

Puerto Rico Treasury Updates Rules for Obtaining Retirement Plan Qualification Letters

On December 23, 2016, the Secretary of Hacienda issued Circular Letter of Tax Policy No. 16-08 (CL 16-08) to update its rules and procedures for requesting qualification letters for Puerto Rico qualified retirement plans. The new rules and procedures are effective immediately.

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Background

Puerto Rico requires that sponsors of all retirement plans intended to be qualified in Puerto Rico, (including “dual-qualified plans” that are qualified both in the US and Puerto Rico), must apply for a “qualification letter” from the Puerto Rico Department of the Treasury (known locally as “Hacienda”), the Puerto Rico equivalent of the US Internal Revenue Service, to confirm its tax qualified status.

Previously, Circular Letters [11-10](#) (CL 11-10) and [13-02](#) (CL 13-02) established guidance and procedures for plan sponsors and other service providers to follow when requesting a favorable determination on the qualified status of their retirement plans under the 2011 Internal Revenue Code for a New Puerto Rico (PR Code). CL 13-02 required the initial qualification letter for plans amended for compliance with the PR Code to be submitted by the due date for filing the plan sponsor's 2013 tax return, without extensions (although an additional 3-month extension was available for those paying an additional \$150 fee). For example, the deadline would have been April 15, 2014 for employers that use the calendar year as their taxable year (with a three-month extension available to July 15, 2014 for those who paid an additional \$150 fee).

CL 13-02 also established a correction procedure allowing plan sponsors of retirement plans covering Puerto Rico participants to voluntarily correct their failure to submit an amended plan for a qualification letter in a timely manner by paying a correction fee equal to three times the sum of the normal qualification letter filing fee and the \$150 additional extension fee. This program was not available to plans and plan sponsors under examination by Hacienda. (See our [June 26, 2013 For Your Information](#).)



Validity of Qualification Letters

[CL 16-08](#) provides that previously issued favorable qualification letters will continue to be valid as long as the plan document or trust agreement (or deed of trust) is not further amended to add, modify, or remove – in whole or in part – any plan provision that would be considered to be a “Qualification Amendment” (as defined in CL 16-08 and discussed further below).

Comment: Previously, under CL 11-10 and CL 13-02, plan sponsors and other service providers would have had to submit all plan document restatements and amendments for a qualification letter. Now, under CL 16-08, plan restatements and/or amendments that do not contain “Qualification Amendments” do not need to submit another application to Hacienda for a favorable determination on the qualified status of the retirement plan.

“Qualification Amendments” Defined

CL 16-08 provides that any of the following modifications made to a previously qualified retirement plan would be considered a “Qualification Amendment”:

- Amendments to incorporate future changes in the qualification requirements of the PR Code
- Changes that affect plan eligibility or benefit accruals/allocations for Puerto Rico participants (including those that prevents new employees from becoming participants, or that freeze future benefit accruals or allocations)
- Changes to the form or method for payment of benefits available to participants in Puerto Rico
- Changes in the participating employers that employ Puerto Rico participants (but only if there are changes to the Employer Identification Number [EIN] of the participating employers)
- Changes in the application of, or correction methods used to comply with, the coverage and nondiscrimination rules under the PR Code
- Amendments that grant credited service to participants in Puerto Rico for service with another employer for purposes of plan participation or the calculation of benefits/contributions
- Amendments that merge the plan with another retirement plan
- Amendments that terminate the plan
- Amendments that make changes to the plan administrator, trustee, insurance provider or the agent responsible for paying benefits to Puerto Rico participants under the Plan
- Changes to the plan sponsor of a master or prototype plan
- Any other amendment to the official plan document, trust agreement or other plan documents that Hacienda subsequently considers as a “Qualification Amendment” through regulations, circular letters or administrative determination
- Amendments not considered “Qualification Amendments”

CL 16-08 further provides that a plan sponsor will not need to reapply for qualification letter from Hacienda if any of the following modifications are made to a previously qualified retirement plan and such modifications are not considered “Qualification Amendments”:

- Amendments that incorporate future changes to the qualification rules under the US Internal Revenue Code or ERISA
- Amendments to the plan's administrative or claims procedures
- Amendments that change the person or entity serving as the plan administrator or the custodian of the plan's assets
- Adding, eliminating or changing a loan program, investment alternatives, contribution types, or early retirement windows
- Changes in the plan's vesting schedule
- Amendments that add, eliminate or change rules for the payment of administration costs of the plan by the employer or its participants
- Changes to the plan eligibility rules, benefit accrual/allocation formula or distribution options that do not apply to Puerto Rico plan participants
- Changes in participating employers that do not employ Puerto Rico plan participants or that do not result in a change in EIN

Comment: Because CL 16-08 lists a change in the plan administrator as both a “Qualification Amendment” and a non-qualifying amendment, it would seem that such a change may require plan sponsors to submit a qualification letter application absent further clarification from Hacienda.

Master/Prototype plan sponsors that make Qualification Amendments that only affect the “master plan document” (sometimes called the “basic plan document”) can submit the Master/Prototype plan to Hacienda for approval without the adopting employers having to file their own qualification letter requests. However, if the employers must execute a new adoption agreement as a result of the change, the adopting employers will have to submit the amendment to Hacienda for their own qualification letters.

On February 8, 2017, the Governor of Puerto Rico signed Act No. 9-2017, which made some changes to the PR Code that will require plan sponsors to adopt a “Qualification Amendment.” This *FYI* focuses on the rules and procedures established by Hacienda that qualified retirement plan sponsors will have to follow to ensure the continued qualification of their plans by requesting a qualification letter. We will address the changes enacted under Act No. 9-2017 in a future *FYI*.

Deadlines for Qualification Letter Submissions

CL 16-08 also establishes some new deadlines to submit qualification requests to Hacienda.

Existing plans that covered Puerto Rico participants on January 1, 2011 and received a qualification letter under the 2011 PR Code (or that have submitted a request for one but have not yet received a determination on their plan's qualified status) must submit a qualification letter request no later than the employer's tax return filing deadline, including extensions, for the taxable year in which the “Qualification Amendment” was adopted.

Comment: Under the new rules, note that the date of adoption of the “Qualification Amendment” determines the filing deadline, not the effective date of the “Qualification Amendment.”

New plans established after January 1, 2011 that cover Puerto Rico participants or that started covering Puerto Rico participants after January 1, 2011 must submit a qualification letter request by the employer’s tax return filing deadline, including extensions, for the later of (i) the taxable year in which the plan was established or (ii) the taxable year when Puerto Rico employees first commence participation in the plan.

If the request for qualification is not timely filed by the deadlines described above, an additional \$350 fee will be charged for the submission.

Changes to the Rules for the Correction of Late Amendments

For plan sponsors of existing plans that missed the initial plan amendment and qualification letter submission deadline for amendments related to the 2011 PR Code under CL 13-02 (as described above under background), CL 16-08 clarifies that they can still request a retroactive qualification letter on the plan by paying the late filing fee (equal to three times the sum of the basic filing fee plus the \$150 extension fee). However, CL 16-08 clarifies that the correction program is only available if the plan or plan sponsor is not under examination, investigation or audit by Hacienda, or the *US IRS or DOL* – either regarding the plan’s operations or the employer’s deduction of contributions. Previously, only an examination, investigation or audit by Hacienda would have precluded a plan sponsor from using the program.

Comment: CL 16-08 does not say whether a plan sponsor that missed the initial plan amendment deadline under CL 13-02 and also misses the deadlines for subsequent amendments will have to pay additional user/compliance fees for subsequent amendments to obtain relief for missing the deadline for later amendments (that were required after the initial deadline spelled out in CL 13-02).

Qualification Letter Submission Materials and Fees

CL 16-08 includes revised lists of the information that must be included with a retirement plan sponsor’s qualification letter submission. Different lists apply to individually designed plans and Master/Prototype plans. Unlike US determination letter applications submitted to the IRS (using IRS 5300 series forms and specified attachments), Hacienda’s procedures do not require the applicant to fill out specific forms. Also, the submission must be bound together, and must be complete. Failure to include all the necessary information can result in an additional fee of \$150 for incomplete applications.

CL 16-08 also includes updated guidance on the filing fees associated with qualification letter submissions, and also where and how to file such requests. The basic filing fees have generally remained the same as in previous guidance issued by Hacienda (for example, for individually designed plans adopted by an employer that is not self-employed the fees are still \$1,500 for a new plan, \$750 for a plan restatement, \$350 for plan amendments; \$500 for plan terminations; with an additional fee of \$350 for a late filing, if applicable).

In Closing

CL 16-08 provides sponsors of Puerto Rico qualified retirement plans and their service providers with valuable guidance on submissions of qualification letter requests to Hacienda. In Puerto Rico, distributions from locally qualified plans receive significant tax benefits – including a special tax rate on lump sums, and a tax exclusion for annuity payments (up to certain thresholds). These tax benefits and the possibility of Hacienda issuing audit sanctions on plan sponsors, make obtaining a plan qualification letter of key importance to both Puerto Rico plan participants and their employers. Plan sponsors and other service providers who have adopted plan amendments may seek to reduce compliance risks by submitting (or resubmitting) a qualification letter application that complies with the new guidance outlined in CL 16-08.

Authors

Kenneth Kim, JD
Fred Farkash, CEBS, Fellow-ISCEBS
Hector Gaitan, FCA, ASA, MAAA, EA, CCP

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