

Circular Letter of Internal Revenue No. 17-05

Taxpayer Rehabilitation Program

TAX ALERT

March 2017

On March 17, 2017, the Puerto Rico Treasury Department ("Treasury") issued Circular Letter of Internal Revenue No. 17-05 ("CL IR 17-05") to implement a Taxpayer Rehabilitation Program. The Taxpayer Rehabilitation Program was designed to reform and rehabilitate taxpayers through the execution of payment plans of outstanding tax debts. With the issuance of CL IR 17-05, Treasury (i) establishes the procedures for the request and approval of payment plans under the Taxpayer Rehabilitation Program (the "Payment Plans"), and (ii) specifies the terms and conditions which will govern such Payment Plans.

Whether the Automatic Payment Plan requires a down payment and the term of the Plan will depend on the Category of debt and the amount owed. The payment terms range between 12 and 36 months and the down payment required ranges from 0% to 20% of the principal amount owed.

Payment Plan Options

Under the Taxpayer Rehabilitation Program, the Secretary of Treasury ("Secretary") will grant Payment Plans for five (5) categories of tax debts ("Categories"):

- Category I: Income Tax
- Category II: Special Temporary State Tax over Real Property (Act 7-2009)
- Category III: Sales and Use Tax ("SUT")
- Category IV: Withholding Tax at Source
- Category V: Excise Tax

The type of Payment Plan that will be granted depends of the Category of the Tax Debt and the accumulated principal amount of such tax debt. There are two (2) types of the Payment Plans: Automatic Payment Plan and Regular Payment Plan. If the principal amount of tax owed does not exceed \$50,000, the Payment Plan will be issued under the Automatic Payment Plan provisions of CL IR 17-05. For debts with principal amount exceeding \$50,000 and for Category V (excise taxes) debts, the Regular Payment Plan provisions will apply.

The Taxpayer must include in the Payment Plan all the debts assessed by Treasury. Taxpayer cannot select specific debts to be included at any Payment Plan.

1. Automatic Payment Plans

a. General Requirements

An Automatic Payment Plan does not require the evaluation of the taxpayer economic capacity for its approval but it does require the filing of a request and the execution of an agreement, as explained below. Under an Automatic Payment Plan:

- i. The taxpayer agrees to make monthly payments by direct deposit until the tax debt, including interest and surcharges (penalties may be totally or partially waived if the Plan is fully applied), within a term that depends on the Category of debt and amount owed, as follows:
 - a. **Category I (income tax)**- 24 months for debts not exceeding \$10,000 in principal amount; 36 months for debts exceeding \$10,000 but not exceeding \$50,000.
 - b. **Category II (special property tax)**- 24 months
 - c. **Categories III (SUT) and IV (withholding tax)**- 12 months for debts not exceeding \$10,000 in principal amount; 24 months for debts over \$10,000 but not exceeding \$25,000; 36 months for debts exceeding \$25,000 but not exceeding \$50,000.
- ii. The taxpayer is required to make an advance payment of a certain percentage of the principal amount owed as follows:
 - a. **Category I (income tax)**- 10% of principal if the debt exceeds \$10,000 but is lower than \$25,000; 20% of principal if the debt exceeds \$25,000 but is lower than \$50,000. No down payment for debts of up to \$10,000 in principal amount.

Automatic Payment Plans may be requested for Category I through IV tax debts not exceeding \$50,000 in principal amount and do not require consideration of taxpayer's economic capacity for repayment.

- b. **Category II (special property tax)**- No down payment required.
- c. **Categories III (SUT) and IV (withholding tax)**- 10% of principal for debts not exceeding \$10,000 in principal amount; 20% of principal for debts not exceeding \$50,000.
- iii. An Automatic Payment Plan issued in connection with Categories III (SUT) and IV (withholding tax), will require the merchant subject to the Plan to make weekly deposits of SUT in through SURI, provided the monthly deposits for SUT exceed \$2,000. This requirement will be considered satisfied if the merchant makes weekly SUT deposits of at least 90% of the total SUT for the month. If the volume of business of the merchant exceeds \$125,000, such merchant will be required to maintain a fiscal terminal in the business facilities.
- iv. The failure to comply with the Automatic Payment Plan may give rise to additional penalties and fines, including the 100% penalty established by Section 6080.02 of the Puerto Rico Internal Revenue Code of 2011. Also, in some cases, Treasury may report the tax debt to different credit bureaus and to the U.S. Treasury Offset Program. The failure to comply with the Automatic Payment Plan in the context of Categories III and IV will cause the cancellation of the Payment Plan, the imposition of fines and penalties without additional notice to the taxpayer, and may cause attachment without additional notice to the taxpayer.
- v. No collateral will be required under an Automatic Payment Plan.

b. Procedure to Request an Automatic Payment Plan

All taxpayers interested in applying for an Automatic Payment Plan must submit an application using Form AS 3509 "Application and Automatic Payment Plan Agreement - Individuals" or Form AS 3510 "Application and Automatic Payment Plan Agreement - Businesses or Corporations", as applicable. The application must be submitted via email to plandepago@hacienda.pr.gov. If an Authorized Representative is designated to help in the Automatic Payment Plan application process, a Power and Declaration of Representation (Form AS 2745) must be included.

When the application is processed, Treasury will contact the Taxpayer or the Authorized Representative to coordinate the execution of the Agreement and the Down Payment, if applicable. If a Down Payment is required, it has to be made through a direct debit. Treasury will not accept checks as Down Payment.

2. Regular Payment Plans

Taxpayers with outstanding tax debts in Categories I, III, IV exceeding \$50,000 may request a Regular Payment Plan. A Regular Payment Plan may not be requested for Category II (special property tax) debts.

With respect to Regular Payment Plans:

- i. Regular Payment Plans will be granted by Treasury only to those taxpayers who can demonstrate to the Secretary that they don't have the economic capacity to totally pay the balance owed. In order to so demonstrate, the taxpayer must submit Form AS 3325, "Balance Sheet of Individuals", or Form AS 3326, "Balance Sheet for Businesses or Corporations", as applicable, as well as additional documents, as explained below.
- ii. The down payment and the term of the Regular Payment Plan for debts in Categories I (income tax), III (SUT) and IV (withholding tax) will depend on the economic capacity of the taxpayer. However, the down payment may not be lower than 10% of the principal amount owed. The down payment and the monthly installments to be made under the Plan must be made by direct deposit.
- iii. The Secretary may require collateral as a condition for the execution of the Regular Payment Plan.
- iv. The Secretary may totally or partially waive fines or penalties that would have been otherwise owed, subject to the full compliance of the Regular Payment Plan.
- v. A Regular Payment Plan issued in connection with Categories III (SUT) and IV (withholding tax), will require the merchant subject to the Plan to make weekly deposits of SUT in through SURI, provided the monthly deposits for SUT exceed \$2,000. This requirement will be considered satisfied if the merchant makes weekly SUT deposits of at least 90% of the total SUT for the month. If the volume of business of the merchant exceeds \$125,000, such merchant will be required to maintain a fiscal terminal in the business facilities.

If the Taxpayer does not comply with the Regular Payment Plan Agreement or any tax responsibility which later arises:

- Treasury will impose all fines and penalties established in the Code without additional notification to the Taxpayer.
- Treasury will cancel the Agreement and proceed with the collection of the outstanding debt balance plus the fines and penalties which were forgiven as part of the Regular Payment Plan.

Income tax, SUT and withholding tax debts over \$50,000, and excise tax debts may be covered by a Regular Payment Plan, provided the taxpayer shows lack of economic capacity to fully satisfy the debt.

- Treasury may collect the Collateral through the attachment procedure, seizure mechanism or any other procedure established in the Code, without the need of additional notification to the Taxpayer.
- Treasury may report the tax debt to different credit bureaus and to the U.S. Treasury Offset Program.

Regular Payment Plans for Category V: Excise Tax

All taxpayers who owe an Excise Tax Debt, regardless of the principal amount due, may visit its Collection District and request a Regular Payment Plan to settle the total amount of its debt. This Category has the same Term and Conditions and default consequences as the Category I (income tax) Regular Payment Plan.

Procedure to Request Regular Payment Plans

Taxpayer interested in applying for a Regular Payment Plan must submit a letter to the Collection District Office which corresponds to the taxpayer's residential area or the physical address of the legal entity's main office. Such Application must include the following information:

- Taxpayer personal information; spouse personal information, in case of married taxpayers;
- Employer information, in case of salaried employee;
- Tax Debt Category which the Taxpayer is eligible for requesting Regular Payment Plan and the balance at the moment of the request;
- Bank account information from where the direct debit payment will be made;
- Copy of Form AS 3325 "Balance Sheet of Individuals" or Form AS 3326 "Balance Sheet for Businesses or Corporations", as applicable, and the corresponding supporting documents;
- Last 2 bank statements or investment accounts kept by the Taxpayer in financial institutions in or outside Puerto Rico;
- Copy of the debt certificate to demonstrate the type and date of the debt to be included in the Regular Payment Plan.

Effectiveness

The CL IR 17-05 provisions became effective immediately. Taxpayers may start submitting the Payment Plans applications starting on March 24, 2017.

Because of the general nature and informative purpose of this newsletter, nothing herein should be considered as legal advice or a legal opinion. For further information about the contents of this newsletter, or should you need further assistance in connection with these matters, please contact any of the attorneys of the firm's Corporate Tax Group.

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The down payment and the term of payment under a Regular Payment Plan will be established on the basis of economic capacity. The down payment may not be lower than 10% of principal amount owed. Collateral may be required.