

Local Opportunity Zones Development Act Signed into Law

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PRACTICE AREAS

- Recovery Financing

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On May 14, 2019, Governor Ricardo Rosselló Nevares signed into law the Puerto Rico Act for the Development of Opportunity Zones for Economic Development (“Act 21-2019” or “Act”). This Act establishes the tax, regulatory and economic framework for the development of opportunity zones in Puerto Rico.

Tax Benefits on Investments in Opportunity Zones:

Act 21-2019 is intended to serve as the Puerto Rico equivalent to the federal opportunity zones created under the Tax Cuts and Jobs Act of 2017. This Act provides tax incentives for Qualified Opportunity Funds (“QOF”) that invest in Priority Projects (as defined below) within the qualified opportunity zones (“QOZ”) which have been designated for Puerto Rico as such under Section 1400Z-1(b)(3) of the United States Internal Revenue Code.

The following summarizes the main tax incentives that Act 21-2019 provides:

For QOF’s:

- Flat income tax rate of 18.5% on the net income from an Exempt Business (as defined below);
- 100% tax exemption for dividends from an Exempt Business;
- 25% property tax exemption (real and personal property), which could be raised to up to 75%, if authorized, through an ordinance issued by the municipality situs of the Exempt Business;
- 25% municipal license (*patente*) and municipal construction tax exemption, which could be increased to a maximum of 75%, if authorized by ordinance issued by the municipality situs of the Exempt Business;
- 100% tax exemption for interest earned on bonds or loans of the Exempt Business and projects; and
- Agile procedure for the evaluation and issuance of permits for the Exempt Business and projects.

For Puerto Rico Investors (individuals or entities):

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- Tax free treatment in dividends received from an exempt business;
- Tax deferral on capital gains from the sale or exchange of capital assets if an amount equal to the capital gain realized from said sale or exchange is invested in a QOF. An investor may defer such taxes until the earlier of (i) the date on which it sells or exchanges its investment in the QOF or (ii) December 31, 2026;
- 100% tax exemption on dividends received from an Exempt Business;
- Step up in basis (reduction of the capital gain) for gains invested in a QOF in Puerto Rico under norms similar to those approved in the federal legislation (10% of step up for a 5-year investment and 15% for a 7-year investment);
- Permanent exclusion from taxable income of capital gains realized from the sale of an investment in a QOF under norms similar to those approved in federal legislation;
- Transferable credit of up to 25% (to be used in 4 installments); and
- Priority ranking for this credit over all other tax credits granted by other Puerto Rico tax incentives.

Exempt Business, and Priority Projects:

In order to benefit from the tax incentives described above, the QOF must invest its funds in an Exempt Business. An Exempt Business: (i) conducts the entirety of its business within the QOZ, (ii) is not eligible for a tax incentive under any other tax incentives law, (iii) is managed by a QOF or entity in which the QOF invests, and (iv) is engaged in an activity considered to be a Priority Project. Eligible businesses must apply to the Director of the Office of Industrial Tax Exemption for classification as an Exempt Business and to obtain a 15-year concession granting the incentives outlined above.

The Act broadly defines the term “Priority Projects” broadly as an industry or business, or other revenue generating activity which contributes to the diversification, recovery or social and economic transformation of the eligible zone’s community. The Act also includes the term “Eligible Priority Residential Project” which includes residential projects within the Opportunity Zones. The Opportunity Zone Priority Projects Committee created under the Act will issue an annual list of commercial and business activities that will be deemed as Priority Projects, and also will also allow any person to request a special designation for non-included activities. The first such list will be issued within sixty (60) days of the enactment of Act 21-2019.

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