

Remote Workers – Welcome to Paradise!

By: Felipe Mariani-Franco

Who has not dreamed of moving to a tropical island and working under the shade of palm trees with the sounds of the waves soothing you? Now that dream may become a reality or, at least, that is what the Puerto Rico Government has tried with the introduction of remote workers provisions in the Puerto Rico Internal Revenue Code of 2011, as amended (the “PRIRC”).

Act 52-2022 introduced the concept of remote workers and provides special treatments to employers of remote workers to lure them into allowing their employees to work remotely from Puerto Rico. This with the purpose of significantly reducing tax impacts to the employer. The catch, collect income tax from the remote employees that moved to Puerto Rico and benefit from the money they spend in the local economy.

Background

Before the amendment of Act 52-2022, companies would determine if they were engaged in trade or business in Puerto Rico for purposes of Puerto Rico income tax by looking into all their facts and circumstances. One of the facts that companies would look into is if they had employees working from the Island. Usually, the company would be considered engaged in trade or business in Puerto Rico for Puerto Rico income tax purposes if the

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Ph. (787) 999-4400
E. taxadvisors@alvatax.com

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company had employees providing services from Puerto Rico on a continuous basis. Furthermore, having those employees in Puerto Rico would also result in all sorts of registration and filing requirements with governmental agencies in Puerto Rico, including having nexus for purposes of sales and use tax, personal property tax filing requirements, employment taxes, informative returns, among others. Also, the Puerto Rico employment laws will be applicable to those employees and their employers.

The cost of managing this maze of requirements would on its own deter a company from allowing their employees to work remotely from Puerto Rico

The Solution

The Government of Puerto Rico opted for a simplified approach to the issue. In summary, they decided to exclude the employers of remote workers from being engaged in trade or business (only for income tax purposes) and from the requirement of withholding and remitting Puerto Rico income tax on the wages paid to their employees. The effect of the first exclusion is significant. The employers that meet the requirements will not be subject to Puerto Rico income tax and will not need to file a Puerto Rico income tax return. The benefit of the second one is not that clear, since employers will still be required to compute and withhold, when required, other payroll taxes and report them to Puerto Rico.

Engaged in Trade or Business

Act 52-2022 amended the PRIRC to exclude companies with a “Remote Worker” in Puerto Rico from the definition of “engaged in trade or business in Puerto Rico”. That exclusion applies for taxable years started after December 31, 2021, and companies must comply with the following to **not** be considered engaged in trade or business in Puerto Rico:

1. The taxpayer (employer) may not have at any moment during the taxable year an office or fixed business location in Puerto Rico
2. The taxpayer may not have economic nexus with Puerto Rico
3. The taxpayer is not considered a merchant for purposes of sales and use tax
4. The remote worker is not an officer, director, or majority shareholder of the taxpayer
5. The services rendered by the Remote Worker are for the benefit of clients or businesses of the taxpayer with no nexus with Puerto Rico, and
6. The taxpayer reports the wages paid to the Remote Worker in Federal Form W-2 or Puerto Rico Form 499R-2/W-2PR.

Furthermore, since the definition of “Remote Worker” requires that she/he be employed by a nonresident person (includes, individuals, business entities, trusts, and estates), only employers that are not residents of Puerto Rico may meet the requirements above.

The PRIRC does not define what constitutes “economic nexus with Puerto Rico”. However, Act 52-2022 provides that the fact that an employer allows its employee to work remotely from Puerto Rico will not result in economic nexus with Puerto Rico even when:

1. The home office is necessary or required for the employment of the remote worker;
2. There is a business purpose to allow the use of the employee’s home as his/her office;
3. The employee is required to perform some basic work tasks from the employer’s office; and
4. The employer refunds some of the expenses of the home office.

Income Tax Withholding on Wages v. Estimated Tax Payments

Act 52-2022 substituted the employer’s requirement of withholding Puerto Rico income tax on wages for a requirement to the employee to pay estimated tax during the year.

Foreign Tax Credit

Act 52-2022 introduced a new foreign tax credit applicable to remote workers. The remote workers that

ABOUT THE AUTHOR Felipe Mariani-Franco

Felipe is a Member at Alvarado Tax & Business Advisors. His Curriculum Vitae includes previous experience in the corporate and individual tax advisory area with an international and a local firm.

Felipe has extensive experience in corporate tax advisory for the retail, distribution and manufacturing industries. Among his areas of expertise, Felipe works with corporate tax incentives, corporate reorganizations, closing agreements with governmental entities, consumption tax issues and tax accounting work. As per his involvement with government, Felipe has participated in special projects related to the drafting of tax related laws, ordinances and regulations for the Commonwealth of Puerto Rico, Municipalities and private entities.

He is frequently invited as speaker at many tax seminars sponsored by the Puerto Rico Society of Certified Public Accountants and other professional associations and private organizations.

Felipe is member of the Puerto Rico Certified Public Accountants Society and the American Institute of Certified Public Accountants. He has a Master in Professional Accounting degree, major in Taxes, from the University of Texas at Austin and a Bachelor in Business Administration degree, major in Accounting, from the University of Puerto Rico.

paid income tax to any possession or State will be able to consider it for purposes of the foreign tax credit if the possessions or States have a source of income rule for salary which is based on the employer’s residence or place of business.

However, remote workers should not assume that they will be able to credit in Puerto Rico the totality of income tax they pay to a possession

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or a State. There are rules that limit the amount of foreign tax credits that may be claimed which may result in a lower credit or even no foreign tax credit at all.

The Pitfalls

Even when Act 52-2022 made substantial and important changes which will affect remote workers and their employers, there are some areas which need clarifications and others that need to be addressed through legislation.

- **Definition of the terms “Economic Nexus” and “Nexus”**
– The companies evaluating if they meet the requirements not to be considered engaged in trade or business must examine whether they or their clients have the minimal contacts with Puerto Rico which result in “economic nexus” or “nexus”, respectively. Since the terms are not defined, this determination may be a challenge in some situations where there are some contacts between the company or its clients with Puerto Rico.
- **Merchant for purposes of Sales and Use Tax** – All businesses that currently are considered a merchant for sales and use tax but that are not engaged in trade or business in Puerto Rico will be excluded from the possibility of not being considered engaged in trade or business if they have remote workers in Puerto Rico. Some of those businesses are in the technological sector of the economy and might have been an important source of remote workers.
- **Personal property taxes, municipal gross receipt tax and other taxes** – Act 52-2022 does not amend the Municipal Code or other tax laws to provide rules for companies with remote workers. That means, that the companies will need to evaluate their specific situation under the provisions of each law to determine the possible registration and compliance requirements, and the tax impact, if any.

- **Payroll taxes** – All Puerto Rico payroll taxes, except for the income tax withholding on wages, may be applicable to remote workers. Therefore, the employer needs to evaluate which of them are applicable and what are their registration and compliance requirements. Furthermore, they will need to determine which resources they need to comply with those.
- **Employment laws** – Although this is outside of our area of expertise, Act 52-2022 does not address any exclusion to Puerto Rico employment laws. Therefore, employers of remote workers should assess their responsibilities under each law (a task best tackled with an employment lawyer).

ATBA Comments:

There is a common say that states that “the times they are a-changin’” and that is not truer than in the way we are doing business. We are leveraging technology and adopting it in a very fast phase. That has also been the case of how we perform our work. Nowadays, we are moving from the office building to the virtual office and only need Internet access and a secure VPN to work from anywhere. However, usually laws, and specially tax laws, move at a different pace. The fact that the Government of Puerto Rico has identified the issue and the need to be addressed should be commended. Now it is time to build on the foundation of Act 52-2022, address the areas which need to be clarified and provide a legislation that attract remote workers and their employees.

Is your business is considering allowing remote work from Puerto Rico, our tax professionals at Alvarado Tax and Business Advisors LLC are ready to assist you.

Alvarado Tax & Business Advisors LLC

104 Acuarela Marginal Street
Martinez Nadal Expressway
Guaynabo PR 00969


PO Box 195598
San Juan PR 00919-5598

T. 787.999.4400
F. 787.999.4646

E. taxadvisors@alvatax.com
www.alvatax.com
www.taxand.com

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Key Contacts at Alvarado Tax & Business Advisors LLC

Juan A. Alvarado-Zayas, Esq., CPA

Managing Member
787-620-7730
jalvarado@alvatax.com

Felipe Mariani-Franco, CPA

Member
787-620-7736
fmariani@alvatax.com

Sandra Marie Torres- Martínez, CPA

Member
787-620-7728
storres@alvatax.com

Carlos R. González-Martínez, CPA

Member
787-620-7739
cgonzalez@alvatax.com

César De Jesús-Umpierre, CPA

Member
787-620-7734
cdejesus@alvatax.com

Rosirma García-Rivera, CPA

Member
787-620-7733
rgarcia@alvatax.com

Coralí Del Llano-Torres, Esq., CPA

Member
787-999-3011
cllano@alvatax.com

Elisa Vélez-Pérez, Esq., CPA

Member
787-999-3001
evelez@alvatax.com

Luis Torres-Llompарт, CPA

Director
787-649-4153
ltllompарт@alvatax.com

Edgardo Sanabria-Valentín, CPA

Special Advisor
787-999-3015
esanabria@alvatax.com