



Tax



Business



Taxpayer

Tax resilience amid global disruption

May 18, 2020

The spread of COVID-19 is disrupting businesses around the globe. As the crisis continues, businesses need to be agile in managing the tax effects on their business. While tax filings and payments may already be front of mind, other international tax areas require consideration.

Multiple sectors have been impacted with some businesses completely side-lined due to widespread labor and supply chain interruptions. The credit markets are only beginning to see the effects of cash strained borrowers struggling to meet their obligations. Consumer demand has all but evaporated as countries continue to encourage limited interaction to control the spread of the virus. Unemployment is sharply increasing in many places with governments stepping in, and in some cases guaranteeing incomes.

Multinationals are especially challenged with a complex web of legal and administrative changes happening around the globe. Operating in what was already a complex environment, businesses are now trying to do more with less as the public health situation weighs on the economy. As the crisis continues, businesses need to be agile in managing the tax effects on their business. We have highlighted a few of the areas below that businesses may look to address as they look to be resilient amid the global disruption.

Tax incentives, law changes and stimulus

Several governments have already enacted legislation to help stimulate their economies while providing for crisis response needs or labor concerns. Global businesses should be staying abreast of these changes to make sure of timely compliance and the usage of appropriate and applicable changes. Changes to laws in China, Italy and other jurisdictions have already significantly impacted the legal landscape for taxpayers.

Visit our website to view additional articles

www.grantthornton.pr



A key law in the United States is the Coronavirus Aid, Relief, and Economic Securities (CARES) Act. A package of over \$2 trillion in economic relief, the CARES Act aims to provide fast and direct economic assistance for American workers, families, and small businesses, and preserve jobs for American industries. The Paycheck Protection Program (“PPP”) of the CARES Act, also available in Puerto Rico, provides small businesses with resources to maintain payroll, hire back employees who may have been laid off, and cover applicable overhead. Funding for PPP loans was extended by \$310 billion by the Paycheck Protection Program Increase Act of 2020. An attractive aspect of the PPP is that it allows borrowers to claim forgiveness of their PPP loans pursuant to the Small Business Administration directives. The CARES Act provides a special rule in connection with the US federal income tax treatment of the loan forgiveness. Generally, under the US Internal Revenue Code (USIRC) the amount of cancelled or forgiven debt is included in gross income for income tax purposes. However, to provide relief to businesses, the CARES Act provides that PPP loan forgiveness is tax-free. In connection to related expenses, Internal Revenue Service (IRS) Notice 2020-32 clarifies that no deduction is allowed under the US Internal Revenue Code for an expense that is otherwise deductible if the payment of the expense results in forgiveness of a covered loan under the CARES Act.

Companies engaged in a trade or business in Puerto Rico are subject to taxation under the PR Internal Revenue Code (PRIRC). The Puerto Rico Internal Revenue Code (PRIRC) contains a similar rule that the amount of cancelled or forgiven debt is included in gross income for Puerto Rico income tax purposes. Therefore, the amount of the PPP loan that is cancelled is considered income subject to taxation in Puerto Rico. Senate Bill 1581, introduced on May 4, 2020, proposes to make the debt forgiveness of PPP loans tax-free for Puerto Rico income tax purposes, while exempting said amount of excluded income from the reduction of tax attributes. Furthermore, unlike IRS Notice 2020-32, it will also allow expenses in connection to the loan to be deducted by the taxpayer. The Bill also amends the Municipal License Tax Act of 1974 to exempt from municipal license tax the amount of debt forgiveness of the PPP loan. If the Bill is converted into law, businesses in Puerto Rico will benefit from the liquidity provided by the PPP, while also lowering the tax bill, or increasing losses that will be carried forward for PR income tax purposes. The Bill has been approved in the Senate and is now under consideration of the House.

A series of bills to provide COVID-19 relief for Americans have been adopted and more are in the making. On May 15, the House of Representatives passed the Health and Economic Recovery Omnibus Emergency Solutions Act, the HEROES Act, a \$3 trillion follow-on relief package to the CARES Act. The HEROES Act will now be considered by the US Senate.

Key questions to now consider include:

- Have you inventoried legal and/or tax changes in your operating jurisdictions?
- Do you have a clear understanding of what you need to do to take advantage of these changes?
- Are you compiling and tracking the necessary documentation to avail yourselves of any incentives, if required?

Tax losses

Many companies may incur tax losses in 2020 as a result of the economic downturn. There may be an opportunity to utilize those losses to obtain refunds of tax paid in earlier years, as part of group or consolidation claims or otherwise.

Puerto Rico House Bill 2468, introduced on March 31, 2020, proposes a loss carry-back period of three years for businesses with a volume of business of \$10 million or less. As approved by the House, eligible losses should have been realized directly as a result of the COVID-19 emergency during 2020 until the emergency is finalized, but not after taxable year 2021.

The bill has been approved by the Puerto Rico House and the Puerto Rico Senate. Since the Senate introduced amendments to the bill, it will have to be approved by the House before it is sent to the Governor.

Key questions to now consider include:

- Will tax losses arise in any of your jurisdictions in 2020?
- If there are tax losses, can these losses be offset against tax paid in earlier periods, future periods or by surrender to other profitable companies?
- Is there any benefit in either filing returns early or shortening the length of an accounting period to more quickly access available tax refunds?
- Is there any scope to surrender tax losses across borders, e.g. via EU tax mechanisms?

Transfer pricing

As companies adjust their supply chains and business models to meet the demands of the new 'now', transfer pricing (TP) should be top of mind. At a basic level, TP means pricing related party transactions on a basis that is comparable with how you price third party transactions. Changing business models and supply disruptions may alter your company's pricing policy. For example, home working may adjust the duties that workers perform for their employing entity and therefore the TP model of an international business. Wider business changes in these turbulent times may require the same.

We expect that companies in Puerto Rico will need to evaluate their transfer pricing studies. The recently adopted Puerto Rico Incentives Code brought upon certain technical changes to incentives laws, which can provide exciting tax planning opportunities. For instance, the export of goods and services incentives, previously known as Act 20 incentives, allows services rendered outside of Puerto Rico to be eligible for a preferable tax rate of 4%. In a post-pandemic business world, many companies will have to adapt to employees working remotely, and Puerto Rico might be the place with the flexibility to conduct these businesses from.

Key questions to now consider include:

- Could workers performing functions in new places affect the taxing rights allocated to group companies in the international supply chain?
- Should closed down or temporarily paused operations be remunerated in the same way as when they were operational?
- Should targeted methods of pricing (e.g. distributor models) be reviewed in these extraordinary times to avoid mismatches of profits and losses?
- If functions are transferred overseas to consolidate business positions, has the transfer pricing impact been considered?
- Have the transfer pricing aspects of treasury matters been considered?

“Sometimes change is so vast and dislocating that it is hard to tell disaster from opportunity.”

The Economist’s April 11, 2020 edition, “The changes COVID-19 is forcing on to business”

Cash tax minimization

With the onset of the economic downturn, businesses must immediately re-evaluate any upcoming cash tax payments. Several taxing authorities have extended payments deadlines while others have enacted incentives that may negate the needs for some or all upcoming estimated tax payments. More likely, companies bottom lines may be significantly different on a projected basis due to the crisis. Given the importance of liquidity, companies would be smart to immediately inventory their upcoming cash tax payments for evaluation.

Click [here](#) for a look of extended due dates in Puerto Rico as a result of COVID-19.

Key questions to now consider include:

- Do I have a full global inventory of upcoming cash tax payments?
- Have there been legal or administrative changes that impact my obligation for payments?

Corporate tax residency

Emergency measures introduced by governments and altered travel plans may mean that company directors and strategic thinkers may be unable to travel for a prolonged period. That may mean that company board meetings are unable to go ahead with directors being physically present. Where directors or other decision-makers are not in the jurisdiction of tax residency of an entity, this could draw into question the tax residency of the company.

In connection to company board meetings, tax grants for the export of services, known as Act 20 tax grants, generally require that the company hold at least two board meetings in Puerto Rico. If the company is not able to meet this requirement, the grant might be at risk of noncompliance, so the company should mitigate this risk in order to protect its incentivized tax treatment in Puerto Rico.

Key questions to now consider include:

- Will ongoing board meetings shift the management and control of a company?
- Could other strategic decisions made separately from home shift the management and control of a company?
- Have governments or taxing authorities released helpful precedent to reduce this as a risk area?
- Can amendments be made to board members, procedure or attendees to reduce residence risk?

Permanent Establishment (PE)

In addition to company directors, many businesses will now have large numbers of workers that do not attend work in their usual office location. This may not create additional tax risk if workers are performing duties within the same taxing jurisdiction or state. However, to the extent that workers are performing their duties from other taxing jurisdictions or states, there is an inherent risk that a company could create a new taxable presence due to those activities.

Key questions to now consider include:

- How can you manage and control employee home-working, with a careful understanding of the location of workers?
- Where there is a need for a worker to be overseas, have you considered their role and responsibilities to determine the level of risk they may create (for example, whether the activities could be deemed preparatory or auxiliary in nature)?
- Have governments or taxing authorities released helpful precedent to reduce this as a risk area?
- Have you created protocol to manage worker requests?

PE questions may extend further than home working, for example delays to construction or installation projects could create a fixed place of business or installation PE. Adjusted areas of doing business will need to be considered in the round.

For Puerto Rico corporations, it is also important to determine whether there has been a change in tax residency of its shareholders since this might have a significant impact in tax planning around the anti-deferral regimes on the USIRC, such as the controlled foreign corporations and passive foreign investment companies' provisions.

Treasury tax matters

As an international business reacts to the impact of the disruption, there is likely to be a greater need for cash in certain jurisdictions. Methods to repatriate excess cash or pay intercompany balances may be considered, as well as addressing external cash needs.

Key questions to now consider include:

- Can tax installments be reduced or eliminated if local legislation permits a rebasing of installments based on projected income or loss
- Where is there a need for cash, and what strategies could be applied to make best use of group funds?
- If there are distributable reserves available from an accounting perspective, can cash be repatriated? Consideration of participation exemptions and dividend withholding taxes would be required.
- If the terms of intercompany agreements allow for altered payments, have you considered their nature?
- What are the tax implications of altered lender relationships / security arrangements and new loans?
- How are exposures to interest rate and foreign exchange changes being managed?
- Has an altered treasury need changed key calculations relating to thin capitalization, or other interest deduction restrictions?



This article has been adapted from a publication "[Tax resilience amid global disruption](#)" authored and published by Grant Thornton International on March 24, 2020.

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.



Lina Morales
Partner Head of Tax
E lina.morales@pr.gt.com



María de los Angeles Rivera
Tax Partner and IBC Director
E maria.rivera@pr.gt.com



Francisco Luis
Tax Partner
E francisco.luis@pr.gt.com



Isabel Hernández
Tax Partner
E isabel.hernandez@pr.gt.com



DISCLAIMER: This update and its content do not constitute advice. Clients should not act solely on the basis of the material contained in this publication. It is intended for information purposes only and should not be regarded as specific advice. In addition, advice from proper consultant should be obtained prior to taking action on any issue dealt with this update.

© 2020 Kevane Grant Thornton LLP All rights reserved. Kevane Grant Thornton LLP is a member firm of Grant Thornton International Ltd (GTIL). GTIL and the member firms are not a worldwide partnership. Services are delivered by the member firms. GTIL and its member firms are not agents of, and do not obligate, one another and are not liable for one another's acts or omissions. Please visit www.grantthornton.pr for further details.