

Puerto Rico Tax Update

Penalty-Free Retirement Accounts' Distributions (Circular Letter No. 20-09)

February 24, 2020

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On February 19, 2020, the Puerto Rico Treasury Department issued Circular Letter No. 20-09 establishing the guidelines for the "Eligible Distributions for Disaster" (defined below) from Retirement Plans and/or Individual Retirement Accounts ("IRA"), to cover the Eligible Expenses (defined below), at a preferential tax rate.

Eligible Period –Eligible Distributions for Disaster received from **February 20, 2020 through June 30, 2020**.

Eligible Individual – The term is defined as a person that during calendar year 2020 fulfill the requirements of Section 1010.01(a)(30) of the Puerto Rico Internal Revenue Code, as amended (hereinafter referred to as "the Code"). In other words, an individual would be eligible if he or she is considered a bona fide Puerto Rico resident for the taxable year 2020.

Eligible Expenses – The term is defined as expenses, either ordinary or extraordinary, incurred by an individual, spouse, ascendants, and/or descendants, to compensate for any loss or damage, and/or to cover basic necessary needs suffered as a result of the disaster declared by the Governor of Puerto Rico (i.e., the recent earthquake's events). These expenses include but are not limited to:

- Repair costs incurred for a motor vehicle, residence and/or commercial establishment,
- Expenses incurred to certify up-to-date building codes,
- Repair and/or replacement of real property (residence or commercial property),
- Repair and/or purchase of electric power generators,
- Repair and/or replacement of personal property (furniture and fixtures),
- Medical expenses, and
- Lodging and food expenses, as a result of total or partial destruction of principal residence.

Eligible Distributions for Disaster

- Distributions from Retirement Plans and/or IRAs during the Eligible Period, by an Eligible Individual covering Eligible Expenses.
- In general terms, annuities or periodic payment distributions are not considered an Eligible Distribution.

- For Retirement Plans, the disbursement can be a total cash distribution or partial cash distributions due to extreme economic emergency.
- For IRAs, the penalties imposed by Section 1081.02(g) of the Code will not apply, however, the person may be subject to the penalties imposed by the Financial Institution or Insurance Company, in accordance to the signed contract agreement.
- The first ten thousand (\$10,000) dollars distributed during the Eligible Period will be considered tax-free.
- Distributions over the first ten thousand (\$10,000) dollars will be subject to a preferential tax rate of ten percent (10%).
- Distributions can be made from different Retirement Plans and/or IRAs, however, the aggregate amount of the total distributions made during the Eligible Period cannot exceed one-hundred thousand (\$100,000) dollars.
- Distributions over the above mentioned threshold will be taxed at applicable ordinary income tax rates.
- Distributions from Retirement Plans must be reported in Form 480.7C.
- Distributions from IRAs must be reported in Form 480.7.

Application Process

- An individual requesting an Eligible Distribution from a Retirement Plan must submit a request to the Employer or Plan Administrator, along with a Sworn Statement, by either mail, e-mail or in person, including the following information:
 - Name and postal address,
 - Principal residence address,
 - Certificate stating that:
 - The individual will be a Puerto Rico resident during the taxable year 2020.
 - The distribution requested does not exceed the threshold imposed by the Circular Letter.
 - The distribution amount requested will be used to cover expenses related to losses suffered, extraordinary expenses incurred to cover basic and necessary needs, and/or to compensate for loss of income (all due to the earthquakes). It is not required to accompany the evidence of the expenses incurred.
 - The individual has not received any other Eligible Distributions, and if they did, it must include the distribution date and amount disbursed.
 - The individual has not received exempt Eligible Distributions, and if they did, it must include the distribution date and amount disbursed.
 - If for any reason the disbursement does not qualify as an Eligible Distribution, the individual is responsible for any tax payments over the disbursed amounts.

- An individual requesting an Eligible Distribution from an IRA must submit to the Financial Institution or Insurance Company, an application by mail, e-mail or in person including the above-mentioned information, accompanied by a Sworn Statement stating the distribution is requested to cover related expenses to the recent earthquake's events.

Withholding Agent's Responsibilities

- Withhold a ten (10%) percent tax upon distributions over ten thousand (\$10,000) dollars.
- Remit the above-mentioned tax withholding to the Puerto Rico Treasury Department, on or before the fifteenth (15th) day of the month following the distribution.
- Prepare Form 480.7C and/or 480.7, as applicable.
- If there is non-compliance from the Withholding Agent, the Department may impose the penalties and fines established in the Code (i.e., Section 6080.02).

For distributions in excess of \$10,000, it is important to mention that if the 10% withholding tax is not made at source, the individual cannot claim the 10% preferential rate on the tax return. Also, it will be subject to the penalties for early withdrawal imposed by the Code.

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