

September 02, 2016

A Proposal for Economic Growth in Puerto Rico
Submitted to the Congressional Task Force on Economic Growth in Puerto Rico
By the Puerto Rico Statehood Council

Introduction

The Puerto Rico Statehood Council (PRSC) appreciates the opportunity to submit this policy proposal to stimulate economic growth in Puerto Rico by building on and adapting established tax law.

The proposal outlined below is based on three policy criteria: first, an approach that is designed to create jobs and economic opportunity in Puerto Rico for those individuals residing and those businesses actually employing people on the island; second, the utilization of various tax incentives present in current U.S. law that have been enacted for other economically-distressed areas or empowerment zones; and, third, proposals advanced in a manner compatible with and as a “down-payment” for broad tax reform as reflected in the tax reform “blueprint” released by House Speaker Paul Ryan (R-WI) and Ways and Means Chairman Kevin Brady (R-TX) in June of 2016.

Thus, this proposal attempts to advance job-creation policies that are consistent with (1) precedents of current tax law for distressed areas or (2) as a “down-payment” for major tax reform.

Puerto Rico Economic Growth and Investment Incentives

1. Empowerment zones: Puerto Rico would be statutorily designated as an empowerment zone for a set period of 10 years, regardless of any change in the status of Puerto Rico during the ten-year period. After the ten-year period, the empowerment zone benefits would be determined and continue to be available for areas of the island under the qualification rules applicable to economically distressed areas throughout the states under present law. As a statutorily designated Empowerment Zone, the following incentives would be available to encourage economic growth and investment in Puerto Rico.

A. Business investment incentives: During the period in which Puerto Rico is a statutorily designated Empowered Zone, entities that invest in Puerto Rico (corporations or pass-through entities) would be eligible to receive the following tax benefits (similar to Ryan/Brady tax blueprint or existing tax code distressed areas investment incentives):

- **Lower tax rate:** During the period in which Puerto Rico is a statutorily designated Empowered Zone, 20% tax rate for both corporations and pass-through entities on Puerto Rico-sourced earnings.
- **Employment tax credit:** During the period in which Puerto Rico is a statutorily designated Empowered Zone:

(a) 20% for new hires in first 5 years

- (b) 15% for new hires in years 6-8; and
- (c) 10% for new hires in years 9 and 10

- **R&D credit:** During the period in which Puerto Rico is a statutorily designated Empowered Zone, a 20% R&D credit (increased from current 14% “alternative simplified credit”).

- **New markets tax credit (NMTC):**
 - (a) Puerto Rico designated as eligible for NMTC.
 - (b) NMTC extended for Puerto Rico investments for life of Puerto Rico empowerment zone designation.

- **Expensing:** During the period in which Puerto Rico is a statutorily designated Empowered Zone, full 100% expensing provided for Puerto Rico Empowerment Zone investments, including in personal property, real property and property that would otherwise be amortizable (similar to Gulf Opportunity (GO) zone incentives contained in Code section 1400N).

- **Zero capital gains tax rate:** businesses that invest in Puerto Rico Empowerment Zone assets, held for more than 5 years, would receive a zero percent capital gains tax rate (similar to the treatment of investments in DC empowerment zones under Code section 1400B).

- **Encouragement of Infrastructure Investment:** The Task Force should consider and endorse mechanisms that encourage investment in infrastructure projects on the island as an additional means of job creation and economic growth.

B. Individual investment incentives:

- **Zero capital gains tax rate:** Similar to the business tax incentive described above, during the period in which Puerto Rico is a statutorily designated Empowerment Zone, individuals who invest in Puerto Rico Empowerment Zone assets, held for more than 5 years, would receive a zero percent capital gains tax rate upon the sale or exchange of such assets (similar to the treatment of investments in DC empowerment zones under Code section 1400B).

- **Tax deferral and zero capital gains rate:** During the period in which Puerto Rico is a statutorily designated Empowerment Zone, a zero percent capital gains rate would also apply to individuals who establish 5-year residency in Puerto Rico and who invest any U.S. source gain in the Puerto Rico Empowerment Zone. U.S. tax would be deferred on any such gain while 5-year Puerto Rico residency is established.

- 2. Domestic manufacturing tax encouragement:** Section 199, which encourages manufacturing activities throughout the United States, currently applies to manufacturing

activity in Puerto Rico. The applicability of Section 199 to Puerto Rico is scheduled to expire at the end of 2016. The application of Section 199 should be made permanent.

- 3. Earned income tax credit (EITC):** The EITC, which does not apply in Puerto Rico, would be extended to residents of Puerto Rico, administered federally, and strengthened to reduce error and fraud.

Conclusion

The PRSC is pleased to present this job creation, economic growth and investment package to the Task Force. We believe that this package, or a package of similar incentives, would produce the kind of growth that Puerto Rico needs to emerge out of its lengthy recession and recent financial crisis.

For too long, Puerto Rico has lagged behind the rest of the United States on job creation and economic growth. We are confident that the right mix of pro-growth, job-creating policy changes which are contained in this enterprise zone plan will create jobs, lower unemployment, increase labor force participation, grow business fixed investment, result in capital in all forms rushing to Puerto Rico, and ultimately raise the standard of living and prosperity for all. There is no reason why Puerto Rico cannot become an economic powerhouse of the Caribbean if unshackled from onerous tax and regulatory policies.

This plan incorporates investment incentives in current federal law which have not been extended to Puerto Rico, limiting its growth. For Puerto Rico to overcome its economic challenges and achieve its full potential, however, history has shown and the simple fact must be recognized that it must be treated equally with the rest of the nation in all respects. Repeated initiatives for different treatment have left the territory underdeveloped and poor compared with the states and have encouraged its U.S. citizens to relocate to a state for greater opportunities. By a majority vote of more than three-fifths, Puerto Ricans have also petitioned the Congress to phase in the equal treatment that they could achieve through statehood.

We would be happy to meet with members of the Task Force to discuss the various recommendations contained in this proposal at your convenience. Thank you again for this opportunity to provide our input.