

PR Treasury Adopts Special Distributions Rules for Retirement Plans and IRAs to Help Victims of Recent Earthquakes in Puerto Rico

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- Employee Benefits

An McV Employee Benefits Alert

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On February 19, 2020, the Puerto Rico Treasury Department (“PR Treasury”) issued Internal Revenue Circular Letter No. 20-09 (“CL 20-09”) to establish the rules to allow participants affected by the January 7, 2020 earthquake and subsequent aftershocks (collectively, the “Natural Disaster”) to request distributions from Puerto Rico qualified retirement plans (“Retirement Plans”), and Puerto Rico Individual Retirement Accounts (“PR IRAs”), subject to a special tax treatment (“Eligible Distributions”).

Eligible Distributions must be requested by individuals who are *bona fide* residents of Puerto Rico during 2020 (“Eligible Individuals”), and must be completed during the period commencing on February 20, 2020 and ending on June 30, 2020 (“Relief Period”). Eligible Distributions must cover damages or losses suffered, and extraordinary expenses incurred, by the individual and/or members of his/her immediate family (i.e., spouse, offspring or parents) resulting from the Natural Disaster (“Eligible Expenses”). Eligible Expenses include, but are not limited to, those incurred for:

- Repairing damages caused to a residence, commercial establishment or a motor vehicle;
- Inspecting real property to ensure it meets the established building codes;
- Repairing real property in conformity with established building codes;
- Purchasing a new principal residence or a commercial establishment due to the Natural Disaster;
- Paying medical expenses;
- Replacing or repairing real estate;
- Acquiring or repairing electric power generators; or
- Paying for lodging and food due to the total or partial destruction of the principal residence, incurred during the recovery period after the Natural Disaster.

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Eligible Distributions will be subject to the tax treatment granted to distributions resulting from a disaster declaration made by the Governor of Puerto Rico under Sections 1081.01(b)(1)(D) and 1081.02(d)(1)(I) of the Puerto Rico Internal Revenue Code (“PR Code”), as follows:

- Distributions up to \$10,000 will be exempt from withholding and income tax (including the basic alternate tax).
- Distributions over \$10,000 (but not greater than \$100,000) will be subject to an income and withholding tax rate of 10% in lieu of any other tax imposed by the PR Code, including the basic alternate tax. To enjoy this benefit, the 10% tax must be withheld at the time of the distribution.
- Any portion of a distribution over \$100,000 will be taxed as a regular distribution from a Retirement Plan or PR IRA.

To qualify for the special tax treatment, Eligible Distributions must be requested and disbursed during the Relief Period, regardless of when the Eligible Expenses are actually incurred.

An Eligible Individual who desires to receive an Eligible Distribution must submit a sworn statement with the administrator/sponsor of the Retirement Plan and/or financial institution providing the PR IRA, as applicable, certifying, among others:

- Puerto Rico *bona fide* resident status for 2020 calendar year;
- Dollar amount requested as an Eligible Distribution meets the \$100,000 maximum limitation,
- Eligible Distribution will cover Eligible Expenses or will recover lost earnings after the Natural Disaster; and
- Any other Eligible Distribution(s) received, including the date(s) of such other Eligible Distribution(s), the dollar amount(s) received, and the tax(es) withheld, if any.
- Full responsibility for payment of income taxes owed if requirements for Eligible Distributions are not met.

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Eligible Distributions from Retirement Plans are optional. Employers have discretion to adopt all or part of CL 20-09. Retirement Plans incorporating distributions resulting from a disaster declaration made by the Governor of Puerto Rico in conformity with PR Code Section 1081.01(b)(1)(D) must be amended by December 31, 2020. Eligible Distributions can be approved and disbursed by the plan administrator/sponsor before the Retirement Plan is formally amended. This amendment, however, does not have to be filed with PR Treasury to update the Retirement Plan's tax qualification letter under the PR Code.

Even though PR Treasury specified that Retirement Plans incorporating PR Treasury Administrative Determination No. 17-29 of November 15, 2017 regarding Hurricane María distributions are deemed amended for CL 20-09, it is recommended that Retirement Plans allowing Eligible Distributions be amended to incorporate disaster declaration distribution rules under PR Code Section 1081.01(b)(1)(D) so they can be operated in conformity with their plan document as required under the Employee Retirement Income Security Act of 1974, as amended.

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