



## Recent Tax Developments: Act 60-2019 and Regulation Number 9094

By: **Carlos R. González-Martínez**

### AMENDMENTS TO THE PUERTO RICO INTERNAL REVENUE CODE BROUGHT BY ACT 60-2019

Act 60-2019, which was approved on July 1, 2019 to create the Puerto Rico Incentives Code (“Act 60-2019”), also amended other laws, including the Puerto Rico Internal Revenue Code of 2011, as amended (the “Code”). In this bulletin, we provide a summary of the main changes to the Code included in Act 60-2019. In future bulletins we will discuss the changes brought by the Puerto Rico Incentives Code, if any, as compared to the existing incentive laws.

Act 60-2019 introduced the following amendments to the Code:

- The contributions made by individual taxpayers to “Mi Futuro Accounts” will be deductible, to the extent the contributions to these and other educational savings accounts do not exceed \$500.<sup>1</sup>
- For taxable years commencing after December 31, 2018, the cash basis method of accounting will be allowed to taxpayers that do not have inventories and whose average annual gross income for the last three years of operations is \$3 million or

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less. No administrative determination will be required from the Secretary of the Treasury for a change from accrual to cash basis.

- The income tax withholding at source of 10% on services rendered will not apply to payments made between persons that are part of a controlled group of corporations or a group of related persons.
  - Taxpayers with a fiscal year end, or those that use the accrual method of accounting, will not be required to include a schedule with their income tax return to reconcile the amount of expenses claimed on such return to the total expenses reported on the informative declarations<sup>2</sup> if audited financial statements are included with the income tax return and the related supplemental schedules are filed as required by the Code.
  - Added a new section to the Code to establish a requirement to entities that provide either telecommunication, internet, cable or satellite TV services, or that receive payments for advertisement or insurance premiums, to prepare annual informative declarations to all commercial or individual clients. Such informative declarations must be prepared and filed by electronic means with the Puerto Rico Treasury Department by February 28 of the following calendar year. These informative declarations must include payor's information such as the name, address, employer's identification (or social security) number and the amount paid. The section that imposes penalties for not complying with the filing of informative declarations was also amended to include failure to comply with this requirement among these penalties.
  - Added a new section to the Code which allows partnerships that are substantially engaged in providing services (i.e. 80% or more of its gross income is from services rendered), the opportunity to elect an optional tax on behalf of its partners.<sup>3</sup> In the case the partnership elects this option,
- the tax would be paid by the partnership and the distributable share would be reported to the partners as an exclusion from gross income (because the tax has already been paid).
- Added a new Subchapter G to the Code to provide entities with an election of special partnership or corporation of individuals the option to convert to a partnership.
  - Included certain provisions regarding real estate investment trusts ("REIT"). Among those more relevant are: changes to the definitions of who will be considered a shareholder, inclusion of warehouses within the definition of "real property", authorization to the Secretary of the Treasury to determine whether the income tax withholding on the taxable dividends distributed by a REIT would be excessive and will cause undue hardship to the taxpayers and to determine whether a taxpayer should be exempt from taxation.
  - Added a new section to the Code to allow corporations of individuals substantially engaged in providing services (i.e. 80% or more of its gross income is from services rendered) the opportunity to elect an optional tax on behalf of their shareholders.<sup>4</sup> In the case the corporation of individuals elects this option, the tax would be paid by the corporation of individuals and the distributable share would be reported to the shareholders as an exclusion from gross income (because the tax has already been paid).
  - For sales and use taxes purposes, the definition of "designated professional services" will now include the continuing education services rendered by a for-profit entity which is certified by a Puerto Rico governmental agency, the United States Government or the Puerto Rico Supreme Court, or by a not-for-profit private entity that offers those services to designated professionals.
  - Amended Section 1081.05 of the Code to include among the definition of a "qualified distribution"<sup>5</sup> those related to "Mi Futuro Accounts" and to exempt those "qualified distributions" from income tax.

## ABOUT THE AUTHOR

### Carlos R. González Martínez

**Carlos** is a Member at Alvarado Tax & Business Advisors LLC (ATBA) and has over twenty five years of experience in the corporate and individual tax advisory area with various international firms and industries. He provides corporate tax services for clients in telecommunications, manufacturing, service and retailing industries, and also is the Operations Manager for the Tax Resolution and Outsourcing Services divisions.

Prior to joining ATBA, Carlos had a seven-year-plus career with Puerto Rico Telephone Company (PRTC) as Executive Tax Advisor in charge of the corporate tax division, and a three-year career with Caribe General Electric as Tax Manager. Prior to that, he worked for ten years in public accounting firms, including experience in both audit and tax, with KPMG, Price Waterhouse LLP's Corporate Tax Practice and Arthur Andersen's Tax Practice. While at PRTC, Carlos was the project leader and successfully implemented the new sales and use tax rules, modifying more than ten different systems and affecting the operating guidelines of fourteen departments.

Carlos has a BBA major in Accounting from the University of Puerto Rico. He is a member of the Puerto Rico Society of Certified Public Accountants and the American Institute of Certified Public Accountants.

## ATBA Comments:

The so-called Puerto Rico Incentives Code was finally approved as Act 60-2019; but unexpectedly, it also included multiple amendments to the Code that may represent opportunities such as:

- a. the transition from accrual basis to cash basis for certain

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- b. entities with annual average gross income of \$3 million or less; and
- c. the opportunity for flow-through entities to elect the optional tax; and
- d. the opportunity for special partnerships and corporation of individuals to convert to partnerships; and
- e. the elimination of the 10% income tax withholding on services between entities of the same group of related entities.

It may also represent additional work and the possibility of additional costs (such as the requirement to entities that provide telecommunication, internet, cable or satellite TV services, or those who receive payments for advertisement or insurance premiums, to prepare an annual informative declaration to all commercial or individual clients). The government keeps changing the rules of the game, and you need to be aware of those changes to determine which are the more convenient to your business. Whether you need assistance with an analysis of your specific business case to avail to any of the recently approved opportunities, or you need assistance to comply with the new informative declarations filing requirements, ATBA has the professionals you need to help your business move forward.

### **REGULATION NUMBER 9094 – MUNICIPAL REVENUE COLLECTION CENTER (“MRCC”)**

Act 77-2017 was approved on August 6, 2017 to allow municipalities to, with previous coordination with the MRCC, carry out efforts for the collection of property taxes, including the appropriation of real and personal property, and contract professionals for the appraisal of properties to determine their taxable values. To avoid the duplicity of functions and make viable the functions authorized by Act 77-2017, it was required that regulations be prepared and approved by the MRCC. Regulation 9094 was approved by the MRCC with this purpose and, hereinbelow, we summarize some of the most important requirements that the municipalities will need to comply if they

are interested in participating in the above-mentioned procedures:

1. Notification – the Mayor of every municipality interested in participating in the property tax collection, appraisal or appropriation procedures must notify the Executive Director of the MRCC of its intention, including the following information:
  - a. competencies that the municipality is interested to participate;
  - b. date of commencement of the efforts;
  - c. name of the person in charge of organizing and directing the efforts on behalf of the municipality.
2. Requirements for the person in charge and the municipal employees and contractors:
  - a. municipal employees and contractors cannot use the MRCC logo;
  - b. any verbal or written communication should be identified as coming from the municipality and not the MRCC;
  - c. municipal employees and contractors must attend an orientation meeting to be provided by the MRCC with respect to the functions to be performed.
3. Competencies
  - a. Appraisal of real property – Includes the following:
    - i. appraisal of the taxable value of real property not previously appraised within the municipal jurisdiction
    - ii. investigation of real property previously appraised within the municipal jurisdiction, but which may have suffered alterations or improvements, or which may require the grouping with other properties or its segregation.
  - b. Collection of property taxes – the municipality must follow these rules:

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- i. it may participate in the collection process of real and personal property tax debts due for more than one year and 90 days related to property located within its municipal jurisdiction;



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- ii. the MRCC will provide a quarterly report to the municipality with a list of the outstanding property tax balances of the properties located within its jurisdiction;
  - iii. each municipality participating in this program must approve a municipal ordinance to adopt the collection process in accordance to the MRCC regulations;
  - iv. the payments received from the taxpayers must be addressed to the MRCC and deposited in the MRCC's bank account.
- c. Appropriation of real property:
- i. each municipality participating of this program must approve a municipal ordinance to adopt the appropriation process in accordance to the MRCC regulations;
  - ii. a file must be prepared for each case, after agreeing with the MRCC the cases to be worked for appropriation, which must include a detail of the tax debt divided by principal, interest and surcharges, copy of the communications made during the collection process and copy of the certified mail receipts or confirmation of hand-delivery, certificate of values, title study and payment history, among other documents;
  - iii. A process must be followed to register the appropriation at the Property Registry and copy must be sent to the MRCC.

### ATBA Comments:

The economic situation of many municipalities is forcing them to be more aggressive in the tax assessment and collection of property taxes. Please be

aware that, after the approval of Regulation 9094, municipal employees or contractors may knock on your door to review the improvements made to the building (be they owned or leased) and to search for other non-assessed real property within your location, or to try to collect past due property taxes. The MRCC maintains information on its systems related to the items assessed and values assigned to those items for real property tax purposes. It is important that you are aware of which real property items have not been assessed in your location so that you can be informed of the possible result of those visits and properly accrue for the potential liability, in case it applies.

Our tax professionals have extensive experience working with deficiency and collection notices from the MRCC and the municipalities. Contact us for more information regarding this regulation or for assistance with matters related with the MRCC or the municipalities.

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### Notes:

<sup>1</sup> "Mi Futuro Accounts" are accounts that the Puerto Rico government intends to open to certain students from the public education system who meet certain conditions.

<sup>2</sup> Section 1063.01 of the Code requires that certain expenses such as salaries, rent, commissions and professional services be reported on an informative declaration for the payor to be able to claim such expenses on its income tax return.

<sup>3</sup> Act 60-2019 added Section 1071.10 to the Code which, among other things, provides for an optional tax computation paid at the partnership's level that ranges from 6% to 20% depending on its gross income.

<sup>4</sup> Act 60-2019 added Section 1115.11 to the Code which, among other things, provides for an optional tax computation paid at the entity's level that ranges from 6% to 20% depending on its gross income.

<sup>5</sup> Qualified distributions are those payments to cover college, technical or vocational studies or as the initial capital for a business of the beneficiary of the account.

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