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CERTIFIED PUBLIC ACCOUNTANTS & CONSULTANTS

TAX ALERT 2015-03

February 6, 2015

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A PUBLICATION FROM THE TAX DIVISION

PR TREASURY ISSUES TAX POLICY INFORMATION BULLETIN No. 15-03 (BI 15-03)



Please contact your account service partner should you have any questions or comments or if you need additional information regarding these matters.

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Exemption of \$40,000 on Income Earned by Young Taxpayers

Act 135-2014, known as the “Act for Incentives and Financing of Young Entrepreneurs”, amended Section 1031.02 of the Internal Revenue Code of Puerto Rico of 2011, as amended, for among other things, establish an exemption from income tax for young residents of Puerto Rico between 16 and 26 years old. This exemption applies to gross income from salaries, services, or self-employment, **up to \$40,000** (“\$40K Exemption”).

The purpose of BI 15-03, issued on February 2, 2014, is to provide employers, withholding agents, and income tax return specialists with guidelines for implementing the provisions of Act 134-2014 with respect to this matter for the 2014 tax year.

Taxpayers Between 16-26 Years Old Who Earn Salaries

The \$40K Exemption is available to all taxpayers between the ages of 16 and 26 years old who are residents of Puerto Rico. This exemption should be included in box 16 of Form 499R-2/W-2PR, or Withholding Statement (W/2) of the taxpayer. In addition, the employer must include in box 16A the exemption code “**E**” to indicate that said exemption corresponds to the benefits of Act 135-2014.

Wages included in box 16 of the W/2 should **NOT** be included in boxes 7, 8, 9 or 10 of said W/2. However, if the employee earned more than \$40,000, the excess over \$40,000 will be considered taxable income, and thus, shall be reported in boxes 7, 8, 9 or 10 in the W/2, as applicable.

The taxpayer must verify that the employer completed boxes 16 and 16A of the W/2 in order for the Treasury Department to recognize and allow the exemption. Should the W/2 not show that a taxpayer qualifies for the \$40K Exemption, even though the taxpayer is entitled to said benefit, the taxpayer must request the employer to correct the W/2 before filing the tax return with the Puerto Rico Treasury Department.

TAX ALERT 2015-02

January 27, 2015

Taxpayers Between 16-26 Years Old Who Are Self-Employed

The \$40K Exemption also applies to income earned from services or self-employment (which are included in Schedules K, L, M, and N of the income tax return)¹. The \$40K Exemption, however, will not be reflected in the Informative Returns (Form 480.6A and Form 480.6B) received by the taxpayer. As a result, if the taxpayer qualifies for the \$40K Exemption, he (she) will be responsible for claiming said benefit on his (her) income tax return.

The \$40K Exemption will apply to the aggregate of all the service and self-employment revenue reported in the income tax return.

Claiming the \$40K Exemption

The exemption benefit is limited to \$40,000 per year. If the taxpayer had more than one employer during the year, he (she) must ensure that the sum of salaries reported in box 16 (identified by code exemption **E**) from all W/2's does not exceed the \$40,000 limit. In the event that said sum exceeds the \$40,000 limit, the taxpayer must request the employer to correct the W/2 as necessary.

Furthermore, if during the taxable year the taxpayer earned income from salaries **and** services or self-employment, the \$40K Exemption should be applied first against salaries, and any remaining balance should be applied against earnings reported in Schedules K, L, M, or N of the income tax return.

¹ **Schedule K** – Industry or Business Income; **Schedule L** – Farming Income; **Schedule M** – Professions and Commissions Income; **Schedule N** – Rental Income.

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