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Tax
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# Puerto Rico individuals 2018 year end tax planning

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With the end of 2018 in sight, November is as good a time to look ahead and consider some important tax planning aspects for the upcoming tax filing season.

### Filing status

As a general reminder, pursuant to the Puerto Rico Internal Revenue Code of 2011, as amended (the "Code"), there are three (3) ways by which individuals can file their corresponding income tax returns: (i) married; (ii) individual taxpayer; and (iii) married filing separately.

### Married couples

- may elect to file one return reporting their combined income, or the optional computation ("split") of tax to avoid higher tax brackets on combined income
- if prenuptial agreements were filed expressly stipulating that economic regime of "community property assets" is one of complete separation of property, you and your spouse will not qualify for the "married" status for income tax purposes.  Consequently, each spouse will be taxed separately as an individual taxpayer
- if one spouse dies during the year, and the surviving spouse did not remarry in said year, the surviving spouse may file a joint return up to the date of the death, and another as individual taxpayer, from the date of the death up to the end of the year
- married persons who choose to file separately should include their own income, and certain deductions must be allocated 50% to each spouse and others may be claimed fully by the spouse to whom they relate

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## Adjusted gross income

- the Adjusted Gross Income ("AGI") is equal to an individual's total gross income less a series of specific deductions
- the AGI is a key aspect of tax planning since a number of tax benefits are tied to or limited by it (e.g. mortgage interests, donations and medical expenses); therefore, a key aspect of tax planning is to estimate both your AGI for 2018 and 2019
- when considering whether to accelerate or defer income or deductions, you should be aware of the impact this action may have on your AGI and your ability to maximize deductions that are tied to the AGI. Your 2017 Income Tax Return and your 2018 pay stubs and other income- and deduction-related materials are a good starting point for estimating your AGI

## Tax brackets

- for the taxable year 2018, the tax rates for ordinary income are:

| Net taxable income | Tax rate |
|---|---|
| up to $9,000 | 0% |
| more than $9,000 but not more than $25,000 | 7% |
| more than $25,000 but not more than $41,500 | 14% |
| more than $41,500 but not more than $61,500 | 25% |
| more than $61,500 | 33% |

## Alternate basic tax

- an alternate basic tax in lieu of any other tax will be paid for each taxable year upon the Alternate Basic Tax ("ABT") income of every individual as follows:

| ABT income | Tax rate |
|---|---|
| from $150,000 to $200,000 | 10% |
| more than $200,000 but not more than $300,000 | 15% |
| more than $300,000 | 24% |

## Gift giving

- the annual gift tax exclusion for 2018 is $10,000 per donee
- if community property, each spouse separately, may use the $10,000 exclusion
- no limitation as to number of donees
- in 2017, the Code was amended to eliminate the 10% tax on gifts for those made after December 31, 2017

## Retirement savings

- the annual deductible contribution for an IRA for 2018 is $5,000 or the aggregate AGI from salaries and the earnings attributable to professions, whichever is smaller. In case of married taxpayers filing a joint return, the contribution cannot exceed $10,000 ($5,000 for each spouse). One spouse may establish an IRA in the name of the other spouse, whether if the other spouse generates income or not.

- participation in an employer pension plan does not disqualify an individual to make deductible contributions to an IRA.
- if you did not elect the maximum plan contribution for 2018, you can increase your amount for the remainder of 2018 to lower your AGI in order to take advantage of some of the deductions described above and/or lower the tax rate on the year. In addition, maximizing your contribution is generally a good tax-saving move.

## Deferring income to 2019 + accelerating deductions into 2018

If you expect your AGI to be higher in 2019 than in 2018, or if you anticipate being in the same or a higher bracket in 2018, you may benefit by deferring income into 2019 and increase deductions in 2018. Deferring income or accelerating deductions may be advantageous as long as it does not bump your income to the next tax rate bracket in 2019.

In case the deferring income or accelerating deductions is beneficial, some options include:

### Billing

If you are self-employed and using cash-basis, delay year-end billing to clients so that payments will not be received until 2019. Send last month billing a few days later, you will be paid in January 2019, instead of getting paid in December 2018.

Likewise, an alternative to accelerate deductions is to pay bills due in January 2019 before year-end and claim that deduction during 2018. For example, consider prepaying your business' property taxes and mortgage payment in December.

### Charitable contributions

Consider making a large charitable contribution in 2018, rather than in 2019.

### Year-end bonuses

If your employer generally pays year-end bonuses, request to have your bonus paid to you after the end of 2018.

### Capital gains

If you are considering selling assets that will generate a gain, postpone the sale until 2019. Also, for the sale of certain property you may consider an installment sale method.

## Accelerating income into 2018 + deferring deductions to 2019

If you anticipate being in a higher tax bracket in 2019 or perhaps you need additional income for 2018 to take advantage of an offsetting deduction or credit this tax year. Note, however, that accelerating income into 2018 will be disadvantageous if you expect to be in the same or lower tax bracket for 2019.

If accelerating income/deferring deductions will be beneficial, some options include:

### Accelerate collection of accounts receivable

If you are self-employed and report income and expenses on a cash basis, issue bills and attempt collection before the end of 2018. Also, provide an incentive that motivates your clients to pay for January 2019 invoices in advance. A good example is to honor discounts.

### Retirement plan distributions

If you are 60 years of age and participate in an employer retirement plan or have an IRA, consider making taxable withdrawals before year-end.

Capital gains

The sale of stock or other assets with taxable gains before year end.

### Deductions for individual taxpayers

- mortgage interest – limited to 30% of the AGI
- casualty loss on principal residence
- medical expenses not compensated by insurance or in any other form, exceeding 6% of the AGI
- charitable contributions – up to 50% of the AGI
- casualty losses of personal property
- contributions to a governmental pension or retirement system
- contributions to an regular IRA and educational IRA's
- contribution to health savings account
- interest paid on student loans

### Personal and dependents exemptions

- Personal exemption of $3,500 per taxpayer (i.e., $7,000 married couple filing a joint return)
- Veteran's exemption of $1,500 per veteran taxpayer
- Dependents exemption of $2,500 per dependent

### Dividends and interest income

- **dividend income:** dividends received by an individual from a domestic corporation are subject to a 15% special tax. in the case of dividends received from a foreign corporation are taxed at individual ordinary rate (up to 33%).
- **interest income:** interest from deposits in interest-bearing accounts or in certificates of deposits of individuals, estates, and trusts in domestic banking institutions may be subject to a special 17% or 10% tax, in lieu of regular tax (above), at the option of the taxpayer.

### Capital gains

- **short term:** capital gains on property held for one year or less are deemed short-term and will be taxed at ordinary income tax rates
- **long term:** capital gains on property held for more than one year are deemed long-term and will be taxed at a preferential tax rate of 15%

### Capital losses

- capital losses may offset up to 80% of capital gains, plus taxpayer net income or $1,000, whichever is less, with a carryover period of 7 years.

We will continue with our commitment to keep you up-to-date with these tax-related developments. Please contact our Tax Department should you require additional information regarding this or any other tax issue. We will be glad to assist you.




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