

Puerto Rico Residency Tax Incentives and Audit Risks for U.S.-Based Individuals and Businesses

Puerto Rico Act 60, Key Issues for Taxpayers,
Navigating IRS Examination and Audits, Tax Planning

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Mr. Armitage's core practice is advising multinational corporations on transfer pricing in all contexts, from planning to cross-border dispute resolution. He has a particularly strong background interacting with tax authorities on advance pricing agreements (APAs) and Competent Authority matters for corporations in a wide range of industries. He spent eight years in the IRS Advance Pricing Agreement Program, serving as Deputy Director, where he both experienced and oversaw the full spectrum of Program activities. He helps clients address transfer pricing, valuation, permanent establishment, and other international tax issues and controversies.



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Mr. Leeds focuses his practice on the tax consequences of a variety of capital markets products and strategies. He advises on the tax aspects of capital markets, structured finance, derivatives, financial products and insurance transactions and has extensive experience working with both buyers and sellers to develop and structure complex derivatives. A significant portion of his work involves the taxation of financial products and trading strategies engaged in by banks and other financial market participants.



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Ms. Schafroth joined Caplin & Drysdale's International Tax Group as an Associate in 2020. Her practice focuses on advising individuals and businesses on a broad range of tax issues with a particular focus on international tax and transfer pricing planning and advocacy for corporate clients.

Puerto Rico Residency Tax Incentives

- Section 933, US Internal Revenue Code:

The following items shall not be included in gross income and shall be exempt from taxation under this subtitle:

- (1) Resident of Puerto Rico for entire taxable year

In the case of an individual who is a **bona fide resident of Puerto Rico** during the entire taxable year, **income derived from sources within Puerto Rico . . .**

- (2) Taxable year of change of residence from Puerto Rico

In the case of an individual citizen of the United States who has been a **bona fide resident of Puerto Rico** for a period of at least 2 years before the date on which he changes his residence from Puerto Rico, **income derived from sources therein . . .** attributable to that part of such period of Puerto Rican residence before such date . . .

- Puerto Rico Act 60 (July 1, 2019)

Section 2032.02(a)(1): The net income derived from Export of Services or Promoter Services, as provided in subsection (a) of Section 2031.01 of this Code, shall be subject to a **flat preferential income tax rate** of four percent (4%) in lieu of any other income tax, if any, provided by the Puerto Rico Internal Revenue Code or any other law. . . .

IRS Campaigns: Background

- **Congressional Letter.** In December 2019, members of Congress sent a letter to Treasury secretary expressing concerns about benefits of US tax laws for taxpayers that become residents of Puerto Rico
- **IRS Report.** At the same time, Congress directed the IRS to determine the number of individuals that had relocated to Puerto Rico since 2012 and been granted tax exemptions under Act 22
 - IRS identified 2,331 individuals who had obtained Act 22 benefits from 2012-2019
- **Criminal Indictment.** In October 2020, a CPA with a large accounting firm was indicted on charges related to assisting clients fraudulently obtain benefits associated with Act 22
- **IRS Activity.** In a May 2024 interview with *The New York Times*, IRS Commissioner Danny Werfel said the IRS has audited “dozens” of taxpayers and assessed “millions of dollars” related to Puerto Rico tax incentives, with the IRS enforcement campaign in Puerto Rico only in its “early chapters”

IRS Campaigns

<https://www.irs.gov/businesses/corporations/lbi-active-campaigns>

Puerto Rico Act 22, Individual Investors Act

Practice Area: Withholding, Exchange & International Individual Compliance

Lead Executive: Orrin Byrd, Director, Withholding & International Individual Compliance

Campaign Point of Contact: Ursula Gee, Program Manager, Withholding, Exchange & International Individual Compliance

This campaign addresses taxpayers who have claimed benefits through Puerto Rico Act 22, "Act to Promote the Relocation of Individual Investors to Puerto Rico", without meeting the requirements of IRC Section 937, Residence and Source Rules Involving Possessions. As a result, these individuals may be excluding income subject to US tax on a filed US income tax return or failing to file and report income subject to US tax. This campaign will also address those individuals who have met the requirements of IRC Section 937 but may be erroneously reporting US source income as Puerto Rico source income in order to avoid US taxation. The objective of this campaign is to address noncompliance in this area through a variety of treatment streams including examinations, outreach and soft letters.

Financial service entities engaged in a U.S. trade or business campaign

Practice Area: Cross Border Activities

Lead Executive: Deborah Palacheck, Director, Cross Border Activities

Campaign Point of Contact: Cindy Kim, Program Manager, Cross Border Activities

This campaign addresses whether foreign investors were subject to U.S. tax on effectively connected income from lending transactions engaged in through a U.S. trade or business. In general, foreign investors who only trade stocks and securities for their own account are not engaged in a U.S. trade or business under the safe harbor rule set forth in 26 USC 864(b)(2). The safe harbor rule, however, is not available to dealers in stocks or securities, or to entities engaged in a lending business, or to foreign investors in partnerships engaged in such activities. The treatment stream for this campaign is issue-based examinations.

IRS Campaigns

- Features of IRS Campaigns:
 - Coordinated and centralized issue focused examinations
 - IRS agents are trained in the specific substantive areas
 - IRS agents report to centralized managers
 - Centralized managers are coordinated and seek consist procedures and examination results across all open examinations
 - Pattern information document requests ("IDR") issued to every taxpayer under examination
 - Follow-up summons issued if IDR is not responded to in a timely and/or complete manner
 - Third-party summonses issued to banks, investment accounts, unrelated parties, and potentially advisers
- Experience with IRS Campaigns:
 - So-called "Syndicated Conservation Easements"
 - So-called "Micro-Captive Insurance Companies"
 - Puerto Rico Residency and Sourcing Examinations

IRS Campaigns: Pattern IDR – Residency Questions

10. Copies of the following Puerto Rico tax returns and information return forms filed with the **Departamento de Hacienda de Puerto Rico**:

A. Complete copies of all individual Puerto Rico income tax returns, including all schedules and attached information returns, filed by you for the year(s) 2016 – 2021.

B. Complete copies of any Puerto Rico corporation tax returns, including all schedules and attached information returns, for the year(s) 2016 – 2021 for each non-publicly traded corporation of which you owned directly or indirectly any class of stock of the corporation.

C. Complete copies of any Puerto Rico partnership returns, including all schedules and attached information returns for the years 2016 – 2021 for each partnership, domestic or foreign, of which you owned directly or indirectly a partnership interest in.

D. Complete copies of any Estate and Trust returns, including all schedules and attached information returns for which were the fiduciary, grantor, creator, director or a beneficiary of the Estate or Trust for the years 2016 – 2021.

11. Copies of any Forms 1099-, and/or the equivalent Form 480 series used in Puerto Rico, received for the years 2016 – 2021 and not previously provided for either U.S. or Puerto Rico tax purposes.

12. All insurance contracts, whether life, medical, automobile, liability, homeowners, etc., in force during the 2016 – 2021 years, which were the owner, the insured or the beneficiary.

13. All closing DOCUMENTS for all real estate purchases and/or sales made by during the years 2016 – 2021.

14. All leases in effect for the years 2016 – 2021, which was the Lessor (or had authority to execute on behalf of the Lessor), or the Lessee (or had authority to execute on behalf of the Lessee).

15. All homestead exemptions filed by or in effect for for the years 2016 – 2021.

IRS Campaigns: Pattern IDR – Residency Questions

16. Copies of all property tax bills paid by or on behalf of [REDACTED] for the years 2016 – 2021, including records to substantiate the payment method used to pay the property taxes.
17. Voter registration cards in effect for the years 2016 – 2021.
18. Driver's license and the registration cards for all vehicles registered in [REDACTED] name for the years 2016 – 2021.
19. All records substantiating social, political, cultural, or religious organizations in which [REDACTED] was a member during 2016 – 2021.
20. All DOCUMENTS related to [REDACTED] change in residency from the U.S. to Puerto Rico, including, but not limited to, invoices for: airline tickets, fees paid to commercial moving companies for moving of automobiles, furniture, personal belongings, and all other physical assets, travel agency services, berthing of personal yachts and other watercraft, hanger or other storage and maintenance of personal aircraft.
21. Daily business and personal planners, calendars, or any other form or device that documents all days [REDACTED] spent in Puerto Rico or elsewhere and the reason or circumstances for his presence in each location, for the years 2016 – 2018. Provide all DOCUMENTS related to these trips including, but not limited to, invoices for: airline travel, hotel/resort/logging accommodations, travel agency services, automobile rentals, vacation packages, deposits and monthly rental or lease of temporary and/or permanent business locations and business property or equipment.
22. Documents for all commercial flights [REDACTED] was on that took off from or landed in Puerto Rico during 2016 – 2018. These documents include but are not limited to airline tickets, receipts for purchase of any tickets, frequent flyer account records, etc.
23. Documentation for any non-commercial, corporate, or personal flights [REDACTED] was on that took off from or landed in Puerto Rico during 2016 – 2018. These documents

IRS Campaigns: Pattern IDR – Residency Questions

include but are not limited to airline tickets, receipts for purchase of any tickets, frequent flyer account records, flight logs, etc.

24. Documents for all commercial watercraft used to enter or leave Puerto Rico during 2016 – 2018. These documents include but are not limited to tickets, receipts for purchase of any tickets, account records, etc.

25. Documentation for any non-commercial, corporate, or personal watercraft used to enter or leave Puerto Rico during 2016 – 2018. These documents include but are not limited to tickets, receipts for purchase of any tickets, account records, captain, or similar, logs, etc.

26. All telephone and cellular phone statements for all phones used by for the years 2016 – 2021. These copies should include all pages included with each billing statement and contain details of calls and text messages made and received by that would include location while utilizing the phone or text message features.

Please note that additional items may be requested as needed during the examination.

Bona Fide Residency Tests: Presence Test

Section 937 of the US Tax Code provides that an individual qualifies as a Bona Fide Resident of Puerto Rico only if the person meets **ALL** of the following three tests:

- Presence Test
- Tax Home Test
- Closer Connection Test

Presence Test: The Presence Test can be met in **any** of five ways:

- The individual is present in Puerto Rico ("PR") at least 183 days during the taxable year;
- The individual is present in PR a minimum of 549 days during the three year period that includes the current taxable year and the two preceding taxable years, as long as the individual is also present in PR for a minimum of 60 day during each year of the three year period;
- The individual's presence in the United States ("US") does not exceed of 90 days during the taxable year;
- The individual generates no "earned income" from sources within the US (i.e., compensation for labor or personal services rendered by the individual in the US in excess of \$3,000), and is present in Puerto Rico for more days than in the US; or
- The individual has "no significant connection" to the US.

Bona Fide Residency Tests: Presence Test

Presence Test: Counting “days of presence in Puerto Rico”:

- Physical presence in Puerto Rico for any length of time during a given day counts as a “day” in PR
- Physical presence in the US for any length of time during a given day counts as a “day” in the US, except that if on the same day the individual is also present in PR, the presence in the US does not count as a day of presence in the US
- Any day that an individual is outside PR to receive or to accompany a parent, spouse or child who is receiving “qualified medical treatment” (in-patient care in a hospital or hospice) will be considered as a “day of presence” in PR
- Any day during a 14-day period within which an individual is outside PR because he/she has left or is unable to return due to a major disaster (i.e. FEMA/Presidential declaration State of Disaster) will be considered as a “day of presence” in PR
- Days spent in transit between two points outside of the US do not count as a day in the US, so long as the presence in the US is less than 24 hours
- Days in the US as a student (as defined in US-IRC §152(f)(2)) do not count as “days of presence” in the US
- Days in the US serving as an elective representative of PR, or as a full time elected or appointed official or employee of the PR Government, do not count as “days of presence” in the US
- Physical presence in PR and in another US possession (i.e., US Virgin Islands) on the same day, count as a “day of presence” in PR if the tax home of the individual is in PR

Bona Fide Residency Tests: Tax Home Test

Tax Home Test: This test is met if the individual does not have a tax home outside Puerto Rico for any part of the taxable year.

- A person's "tax home" is that individual's regular or principal place of business that is claimed by the taxpayer for purposes of determining income tax deductions for traveling expenses while away from home in the pursuit of a trade or business.
- If the individual does not have a regular or principal place of business—because the individual is not engaged in a trade or business or does not conduct it at any principal place—then the tax home is the individual's regular place of abode in a real and substantial sense.

Bona Fide Residency Tests: Closer Connection Test

Closer Connection Test: This test is met if the individual has a closer connection with Puerto Rico than with the United States or a foreign country. It is a facts-and-circumstances test, with the following factors specifically identified (IRS Publication 570):

- The location of the individual's permanent home
- The location of the individual's family
- The location of personal belongings, such as automobiles, furniture, clothing and jewelry owned by the individual and that individual's family
- The location of social, political, cultural or religious organizations with which the individual has a current relationship
- The location where the individual conducts his/her routine personal banking activities
- The location where the individual conducts business activities (other than those relevant to the individual's tax home)
- The location of the jurisdiction in which the individual holds a driver's license
- The location of the jurisdiction in which the individual votes
- The location of charitable organizations to which the individual contributes
- The country of residence designated by the individual on official government forms, documents and tax returns
- The types of official forms and documents the individual files, such as Form W-8BEN or Form W-9

US Taxation of Capital Gains from Puerto Rico Sources

“[T]he principles of sections 861 through 865 and the regulations under those provisions . . . generally will be applied in determining the gross and the taxable income from sources within and without [Puerto Rico]. In the application of such principles, it generally will be sufficient to substitute, where appropriate, [“Puerto Rico”] for the term “United States.” Treasury Regulation §1.937-2(b).

“Except as otherwise provided in this section, income from the sale of personal property . . . by a [Puerto Rico] resident shall be sourced in [Puerto Rico].” Section 865, applying Treasury Regulation §1.937-2(b).

US Taxation of Capital Gains from Puerto Rico Sources

Exceptions to exemption of capital gains from US taxation:

- **10-Year Lookback Rule:** “[I]ncome from sources within [Puerto Rico] will not include gains from the disposition of property described in paragraph (f)(1)(ii) of this section by an individual described in paragraph (f)(1)(iii) of this section.” Treas. Reg. §1.937-2(f)(1)(i).
 - **What kind of “property”?** “Property . . . of a kind described in section 731(c)(3)(C)(i) or 954(c)(1)(B) . . . [if the] property was owned by the individual before such individual became a bona fide resident of Puerto Rico.”
 - **Which “individuals”?** The 10-year rule applies to a bona fide resident of Puerto Rico is “[f]or any of the 10 years preceding [the taxable] year, the individual was a citizen or resident of the United States (other than a bona fide resident of [Puerto Rico]).”
 - **Election to split-source gains:** Marketable securities vs. other property. Treas. Reg. §1.937-2(f)(1)(vi).
- **Treatment of losses:** Generally follows sourcing of gains. Treas. Reg. §1.865-2(a)(1).
- **US and Foreign Office Rules:** US and foreign sourcing of gains “attributable” to US and foreign offices, respectively. IRC §§865(e)(1)(A) and 865(e)(2)(A).
- **FIRPTA:** Gains on US real property interests are US source. IRC §861(a)(5).

US Taxation of Puerto Rico Corporations

A Puerto Rico LLC is, by default, a **foreign** corporation:

- The US taxes foreign corporations on their “ECI”: “A foreign corporation **engaged in trade or business within the United States** during the taxable year shall be taxable as provided in section 11. . . on its taxable **income which is effectively connected** with the conduct of a trade or business within the United States.” IRC § 882(a).
- The US also taxes foreign corporations on certain US source income: “there is hereby imposed for each taxable year a tax of 30 percent of the amount received from sources within the United States by a foreign corporation as . . . interest . . . , dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, and other fixed or determinable annual or periodical gains, profits, and income.” IRC § 881(a).

US Taxation of Puerto Rico Corporations

When is a foreign corporation engaged in a US trade or business?

- Section 864(b), Internal Revenue Code:
 - “. . . the term ‘trade or business within the United States’ includes the performance of personal services within the United States at any time within the taxable year”
 - “. . . but does not include . . . [t]he performance of personal services . . . for a . . . foreign corporation, not engaged in trade or business within the United States . . . by a nonresident alien individual temporarily present in the United States for a period or periods not exceeding a total of 90 days during the taxable year and whose compensation for such services does not exceed in the aggregate \$3,000.”
- “Regular and continuous activities directed at income or profit are, by definition, activities of a trade or business. If those activities are conducted in the United States and are outside the judicially created exception for investment and the statutory safe harbor for trading, then the activities are those of a US trade or business.” *YA Global Investments, LP v. Commissioner*, 161 T.C. No. 11 (2023)
- No US-Puerto Rico treaty to heighten nexus threshold

US Taxation of Puerto Rico Corporations

- “Doing Business in the US” Tax Risks
 - If a PR corporation is treated as engaged in the conduct of a US trade or business, interest income “effectively connected” to such trade or business will be subject to US net basis taxation
- Dividends are subject to a 10% withholding tax
- Interest Subject to 30% US Withholding
 - Participating Interest
 - Interest received from 10%-owned affiliates
- Withholding Tax Free Interest Income
 - Portfolio Interest
 - Short-Term Interest
 - Bank Deposit Interest

US Taxation of Puerto Rico Corporations

- Rules for determining whether income is US-source income or ECI to a US trade or business apply for purposes of determining whether income is Puerto Rico source income or ECI with a Puerto Rico trade or business
- Income treated as “US-source income” is excluded from Puerto Rico-source income even if it is earned in connection with a Puerto Rico Trade or Business
- Interest and dividend income is sourced to the residence of the payer of such income
- Income from sale of goods traditionally has been sourced under title passage rule.
 - 2017 Tax Act relaxes title passage rule, provided that no US office is involved with the sale.
- Source rules for patents and other IP look to where the IP is used.
- Internet services may still look to where servers are located under specific circumstances.

US Taxation of Puerto Rico Corporations

- A non-US person is subject to tax on its income that is effectively connected with the conduct of a US trade or business (“USTB”) under rules that are substantially similar to those applicable to a US person
 - Treas. Reg. § 1.882-5
 - Imputation of agent activities
- Lending money on a regular and continuous basis in the US will be treated as the conduct of a US trade or business
- Buying loans in secondary and tertiary market transactions should not be treated as trade or business activities

US Taxation of Puerto Rico Corporations

Imputation of agent activities:

- Authorities attribute activities of agents to the foreign person, when this imputation will occur is uncertain.
- If the agent is an independent agent, it is less likely that the agent's activities will be imputed to the non-US principal.
 - There have been instances in which the Internal Revenue Service has been successful in imputing an independent agent's activities to a principal. *De Amodio v. Comm'r*, 34 T.C. 894 (1960), *aff'd*, 299 F.2d 623 (3rd Cir. 1962).
- If the agent is a dependent agent, its activities will be imputed to the non-US principal.

US Taxation of Puerto Rico Corporations

Lending as a US trade or business:

- Two non-binding authorities issued to date:
 - Generic Legal Advice Memorandum 2009-010 (Sept. 22, 2009) (the “GLAM”)
 - Internal Legal Memorandum 201501013 (Sept. 5, 2014) (the “ILM”)
- In the GLAM, the IRS determined that a foreign corporation was engaged in a USTB and recognized ECI as a result of lending activities (solicitation, due diligence, and negotiation with borrowers) attributed to the foreign corporation through an independent agent in the US
- In the ILM, the IRS concluded that a foreign fund engaged in “lending” and “underwriting” activities that constituted a USTB not covered by the trading safe harbors.

US Taxation of Puerto Rico Corporations

Avoiding a US trade or business:

- Place of performance of services.
- The CEO Rule: “R, a foreign holding company, owns all of the voting stock in five corporations, two of which are [US] corporations. All of the subsidiary corporations are engaged in the active conduct of a trade or business. R has an office in the United States where its chief executive officer, who is also the chief executive officer of one of the [US] corporations, spends a substantial portion of the taxable year supervising R's investment in its operating subsidiaries and performing his function as chief executive officer of the [US] operating subsidiary. R is not considered to be engaged in a trade or business in the United States during the taxable year by reason of the activities carried on in the United States by its chief executive officer in the supervision of its investment in its operating subsidiary corporation.” Treas. Reg. §1.864-3(b), Example 2.
- Multiple service provider entities.
- Branch structure.

US Taxation of Puerto Rico Corporations

Filing obligation if engaged in a US trade or business:

- 1120-F: Income tax return for a “F”oreign corporation
- Penalties for non-filing may include accuracy-related, late payment and denial of deductions penalties.
- Underpayment interest will be due.
- Protective 1120-F: “If a foreign corporation conducts limited activities in the United States in a taxable year which the foreign corporation determines does not give rise to gross income which is effectively connected with the conduct of a trade or business within the United States . . . , the foreign corporation may nonetheless file a return for that taxable year on a timely basis . . . and thereby protect the right to receive the benefit of the deductions and credits attributable to that gross income if it is later determined, after the return was filed, that the original determination was incorrect.” Treas. Reg. §1.882-4(a)(3)(vi).

US Taxation of Puerto Rico Corporations

How much ECI?

- Personal services:
 - “In the case of compensation for labor or personal services performed partly within and partly without the United States by a person other than an individual, the part of that compensation that is attributable to the labor or personal services performed within the United States, and that is therefore included in gross income as income from sources within the United States, is determined on the basis [of] the facts and circumstances of the particular case. In many cases, the facts and circumstances will be such that an **apportionment on the time basis.**” Treas. Reg. §1.861-4(b)(1)(i).
 - “The amount of compensation for labor or personal services performed within the United States determined on a time basis is the amount that bears the same relation to the individual's total compensation as the **number of days** of performance of the labor or personal services by the individual within the United States bears to his or her total number of days of performance of labor or personal services. A **unit of time less than a day** may be appropriate for purposes of this calculation.” Treas. Reg. §1.861-4(b)(1)(ii)(E).

US Taxation of Puerto Rico Corporations

- **Corporate income tax:** “A tax is hereby imposed for each taxable year on the taxable income of every corporation. . . . The amount of the tax imposed . . . shall be **21 percent** of taxable income.” IRC §11(a) and (b).
- **Branch profits tax:** “In addition to the tax imposed by section 882 for any taxable year, there is hereby imposed on any foreign corporation a tax equal to **30 percent** of the dividend equivalent amount for the taxable year. . . . [T]he term ‘dividend equivalent amount’ means the foreign corporation’s effectively connected earnings and profits for the taxable year.” IRC §884(a) and (b)/
- **Dividend tax** also may apply at 23.8%, including the highest capital gains rate and the NIIT:
 - “With respect to any possessions shareholder, only the possessions source ratio of any dividend paid or accrued by a corporation created or organized in a possession (possessions corporation) will be treated as income from sources within such possession. . . . The possessions source ratio will be a fraction, the numerator of which is the gross income of the possessions corporation from sources within the possession . . . and the denominator of which is the total gross income of the corporation.” Treas. Reg. §1.937-2(g)(1)(i).
 - “The entire amount of any dividend . . . will be treated as income from sources within the possession [if] 80 percent or more of the gross income of the corporation . . . was derived from sources within . . . or was effectively connected with the conduct of a trade or business in such possession . . . And 50 percent or more of the gross income . . . was derived from the active conduct of a trade or business within such possession. Treas. Reg. §1.937-2(g)(1)(ii).
- The overall effective tax rate could be as high as about 58%.

US Taxation of Puerto Rico Corporations

Application of transfer pricing principles:

- “In any case of two or more organizations, trades, or businesses (whether or not incorporated, whether or not organized in the United States, and whether or not affiliated) owned or controlled directly or indirectly by the same interests, the Secretary may distribute, apportion, or allocate gross income, deductions, credits, or allowances between or among such organizations, trades, or businesses, if he determines that such distribution, apportionment, or allocation is necessary in order to prevent evasion of taxes or clearly to reflect the income of any of such organizations, trades, or businesses.” Section 482, Internal Revenue Code
- Application as between:
 - A Puerto Rico corporation and its shareholder
 - A Puerto Rico corporation and its US branch

Are IRS Puerto Rico Regulations Vulnerable?

- *Loper Bright Enterprises v. Raimondo*, 603 U.S. __ (2024):
 - “Does the statute authorize the challenged agency action?”
 - “When the best reading of a statute is that it delegates discretionary authority to an agency, the role of the reviewing court under the APA is, as always, to independently interpret the statute and effectuate the will of Congress subject to constitutional limits.”
- Regulatory issues in Puerto Rico:
 - §937(b)(1): “Source rules. Except as provided in regulations”
 - **10-year lookback rule**: Treas. Reg. §1.937-2(f).
 - **80/50 dividend sourcing rule**: Treas. Reg. §1.937-2(g).
 - Treatment of US-source income or ECI as not Puerto Rico ECI (other than inventory): Treas. Reg. §1.937-3(b).
 - §864(c)(8): “The Secretary shall prescribe such regulations or other guidance as the Secretary determines appropriate”
 - Formulary ECI allocation for sale of a partnership interest by a foreign (PR) corporation or nonresident alien individual: Treas. Reg. §1.864(c)(8)-1.

US Taxation of Puerto Rico Corporations

Sourcing services income to Puerto Rico and benefiting from Act 60 can require more than creating a Puerto Rico entity:

- Entity classification
- Time basis apportionment
- US trade or business
- Effectively connected income
- Export services and services incidental thereto
- Obligation to report Puerto Rico-source income on a US tax return

Audit Risks for US-Based Individuals and Businesses

- Bona Fide Residency
 - Presence Test
 - Tax Home Test
 - Closer Connection Test
- Sourcing
 - Capital Gains
 - US Trade or Business
 - Imputation of Agent Activities
 - Loan Acquisitions

Thank You!



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