

# TAX ALERT

## PUERTO RICO ESTATE AND GIFT TAXES ARE ELIMINATED

On August 6, 2017, the Governor of Puerto Rico signed into law Senate Bill No. 582. As a result, Act 76 of August 6, 2017 ("Act 76-2017") repealed estate and gift taxes in Puerto Rico after December 31, 2017. Act 76-2017 eliminates the 10% tax on transfers for both residents and nonresidents of Puerto Rico.

### Estate and Gift Tax

Before Act 76-2017 was approved, the PR taxable estate was determined based on the fair market value of the property inherited at the time of the decedent's death, reduced by the fixed deduction of \$1,000,000 provided by Section 2023.08 of the 2011 Puerto Rico Internal Revenue Code, as amended (the "Code"), claimed before the deduction on property located in Puerto Rico provided by Section 2023.02 of the Code. Pursuant to such computation, heirs inherited property at its fair market value determined at time of death.

Under Act 76-2017, no tax will be imposed on the estate of a decedent whose date of death is after December 31, 2017, thus, the tax basis of the inherited property will now be the same basis of the property had in the hands of the decedent, instead of its fair market value at time of death.

To better illustrate this, let's say that the PR born decedent acquired a property with a cost of \$50,000. At the time of death, the fair market value of such property was \$250,000. As a general rule, before Act 76-2017, the tax basis of this inherited property was the fair market value of the property at the time of death of the decedent, i.e., \$250,000. If later, the PR born heir residing in PR sells the property for say \$220,000, the result would be a \$30,000 loss claimed on the heir's PR individual income tax return.

Under the new legislation, however, after December 31, 2017, the tax basis of the inherited property will be the same basis the property had in the hands of the decedent. In this example, the basis of the property in the hands of the decedent was \$50,000. If the heir sells the property for \$220,000, the heir would have a gain of \$170,000.

Similarly, Act 76-2017 eliminated the tax imposed on gifts made after December 31, 2017. Before Act 76-2017, the tax basis of the property acquired by gift after December 31, 2010 and before January 1, 2018, was the fair market value of the property as of the date of the gift. As an exception, the basis of the property for gifts that qualify for the special deduction provided in Section 2042.02 of the Code (deduction on property located in Puerto Rico), was the same as it was in the hands of the donor, increased by that portion of the amount of exclusions provided in Sections 2041.03 and, if applicable, 2042.13 of the Code<sup>1</sup>. Under no circumstance, such basis could exceed the fair market value of the property at the time of the gift.

Under Act 76-2017, however, the step-up basis for the property obtained by gift was eliminated and the basis of the donated property after December 31, 2017 will now be the same basis the property had in the hands of the donor at the time such gift was made.

<sup>1</sup>Section 2041.03 of the Code provides an annual deduction of the first \$10,000 donated to a person. Section 2042.13 of the Code, provides a special annual deduction of the first \$5,000 donated each year to each of the donor's children declared as physically or mentally incapacitated by the court.



## Estate and Gift Tax Returns

Act 76-2017 also changes the tax forms to file for both estate and gift taxes. Namely, for estate tax, instead of filing an estate tax return, an informative return will be required listing the property of the estate and which will be due 12 months after the decedent's death. For the gift tax, an informative return will also be required to be filed instead of the gift tax return. This gift informative return is required when the amount of the gifts or property transferred exceeds \$10,000. The return will be due on January 31 of the year following the year the gift is made.

Act 76 provides for the immediate issuance of the Certificate of Cancellation of Lien upon filing the informative return if the decedent or the donor does not owe any taxes. The Puerto Rico Treasury Department may impose a \$25 fee for the issuance of the Certificate of Lien Cancellation and, if the informative return is amended to include additional property, the fee can be requested again to issue an amended Certificate. If there are taxes due under examination, the Secretary of the Treasury may issue a Conditional Certificate.

Based on these changes to the current tax treatment for property transferred by inheritance or gift, we strongly suggest you review your current estate and gift tax plan to determine how it may be impacted; changes to such plans may need to be implemented before December 31, 2017.

Our BDO team can help you understand and minimize the risks associated with the temporary relocation. We are here to help you analyze your particular situation and to help you plan accordingly during these extraordinary times.

Please contact any of the members of the BDO team to continue the conversation.

## OUR EXPERTS

**Gabriel Hernández, CPA**  
Partner  
Tax Advisory Services  
gaby@bdo.com.pr

**Patricia Wangen, CPA, Esq.**  
Partner  
Tax Compliance Services  
patricia@bdo.com.pr

**Dialy M. Otero, CPA**  
Director  
Tax Advisory Services  
dotero@bdo.com.pr

**Adianez Ortega, CPA, Esq.**  
Manager  
Tax Advisory  
aortega@bdo.com.pr

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Tel. (787)754-3999 • Fax (787)754-4493 • 1302 Ponce León Avenue Suite 101, San Juan, PR 00907 • [www.bdopr.com](http://www.bdopr.com)

