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Volume 36 | Issue 10 | January 29, 2013

## Puerto Rico retirement plans: Puerto Rico Treasury extends deadlines—but US transfer extension expires

Puerto Rico's Treasury Department has extended the deadline for amending qualified plans covering employees in Puerto Rico to no earlier than June 30, 2013, and extended the deadline for submitting qualification letter requests to no earlier than September 30, 2013. The IRS has not yet followed suit on extending the deadline for transfers and transition relief for coverage tests when Puerto Rico employees are covered under certain Puerto Rico plans.

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### Background—Puerto Rico tax law changes

In Puerto Rico, for a plan to be considered qualified, the plan sponsor must obtain a qualification letter by requesting one from Hacienda (the Puerto Rico equivalent of the US Internal Revenue Service). In January 2011, Puerto Rico enacted the Internal Revenue Code for a New Puerto Rico (2011 Code). On December 16, 2011, Puerto Rico's Treasury Department published [Circular Letter 11-10](#) requiring sponsors of qualified retirement plans to adopt amendments reflecting the 2011 Code (and subsequent technical corrections) by the last day of the first plan year beginning on or after January 1, 2012.

That circular also required employers to submit their amended plans to Hacienda for a plan qualification letter no later than the due date for filing the 2012 income tax return of the employer maintaining or participating in the plan. (The due date for filing an employer's Puerto Rico income tax return is generally either 3½ months after the end of the employer's fiscal year or 6½ months after the end of the employer's fiscal year if the employer files for an extension.) It also permitted plan sponsors to request retroactive qualification of their plans under the Puerto Rico Internal Revenue Code of 1994 (1994 Code) if they had not previously obtained a plan qualification letter.

### Puerto Rico's amendment and qualification letter filing deadlines extended

Puerto Rico's Acting Secretary of the Treasury published [Circular Letter 12-09](#) on November 28, 2012, providing additional time for most plan sponsors to adopt plan amendments and file plan qualification letter requests.

Plan sponsors must now adopt plan amendments to comply with the 2011 Code by the later of June 30, 2013, or the last day of the plan year beginning in 2012. For calendar year plans, the deadline will now be June 30, 2013,

rather than December 31, 2012. If a plan's 2012 plan year ends after June 30, 2013, the previously announced deadline (i.e., the last day of the 2012 plan year) applies.

In addition, plan sponsors must file their qualification letter requests (including requests for retroactive qualification under the 1994 Code) with Hacienda by the later of the due date for the employer's income tax return (including extensions) for the first taxable year commencing in 2012 or September 30, 2013. For employers with taxable years ending on December 31, the new deadline is September 30, 2013. If the employer's income tax filing deadline for the 2012 taxable year (with extensions) is after September 30, 2013, the due date for the qualification letter request remains the employer's income tax filing deadline.

## Background—US qualification relief for transfers

Absent IRS relief, transfers from US qualified plans to foreign plans that do not satisfy US qualification rules are treated as taxable distributions under US law. Unless the employee for whom funds are transferred had incurred a distributable event at the time of the transfer, the transfer would be seen as an impermissible distribution that could disqualify the plan. The IRS issued [Revenue Ruling 2008-40](#) to explain this limitation and to provide transition relief for employers that wanted to transfer participants who were Puerto Rico residents to a plan that would only satisfy the qualification rules under the Puerto Rico Tax Code. This type of transfer would allow the employer to reduce tax burdens for employees and help avoid the administrative and compliance challenges associated with having to comply with both the US and the Puerto Rico Tax Code as a dual qualified plan.

The ruling also allowed certain US qualified plans making these transfers to exclude those covered by the Puerto Rico-only plan when applying the US coverage tests for pre-2011 plan years.

[Revenue Ruling 2011-1](#) was issued shortly after the initial deadline for the transfer relief on December 31, 2010, extending the transfer deadline (and the special rule for coverage testing) until December 31, 2011. In January 2012, the IRS issued [Notice 2012-6](#) announcing a further extension of the deadline for these provisions to December 31, 2012. Unless a further extension of this transfer deadline is announced, in addition to the loss of the relief for coverage testing, a transfer after 2012 would result in sanctions for the plan sponsor initiating the transfer (up to and including disqualification), and adverse tax consequences for the plan's participants and beneficiaries.

**Buck Comment:** The exceptions and deadlines noted above did not apply to transfers involving Puerto Rico employees among plans that maintain their US qualification. The relief only applied if the US qualified plan made a transfer to a plan that only complied with the Puerto Rico Tax Code's qualification rules (and not also those of the US).

In addition to extending the transfer and coverage rules, Revenue Ruling 2011-1 refined the requirements for group trusts (described in Revenue Ruling 81-100) in general. So-called 81-100 group trusts include master trusts (trusts that commingle the assets of more than one plan of a single employer or controlled group) and bank collective trust funds (trusts that commingle the assets of plans of more than one employer). Revenue Ruling 2011-1 provided a temporary special rule for the inclusion of plans that only meet the Puerto Rico qualification requirements, because of controversy about whether they could be treated as US qualified trusts for this purpose. Trusts in Puerto Rico that had been transferred from US plans as described above or that had been participating

in the group trust as of January 10, 2011 were permitted to stay in the group trust until the IRS provides further guidance. This allowed the plans to continue to benefit from the investment advantages of pooling their assets with those of US plans.

## Currently no extension of US transfer deadline or coverage relief

Although all of the transition rules noted above are still available for transfers involving group trusts (as described in the preceding section), the IRS has not extended the relief for transfers that don't involve group trusts.

## In closing

Plan sponsors have a number of issues to consider given both the little time remaining to come into compliance with the Puerto Rico rules and the uncertainty about some of the US deadlines.

- Unless sponsors of Puerto Rico qualified plans (including dual qualified plans) have already done so, they should begin preparing the necessary plan amendments and the associated qualification letter filings with Hacienda to ensure that any plan maintained for the benefit of Puerto Rico participants is qualified under Puerto Rico's 2011 Code.
- If the IRS transfer relief is eventually extended beyond December 31, 2012, sponsors of dual qualified plans with participants who are Puerto Rico residents may wish to consider transferring their Puerto Rico participants into a separate Puerto Rico-only qualified plan.

**Buck Comment:** Without the extension of the transfer relief, sponsors of dual qualified plans that cover both US and Puerto Rico employees can consider transferring the portion of the plan for Puerto Rico employees to a separate dual qualified plan so that only the transferred population is in a plan that has to meet both sets of qualification rules. This can be particularly useful for 401(k) plans endeavoring to simultaneously pass the two different nondiscrimination tests stemming from the US and Puerto Rico Tax Codes. For dual qualified plans, actual deferral percentage test failures can typically only be corrected by adding sufficient qualified non-elective contributions or qualified matching contributions to the accounts of non-highly compensated participants to pass both tests. Limiting the size of the population subject to dual testing should reduce the contribution commitment.

- If the coverage testing transition rule for plans that had transferred Puerto Rico employees to a Puerto Rico-only plan is not extended, US plan sponsors will need to reconsider their options for ensuring continued compliance with the US coverage testing requirements.
- Even if they don't have any Puerto Rico employees, sponsors of US tax-advantaged retirement plans that participate in a group trust should find out whether the group trust includes the assets of Puerto Rico qualified plans that haven't elected dual qualified status. Sponsors whose plans participate in such group trusts must stay alert and prepare to work with the plan trustee to ensure that their plans avoid adverse tax consequences once the end of the IRS transition relief is announced.

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