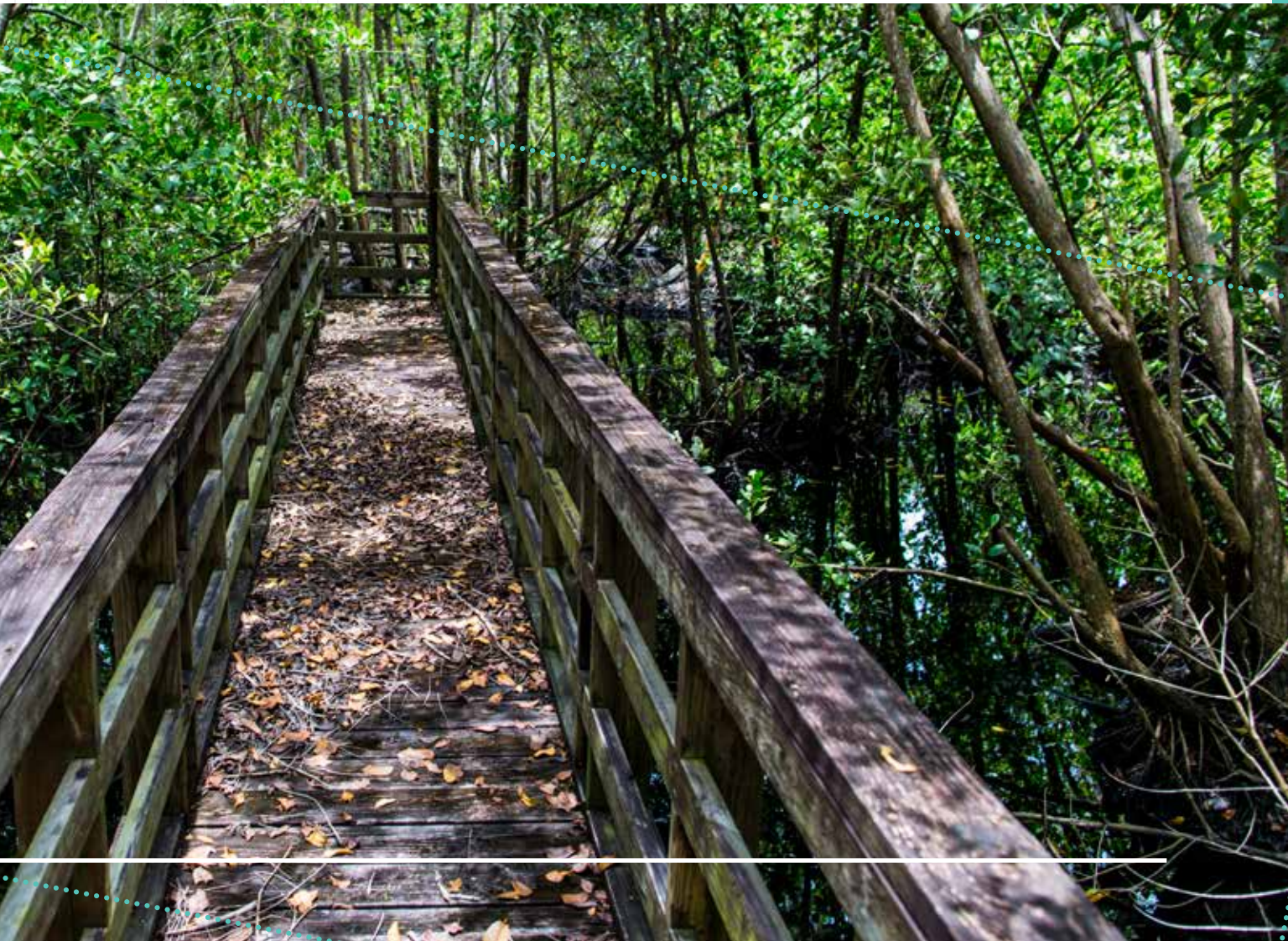


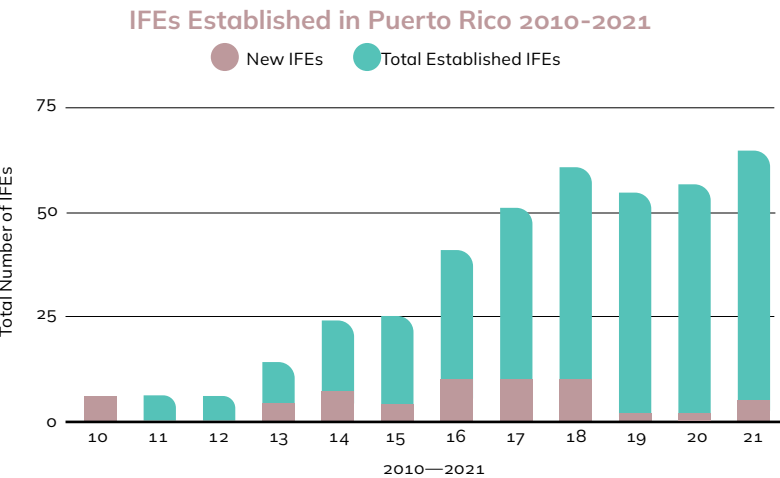
Finance, Investments, and Insurance



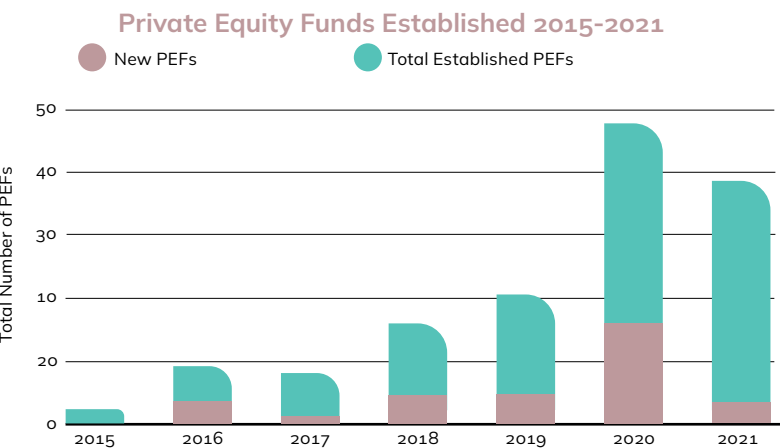
This chapter is dedicated to the tax incentives for different financial entities: international financial entities (IFE), international insurance and reinsurance companies (IIRC), and private equity funds (PEF). The goal behind this collection of incentives is twofold: to compete with other jurisdictions in which financial services are exported abroad and to foster local investment in established and private corporations.



To date, data for the past decade from the Puerto Rico Office of the Commissioner of Financial Institutions (OCIF, by its Spanish acronym) highlights the growth of IFEs in the island. As can be seen in the diagram below, over 60 IFEs have established their operations in Puerto Rico since 2010.¹



Since the introduction of tax incentives for PEFs in Puerto Rico in 2015, more than 31 funds have applied for a decree, with over half establishing operations in the past 3 years (see the diagram below). Although minimum assets under management (AUM) are required to be no less than \$10,000,000, most of these funds have operated with AUMs between \$500,000,000 and \$5,000,000,000.²



¹ Christian Reeves, "How Many International Banks are there in Puerto Rico," Premier Bank Consultancy, last modified October 15, 2021, <https://banklicense.pro/how-many-international-banks-are-there-in-puerto-rico/>.

² U.S. Securities and Exchange. EDGAR-Search and Access, accessed December 16, 2019, <https://www.sec.gov/search-filings>.

→ International Financial Entities³

International Financial Entities (IFE) are export services companies that provide financial services to non-residents. These services can include brokerage houses, banks, lending, and credit financing, among others.

All IFEs must comply with local laws and market regulations established by the federal financial regulator. This includes complying with the Bank Secrecy Act, the Patriot Act, the Foreign Account Tax Compliance Act (FATCA), the Truth in Lending Act (TILA), the Fair Credit Reporting Act (FCRA), the Office of Foreign Assets Control (OFAC), the Security and Exchange Commission (SEC), the Commodity Futures Trading Commission (CFTC), the Consumer Financial Protection Bureau (CFPB) regulations, among others. IFEs must also comply with the International Financial Center Regulatory Act (Act 273-2012), as amended.⁴ In all cases, they must work with the OCIF.

While being a jurisdiction of the United States yet not a state, Puerto Rico can bypass federal taxation locally. However, Puerto Rico must still abide by all the federal banking as well as financial and compliance reporting requirements that all United States financial institutions must follow.

Eligible Businesses and Activities

1. Depository institutions, including collateralized deposits
2. Credit card services and credit card refinance institutions
3. Money order services, including similar services
4. Investing in Puerto Rico securities, notes, and bonds of the government of Puerto Rico
5. Banking transactions in foreign currencies, foreign currency exchanges (FOREX), or traffic in gold and silver

³ Puerto Rico Incentives Code, Art. 2041.01, 13 L.P.R.A. § 45331 (2023). <https://bvirtualogp.pr.gov/ogp/Bvirtual/leyesreferencia/PDF/2-ingles/60-2019.pdf>

⁴ *International Financial Center Regulatory Act, Act No. 273 of September 25, 2012*, 7 L.P.R.A. § 3081 (2024). The Rules under the prior law, the International Banking Center Regulatory Act (Act 4-1985), are still used as a reference. See Regulation No. 5653 of 1997.



6. Underwriting securities, bonds, and other instruments
7. Financing trade of imports and exports in all types of exported goods
8. Any financial service permitted by law
9. To act as a fiduciary or administrator, among others, in any fiduciary capacity of foreign persons' bonds and securities (for example, certified financial advisors)
10. Renting personal property for foreign persons
11. Brokerage house or trading platform for foreign persons
12. Management of foreign financial entities
13. Asset management
14. Alternative investments
15. Management related to private equity
16. Management of private equity funds
17. Management of high-risk funds and insurance funds
18. Management of pools of capital
19. Management of trusts that serve to exchange different groups of assets
20. Management of escrow accounts

Eligibility Requirements

As IFEs are regulated by both local and federal entities, they must meet heightened financial compliance requirements. As a result, IFEs are subject to more requirements than are applicable to all other entities in the Act and include the following:

1. The entity must have \$10,000,000 in capital, and it must be paid in full in order to receive the relevant banking license. The law provides that the company may request the amounts required to capitalize the entity be lowered, but in no instance will the amount be less than 10% of the deposits of the entity.⁵
2. In addition to the initial capital paid, and as a requirement to obtain a license, all international financial entities must possess at least \$1,000,000 in unencumbered assets or acceptable financial guarantees.
3. The articles of incorporation or the bylaws of the entity must contain:
 - a. The name and address of the members or stockholders of the entity
 - b. The term for its existence (if the entity will not persist indefinitely)
 - c. The business reasons as to why the entity is formed
 - d. A specification of the business in which the entity will engage
 - e. Any relevant information required by law, regulation, or business needs
 - f. Furthermore, if an entity operates as a division or branch (often called units)⁶ of a banking entity, the articles of incorporation or bylaws must also include the following information for the unit:
 - i. The name under which it will be known
 - ii. The address
 - iii. Capital authorized by the primary entity
 - iv. Specific purposes and specifications of the eligible business

⁵ It can also be capitalized with assets that accrue to the same value.

⁶ An example of this would be the following: Cacique Bank establishes the banking unit Cacique Bank International Finance Division as a subsidiary or division.

v. Any other requirement⁷ that the Secretary of the DDEC may request

4. In all cases, the customers must be foreign persons.

General Benefits

1. The IFE Incentive Decree grants the benefit of a fixed 4% tax rate to that entity that offers eligible financial services to non-residents of Puerto Rico.
2. There is a 50% exemption on municipal taxes.
3. The incentive grants a 75% exemption on personal and real property.
4. It has a duration of 15 years, with an additional 15-year extension if requested.
5. Shareholders pay 6% on dividends or profit distribution of the net income.
6. If the IFE operates as a unit of another bank (for example, the international banking division of ABC bank), a 4% rate applies to the income of that division until it exceeds 20% of the entity's total income, in which case, that surplus is then taxed at the standard rate.

⁷ The "any other requirements" catch-all terms include but are not limited to, reporting, anti-money laundering, provisions and policies, data management, human resources, and oversight.

→ International Insurers⁸

The International Insurers Incentive looks to promote the establishment of more insurance companies in Puerto Rico that cater to both international and local insurance clients.

Eligible Businesses⁹

1. Life insurance
2. Physical Disability insurance
3. Property insurance
4. Insurance against maritime and transportation accidents
5. Agricultural insurance
6. Vehicle insurance
7. Accidents insurance
8. Guarantee Insurance
9. Title Insurance

Eligibility Requirements

1. Insurers must fall under the categories of International Insurers and Reinsurers described in Chapter 61 of the Insurance Code of Puerto Rico.¹⁰
2. Insurers must meet the requirements of the Insurance Code of Puerto Rico related to International Insurers, those included in this chapter, and any released regulations.
3. Insurers must provide the documents required in Article 61.050 of the Insurance Code of Puerto Rico. These include but are not limited to:
 - a. Personal information about the members and stockholders
 - b. The type of license requested

8 Puerto Rico Incentives Code, Art. 2041.02 13 L.P.R.A. § 45332 (2023). <https://bvirtualogp.pr.gov/ogp/Bvirtual/leyesreferencia/PDF/2-ingles/60-2019.pdf>

9 Insurance Code of Puerto Rico, 26 L.P.R.A. § 3803 (2023). <https://bvirtualogp.pr.gov/ogp/Bvirtual/leyesreferencia/PDF/C%C3%B3digos/77-1957/77-1957.pdf>

10 Insurance Code of Puerto Rico, 6 L.P.R.A. § 4301 (2023). <https://bvirtualogp.pr.gov/ogp/Bvirtual/leyesreferencia/PDF/C%C3%B3digos/77-1957/77-1957.pdf>

- c. Corporate resolutions for the application
- d. Certified copy of the certificates of formation
- e. Copy of the bylaws, certified by the president or secretary
- f. Designation of a principal representative, who will be a resident of Puerto Rico
- g. Personal information of the auditor and actuary associated with the entity
- h. Recent financial documents
- i. Certified copy of any audits
- j. Appropriate certification of which services the company is authorized to engage in
- k. Acceptance of being sued in Puerto Rico
- l. That the members can show domain knowledge in insurance
- m. That the employees can engage in the activities of the business
- n. That the place of business is adequate for the company

General Benefits

1. Net income over \$1,200,000 is taxed at 4% for 15 years. At the company's request, a 15-year extension is possible.
2. Issuers will enjoy a 75% exemption on personal and real property taxes and a 50% exemption on municipal taxes.¹¹
3. The income derived from dividends and distribution of profits is exempt from taxes and payment of municipal patents.
4. Associated companies and service providers to the International Insurers will not be subject to Puerto Rico withholding requirements and taxes.
5. International Insurers may request to offer insurance to residents. They may insure local clients if the local business volume is less than 50% of the total volume. To wit: this may be as low as 51% in income from foreign clients and up to 49% in income from local clients.
6. Insurers are exempt from all Insurance Code requirements that are not related to international insurance agencies.

¹¹ Puerto Rico Incentives Code, 13 L.P.R.A. § 45341 (C) (2023). <https://bvirtualogp.pr.gov/ogp/Bvirtual/leyesreferencia/PDF/2-ingles/60-2019.pdf>

→ Private Equity Funds and Puerto Rico Private Equity Funds¹²

The Private Equity Funds Decree offers incentives for Accredited Investors (as defined by the U.S. Treasury and the SEC) seeking to invest through a fund and receive tax benefits. The incentives provided are meant to foster the creation of professional fund managers and investors that identify market opportunities in Puerto Rico and other locations. Famous funds like Sequoia Capital, Y Combinator, Union Square Ventures, and Thomas Bravo (run by Puerto Rican entrepreneur Orlando Bravo) have financed startups, such as Apple, Facebook, and Airbnb, among others.

The Private Equity Funds under these incentives can operate as venture capital or traditional private equity funds. These funds buy or invest in all types of businesses, not just in innovative and tech-driven companies. However, most of its capital (80%) must be in shares not sold on the public market. This means that they must invest in private companies or in assets that do not sell their shares on the stock market.

While requirements will vary depending on how much is invested on the island, the Incentives Code includes two types of treatment for these funds. In short, the available designations are Private Equity Funds (PEF) and Puerto Rico Private Equity Funds (PRPEF). What distinguishes them from each other is how much and how early they invest in opportunities on the island.

A. Private Equity Funds

Eligibility Requirements

1. The fund must invest at least 15% of the capital received from its investors in bonds, promissory notes, stock, and notes (including collateralized or otherwise) by a private entity that derives its income from Puerto Rico sources.
2. All investors are Accredited Investors.
3. The fund employs a Registered Investment Advisor with an office in Puerto Rico.

¹² Ibid., ¹³ L.P.R.A. § 45333 (2023). <https://bvirtualogp.pr.gov/ogp/Bvirtual/leyesreferencia/PDF/2-ingles/60-2019.pdf>



4. It operates with a diversified portfolio, where, after 4 years, at most 50% of their capital is invested in one business. If the percentage changes due to fluctuations in the values of the investment portfolio, the percentage difference will not be considered from a compliance perspective with this requirement.
 - a. Suppose an investment becomes over 50% because another business took on more debt as part of a broader strategy. Now their liabilities change their on-paper value. In this case, the DDEC will take that into consideration and will not consider this noncompliance with the diversification requirement.
5. The minimum capital amount, including commitments that have yet to be paid, will have to have a minimum of \$10,000,000 before the 24 months of the fund establishing its first investment round.
6. The fund has an advisory board that includes at least one investor or limited partners.
7. If the entity is foreign, its managing partner or Registered Investment Advisor must derive at least 80% of their income from sources in Puerto Rico.

General Benefits

1. The incentive has a duration of 15 years, with an additional 15-year extension upon request.
2. Funds will have a 75% exemption on property taxes and a complete exemption on municipal taxes.

3. The fixed tax rate for investors is 10% for interest and dividends; if the distribution comes from capital gains, the distribution will be completely exempt.
4. If an investor sells their stake in the entity, they will pay 5% (unless they reinvest it in the fund within 90 days).
5. The managing or general partners of the fund and the Registered Investment Advisor will pay a fixed 5% interest on dividend distributions. Both will pay 2.5% when a capital gain is distributed to them.
6. Investors who reinvest their profits straight into another PEF can deduct up to 30% of the adjusted basis of their investment in full or partially for 10 years. However, if the fund is designated as a Puerto Rico Private Equity Fund (as explained below), the deduction will be greater.

B. Puerto Rico Private Equity Funds (PRPEF)

General Benefits

1. Investors in a PRPEF can deduct up to 60% of their investment in full or partially over a 15-year period (subject to restrictions). This exception encourages the PRPEF to focus most of its investments on the island.
2. To be considered as a PRPEF, it must have contributed at least 60% of its capital in the following eligible investments within its first 4 years:
 - a. Bonds, promissory notes, and stock, and notes (including collateralized or otherwise) by a private entity that derives its income from Puerto Rico sources
 - b. Bonds, promissory notes, or other instruments from the Government of Puerto Rico, instrumentalities, agencies, municipalities, and any other political subdivision
 - c. Puerto Rico Investment Trusts qualifying under Section 1112.02 of the Puerto Rico Internal Revenue Code that are taxed as corporations and have eligible investments that benefit their stockholders as they will not be taxed; these investments include, among others:
 1. Lending to tourism companies to remodel hotels and other tourism activities as described in Act 74-2010
 2. Investments in export companies
 3. Investments in developing new technologies and intellectual property

4. Commercializing new products in Puerto Rico
 5. Acquiring closed manufacturing plants to rehabilitate and begin operating a new business, similar to the previous company that operated in the facilities
- d. Investment in a foreign company, but the company must move to Puerto Rico within 6 months of the investment
1. Term can be extended for companies already deriving 80% of their income from Puerto Rico sources

Becoming a Member of a Private Equity Fund and a Puerto Rico Private Equity Fund

While eligible investors may be individuals or entities, only certain people can become members or investors in a PEF or invest in a private offering of stocks. As to the latter, federal regulations establish the criteria to qualify as an investor in a private security offering. Meanwhile, 2020 amendments modified the criteria for what constitutes an Accredited Investor and a Qualified Investor.

Moreover, the amendments allow professionals and founders on the island to obtain similar tax treatment as provided to Resident Individual Investors (see Chapter 2). Any individual or entity may benefit if the distribution is paid through capital gains instead of dividends. The return on capital will be taxed at 0% without having to reside outside of Puerto Rico between 2006 – 2014. The SEC website provides the following descriptions:¹³

Accredited Investor

To obtain the Accredited Investor status, an individual must qualify through one of the following criteria:

- a. Either possess a net worth of over \$1,000,000, excluding the primary residence (individually or with a spouse or partner), or
- b. Receive an annual income exceeding \$200,000 as an individual or \$300,000 with a spouse in the prior 2 years. Furthermore, the individual must reasonably expect the same income for the current year it invests in a fund.

¹³ See the SEC website for additional information: <https://www.sec.gov/resources-small-businesses/capital-raising-building-blocks/accredited-investors>

Qualified Entities

The entities that may invest funds under this incentive are the following:

- a. **Entities** having assets or investments above \$5,000,000
- b. **Corporations** having assets exceeding \$5,000,000, including:
 - 1. Partnerships, LLCs, trusts, 501(c)(3) organizations, employee benefit plans, “family office,” and any “family client” associated with that office
- c. **Owners as accredited**, including entities where all equity owners are Accredited Investors and may invest as a corporation instead of as individuals
- d. **Any investment advisers** who are duly registered with the SEC or an equivalent organization in their state or jurisdiction, as well as SEC-registered broker-dealers
- e. **Financial entities**, including a bank, savings and loan association, insurance company, registered investment company, business development company, small business investment company, and rural business investment company

Professional Criteria for Employees at a Fund

- a. Investment professionals in good standing and hold the general securities representative license (Series 7), the investment adviser representative license (Series 65), or the private securities offerings representative license (Series 82)
- b. Directors, executive officers, or general partners (GP) of the company selling the securities (or of a GP of that company)
 - 1. To wit: Stockholders of the company being invested in
- c. Any “family client” of a “family office” that qualifies as an Accredited Investor
- d. For investments in a private fund, “knowledgeable employees” of the fund

Illustrative Example

Horizon Trust Bank is capitalizing on the Puerto Rico Incentives Code to deliver seamless digital banking solutions for international freelancers and entrepreneurs. Through their platform, clients from over 100 countries can open a U.S. bank account and access a virtual debit card without needing U.S. residency or citizenship. Horizon Trust Bank's services allow freelancers in regions like Southeast Asia and Latin America to receive payments in U.S. dollars and easily manage their funds globally. As a SWIFT member, the bank caters to independent contractors, small businesses, and startups, enabling them to securely transact in multiple currencies while benefiting from U.S. banking regulations.

Cost to File

The cost to file for an International Insurance and Reinsurance Company, International Financial Entity, and a Private Equity Fund or Puerto Rico Private Equity Fund is equivalent to \$5,005. These costs do not take into account all business permits, licenses, compliance, and fees incurred hiring service professionals, accountants, or lawyers.

Cost to File		
Filing	Transaction Fee	Service Fee
International Insurance and Reinsurance Company	\$5	\$5,000
International Financial Entity	\$5	\$5,000
Private Equity Fund/Puerto Rico Private Equity Fund	\$5	\$5,000

