

September 25, 1998

**Circular Letter No. 98-05**

Hurricane Georges has caused severe damages in Puerto Rico. The Department of the Treasury empathizes with our people and join forces with other governmental agencies to facilitate the recovery.

For these purposes, the Department establishes the following instructions:

1. Every employer may offer to its employees goods or cash as an interest free loan or at reduced interest rates, to compensate for damages caused by hurricane Georges. The employer will not include as taxable income the foregone interest on said loan.

On the other hand, the employee will not be required to include as taxable income the foregone interest that, under normal circumstances, would have paid over said loan.

The terms for the repayment of these loans will be determined between the employee and his/her employer according to the particular needs of each case.

2. Every employer may offer to its employees goods or cash as a donation to compensate for damages caused by hurricane Georges. Even though this amount does not constitute an ordinary and necessary expense, in view of the substantial damages caused by hurricane Georges, the employer may deduct the value of said goods or cash as an ordinary and necessary business expense, according to the provisions of Section 1023(a) of the Puerto Rico Internal Revenue Code of 1994, as amended (Code). This expense will not be considered as a contribution under Section 1023(o) of the Code, nor will it be treated as a gift under Subtitle C of the Code.

The employee who receives said goods or cash as a donation will not treat their value as taxable income.

The employer will be responsible of gathering all the necessary information and evidence to support the loans or donations granted. Furthermore, the employee must submit his/her request to the employer in writing under penalty of perjury.

The amount to be loaned or donated cannot be determined on the basis of the compensation earned by each employee, but must be strictly based on the amount of damages suffered. Also, the loans or donations granted to compensate damages cannot be pursuant to an arrangement which discriminates on behalf of employees who are partners, officials, shareholders or persons whose principal duties are to supervise the work of other employees, or highly compensated employees. Only loans or donations up to \$10,000 per employee are covered by the provisions of this Circular Letter. Since the amount granted as loan or donation is not considered compensation, it will not be reported in the Withholding Statement (Form 499R-2/W-2PR).

The benefits described in this Circular Letter will not apply to shareholders or partners who own more than 5% of the entity's equity.

These rules shall have immediate effectiveness and will apply to loans and donations requested and paid not later than 60 days from September 21, 1998.

Xenia Vélez Silva  
Secretary of the Treasury