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Global Tax Alert

News from Americas Tax Center

Puerto Rico's new Incentives Code includes various tax incentives for investments in opportunity zones

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On 1 July 2019, the Governor of Puerto Rico signed into law Act 60, also known as the Puerto Rico Tax Incentives Code (Incentives Code), which consolidated dozens of tax decrees, incentives, subsidies and tax benefits in a single statute, including Act No. 21 of 14 May 2019, also known as the "*Development of Opportunity Zones of Economic Development Act of Puerto Rico of 2019*" (the Act). Through the enactment of the Incentives Code, the Act was repealed. However, most of the provisions of the Act establishing various tax incentives in Puerto Rico for investments in qualified opportunity zones were codified in the Incentives Code. For more information on the Act's proposed bill, see EY Global Tax Alert, [Puerto Rico's Governor proposes tax incentives for Opportunity Zones](#), dated 5 February 2019.

The tax incentives for investments in qualified opportunity zones include preferential tax rates, transferable tax credits, and partial exemptions of property and municipal taxes. Generally, these incentives are available to an eligible business under the Act that complies with certain requirements, including being certified as a priority project. The eligible business is required to file an application to request the benefits, and if approved, it will be issued with a tax grant. A tax grant constitutes a contract between the parties. This Tax Alert highlights some of the tax incentives for opportunity zone projects under the Incentives Code, as well as a recent change related to when the list designating all the commercial activities and eligible businesses that are recognized as priority projects in a qualified opportunity zone will be issued.

The following tables summarize the tax incentives under the Incentives Code:

| Income tax provision | Benefit |
|--|--|
| Net income from opportunity zones | The net income is subject to a fixed 18.5% income tax rate. |
| Royalty payments and licensing made to foreign entities and nonresident individuals not engaged in a trade or business in Puerto Rico for the use of intangible property related to the exempt operation | Such payments are subject to a fixed 18.5% income tax rate and withholding at source. |
| Dividend distributions | Dividend distributions are tax exempt and not subject to the alternative minimum tax, the additional tax on corporations improperly accumulating surplus or profits, and the alternative minimum tax on individuals. |
| Sale or exchange of assets | Gains from the sale or exchange of assets are tax exempt, if the gains are reinvested to maintain the 90% asset threshold of Section 1400Z-2(d)(1) of the United States Internal Revenue Code of 1986, as amended. |
| Interest payments | Interest payments are tax exempt if they are related to bonds, promissory notes or other obligations of an exempt business, provided certain criteria is met. |
| Tax credits | <p>Taxpayers are allowed a tax credit of up to 25% of cash contributed by investors in exchange for shares or a membership interest of: (i) an opportunity zone fund which in turn contributes the money to the exempt business in exchange for shares or a membership interest in the exempt business and (ii) an exempt business when such exempt business is carried out directly by the fund.</p> <p>The credit is available in four installments and any amount not used in a year can be carried forward until exhausted; and may be sold or transferred to third parties.</p> |
| Capital gains | <p>A taxpayer may elect to defer capital gains from the sale of a capital asset to nonrelated parties, if the gains are reinvested in an opportunity zone fund 180 days after the sale or exchange of the capital asset.</p> <p>The capital gains may be deferred until the investment on the opportunity zone fund is sold or exchanged or 31 December 2026, whichever is earlier.</p> <p>In computing any gain, the basis on the investment held in the opportunity zone fund may be gradually increased depending on the number of years in which the investment is held.</p> |

| Property taxes | Benefit |
|-----------------------|---|
| Personal property tax | Taxpayers are allowed a 25% exemption from the personal property tax. Municipalities may increase the exemption to up to 75% by municipalities. |
| Real property tax | Taxpayers are allowed a 25% exemption from the real property tax. Municipalities may increase the exemption to up to 75%. |

| Municipal license tax/ Construction excise tax | Benefit |
|---|---|
| Municipal license tax/Construction excise tax | <p>A tax-exempt business is allowed a 25% exemption from the municipal license tax, the construction excise tax or any other municipal tax imposed by municipal decree.</p> <p>A tax-exempt business also is allowed a 25% exemption from construction taxes imposed by the municipality (excluding municipal license tax) that are applicable to the exempt business, as well as its contractors or subcontractors, on the construction activities.</p> <p>Municipalities may increase the exemption to up to 75%.</p> <p>The taxable portion will be subject to the current rates at the date of the signing of the tax grant.</p> <p>Dividends and distributions from tax-exempt businesses are exempt from municipal taxes.</p> |

Implications

Approximately 95% of the territory of Puerto Rico is considered a qualified opportunity zone under the parameters established by the United States (US) Federal Government. The opportunity zone provisions under the Incentives Code are intended to align local tax statutes with the benefits afforded under the *US Tax Cuts and Jobs Act of 2017*. In addition to the preferential income tax treatment, the local statute provides for reductions in other local taxes and a transferable tax credit of up to 25% of cash contributed. These provisions, among other benefits like the expedited permitting process, are intended to make Puerto Rico's market more appealing for investors looking to take advantage of opportunity zones.

The Act's repeal affected the issuance of the list designating the commercial activities or eligible businesses by geographic area that will be recognized as priority projects in a qualified opportunity zone. Under the Act, a committee was supposed to issue the list by 13 July 2019. Under the provisions of the Incentives Code, this deadline has been pushed to 31 July 2019.

Government officials have stated that they are working on guidance related to statutory interpretation (i.e., resolution with list of priority projects within an opportunity zone) and administrative procedures (i.e., process for requesting a tax decree). We will continue monitoring the events and will issue updates as more information becomes available.

For additional information with respect to this Alert, please contact the following:

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