



## Act 44-2015: Tax Prepayment Windows and Tax Amnesty

By Carlos R. González-Martínez

In our February 2015 Special Bulletin titled “Proposed Extension of Tax Prepayment Windows and Tax Amnesty” we explained House and Senate Bills 2316 and 1299 (herein after the “Bills”), respectively, which had the main purpose to collect tax revenues in anticipation of the proposal to transform the Puerto Rico Tax Regime. The Bills have now been converted into Act 44-2015 (the “Act”) which provides: 1) an additional extension of the tax prepayment windows originally approved under Act 77-2014 (later extended by Act 238-2014), 2) a new window with special tax rates for the tax prepayment of dividend and deemed dividend distributions, and 3) a Tax Amnesty that provides the opportunity to pay tax debts with a total abatement of interest, surcharges and penalties related to income tax, estate and gift taxes, excise taxes, sales and use tax, tax withholding debts and other taxes imposed by any tax incentives acts.

Next we present a detailed explanation of the various incentives provided by the Act. Please note that there were minor changes to the original Bills explained by us in February that were incorporated in the Act.

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### Extension of the Tax Prepayment Windows

The following tax prepayment windows originally approved under Act 77-2014, are now extended through April 30, 2015 including:

#### 1. Individuals, Estates and Trusts

- a. The tax prepayment of 8% on capital gains
- b. The tax prepayment of 15% on assets, the sale of which would generate ordinary income

#### 2. Individuals

- a. The tax prepayment of 10% on undistributed accumulated amounts of a variable annuity contract.
- b. The tax prepayment of 8% on undistributed accumulated amounts of an Individual Retirement Account or an Educational Contribution Account. The tax prepayment applies to contributions made and accumulated value for year 2014 to the extent the contributions were made prior to the approval of the Act.

#### 3. Corporations

- a. The tax prepayment of 12% on capital gains.

### New Window for the Tax Prepayment on Dividends or Deemed Dividends

The Act provides a new tax prepayment window with a special tax rate of 5% on the distribution of dividends or deemed dividends between January 1<sup>st</sup> and April 30, 2015, and 8% on the distribution of dividends or deemed dividends between May 1<sup>st</sup> and June 30, 2015. The election to pay the special tax must be submitted and the tax paid to the Puerto Rico Treasury Department within the prescribed period. The special tax is in lieu of any other taxes imposed by the Code, including alternative minimum tax and the basic alternate tax, and the amount subject to the prepayment will reduce the earnings

and profits (E&Ps) of the corporation. Please note that an actual distribution of the dividends is not required to benefit from this special tax prepayment rates. Also, public corporations are not allowed to apply for the benefits of the special dividend tax prepayment, however they may apply for the benefits of the tax prepayment on deemed dividends. For purpose of the Act, a public corporation is a corporation whose stock is traded in any national stock exchange, including the New York Stock Exchange and NASDAQ.

### Tax Amnesty

The Act provides the opportunity to pay tax debts with a total abatement of interest, surcharges and penalties for the following taxes:

1. Income tax, except for taxable years commenced after December 31, 2013
2. Estate and gift taxes.
3. Excise Taxes.
4. Sales and Use Taxes for all months before July 1, 2014.
5. Income tax withholding at source for all months up to December 31, 2014.
6. Any other tax imposed by the Special Act Declaring a State of Fiscal Emergency and Establishing an Integrated Fiscal Stabilization Plan to Save Puerto Rico's Credit (Act 7-2009), the Economic Incentives for the Development of PR Act (Act 73-2008), the 2010 Tourism Development of PR Act (Act 74-2010), the PR Green Energy Incentives Act (Act 83-2010), the Film Industry of PR Economic Incentives Act (Act 27-2011), the Export Services Act (Act 20-2012), or any other act of similar nature, or which imposes a special tax rate on income.

### Requirements to Avail to the Tax Amnesty

To benefit from the Tax Amnesty, the taxpayer must comply with the following:

1. Complete and file the document to be provided by the Secretary of the Treasury (the "Secretary") and pay the principal amount of the tax debts on or before June 30, 2015.
2. Be in compliance with all tax and filing requirements of periods commenced after December 31, 2014.

### ABOUT THE AUTHOR

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**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.

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# Amnesty

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3. The taxpayer must detail which tax debts will be covered by the Tax Amnesty, and no objections can be claimed with regard to those debts.
4. Taxpayers under audit may benefit from the Tax Amnesty by paying the corresponding tax on the proposed audit adjustments (without any interest and penalties), resulting in the discontinuance of the audit process.
5. Taxpayers under administrative proceedings on deficiency notices who have been sent final deficiency notices or that have contested a deficiency notice determined by the Treasury Department, may benefit from the Tax Amnesty by paying the total amount of the principal shown in the deficiency as determined by the Secretary.
6. Taxpayers who have filed a judicial action objecting the payment of a deficiency notice determined by the Secretary for any tax and period covered by the Tax Amnesty, may benefit from it by paying the total amount due (limited to principal), resulting in the discontinuance of the judicial process.

7. Taxpayers with an active payment plan for tax debts with the Treasury Department may also qualify for the Tax Amnesty, and will be able to renegotiate the balance due and pay under the terms of this incentive.
8. Taxpayers who received or accrued gross income subject to tax under the Puerto Rico Internal Revenue Code of 2011, as amended (the "Code") on or before December 31, 2013, and have not filed an income tax return nor have paid the related income tax for taxable years ended on or before December 31, 2013, or who did not report the totality of the gross income received or accrued for those periods, or who reported deductions in excess for those periods, shall be allowed to file a special declaration reporting that gross income or adjusting those

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deductions claimed in excess, and will be allowed to pay a tax of 20% over the amount reported with a total abatement of interest, surcharges and penalties.

9. Taxpayers with a tax debt balance consisting only of interest, surcharges, fines and penalties (no principal amount due) will be allowed to eliminate the tax debt subject to the payment of 25% of the total amount due.
10. Payments under the provisions of the Tax Amnesty will be voluntary and final for all purposes and will not be subject to subsequent claims of refund or credit.

### Who may not Benefit from the Tax Amnesty?

1. Taxpayers who have an ongoing proceeding for tax related crimes.
2. Taxpayers who were convicted for tax fraud or whose source of income is illegal, or where activities or businesses may be identified as criminal activities under "the Act against Organized Crime".

### ATBA Comments

Depending on your circumstances, the tax prepayment windows may offer a good opportunity to reduce your overall effective tax rate.


The new window for the prepayment of the tax on dividends and deemed dividends might be an attractive alternative considering the fact that under the proposed Tax System Transformation (House Bill 2329), corporations are given the opportunity to convert to a flow-through entity by prepaying the tax on the current and accumulated E&Ps, and also, because the preferential tax rates, including those of dividends, would be eliminated. Another good reason to consider this window for the tax prepayment on dividends is to reduce your E&Ps, particularly in the case the corporation is subject to the deemed dividend tax of 10%.

On March 31, 2015, the Puerto Rico Treasury Department issued Circular Letter No. 15-04 to establish procedures related to the Tax Amnesty. This Tax Amnesty is probably the most ample and flexible seen in recent times. It not only covers all the types of taxes imposed by the Code, but also includes all other taxes on income imposed by special laws and tax incentives acts, which have been left out of these programs in the past, and interestingly, also allows elected government officers to avail to the benefits of this incentive, benefit which has also been denied in previous amnesties. On the other hand, this Tax Amnesty does not provide an option for establishing a new payment plan.

Article 9 provides that in order to eliminate a tax debt balance composed of only interest, surcharges and penalties under the Tax Amnesty, the taxpayer will be required to pay 25% of the total balance due. In past amnesties, these tax debts with zero principal balance have been eliminated without the requirement of a payment by the taxpayer.

Tax amnesties always present a new opportunity for taxpayers to clarify pending tax debts and at the same time save some money in interest, surcharges and penalties. We encourage you to be proactive in analyzing and resolving any pending tax issues with Treasury. Let us know if you need any assistance with any of these tasks.

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