

## NET REVENUES TO THE GENERAL FUND

### A. INTRODUCTION

During fiscal year 2013-14, the provisions of several tax measures adopted in order to generate additional revenue to the General Fund came into effect. The aim of these measures was to close partially the structural fiscal deficit that was estimated to be approximately \$2.157 million for the 2012-2013 fiscal year. The estimated total net revenues of the General Fund for the budget adopted for fiscal year 2013-14 was estimated at \$9.525 million, taking into account the estimated additional revenue largely from the provisions of Act 40 of 2013, "Redistribution and Adjustment of the Tax Burden Law."

In January 2013 the distribution of the estimate of revenues by items were reviewed and the next six months of the fiscal year were projected. The exercise was made taking into account the pattern of economic behavior of revenues for each of the categories in the first six months as well as the current and expected tax effect of legislation passed and ongoing administrative plan actions to comply with payment of taxes. The estimated revenue stood at \$9.525 million, but the distribution was revised by item.

Preliminary revenues in this fiscal year for the period from July to March totaled \$6.080 billion, some \$269 million or 4.6% more than the same period last year. Total revenues exceed by \$86 million the estimate for the period; however, there were combined variations between items.

The budget exercise to estimate net revenues to the General Fund for the next fiscal year 2014-15, took into consideration several factors that influence the level of tax revenue. Among these, that the level of tax revenue expected to be reached this year taking into account the non-recurring revenues for fiscal year 2013-14 be achieved, the behavior of macroeconomic variables, administration of the tax system as well as the expected tax effect of tax legislation approved in FY 2013-14 and the proposal.

The recommended budget proposes legislation of diverse measures to muster resources in order to have a balanced budget. These measures are estimated to total \$540 million in additional revenue to the General Fund. A table with the different proposed measures follows below.

Proposed Legislation	Estimate
1. Eliminate the Work Credit	\$124
2. The \$400 bonus for Seniors is to be distributed only if certain collection goals are met; if not, guarantee a maximum of \$200, postponing payment to between July and October of 2014.	\$100
3. Limit Food Exemption (Food Basket) clarifying the taxation of certain products which varies between merchants	\$10
4. 5% to Tax Remittances (Total \$ 30M, \$ 15M spent on housing projects)	\$15
5. HB 1362: Charges for therapeutic use	\$5
6. Law No. 83 – 2010, Amendments to the Green Energy Fund	\$10
7. Fines ATI – which will go to Roads SB 851	(\$39)
8. Slot machines – measure to regulate illegal gambling machines and impose certain charges for use; as discussed by the Executive and Legislature	\$10
9. Changes to taxing of passive income	\$30
10. Modify capital gains of corporations	\$30
11. Adjust the brackets of the alternate basic tax	\$32
12. 4% dividend on foreign assets of regular corporations (creditable)	\$30
13. Amendments to legislation on collection of sales and use tax (IVU) at ports of entry E	\$170
14. Implementation of Power Ball (legislation not required)	\$13
<b>Total</b>	<b>\$540</b>

Estimates are that for fiscal year 2014-15 the total net revenue for the General Fund will reach \$9.640 million, which represents \$115 million or 1.2% more compared to the estimate for FY 2013-14.

Before presenting a description of the revenue level expected for the fiscal year 2014-15 of the major categories of revenue collection, it is important to note that the estimates of income presented in the recommended budget is based on a series of premises and assumptions that are subject to change, such as approval of proposed

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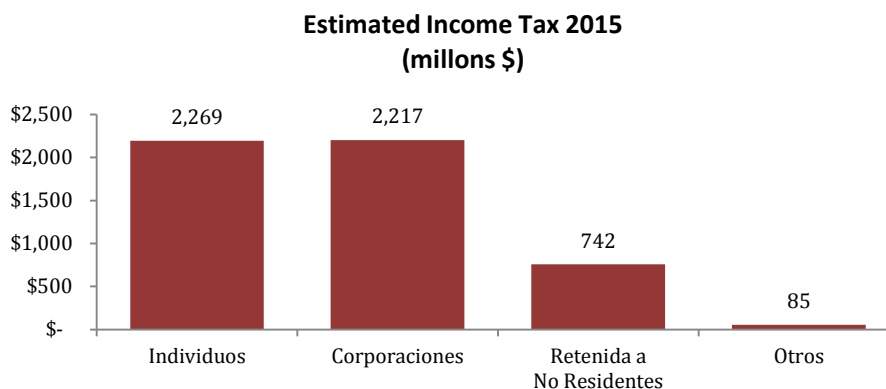
legislation, fluctuations in economic activities and the level of expected revenues for the current fiscal year. On this last point, the estimated revenue for fiscal year 2014-15 was prepared using the results to March 2014, which is the last full month of revenues we have, and it was prepared taking into consideration that a number of premises and assumptions are met. Among these achieving the estimated income of \$9.525 million this fiscal year 2013-14, as adjusted for non-recurring income. The Treasury Department will continue to monitor the monthly income of the current fiscal year 2013-14. If these revenue estimates are not met, revenue estimates for the 2014-15 year will be reduced during the budget approval, unless additional measures are adopted to fill the gap in revenues or reduction in spending occurs.

### B. INCOME TAX

The largest tax producing revenue to the General Fund in the Puerto Rico tax system in income tax, individual and corporate. The total estimated income tax revenue for fiscal 2014-2015 amounts to \$5,313 million. This figure represents 55% of total projected General Fund resources.

As for the distribution of the estimated revenues by item, estimated income tax revenue from individuals totals about \$2.269 million, which includes a component of additional revenue related to changes and adjustments proposed in the determination of the tax.

In fiscal year 2013-2014 Law 40 was introduced, which established an additional tax on gross income, known as the national patent. The accumulated revenues from corporate income tax in July-March FY 2013-2014 show a 72% increase over last year. After adjusting for non-recurring payments of corporate income tax for the current year, it is estimated that for FY 2014-2015 General Fund will receive about \$2.217 billion. Another significant item of this tax is income tax withheld from non-residents, estimated at \$ 742 million. Much of this tax is paid by corporations in the manufacturing industry for the use of patents in the production process.



### C. EXCISE TAXES ON SALES AND USE (IVU)

The indirect taxes of the tax system are the sales and use tax and the excise taxes on specific products or services. These are the second most important category of revenue to the General Fund. The estimated total revenue from excise taxes for fiscal year 2014-15 is \$3.001 million, which represents 31% of total resources. This estimate also includes additional revenue from changes proposed such as limiting the motor vehicle excise tax that goes to the Green Energy Fund and the collecting the IVU when the merchandise is unloaded to the docks. A general description of the estimated revenues from the major categories of excise taxes is presented.

#### 1. Excise Tax on Foreign Corporations

The excise tax on Foreign Corporations has been an essential source of revenue to the treasury. The accumulated revenues from July to March for fiscal year 2013-14 show a \$70 million (5%) increase over the same period last year. This is due to the increase in the tax rate from 2.75% to 4.0% which came into effect in July 2013 and whose payment was effective as of August 2013. By establishing a fixed 4% rate, this tax becomes an important source of income to the General Fund. For the next fiscal year 2014-15, an income level of \$1.962 million is expected.

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**Special Excise Tax Foreign Corporations  
(millions \$)**



### 2. Sales and Use Tax (IVU)

In fiscal year 2013-14, the tax base of the Sales and Use Tax was amended as part of legislative changes to expand coverage by eliminating certain tax exemptions and improving efficiency in its administration. Regarding tax administration, the Department has undertaken many initiatives to improve and strengthen controls such as hiring more inspectors, internal revenue agents, specialized staff, new audits focused on the changes of Law 40, campaign media against evasion of the Sales and Use Tax (IVU), evasion cases referred to the Department of Justice and promoting legislation to streamline control efforts, among others.

The estimated revenue of the 5.5% IVU for fiscal year 2013-2014 is \$1261.2 million. For the month of March, Sales Tax and Use Tax (IVU) reached a total of \$93.5 million, the highest level for a March since the IVU was introduced in November 2006. This amount represented an increase of \$7.1 million for an annual rate of 8.3%, the highest observed this fiscal year since July 2013. The revenues accrued from July to March fiscal 2013-2014 show an increase of 6.1% over the same period last year.

For fiscal year 2014-15 an increase the collection capacity of the IVU is expected as a result of legislation, including Law 117 of 2013 and greater control measures. As of July, the IVU of every taxable item will begin to be collected at the docks. The tax paid by importers will be taken it as a credit against the IVU charged by sale of the goods in the supply chain. Law 18 of 2014 restructured the IVU so that the tax rate is six (6) percent statewide and one (1) percent at the municipal level. This Law also established the Local Government Fund, which will receive zero point five (0.5) percent. In practical terms, the state-level will receive the equivalent to the rate of 5.5%.

For FY 2014-15, the Department of the Treasury projected total IVU collections at the rate of 5.5% at \$1,431.7 million, representing \$170.4 million when compared to the 2013-14 estimate. COFINA will receive the first \$670 million that are collected, and the General Fund will receive \$ 759 million.

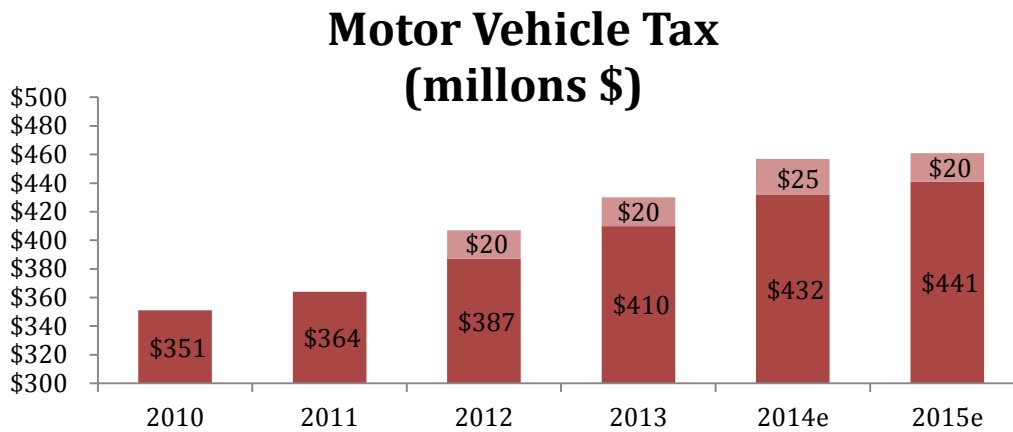
### 3. Motor Vehicle Tax

In the period from July to March of the current fiscal year, revenues from the excise tax on motor vehicles show a slight increase over the previous year.

In fiscal year 2011-12, the provisions of Law 83-2010 which created the Green Energy Fund came into effect. The Law provides that the first proceeds of the excise tax on motor vehicles will enter the Fund as soon as received by the Treasury Department. For FY 2013-14 this amount entering the special fund increased from \$20 million to \$25 million. The revenues to the General Fund from the excise tax on motor vehicles were estimated at \$432 million for FY 2013-2014.

Law 83-2010 provides that the amount entering the Green Energy Fund increase to \$30 million in fiscal year 2014-2015. However, an amendment has been proposed to decrease the amount to \$ 20 million. If approved, the estimated collection for the General Fund from motor vehicle excise tax totals \$441 million for fiscal 2014-2015.

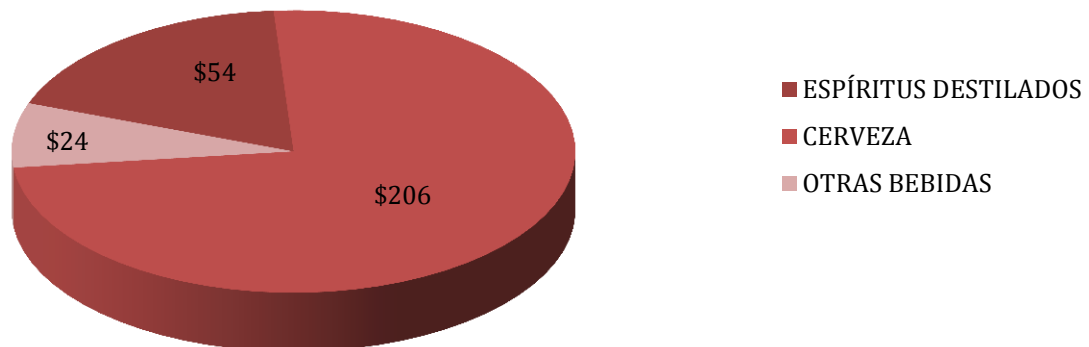
## NET REVENUES TO THE GENERAL FUND



#### 4. Excise Tax on Alcoholic Beverages

The revenues from excise taxes on alcoholic beverages are composed of three categories, beer, distilled spirits, wines and others. For fiscal year 2014-15 a growth of 0.4% is projected for total liquor revenues a total of \$284 million. The estimated distribution of beverage revenues is illustrated in the graph below.

### Estimates for Alcoholic Beverages FY 2015 (in millions \$)



The revenues from beer are the main source of revenue from taxes on alcoholic beverages, accounting for 73%. The excise tax on beer is scaled upward depending on the enterprises' level of production.

#### 5. Lotteries

The lottery market in Puerto Rico is composed of the Traditional Lottery and the Additional Lottery, the latter also known as the Electronic Lottery. Revenues received by the government from the operation of both lotteries are divided into separate funds and legislative appropriations for various needs such as housing, municipalities, compulsive gamblers program, catastrophic illness, Olympic Committee, among others.

In recent years, there has been a reduction in sales of tickets for the Traditional Lottery, which has caused a decline in revenue. In fiscal year 2012-13, the General Fund received from the operation of the Traditional Lottery \$24 million. It is estimated that for FY 2014-15 this will decrease to \$ 17 million.

In the particular case of the Electronic Lottery, introducing a new game mode called "powerball" is under contemplation. About \$13 million in revenue from this new game are estimated. Given the above, the projection in revenue to the General Fund for FY 2014-15 from operation of the Electronic Lottery totals \$93 million.

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### **6. Cigarettes**

Law 41-2013 increased the cigarette excise tax from \$11.15 to \$16.15 for fiscal 2013-2014 and \$17.00 for 2014-2015 on each hundred or fraction of one hundred (100) cigarettes. Taking into account the experience of previous increases and the downward trend in consumption, the estimated increase in revenues for the next fiscal year is \$4 million. The estimated total revenue from the cigarette excise tax is \$209 million.

The law states that from the total income generated by the excise tax on cigarettes, \$20 million is designated for the Highway Authority, \$10 million to the Metropolitan Bus Authority, and \$1 million to the Special Fund for the Custodian of Archives and Relics of Ex Governors and former First Ladies of Puerto Rico.

Last year Law 166-2013 was approved. This legislation assigned one (1) percent of the revenues earned as a result of the excise tax on cigarettes and tobacco derivatives as follows: thirty-three (0.33) percent of the revenues will go to the Puerto Rico School of Plastic Arts, about thirty-three (0.33) percent of the revenues will go to the Conservatory of Music of Puerto Rico and about thirty-four (0.34) percent of the revenues to the Corporation of Musical Arts. After these adjustments, total estimated revenues from cigarette excise taxes for fiscal year 2014-2015 that go into the General Fund are about \$176 million.

### **7. Motor Vehicle Fines**

Senate Bill 851, as approved, creates the Integrated Transport Authority of Puerto Rico. This bill is under consideration for adoption by the House of Representatives. Article 18 provides, among other things, that the Special Fund for the Development of the Integrated Public Transport will draw on the administrative fines imposed under the provisions of the Law 22-2000, as amended, known as the Puerto Rico Transit and Vehicle Act. This means that the revenues previously received by the General Fund for that concept are to be transferred to this new Fund. The estimate of this amount is about \$39 million.

### **8. Federal Excise Tax on Rum Shipments**

Another source of revenue for the General Fund is the federal excise tax refund on rum exports. In fiscal year 2013-14 the estimate is that the General Fund will receive \$220 million. Due to several factors, the revenues from this source decreased compared to the levels that were received in the 2011-12 fiscal year. The first was a reduction in production as a result of the agreement between the Virgin Islands and one of the largest producers of rum in the world, since the producer used bulk rum produced in Puerto Rico in its products. In turn, the increase established by Law 178-2010 from 10% to 25% and then 46% of the portion of funds to promote and boost the rum industry had an effect. Income received by the local government from this revenue source is distributed to the General Fund, the Conservation Trust, the Fund for Science and Technology, and the Program for Promotion of Rums.

Recently, Governor Alejandro García Padilla announced along with the Serrallés Distilleries, Inc., the expansion in the production of rum. This will have an economic impact through the creation of jobs, and will draw additional revenue through the excise tax Puerto Rico receives from the export of this product. Taking the above into consideration and the behavior of the estimated revenues in fiscal year 2014-15, the General Fund will receive about \$225 million in federal reimbursement.

# NET REVENUES TO THE GENERAL FUND

**Department of the Treasury**  
Office of Economic and Financial Affairs  
Final Revenues FY 2013 and Estimate FY 2014

Items	Final FY 2013	Revised Estimate FY 2014	Dif.	Change %
Net Revenues to the General Fund	8,502	9,525	1,023	12.0%
From State Sources	8,256	9,305	1,049	12.7%
Taxex	7,695	8,970	1,276	16.6%
Property Tax	34	16	(18)	-52.9%
Income Tax, Total	4,398	5,392	994	22.6%
Individuals	2,079	2,004	(74)	-3.6%
Corporations	1,287	2,513	1,227	95.3%
Parnterships	1	1		0.0%
Withheld from non-residents	983	820	(163)	-16.6%
Tollgate Tax Regular	9	7	(2)	-21.3%
Interests	5	6	1	11.1%
Dividends	34	41	7	20.6%
Donations and Estate Tax	2	3	1	66.7%
Sales and Use Tax (IVU)	553	614	61	11.1%
Excise Taxes, Grand Total	2,627	2,931	304	11.6%
Alcoholic Beverages, Total	282	283	1	0.2%
Distilled Spirits	55	53	(2)	-2.3%
Beer	207	206	(1)	-0.4%
Other Beverages	21	24	3	15.9%
General Taxes, Totals	2,345	2,648	303	12.9%
Foreign Corporations (Law 154)	1,677	1,938	261	15.5%
Cigarettes	185	174	(11)	-6.1%
Petroleum Based Products	5	4	(1)	-11.1%
Motor Vehicles	411	432	21	5.2%
Horse Racing	13	16	3	21.2%
Insurance Premiums	25	48	23	95.1%
Cement	1	1	(0)	-9.1%
Slot Machines	25	31	6	26.0%
Other Taxes	4	4	0	8.1%
Licensing	81	14	(67)	-82.7%
Motor Vehicle Registrations	64	0	(64)	-100.0%
Alcoholic Beverages and others	17	14	(3)	-16.7%
No Contributivos	562	335	(267)	-40.4%
Lotería Tradicional	24	19	(5)	-21.8%
Lotería Electrónica	39	80	41	105.7%
Miscellaneous Revenues Total	499	236	(263)	-52.7%
Fines and Penalties	54	64	10	17.6%
Registration and Certification of Documents	106	102	(4)	-3.4%
Other	339	70	(269)	-79.3%
From other sources	246	220	(26)	-10.5%
Excise Tax on Rum Shipments	246	220	(26)	-10.5%

# NET REVENUES TO THE GENERAL FUND

**Department of the Treasury**  
Office of Economic and Financial Affairs  
Revised revenues FY 2014 and Preliminary FY 2015

Items	Revised FY 2014	Preliminary FY 2015	Dif.	Change %
Net Revenues to the General Fund	9,525	9,640	115	1.2%
From State Sources	9,305	9,415	110	1.2%
Taxes	8,970	9,094	124	1.4%
Property Tax	16	0	(16)	-100.0%
Income Tax, Total	5,392	5,313	(79)	-1.5%
Individuals	2,004	2,269	265	13.2%
Corporations	2,513	2,217	(296)	-11.8%
Partnerships	1	2	1	100.0%
Withheld from non-residents	820	742	(78)	-9.5%
Tollgate Tax Regular	7	5	(2)	-28.6%
Interests	6	7	1	16.7%
Dividends	41	71	30	73.3%
Donations and Estate Tax	3	6	3	100.0%
Sales and Use Tax (IVU)	614	759	145	23.6%
Excise Taxes, Grand Total	2,931	3,001	70	2.4%
Alcoholic Beverages, Total	283	284	1	0.4%
Distilled Spirits	53	54	1	1.9%
Beer	206	206	0	0.0%
Other Beverages	24	24	0	0.0%
General Taxes, Totals	2,648	2,717	69	2.6%
Foreign Corporations (Law 154)	1,938	1,962	24	1.2%
Cigarettes	174	176	2	1.1%
Petroleum Based Products	4	5	1	25.0%
Motor Vehicles	432	441	9	2.1%
Horse Racing	16	16	0	0.0%
Insurance Premiums	48	71	23	47.9%
Cement	1	1	0	0.0%
Slot Machines	31	41	10	32.3%
Other Taxes	4	4	0	0.0%
Licensing	14	15	1	7.1%
Motor Vehicle Registrations	0	0	0	0.0%
Alcoholic Beverages and others	14	15	1	7.1%
No Contributivos	335	321	(14)	-4.2%
Lotería Tradicional	19	17	(2)	-10.5%
Lotería Electrónica	80	93	13	16.3%
Miscellaneous Revenues Total	236	211	(25)	-10.6%
Fines and Penalties	64	16	(48)	-75.0%
Registration and Certification of Documents	102	104	2	2.0%
Other	70	91	21	30.0%
From other sources	220	225	5	2.3%
Excise Tax on Rum Shipments	220	225	5	2.3%