PUERTO RICO TAX INCENTIVES

Not many places in the world can offer a Return on Investment the way the beautiful island of Puerto Rico does. In fact, most of the fast-expanding array of services and rising industries generally attribute their success to the incentives made available by the Puerto Rican government. All US federal laws apply to Puerto Rico. They share a common currency, the US dollar, a common military defense, and citizenship with the US. In traveling to and from the US mainland, no passports are needed. But because it is not a state but a commonwealth of the US, Puerto Rico enjoys fiscal independence and autonomy. This means attractive Puerto Rico tax incentives not available in the US mainland. These elements critical to investors, and businessmen are formidable. Over and above these, investments are safeguarded by the prevailing rule of law, the absence of any risks on the currency and Puerto Rico's political stability.

PUERTO RICANS AND CORPORATIONS ARE NOT SUBJECT TO US FEDERAL TAXES

All Puerto Ricans born from 1917 onwards have automatically become citizens of the US. Because they all reside within the commonwealth, US federal taxes do not apply to income generated by individuals and corporations. For federal tax purposes, corporations in Puerto Rico are treated as foreign corporations and are not subject to US corporate taxes.

Act 20 Puerto Rico (<u>The Export Services Act</u>)

Act 20 was one of two laws passed in 2012 to stimulate Puerto Rico's stagnant economy and revised into act 60. These new laws enabled the establishment of a legal framework of incentives that were worked out to encourage the development of a wide range of ventures. Among these were manufacturing, social media, other interest-based businesses and operations, and the export of services. In particular, The Export Services Act 20 Puerto Rico was aimed at developing in Puerto Rico an international export services center. This was enacted to encourage local service companies to expand their services to persons and groups outside of Puerto Rico and rev-up the development of new businesses. Below are the major tax incentives that went along with these:

- Corporate tax rate of only 4%, which may be reduced to 3%
- 100% tax exemption on dividends or profit distributions from export services
- 100% exemption of property taxes for certain export service businesses
- 60% exemption on municipal taxes
- Decree of 20 years guaranteeing these rates, renewable for an additional ten years
- No federal taxes on Puerto Rico source income

Act 20 Requirements

- Any entity must be a bona fide establishment in PR that is engaged in an illegible export service
- Service include (but are not limited to) investment banking and other financial services, research and development, advertising and public relations, consulting, electronic programming development, call centers, professional services, and centralized management services.
- An eligible service done by a foreign entity or non-resident individual that does not relate to business activities within Puerto Rico qualifies as an export service.
- An eligible service provider is required to obtain a Tax Exemption Decree that will endure for a term of 20 years and may be renewed for an additional ten years.
- The Tax Exemption Decree constitutes a contract between the service provider and the Puerto Rican Government that is immune to any future legislation.
- 100% tax exemption from Puerto Rico income taxes on all dividends
- 100% tax exemption from Puerto Rico income taxes on all interest
- 100% tax exemption from Puerto Rico income taxes on all short and long-term capital gains accrued after the individual investor becomes a bonafide resident of Puerto Rico
- 0% federal taxes on Puerto Rico sourced income
- Decree benefits secured until December 31, 2035.

These are but some of the incentives available to those who would like to invest in Puerto Rico. Depending on which industry an entrepreneur may want to invest his money in, several other sets of incentives are available.

Act 273 International Financial Entities (IFE – ACT 273)

Another important legislation that was conceived as a complementary one to Acts 20 and 22 was The International Financial Center Regulatory Act (Act 273 of 2012).

4% income tax

- 0% on dividends or other distributions of profits to non-Puerto Rico residents
- 100% exemption on municipal taxes
- 100% exemption on property taxes
- This highly attractive incentives package that includes a fixed corporate income tax rate – one of the lowest in comparison with any U.S. jurisdiction – various tax exemptions and special deductions, training expenses reimbursement and special tax treatment for pioneer activities. The goal of Tax Act 273 is to expand Puerto Rico as an international financial center and promote economic growth by broadening the scope of banking activities for international financial entities (IFEs) organized in Puerto Rico as well as additional tax incentives for these IFEs.
- This law was enacted with the objective of making Puerto Rico an international banking and financial center by providing tax incentives for new banking and financial activity in Puerto Rico that is done for clients outside of Puerto Rico.
- The tax incentive offer is mainly a four (4) % income tax rate for new banking and financial businesses established in Puerto Rico under qualifying circumstances.
- 4% or 8% fixed income tax rate
- 2% or 12% withholding tax on royalty payments
- “Pioneer” industries are subject to an income tax rate of 1% or 0% in cases where the intangible property was created or developed in Puerto Rico
- Minimum combined tax rate of 3% if at least 50% of the exempt business shareholders are residents of Puerto Rico
- Minimum combined tax rate of 1% if a small or medium-sized business (average gross income of $10 million or less during the previous three years)
- The Tax Incentives – Act 273 also allows companies to take a tax credit on their corporate income tax return. Tax credits allow for:
- Job creation tax credit of $1,000, $2,500 or $5,000 depending on the physical location of the business operations
- 50% income tax credit of qualified R&D expenses
- 50% income tax credit for investment in machinery and equipment for the production of energy using renewable resources
- 25% income tax credit for the purchase of locally manufactured products
- Up to 10% credit to reduce the electric energy cost of the exempt industrial business