DOING BUSINESS

IN PUERTO RICO

The network for doing business

CONTENTS

1 – INTRODUCTION

UHY is an international organisation providing accountancy, business management and consultancy services through financial business centres in around 90 countries throughout the world.

Business partners work together through the network to conduct transnational operations for clients as well as offering specialist knowledge and experience within their own national borders. Global specialists in various industry and market sectors are also available for consultation.

This detailed report providing key issues and information for investors considering business operations in Puerto Rico has been provided by the office of UHY representatives:

UHY DEL VALLE & NIEVES PSC
PO Box 361863
San Juan, PR 00936-1863
Puerto Rico

Phone +1 787 793 4650
Website www.uhy-pr.com

You are welcome to contact Rafael Del Valle-Vega (r.delvalle@uhy-pr.com) for any inquiries you may have.

A detailed firm profile for UHY's representation in Puerto Rico can be found in section 8.

Information in the following pages has been updated so that they are effective at the date shown, but inevitably they are both general and subject to change and should be used for guidance only. For specific matters, investors are strongly advised to obtain further information and take professional advice before making any decisions. This publication is current at September 2015.

We look forward to helping you do business in Puerto Rico.

2 – BUSINESS ENVIRONMENT

The Commonwealth of Puerto Rico is a semi-autonomous territory of the United States located in the north-eastern Caribbean, east of the Dominican Republic and west of the Virgin Islands.

Puerto Rico has a republican form of government, which is subject to the jurisdiction and sovereignty of the United States of America. The president of the United States is the head of state.

The government of Puerto Rico is composed of three branches – executive, legislative, and judicial. The executive branch is headed by the governor. The legislative branch consists of a bicameral legislative assembly made up of a Senate and a House of Representatives. The judicial branch is headed by the Chief Justice of the Puerto Rico Supreme Court. The governor and legislators are elected by popular vote every four years. The governor, with the advice and consent of the Senate, appoints members of the judicial branch.

Puerto Rico has 78 municipalities. Each municipality has a mayor and a municipal legislature elected for a four-year term.

POPULATION
The territory had a population of almost four million inhabitants (3.5m) according to the census of 2014.

AREA
The territory is 9,104 square kilometres (3,515 square miles), including the neighbouring islands of Vieques and Culebra. The maximum length from east to west is 180km (110 miles) and the maximum width from north to south is 64km (40 miles).

CURRENCY
The currency of the territory is the US dollar (USD).

LANGUAGE
The official languages are Spanish and English, with Spanish being the primary language.

THE ECONOMY
Puerto Rico had an estimated per capita gross domestic product (GDP) of USD 19,801.39 in 2013.

UNEMPLOYMENT
The unemployment rate in Puerto Rico is around 12.2% (as at April 2015).

3 – FOREIGN INVESTMENT

FINANCING

Credit for financing a business may be obtained from commercial banks doing business in Puerto Rico including United States or foreign banks.

In addition, the Government Development Bank for Puerto Rico (GDB) may provide financing.

An affiliate of the GDB, the Puerto Rico Industrial, Tourist, Educational, Medical and Environmental Control Facilities Financing Authority (AFICA), also provides an alternative method for financing investment capital in Puerto Rico for projects in the public and private sectors in order to promote economic development.

In addition, the Economic Development Bank, which targets small- and medium-sized entrepreneurs, is another source for financing a business.

INCENTIVES

Puerto Rico has approved legislation intended to provide the right opportunities for continued development of local industry, to offer an attractive tax environment for foreign investment and promote economic development and social improvement in Puerto Rico.

With this purpose in mind, several incentive acts and programs for specific types of industries or services have been enacted and are described below:

- Economic Incentives for the Development of Puerto Rico Act of 2008
- Tourist Development Act of 2010
- Film Industry Development Act
- Foreign Trade Zones Incentives
- Green Energy Incentives Act of 2010
- Export Services Act of 2012
- Act to Incentivise the Transfer of Individual Investors to Puerto Rico of 2012
- Agricultural Incentive Act of 1995
- International Financial Entities Act of 2012
- International Insurer and Reinsurer Act of 2011
- Cruises Industry Incentive Act of 2011

ECONOMIC INCENTIVES FOR THE DEVELOPMENT OF PUERTO RICO (EIDA)

This Act became effective on 1 July 2008 and is focused on attracting and developing high-technology enterprises like bioscience, information technology and professional services firms.

FLAT INCOME TAX RATE

The law provides a flat income tax rate on the income derived from an exempted business. An exempted business is an eligible business established or yet to be established by a natural or juridical person, or combination thereof, organised under a common name, which has been granted one of various tax exemptions, but excluding hotel, inns, and other special facilities that are exempted under specified acts.

ELIGIBLE BUSINESSES

Eligible businesses include manufacturing and service units, property devoted to industrial development, research operations, industrial units for the production of energy, recycling activities, software developers, renewable energy equipment assemblers, certain strategic projects, and construction of social interest housing and planning and development of self-sustainable housing projects.

RATES

The income tax rates for new businesses are:

- 4% as a general rule (during the period of the exemption). An exempted business in a low or intermediate development zone may reduce the tax rate by an additional 0.5%
- 0% in the municipalities of Vieques and Culebra during the first ten years and 2% thereafter
- 0% on certain eligible investment income
- 100% exemption on dividends
- 0% tax on liquidations.

For an innovative pioneer activity, the flat income tax rate is 1%. The Secretary of the Department of Economic Development shall determine what an 'innovative pioneer activity' is, after considering the factors indicated in the law. The income from intangible property created or developed in Puerto Rico shall be 100% exempt.

SPECIAL DEDUCTION

EIDA allows an exempted business the option of deducting in the year incurred (in lieu of capitalising and depreciating them) the expenses incurred in the acquisition or construction of buildings and structures, and machinery and equipment not previously used or depreciated in Puerto Rico, if deployed for manufacturing or the rendering of the exempted service.

CREDITS

The law also allows credits for:

- The purchase of products manufactured in Puerto Rico
- The creation of jobs
- Investment in research and development, clinical and toxicological tests, infrastructure, energy renewal or intangible property
- Investment in machinery and equipment for the production and efficient use of energy
- Reduction in the cost of electric energy
- Investment in the transfer of technology
- Investment in strategic projects
- Industrial investment of the investor or investors.

PERIOD OF EXEMPTION

The exemption period is 15 years and the exempted business has the option of selecting the years to be covered with respect to the income tax exemption when they notify the Secretary of the Treasury and the Executive Director of the Puerto Rico Industrial Development Company (PRIDCO) within the time prescribed.

APPLICATION FOR EXEMPTION

Any person may request the benefits of the EIDA by filing a request under oath, together with a service fee, with the Industrial Exemption Office.

PROPERTY TAX EXEMPTION

There are the following property tax exemptions:

- 90% exemption on eligible real and personal property
- 100% exemption on real property for corporate headquarters engaged in rendering centralised management services during the first five years and 90% exemption thereafter
- 100% exemption on real property during the construction or expansion period as authorised in the tax decree.

Election for self-assessment of real property not previously assessed brings:

- 90% exemption
  - The property shall be assessed at 35% of the book value or at a minimal residual value, whichever is higher. The minimal residual value for the useful life of the property shall be:
    - 2 – 5 years 25%
    - 6 – 10 years 17%
    - 11 – 15 years 15%
    - 16 years and more 10%

An annual real property tax return shall be filed on or before 15 May. The election requires the payment of the real property tax for the current and four prior taxable years, or the number of years the business was in operation, whichever is less. The tax for the prior years may be paid in two instalments, the first one with the corresponding return and the second one within six months.

MUNICIPAL LICENCE TAX

For municipal licence tax, there are the following exemptions:

- 60% exemption
- 90% exemption for businesses in the municipalities of Vieques and Culebra
- 75% exemption for small- and medium-sized businesses. These are classified as businesses whose average gross income for the preceding three years does not exceed USD 10 million. For existing businesses, the 75% exemption shall be on the volume of business in excess of the average for the prior three years
- 100% exemption for central or regional corporate headquarters engaged in rendering centralised management services during the first five years, and 90% exemption thereafter
- 100% exemption during the first semester of commencing operations and during the following two semesters if requested from the municipality
- 100% exemption on eligible investments.

A business may give up the 5% discount for prompt payment of the tax in order to reduce the statute of limitation period from four years to three years.

CONSTRUCTION EXCISE TAX

The construction excise tax includes:

- 100% exemption for exempted business, and their contractors and subcontractors, on any construction to be used by the exempted business during the period authorised by the grant of tax exemption.

Municipalities may grant a total or partial credit for the total cost in self-sustainable housing projects.

EXCISE AND SALES AND USE TAX

Where excise and sales and use tax are concerned, there is:

- 100% exemption on raw materials (excluding hydraulic cement, crude oil, unfinished or end products derived from oil, and other hydrocarbon mixtures), manufacturing machinery, equipment and vehicles and accessories used in the exempt operations, energy efficiency equipment certified by Energy Affairs Administration, etc.

TOURISM DEVELOPMENT ACT

The Tourism Development Act of Puerto Rico is intended to facilitate the establishment of tourism development projects throughout Puerto Rico.

This Act provides incentives for the ownership or administration of hotels, condo hotels, timeshares/vacation clubs, hostels, guesthouses, excluding the operations of casinos. Also includes incentive for the ownership or administration of theme parks, golf courses, marinas for tourism purposes, port facilities in areas which promote tourism activities, natural resources as a source of entertainment value, and other entertainment or recreational tourism-related facilities. The Act also includes business operations dedicated to renting or leasing to an exempt business dedicated to tourism-related activities.

It also provides financial benefits for developers and investors in the tourism industry. For granting a tax exemption, the physical facilities of the business, number of jobs, total payroll, and total investment, location of the project, environmental impact and other factors which merit the exemption are considered.

TAX BENEFITS

Benefits on the following taxes apply:

- Income tax – 90% exemption on tourist development income or 100% exemption on tourist development income if established in Vieques or Culebra during a ten-year period. The tourist development income is the income derived by the exempted business from the operation of a tourist activity, and the income from the reinvestment in Puerto Rico in a tourist activity of the profits of an exempted business derived from a tourist activity
  - The tourist development income will not be subject to the alternative minimum tax or to the additional tax on corporations and partnerships improperly accumulating surplus or profits, nor to the basic alternative tax for individuals

- Property tax – 90% exemption during a ten-year period from real and personal property taxes. The stock of an exempt corporation or the interest in an exempt partnership is 100% exempt
- Municipal licence tax – 100% exemption to new businesses with respect to licence fees, excise taxes and other municipal taxes. An existing business will enjoy 90% exemption. The exemption is for ten years
  - The contractors and subcontractors performing work for an exempt business shall determine their volume of business for municipal licence tax purposes, by deducting the payments required to be made to subcontractors under the principal contract of the exempt business. The subcontractors which at the same time use other subcontractors in the same project shall also reduce these payments in the determination of business volume. The contractor or subcontractor must certify to the Executive Director of the Puerto Rico Tourism Company that he did not include in the contract executed for the work or services to be performed with respect to the exempt business, an item equivalent to the municipal licence tax attributable to the volume of business reduced. Every contractor and subcontractor performing work for an exempt business shall file copy of every contract related to such work, in the municipality or municipalities where such works are performed, within ten calendar days from their execution, providing the name, physical and postal address and social security number of the subcontractor
- Excise tax – up to 100% exemption during a ten-year period with respect to articles manufactured in Puerto Rico used in connection with the tourist activity. The exemption is also applicable to articles acquired outside of Puerto Rico if the exempted business demonstrates that it made a genuine effort to acquire the manufactured articles in Puerto Rico, but the acquisition was not feasible after considering the quality, quantity, price or availability of the same in Puerto Rico
  - The exemption shall not be applicable to articles which are properly part of the inventory, property principally held for sale in the regular course of the business nor to the hotel room occupancy tax
- Municipal construction taxes – up to 100% exemption during a ten-year period for the exempted businesses and their contractors on any tax, levy, fee, licence, excise tax, import tax or duty on the construction of works to be devoted to a tourist-related activity
- Sales and use tax – up to 100% exemption with respect to articles manufactured in Puerto Rico used in connection with the tourist activity. The exemption is also applicable to articles acquired outside of Puerto Rico if the exempted business demonstrates that it made a genuine effort to acquire the manufactured articles in Puerto Rico, but the acquisition was not feasible after considering the quality, quantity, price or availability of the same in Puerto Rico
  - The exemption shall not be applicable to articles which are properly part of the inventory, property principally held for sale in the regular course of the business nor to the hotel room occupancy tax. The exempt business must present to the selling merchant the Certificate for Exempt Purchases (Form SC 2916), and shall indicate the Tax Exemption Grant number.

Commencement dates of the exemptions are as follows:

- Income tax – from the first day in which the tourist activity commenced, but not before the date on which the application was duly filed
- Property tax:

- Existing businesses – from 1 January of the calendar year during which the application for exemption was duly filed

- New businesses – from 1 January of the calendar year in which the tourist activity commenced

- Municipal licence tax – 1 July next following the date on which the application for exemption was duly filed
- Excise tax – 30 days after the date on which the application for exemption was filed, provided that the bond required was posted before the date selected and the application has not been denied. If the application for exemption is denied, the excise taxes shall be paid within 60 days from the notification of the denial
- Municipal construction tax – as of the date on which the application for exemption was filed. In the case of condo hotels, contractors and subcontractors, the exemption shall commence from the date the developer files the petition for an original concession which describes the nature of the project and which meets the requirements established by the Executive Director of the Puerto Rico Tourism Company
- Distributions – distributions from tourist development income before the expiration of the grant will be subject to income tax (if any) only once. Subsequent distributions will be exempt from additional taxation
- Sales or exchange – gain or loss resulting from the sale or exchange of stock, shares in partnerships, shares in joint ventures or of substantially all the assets of an exempted business is recognised in the same proportion as the tourist industry development income of the exempted business is subject to tax, provided that the property continues to be engaged in a tourist activity for a period of at least 24 months after the sale. This requirement does not apply when the seller is neither the developer nor someone who exercises any control over the exempted business
- Flexible tax exemption – the exempted business is entitled to elect the years to be covered by the income exemption by attaching a notification to this effect to the income tax return for the year on or before the date prescribed for filing, including extensions.

DEDUCTION AND CARRYOVER OF NET LOSSES

Net losses not from a tourist activity will be deductible exclusively against income other than tourist activity. Net losses from the tourist activity will be deducted in an amount equal to the percentage that the tourist development income would have been taxable.

Special rules are provided for distribution of revenues among owners of condo hotel units and the operator of the integrated leasing programs established for said condo hotels. The rules are for income tax, municipal licence tax and property tax purposes:

- Postposition of the date of commencement of the exemption – the exempt business has the option of postponing the commencement date of the income tax exemption by filing a notice to that effect with the Executive Director of the Puerto Rico Tourism Company and with the Secretary of the Puerto Rico Treasury. The commencement dates may not be postponed for a period in excess of 36 months
- Extension of exemption period – an exempt business may request an extension of its exemption for an additional ten years by filing a request with the Executive Director of the Puerto Rico Tourism Company not later than the date prescribed for filing the income tax return of the last taxable year of the exemption period, including extensions

- Renegotiation of a tax exemption decree – the Act contain provisions for renegotiation of a tax exemption decree granted under the previous Tourist Incentives Act of 1983 provided compliance with certain requirements
- Transfer of an exempted business – generally the transfer of the exemption granted, or of the stock, participations or other proprietary interest in an exempted business, must be previously approved by the Executive Director of the Puerto Rico Tourism Company. However, the following transfers are exempted from the prior-approval requirement:
  - The transfer of assets of a decedent to his estate or the transfer by bequest or inheritance
  - The transfer of the shares of a corporation or participation in a partnership that does not result in a change of ownership or control of the exempted business
  - A pledge or mortgage given in the normal course of business solely for the purpose of creating security for bona fide indebtedness. However, a transfer of any control, title or resulting interest requires the prior approval of the Executive Director of the Puerto Rico Tourism Company
  - A transfer by operation of law, by a court order or by a bankruptcy judge to a receiver or trustee. Any subsequent transfer to a third party other than the same debtor or former bankrupt requires the prior approval of the Executive Director of the Puerto Rico Tourism Company
    - Transfers which do not require the prior approval of the Executive Director of the Puerto Rico Tourism Company shall be reported to him within 30 days
- Application for the exemption – an application for exemption under the Act must be filed with de Executive Director of the Puerto Rico Tourism Company and with the Secretary of the Puerto Rico Treasury. A negative debt certificate from the Department of the Treasury, from the Labour and Human Resources Department, from the State Insurance Fund, and from the Municipal Revenue Collection Centre must also be submitted. In addition the petitioner must show that he has no outstanding balance with respect to the room occupancy tax
  - Regulations under the Act indicate additional documents to be included together with the application for the exemption
- Filing fee – the filing fee is USD 1,500 (USD 500 in the case of paradores and hostelries of 15 rooms or less and of individual units of a condo hotel), plus 1/10 of 1% of the amount of investment tax credit claimed, if any. The fee is payable by certified check, or money order to the order of the Executive Director of the Tourism Company
- Accounting records and other requirements – the exempted business is required to maintain separate accounting with respect to the tourist activity and any income taxes from tourist development will be computed separately. The exempted business must also comply with the requirements established by regulations or otherwise by the Executive Director of the Puerto Rico Tourism Company
- Investment credit – a person making an eligible investment in a tourist activity is entitled to a credit against any income tax, including the alternative minimum tax. The credit is equal to 50% of the eligible investment or the investment in fund securities, to be taken in two instalments: the first half in the year in which the exempt business obtained the necessary financing for the construction of the total tourist project, and the balance in the following year. The maximum amount of the credit shall not exceed the lesser of, 10% of the total cost of the tourist project or 50% of the cash contributed to the exempt business in exchange for shares or participations in the exempted business. The maximum amount of the credit is distributed among the investors and participants in the proportion desired by them

- Eligible investment – an eligible investment means:
  - The cash or fair market value of land contributed to an exempt business to be used in a tourist activity in exchange for shares or participations or in exchange for a unit in a condo hotel devoted to integrated rental program for a period of ten years and for 11 months of every calendar year fully owned by the investor who acquires the unit directly from the developer in the first purchase and sale transaction
  - The cash contributions made by a fund that as an investment vehicle functions pursuant to the purposes and complies with the requirements of the Act
  - Any credit not used in a taxable year may be carried over to subsequent taxable years until exhausted

In cases when the investment credit taken by the investor exceeds the credit allowed, the excess credit will be due as an income tax payable by the investor in two instalments. In the case of a condo hotel, a recapture is also provided for the withdrawal from an integrated rental program before the end of a ten-year period.

With certain exceptions, investments under the 1996 Investment Capital Fund Act are also entitled to the credit.

FILM INDUSTRY DEVELOPMENT ACT

This Act was approved to promote the cinematographic industry and other related activities, to create incentives for private investment, to attract foreign investment and to create an adequate infrastructure. The Act defines and installs the necessary mechanisms.

The Act will expire on 31 December 2019. It provides for the following set out below.

TAXATION OF FILM PROJECTS

A 7% fixed tax rate is applicable on income directly derived by a film entity for a film project or an infrastructure project. The activities covered by a 'film project' are productions of:

- Feature length motion pictures
- Short subjects:
  - For distribution outside Puerto Rico
  - Which do not constitute promotion of another film project, and
  - have a budget of no less than USD 100,000
- Series of episodes, which:
  - Are for distribution outside Puerto Rico
  - Have a budget of no less than USD 1,000,000
- Catalogues for the sale of articles through the photographic exhibition of professional models for distribution in Puerto Rico
- Original sound track recordings
- Television programs to be broadcast or distributed within and outside of Puerto Rico and having a minimum budget of USD 100,000.

The dividends or profit distributions derived by the exempt entity shall be totally exempt from income taxes.

The period of exemption is ten years.

DEDUCTION AND CARRYOVER OF LOSSES

Deduction and carryover of losses against the income of a film project or infrastructure project, as the case may be, can take place. At the expiration of the exemption, the losses not claimed may be deducted against any taxable income, subject to the limitations established in the Internal Revenue Code of Puerto Rico.

The following exemptions apply:

- Property taxes – up to 90% exemption during a ten-year period starting on 1 January of the calendar year subsequent to the commencement of the film project or the infrastructure project
- Municipal taxes – 100% exemption during a ten-year period commencing on 1 January or 1 July subsequent to the date of filing the licence. With respect to construction excise taxes, the exemption commences on the date of filing the request for the licence
- Excise taxes on articles for use or consumption – 100% exemption on articles introduced directly and exclusively into the production of a film project or as part of an infrastructure project. The exemption commences 30 days after filing a request for a licence, provided a bond is posted. Excluded from the exemption are the materials used in the construction of buildings known as 'construction materials' and the machinery, equipment and accessories used in the administrative phase, merchandising, or articles not related to the incentives activities
- Excise tax on occupancy in hotel rooms – 100% exemption on rooms occupied by artistic personnel and technicians of film projects while realising the functions of those projects
- Postponement of date of commencement of the exemption – the film entity may opt to postpone any of the dates for commencement of the exemptions by filing a notice with the Executive Director of the Corporation for the Development of the Arts, Science and Cinematographic Industry of Puerto Rico and to the Secretary of the Treasury
- Income from the rental of real property to a film entity engaged in an infrastructure project – taxed at a fixed 7% rate if the property is used exclusively in an infrastructure project during a ten-year period
- Tax credit to an investor in a film project – the Act allows a credit of 40% of the budget for amounts paid to residents of Puerto Rico, as certified by a Certified Public Accountant (CPA) hired by the Executive Director of the Corporation for the development of the Arts, Science and Cinematographic Industry of Puerto Rico
  - In the case of a film project for the production of a television program, the tax credit is limited to 25% of the budget for amounts paid to residents of Puerto Rico as certified by the CPA hired by the Executive Director of the Corporation for the development of the Arts, Science and Cinematographic Industry of Puerto Rico.
  - The credit shall not exceed 50% of the real capital contributed to the film entity in exchange for stock or participation in a primary issuance. The items in the budget for the acquisition of assets to be capitalised do not generate tax credits, except for the assets to be located in Puerto Rico during their useful life or for no less than five years, whichever is less
  - No credit is allowed for payments to residents of Puerto Rico from any type of government contributions

- As a general rule, 50% of the tax credit is available in the tax year in which the CPA hired by the Executive Director of the Corporation for the development of the Arts, Science and Cinematographic Industry of Puerto Rico certifies to him and to the Secretary of the Treasury that 40% or more of the budget to be paid to residents of Puerto Rico has been paid and is in compliance with the law. The Secretary of the Treasury may accelerate the date in which the credit is available if the film entity posts a bond or bank credit card or guarantee in which the Secretary is the beneficiary
- The remaining 50% credit, or the total if no payment in advance was made, will be available in the year in which the CPA certifies to the Executive Director of the Corporation for the development of the Arts, Science and Cinematographic Industry of Puerto Rico the total of the items in the budget paid to residents of Puerto Rico and the real capital contributed to the film entity in exchange for stock or participations in a primary issuance. The Secretary of the Treasury will confirm in a letter the amount of the tax credits available to the investors of the Film Entity within 30 days after the certification of the CPA
- The certification of the CPA issued on or before the date for filing the income tax returns of the investors, including extensions, is considered as issued within the taxable year in which the return is to be filed

- Tax credit to an investor in an infrastructure project – at the request of a film entity the Executive Director of the Corporation for the development of the Arts, Science and Cinematographic Industry of Puerto Rico may treat separately the different stages of an infrastructure project and may authorise the credit by stages as if each stage were an infrastructure project when it is justified by the nature, size and importance of the project.
  - The credit will be a) 40% of the real investment in exchange for stock or participation in a primary issuance, or b)20% of the budget of the infrastructure project
  - Any investment originated from financing guaranteed by the film entity engaged in an infrastructure project or from its assets will not be considered as real investment
  - As a general rule, 50% of the tax credit is available in the tax year in which the CPA hired by the Executive Director of the Corporation for the Development of the Arts, Science and Cinematographic Industry of Puerto Rico certifies to the Secretary of the Treasury that 40% or more of the budget to be paid to residents of Puerto Rico has been paid. The film entity may accelerate the date of availability of the credit if it posts a bond in which the Secretary of the Treasury is the beneficiary
  - The remaining 50% tax credit will be available in the tax year in which the CPA certifies to the Secretary of the Treasury that the remaining 60% of the budget was paid and the project is substantially complete
  - The certification of the CPA issued on or before the date for filing the income tax returns of the investors, including extensions, is considered as issued within the taxable year in which the return is to be filed
  - The Act provides for a recapture of part of the credit when the infrastructure project ceases operations before the five-year's period which started on the day the eligible investment was made. No credit is allowed for payments to residents of Puerto Rico from any type of government contributions
- Maximum credits – the maximum of available credits per fiscal year is USD 15,000,000. However, the Secretary of the Treasury may increase that amount. The Executive Director of the Corporation for the Development of the Arts, Science and Cinematographic Industry of Puerto Rico will confirm in writing to the Film Entity the amount of the credits available

- Use of the tax credits – the tax credits may be used against the income tax of the investor in a film entity or by a cessionary, and can be transferred totally or partially. Any unused credit may be carried forward until exhausted. The money or value of the property received by an investor in exchange for a tax credit is tax exempt up to an amount equal to the amount of the credit transferred. When the amount paid for a credit is less that the amount of the credit, the difference in not considered income to the transferor, or loss to the investor
- Licence – a licence may be obtained by filing the "Solicitud de Inscripción para Operar como Entidad Fílmica" (Enrolment to Operate as a Film Entity). The licence obtained from the Executive Director of the Corporation for the development of the Arts, Science and Cinematographic Industry of Puerto Rico is non-transferable and the stock or participation of an investor in a film entity is equally non-transferable, except:
  - i) with the consent of the Executive Director of the Corporation for the development of the Arts, Science and Cinematographic Industry of Puerto Rico
  - ii) as result of the death of the investor, or
  - iii) by order of a court having jurisdiction
- Budget – this is the detail of payments to be made to residents of Puerto Rico which are necessary for the development of a film project or an infrastructure project, submitted for the consideration of the Executive Director of the Corporation for the development of the Arts, Science and Cinematographic Industry of Puerto Rico with the application for a licence.

FOREIGN TRADE ZONES INCENTIVES

Puerto Rico has the largest non-contiguous Foreign Trade Zone (FTZ) system in the United States.

The system allows companies to obtain significant financial savings, since raw materials, components and packaging can be transported tax-free throughout these zones and items shipped abroad (after processing) are exempt from United State tax. Benefits include:

- Deferment of federal customs duties and Puerto Rico excise taxes;
- 100% exemption on Municipal License Taxes on exports outside of the United States;
- 100% exemption on tangible property and equipment used;
- 60% exemption on the value of the property that is designated intangible; and
- 100% exemption on exports from the zone and sub-zones.

GREEN ENERGY INCENTIVES ACT OF 2010

Puerto Rico is entering a new age in terms of its diversification of energy sources with the implementation of a new public energy policy and programs to diversify energy sources, ensuring that the generation of electricity on the island is affordable, viable and sustainable.

The Green Energy Incentives Act of 2010 creates a Green Energy Fund (GEF) through which the government of Puerto Rico will co-invest USD 290 million in renewable energy projects over the next ten years.

Initially, funding of USD 20 million began on 1 July 2011 (and will rise to USD 40 million by the fiscal year 2016). Through the GEF, the PR Energy Affairs Administration will offer cash rebates of up to 60% on the cost of installing Tier 1 or small projects (0–100kW) for residences and small businesses and up to 50% on the cost of Tier 2 projects (100kW–1 MW) for commercial or industrial use. The Tier 1 rebate program is managed through a reservation process, whereas the Tier 2 program is managed through a quarterly competitive process ('reverse auction').

EXPORT SERVICES ACT OF 2012

The main objectives of the Export Services Act of 2011 are to turn Puerto Rico into an international hub of export services, retain local talent, attract foreign talent and foreign capital, and create a special fund for promoting the establishment of new businesses to export services from Puerto Rico.

The Act includes, but is not limited to, the following types of designated business activity (among many others):

- Research and development
- Advertising and public relations
- Economic, environmental, technological, scientific, managerial, marketing, human resources, information systems, engineering, auditing, and other consulting services
- Advising and consulting on matters related to any industry or business
- Commercial art and graphic services
- Production of engineering and architectural blue prints and designs
- Advanced professional services such as, legal, tax and auditing services
- Centralised managerial services including, but not limited to, strategic direction, planning and budgeting performed for affiliated entities and by a regional headquarters
- Electronic data processing centres.

The tax rate and tax incentive period are as follows:

- 4% income tax
- Tax can be reduced to 3% when:
  - More than 90% of all gross income of the company and its affiliates which conduct a designated business is derived from exporting services and
  - Rendered export services are considered Strategic Services, as described under the Act
- 0% income tax rate on dividends or profit distributions
- 90% exemption of real and property taxes on call centres, corporate headquarters and distribution centres
- A 20-year decree which can be extended by a period of ten years when designated businesses fulfil the requirements of employment, income, investment and other factors mentioned in the decree and prove to the Secretary that the extension of the decree will benefit the economic and social interests of Puerto Rico.

ACT TO INCENTIVISE THE TRANSFERRAL OF INDIVIDUAL INVESTORS TO PUERTO RICO OF 2012

The Act intends to mobilise investments (mutual funds, stocks, fixed income) from outside the country to Puerto Rico, through the movement of individuals (resident individual investors – RII) who have not been residents of PR during the 15 years prior to the approval of this Act.

The following exemptions apply:
- 100% tax exemption from Puerto Rico income taxes on all dividends;
- 100% tax exemption from Puerto Rico income taxes on all interest; and
- 100% tax exemption from Puerto Rico income taxes on all short-term and long-term capital gains accrued after the individual becomes a bona- fide resident of Puerto Rico ("Puerto Rico Gain").

The implementation of the Act aims to boost the economy of Puerto Rico through the consumption and investment of the new residents. The tax exemption is not for an unlimited time period, ending on 31 December 31, 2035.

AGRICULTURAL INCENTIVE ACT OF 1995

The Act provides incentives to bonafides farmers and agricultural businesses. Farming, animal breeding, agro-industrial operations and other agriculture related operations are considered eligible activities under this Act.

The Act offers those who qualify the following tax benefits:
- 100% exemption on taxes for agricultural equipment
- 100% exemption on property taxes (land, buildings, vehicles, etc.)
- 100% exemption on municipal taxes
- 100% exemption on stamp payments to PR's Treasury Department and fees to register a property
- 90% exemption on earning contribution from agricultural activity
- 50% tax credit for investment in eligible agricultural business

In addition, there other benefits as annual bonus for agricultural workers and wage subsidy program to eligible farmer, which can be requested as well.

INTERNATIONAL FINANCIAL ENTITIES ACT OF 2012

The Act expands Puerto Rico as an international financial centre and promotes 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.

An entity must obtain a license from the Commissioner of Financial Institutions to form an IFE in Puerto Rico. An IFE must be physically located in Puerto Rico, have authorized capital of at least $5,000,000, paid-in capital of at least 250,000, and $300,000 in unencumbered assets or other financial guarantees to obtain licensing, unless a lesser amount is requested by an interested party and approved at the Commissioner's discretion.

The application process requires financial statements of the preceding 10 years of any person who controls or intends to control 10% or more in capital of the proposed IFE. The Commissioner will issue or deny the licensure after an investigation and review of the proposed IFE.

A licensed IFE may obtain a Tax Exemption Decree for a term of 15 years, which may be renewed two additional terms.

Under this Act the following IFE activities are permitted:

- Accept demand deposits from non-residents of Puerto Rico for commercial purposes or otherwise borrow from other IFEs and non-residents under the Regulations of the Commissioner
- Accept adequately collateralized deposits or otherwise borrow money properly secured by the Government Development Bank of Puerto Rico (GDB) and the Economic Development Bank of Puerto Rico (EDB)
- Place deposits in any bank or any IFE
- Provide loans to any non-resident individuals or entities
- Issue or refinance letters of credit for any non-residents and for P.R. residents for financing exports
- Invest in securities of the government of P.R.
- Engage in foreign currency trade
- Trade securities outside of P.R. issued by non-residents

The Act offers those who qualify the following IFE tax incentives:

- 4% Income Tax on Permitted IFE Activities:
- 0% Property Tax on Real, personal, tangible, and intangible property

Also, the Act provides the following tax incentives to the IFE Shareholder:

- 6% Income Tax on Distributions for P.R. residents
- 0% income Tax on Distributions for non-residents

INTERNATIONAL INSURER AND REINSURER ACT OF 2011

The Act provides for the creation of international insurers, branches of international insurers, international reinsurers and holding companies. Protected cell plans and securitization plans are allowed. The Act facilitates the establishment of entities that export insurance and reinsurance services, allowing Puerto Rico to compete with jurisdictions such as Bermuda, the Cayman Islands and Vermont, which for years have successfully engaged in promoting this type of activity.

To qualify as an international insurer or reinsurer under the Act, an insurance company must be approved by the Insurance Commissioner. Tax exemptions conferred under the International Insurers and Reinsurers Act of Puerto Rico includes:

- Exemption from premium taxes,
- Exemption on dividends and other profit distributions made by the International Insurer and International Insurance Holding Company,
- Exemption on municipal franchise, real and personal property taxes,
- Exemption to the International Insurer and qualifying International Insurance Holding Company from withholding taxes on payments of dividends and other profit distributions made to third parties, and from filing tax returns with the Puerto Rico Internal Revenue Service,
- Isolation of the proceeds and benefits paid by international insurers from state and donation taxation procedures,
- $1.2 million tax exemption on net income. Exemption applicable at the individual cell level for protected cell company arrangements and at the company level. Preferred 4% tax rate on net income, guaranteed by a decree effective over a renewable period of 15 years.

International Insurers are also subject to an annual contribution based on premium level.

CRUISES INDUSTRY INCENTIVE ACT OF 2011

The Act strengthens the integral link between Puerto Rico's economy and its $3.6 billion tourism industry and its $250 million cruise industry. The Act establishes an annual promotional fund of $11 million designed to increase both homeport and transit cruise visits to Puerto Rico by providing several incentives.

The Act offers the following incentives:

- **Discounts on Port Tariff Incentive**
  The Act provides increasing benefits depending on the passenger volume in order to incentivize the cruise industry to increase passenger volume to Puerto Rico.
- **Cash Incentive for Homeport Embark**
  Also provides increasing cruising incentives through the Ports Authority, depending on the number of homeport cruise embarks, as a way to increase home-porting in Puerto Rico.
- **Cash Incentive for Time in Port**
  It is estimated that each cruise passenger on a transit ship spends $69.74 in Puerto Rico in restaurants, shops, transportation, excursions, among many others. A Cash Incentive for Time in Port was created to stimulate longer cruise ship stays in Puerto Rico ports in order to increase this expenditure.

- **Incentives for Purchases of Goods and Services**
  Puerto Rico has created Incentives for Purchases of Goods and Services that provide that any cruise ship that stops in any port in Puerto Rico's jurisdiction will be eligible to receive an incentive equivalent to 10% of the cost of the purchase of provisions and/or the cost of maintenance services or repairs that may be done on the cruise ships in Puerto Rico, excluding the cost of materials, products or equipment that may be installed as part of the service provided. An additional 5% reimbursement applies to the purchase of products that are manufactured in Puerto Rico, as certified by the Puerto Rico Industrial Development Company, or agricultural products of Puerto Rico, as certified by the Department of Agriculture.

- **Coop Marketing Program**
  The Act also creates a Coop Marketing Program to increase awareness of Puerto Rico as a homeport and to position Puerto Rico as the primary port of the Caribbean.

- **Incentive for Vacation Packages and Incentive for Tour Transportation Providers**
  The Act also creates an Incentive for Tour Transportation Providers that provides an incentive of $1.00 for every passenger that buys an excursion on board the cruise ship. The incentive has an annual cap of $500,000, and is regulated by the Tourism Company.

4 – SETTING UP A BUSINESS

There are many ways in which a business may be set up in Puerto Rico and the most common alternatives are set out below.

CORPORATION

A corporation is a legal form of organisation used to carry on a business enterprise. It is an entity separate and distinct from its shareholders, directors and officers.

A corporation has the power to enter into contracts and to hold property in its own name, to sue and be sued in its own name, to have continuity of life and free transferability of ownership interests.

Additionally, the liability of corporate shareholders for the acts of the corporation, except in certain cases, is limited to their investment in its stock. Management of the corporation is centralised in its board of directors.

PUERTO RICAN CORPORATIONS

Any natural person with legal capacity or any juridical person singly or jointly with another, may incorporate or organise a corporation by filing to the Department of State of Puerto Rico a certificate of incorporation which shall be executed, acknowledged, filed and recorded in accordance with the provisions of the General Corporation Law of Puerto Rico of 2009.

NON-PUERTO RICAN CORPORATIONS

Any corporation organised under the laws of any jurisdiction other than the Commonwealth of Puerto Rico may request a certificate of authorisation to do business in Puerto Rico by filing to the Department of State of Puerto Rico an application setting forth the information required by the General Corporation Law of Puerto Rico of 2009.

The approval to do business within Puerto Rico is usually granted as a matter of course as long as no other corporation is doing business under the same name and as long as the activity the corporation intends to pursue is one permitted under the law.

No foreign corporation shall do any business in the Commonwealth of Puerto Rico until it receives authorisation to do so, pursuant to the procedures established in the law.

A foreign corporation may establish a branch in Puerto Rico by filing the documents required.

ANNUAL CORPORATION REPORT

Every corporation (domestic or foreign) is required to file an annual corporation report with the Puerto Rico Department of State on or before 15 April each year. A USD 150 annual fee is payable when filing the report.

The report must include a balance sheet prepared to generally accepted accounting principles, showing the financial condition of the Puerto Rican operations of the corporation at the close of its year. The balance sheet must be audited and certified by a certified public accountant with a licence from the Commonwealth of Puerto Rico. The auditor's opinions must have the stamp from the Puerto Rico Association of Certified Public Accountants and the accountants' seal.

The balance sheet must be duly certified by a certified public accountant licensed in Puerto Rico only when the volume of business of the corporation exceeds USD 3,000,000. A non-Puerto Rican corporation whose volume of business does not exceed USD 3 million must include a balance sheet compiled by a certified public accountant in Puerto Rico.

The Annual Corporation Report is a public document available for anyone to see at the premises of the Department of State.

PARTNERSHIP

A partnership is an organisation of two or more persons who carry on business for profit.

It is a legal entity which can own property and sue or be sued in its own name. As a general rule, each member of a partnership is liable for the debts of the business and is held liable for the partnership's obligations.

Partnerships are subject to income taxes on the partnership's income. The liability for taxes applies regardless of whether the partnership's profits are distributed or retained.

Similarly, a distribution of the partnership profits is taxable to the recipient at a 10% rate, if the distribution is made by a domestic partnership or certain foreign partnerships.

LIMITED LIABILITY PARTNERSHIP

A limited liability partnership is a partnership formed by no less than two natural persons under the provisions of the Limited Liability Partnership Act, including those rendering professional services, or a related limited liability partnership. Its name must be followed by the words 'limited liability partnership' or 'sociedad de responsabilidad limitada', or the abbreviation 'L.L.P.', 'LLP', 'S.R.L.' or 'SRL'.

To be considered as a limited liability partnership, it must register with the Department of State by filing a certified copy of the constituent deed accompanied by payment of a USD 100 fee. The deed must contain the partnership name, the address of the principal office, the name and address of the managing partner and of each partner, and a brief description of the business.

A foreign limited liability partnership must also submit an application for registration, which needs to include information from the jurisdiction in which it was registered and the name of the person designated to receive summons.

A partner of a limited liability partnership is personally liable for the partnership obligations solely to the extent of his contribution to the partnership. He is not generally responsible for the obligations of other partners arising as result of error, omission, negligence, incompetence, or illicit acts committed by another partner, or employee, agent, or representative of the partnership.

LIMITED LIABILITY COMPANY

A limited liability company is a corporation formed by one or more persons who have executed the Limited Liability Company Certificate of Formation and filed it with the Puerto Rico Department of State. The certificate must state the name, address of the registered office and name and address of its resident agent. The company name must be followed by the words ‘Limited Liability Company’ or ‘Compañía de Responsabilidad Limitada’, or the abbreviations ‘LLC’, ‘L.L.C.’, ‘CRL’ or ‘C.R.L.’. The fee (currently in force) needs to accompany the Limited Liability Company Certificate of Formation.

A foreign LLC may register in Puerto Rico by providing a petition signed by an authorised person following the procedures specified in the General Corporation Act. When registered, it shall have some powers as a domestic LLC, provided that a foreign LLC’s internal affairs and the liability of its manager and members shall continue to be governed by laws of the jurisdiction where the LLC is organised.

A LLC may engage in any lawful activity. Each LLC must maintain a registered office and resident agent for services of process in Puerto Rico. A LLC is required to prepare the LLC Agreement, which sets out the duties of the LLC to its managers and members, and duties of these to the LLC and to each other, as well as the management structure of the LLC, the rights of the management and members and their respective share of interest in the LLC profits and losses.

Unless otherwise provided in the LLC Agreement, no manager or member is personally liable for the LLC’s obligations solely by reason of being a manager or member of the LLC.

An annual fee needs to be filed each year with the Puerto Rico Department of State with a payment of USD 100 in order to maintain a good standing with the agency.

CORPORATION OF INDIVIDUALS

A corporation of individuals is a corporation with only one class of stock and having no more than 75 shareholders who are individuals, estates, or certain trusts.

With limited exceptions, a corporation of individuals is not taxed at the corporate level; instead the items of income, loss, deduction, and credit are passed through to, and taken into account by, its shareholders or partners in computing their individual tax liabilities.

The corporation must be created under the laws of the Commonwealth of Puerto Rico or a corporation created under the laws of any state of the United States or the District of Columbia whose trade or business is exclusively in Puerto Rico, except for:

- An insurance company
- A registered investment company
- A special corporation owned by employees

- A corporation exempt under any tax incentives or similar acts, except under the Tourists Development Act
- Other exempt corporations
- A financial institution
- A corporation licensed as a capital investment fund.

Certain partnerships may also elect to be treated as a corporation of individuals.
The election to be considered as a corporation of individuals must be made by filing a Subchapter N Election with the Puerto Rico Treasury Department.

Generally the corporation (or partnership) can make the election for any taxable year:
1) At any time during the preceding tax year, or
2) At any time before the 15th day of the fourth month of the tax year, if filed during the tax year the election is to take effect.

TAX CONSEQUENCES OR CONSIDERATIONS FOR THE CORPORATION OF INDIVIDUALS

An electing corporation (or partnership) which used the LIFO inventory method, flexible or accelerated method of depreciation, long-term completed contract, or instalment sales method for the tax year prior to the election to be treated as a corporation of individuals, must recapture as income these items in the last year before the election is made. The increase in tax resulting from the recapture is payable with the final income tax return of the regular corporation (or partnership), except for the tax resulting from the LIFO recapture which is payable in three equal instalments over three taxable years. The first instalment is payable with the final return of the regular corporation (or partnership).

All accumulated earnings and profits of an electing corporation are deemed distributed during the first two years of the election and are generally subject to the 10% special tax on eligible distributions.

Before making the election, a corporation (or partnership) may be subject to a built-in gains tax at the corporate level during the ten-year period beginning on the first day of the corporation’s first tax year as a corporation of individuals.

REAL ESTATE INVESTMENT TRUSTS

A real estate investment trust (REIT) is a tax designation reserved for corporations investing in real property which reduces or eliminates corporate income taxes. The term ‘real property’ includes, among other things:

- Hospitals and related facilities
- Schools and/or universities
- Public and private housing
- Transportation facilities and private or public roads
- Office and residential buildings
- Buildings occupied by government agencies, departments or corporations of the government of Puerto Rico
- Manufacturing buildings and related facilities
- Recreational centres
- Parking facilities
- Shopping facilities and centres

- Buildings purchased from the government of Puerto Rico, its agencies and instrumentalities
- Hotels.

To qualify as a REIT under the Puerto Rican code, an entity must:

- Be organised as a corporation, partnership, trust, or association
- Have 50 or more shareholders or partners during at least 335 days over a 12-month period
- Be managed by one or more trustees or directors
- Evidence capital contributions with shares of transferable certificates
- Be treated for tax purposes as a Puerto Rican corporation (except for the provisions relating to REITs)
- Not be qualified as a financial institution or insurance company
- File an election to be treated as a REIT or have made such an election for a previous taxable year
- At the end of the first quarter of its first year as a REIT, have 50% or more of the total value of all the outstanding shares or participation certificates owned by more than five individuals.

A REIT also needs to comply with the following type-of-income and source-of-income requirements. Specifically, 95% or more of the gross income of the REIT must be derived from:

- Dividends
- Interest
- Rents from real property
- Gain from the sale or other disposition of securities or real property (including interests in real property and interests in mortgages on real property) which is not inventory, amounts received or accrued as consideration for entering into agreements either to make loans secured by mortgages on real property or to purchase or lease real property, and
- Gains from the sale or disposition of real property.

Moreover, 75% or more of the gross income of the REIT must be derived from:

- Rents from real property located in Puerto Rico
- Interest on obligations secured by mortgages on real property or rights to real property located in Puerto Rico
- Gains from the sale or other disposition of real property which is not of the type of property that qualifies as inventory
- Dividends or other distributions derived from, and gains derived from, the sale or other disposition of shares of transferable stock, certificates, or participation in another REIT, and
- Amounts received or accrued as consideration for entering into agreements to make loans secured by mortgages on real property and/or rights to real property located in Puerto Rico, and/or to buy or lease real property and/or rights to real property located in Puerto Rico.

REITs organised under the laws of the United States or a state of the United States (US REIT) must meet the following requirements to be treated as a REIT under the PR Code:

- The US REIT must have qualified as such under the US Internal Revenue Code during the taxable year
- The US REIT must invest in real property located in Puerto Rico and constructed after 30 June 30 1995
- The US REIT must file with the Puerto Rico Treasury Department, not less than 30 days before the first taxable year in which it wishes to be regarded under the PR Code as an exempt REIT, a sworn statement with the information required by the Department.

PUBLIC-PRIVATE PARTNERSHIPS

Act No. 29 of 8 June 2009 codified Puerto Rico's policy favouring the use of Public-Private Partnerships (PPPs) – contractual agreements between government agencies and private or non-governmental entities – as a means for achieving greater private sector participation in the development and financing of infrastructure and services, especially for priority projects, which include:

- Landfills
- Water reservoirs
- Power plants which use alternative sources of energy or renewable sources of energy
- Transportation systems
- Health, security, education, correctional and rehabilitation facilities
- Low-income housing projects
- Facilities for sport, recreation, tourism and cultural activities
- Ground and wireless communication systems
- High-technology information and mechanical systems
- Any other kinds of activity, facility or service identified as a priority project through legislation.

Act No. 29 creates a Public-Private Partnership Authority as a public corporation of the government of Puerto Rico, attached to the Government Development Bank for Puerto Rico (GDB). The Authority is designated as the sole government entity authorised and responsible for implementing the public policy on partnerships and for determining the functions, services or facilities for which such partnerships are to be established.

The Authority shall establish priorities in the development of projects, in order for partnership contracts to address infrastructure needs or services which are a priority for the government of Puerto Rico. The Authority, with the support of the GDB, shall conduct analysis on the desirability and convenience of the project as necessary to determine whether it is advisable to carry out the project and establish such a partnership.

Generally, contractors in a partnership established under the PPP Act receive special tax treatment. For example, such contracts will typically pay a fixed income tax rate of 10% over the net income derived from the operations provided in the Partnership Contract and receive exemptions from paying taxes on personal property.

BASIC REQUIREMENT OF LICENSING AND REGISTRATION FOR STARTING A BUSINESS

REQUESTING AND REGISTERING AN EMPLOYER IDENTIFICATION NUMBER (EIN)

Except for sole proprietorships which do not employ anyone (other than the sole proprietor), every entity engaged in a trade or business in Puerto Rico must obtain a federal Employer Identification Number from the US Internal Revenue Service (IRS) by filing Form SS-4. Upon obtaining an EIN, the entity must file with the PR Department of Treasury a Form SC-4809, a copy of the certificate of incorporation and a copy of Form SS-4.

MERCHANT'S REGISTRATION CERTIFICATE

All merchants seeking to engage in a trade or business in Puerto Rico must register with the Puerto Rico Treasury Department Merchant Registry of Businesses at least 30 days prior to commencing business operations. The Certificate of Registration issued by the Treasury Department must be placed in a location at the trade or business which is visible to the general public.

A merchant may not transfer its Certificate of Registration or Certificate of Exemption unless the transfer is previously approved by the Secretary of the Treasury.

Any merchant who acquires taxable items for resale or any manufacturing plant may request a certificate of exemption of the sales and use tax. Every certificate of exemption is valid for three years. The exemption certificate is important because every merchant who has been issued this certificate will not have to pay sale tax when he/she purchases the items listed in the certificate.

BIDDERS REGISTRY

Any person (natural or juridical) who wants to pursue business with any agency from the executive branch of the government of Puerto Rico is required to register with the Bidders Registry. This registry is administered by the General Services Administration (GSA) and it is through them that the application has to be filed. Requirements for entering the Bidders Registry include:

- An annual fee, which will depend if the application is filed by a corporation, individual, partnership, etc.
- A copy of the payment of municipal taxes
- A certificate which shows the payment of taxes in the Treasury Department of Puerto Rico
- Certain other documentation which varies according to the type of business/service.

INTERNAL REVENUE LICENCES

A licence from the Puerto Rico Treasury Department may be required to carry out certain activities, including:

- Selling cigarettes, gasoline, vehicles and parts and accessories of vehicles, jewellery, cement, arms and ammunitions
- Operating coin-operated machines
- Operating duty-free port stores
- Selling firearms and munitions
- Operating public carrier businesses.

Such licences may not be transferred without the authorisation of the Puerto Rico Secretary of the Treasury. A manufacturer of articles whose sale requires a licence is not required to have such a licence, provided the manufacturing operations are completely apart from any location in which an activity subject to such a licence is conducted.

5 – LABOUR

WAGES

The United States Federal Fair Labour Standards Act (FLSA) applies in Puerto Rico.

Employers covered by the FLSA are subject only to the federal minimum wage and all applicable regulations. Employers not covered by this act are subject to a minimum wage which is at least 70% of the federal minimum wage, or the applicable mandatory decree rate, whichever is higher. The Secretary of Labour and Human Resources of Puerto Rico may authorise a rate based on a lower percentage for any employer who can show that implementation of the 70% rate would substantially curtail employment in that business.

The FLSA establishes the minimum wage, overtime pay, record keeping, and youth employment standards which affect employees in the private sector and in federal, state, and local governments. Covered non-exempt employees are entitled to a minimum wage of not less than USD 7.25 per hour effective 24 July 2009.

Puerto Rico also has minimum wage rates which vary according to the industry. These rates range from a minimum of USD 4.25 to USD 7.25 per hour.

UNEMPLOYMENT TAXES

FEDERAL UNEMPLOYMENT TAX

The provisions of the Federal Unemployment Tax Act (FUTA) apply in Puerto Rico as well as in the United States.

The tax is imposed on persons who employ one or more individuals for a portion of a day in each of 20 weeks in the current or preceding calendar year, or who pay in the aggregate USD 1,500 or more of wages in a calendar quarter of the current or preceding calendar year.

The FUTA tax rate for 2015 is 0.6% after a credit of 5.4% for the Puerto Rican unemployment tax on the first USD 7,000 of wages paid to an employee each calendar year.

The tax is deposited quarterly. Any excess is deposited with the last quarterly instalment along with the annual return Form 940-PR due on 31 January. The address to which the form should be filed depends on whether payment is included or not. When there is no payment, the return should be filed with Internal Revenue Service, P. O. Box 409101, Ogden, UT 84409. When payment is included, the form should be filed with the Internal Revenue Service, P.O. Box 105174, Atlanta GA 30348-5174.

The taxpayer can file and pay electronically by using electronic options available from the Internal Revenue Service.

PUERTO RICO UNEMPLOYMENT TAX

Each employer pays this tax on the first USD 7,000 of annual wages, based on an experience rating system.

In addition, every employer must pay a special tax of 1% of all taxable wages. However, the special tax, together with the experience-based tax, will not exceed 5.4% and may be credited against the Federal Unemployment tax mentioned above.

The total tax is paid by the employer and applies to every employer having one or more employees. The tax is paid quarterly on the last day of the calendar month following each calendar quarter. The cheque for payment of the tax should be made payable to the Secretary of the Treasury of Puerto Rico.

SOCIAL SECURITY

The provisions of the United States Federal Insurance Contributions Act (FICA) apply in Puerto Rico.

Under this act, both employers and employees are required to contribute to the Social Security Fund which was established to provide retirement benefits for all workers.

The tax rate is 7.65% for employers and 7.65% for employees. The percentages are comprised as follow:

	SOCIAL SECURITY	HOSPITAL INSURANCE
Employer	6.20%	1.45%

The maximum social security wage base for 2014 and 2015 is as follow: USD 117,000 and USD 118,500; and the 1.45% for hospital insurance are computed on all wages regardless of amount.

Self-employed individuals are subject to the total 15.3% tax rate on net earnings from carrying on a trade or business.

DISABILITY BENEFITS TAX

The Disability Benefit Act provides benefit payments to employed workers who suffer the loss of wages as a result of incapacity to perform their customary work due to injury, illness or pregnancy.

This Act provides a tax of 0.60% on the first USD 9,000 of wages paid during the calendar year by an employer to an employee. Both the employer and employee share the tax evenly. An employer can set up a private plan to cover the benefits provided in this act.

Employers subject to the chauffer social security tax are not subject to this tax.

WORKMEN'S COMPENSATION

Workmen's compensation provides for indemnification for accidents incidental to or as a consequence of the employment. All employees of a business, including executive officers, are covered. The rate varies according to the type of labour performed by the employee. Rates are revised every year. The tax is entirely borne by the employer and is usually paid in two instalments.

WORKER BONUSES

CHRISTMAS BONUS

Every employee having worked at least 700 hours (100 hours in the case of dock workers) during the twelve months period, beginning 1 October and ending on September 30 of the following year, is entitled to receive a Christmas bonus. The maximum bonus to be paid to each employee who has worked the required 700 hours during the base period is 6% for 2008 and thereafter.

The maximum individual employee wage subject to the bonus is USD 10,000 and the maximum bonus payable to each employee is USD 600 for 2008 and thereafter. If the business has 15 or fewer employees, the bonus is 3% for 2008 and thereafter, and the maximum bonus payable is USD 300 for 2008 and thereafter.

The aggregate bonus to be paid should not exceed 15% of the net annual profit from Puerto Rico during the base period. The bonus is generally to be paid during the first 15 days of December but the employer and employee may agree on a different payment date, which may be set by a collective bargaining agreement.

Persons employed in farm activities, household duties, domestic service in a private residence and charitable not-for-profit institutions are not entitled to the bonus.

BONUS TO AGRICULTURAL WORKERS

The government of Puerto Rico pays this bonus until the agricultural industry is able to pay from its own funds. The farmer-employer only has to file certain reports.

A person working in the agricultural industry in Puerto Rico in the employ of a farmer is entitled to the bonus if:

1) He/she worked in Puerto Rico for not less 200 hours, or
2) He/she received wages and supplementary payments of not less than USD 200 for agricultural tasks performed in Puerto Rico, within the 12 months fiscal year ending 30 June.

The bonus is the greater of USD 165 or 4% of the annual income of the worker. The maximum amount of the bonus is USD 235.

6 – TAXATION

The major taxes imposed in Puerto Rico are income taxes, property taxes, municipal licence taxes, sales and use taxes, excise taxes and payroll taxes.

Entities doing business in Puerto Rico must comply with the requirements imposed by the different laws such as payments of tax, withholdings on certain payments and filing returns and reports with different government agencies.

INCOME TAX

Income tax is imposed on individuals and businesses.

INDIVIDUALS

The tax rate for an individual depends on whether he/she is a resident of Puerto Rico or not. For the year 2015, the ordinary taxable income of resident individuals is taxed at progressive rates ranging from 7% to 33% (on taxable income over USD 61,500).

Married individuals living together, filing a joint return and both working may choose the optional computation of the tax to determine the tax individually.

Preferential rates are provided for capital gains, certain dividends and partnership's distributions, as well as for interests on certain obligations or deposits with organizations of banking nature. For determining the taxable income, the individual may claim the deductions and exemptions provided in the Puerto Rico Internal Revenue Code of 2011, as amended. For additional information please refer to Appendix I.

Non-residents are taxed only on their income from sources within Puerto Rico or on income effectively connected with the conduct of a trade or business within Puerto Rico. The tax rate for non-residents depends on the class of income and on whether or not the individual is engaged in trade or business in Puerto Rico.

PARTNERSHIPS

The tax rate will be calculated at each partner's level based on their share of the partnership net taxable income, and considering their other type of income, since partnerships are treated as pass-through entities.

However, since this new treatment was established due to the New Internal Revenue Code of 2011, existing partnerships before the approval of the law could elect to keep their previous election to be considered as a corporation for income tax purposes.

LIMITED LIABILITY COMPANIES

The tax rate will be calculated at each member's level based on their share of the LLC net taxable income, and considering their other type of income, since LLCs are treated as pass-through entities. LLCs have the power to elect, if they prefer, to be treated as a partnership or as a corporation for purposes of income tax.

However, in the case of LLCs which are treated as pass-through entities or are disregarded entities under the United States Internal Revenue Code of 1986 (as amended), or under any other jurisdiction, they will also be treated as pass-through entities for Puerto Rico income tax purposes and no other election will be available.

CORPORATIONS

The tax rates for corporations and partnerships that elect to be treated as corporations for income tax purposes, organised under the laws of Puerto Rico, range from 20% to 39% on taxable income. The taxable income is determined after the allowable deductions and credits.

The ordinary rates for corporations and partnerships are shown in Appendix II. The rates for corporations and partnerships not organised under the laws of Puerto Rico depend on whether or not the entity is engaged in trade or business in Puerto Rico.

In addition, and as a general rule, every person subject to this tax for the purpose of enabling the Secretary of the Treasury to determine the correct amount of income subject to the tax, shall keep permanent books of accounts or records as are sufficient to establish the amount of the gross income and the deductions, credits and other matters required to be shown in any return.

OTHER TAXES

PROPERTY TAX

As a general rule, property taxes are imposed on the assessed value of real and personal property. The real property tax is imposed on the value of the property as assessed by the Municipal Revenue Collection Centre. The tax is payable semi-annually on 1 July and 1 January each year.

The personal property tax is self-imposed upon the filing of a return by any natural or legal entity engaged in a Puerto Rico trade or business and which on 1 January owns personal property used in the trade or business. The tax rate depends on the place (municipality) in which the property is located.

For the taxable year 2015–16, the personal property tax rates range from 5.80% to 9.83%. The real property tax rates are 2% higher.

MUNICIPAL LICENCE TAX

This tax is similar in nature to the gross receipts. It is imposed on all persons engaged in business based on the volume of business attributable to the corresponding municipality.

The tax rate is not the same in every municipality. For determining the applicable rate, businesses are grouped into two categories: financial and non-financial. Financial businesses are subject to a maximum rate of 1.5% of the volume of business. Non-financial businesses are imposed a maximum tax of 0.5% of the volume of business. The definition of the volume of business is different for financial and non-financial businesses.

In order to conduct operations free of this tax for the semester a business commenced operations, every person who commences any industry or business is obliged to notify the Municipal Treasurer within 30 days of commencement of operations.

SALES AND USE TAX

Every merchant engaged in any business that sells taxable items is responsible to collect the Sales and Use Tax ("SUT") as a withholding agent. The SUT is imposed on every sale of tangible personal property or taxable service, admission, use, storage or consumption in Puerto Rico, unless specifically exempted.

The sales and use tax is 11.5% since July 1, 2015 (10.5% for the Commonwealth of Puerto Rico and 1% for the municipalities). Generally, retail sales are taxable, but sales for export are exempt. The sales and use tax is paid monthly on or before the tenth of the next month.

Starting on October 1, 2015, the SUT will have a broader base since certain services to other businesses and designated professional services will be subject to a 4% SUT.

EXCISE TAX

This tax is imposed only once on articles imported, sold, consumed, used or transferred in Puerto Rico. This tax is imposed on cement manufactured or introduced into Puerto Rico, sugar, plastic products, cigarettes, and fuels, products derived from oil and hydrocarbon mixture, vehicles and on certain transactions. The tax rates are different for the different products.

Some other transactions are also subject to an excise tax. Included in these transactions are sales of jewellery, occupancy or rooms in hotels, public shows and horse racing winnings. The tax rate varies depending on the transaction.

PAYROLL TAX

A business operating in Puerto Rico must comply with the US Federal Insurances Contribution Act (FICA), the US Federal Unemployment Tax Act (FUTA), the Puerto Rico Unemployment and Disability Taxes Provisions, the Puerto Rico Chauffeur's Social Security, the Puerto Rico Workmen's Compensation Insurance and the Puerto Rico Christmas Bonus Act provisions.

ANNUAL REPORT

Every corporation is required to file an annual corporation report with the Puerto Rico Department of State. A USD 150 annual fee is payable when filing the report. In addition, the corporation must file a balance sheet certified by a CPA licensed in Puerto Rico when the volume of business exceeds USD 3,000,000.

In the case of foreign corporations authorised to do business in Puerto Rico, whose volume of business does not exceed USD 3,000,000, the annual report needs to be accompanied by a balance sheet of the Puerto Rico operations compiled and certified by a CPA licensed in Puerto Rico.

7 – ACCOUNTING & REPORTING

As in the United States, certified public accountant (CPA) firms which provide attest services are required to be registered with the Public Accounting Oversight Board.

This Board was created to provide registration, inspection, auditing standards, and enforcement for all CPA firms providing audits of publicly owned companies, including those listed in the US exchanges.

In addition, every person engaged in trade or business in Puerto Rico (domestic or foreign) whose volume of business exceeds USD 3,000,000 must file with the income tax return, property tax return and volume-of-business return, financial statements certified by a public accountant (CPA) licensed in Puerto Rico.

Licences to engage in the practice of public accounting in Puerto Rico are issued by the Board of Accountancy to those holding a certificate showing them to be a certified public accountant and registering as a public accountant.

8 – UHY REPRESENTATION IN PUERTO RICO

UHY DEL VALLE & NIEVES PSC
PUERTO RICO

UHY

CONTACT DETAILS

UHY Del Valle & Nieves PSC
PO Box 361863
San Juan
PR
Puerto Rico
Tel: +1 787 793 4650
Fax: +1 787 783 7834
www.uhy-pr.com

CONTACTS

Liaison contact: Rafael Del Valle-Vega
Position: Owner & Partner
Email: r.delvalle@uhy-pr.com

Liaison contact: Carlos Nieves-Vega
Position: Owner & Partner
Email: c.nieves@uhy-pr.com

Year established:	1988
PCAOB registered?:	Yes
Number of partners:	2
Total staff:	31

BRIEF DESCRIPTION OF FIRM

The current managing partners are a new generation of a firm first established in 1988 that is continuing to grow both in terms of volume of business and employees. We are recognised by bonding companies, insurance brokers, financial institutions and the general public as a leader in Puerto Rico public accounting services. Among the industries we serve are: construction, real estate, manufacturing, dealers, transportation and services.

Our vision is to be CPA Firm leader in Puerto Rico providing excellence services and innovations to our clients throughout the professional development of our staff.

SERVICE AREAS

Audit, review and compilation
Management advisory services
Litigation support
Preparation of tax returns
Assistance with revenue agents examinations
Interpretation of existing tax law and their effect
Compliance with tax exempt grants
Business reorganisation
Tax planning

PRINCIPAL OPERATING SECTORS

Construction
Retail

LANGUAGES

Spanish, English.

CURRENT PRINCIPAL CLIENTS

Luis Ayala Colón Sucesores, Inc
Cemex Puerto Rico Pension Plans
Puerto Rico Chapter, Associated General Contractors of America, Inc.
Puerto Rico Chamber of Commerce

The network for doing business

UHY DEL VALLE & NIEVES PSC
PUERTO RICO

Worldnet Telecommunications, Inc
Empresas Contreras and affiliates
R.B. Construction Group, Inc.
Perfumania Puerto Rico, Inc.
Omega Engineering, Corp and affiliates
Softek, Inc and affiliates
Roger Electric Corp.
Neolpharma, Inc
Ameriflight PR, Inc

OTHER COUNTRIES IN UHY CURRENTLY WORKING WITH, OR HAVE WORKED WITH IN THE PAST

UHY, LLP
UHY ADVISORS, INC
UHY Advisors TX, LLC

BRIEF HISTORY OF FIRM

For over 20 years, we have shared the aspirations of efficient operations of our clients. That is why our clients have constantly relied on us to deliver customized-timely advice to help them make the right business decisions.

First as HTR-Del Valle & Nieves, PSC (HTR Group) and now as UHY Del Valle & Nieves PSC, we keep offering our demanding clientele advanced solutions for all their business accounting and tax needs.

The business partnership between HTR-Del Valle & Nieves and UHY International combines the advantages of a powerful global network with personalized service and local expertise. Our clients include publicly-traded companies, privately-owned businesses and non profit organizations.

The firm joined UHY in 2008.

The network for doing business

APPENDIX I – INDIVIDUAL TAX RATES

A) For the taxable year 2015, individuals (including singles, heads of household and those marriage with a pre-nuptial agreement), married individuals living with their spouse and filing a joint return and married individuals filling separately, estates or trusts are taxed as follows:

TAXABLE INCOME (USD)	TO PAY	PLUS % ON EXCESS
1 – 9,000		0%
9,000 – 25,000		7%
25,001 – 41,500	USD 1,120	14%
41,501 – 61,500	USD 3,430	25%
61,501 and over	USD 8,430	33%

For taxable income over USD $500,001, a special surtax of 5% applies and the tax shall not exceed USD $8,423 plus 33% of personal and dependents' exemptions.

B) Alternative minimum tax – in lieu of any other tax when greater than the regular tax

ADJUSTED GROSS INCOME (USD)	TO PAY
150,000– 200,000	10%
200,001– 300,000	15%
300,001 and over	20%

C) Net long-term capital gains are taxed 15% or at regular rates. Losses on sale or exchange of capital assets are allowable up to ninety (80%) percent of capital gains, plus the net income of the taxpayer or one thousand ($1,000) dollars, whichever is lower.

D) Special tax on eligible dividends and profit distributions received by an eligible person is 15%

E) Interest on certain deposits is taxed at 17% or 10% for any excess over the USD 2,000 exclusion or at regular tax rates

F) Interest upon certain bonds, notes or other obligations and upon certain mortgages is taxed at 10%.

Appendix II – Corporate and Certain Partnerships Income Tax Rates

This does not apply for insurance companies, special partnerships, corporations of individuals, foreign corporations and partnerships not engaged in trade or business in Puerto Rico and income from operations under the Tourist Development Act and other prior tax incentives acts.

Normal tax is 20% of net income.

SURTAX

Surtax net income after a credit of USD 25,000, apply as follows:

INTERNAL REVENUE CODE OF 1994		
Table based on net taxable income considering the surtax deduction of $ 25,000		
From	To	Marginal tax Rate
-	100,000	25%
100,001	150,000	35%
150,001	200,000	36%
200,001	250,000	37%
250,001	300,000	38%
300,000	-	39%

The maximum combined tax of normal tax and surtax is 39%.

NET OPERATING LOSSES (NOLS)

All corporations are generally entitled to the NOL deduction in computing their tax. NOLs created from taxable years beginning prior to 31 December 2012 (and after 31 December 2004) may be carried forward for 12 taxable years (there are no carryback provisions). For taxable years beginning after 31 December 2012, the NOL carryforward period is ten years. The use of the NOL deduction is limited to 80% of the taxable income for the year. The NOL to be carried forward should exclude the deductible portion of the expenses or payments to foreign affiliates.

Also, losses from sales or exchanges of capital assets are allowed only to the extent of gains from such sales or exchanges. The carryforward period in this instance, however, is seven years. The use of capital losses is limited to 80% of the capital gains for the taxable year.

PAYMENTS TO FOREIGN AFFILIATES

51% of expenses attributable to payments made to a related party that is not engaged in a trade or business in Puerto Rico or to the home office located outside of Puerto Rico (i.e. foreign affiliate) will not be deductible for purposes of computing the net taxable income, as long as these payments are not subject to income taxes in Puerto Rico.

ALTERNATIVE MINIMUM TAX

All corporation or entities who are treated as corporations, are subject to an Alternative Minimum Tax (AMT) if it results in a tax liability greater that the regular tax liability. The AMT tax is 30%, levied on the "alternative minimum net taxable income". This is generally calculated adding back to the net taxable income certain items which received preferential tax treatments in computing the regular tax.

The AMT includes various components in order to calculate the tentative minimum tax. Such tentative minimum tax is the higher of the following:

- 30% of the alternative minimum net income.
- The sum of the following components:
    - 20% of the expenses paid or incurred by a related party, including those expenses allocated from a home office to its Puerto Rico branch, as long as these expenses or cost allocations are not subject to income taxes in Puerto Rico, plus
    - a percentage of the value of personal property purchases from related parties, including those transfers of personal property from the home office to the Puerto Rico branch. The percentage for years commenced after 31 December 2012 and before 1 January 2015 is 2%. For years commencing after 31 December 2014, the percentage fluctuates from 2.5% to 6.5% depending on the amount of gross income earned during the taxable year.

For AMT purposes, expenses paid or incurred for services performed by a related party outside Puerto Rico are considered a permanent adjustment in the determination of the alternative minimum net income (i.e. non-deductible for AMT purposes), unless such payment were subject to a withholding at sources in Puerto Rico.

GROSS INCOME ADDITIONAL TAX (GIAT)

Effective for years beginning after December 31, 204, the GIAT was repealed.

BRANCH PROFIT TAX

Corporations operating in Puerto Rico as a branch may be subject to a 10% tax on the dividend equivalent amount (commonly known as the branch profit tax or BPT). The BPT should be determined and paid along with the corporation income tax return. There will not be an income tax withholding at source at the time cash transfers are made by the Puerto Rico branch to its home office outside of Puerto Rico.

DEEMED DIVIDEND TAX (DDT)

For taxable years commencing after December 31, 2014, a ten (10%) percent tax is imposed on Deemed Dividend Amount deemed received by a foreign owner from a corporation.

- Foreign owner is a person not resident of Puerto Rico, who is not engaged in trade or business herein, and that owns ,directly or indirectly, at least fifty (50%) percent or more interests in the corporation.
- The Deemed Dividend Amount is the lesser of: the total average value Foreign Asset; or, the accumulated earnings and profits at the end of the taxable year.

  - Foreign Assets include: tangible property located outside of Puerto Rico; stock of a foreign corporation; obligations of a foreign corporation or a non-resident individual and, certain intangibles acquired or developed by a domestic corporation for use outside of Puerto Rico.
  - Accumulated earnings and profits are reduced by: income generated under tax incentives acts such as Act 73-2008, Act 74-2010, Act 225-1995, Act No. 52 of August 11, 1989, or other similar incentives acts; and the Deemed Dividend that has been subject to the tax.
  - Total average value of Foreign Assets is the sum of all average values at the end of each taxable year reduced by the Deemed Dividend Amount that has been subject DDT in prior years. The average value is the adjusted basis of each asset at the end of each quarter divided by four (4).
- DDT does not apply to Non-profit Organizations, International Insurers, International Financial Entities, and foreign corporation subject to the Branch Profit Tax (BPT).
- The DDT must be paid with the Corporation Income Tax Return, and it is creditable against the tax withholding requirements on actual dividend distributions.

LET US HELP YOU ACHIEVE FURTHER BUSINESS SUCCESS

To find out how UHY can assist your business, contact any of our member firms. You can visit us online at www.uhy.com to find contact details for all of our offices, or email us at info@uhy.com for further information.

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