

The Tax Advisor

Special Bulletin on Latest Tax News

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Recently Approved Administrative Determinations by the PR Treasury Department

By: María De L. Adorno Santos

On September 17, 2017, the Governor of Puerto Rico issued Executive Order No. OE-2017-047, to declare Puerto Rico in a state of emergency due to the upcoming passage of hurricane María.

The extensive damages left by the hurricane have required the issuance of additional Executive Orders by the Governor together with administrative determinations and informative bulletins by the Puerto Rico Treasury Department ("PRTD") to continue with an effective tax administration and provide relief to the taxpayers in Puerto Rico. This bulletin summarizes two of the most recent publications issued by the PRTD due to the passage of hurricane María.

Administrative Determination 17-26: Exemption on the Collection of Sales and Use Taxes ("SUT") to Certain Merchants

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On November 8, 2017, the Governor of Puerto Rico issued Executive Order No. OE-2017-068 authorizing the Secretary of the Treasury to exempt Small and Medium Businesses ("SMB") that comply with certain requisites from collecting SUT on the sale of tangible property or services, including the payment of SUT on inventory purchased for resale ("Exempt Merchants"). Due to the issuance of the OE-2017-068, the PRTD issued the Administrative Determination 17-26 ("AD 17-26") to establish the requirements and temporary period of such SUT exemption.

I. Exempt Merchant

The AD 17-26 states that those merchants with an annual volume of business that does not exceed one million dollars (\$1,000,000) and are **not** "Large taxpayers", as such term is defined on the Puerto Rico Internal Revenue Code ("the Code"), will be exempt of the collection of the **State and Municipal** SUT. Such merchants will be considered as Exempt Merchants during the temporary period of exemption (as explained below). Additionally, and as mentioned above, this SUT exemption also applies to purchases of inventory for resale, whether purchased within Puerto Rico or imported. However, please note that the exemption does not apply to property acquired for the merchant's use or to services received.

This SUT exemption will be temporary as it will cover the period from November 20, 2017 through December 31, 2017. As of today, the PRTD should have evaluated the SUT Returns of the applicable SMB merchants, and should have issued by electronic means through the SURI portal, an Exempt Merchant Temporary Certificate (the "Certificate"). This Certificate should indicate that the merchant is a Non-Withholding Agent. Note that the Certificate must be placed on the merchant's establishment, visible to the costumers. Otherwise, the merchant could be exposed to the revocation of the exemption.

2. Determination of the Volume of Sales

To determine which SMBs are exempt from the collection of SUT, the PRTD will consider the total volume of sales, taxable and exempt, reported on the SUT returns for the 12-months period beginning on August 2016 through July 2017. If the merchant began operations after August 31, 2016, then the annual volume of sales will be determined by annualizing the sales presented on the SUT Returns filed by the merchant from the beginning of their operations through July 2017. Please note, that the merchants should had filed the SUT Returns up to July 2017 to be eligible for this SUT exemption. However, if the merchant began its operations after July 31, 2017 and it is registered in SURI, the taxpayer will be considered an Exempt Merchant for these purposes.

3. Filing Requirements

Since this SUT exemption does not exempt merchants from the filing of the SUT returns, the total sales subject to the exemption must be reported as "Exempt Sales" on the monthly SUT return. For merchants under the cash basis method, the Exempt Sales will be those to which the collection of payment was made during the exemption period. However, if merchants use the accrual basis method and do not receive payment at the moment of the sale, then the transactions considered exempt will be those invoiced to the clients during the period from November 20, 2017 through December 31, 2017.

Additionally, to benefit from the exemption on purchases of inventory for resale, the Exempt Merchant must forward a duly completed *Model SC 2916, Certificate of Exempt Purchases and Services Subject to Special SUT of 4%*, together with a copy of its Certificate to its supplier in Puerto Rico. If the inventory for resale is imported, the merchandise must be declared through SURI as exempt merchandise.

4. Penalties

If Exempt Merchants charge SUT during the temporary period of exemption, they may be subject to a penalty of \$100 for each receipt, invoice or other evidence of sale.

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María is a Senior Tax Associate at Alvarado Tax & Business Advisors LLC (AT&B). She started her career in taxes as an intern in Alvarado Tax & Business Advisors (formerly known as Zaragoza & Alvarado LLP) and has over five years of experience in the corporate and individual tax advisory areas. She provides corporate and individual tax services for clients in the retail, manufacturing, and service industry among others.

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Also, if the Exempt Merchant collects SUT during the Exemption Period, it is required to remit it to the PRTD.

Administrative Determination 17-29: Applicable Rules for Distributions from Qualified Retirements Plan and Individual Retirements Accounts due to the Passage of Hurricane María

On November 8, 2017, the Governor of Puerto Rico issued Executive Order OE-2017-67 authorizing the Secretary of Treasury to establish tax rules for residents of Puerto Rico to withdraw amounts from their qualified retirement plans and individual retirement accounts ("IRAs") at preferential rates during the emergency period. Based on the above, the PRTD

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issued the Administrative Determination 17-29 (“AD 17-29”) to provide such requirements.

AD 17-29 allows individuals to make cash distributions or retirements in forms of partial payments of cash from qualified retirement plans or IRA accounts during the period of September 20, 2017 through June 30, 2018 to cover expenses that the individual will incur due to the losses or damages suffered by the passage of Hurricane María. Only individuals who are residents of Puerto Rico during the taxable years 2017 and 2018 qualify to make the distributions.

The expenses that are eligible for the cash distributions or retirements are expenses that the individual will incur to cover for the losses or damages suffered by the passage of hurricane María or/and to cover extraordinary expenses of basic needs due to the disaster. These expenses may be incurred by the individual, his/her spouse, decedents or ascendants. Additionally, the expenses do not need to be incurred during the period which the cash distribution or retirement is allowed.

AD 17-29 provides that the individual may distribute or retire up to \$100,000, in aggregate, from its qualified retirement plans or IRAs without being subject to the early retirement penalty imposed in the Code. The first \$10,000 are exempt from income taxation. It also provides a reduced income tax rate of 10% for any distribution that exceed \$10,000 up to \$100,000. The income tax determined using the reduced income tax rate must be withheld from the distribution or retirement. If no withholding is made, the distribution or retirement will be subject to the ordinary income tax rate and may also be subject to early retirement penalties. Any cash distribution or retirement in excess of \$100,000 will be subject to the ordinary income tax rate and may be subject to early retirement penalties.

Please note, that the distributions along with the tax withheld must be reported on Form 480.7C for Qualified Retirement Plans and on 480.7 for IRAs.

I. Process to Apply for an Eligible Distribution

Any individual that wishes to receive a distribution under AD 17-29 must include with the regular application process of the qualified retirement plan or IRA a sworn statement that should include: (1) basic information of the individual, (2) certification that the individual is and will be a resident of Puerto Rico for the years 2017 and 2018, (3) a statement that the amount of distribution will be used to cover Eligible Expenses, (4) a certification that the individual has not received eligible distributions exempt of the tax withholding at source (first \$10,000) from other qualified retirements plans or IRA accounts, if applicable, (5) detail of eligible distributions received showing the amount and date of the distribution, if applicable, and (6) a certification that the individual assumes responsibility for the payment of the taxes over the distributions requested if at the end of the year the requirement of residency is not met, the amount received was not used to satisfy the eligible expenses or he or she received distributions in excess of the limit established by the DA 17-29.

2. Responsibilities of the Administrators

The administrators of the qualified retirement plans or IRA accounts do not have to validate the information included on the sworn statement. However, they must corroborate if the individual is a resident of Puerto Rico. The administrator will also act as a withholding agent and will be responsible for the withholding and remittance of the tax to the Secretary of Treasury on or before the fifteenth day (15) of the following month in which the distribution was made. If the administrator does not withhold and remit the taxes, it will be responsible for the payment of such taxes and will be subject to the penalties imposed by Subtitle F of the Code. The qualified retirement plans are not required to adopt the dispositions of the AD 17-29. However, if they decided to adopt them, the administrator must amend the

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retirement plan no later than December 31, 2018. Such amendment will not have to be filed with the PRTD since such amendment will not be considered as a “qualification amendment.”

ATBA Comments

AD 17-26 – The purpose of the OE-2017-068 and AS 17-26 is to provide relief to SMBs that suffered losses due to the passing of

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hurricane María, by providing them a competitive advantage from large businesses. It however, will require them to modify their billing system quickly in order to avoid collecting the SUT and to do it once again at the end of the year, to commence collection again. This may result in additional costs to those merchants.

This determination is also important for merchants who are not considered SMB. These merchants may benefit from the exemption provided to those SMB by acquiring goods or services free of SUT. If you believe that one of your providers may be considered a SMB under AD 17-26, you should request the exemption certificate from them before paying the SUT. Other merchants should also be aware that some of their clients may be SMB exempt on the purchase of personal tangible property for resale. If that is the case, you should establish procedures to document the exempt transaction and to avoid the collection of the SUT.

If you considered yourself to qualify under the provisions of this AD as an SMB and have not received notice from SURI that your Certificate has been issued, our tax professionals may assist you in determining if you should have been entitled to receive such Certificate and in obtaining it.

AD 17-29 – The AD 17-29 provides a monetary relief to the Puerto Rico residents that have either suffered losses or incurred in extraordinary expenses due to the passage of hurricane María. Individuals must determine their needs of funds to cover the eligible expenses and the source from which those funds may be obtained. If the individual determines that the needs exceeds \$10,000, he/she must make sure that the 10% tax in the excess of \$10,000 is withheld at source.

Individuals should keep records of the distributions requested and received, as well as a detail of the expenses in which such distribution was used. Even when a detail of the current or expected expenses is not required to be provided to make a distribution, the PRTD may always request

it as part of an investigation. Also, the individual should request the distributions with enough time to receive it before June 30, 2018. All distributions received after such date will be subject to regular rates and to penalties for early retirement.

Since qualified retirement plans are not required to modify their plans to allow the retirement of funds under AD 17-29, every individual should consult their plan managers to make sure this option is or will be available for them.

Our tax advisors may help plan administrators to make sure that amendments to the plan comply with AD 17-29 and with the withholding and informative declaration requirements.

Upcoming Due Dates Only for Non Large Taxpayers

Due Date	Returns, Payments, and Deposits
December 11, 2017	<ul style="list-style-type: none">Excise Tax Return for the period of October 2017.Tax on Imports Monthly Return for the periods of August, September October and November 2017.
December 15, 2017	<ul style="list-style-type: none">Third Estimated Tax Payment for Calendar Taxpayers.Payment due with Income Tax Return (Return is due on January 15, 2018).Deposit of Tax Withheld at Source for the period of August and September 2017.Form 6048: Request of Information of Tax Credits Reported on Form 480.71 (this also applies to Large Taxpayers).
December 20, 2017	<ul style="list-style-type: none">Sales and Use Tax Return for the periods of August, September, October and November 2017.

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