



Rev. 04.21

SCHEDULE PCI

UNCERTAIN TAX POSITIONS

GENERAL INSTRUCTIONS

WHO MUST FILE THIS SCHEDULE?

Any taxpayer that under Section 1061.15 of the Puerto Rico Internal Revenue Code of 2011, as amended (Code), is required to file audited financial statements with its income tax return must complete this Schedule of Uncertain Tax Positions (Schedule PCI) and include it as part of the income tax return reporting any uncertain tax position that has been taken or recorded as a reserve in the taxpayer's audited financial statements in accordance with the provisions of the Generally Accepted Accounting Principles in the United States of America (GAAP), specifically under Accounting Standards Codification subtopic 740-10, Income Taxes, FASB ASC 740-10 or any successor pronouncement.

Notwithstanding the above, a taxpayer is not required to submit Schedule PCI for tax positions taken in a taxable year beginning before January 1, 2019, even if a reserve is recorded with respect to that tax position in the audited financial statements issued in the year 2019 or later. Furthermore, a taxpayer is not required to report accruals of interests related to registered reserves with respect to tax positions taken prior to taxable year 2019.

For the purposes of this Schedule the following terms will be defined as follows:

Audited financial statements - The term "financial statements" means, with respect to any taxable year, a report that includes: (i) an income statement showing the results of operations of the business for said taxable year; (ii) a balance sheet as of the close of the particular taxable year; (iii) a statement of cash flows, and (iv) a statement of stockholder' equity for such year. Said financial statements shall be prepared in accordance with GAAP and shall be accompanied by notes, including a summary of significant accounting policies, and other corresponding clarifying notes, in accordance with the disclosure requirements of such accounting principles. The audited financial statements to be submitted with the income tax return will be accompanied by an Auditor's Report issued by a Puerto Rico licensed Certified Public Accountant.

Tax position adopted in an income tax return - A tax position taken in an income tax return means a position that would result in an adjustment to an item reported on any line or schedule that is part of the income tax return. If several tax positions affect a single line in an income tax return, each tax position will be considered as a separate tax position taken on the return and so must be reported on Schedule PCI. Similarly, it will be considered and will be included on Schedule PCI any tax position taken on a schedule of the income tax return, even when the adoption of said position does not result in the payment of any additional income tax.

Record a reserve - It is considered that a taxpayer (or a related entity) records a reserve for an uncertain tax position when, under the applicable accounting standards, a reserve for income taxes, interests or penalties related to a tax position is taken in an income tax return is registered in the audited financial statements of said taxpayer or related entity. If the taxpayer or a related entity determined, under the applicable accounting standards, that there was no need to record a reserve, either because the amount was immaterial for the purposes of the audited financial statements, or because the tax position was sufficiently certain, then the taxpayer does not have to report said tax position on Schedule PCI.

Uncertain tax positions to report on a Schedule PCI

It is required to report on Schedule PCI each tax position taken by a taxpayer on his income tax return if the following two (2) conditions are met:

1. The taxpayer has taken a tax position on his income tax return for the current taxable year.

2. Either the taxpayer or a related entity, as established in Section 1010.05 of the Code, has recorded in their audited financial statements a reserve with respect to the tax position presented in the income tax return, or the taxpayer or its related parties did not register a reserve for the tax position because they expect to litigate the position.

The initial registration of a reserve requires that said uncertain tax position be reported on a Schedule PCI that accompanies the taxpayer's income tax return. However, increases or decreases of a reserve previously registered in the taxpayer's audited financial statements will not require to be reported on Schedule PCI.

A tax position for which a reserve was recorded (or for which a reserve was not recorded due to the expectation of litigation) must be reported regardless of whether the audited financial statements are prepared based on GAAP, the International Standards of Accounting ("IFRS"), or any other accounting principle of any country, including a modified version of any of the above (for example, modified GAAP).

The taxpayer will report the tax positions taken during the current taxable year. The taxpayer will not be required to report a tax position taken in a previous taxable year if the taxpayer reported said tax position on a Schedule PCI of an income tax return filed in said previous year. If a transaction results in a tax position taken in more than one taxable year, the tax position must be included as part of Schedule PCI that is part of each of the income tax returns in which said position is included, regardless of whether the transaction or tax position was reported on a Schedule PCI filed with a previous year return. However, do not include tax positions on Schedule PCI before the taxable year in which said tax position was taken on the taxpayer's income tax return.

The decision on how to report an item of income, gains, losses, deductions or credits in a specific taxable year can affect items that will be part of the income tax return for subsequent taxable years. For example, the decision to amortize an expense instead of deducting it in the taxable year in which it is incurred, will affect not only the return corresponding to the taxable year in which the expense is incurred, but also each of the income tax returns that cover the amortization period of said expense. Whether these tax positions taken on a return are reported on a Schedule PCI for a particular tax year, and when they are reported, depends on whether and when the reserve is recorded in the taxpayer's audited financial statements.

On the other hand, although the use of a net operating loss or a credit carryforward is a tax position taken on an income tax return, the use of said loss or the credit will not be reported if the taxpayer has previously reported the tax position that created or added to the loss or credit carryforward on a Schedule PCI included with a prior income tax return filed.

The following examples provide details of various instances in which Schedule PCI must be used to inform the tax positions for a specific taxable year:

Example 1: General rule - Recording reserves

A taxpayer recorded a reserve in its 2019 audited financial statements related to a tax position taken on its tax return for said taxable year. The taxpayer reported the tax position taken in taxable year 2019 on Schedule PCI that accompanied his income tax return. If the taxpayer increases his reserve with respect to the tax position adopted in his 2019 income tax return in its 2021 audited financial statements, the taxpayer will not be required to report again the 2019 tax position on the income tax return to be filed for taxable year 2021 as a result of the reserve increase registered.

Example 2: Reporting reserves in subsequent years

A taxpayer claimed a deduction for taxable year 2019 and determined under the applicable accounting standards that it could recognize the full benefit of said position. In 2021, the Department began an examination of the income tax return for taxable year 2019 and decided to examine whether the deduction was appropriate. Subsequently, the taxpayer reevaluated the tax position and registered a reserve for that position in the year 2021. The taxpayer took a tax position on his 2019 income tax return and registered a reserve with respect to that tax position. In this case, the taxpayer must report the tax position on Schedule PCI that accompanies his return for taxable year 2021, even if the Department identifies the tax position for the examination before recording the reserve.

Example 3: General rule - Related entities

Corporation A is a corporation that files its Corporation Income Tax Return, Form 480.20. Corporation B is a foreign corporation not doing business in Puerto Rico and is a related party to Corporation A, as established in Section 1010.05 of the Code. Corporations A and B, are part of a group of related entities, and issue their own audited financial statements. Corporation A takes a tax position on its income tax return. If Corporation B records a reserve with respect to that tax position in its own audited financial statements, even though Corporation A does not record such position in its statements, Corporation A must report such position on its Schedule PCI.

Example 4: Reserve recorded in consolidated financial statements

Corporations C and D are part of a group of related entities, as defined in Section 1010.05 of the Code. In compliance with the requirements of Section 1061.15 of the Code, they issue a consolidated audited financial statement for taxable year 2019. Corporation C takes a tax position for which a reserve was recorded in the consolidated financial statements of Corporations C and D. The tax position adopted by Corporation C in its income tax return must be reported on its Schedule PCI since a reserve for said tax position was recorded in the consolidated financial statements in which Corporation C was included.

Example 5: Multiple year positions

A taxpayer incurred an expense in the year 2019 and claimed the total amount as a deduction in its 2019 income tax return. During the course of reviewing its tax positions in order to establish any reserve of his income tax return in its 2019 audited financial statements, the taxpayer determined that it was unsure whether the expense should be amortized over a 5-year period and recorded a reserve with respect to the position taken in the year 2019. The taxpayer did not record a reserve for any of the positions taken in taxable years 2020 to 2024, even though it has taken a tax position in each of those years (there would be an adjustment to an item in the income tax return for each of those 5 year if the position taken in said return is not sustained). In this case, the tax position adopted in taxable year 2019 must be reported on Schedule PCI that is included as part of the income tax return filed for year 2019. However, the tax positions corresponding to the years 2020 to 2024 should not be reported on the Schedule PCI to be included with the income tax return for those years because the taxpayer did not record a reserve with respect to any of those tax positions.

Example 6: Multiple year positions

A corporation incurred an expense in the year 2019 and took the position that the expense can be amortized over a period of 15 years beginning on its 2019 income tax return. During the course of reviewing its tax positions for purposes of establishing any reserve related to its income tax return in its 2019 audited financial statements, the corporation determined that it was uncertain whether any deduction or amortization of this expenditure is allowable. In the 2019 audited financial statements, the corporation recorded a reserve with respect to the amortization deduction that will be claimed in each taxable year. The corporation has taken a tax position in each of the 15 taxable years because in

the income tax return for each of those years there would be an adjustment to a line item on that return if the position taken in that year is not sustained. In this case, the corporation must report the tax position taken in 2019 on Schedule PCI and include it as part of the 2019 income tax return. In addition, the tax position that will be taken in each of the taxable years from 2020 to 2033 must be informed on the Schedule PCI that will be included with the income tax return for those taxable years in which the tax position was taken. The result would be the same if, instead of registering the reserve in 2019 for all tax positions taken in each of the 15 years, the corporation registers a reserve in each year that is specifically related to the tax position taken in the income tax return for that year.

Example 7: Transition rule

The facts are the same as in Example 6, except that the corporation incurred expenses and recorded the reserve in its audited financial statements for the year 2009. The corporation has taken a tax position on each of the income tax returns of the 15 subsequent taxable years (2009 to 2023) given that in each of these returns a line of the return has been adjusted considering that the positions taken in the specific taxable year would not be sustained. However, the corporation was not required to report the tax position adopted in taxable year 2009 because it was taken in a taxable year that begins before January 1, 2019. The corporation will report the tax position taken in each of the taxable years 2019 to 2023 on Schedule PCI that accompanies the income tax returns for the respective taxable year in which the position was taken.

Example 8: Creation and use of net operating loss

A corporation incurred an expense of \$50 in year 2019 and claimed the total amount as a deduction in its 2019 income tax return. The deduction increased the carryover of the corporation's net operating loss (NOL) from \$100 to \$150. The corporation used the entire \$150 NOL carryforward on its 2020 income tax return.

Claiming the deduction of \$50 in the year 2019 is considered as a tax position taken in taxable year 2019 because the position would result in an adjustment to an item of the income tax return for the year 2019 if said position is not sustained. Furthermore, the deduction in taxable year 2020 related to the NOL carried forward that comes from 2019 is a tax position adopted in the income tax return for taxable year 2020, because the position would result in an adjustment to an item on the 2020 income tax return if the position is not sustained. The corporation recorded a reserve with respect to its 2019 tax position in its 2019 audited financial statements and reported said tax position on the Schedule PCI filed with its 2019 income tax return. Because it reported the tax position in its 2019 income tax return, the corporation should not report the 2020 tax position on the Schedule PCI to be filed with its income tax return for the taxable year 2020.

Example 9: Corporate merger

On June 30, 2019, Corporation M merges with Corporation A in a transaction in which Corporation A survives. Corporation M's taxable year ends on that date (that is, June 30, 2019). After the merger, Corporation A records a reserve in its audited financial statements for the year ended December 31, 2019 with respect to a tax position that is taken on Corporation M's final income tax return. This tax position must be reported on Schedule PCI that is included with Corporation M's final income tax return, even if Corporation A has recorded the reserve in its audited financial statements. Notwithstanding, Corporation A should not report the tax position on a Schedule PCI with its income tax return for the taxable year ended December 31, 2019 because Corporation M's final income tax return is a previous period return on which the tax position was reported.

SPECIFIC INSTRUCTIONS

PART I - QUESTIONNAIRE

The taxpayer must indicate if it is required to submit audited financial statements as part of the income tax return, pursuant to Section 1061.15 of the Code. In the event that it is not required to include audited financial statements with the

return, the taxpayer will not be required to complete this Schedule and to include it with the return.

PART II - UNCERTAIN TAX POSITIONS

UTO No. - Number the uncertain tax positions included on this schedule.

Code Section - Include the specific section of the Code to which the uncertain tax position included in the audited financial statements and the income tax return being filed relates to.

Brief Description of the Uncertain Tax Position - Include a description that provides the most relevant facts that affect the tax treatment that the included tax position will have. Also, include any information that could reasonably be requested by the Department related to the nature and matter of the tax position taken. It is established that it will not be accepted as an adequate description that the taxpayer includes the phrase "Available upon request".

A concise description must not include an evaluation of the tax position taken or an analysis that supports the points for or against said tax position.