debate, saying it would hurt the island's credibility in the international investment community.

Other critics say the behavior of the offshore affiliates is far from certain (the first excise tax payments are due Feb. 15), which means that government revenue expectations may not hit their targets under the tax. Some concerns will simply flee, opponents worry.

The administration believes, however, that the plan "strikes a good balance between what is necessary to meet our goals while providing the flexibility with which to work with the companies to reduce any undue burden imposed on them," Pérez-Riera said.

The governor has been personally meeting with the heads of affected manufacturing operations to lessen the impact of the six-year tax, and to offer other assistance for firms that want to expand on the island. Also, he has been making the case that the tax is necessary for Puerto Rico to remain a viable investment destination for offshore investors.

Méndez also emphasized that the six-year tax is temporary in nature and that for most firms, the effect of the tax will be ameliorated by the ability to take a federal tax credit against it (a request by the commonwealth government for a U.S. Treasury Department ruling on the matter is still pending.)

"These entities have a significant investment in Puerto Rico," Méndez said. "They rely on our infrastructure, our human resources and a strong local economy. They understand the economic situation here in Puerto Rico, in the States and in other countries like Spain and Ireland. They realize it is in their best interest to do business in a healthy economy. These are very intelligent investors who understand what we are trying to do."

Benchmarking reform

GDB President Carlos García said the tax relief will be financed not only by the Law 154 tax, but also through increased tax collection, greater fiscal discipline and increased economic development.

García said the administration's "unprecedented" fiscal austerity measures implemented over the past two years have cut the budget deficit it inherited nearly in half, and that

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most of the painful measures, like temporary tax increases and public-employee layoffs, were now in the rear-view mirror. The progress achieved would "guarantee" the tax relief pledged in the proposed reform through 2013.

Méndez, meanwhile, said Treasury revenue has been meeting estimates this current fiscal year.

In 2014, three litmus tests will need to be met in order for the additional cuts contemplated in the reform to be put into effect. These will corroborate whether public fiscal discipline is being maintained, government earnings are meeting targets and expected economic development is being realized under the reform.

"This is the responsible way to assure that the relief being granted won't burden public finances and will help growth," García said. "The reform is based on two important things. Fiscal discipline is balanced with the establishment of the basis for sustainable economic development."

Méndez stressed that corrective measures, should they be required, are an integral part of the administration's approach to tax reform.

"We are not doing this blindly," he said. "We want to make sure that if the reform is not contributing to growth, we can make adjustments."

The impact on economic development

Economists are nearly unanimous in their conviction that the reform is a step in the right direction and will help the island economy over the long run, and they hail the reform's wide reach and its effort to simplify and streamline the tax code.

They also have hailed its support of the nonprofit sector, added tax-compliance tools and its overarching emphasis on implementing a more equitable system.

However, they are less in agreement over the short-term economic impact of the reform, which is taking on increasing importance since the $6.5 billion in American Recovery & Reinvestment Act (ARRA) funds Puerto Rico receives is running out this year and the PPP program, which envisions attracting billions in private investment, is just now getting off the ground.

Méndez argued that because the tax relief is immediate for both individuals and businesses, there will be more money available for investment and hiring employees, which should offer two means of job creation.

Puerto Rico Certified Public Accountants (CPAs) College President Rubén Rodríguez said the average citizen under the reform "comes out better" than under the current tax system, and his major recommendation to lawmakers was to retain the current retention rate at 7% for professional-service payments, instead of increasing it to 10%.

"At this time, when we are passing through a grave and difficult economic situation, it is advisable not to affect the cash flow of taxpayers and businesses that provide services in Puerto Rico," he said.

Lawmakers were set to abide by that recommendation, and administration officials have signaled that the withholding measure could remain as is without affecting estimates.

Yet some economists said the biggest benefit being conceded under reform, a 50% cut in individual tax rates, would have only a limited impact on economic growth. That is because such a cut would essentially stimulate consumption, which would have only a minor impact on the island economy since 90% of what is consumed here is imported, versus 16% in the United States, said Sergio Marxuach, the public-policy director at the Center for the New Economy (CNE).

Cao said any revenue above $1.4 billion should be plowed into strategic infrastructure projects because "we have serious infrastructure problems on the island coupled with serious financial limitations among the public corporations charged with attending to them.

"Such projects are a far more effective tool than tax incentives to stimulate economic activity and private investment," the economist said.

The administration has proposed using the first $100 million of any surplus to create a 10-year fund to be used in the future.

The CNE's Marxuach, meanwhile, said the Law 154 revenue would be put to better use funding public infrastructure than providing tax relief that would only spark consumption of imported goods.

"Investment in public works

Economic Development & Commerce Secretary José R. Pérez-Riera

generates a significant amount of employment in the shorter term and produces public benefits like schools, hospitals and highways that have a useful life for several decades," Marxuach said.

Méndez and other administration officials said the reform was "pro-growth" and would spark economic growth on both a long-term and short-term basis through the "unprecedented" cut in corporate and individual tax rates. Administration officials say that by combining tax reform with other measures, such as the energy and permits reforms and the PPP program, they hope to hit 3% growth by 2014.

In fact, in announcing the reform, Gov. Fortuño called high tax rates on businesses in Puerto Rico "one of the biggest obstacles to our economic development."

"As we are doing with our workers, it is now time that we reward, rather than punish, the successful businessperson who works hard, creating jobs and developing their business," the governor said.

Currently, corporate taxes run as high as 39%, and with surtaxes, the highest marginal tax rate faced by corporations is a whopping 41%. Under the reform, corporate tax rates will be capped at 30% for concerns earning above $2.5 million, while entities earning from $750,000 to $2.5 million will pay 25% and firms with earnings below $750,000 will be taxed at a 20% rate.

After the reform, the average effective corporate tax rate in Puerto Rico will be 26%, which puts the island in a more competitive position, moving it up to 14th place from 29th in a World Bank ranking of global tax rates.

Along with bringing down tax rates substantially, the reform also simplifies the tax code, reducing to three from five the different taxpayer classifications and eliminating all deductions, except for mortgage interest, charitable donations, medical costs, student-loan interest and contributions to retirement or education funds. Business-related deductions and tax credits are also being streamlined under the effort.

An expansion of the EITC should spark more low-wage workers to enter the formal economy, now that workers earning up to $20,000 annually won't pay taxes, and a new tax credit for the elderly with annual earnings of $15,000 should also have a stimulative effect, the new Treasury chief said.

"The reform rewards hard work by basically doubling the EITC, and it incentivizes capital investment by substantially reducing corporate tax rates," Méndez said.

Putting more teeth into compliance

While the reformed tax system will be much more equitable than the current system, Treasury is making enforcement of the island's tax code a top priority, Méndez said.

"There can be no equitable tax system unless everyone participates," he said.

Méndez believes a fairer tax system will spur compliance among individuals currently not participating in the system, and might encourage some not paying all they should to pay their fair share.

The reform, however, also contains specific enforcement mechanisms, such as limiting mortgage deductions to 30% of income, which government planners believe will cut down on abuse of this tax break without undercutting its goal of promoting home ownership. The Treasury Department estimates it could reap an additional $30 million annually through the new cap.

Also, under recently passed legislation, financial institutions approving mortgage and other loans in excess

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of $250,000 are now required to share information with the Treasury Department. Tax laws have also been toughened so that employees in private companies that make withholdings but don't remit them to Treasury will now face criminal penalties and be hit with felony charges. This applies to both employee-payroll and IVU withholdings.

Treasury officials also believe that low-wage workers are particularly susceptible to employers who withhold taxes from them but don't remit that withholding to Treasury. The loss is often compounded because the agency has to pay rebate checks to taxpayers on withholdings that were never delivered to Treasury.

Under reform, since those earning $20,000 or less won't have to pay taxes, withholdings will no longer be required. This effort is expected to save the government $40 million annually.

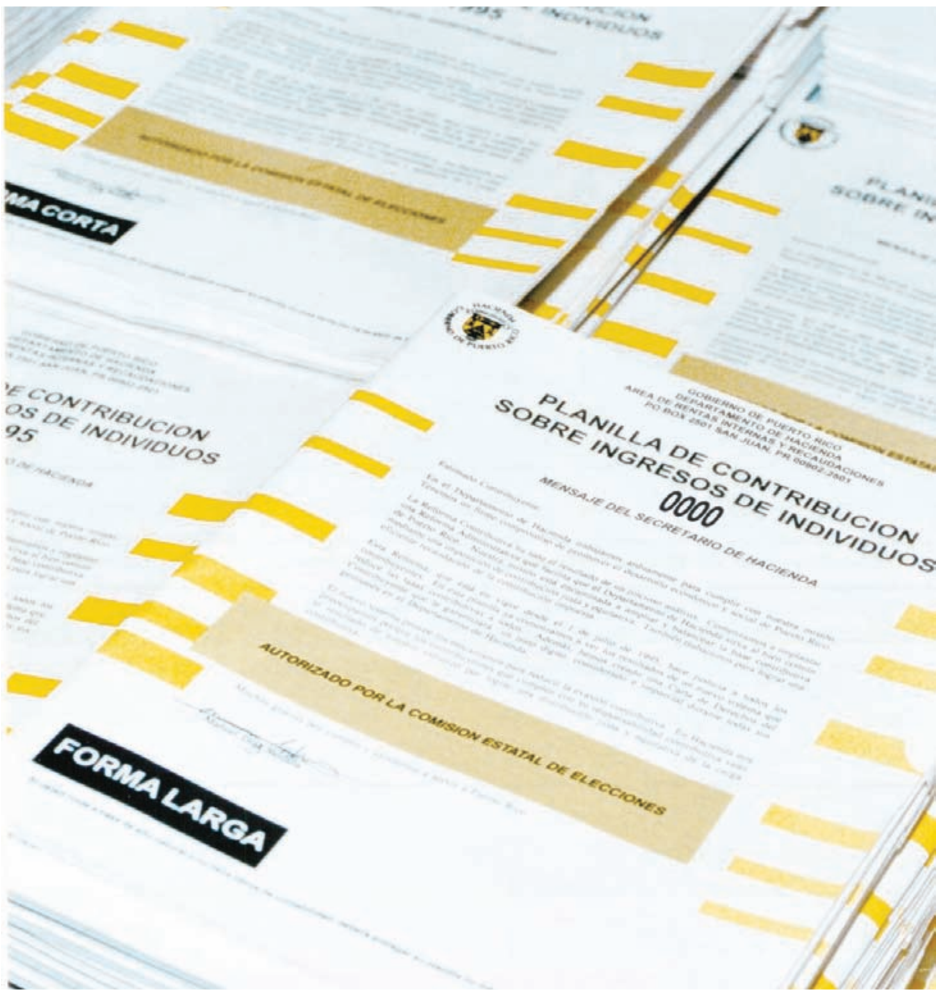
A new 1% tax on purchases from affiliates for island businesses with sales in excess of $50 million annually is aimed at attacking the "transfer pricing" strategies of mega-retailers and other multinationals operating on the island, in which they hold down their local tax burden by paying inflated prices to related companies for articles they sell on the island.

Raw materials and other articles used in local manufacturing processes are excluded, and the tax shouldn't be a burden to most businesses because the amount paid can be taken as a credit against taxes the island businesses would owe Treasury. It would impact operations not reporting a profit, however, government officials said.

However, administration officials acknowledge that the reform must be accompanied by other aggressive steps to clamp down on tax evasion, as well as continued controls on public spending, if it is to succeed.

A priority, Méndez said, was to increase collections on the IVU, where evasion is rampant. Treasury only has a 52% capture rate on the IVU, according to a recent study by the Puerto Rico Society of CPAs. That means nearly half of all businesses on the island fail to pay the tax to the Treasury Department. Another study by economist Gustavo Vélez pegged annual IVU evasion at $800 million.

Gov. Luis Fortuño and Tax Reform Commission Executive Director Xenia Vélez



Méndez and the administration is betting on the "IVU-Loto" to boost compliance with the IVU and bring in $100 million in its first year of operation, a figure that should increase to $400 million in additional annual revenue by 2013.

Treasury will sponsor a free lottery through drawings, probably twice a week, based on numbers printed on purchase receipts. The idea is to get shoppers to ask for receipts with the hope of playing the free lottery, which will ensure the merchant is both charging the IVU tax and remitting it to Treasury. If a merchant declines to provide a receipt, there will be a process for reporting the merchant to the Treasury Department.

The system also will work by giving Treasury real-time information about businesses and their sales, which can help the government ward off tax evasion, and will also boost collection efficiency.

Officials said arrangements are being made so that even businesses like street vendors, which operate largely in cash, will be able to participate. The plan shouldn't cost merchants any money, since they will be provided with point-of-sale machines provided by Treasury. In fact, it is expected to drive business to their stores.

The island has 55,000 businesses that accept electronic payments, while 30,000 operate by cash only, according to the Treasury Department. Yet only 52,000 businesses are sending the IVU to the agency.

An IVU-Loto pilot project involving 200 businesses has begun in Ponce, and the process of analyzing the data from it is currently underway, Méndez said. The government aims to implement the IVU-Loto islandwide by April.

The pilot program started out with a weekly prize every Tuesday of $1,000. When the full program is rolled out by next April, there will be drawings every Tuesday and Saturday and 16 winners weekly, with two $1,000 prizes, four $500 prizes and 10 $100 prizes. Treasury officials have said they are spending $10 million to get the program off the ground. Méndez said he was mulling possibly increasing prizes, which total a mere $260,000 annually. If the public is really to get involved, there should be a greater investment and robust marketing efforts, proponents of a substantial increase say.

ENHANCING THE THIRD SECTOR

The Tax Reform also bolsters the so-called "third sector" by incentivizing charitable giving to nonprofits and charities through greater tax-exemption benefits. This dovetails with administration plans to work more closely with this sector, turning to nonprofits to deliver essential services in areas ranging from special education to healthcare, because of their expertise and ability to deliver services more effectively and efficiently than the government.

Current law offers taxpayers two options: 100% of the amount above 3% of adjusted gross income or 33% of all donations. In either case, the deduction can't exceed 15% of the adjusted gross income. The first option is too far beyond the reach of

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most middle-income taxpayers to be beneficial.

The Tax Reform will change the rules to allow for a total deduction from taxes of charitable giving, up to 50% of adjusted gross income. A recent Urban Institute (UI) study found that of the various alternatives it studied, this was the most effective change to make. Charitable donations would increase by over 32%. Using 2007 figures, donations would increase by $13.4 million to $116.8 million from $103.4 million at a cost to the government of $12.1 million.

The government is looking to nonprofits to outsource some professional services because they often have the expertise to handle more effectively certain tasks, and also can deliver services up to six times more efficiently than government.

In 2007, 23,000 tax returns, less than 7% of all returns filed with detailed deductions, listed charitable deductions, according to the UI study, which was sponsored by Fundación Flamboyán, Jaime Martí and Kinesis. Donations, which totaled $103.4 million, averaged $4,517 and fluctuated from an average $2,000 among donors with the lowest incomes, to an average $12,788 among earners of the highest wages. The donations averaged 6.1% of a taxpayer's adjusted gross income, according to the UI study.

"The increase in the deduction to nonprofits is positive and should have a significant impact on donations to charity organizations in Puerto Rico," CNE's Marxuach said.

Secretary of State Kenneth McClintock, the administration's point man on government reform, told CARIBBEAN BUSINESS that such partnerships with nonprofits were already being carried out by the administration as a way of trimming costs and improving services.

"We are entering into agreements with organizations that can deliver services more effectively and efficiently in certain areas," McClintock said.

McClintock authored legislation to bolster charitable-giving back in 2000 that he said charitable organizations failed to capitalize on. While the legislation boosted charitable giving to a 33% write-off up to a certain limit, the nonprofit sector

Assistant Treasury Secretary for Economic & Financial Affairs Edwin Ríos Rivera

failed to market the change to potential donors.

"That was a major change in tax law to benefit charitable contributions and they did not take advantage of it," he said.

The reform will require nonprofits to meet the federal requisites for being a nonprofit, which should strengthen their operations and enhance their fund-raising ability, McClintock said.

Under the legislation, island nonprofits would need to comply with the requirements of section 501(c)(3) of the U.S. Internal Revenue Code, which requires the filing of annual audited financial statements and a tax return. Most U.S. and international foundations only donate to 501(c)(3) institutions, so complying with federal requirements would open up a new set of potential donors for local nonprofits. It would also open the door to direct federal funding.

"In addition to incentivizing charitable giving, this will help formalize the sector, which is also positive," McClintock said. "However, the organizations have to market these new benefits."

A progressive tax

Administration officials say the reform is also a response to different local sectors that have been clamoring for a more balanced distribution of the tax burden and a larger contribution from the industrial sector. They point to four bills, authored by legislators from both the majority and minority delegations last year and discussed at public hearings, seeking to impose a much larger contribution on the corporate sector.

Meanwhile, the move to simplify and expand the tax base, while spreading the relief across nearly all sectors, complies with key criteria that any reform proposal should meet, several economists said. These include being comprehensive, expanding the tax base and promoting economic development.

Former Treasury Secretary Xenia Vélez, who headed the Tax Reform Committee appointed by the governor to draft a tax-reform proposal, said the reform gives relief "to everyone."

"The proposed relief will first and most dramatically impact the people who earn the least, or those earning under $40,000 annually," Vélez said.

The head of the executive committee, which was also charged with developing the unique mechanism to fund the roughly billion-dollar annual cost of the reform, also stressed that the reform would retain existing benefits to heads of households and retirees, which would also have a progressive effect on the budgets of some of society's most vulnerable members.

The reform will also shield businesses, from hotels to manufacturers, from the loss of their special incentives even as it moves to redistribute the corporate tax burden.

"The breadth of the Tax Reform is really incredible," Méndez said. "The Tax Reform is the spearhead of the economic reconstruction, with unprecedented tax relief." ■

Taxpayers wait on line at the Treasury Department.

Key highlights of Tax Reform

Tax relief will average $1.2 billion annually for taxpayers and $262 million annually for businesses over the next six years

These new reduced rates will be phased in over the six-year period:

- 0% tax rate for those who earn less than $20,000 annually
- 7% rate for those who earn from $20,000 to $30,000
- 14% rate for those who earn from $30,000 to $70,000
- 25% rate for those who earn from $70,000 to $125,000
- 30% rate for those who earn over $125,000 the maximum tax rate for businesses will be cut to 30% from 39%. Firms earning from $750,000 to $2.5 million in profits will pay at a 25% rate and firms with profits below $750,000 will pay at 20%.

The new code allows the following six general deductions from gross income:

- Mortgage interest, limited to 30% of the sum of the adjusted gross income
- Charitable donations, limited to 50% of the adjusted gross income
- Health and orthopedic-equipment expenses that are not covered by a healthcare plan and exceed 10% of the taxpayer's adjusted gross income
- Student-loan interest
- Contributions to the government retirement system
- Contributions to individual-retirement accounts (limited to $5,000 in the case of individuals and $10,000 in the case of married couples filing joint tax returns), for education-contribution accounts (limited to $500) and for health-savings accounts.

The new code repeals at least six existing deductions from gross income:

- The deduction up to $1,500 for ordinary and necessary expenses
- The deduction up to $1,200 for automobile-loan interest
- The $1,000 fixed deduction for taxpayers 16 to 25 years of age who are employed
- The 100% deduction for contributions to the Endowment Fund of the University of Puerto Rico
- The $3,000 fixed deduction for spouses who both work and file tax returns jointly
- The $500 deduction for expenses incurred in the acquisition and installation of a personal computer.

The Earned Income Tax Credit, which encourages low-wage earners to continue working through preferential tax treatment, is doubled to $600 and the income cap for eligibility is now $35,000 rather than $20,000.

The reform grants a $400 tax credit for people 65 and older with income under $15,000 annually.

Local properties remain exempt from the estate tax, and so do the holdings of taxpayers who die in good standing with the island Treasury Department. The rates, which range from 10% to 50%, have also been reduced.

The new code repeals Law 7's 5% additional special tax on individuals whose gross income exceeds $100,000 ($150,000 for married couples) and ends its special property surtax on June 30.

The reform repeals in 2016 the gradual tax adjustment that is applied to earning more than $75,000 a year. Until its repeal, the level at which it is applied is increased to $100,001 in 2011, $200,001 in 2012, $300,001 in 2013 and $500,001 in 2015.

The new code increases the personal exemption for individual taxpayers from $3,000 to $3,500, but then reduces it to $2,750 in 2012, $2,000 in 2013, $1,250 in 2014 and $750 in 2015. Married taxpayers filing their tax returns jointly will qualify for a personal exemption double the amount available for individual taxpayers. The personal exemption will be completely eliminated in 2016.

The exemption for dependents remains at $2,500 for each dependent, and divorced parents who have joint custody of a child can split the exemption for dependents between them. ■

Jesús F. Méndez Rodríguez is Puerto Rico's new tax man

Entrepreneur, businessman, investment banker and government official to head Hacienda

BY CARLOS MÁRQUEZ
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Jesús F. Méndez Rodríguez was appointed Treasury secretary by Gov. Luis G. Fortuño Jan. 7, and became Puerto Rico's new tax man.

Méndez's appointment requires Senate confirmation. Senate President Thomas Rivera Schatz said Méndez would get the approval of the upper chamber and CARIBBEAN BUSINESS sources at the Legislature confirmed he has the votes.

Prior to his appointment as Treasury secretary, Méndez wore two hats, as executive vice president of administration at the Government Development Bank (GDB) and as executive director of the Public Buildings Authority (PBA).

Before being recruited by the Fortuño administration for public service, he had a long and outstanding professional career in the private sector. Méndez has been an entrepreneur, businessman, investment banker and public accountant.

The Treasury secretary-designate provided a telephone interview to CARIBBEAN BUSINESS Jan. 8, just hours after his appointment. On Jan. 9, he was again available for questions and clarifications (CB Jan. 13).

At the request of CARIBBEAN BUSINESS for a more in-depth interview Jan. 13 or 14 regarding the upcoming Tax Reform, he replied: "Let's do it on Friday [Jan. 14], please. Give me one more day to prepare." Méndez had been at the Treasury Department less than a week and was still in transition from his two prior jobs, but one day was more than enough for Méndez, who was fully prepared for the interview.

The Tax Reform is expected to be approved this week.

The next Treasury secretary arrived five minutes late to the scheduled interview after calling to apologize for the delay. He was in a board

Treasury Secretary-designate Jesús Méndez Rodríguez

meeting with the Health Insurance Administration. The Treasury secretary belongs to at least 20 government boards.

Méndez arrived at CARIBBEAN BUSINESS without the typical entourage that customarily accompanies many of Puerto Rico's high government officials, although this practice has changed during the Fortuño administration, at least in the economic development and fiscal agencies with which CARIBBEAN BUSINESS interacts.

He arrived driving his personal car, no chauffeurs, no security, no press aide, and well-prepared for an in-depth interview on the Tax Reform and other Treasury Department matters. (See main bar)

Méndez had been the executive director of the PBA since January 2009, when he was also appointed executive vice president at the GDB in charge of administration, operations & controllership.

The PBA was created in 1958 to design and construct government-office buildings, courthouses, schools, and health, police and correctional facilities for lease to the different government agencies. It owns and manages more than 600 government properties and provides maintenance for approximately 400 of the 1,500 public schools islandwide.

From 2005 to 2008, Méndez was president & CEO of a closely held corporation dedicated to the administration of assisted-living facilities, of which he holds one-third ownership participation.

From 1996 to 2004, he held several senior-management positions within Banco Santander SA subsidiaries in Puerto Rico, including president of Santander Asset Management, first senior vice president & trust officer of Banco Santander de Puerto Rico, and managing director of Santander Securities Corp.

While at Santander, Méndez collaborated with the former GDB president during the Popular Democratic Party's Rafael Hernández Colón administration, former Santander President José Ramón González (now senior vice president at Oriental Bank), and current GDB Chairman & President Carlos M. García, who was also president of Santander until January 2009.

"I have had the privilege of working with Jesús for a long time during my professional career [at Santander and the GDB]. He always makes a difference in everything he gets involved with. Wherever he steps, he will leave his footprints. I'm sure he will be successful in his new endeavors and will leave an important legacy as Treasury secretary on behalf of the people of Puerto Rico," García told CARIBBEAN BUSINESS.

"Jesús has a special sensibility that allows him to immediately earn the respect and appreciation of his fellow workers and others with whom he interacts. He is a hard worker, a dedicated professional and an outstanding public official," García added.

"He is characterized for listening with patience and acting firmly. The combination of these qualities makes him an effective professional who delivers results supported by his work team," the chairman & GDB president said.

"I have known Jesús for more than 25 years. He is an accomplished private-sector professional with outstanding management skills, aside from being a certified public accountant. However, most importantly, his personal and professional integrity is unquestionable. His designation as Treasury secretary was an asserted decision by Gov. Fortuño," González told CARIBBEAN BUSINESS.

Prior to joining Santander, Méndez served as chief financial officer & managing director of BP Capital Markets. He worked as vice president at Credit Suisse First Boston Puerto Rico Inc. and was a senior auditor at Deloitte & Touche. He also held the position of assistant bank examiner at the Federal Deposit Insurance Corp. in New York.

Méndez has a bachelor's degree in business administration from University of Puerto Rico and is a certified public accountant.

He is married to Beba García, a professional and published writer. They have two daughters, Cristina María, 28, and Alina María, 24. Cristina María, a law-school graduate, is studying for her bar exam. She is married to Eric Levins and they have a son named Daniel. Alina María is a mechanical engineer and lives in Wisconsin. ■

Vote on new Internal Revenue Code postponed

Silva: Governor wants to sign new code into law Jan. 31

BY MARIO SANTANA
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The vote on Puerto Rico's new 1,653-page internal revenue code, originally slated for today and tomorrow, has been postponed until next week, House Treasury Committee Chairman and Executive Director, Antonio "Toñito" Silva and Raúl Candelario, respectively, told CARIBBEAN BUSINESS.

Last week, Silva announced that the House would pass the new code, the centerpiece of Gov. Luis Fortuño's tax reform, today, and that the Senate would follow suit tomorrow. The plan changed over the weekend, however.

At press time Monday, Silva and Candelario explained that the vote on the new code was postponed until next week because the governor and his economic team are spending this week on a trade mission in Spain.

One of the amendments would keep tax withholdings from professional service fees at the current 7% rate, but allow those who provide professional services to choose higher withholdings. The new code proposes to increase those withholdings to a 10% rate.

House Treasury Committee Executive Director Raúl Candelario

House Treasury Committee Chairman Antonio Silva

Candelario said all proposed amendments to the new code have been discussed with the governor's economic team. The Government Development Bank (GDB) evaluates some amendments through econometric models, using data provided by the Treasury Department, he explained.

Silva, however, said that the House ethics probe against Popular Democratic Party Rep. Luis Farinacci was yet another reason the code's vote was delayed.

Although Silva did not specify a day for the House vote, he said Fortuño wants to sign the new code into law on Jan. 31.

Several amendments will be introduced to the new code before it is enacted, but Candelario clarified that "most of them are of a technical nature and aim at clarifying the legislative intention." The amendments were discussed Saturday during a five-hour meeting headed by Fortuño, Silva said, adding that the meeting took place at GDB headquarters and included the participation of the legislative presidents and the heads of several agencies, among others.

One of the amendments would keep tax withholdings from professional service fees at the current 7% rate, but allow those who provide professional services to choose higher withholdings, Silva said. The new code proposes to increase those withholdings to a 10% rate. Another amendment is aimed at maintaining the current level of tax deductions for local companies that engage in exports, he added.

Silva and Candelario acknowledged that the committee evaluated and turned down a petition from the island's motor-vehicle importers to exempt them from the new 1% general excise tax. Silva explained that because companies that pay the new excise tax will have the right to claim a 100% tax credit, the exemption is unnecessary.

Silva also said the amendments introduced in the House will only be those agreed to by the Senate and, therefore, the upper chamber will not introduce further changes.

The legislative assessment of the proposed new code included 14 days of joint public hearings before the House and Senate Treasury committees. The hearings started Dec. 2 and were slated to end last Tuesday. Around 10 leading business organizations, seven well-respected economists and seven agency chiefs testified before the committees. The legislation was filed Nov. 22. ■