

# *Kevane mailbag*

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Our Kevane mailbag is your link to all our communications related to the operations of businesses in Puerto Rico. Our purpose is to offer you up-to-date information concerning tax, accounting and any other matters that might have an impact on the way you conduct business in Puerto Rico.

The Alerts contained in our mailbags can also be accessed through our website under the Publications tab\Professional Articles section or by downloading our business and tax application for mobile, tablets and iPad for free through the App Store and Google Play. We welcome your feedback at [kgt@pr.gt.com](mailto:kgt@pr.gt.com)

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## Audit

This month we refer to the FASB discussion over income tax disclosures which is one of its four ongoing projects.

 Read more

## Tax

We provide you with various tools to help you stay abreast of the VAT changes and basics.

 Read more

## Advisory

Turnaround “apps” to tackle the increasingly complex problems in Puerto Rico’s public sector.

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## Outsourcing

Employees have the option to decide the method thru which the employer will deduct their income tax from wages earned.

 Read more

## General Information

Remember you can download our 2016 Tax Calendar from our website [www.kevane.com](http://www.kevane.com). An excellent tool to stay up-to-date on individuals, businesses and other entities returns filing due dates.

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# Audit Alert: FASB deliberates income tax disclosures

The Financial Accounting Standards Board [met](#) on March 23 to discuss various issues related to four of its ongoing projects: income tax disclosures, hedge accounting, not-for-profit financial statements, and long-duration insurance contracts. The Board made tentative decisions and took the actions summarized below for each project.

## Disclosure framework: income tax disclosures

The Board continued its initial deliberations on disclosure requirements for income taxes and tentatively decided to require all entities to (1) disaggregate income tax expense (benefit) between domestic and foreign amounts, and (2) separately disclose foreign income taxes paid to any country that are significant to total income taxes paid. The Board also tentatively decided to require prospective transition for all income tax disclosures.

In addition, the Board affirmed prior tentative decisions that would require an entity to disclose certain changes in tax law with a probable future financial impact, as well as income (loss) before income tax expense (benefit) and income taxes paid, disaggregated between domestic and foreign amounts.

The Board further clarified prior tentative decisions related to disclosing the amounts of, and explanations for, a change in assertion about the temporary difference for the cumulative amount of investments associated with undistributed foreign earnings.

Prior tentative decisions were reversed that would have required all entities to disclose both the line item on the balance sheet that includes deferred income taxes and domestic tax expense (benefit) on foreign-sourced earnings. The Board also reversed a tentative decision that would have required non-public entities to provide a rate reconciliation, explanation of valuation allowance changes, and certain information related to operating loss and tax credit carry forwards.

The Board directed the staff to perform further outreach on disclosing certain assets related to the temporary difference for the cumulative amount of investments associated with undistributed foreign earnings that are essentially permanent in nature.

Source: Grant Thornton, *On The Horizon*, March 31, 2016

**We are committed to keep you updated of all developments that may affect the way you do business in Puerto Rico. Please contact us should we may be of further assistance in relation to this or any other matter.**



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# Tax Insights: Value added tax developments and basics

Considering the importance of the new tax system - Value Added Tax (“VAT”) - that will become effective on June 1, and its impact on your business, we provide you with various tools we have developed through which you can stay abreast of the VAT basics and changes. Our publications and materials in our website – [www.kevane.com](http://www.kevane.com) - will give you fundamental concepts to manage this new system.

## Insight into value added tax

Through a series of tax articles, we explain the terms introduced and progress of the new tax system since its approval.

### Insight into value added tax



Getting to understand the proposed value added tax (VAT) in Puerto Rico.  
[Read more](#)

## Industry guides

Through a series of eight articles by industry, we explain the changes the new tax system brings for each of these industries.



### Value added tax – impact on the Services Industry

An IT which amends the Internal Revenue Code for a New Puerto Rico introduces a value added tax system in Puerto Rico that will replace the Sales and Use tax system (“SUT”) effective April 1, 2016, for some tax purposes. The SUT will continue to be in place for municipal tax purposes after March 31, 2016.

From a municipal point of view, the sales and use tax will continue to be U.S. Services to other municipalities and designated professional services will be exempt from the municipal tax.



## Webcasts hosted

You can access our past webcasts recordings through our YouTube channel. These include:

- June 2, 2015 - Tax Reform Process Act 72-2015 P de la C. 2482**  
<https://youtu.be/DpmjoNhDQWk>
- June 24, 2015 - SUT Transition Period**  
<https://youtu.be/Oa3eKTVAkFk>
- August 12, 2015 - General Aspects**  
<https://youtu.be/AqtQqMliuyg>
- August 19, 2015 – Accounting methods, fiscal invoice, adjustments and debit/credit notes**  
[https://youtu.be/utro1g\\_O0iU](https://youtu.be/utro1g_O0iU)
- August 26, 2015 – Filings, documentation, certificates and taxable transactions**  
<https://youtu.be/LQ7ykQ4I8e8>
- September 2, 2015 – Implementation process**  
<https://youtu.be/ErDofopmfGw>

Contact our Tax Department should you require additional information regarding this or any other tax issue. We will be glad to assist you.



## Contact us

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# Advisory Alert: Turnaround “apps” for the public sector - the Strategy platform

## Introduction

A successful restructuring process calls for a clear action plan. Restructuring activities must be objective and analytical – in other words, apolitical. Back in June 2015, we published a [piece](#) that addressed the need for pragmatic and simple solutions to tackle increasingly complex problems in Puerto Rico’s public sector. These solutions come in the form of turnaround “apps” in four platforms for executing turnarounds in the public sector, and includes:

- Strategy
- Operations
- Finance
- Leadership

In the next series of articles, we aim to further explore the platforms of these turnaround “apps” to offer the government constructive suggestions on addressing important issues and resolving complex economic and service issues in the current difficult environment.

## The strategy platform

Every private enterprise has a mission; government, too, has a mission, which is often defined in local charters and constitutions. Current leadership interprets the mission, and public policy embodies the prioritization and execution. Public policy is the strategy of government, but government units need to adopt corporate-like strategic planning in order to allocate scarce resources and manage constituents’ expectations most effectively.

## Strategy app #1:

### Determining core services

Defining government’s core services is at the heart of any governmental restructuring effort. For example, all governments share a common concern for public safety that is reflected in the strength of their police and fire departments. One or several school districts often claim a major portion of the local budget but the quality of the educational program will vary with the allocation of budget dollars, demographic mix of the students and the capability of the teachers. Infrastructure in the form of roads, bridges and buildings, along with related maintenance, is generally in the exclusive purview of the government unit. The degree to which other services such as health care, sanitation, environmental management and business regulation should be prioritized is usually subject to debate and prevailing political sentiment.

But, must government provide services that are often available in a community from private for-profit or nongovernmental not-for-profit organizations? In general, government units need to engage in a strategic assessment that includes a decision framework for prioritizing its activities.

The first question to be answered is this: What should be included in the government’s service offering?

The question can be answered after determining if the service is mandated by either law or public policy. If yes, the follow-



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up question is: What level or type of service is required? A government must protect the safety of the public; what about providing security for a local music festival? Is it necessary for the police to be called every time the fire department is summoned to a private residence? The answer to the first question might seem simple, but the answer to the follow-up question presents some challenges.

Governments pride themselves on their contributions to the quality of their residents' lives. The more parks, the more summer programs, the cleaner the streets, some would say, the better. As prioritization becomes less clear, the debate can turn political over public policy concerning "must-have" versus "want-to-have" programs.

#### Strategy app #2:

##### Core competencies and priorities

Having identified the strategic activities of the government unit, the next question that needs to be answered is: What are the government's core competencies? In other words, what activities does this government unit perform that are unique to the community, cannot be easily imitated or deliver value that is best in class?

In the private sector, turnaround specialists evaluate business units based on profitability and return on investments. The equivalent in the public sector is performance metrics that evaluate how effectively the program serves its purpose. In the category of "must-have" programs such as police, fire protection and schools, the departments' effectiveness can be evaluated in terms of crime rates, protection against property damage, student performance and any number of other logical, empirical metrics.

How do these departments compare with those found in other communities? Is there a

private sector alternative that can serve as a benchmark? There is an order to the analysis and economic logic in addressing the inefficiencies of the "must-have" programs that should be part of a government's core competency before addressing the "want-to-have" programs.

"Want-to-have" programs can vary from community to community and should not be assumed to be luxurious extravagances. It is often in these programs that public sector providers operate as best in class. For example, consider a city-sponsored health clinic: What is the annual cost of delivering the program? How many patients has it seen? How many jobs does it provide in the community? Has the general health index increased? Has absenteeism at work or in the schools declined as a result? What are the opportunity costs of not providing the program? What are the health care alternatives within the same and neighboring communities for the citizens who use the clinic? The evaluation of government's competency in managing this and any other program relies on benchmarking its performance against private sector alternatives and/or comparable programs in other cities.

Services that are nonessential but enriching for the community can provide an opportunity for a government to perform like a business. This is where "profit" can enter the public sector picture. Government entities should not be precluded from earning profits on their activities and creating benefits for their constituencies. For example, if the recreation department can generate enough revenue to cover its expenses from user fees, it may be able to offer summer programs to disadvantaged youth at little or no cost.

As with any strong business, the "must-have" programs should be analyzed and restructured in a way that maximizes their efficacy. The

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“want-to-have” programs often generate political conflict that can lead to systemic breakdown and inefficiency. Experts recognize that the trouble with evaluating disparate “want-to-have” programs is that there are rarely common criteria around which to measure performance or value. The metrics for a health care clinic are not comparable to those used in evaluating the parks and recreation department that manages parade permits. The number of citizens served may be the most readily identified metric. This “for the greater good” approach, however, can easily overrun the needs of underserved populations. And in the world of performance metrics, the measure of our humanity may be the ability to afford social programs that help just a few.

The tragedy is when government’s inefficiency precludes the ability to deliver an important, albeit uneconomic, humanitarian program. Nevertheless, to be successful, an appreciation of the political and humanitarian landscape is required.

In our next article we will talk about turnaround “apps” for governments in the **Operations platform**.



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# Outsourcing Alert: Withholding Exemption Certificate (Form 499R-4)

The Withholding Exemption Certificate (Form 499 R-4) is the document used by employees to notify the employer of their personal exemption, exemption for dependents and/or the allowance based on deductions to determine the income tax to be withheld from the employee's wages.

If the annual gross wages of an employee does not exceed \$20,000, it will not be subject to withholding at source. However, with the elimination of the special deduction for certain individuals, it is possible that taxpayers with gross wages of \$20,000 have an income tax liability when filing their individual income tax return. Therefore, any employee may elect to request his/her employer to withhold an amount in addition to the one required by law.

## Personal exemption

- Individual taxpayer (single person, married that granted prenuptial agreement of total separation of assets or married not living with the spouse)
- Married – married taxpayer who chooses the optional computation. The personal exemption will be considered on a 50% basis for each spouse.
- Veterans – every veteran is entitled to claim an additional personal exemption.

## Exemption for dependents

The number of dependents in the Certificate shall be the same number of dependents claimed in the personal income tax return. If the employee has joint custody and has not given up the claim to this exemption, only 50% of the exemption will be considered.

## Allowance based on deductions

An employee has the option to consider in the withholding computation, the deductions that will be able to claim on his/her tax return, such as home mortgage interest, charitable contributions, medical expenses, interest paid on student loans or retirement systems, contributions to IRAs and educational IRAs, contributions to health savings accounts, casualty loss on your principal residence and loss of personal property as result of certain casualties.

The employer shall consider the information provided by the employee on this Certificate in order to make the withholding according to the Puerto Rico Department of Treasury - Employer's Guide on the Withholding of Income Tax at Source on Wages for the corresponding taxable year.

Link-Department of Treasury  
[http://www.hacienda.gobierno.pr/sites/default/files/documentos/499\\_r-4.pdf](http://www.hacienda.gobierno.pr/sites/default/files/documentos/499_r-4.pdf)



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