

## Technical Amendments Act: Income Tax Withholding and Informative Returns

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### An McV Tax Alert

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Following is a summary of the technical amendments approved by the recently enacted Act 40-2020 (“Act 40”) which incorporates technical amendments to the Puerto Rico Internal Revenue Code of 2011, as amended (“PR Code”).

This summary specifically addresses Income Tax Withholding and Informative Returns. **Unless otherwise stated, the amendments become effective as of April 17, 2020, when Act 40 was approved.**

#### I. Withholding Tax

##### Wages not Subject to Withholding Tax

As of January 1, 2019, the following payments, instead of being excluded from the definition of wages, will be considered “wages” not subject to withholding tax:

- Agricultural services;
- Housekeeping services for households, local college clubs or local chapters of a college fraternity or sorority;
- Services provided by a duly ordained, commissioned or authorized minister of a church, in the exercise of his ministry, or by a member of a religious order in the performance of duties required by that order; and
- Compensation or indemnity received by an employee by reason of termination.

##### Judicial or Extrajudicial Settlement Payments

If judicial or extrajudicial settlement payments are made to:

- Non-resident individuals:
  - The individual or entity making the payment must deduct and withhold 20% income tax in the case of U.S. citizens, and 29% in the case of non-

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U.S. citizens.

- A foreign corporation or partnership not otherwise engaged in trade or business in Puerto Rico:
- The individual or entity making the payment must deduct and withhold a 29% income tax.

The Secretary can relieve the withholding agent, in whole or in part, from its withholding obligation if he determines that the withholding will cause undue hardship because the amounts withheld will have to be reimbursed to the taxpayer or because the withholding will be excessive.

### Payments for Services Rendered

Payments made for continuing education services provided by certain entities to professionals who render Designated Professional Services, as defined by the PR Code, will not be subject to income tax withholding.

During the first three years of operations of an economic activity, a person or entity that has not obtained a withholding waiver for said activity will be deemed to have established that the withholding on payments for services rendered causes undue hardship, so that a withholding waiver will be issued by the Secretary. The fact that a taxpayer has carried out the same economic activity in another jurisdiction or has carried out another economic activity in or outside of Puerto Rico will not be taken into consideration for these purposes. However, the Secretary may deny the waiver to those who carry out substantially the same activity for which they had previously received a waiver.

### Sale of an Interest in a Partnership by Non-resident Individuals

If a non-resident person sells an interest in a partnership, the buyer (i) will be exempt from the requirement to withhold 15% on the amount of the gain that constitutes income from Puerto Rico sources if the seller obtains a waiver from the PR Treasury by establishing to the satisfaction of the Secretary that such withholding will cause undue hardship and that the amounts otherwise withheld will have to be reimbursed, or (ii) can reimburse amounts withheld when, before remitting the amounts withheld to the Secretary, (a) the non-resident person provides the buyer with a written statement issued by the Secretary stating that the seller has satisfied its tax obligation on the transaction, or (b) the Secretary determines that no gain was realized in the

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transaction and, therefore, no income tax is due.

### II. Informative Returns

*Informative Returns for Advertising, Insurance Premiums, Telecommunication, Internet Access and Cable or Satellite Television Services ("Form 480.7E")*

For taxable years beginning **after December 31, 2019**:

- Any entity that receives payments for insurance premiums, telecommunications, advertising, internet and cable services or satellite television services ("Applicable Services") will be required to provide Form 480.7E to every commercial customer on or before February 28<sup>th</sup> of the year following the payment.
- For bundled services, or when the entity's systems cannot segregate or assign the payments made by customers to the specific services provided, the entity will be required to inform all the payments received by the client (even those not related to the Applicable Services) on Form 480.7E.
- Providers of Applicable Services will not be required to provide Form 480.7E to residential customers, except upon request by any such customer.
- Taxpayers who pay for Applicable Services used in a trade or business through a residential account must request Form 480.7E from the service provider to be able to claim a deduction for said payments without being required to present an Agreed Upon Procedures Report or audited financial statements. If a request by a residential customer is submitted after January 31<sup>st</sup> of the year following the payment, the service provider will have 45 days from the date of the request to furnish the related Form 480.7E. In such cases, Form 480.7E can be furnished to the payer after February 28<sup>th</sup> of the year following the payment.

For taxable years beginning **after December 31, 2018 but before January 1, 2020**:

- Taxpayers that wish to claim a deduction for payments made for Applicable Services, but do not want to include with their return an Agreed Upon Procedures Report or audited financial statements, must file Form 480.7E on or before the filing due date of their income tax return, including extensions. Providers of Applicable Services were required to furnish, electronically or by mail, to their residential and/or commercial customers their name, address and employer identification number on or before March 31, 2020.

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- For taxable year 2019, the filing due dates for certain entities may have already been extended as a consequence of the COVID-19 emergency. For more information, please access our Tax Alert of March 26, 2020 through the following **link**.

The Secretary may exempt an Applicable Services provider from the obligation to declare payments received for which the service provider normally does not keep the information required by Form 480.7E.

Taxpayers may file an optional Form 480.7E to declare the payments made for the Applicable Services on or before the filing due date of their income tax return, including extensions.

*Informative Returns for: (1) Payments to Non-resident Individuals (Form 480.6C), (2) Interest Payments, and (3) Income Subject to Alternate Basic Tax (Form 480.6D)*

Accrual basis taxpayers and those that determine their income on a fiscal year will not be required to submit with their income tax returns a reconciliation between: (i) the expenses claimed in the return related to payments to non-resident individuals, interest payments, and payments of income subject to alternate basic tax and (ii) the amount reported in an informative return, in order to be able to claim a deduction, so long as they include with their income tax returns audited financial statements and the Supplementary Report required under the PR Code.

*Informative Return on Credit Extension Transactions - Affirmative Declaration of Transactional Amounts ("Declaration")*

The Secretary is instructed to review the information provided on the Declarations so that financial businesses may automate compliance with said requirement.

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