



Update on the Deduction of Automobile Expenses

By Rosirma García-Rivera

In our Special Bulletins of the Tax Advisors of December 2010, July 2012 and January 2013, we addressed the limitations on the deductibility of expenses related to the use of automobiles in businesses. Since then, the Puerto Rico Treasury Department (“Treasury”) issued on December 27, 2016 a proposed regulation (“Proposed Regulation”) to among others, repeal the approved Regulation 8297 dated December 18, 2012 (“Approved Regulation”).

The purpose of this bulletin, is to provide the most important proposed changes to the above-mentioned deduction.

Background on the Deduction of Automobile Expenses

Section 1033.07 of the Puerto Rico Internal Revenue Code of 2011, as amended (the “Code”), provides that a standard mileage rate will be used in lieu of the actual incurred expenses to determine the automobile expense deduction for automobiles used in the taxpayer’s trade or business.

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On December 22, 2011, Treasury published proposed regulations to Section 1033.07 of the Code. These proposed regulations established the requirements to determine the deductions for expenses incurred or paid for the use and maintenance of an automobile based on the actual mileage that automobile was used as part of the business multiplied by a standard mileage rate. These proposed regulations were not well received by the business community and were never filed before the Department of State, therefore, never becoming effective.

To provide some guidance, Treasury issued Administrative Determination 12-06 ("AD 12-06") on March 14, 2012. AD 12-06 provided two alternatives to calculate the amount to be deducted for expenses related to the use and maintenance of automobiles:

1. A deduction determined based on a standard mileage rate of \$0.60 per each mile a taxpayer used in its trade or business or for the production of revenue ("Standard Mileage Rate Option"); or
2. Actual expense incurred for the use and maintenance of automobile in a trade or business or for the production of revenues, including those expenses that are duly documented by the employees under an expense reimbursement plan established by the employer ("Actual Expense Option").

AD 12-06 established that the above alternatives were applicable only for expenses incurred until June 30, 2012. Therefore, after July 1, 2012, the deduction was to be determined only based on the Standard Mileage Rate Option (item #1 mentioned above).

Afterwards, on July 23, 2012, Treasury issued Administrative Determination 12-10 to extend the applicability of AD 12-06 until December 31, 2012. This in turn meant that until December 31, 2012, the taxpayers had the option to calculate the deduction based on either the Standard Mileage Rate Option or the Actual Expense Option, whichever provided the most benefit.

As previously mentioned, on December 18, 2012, Treasury filed before the Puerto Rico Department of State the Approved Regulation. These regulations did not include the Actual Expense Option as an alternative to compute the automobile expense deduction. Therefore, the automobile expense deduction had to be computed using the Standard Mileage Rate Option. This limitation was not well received by the business community which again complained of the complexities of managing the Standard Mileage Rate Option.

Due to the taxpayers concerns regarding the provisions of the Approved Regulation, Treasury issued Administrative Determination 13-03 on March 19, 2013 to extend the applicability of AD 12-06 until September 30, 2013. Thus, taxpayers continued to have the option to calculate the deduction based on either the Standard Mileage Rate Option or the Actual Expense Option. Subsequently, Treasury issued Administrative Determination 13-18 on September 27, 2013 to further extend the applicability of AD 12-06 until the end of the taxable year 2013.

Finally, on January 9, 2015 Treasury issued Administrative Determination 15-01 ("AD 15-01"). This administrative determination expressed the intent of Treasury to issue a new regulation which will revoke the Approved Regulation. AD 15-01 also reestablished the options to determine the automobile expense deductions in AD 12-06 with the limitation that taxpayers were required to use the same methodology during the entire taxable year.

Proposed Regulation

The Proposed Regulation issued on December 27, 2016 provides that the taxpayers will continue to be able to select one of the two methods mentioned above (i.e. Standard Mileage Rate Option or Actual Expense Option). Once the taxpayer selects one of these methods, the taxpayer will be required to use the same one for the following taxable years. If the taxpayer wants to change the method used, the taxpayer will be required to file a request for ruling about a change of accounting method, pursuant to the provisions of Section 1040.02(f) of the Code.

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Rosirma is a Senior Manager at Alvarado Tax & Business Advisors LLC. Prior to that, she was Senior Manager at Zaragoza & Alvarado LLP. Her Curriculum Vitae also includes previous experience in the corporate and individual tax advisory area working for local and international firm in Puerto Rico.

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In addition, the Proposed Regulation repealed Articles 1031.02(a)(33)-1 to 1031.02(a)(33)-6 of the Regulations issued under the Code. Among the significant provisions included therein were the following:

1. Requirement that the employer had a reimbursement plan (i.e. accountable plan or non-accountable plan);
2. An exception to qualify an expense reimbursement plan which covers exclusively, or mainly, managerial or highly compensated employees; and
3. An alternate method to account for the traveled business miles in lieu of the odometer reading.

Note that items #1 and #2 above will be eliminated with the approval of the Proposed Regulation. In regards with item #3, the alternate method to account the traveled business miles, it will continue to be valid if you elect to compute the automobile expense deduction under the Standard Mileage Rate Option. Such method provides for the use of a daily mileage journal of the municipalities visited and the mileage calculator of the Puerto Rico Highways and Transportation Authority to compute the traveled miles. In addition, it will continue to be accepted, that the employee changes from one method (i.e. odometer reading) to another (i.e. mileage calculator) during the taxable year but not within the same day.

Keep in mind that if the employer decides to determine the deduction of the use and maintenance of automobiles based on the

actual expenses incurred, the employer must keep copies of all the receipts to document the deduction claimed on the income tax return.

Finally, but not less important, note that the "automobile expense" is exclusive of any depreciation or lease expense that may be deductible. However, automobile expense does include gas, repairs, changes of oil, tires, insurance, annual license fees and other expenses of similar nature that relate to the maintenance and use of an automobile.

ATBA Comments

It is important that the taxpayers select the method to account for the automobile expense and then to keep the required documentation to sustain and support the use and maintenance of automobile expense in case of an audit from Treasury. Our tax professionals are ready to assist you with any questions or concerns that you may have on this subject.

We will inform any new development regarding this matter.

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