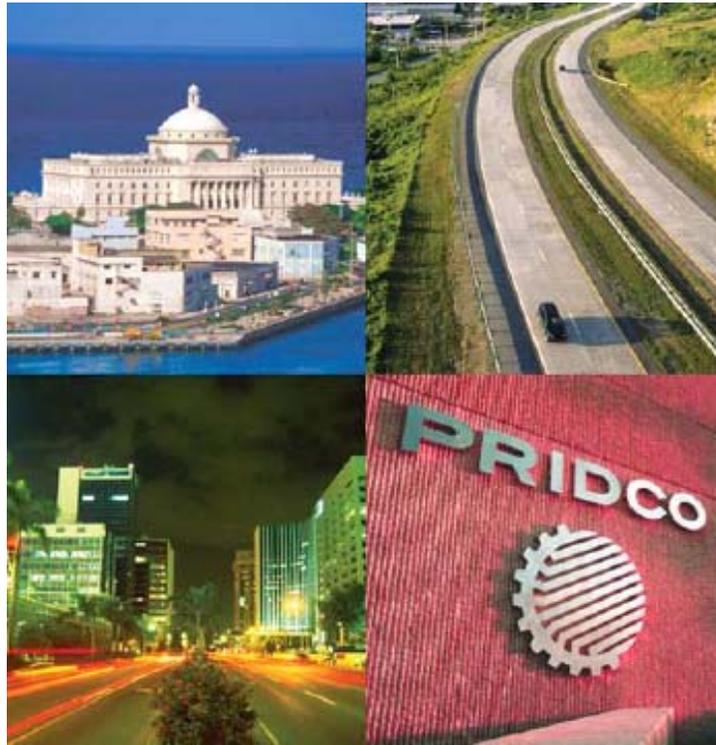


Economic Incentives for the Development of Puerto Rico Act

(Act No. 73 of May 28, 2008)



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(H.B. 4350)

Economic Incentives for the Development of Puerto Rico Act

To enact the “Economic Incentives for the Development of Puerto Rico Act”, with the purpose of providing an adequate environment and opportunities for the continued development of our local industry; providing an attractive tax proposal that appeals to foreign direct investments and fosters the economic development and social betterment in Puerto Rico; to add Subparagraph (S) and subparagraph (T) of Section 1022(b)(4), amend Section 1232(f)(2) of the Puerto Rico Internal Revenue Code of 1994; and create the Energy Affairs Administration.

LEGISLATIVE INTENT

Puerto Rico has a trajectory of more than 60 years of capital investments promoted by its industrial incentives program. This program has evolved through time responding to the challenges and opportunities of the different moments in history. The program has had, as common denominator, the concession of tax incentives, which have been calibrated in order to respond to the industrial development strategies of each period. Act No. 135 of December 2, 1997, as amended, known as the “Tax Incentives Act of 1998”, was no exception. Said Act incorporated a significant change in the focus of industrial promotion, because it effectively embraced the “controlled foreign company” structures model, which became more pertinent when certain federal incentives were eliminated.

Efforts to promote Act No. 135 have created over 113,000 direct jobs and 273,000 indirect jobs, which constitutes more than 40% of the labor force of Puerto Rico. One of the most recent initiatives incorporated to this Act, the pioneer industry, has attracted significant investments in biotechnology, medical instruments, telecommunications, and information technology and has generated over 3,000 jobs. Of the 1,400 business covered by Act No. 135, 70% are from local capital. Multinational entities also covered by Act No. 135, contribute approximately 1.3 billion dollars in income taxes and withholdings of payments for royalties to non-residents. These companies also make significant tax contributions to our municipal governments.

The manufacturing sector has been and continues to be vital for Puerto Rico’s economy. Nonetheless, the economic models that we had in place 60 years ago, and even those from 10 years ago, have changed. The globalization of markets, the increase in productivity due to the use of high technology, the appearance of new markets, the signing of free commerce treaties, regionalization and new models of production, have turned the world into a global village. These changes present new challenges and opportunities for the industry and for our people.

Puerto Rico faces a historic moment with great challenges. Its competitive position against other jurisdictions in attracting capital investments has been undermined by internal and external

circumstances. Emerging economies are ever more aggressive and effective in their efforts to attract capital. Advances in the areas of technology, information technology, communications, biotechnology, robotics, and renewable energy, among others, have changed the interests of investors and the skills required from human capital. The increase in energy costs and in the costs of doing business in Puerto Rico, in general, harm our competitiveness.

The international tax system has undergone changes which eliminate barriers. The world is turning into one great, but single, jurisdiction. Isolated focuses take away from competitiveness. As global barriers are being eliminated in every scope, in the same way synergies between manufacturing and service providers are achieved through new processes, which can be manual, technological, or virtual. Recognizing this reality and accepting it as an indispensable part of the new promotion strategy, requires the search for alternatives to develop and strengthen the value added chains.

The future of our people depends on the establishment of strategies to insert us into the global economy based on knowledge, that brings Puerto Rico to a development based on technology transfer process, creation of intellectual property, and innovation. For that reason, we must adopt a perspective of sustainable development that pays attention to economic, social, political, technological, and environmental factors. Education should be a priority. Puerto Rico must establish an action plan that is a cohesive instrument and in agreement with the commitment for an educational system based on languages, mathematics, and science.

The “Economic Incentives for the Development of Puerto Rico Act” will be the spearhead center of multiple initiatives that Puerto Rico must make in order to be successful in this effort. It recognizes how important it is for Puerto Rico to continue being attractive for the group of businesses that constitute the backbone of the incentives program, elevating to a maximum the competitive advantages that 60 years of experience and association with this industry have given us. This sector has had great impact on multiple sectors, such as the creation of a middle class and a world class offer of technical service providers. In the same way, we must emphasize and recognize the preponderance of the local sector, an indispensable tool for the creation of jobs and for the strengthening of the value chains.

This “Economic Incentives for the Development of Puerto Rico Act” responds to strategic decisions about what should be the public policy of Puerto Rico, which are:

1. Provide an entrepreneurial environment and the adequate economic opportunities in order to continue developing a local industry, recognizing that the local businessman person is the cornerstone an essential part in the current present and future economic development of Puerto Rico. It is our interests to prioritize the emerging business person to support his or her development and growth which integrates the interlinking of our economy and the value added chains.

2. Offer an attractive tax proposal to attract direct foreign investment and be on par with the most competitive jurisdictions for high technology and high value added industries.
3. To guarantee a relationship between the promoted industry the Government of Puerto Rico and its components, which is founded on public transparency, stability, certainty, and credibility. All of the components of our society must offer strong support to this program and to the respect and fulfilment of the commitments that are part of it for the well-being of Puerto Rico.
4. To support the initiatives of the private sector, the academia, community enterprises, and municipalities, leading to economic development of Puerto Rico through innovation, research and development, and investment in the necessary infrastructure for a better quality of life and efficiency of industrial operations.
5. To mitigate high operational costs and soften regulatory limitations which discourage the competitiveness of Puerto Rico. For instance, it is essential to promote the revision of laws and/or regulations which limit the use of certain fuels in the manufacturing process in a way that allows the industrial sector to utilize more economic fuels, provided that the efficiency of absorption of the process or of the control equipment does not interfere with the requirements for pollutant concentrations in the atmosphere established by law, or any other applicable requirement.
6. To take conclusive actions in order to reduce energy costs through different alternatives of renewable energy.
7. To recognize the importance of the decentralization of the Government and, in function of the aforementioned, support the efforts being developed at the regional level to promote economic development and technological innovation. Said efforts, which integrate government, business and academia, have already produced results and it is necessary that they be supported, to ensure their contribution to Puerto Rico economic future.

In consideration of the above, this Act gathers the benefits of Act No. 135 and of proposals such as H. B. 3798, and amplifies the definition of eligible business in order to recognize the importance of the services industry, based evermore on the knowledge economy, and in that way trigger the local industry. It also establishes a system of fixed income tax rates, calibrated to attend to the permanency and stability of the existing businesses, to respond to the growing world competition, and to protect Puerto Rico's taxable base in an equitable manner. On the other hand, it offers different tax alternatives to promote strategic investments and increase the acceleration of the economy, and provides mechanisms for the autonomous and non-autonomous municipalities to have a more ample and stable income base, while reducing unnecessary friction and uncertainty with investors in these municipalities. In this way, the "Economic Incentives for the Development of

Puerto Rico Act” establishes, as a key piece, the Development Fund and increases its resources in order to increase its positive impact in the economy in general. The success and accomplishments of this Act, as well as the need to make decisions in a proactive manner, in the short, medium, and long term, so that it continues to be effective, will be measured through a number of processes, performance metrics, and information requirements, as established in the statute. For purposes of the effectiveness and continuity of this Act, an expiration term is not established, as mechanisms for measurement, revision, and oversight have been included. These mechanisms ensure that this statute remains as an instrument for agile and competitive promotion, and that the continuous compliance of its provisions is supervised.

This “Economic Incentives for the Development of Puerto Rico Act” is the result of a historic process of collaborative efforts between the private sector and the Executive and Legislative branches of the Government of Puerto Rico. It is one of many initiatives that should be considered and emulated in order to accommodate the public policy of Puerto Rico to the current global tendencies to satisfy our current needs, setting the stage for the well-being of our future generations. This initiative constitutes a great starting point for the investment in Puerto Rico’s future and an excellent first step towards the solution of the problems that affect our society.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF PUERTO RICO:

Article 1 - The “Economic Incentives for the Development of Puerto Rico Act” is created to read as follows:

Section 1.- Declaration of Public Policy

The public policy of the Government of Puerto Rico shall be:

- (1) To provide an adequate environment and opportunities for the development of local industry.
- (2) To offer high technology and high value added industries an attractive tax proposal in order to attract foreign direct investment to compete with other jurisdictions.
- (3) To guarantee a relationship between industry and the Government of Puerto Rico which is founded on stability, certainty, and credibility. All of the components of our society must offer strong support to this program and to the respect and fulfilment of the commitments that are part of it, for the well-being of Puerto Rico.
- (4) To support the initiatives of the private sector, academia, community enterprises, and municipalities. This with the purpose of contributing to the economic development of Puerto Rico.

Rico through innovation, research and development, and investment in the necessary infrastructure for a better quality of life and efficiency of industrial operations.

(5) To mitigate high operational costs and soften regulatory limitations which discourage the competitiveness of Puerto Rico. For instance, it is essential to promote the revision of laws and/or regulations which limit the use of certain fuels in the manufacturing process in a way that allows the industrial sector to utilize more economic fuels, provided that the efficiency of absorption of the process or of the control equipment does not interfere with the requirements for pollutant concentrations in the atmosphere established by law, or any other applicable requirement.

(6) To take conclusive actions in order to reduce energy costs through different alternatives of renewable energy.

(7) To recognize the importance of the decentralization of the Government and, in function of the aforementioned, support the efforts being developed at the regional level to promote economic development and technological innovation. Said efforts, which integrate government, business and academia, have already produced results and it is necessary that they be supported, to ensure their contribution to Puerto Rico economic future.

Section 2- Definitions

For the purposes of this Act, the following terms, phrases and words shall have the meaning expressed below:

(a) Industrial Development Income -

(1) The net income of an exempted business with a grant issued under this Act derived from the operation of an eligible activity or designated service, computed according to the Puerto Rico Internal Revenue Code, as amended, adjusted by the special deductions provided by this Act, including the income from operations of such exempted business when an election under subsection (b) of Section 10 of this Act is made.

(2) The eligible income described in subsection (j) of Section 2 of this Act, or by analogous provisions under similar prior or subsequent acts.

(3) Net income derived by the operation of an exempted business with a grant issued under this Act, as a result of currency exchange that can be attributed to the sale of its products or rendering of services to foreign countries, including the net income derived from hedging transactions.

(4) Income received as dividends or profits by a corporation or partnership that has stock or partnership shares in the exempted business that makes the distribution, and said income is attributed to industrial development income derived by said exempted business.

(5) Net income derived by the exempted business that holds a grant under this Act, obtained from business interruption insurance policies, provided there is no reduction in the level of employment in the exempted business as a result of the act that gave rise to the collection of said income.

(6) Net income derived from the sale of intangible property or any other right to receive income related to activities or intangible property owned by the exempted business with a grant under this Act.

(b) Property devoted to industrial development -

(1) Real property, including land and improvements, or parts thereof, as well as any addition equal to not less than twenty-five percent (25%) of the area of the main plant engaged in the operation of an industry, that is placed at the disposal of and used or held by an exempted business holding a grant under this Act, in its development, organization, construction, establishment or operation.

(2) An ensemble of machinery and equipment necessary for an exempted business holding a grant under this Act, to perform the activity for which the tax exemption is granted, which is possessed, installed, or otherwise used under contract by said exempted business.

None of the provisions under this subsection shall apply to leases denominated as financing leases.

(c) Exempted business -

An eligible business, as defined in this Act, that is or will be established in Puerto Rico by a natural or juridical person, or a combination thereof, whether or not it is organized under a common name, to which one or various grants of tax exemption have been issued, but excluding hotels, inns or other special facilities which are exempted businesses under Act No. 52 of June 2, 1983 or Act No. 78 of 1993, as amended.

(d) Eligible business -

(1) The following are eligible businesses for the purposes of this Act:

(A) Any industrial unit, that is established with permanent character, for production of a manufactured product on a commercial scale.

(B) Notwithstanding the provisions in sub-paragraph (A) of this paragraph, any industrial unit established with permanent character for the production of a manufactured product on a commercial scale and that was not eligible under Section (2)(d)(1), nor considered as a designated article under Section (2)(e) of Act No. 135 of December 2, 1997, as amended, or analogous provisions under previous acts, will enjoy the benefits provided in this Act only with regards to its export activities, subject to the limitations established with respect to the determination of industrial development income and base period income, of subsections (f) and (g) of Section 3 of this Act.

(C) Any industrial unit that would normally qualify as an eligible business under the preceding sub-paragraphs, but that due to competition with other jurisdictions caused by lower production costs, among other factors, is not economically feasible to perform the complete manufacturing operation in Puerto Rico, which would require some processing or elaboration of the product outside of Puerto Rico.

For purposes of this sub-paragraph, the Secretary of Development, as recommended by the Executive Director and the Secretary of the Treasury, may determine that said industrial unit is an eligible business in view of the nature of the facilities, the investment made in property, machinery, and equipment, and the number of jobs to be created in Puerto Rico, the total payroll and any other special factors that justify said determination.

(D) Any bona fide office, business or establishment along with its equipment and machinery, with the capability and skills necessary to render a service on a commercial scale, provided that it meets the following characteristics:

(i) The rendering on a commercial scale, in Puerto Rico, of a designated service, as described in subsection (h) of this Section, for markets abroad, including United States markets, provided that within a reasonable period of time it renders a substantial amount of such services on a continuous basis, as determined by the Executive Director by means of regulation.

It shall be understood that the service is rendered to foreign markets, even when the service is rendered to another business established in Puerto Rico, which finally exports the designated service.

An entity providing designated services may, also, render services in local markets provided it can demonstrate, to the Secretary of Treasury's satisfaction the income derived from sources outside Puerto Rico pursuant to an accounting method that clearly reflects said income.

(ii) The rendering in Puerto Rico of a service through sub-contracting, that is fundamental to the production process of a manufacturing exempted business belonging to a cluster classified as one of high economic impact by the Executive Director, in consultation with the Planning Board, as established in the Proposal for Promotional Planning of the Industrial Development Company. The Executive Director shall establish the criteria used to classify clusters as high economic impact by means of regulation.

(iii) The rendering in Puerto Rico of a service in a commercial scale and on a continuous basis to an exempted business as a key supplier of said exempted business that is a unit devoted to manufacturing. A supplier is considered as key supplier if its services allow the exempted business that is its regular customer to concentrate in its core competency activities.

For purposes of this subsection, there shall be considered as key supplier services those that are costs directly related to manufacturing activities of an exempted business, including among others, the following:

- (aa) Specialized storage.
- (bb) Management of raw material inventory, work in progress, finished goods, and parts inventory, including receipt, storage, and inspection.
- (cc) Logistics related to the distribution of manufactured products and exports of services of exempted businesses, except transportation services of materials and documents offered by businesses mainly dedicated to transportation for consumers and non exempted businesses.
- (dd) Inserts and distribution of printed material.
- (ee) Digitalization of documents.
- (ff) Sterilization of instruments, equipment, and garments for clean rooms.

- (gg) Quality control services and services for the validation of processes, equipment, and systems.
- (hh) Equipment, utilities or facilities qualifications as well as calibration and maintenance of equipment.
- (ii) Repair and re-manufacturing of products.
- (jj) Project engineering.
- (kk) Programing services and data systems management services.
- (ll) Specialized technical training.
- (mm) Development and reproduction of educational programs.
- (nn) Logistics related to purchase and sale functions such as those relating to orders and transportation.
- (iv) In the case of the service units described under this clause, no less than eighty per cent (80%) of the employees, technicians, and professionals of the service units shall be residents of Puerto Rico.
- (v) In the case of service units described under this clause that are operating in Puerto Rico before filing their application, they shall be subject to the base period income limitations, established in subsection (g) of Section 3 of this Act.
- (vi) Legal, accounting or tax consulting services will not constitute key services.
- (E) Property devoted to industrial development.
- (F) Raising of animals for experimental use in scientific research and medical laboratories and other similar uses.
- (G) Scientific or industrial research and development laboratories for the development of new products or industrial processes, or for the improvement of existing ones, for experimental purposes, clinical investigations, epidemiological and basic science in mental health projects, medical scientific research and similar purposes.

(H) Any business dedicated to the production, whether on a commercial scale or not, of energy for consumption in Puerto Rico, through the use of natural gas or coal, or through the use of renewable sources, including but not limited to: solar, eolic, geothermic, oceanothermic, ocean kinetic, hydroelectric, biomass or hydrogen or solid waste, methane recovery using high technology for the production of energy at competitive costs, including, but not limited to, alternate thermic conversion technology. Three (3) years after the approval of this Act, the generation of energy from fossil sources or non-renewable sources will not be considered eligible. Included in this sub-paragraph are units participating in public or “public-private” consortiums whose primary’ objective is the one mentioned in this sub-paragraph.

(I) Any of the recycling activities defined below:

(i) Partial Recycling Activities- Recycling activities which undertake two or more of the following processes: recollection, distribution, reconditioning, compacting, shredding, pulverizing, or other physical or chemical process that transforms the articles of recyclable materials, or recyclable materials, as defined in Article 2(O) of Act No. 70 of September 18, 1992, as amended, and recovered in Puerto Rico, into raw material, aggregates for the elaboration of a product, prepare the material or product for its sale or local use or for exporting, and that sell or utilize locally or export the processed material or product for its ulterior use or recycling.

(ii) Total Recycling Activities- The transformation into articles of commerce of recyclable materials that have been recovered primarily in Puerto Rico, provided that such activity contributes to promoting the industry of recycling in Puerto Rico.

(J) Harvesting and cultivation by means of hydroponics, as well as the intensive cultivation of mollusks, crustaceans, fish, or other aquatic organisms by means of aquaculture, the process of pasteurization of milk as well as Agrarian Biotechnology processes, provided that these operations take place under regulations and practices approved by the Department of Agriculture of Puerto Rico.

(K) Value added activities related with the operation of the Port of the Americas, the port located in the former Roosevelt Roads Base, and the ports of Mayagüez, Yabucoa, San Juan, Guayama, and any other port designated by the Secretary of Economic Development, by means of regulation or other official communication, such as: storage, consolidation and dispatch of merchandise, re-packaging of consolidated products for shipment from the mentioned ports, the finishing of semi-processed products to be shipped to regional markets, and any other commercial or

service activity related to the administration and management of finished, semiprocessed, or manufactured products or goods that are associated with, are part of, or pass through such ports.

(L) Development of licensed or patented software that can be reproduced at commercial scale. Provided that, in the case that such eligible business is operating in Puerto Rico before submitting its application, the limitations established in section (f) of Section 3 of this Act will apply.

(M) Assembly of equipment for the production of energy from renewable sources.

(N) Research, development, manufacturing, transportation, launching and operation from Puerto Rico of satellites and development service centers for the processing and storage of data, excluding telephony, radio broadcasting, and telecast operations.

(O) Strategic Projects, as defined in subsection (p) of this Section.

(Q) Any industrial unit that produces purified bottled water that complies with the U.S. Food and Drug Administration's norms for purified water and the codes of the U.S. Pharmacopodia 23rd Revision, using processes that result in physical and chemical changes to the original water, including reverse osmosis, recovery of reverse osmosis, and mineral injection, among others. Provided that these industries will only be eligible to receive the benefits discussed on Section 5 of this Act.

(R) Construction of affordable interest housing and planning and development of self-sustainable or partially sustainable communities. For purposes of this sub-paragraph, the term self-sustainable community shall mean the development of housing projects that have the capacity to fulfill their own energy, water, and solid waste management needs. For purposes of this sub-paragraph, the term partially sustainable shall mean, the development of housing with capacity to fulfill seventy five percent (75%) or more of its water needs (calculated based on average daily consumption per family of two hundred and fifty (250) gallons), the development of an adequate sanitary infrastructure, the management of solid waste according to the laws and regulations in force, and the use alternate techniques for the production of energy, to supply, as a minimum, the common areas of the housing project.

In the case of construction of affordable or private housing, prior endorsement from the Department of Housing of Puerto Rico will be required. The Department of Housing of Puerto Rico must consider and issue a determination on

applications for endorsement, filed pursuant to this sub-paragraph, within forty five (45) days, to be computed beginning the day the application is received.

If no determination is received within the terms established above, as may apply, such application shall be considered approved.

The equipment for alternate energy production must be certified to those effects and to the effects of its functioning in the location where they are installed, by an Electrical Engineer or by a Certified Electrician, both licensed and members of the respective professional associations, in conformity with the laws that regulate these professions, and who possess specialized knowledge regarding the installation of distributed generation equipment based on any type of renewable energy, being said professionals registered with the Energy Affairs Administration of Puerto Rico, providing a certified copy issued by the professional association of Engineers and Land Surveyors of Puerto Rico or by the association of Certified Electricians of Puerto Rico, as the case may be, and a copy of their licenses to practice the profession of Electrical Engineer or Certified Electrician. During the term the tax benefit persists, the equipment shall be inspected and certified annually by one of the aforementioned professionals and in order to receive the credits for which they qualify, the eligible business will submit a copy of this certification along with its declaration of income.

(2) Except as provided in Section 13 of this Act about renegotiations and conversions, petitioners receiving tax benefits or incentives under any other special law of the Commonwealth of Puerto Rico which are similar to those provided by this Act, as determined by the Executive Director, may not be considered as an eligible business under this Act, with respect to the activity for which they enjoy such tax benefits or incentives.

(e) Production on Commercial Scale -

Production for sale on the market in the normal course of business, in quantities and prices that justify the operation of an eligible business, as a going concern.

(f) Manufactured Product -

Shall include products transformed from raw material into commercial articles, designated articles under previous incentives acts, and any product for which substantial industrial operations are carried out in Puerto Rico which, in the judgment of the Executive Director, deserve to be considered as manufactured products under this Act, due to their nature and extent, the technology required, the substantial employment provided, or any other benefit said operations represent for the welfare of Puerto Rico.

An exempted business with a grant issued under this Act may subcontract the production in Puerto Rico of one or several components or products, or all or part of the manufacturing processes, or services related to said processes of products covered under its grant, or key functions necessary for its operation, and the subcontractor shall also qualify as an eligible business, provided the Secretary of Development determines said subcontracting shall be in the best interests of Puerto Rico, taking into consideration the factors outlined in the first paragraph of this subsection.

(g) Industrial Unit-

(1) A plant, factory, machinery or group of machinery and equipment with the capacity to perform the main functions used in the production of a manufactured product on a commercial scale, even when certain facilities are shared with other industrial units of lesser importance such as buildings, power plants, warehouses, material conveyors, or other production facilities of lesser importance, or performs certain industrial operation outside of said industrial unit.

(2) An industrial unit may use facilities in common with other industrial units of greater importance when the Secretary of Development determines that said common use is necessary and convenient for the industrial and economic development of Puerto Rico, in view of the nature of the operations, the additional investment and the number of jobs created.

(3) Any exempted business with a grant issued pursuant to this Act that establishes an eligible business to manufacture an article that is separate and distinct from that produced by said exempted business, with the machinery and equipment needed for an efficient operation, in addition to any other operation that has enjoyed or is enjoying an exemption, with an accounting system that clearly reflects the operation of said eligible business according to generally accepted accounting standards and principles.

(h) Services Designated for Foreign Markets-

The designated services shall include the following economic activities:

(1) Commercial and mercantile distribution, including the export of products manufactured in Puerto Rico.

(2) Investment banking and other financial services, including but not limited to: (i) asset management ; (ii) alternative investment management ; (iii) management of activities related to private capital investments; (iv) management of hedge funds or high risk funds; (v) management of pools pf capital; (vi) administration of trusts

which serve to convert different groups of assets into stocks; and (vii) administration of escrow accounts.

- (3) Advertising and public relations.
- (4) Economic, environmental, technological, scientific, managerial, marketing, human resources, information technology, engineering, and auditing consulting services.
- (5) Commercial and graphic arts services.
- (6) Assembly, bottling, and packaging operations.
- (7) Electronic data processing centers.
- (8) Airport and seaport facilities.
- (9) General repair and maintenance of ships and aircrafts as well as machinery and equipment, including electric, electronic and watch repair equipment.
- (10) Production of engineering and architectural plans and designs, and related services.
- (11) Marketing centers mainly engaged in providing, through leasing, service fees or other charges, space and services such as: secretarial, translating and data processing services, communications, marketing, telemarketing and other consulting services, to firms engaged in, or otherwise related to the purchase and export of products or the rendering of services for markets outside of Puerto Rico, including export and marketing companies, adjunct offices of commercial attaches, government agencies responsible for foreign trade, exchange, and product and service exhibition centers.
- (12) Central or regional corporate headquarters engaged in rendering centralized management services, including strategic and budget management or planning, to affiliated entities.
- (13) International trading companies.

For purposes of this section, international trading companies shall mean any entity that derives not less than eighty percent (80%) of its gross income from:

- (A) The purchase of products manufactured in or outside of Puerto Rico and their resale for use, consumption or disposition outside of Puerto Rico, and

(B) commissions derived from the sale of products for the use, consumption or disposition outside of Puerto Rico; provided, that no part of the income derived from the sale or resale of products for their use, consumption or disposition in Puerto Rico shall be deemed to be industrial development income.

- (14) Development of general application software subject to licensing and custom made software.
- (15) Educational services and training in general.
- (16) Medical and hospital services, including reference laboratories and telemetry services.
- (17) Strategic and organizational planning of processes, distribution, and logistics.
- (18) Shared Services Centers- For purposes of this Section, the term “shared services centers” refers to a unit dedicated to providing centralized accounting, finance, tax, auditing, marketing, engineering, quality control, human resources, communications, electronic data processing, and other centralized managerial services, to affiliated entities.

The Secretary of Development, with previous favorable recommendation from the Executive Director and the Secretary of Treasury, may designate through regulation, other services that should be included in this Act, when determining that such designation will be in the best interests and economic and social welfare of Puerto Rico, taking into consideration the demand that may exist for such services outside of Puerto Rico, the total number of jobs that will be created, and the investment that the service unit would make in Puerto Rico, or any other additional factor that may deserve special consideration.

(i) Small or Medium Sized Businesses -

Any exempt business with a grant issued under this Act and that generates an average gross income of less than ten million dollars (\$10,000,000) during the previous three (3) taxable years. To determine the average annual gross income, the calculation shall include all types of income, whether covered or not by a grant of industrial tax exemption.

(j) Income from Eligible Investments-

(1) The interests and dividends of eligible funds invested by the exempt business with a grant issued under this Act, in:

(A) loans for the financing of construction, acquisition, or improvements of housing in Puerto Rico;

(B) loans for the construction, expansion, or acquisition of buildings or land, and for the purchase of machinery and equipment or for operating capital used in exempted businesses. The borrower exempted business or the borrower legal entity that is part of the same exempted business, will not qualify for the benefits in this subsection (j) with respect to those investments that it makes, up to the total unpaid balance of its loans for operating capital;

(C) loans for the acquisition of intangible property to be used by exempted businesses in their operations in Puerto Rico, as well as for the financing of research, experiments and development of new industrial products or processes, or the improvement of these, which take place in Puerto Rico;

(D) debt instruments issued by the Puerto Rico Conservation Trust and the Puerto Rico Housing and Human Development Trust, provided that when issuing such debt instruments, the Secretary of the Treasury has not revoked the determination that they are a nonprofit trust in compliance with the terms and conditions established by the Commissioner;

(E) capital notes or preferred stock, as authorized by Act No. 55 of May 12, 1933, as amended, known as the "Banking Act of Puerto Rico", as well as equity securities issued by financial institutions, provided that the total capital raised by equity securities or preferred stocks issued is invested in Puerto Rico, in agreement with the terms and conditions established by the Commissioner;

(F) debt instruments issued by any subsidiary of the "Farm Credit Banks of Baltimore or of its successor the AgFirst Farm Credit Bank, dedicated to finance agricultural loans directly or indirectly with said funds, as well as farmers in Puerto Rico, including loans to rural residents to finance rural housing; loans to cooperative societies owned and controlled by farmers and dedicated to marketing or distribution of agricultural products, purchasing of materials, render services to agricultural businesses, and the acquisition of loans or discounts on notes that have already been granted;

(G) loans issued to finance maritime and air operations directly related to trade and industry in Puerto Rico, including but not limited to the moneys used in the construction, acquisition, and operation of all types of vessels, ships, and aircrafts;

(H) corporate stock or shares in partnerships that own or operate tourist businesses exempted under Act No. 78 of September 10, 1993, as amended, known as the "Puerto Rico Tourist Development Act of 1993," which constitute an eligible investment under Section 2(n) of said Act;

(I) stock in corporations or shares in partnerships established as Capital Investment Funds under Act No. 3 of October 6, 1987, as amended, known as the "Puerto Rico Capital Investment Funds Act," provided the Fund invests at least twenty percent (20%) of the total contributions received in tourism activities;

(J) loans to finance any of the Strategic Projects, as such term is defined in subsection (p) of this section; and

(K) any other debt instruments or loans designated by the Commissioner with the approval of the members of the public sector of the Financial Board and of the Executive Director. The Commissioner is hereby authorized to issue the regulations needed for the administration of this subsection, with the approval of the members of the public sector of the Financial Board and of the Executive Director.

(2) Interest on eligible funds deposited or invested by the exempted business with a grant issued under this Act, in institutions engaged in the banking business, including the Bank for the Economic Development Bank of Puerto Rico, savings and loan associations, savings banks, stock brokerage firms and other similar institutions engaged in business in Puerto Rico, which the Commissioner, with the approval of the members of the public sector of the Financial Board and of the Executive Director, determines to be eligible institutions to receive such eligible funds. Regulations on eligible institutions shall consider, among other things, that said funds be channeled towards activities that promote production, income and employment in Puerto Rico, such as loans for commercial, industrial, agricultural, construction or to preserve natural resources.

(3) Regulations issued under equivalent provisions of preceding laws shall continue in effect and shall apply to investments under this Act until the Commissioner, with the approval of the Financial Board and the Executive Director, amends or repeals such regulations or issues new regulations specifically for funds invested under this Act.

(4) Should the Commissioner determine that an institution is no longer eligible to receive said funds, such determination shall not prevent the interest earned thereon, invested before the institution's loss of eligibility, to continue being considered as eligible interest under this Act until said investment has matured.

For purposes of this subsection (j), the term "eligible funds" shall include funds generated by industrial or service activities covered by an exemption grant issued under this Act (including the taxable years covered by the option of subsection (b) of Section 10 of this Act) or similar provisions of preceding incentive laws.

(k) Predecessor Exempted Business -

(1) Any business that is or was exempt under this Act or preceding incentives acts for the execution of an economic activity substantially similar to the one specified in the grant of a successor business; and

(2) is or was owners to the extent of twenty-five percent (25%) or more of its issued and outstanding stock or other property interest by the successor business or by any of the stockholders or owners of the successor business who own twenty-five percent (25%) or more of the stock or other property interest of the successor business. This last requirement shall not apply when reference is made to a predecessor exempted business in paragraph (4) of subsection (a) of Section 16 of this Act.

(A) The holding of stock or other property interest shall be determined according to the rules concerning the holding of corporate stock or shares in partnerships under Subtitle A of the Puerto Rico Internal Revenue Code.

(B) If any of the stockholders or owners of a successor business affected by said rules can prove to the satisfaction of the Secretary of Treasury that the capital invested or to be invested in the successor business does not proceed directly or indirectly from their spouses, lineal ancestors or descendants, or siblings, but that it proceeds from their own private money, such rules shall not apply to them.

(l) Successor Business-

Any business that obtains a grant issued under this Act to conduct an economic activity substantially similar to that specified in the grant of an predecessor exempted business.

(m) Industrial Tax Exemption Grant-

Shall have the same meaning as "exemption grant," "tax exemption," or merely "exemption" or "grant" which can be used interchangeably as may be convenient for the purpose of illustrating what is provided in the text.

(n) Extraordinary Circumstances-

Any cause of an exceptional nature such as strikes, wars, actions by the Government or the elements, fire and others, or any other cause beyond the control of the exempted business.

(o) Intangible Property-

Patents, inventions, formulas, processes, designs, patterns, “know-how”, copyrights, trade secrets, literary, musical, or artistic compositions, trademarks, trade names, brand names, franchises, licenses, contracts, methods, programs, systems, procedures, goodwill, campaigns, surveys, studies, trials, projections, estimates, client lists, technical data, or any other similar property.

(p) Strategic Projects-

The following units participating in public-private consortiums shall be considered strategic projects for the purposes of this Act:

- (1) cleaning, recovery, conversion, and restoration of the landfills that have been closed in Puerto Rico, including activities of methane recovery and cleaning of aquifers;
- (2) construction of dams and/or reservoirs, including the infrastructure needed for its functioning, with the purpose of increasing storage and reserves, and safeguarding the value of water-production of the Puerto Rico Aqueduct and Sewer Authority and the production of hydroelectric energy; and the construction of water treatment plants;
- (3) construction of plants for the production of energy that use alternative fuels and renewable sources. Provided that after the third year of this Act’s effective date, every plant that requests the benefits of this Act under this paragraph shall be of renewable resources and after the sixth year of this Act’s effective date every plant that begins operations according to what is provided in this subsection must be of renewable sources; and
- (4) construction of mass transportation systems, including but not limited to, railroad systems of mass transportation.

(q) Local Investment Business-

Eligible business owned directly in at least fifty percent (50%) by residents of Puerto Rico.

(r) Community Businesses-

An organization, corporation, workers corporations, production cooperatives, or business initiatives, that in addition to producing goods, provides social and economic impact within the community where it resides and which complies with the requirements that the Executive Director establishes through regulations.

(s) Other Terms-

For purposes of this Act, "Governor" means the Governor of the Commonwealth of Puerto Rico; "Secretary of Development" means the Secretary of the Department of Economic Development and Commerce; "Executive Director" means the Executive Director of the Puerto Rico Industrial Development Company; "Director" means the Director of the Office of Industrial Tax Exemption; "Commissioner" means the Commissioner of Financial Institutions, created by Act No. 4 of October 11, 1985, as amended; "Financial Board" means the Financial Board ascribed to the Office of the Commissioner of Financial Institutions created by Act No. 4 of October 11, 1985, as amended; "Office of Exemption" shall mean the Office of Industrial Tax Exemption; "Puerto Rico Internal Revenue Code" means the Puerto Rico Internal Revenue Code of 1994, Act No. 120 of October 31, 1994, as amended, or any subsequent act that substitutes it; "Federal Internal Revenue Code" shall mean the United States Internal Revenue Code of 1986, Pub. Law 99-514, 68A Stat. 3, as amended, or any subsequent act that substitutes it.

(t) Stocks-

Shall mean shares in a corporation or interests in a partnership or limited liability company.

(u) Energy from Renewable Sources-

Shall mean energy generated from solar, eolic, geothermic, oceanothermic, ocean kinetic, hydroelectric, biomass, hydrogen, solid waste, and methane recovery energy, among other similar sources.

(v) Regional Initiatives -

Shall mean those alliances between municipalities, businesses established in the region, and universities with the purpose of promoting the development of a region in particular, incorporated as non-profit entities, as authorized by Act No. 81 of August 30, 1991, as amended, known as "Puerto Rico Autonomous Municipalities Act". This definition includes the following: Middle Eastern Technological Initiative ("INTECO" for its Spanish acronym), Northern Technological Initiative ("INTENOR" for its Spanish acronym), Northeastern Technological Initiative ("INTENE" for its Spanish acronym), Southern Integral Development ("DISUR" for its Spanish acronym), and the Techno-Economic Corridor ("PR-TEC" for its Spanish acronym). This definition also includes other similar initiatives of municipal governments to incorporate regions and promote their development through alliances between municipalities, the private sector, and the academia.

The remaining terms used in this Act, unless otherwise specifically provided, shall have the same meaning that they have in the Internal Revenue Code of Puerto Rico and its regulations.

Section 3- Tax Rates

(a) Fixed Income Tax Rate- Exempted businesses with a grant issued under this Act, shall be subject to a fixed income tax rate on their net industrial development income during the entire period of exemption as provided in this section, beginning on the date of commencement of operations as determined under section 10 of this Act, in lieu of any other income tax, if any, provided by the Puerto Rico Internal Revenue Code or any other law

(1) In General-

Exempted businesses with a grant issued under this Act shall enjoy a fixed rate on their net industrial development income of four percent (4%) excluding the income derived from the investments described in subsection (j) of Section 2 of this Act. Provided that exempted businesses whose royalty payments to nonresident persons not engaged in trade or business in Puerto Rico for the use or right to use intellectual property in Puerto Rico are subject to the withholding tax rates provided for by paragraph (4), subsection (b) of this Section, shall be subject to a fixed income tax rate of eight percent (8%) on their net industrial development income, excluding the income derived from the investments described in subsection (j) of Section 2 of this Act.

(2) Existing Businesses

Exempted businesses which have had exempt operations under Act No. 135 of December 2, 1997, as amended, and have enjoyed a fixed income tax rate not greater than four percent (4%), but not lower than two percent (2%), may continue to enjoy a fixed income tax rate on their net industrial development income under this Act equal to the rate imposed under said predecessor grant, provided that the Secretary of Development, prior the favorable recommendation of the Secretary of Treasury, and the Executive Director, determines that such reduced rate shall be in the best economic and social interests of Puerto Rico. The Secretary of Development shall require, in exceptional cases, that the exempted business maintains an employment level equal to or greater than eighty percent (80%) of its average employment for the three (3) taxable years prior to the application date for a grant under this Act, or may require a minimum tax payment equivalent to the average tax paid in said period. Any exceptions to these requirements shall have the approval of the Secretary of the Treasury. To determine of what constitutes the best economic and social interests of Puerto Rico factors such as the following shall be analyzed: the nature of the exempted business under this Act, the technology used, the

substantial employments that the same provides, location of the exempted business, potential impact of hiring local suppliers, convenience of having local suppliers of the product, or any other benefit or factor that entails such determination.

(3) Novel Pioneer Activity

Notwithstanding the provisions of paragraphs (1) and (2) of this subsection, the fixed income tax rate will be one percent (1%), provided the Secretary of Development, prior the favorable recommendation of the Secretary of Treasury, and the Executive Director and its Board of Directors, determines that the exempted business under this Act will carry on an economic activity that has not been produced, carried on nor realized in Puerto Rico in the twelve (12) months ending on the date in which the exemption for the pioneer activity is requested, and that such activity has characteristics, attributes or special and impacting qualities for the benefit of Puerto Rico's socioeconomic development, including a profile of the jobs to be created by such pioneer activity.

(A) Determination of a Novel Pioneer Activity

To determine whether an activity constitutes a novel pioneer activity, the Executive Director shall consider the economic impact said activity will represent to Puerto Rico on the basis of priority factors, in particular:

- (i) the degree or level of utilization and integration of research and/or development activities to be carried out in Puerto Rico;
 - (ii) the tax impact that the novel pioneer activity can generate in Puerto Rico;
 - (iii) the nature of the activity;
 - (iv) the capital investment to be made in property, plant and equipment;
 - (v) the uniqueness of the novel pioneer activity in Puerto Rico for the international market;
 - (vi) the technological improvements that will be part of the operations;
- and

(vii) any other factor that merits the recognition of the activity as a novel pioneer activity, given that such activity will result in the best economic and social interests of Puerto Rico.

(B) Economic Activities Created or Developed in Puerto Rico as Intangible Property -

Notwithstanding the provisions of paragraphs (1), (2), and (3) of this subsection, the fixed income tax rate will be zero percent (0%) in the case of novel pioneer activities for which the intangible property was created or developed in Puerto Rico, including but not limited to, activities leading to the commercial feasibility of the product.

(C) Duration of the Period -

The fixed rate applicable by virtue of this paragraph (3) will be granted for the term of the grant. The exempted business that has been granted the benefit provided in this paragraph shall file reports every two (2) years, beginning on the effective date of its grant, to the Executive Director with copy to the Secretary of Development and Secretary of the Treasury, in which report the business will accredit that it has substantially complied with the parameters expressed in the grant. The Executive Director will establish, by means of regulation, the information that such reports shall contain and will have the authority to conduct those investigations and audits that he may deem required for the purpose of confirming that the exempted business has substantially complied with the parameters established in the grant.

(4) Any exempted business under this Act that is located or locates its operations in a municipality classified as low industrial development zone or intermediate industrial development zone, according to what is stated in Section 11 of this Act, may reduce the fixed income tax rate established in the previous paragraphs by an additional point five per cent (.5%). In those cases where an exempted business with a grant issued under this Act, maintains operations in more than one industrial zone, such business shall enjoy the reduction established in this paragraph with regards to the industrial development income attributable exclusively to its operations in the low industrial development zone.

(5) Any exempted business with a grant issued under this Act that is located or locates its operations in the special development zone composed of the municipalities of Vieques and Culebra, shall be totally exempted from the payment of income tax on the industrial development income resulting from those operations during the first ten (10) years of the corresponding period, as provided, and starting on the date of commencement of operations

determined under Section 10 of this Act. The remaining exemption period of said exempted business will be taxed at fixed income tax rate of two per cent (2%) in lieu of any other taxes, if any.

(b) Royalties, Rents and Licensing Rights - Notwithstanding the provisions of the Puerto Rico Internal Revenue Code, in the case of payments made by exempted businesses with a grant issued under this Act, to corporations, partnerships, or non-resident persons, not engaged in trade or business in Puerto Rico, for the use or privilege of use in Puerto Rico of intangible property related to the operation declared exempt under this Act, and provided that such payments are considered to be totally from sources within Puerto Rico, the following rules shall be observed:

(1) Tax on Corporations, Foreign Partnerships, or Non-Residents Not Engaged in Trade or Business in Puerto Rico- Tax Imposition- A tax of twelve percent (12%) will be levied, collected, and paid, in lieu of the tax imposed by Sections 1221 and 1231 of the Puerto Rico Internal Revenue Code, on the amount of those payments received or implicitly received, by any foreign corporation or partnership not engaged in trade or business in Puerto Rico, derived exclusively from sources within Puerto Rico.

(2) Tax Withholding at Source in the Case of Foreign Corporations and Partnerships not Engaged in Trade or Business in Puerto Rico- Every exempted business with the obligation to make payments to non-residents for the use in Puerto Rico of intangible property related to the operation exempted under this Act, shall deduct and withhold at source a tax equal to that imposed in paragraph (1) or (3) of this subsection.

(3) Existing Businesses- In the case of persons who transfer technology or intangibles to exempted businesses that have had exempted operations under Act No. 135 of December 2, 1997, as amended, enjoying a rate lower than twelve percent (12%), the Secretary of Development, prior the favorable recommendation from the Secretary of the Treasury and the Executive Director, may authorize the imposition of a rate equal to the one imposed under such grant, approved according Act No. 135 of December 2, 1997, in lieu of the rate established in paragraph (1) of this subsection, provided he determines that such reduced tax attends to the best economic and social interests of the Commonwealth of Puerto Rico. The Secretary of Development shall require, except on exceptional cases, that the exempted business maintains an employment level equal or greater than eighty percent (80%) of its average employment for the three (3) taxable years prior to the date of its application for exemption under this Act, and any exception to this requirement must have the approval of the Secretary of Treasury. To determine what constitutes the best interests of the Commonwealth of Puerto Rico, factors shall be analyzed, such as: the special nature of the exempted business, the technology used, the substantial employment provided by such business, the location of the business, the possible contracting with local suppliers, the

convenience of having local supplies of the product, or any other benefit or factor that merits such determination.

(4) Alternative Tax- The Secretary of Development shall have the power to allow that exempted businesses which make payments of income considered to be totally from sources within Puerto Rico, because of being for the use in Puerto Rico of manufacturing intangibles related to the exempted operation, such as patents, intellectual property, formulas, technical “know-how” and other similar property, be subject to the following treatment:

(A) A two percent (2%) tax will be levied, collected, and paid for each taxable year, in lieu of the tax imposed by Sections 1221 and 1231 of the Puerto Rico Internal Revenue Code, on the amount of those payments received or implicitly received, by every foreign corporation or partnership not engaged in trade or business in Puerto Rico, derived from sources within Puerto Rico.

(B) Every exempted business subject to paragraph (4) of this subsection, with the obligation to make payments to non-residents for the use in Puerto Rico of intangible property related to the exempted operation, shall deduct and withhold at source from such payments a tax equal to that imposed in sub-paragraph (A) of this paragraph.

The alternative tax imposed by this paragraph (4) will be established before the start of the effectiveness of the tax exemption grant, it shall be irrevocable while the grant is in effect, and will be documented as part of the terms and conditions agreed upon in the grant. This alternative tax will not apply to exempted businesses described in paragraphs (2) and (3) of subsection (a) of this Section 3.

(c) Investment Income -

An exempted business with a grant issued under this Act shall enjoy total exemption on income derived from eligible investments described in subsection (j) of Section 2 of this Act. The expiration, renegotiation, or conversion of the grant or other concession of incentives of the investing or issuing entity, as the case may be, will not prevent the income earned from the investment from being treated as income from eligible investments under this Act during the remaining period of the investment.

(d) Distribution, Sale or Exchange of Stock or Assets -

(1) The stockholders or partners of a corporation or partnership which is an exempted business with a grant issued under this Act will not be subject to income tax on distributions of dividends or profits from the industrial development income of such exempted business,

or in the case of exempted businesses that are not domestic corporations, on distributions of dividends or profits from the income from sources outside of Puerto Rico earned by the exempted business, pursuant to the Puerto Rico Internal Revenue Code.

Subsequent distributions of the industrial development income of any corporation or partnership will also be exempted from all taxation.

Gains realized on the sale, exchange, or other disposition of stock of corporations or interests in partnerships that are or have been exempted businesses; shares in joint ventures and similar entities composed of various corporations, partnerships, individuals, or a combination thereof, that are or have been exempted businesses, and stock of corporations or interests in partnerships that in some way own the previously described entities, shall be subject to the provisions of paragraph (3) of this Section when such sale, exchange, or other disposition takes place, and any subsequent distribution of such gains, whether as dividend or as a liquidating distribution, shall be exempted from any additional taxation.

(2) Imputation of Exempted Distributions-

The distribution of dividends or profits made by an exempted business with a grant issued under this Act, even after the expiration of its tax exemption grant, shall be deemed as made from its industrial development income if upon its date of distribution it does not exceed the undistributed balance of its accumulated industrial development income, unless said exempted business chooses, at the time of declaration, to distribute the dividends or profits wholly or partially, from other earnings or profits. The amount, year of accumulation and nature of the distribution of the industrial development income shall be that designated by said exempted business by a notice sent jointly with the payment thereof to the stockholders or partners and to the Secretary of Treasury, through an informative statement, not later than the 28th of February following the year of the distribution.

In the case of corporations or partnerships which, on the date they commence operations as exempted businesses have accumulated earnings and profits, distributions of dividends or profits made from such date toward shall be deemed to be made from the undistributed balance of said earnings and profits, but once this balance is exhausted as a result of said distributions, the provisions of the first paragraph shall apply.

(3) Sale or Exchange of Stock or Assets -

(A) During the Exemption Period - Gains from the sale or exchange of stock or interest in a partnership or substantially all assets of an exempted business with a grant issued under this Act made during its exemption period and that would have been subject to the payment of income taxes under the Puerto Rico Internal Revenue

Code, shall be subject to a four percent (4%) tax on the amount of the realized gain, if any, in lieu of any other tax levied by said Code. Any loss on the sale or exchange of said stock or assets shall be recognized according to the provisions of the Puerto Rico Internal Revenue Code.

(B) After the Termination Date of the Exemption Period - The gain in the event that said sale or exchange takes place after the termination date of the exemption, shall be subject to the tax provided for in sub-paragraph (A) above, but only up to the book value of the stock or of substantially all the assets of the corporation as of the termination date of the exemption period reduced by the amount of the exempted distributions received on the same stock after said date, minus the basis of said stock or of substantially all the assets. Any remainder of the gain or any loss, if any, shall be recognized according to the provisions of the Puerto Rico Internal Revenue Code in effect on the date of the sale or exchange.

(C) Exempt Exchanges - Exchanges of stock that do not result in taxable events due to their being tax free reorganizations, shall be treated according to the provisions of the Puerto Rico Internal Revenue Code in effect on the date of the exchange.

(D) Determination of Basis in Sale or Exchange of Stock - The basis of the stock, interests, or assets of exempted businesses under this Act upon the sale or exchange will be determined according to the applicable provisions of the Puerto Rico Internal Revenue Code in effect at the time of the sale or exchange, increased by the amount of industrial development income accumulated under this Act.

(E) For purposes of this paragraph (3), the term “substantially all assets” will mean those assets of the exempted business that represent no less than eighty percent (80%) of the book value of the business at the time of the sale.

(F) The Secretary of the Treasury shall establish necessary regulations to place in effect the provisions of this paragraph.

(4) Liquidation -

(A) General Rule - No income tax shall be levied on or collected from the transferor or transferee with respect to the complete liquidation of an exempted business with a grant under this Act, on or before the expiration of its grant, provided the following requirements are met:

- (i) All property distributed in liquidation was received by the transferee pursuant to a plan of liquidation on or before the expiration of the grant, and
- (ii) the distribution in liquidation by the transferor, whether at one time or from time to time, was made by the transferor in cancellation or in full redemption of its entire capital stock.

The basis of the transferee in the property received in liquidation shall be equal to the adjusted basis of said the exempted business in such property immediately before the liquidation. In addition, and for purposes of this section, a corporation or partnership that is a partner in a partnership that is an exempted business shall be deemed, in turn, an exempted business.

(B) Liquidation of Transferors with Revoked Grants.- If the grant of a transferor is revoked before its expiration, the provisions of Section 13, the accumulated surplus industrial development income pursuant to as of the effective date of the revocation may be transferred to the transferee at any later time, subject to the provisions in sub-paragraph (A) of this paragraph. In cases of mandatory revocation, the accumulated surplus from industrial development income shall be taxed as provided in the Internal Revenue Code.

(C) Liquidations after Expiration of the Grant. - After the grant of the transferor has expired, it may transfer to the transferee the accrued surplus industrial development income earned during the effectiveness of the grant, subject to the provisions of sub-paragraph (A) of this section.

(D) Liquidation of Transferors with Exempt and Nonexempt Activities. - In case the transferor carries out exempt and nonexempt activities, the latter may transfer to the transferee the surplus industrial development income accrued under this Act and the property devoted to industrial development under this Act as part of its total liquidation, subject to the provisions of sub-paragraph (A) of this section. The accrued surplus that is not industrial development income and the property that is not devoted to industrial development shall be distributed according to the provisions the Puerto Rico Internal Revenue Code.

(e) Payment of the Tax. -

Absent a contrary provision, withheld or payable taxes shall be withheld or paid in the manner provided by the Puerto Rico Internal Revenue Code for the payment of income taxes and withholdings in general.

(f) Ineligible Businesses Under Previous Acts. -

During the first four (4) years of effectiveness of this Act, in the case of eligible businesses, under Section 2(d)(1)(B) of this Act, which are dedicated to the production of manufactured products, or to the rendering of services that have not been eligible to receive incentives under Act No. 135 of December 2, 1997, or previous incentives acts, the fixed income tax rates provided in this Section 3, shall partially apply to the industrial development income, as provided below:

(A) Twenty five percent (25%) of the net industrial development income generated during the first taxable year of the exempted business, shall be subject to the applicable fixed income tax rate provided in this Section 3, and the remaining seventy five percent (75%) of the net industrial development income, shall be subject to taxation as provided by the rules and rates applicable under the Puerto Rico Internal Revenue Code.

(B) Fifty percent (50%) of the net industrial development income generated during the second taxable year of the exempted business, shall be subject to the applicable fixed income tax rate provided in this Section 3, and the remaining fifty percent (50%) of the net industrial development income shall be subject to taxation as provided by the rules and rates applicable under the Puerto Rico Internal Revenue Code.

(C) Seventy five percent (75%) of the net industrial development income generated during the third taxable year of the exempted business, shall be subject to the applicable fixed income tax rate provided in this Section 3, and the remaining twenty five percent (25%) of the net industrial development income shall be subject to taxation as provided by the rules and rates applicable under the Puerto Rico Internal Revenue Code.

(D) For the fourth taxable year of the exempted business, the totality of its net industrial development income shall be subject to the applicable fixed income tax rate, as provided under in this section.

(g) Limitation of Benefits. -

(A) In the case that on the date of its application for incentives, according to the provisions of this Act, an eligible business is dedicated to the activity for which the benefits of this Act are granted, the eligible business may enjoy the fixed industrial development income tax rate provided by this Section, but with respect to the excess net income from such activity over the average net income of the three (3) taxable

years prior to the date when the application was filed, which shall be designated as “base period income” for purposes of this subsection, .

(B) In order to determine the base period, the production and sales of any predecessor business to the applicant business shall be taken into account. For these purposes “predecessor business” shall include any business related to the applicant business, even if it was not previously exempted, and without taking into account if it operated under a different legal name or owners.

(C) The income attributable to the base period shall be subject to the tax rates provided by the Puerto Rico Internal Revenue Code.

(D) The base period income shall be adjusted, reducing such amount by twenty five percent (25%) annually, until it is reduced to zero (0) by the fourth taxable year of the application of the terms of the grant of the business exempted under this Act. For this purpose, those years for which the exempted business made an election under subsection (b) of Section 10 of this Act, will be taken into consideration.

Section 4 – Special Deductions

(a) Deduction and Carryover of Net Operating Losses.-

- (1) **Deduction for Current Losses Incurred in Activities Not Covered by an Exemption Grant.** – If an exempted business whose grant has been issued under this Act incurs a net loss that is not from the operation declared exempt determined without the benefit of the special deductions provided in subsection (b) of this section, such loss shall only be used against income not covered by an exemption grant and shall be governed by the provisions of the Puerto Rico Internal Revenue Code. The share of losses in special partnerships that own or operate tourist businesses exempted under the Puerto Rico Tourist Development Act of 1993, as amended, may be used against income covered by a tax exemption grant issued under this or previous acts.
- (2) **Deduction for Current Losses Incurred in the Operation of the Exempted Business.** – If an exempted business whose grant has been issued under this Act incurs a net loss in the operation declared exempt under this Act determined without the benefit of the special deductions provided in subsection (b) of this section, said loss may be deducted against the industrial development income of the operations which generated the loss or in operations covered by other exemption grants under this Act or previous acts.

- (3) Deduction of Carryover Losses of Prior Years. – A carryover deduction of losses from prior years shall be granted as provided below:
- (A) The excess of the losses deductible under paragraph (2) may be carried over and applied against the industrial development income of subsequent taxable years. The losses shall be carried over in the order they were incurred.
 - (B) Any net loss incurred in a year in which the election of subsection (b) of Section 10 is effective may be carried over only against industrial development income generated by the exempted business under the grant in which the election of subsection (b) of Section 10 was made. Such losses shall be carried over in the order they were incurred.
 - (C) Once the period of tax exemption is expired for income tax purposes, the net losses incurred in the operation declared exempt under this Act, as well as any excess of deductions allowed under subsection (b) of this section that the exempted business is carrying over as of the date of expiration of such period, may be deducted against any Puerto Rico taxable income, subject to the limitations provided in Subtitle A of the Puerto Rico Internal Revenue Code. Such losses shall be considered as incurred in the last taxable year in which the exempted business with a grant issued under this Act enjoyed income tax exemption under the grant.
 - (D) The amount of the net operating loss to be carried over shall be determined in accordance with the provisions of section 1124 of the Puerto Rico Internal Revenue Code, except that, in addition to the exceptions, additions and limitations provided in such section, the loss shall be adjusted by the income derived from eligible activities under subsection (j) of section 2 of this Act.

(b) Special Deduction for Investment in Buildings, Structures, Machinery and Equipment.-

Every exempted business whose grant has been issued under this Act shall be allowed to deduct in any taxable year in which incurred, in lieu of any expense capitalization required under the Puerto Rico Internal Revenue Code, the total expenses incurred after the effective date of this Act in the purchase, acquisition or construction of buildings, structures, machinery and equipment, provided such buildings, structures, machinery and equipment: (i) have not been previously used or depreciated by any other business or person in Puerto Rico; and, (ii) are used for the manufacture of the products or the rendering of the services for which the benefits under this Act were granted. The deduction herein provided shall not be in addition to any other deduction provided by law, but merely an acceleration of the deduction of the expenses described above. Provided that in the case of machinery and equipment previously used outside of Puerto Rico, but not previously used or

depreciated in Puerto Rico, the investment in such machinery and equipment shall qualify for the special deduction provided in this subsection (b) solely if at the time of its purchase by the exempted business, it has a remaining life of at least fifty (50%) percent of its useful life determined in accordance with the Puerto Rico Internal Revenue Code. The exempted business whose grant has been issued under this Act shall be allowed to deduct in any taxable year in which incurred, in lieu of any expense capitalization required under the Puerto Rico Internal Revenue Code, the total expenses incurred after the effective date of this Act in the remodeling or repair of buildings, structures, machinery and equipment, whether such buildings, structures, machinery and equipment have been acquired or constructed before or after the effective date of this Act, and regardless of whether used or depreciated by other business or person before such acquisition by the exempted business whose grant was issued under this Act or under previous tax incentives acts. The amount of the eligible investment qualifying for the special deduction provided in this subsection in excess of the industrial development income of the exempted business whose grant was issued under this Act in the year of the investment, may be claimed as a deduction in subsequent taxable years until such excess is exhausted. No deduction shall be allowed under this subsection in connection with the investment in buildings and structures, machinery and equipment that has enjoyed any of the credits provided in sections 5 or 6 of this Act.

Provided that the special deduction provided in this subsection may also be claimed by the exempted business in any year in which it opts to select the benefit of the flexible tax exemption provided by section 10 (b) of this Act.

Section 5.- Credits

(a) Credit for the Purchase of Products Manufactured in Puerto Rico. -

(1) If an exempted business that holds a grant issued under this Act or under previous incentives acts, purchases products manufactured in Puerto Rico, including components and accessories, it will have the right to claim a credit against its tax on industrial development income provided in subsection (a), Section 3 of this Act, or against the income taxes under the preceding applicable incentives act, equal to twenty-five percent (25%) of the purchase of said products during the taxable year in which said credit is claimed, up to a maximum of fifty percent (50%) of said tax. This credit shall be granted only for purchases of products manufactured by business not related to the exempted business.

(2) In the event the exempted business with a grant under this Act or under previous incentives acts purchase or uses products transformed into articles of commerce from recycled materials or recycled raw materials or recollected and/or refurbished by exempted businesses with a grant under sub-paragraph (J) of paragraph (1) of subsection (d) of Section 2 of this Act, or of similar provisions of previous acts, the credit stated in the last

paragraph shall be equal to thirty-five percent (35%) of total purchases of said products, or of the amount paid for its use, as the case may, be, during the taxable year for which the credit is claimed, up to a maximum of fifty percent (50%) of the tax against which such credit is claimed, as stated in paragraph (1) of this subsection (a). This credit shall be granted solely for purchases of products manufactured by businesses not related to the exempted business.

(3) The credit provided in this subsection shall be nontransferable, except in the case of a tax free reorganization. The amount of the credit not used by the exempted business in a taxable year may be carried over to subsequent taxable years, until exhausted. This credit will not generate a tax refund.

(4) In the case of an exempt business whose grant was issued under a previous incentives act the credit provided in this section shall not be available and no credit shall be granted under this subsection for a taxable year, if such exempted business claims any special deduction or credit of an analogous nature under previous incentives acts for said taxable year.

(b) Job Creation Credit.-

(1) A credit for each job created during its first year of operations shall be granted to all exempted business beginning operations after July 1, 2008. The amount of this credit depends on the industrial development zone where the exempted businesses are located, as hereinafter provided:

Area	Credit
Vieques and Culebra	\$5,000
Low Industrial Development Zone	\$2,500
Intermediate Industrial Development Zone	\$1,000
High Industrial Development Zone	\$0

(2) In cases in which an exempted business with a grant issued under this Act, establishes operations in more than one zone, the amount of the credit shall correspond to the site where the operations creating the employments is located.

(3) For purposes of this subsection, the employment of the aforementioned exempted business shall consist of the number of Puerto Rico residents working as permanent, full-time employees with regular work load in the exempted business, but shall not include employees such as consultants or independent contractors. The exempted business shall be

required maintain an average employment equal to or greater than the employment amount that generated the credit, for each of the subsequent three (3) years following the year in which the credit was granted. The Secretary of Treasury shall establish through regulations the applicable mechanism of proportional recapture based on the time elapsed and the level of employment maintained, in case that said exempted business ceases to comply with the required level of employment.

(4) Said exempted business may claim the credit provided in this subsection, only against the tax on industrial development income provided in subsection (a) of Section 3 of this Act. This credit may not be sold, transferred, or exchanged, nor create a refund for the exempted business. However, the credit provided by this subsection not used during the first year of operations may be carried forward for a period that shall not exceed four (4) years since the first taxable year in which the exempted business generates net income.

(c) Credit for Investment in Research and Development, Clinical Trials, Toxicology Tests, Infrastructure, Renewable Energy, and Intangible Property.-

(1) Any exempted business with a grant issued under to this Act or any previous incentives acts, may claim a credit for investment equal to fifty percent (50%) of the special eligible investment made in Puerto Rico after the approval of this Act by said exempted business or by any of its affiliates. All special eligible investments made prior to the income tax return filing due date, as provided by the Puerto Rico Internal Revenue Code, including any extension granted by the Secretary of Treasury, shall qualify for the tax credit of this subsection for the taxable year for which said tax return is being filed. This credit may be applied, at the option of the exempted business, against the tax on industrial development income provided in subsection (a) of Section 3 of this Act, or to the income tax applicable under the previous incentives act under which the grant was issued to the exempted business and/or against operating expenses of the exempted business related to electric energy, water, and sewage.

(2) For purposes of the credit provided in this Section, the term “special eligible investment” means the amount of cash used by the exempted business with a grant issued under this Act, or any entity affiliated to said exempted business, in research and development activities, including operating expenses, clinical trials, toxicology tests, infrastructure, renewable energy, or intellectual property. The term special eligible investment shall include an investment made by the exempted business with cash from a loan guaranteed by the exempted business or its assets, or by any of its affiliates or their assets.

The Secretary of Treasury shall establish through regulation the expenses qualifying as special eligible investment.

(3) Credit Usage - The tax credit provided in this subsection may be taken in two (2) or more installments: up to fifty percent (50%) of said credit may be taken in the year the eligible investment is made and the balance of said credit in subsequent years until exhausted; provided that such limitation shall not apply to operating expenses of said exempted business related to electric energy, water, and sewage. This credit shall not generate a refund.

(4) Transfer of Credit for Special Eligible Investment -

(A) The credit for special eligible investment provided in this subsection may be transferred, sold, or otherwise disposed of by the exempted business to any other person, totally or partially, and it shall be governed by the provisions in paragraphs (1) and (3) of this subsection, except that if the transferor is not an exempted business, the credit may be used against the income tax provided in Subtitle A of the Puerto Rico Internal Revenue Code.

(B) The money or the value of the property received in exchange for the investment credit shall be exempt from taxation under Subtitle A of the Puerto Rico Internal Revenue Code and under the "Municipal License Tax Act", up to the amount of the investment credit transferred.

(C) Purchasers of investment tax credits shall be exempted from taxes under Subtitle A of the Puerto Rico Internal Revenue Code on the difference between the amount paid to purchase said credits and the value thereof, and said purchasers shall not be subject to the provisions of Chapter 1 of Subtitle F of the Puerto Rico Internal Revenue Code.

(5) Adjustment to Basis - The basis of any asset for which the credit in this subsection is claimed shall be reduced by the amount of the credit claimed.

(6) The exempted business may not claim this credit with respect to the portion of eligible investment for which it claimed the deduction established in subsection (b) of Section 4 of this Act, or any analogous special deduction under previous incentives acts or

claims or with respect to which it has claimed any of the credits in this Section or in Section 6 of this Act or analogous credits or special deductions under previous incentives acts. This credit shall not generate a refund.

(7) In the case of an exempted business with a grant issued under a previous incentives act, the credit provided under this subsection shall not be available, and no credit shall be granted under this subsection for the taxable year, if said exempted business claims any credit of an analogous nature or special deduction under said incentives act for said taxable year.

(d) Investment in Machinery and Equipment for the Generation and Efficient Use of Energy -

(1) Any exempted business with a grant issued under this Act or under previous acts, may claim a credit of fifty percent (50%) of its eligible investment made after the approval of this Act. An eligible investment made prior to the income tax return filing due date provided by the Puerto Rico Internal Revenue Code, including an extension granted by the Secretary of Treasury, shall qualify for the tax credit in this subsection in the taxable year for which said return is filed. Said credit may be applied, at the election of the exempted business, toward income tax provided by subsection (a) of Section 3 of this Act or the applicable income tax under previous incentives acts.

(2) Eligible Investment- For purposes of this subsection, eligible investment shall mean the amount of cash used to purchase machinery and equipment to generate energy with alternate fuels (to oil). Provided that after the third year this Act is in effect, only purchases of machinery and equipment to generate energy from renewable sources of energy shall qualify for the credit. Purchases by exempted businesses with a grant issued under this Act, or a previous act, of this type of equipment, regardless of whether said equipment generates energy to be sold, whether on a commercial scale or not, or only for the exempted businesses' own consumption, shall qualify as eligible investment. The term eligible investment shall not include an investment made with cash from a loan guaranteed by the exempted business itself or by its assets. The Department of Treasury, along with the Energy Affairs Administration, shall establish through regulation the machinery and equipment that qualify as eligible investment.

(3) Maximum Amount of the Credit-

(A) In the case of an eligible investment made by an exempted business with a grant issued under this Act or previous acts, to generate energy for its own consumption, the credit shall not exceed twenty five percent (25%) of the income tax provided in subsection (a) of Section 3 of this Act, or the income tax applicable under previous acts.

(B) In the case of an eligible investment made by an exempted business described in Section 2(d)(1)(H) or an analogous section under previous incentives acts in order to establish or make a substantial expansion in its energy generating operations, the maximum amount of credit that can be granted exempted [sic] shall be eight million dollars (\$8,000,000) for each exempted business, up to an aggregate maximum of twenty million dollars (\$20,000,000) per taxable year.

(4) In the situation described in sub-paragraph (B) of paragraph (3) of this subsection, the provisions of subsection (d) of Section 6 shall apply. The provisions in subsection (e)(1) of Section 6 will apply to the credit described in this subsection. For purposes of applying said provisions, the word “investor” shall be substituted by “exempted business”.

(5) The exempted business may not claim this credit with respect to the portion of the eligible investment for which it takes or has taken the deduction provided in subsection (b) of Section 4 of this Act, or analogous special deductions under previous incentives acts or claims or has claimed any of the credits provided in this Section or in Section 6 of this Act or analogous special deductions credits under previous incentives acts. This credit shall not generate a refund.

(e) Tax Credit for Reducing the Cost of Electric Energy-

(1) Base Credit - Any exempted business that is an industrial customer of the Electric Power Authority with a grant issued under this Act or under previous incentives acts, may take a credit only against the income tax under subsection (a) of Section 3 of this Act, or the income tax applicable under previous incentives acts equal to three percent (3%) of the payments made to the Electric Power Authority for net electric energy consumption of the eligible business operation during the corresponding taxable year.

(2) Additional Credits- In addition to the credit provided in paragraph (1) of this subsection, the following credits shall be granted for net electric energy consumption:

(A) Any exempted business that is an industrial customer of the Electric Power Authority with a grant issued under this Act or under previous acts and has maintained an average of twenty five (25) employees or more during the taxable year, may take an additional credit of three point five percent (3.5%) of payments made to the Electric Power Authority in the operation of the eligible business.

(B) Any exempted business that is an industrial customer of the Electric Power Authority with a grant issued under this Act or under previous acts and has maintained an average payroll of five hundred thousand dollars (\$500,000) or more during the taxable year, may take an additional credit of three point five percent (3.5%) of the payments made to the Electric Power Authority in the operation of the eligible business.

(C) Any exempted business that is an industrial customer of the Electric Power Authority with a grant issued under this Act or under a previous incentives acts and that complies with requirements of sub-paragraphs (A) and (B) of this paragraph in one taxable year, may claim both tax credits along with the base credit for an annual maximum of ten percent (10%) of payments made to the Electric Power Authority in the operation of the eligible business. The maximum credit to be claimed starting in 2013 shall be reduced on reason by one percent (1%) per year as follows manner:

Taxable Year	Maximum Claimable Credit
2013	9%
2014	8%
2015	7%
2016	6%
2017	5%

(3) The credits provided by this subsection shall not be transferable. Nonetheless, the amount of the credits for energy costs not used in the taxable year in which it was originated may be carried over to subsequent taxable years. Provided the amount of credit generated

and not used by the end of Fiscal Year 2017-2018, may be carried over only during the subsequent four (4) taxable years. These credits may not generate a refund.

(4) The Executive Director of the Electric Power Authority shall issue, upon request from the exempted business that is an industrial customer of the Electric Power Authority, a certification indicating the total payments to that agency for net electric energy consumption during the corresponding taxable year.

(5) Duration and Oversight Provisions -

The credits provided in this subsection shall have a duration of ten (10) years beginning on July 1, 2008. During the ten (10) year duration of the credits, the maximum amount to be granted shall be seventy five million dollars (\$75,000,000) per year up to a maximum of six hundred million dollars (\$600,000,000), during said ten (10) year period. Costs associated to them shall be covered by the General Fund of the Government of Puerto Rico and the Puerto Rico Electric Power Authority in the following proportions:

Fiscal Year	Electric Power Authority	General Fund
2008-2009	---	100%
2009-2010	4%	96%
2010-2011	8%	92%
2011-2012	12%	88%
2012-2013	16%	84%
2013-2014	20%	80%
2014-2015	35%	65%
2015-2016	50%	50%
2016-2017	65%	35%
2017-2018	80%	20%

(6) The cost to the Electric Power Authority shall be recovered from reductions of operating expenses, efficiency increases, income generated from wheeling, and reduction in the cost of generating or purchasing energy, and shall not be recovered directly or indirectly from customers of the Electric Power Authority nor shall it be interpreted as cause for

layoffs or payroll reduction, hence it is provided that the Electric Power Authority shall not pass the cost of this credit to its customers. If during the duration of this credit the average cost per kilowatt of energy reduces to ten (10) cents during two (2) consecutive years the credit hereby provided shall cease.

(f) Intellectual Property Transfer Credit -

Any exempted business with a grant issued under this Act (except those subject to paragraph (4), subsection (b), of Section 3 of this Act, or that enjoy the benefit provided in paragraph (3), subsection (b), of Section 3 of this Act), may take a credit only against the fixed tax industrial development income provided in subsection (a) of Section (3) of this Act, equal to twelve percent (12%) of the payments made to corporations, partnerships, or non-resident persons, for the use or right to use in Puerto Rico of intangible property in their exempt operation, provided that the income from such payments is from sources in Puerto Rico. In the case of exempted businesses that are subject to the alternate imposition provided in paragraph (4) of subsection (b) of Section 3 of this Act, the applicable percentage for the purposes of the previous sentence shall be two percent (2%). The exempted businesses that availed themselves of the benefit for existing businesses provided in paragraph (3) of subsection (b) of Section 3 of this Act shall not be entitled to claim the credit herein provided. The tax credit established in this subsection shall not be transferable, but may be carried over until it is exhausted. However, said carry forward shall never exceed the period of eight (8) taxable years counted from the closing of the taxable year in which the credit was originated. This carry forward shall never result in a tax lower than that provided in paragraph (3) of subsection (h) of this Section. This credit shall not be refunded.

(g) Credit for the Investment in Strategic Projects-

(1) Any exempted business that holds a grant issued under this Act or under prior acts may claim an investment credit equal to fifty percent (50%) of the eligible investment in strategic projects made in Puerto Rico after the approval of this Act by the exempted business or by any entity affiliated to the exempted business. Every eligible investment made prior to the due date established in the Puerto Rico Internal Revenue Code for filing income tax returns including any extension granted by the Secretary of the Treasury to file the same, shall qualify for the tax credit of this Section for the taxable year for which the tax return is being filed. Said credit may be applied, at the option of the exempted business, against the fixed tax of industrial development income provided in subsection (a) of Section 3 of this Act, or the income tax applicable under prior incentives acts pursuant to which the grant for the exempted business was issued, and/or against the operational costs of the exempted business related to electricity, water, and sewage.

(2) For purposes of the credit in this Section, the term “Eligible Investment in Strategic Projects”, means the amount of cash, from any source of financing, used by the exempted business, or by any entity affiliated to the exempted business, in activities of design, development, and construction of dams and/or reservoirs and all infrastructure necessary for its operation, as well as any infrastructure for the operation of a strategic project. The term eligible investment shall include an investment made with the cash from a loan that is guaranteed by the exempted business or by its assets, or by any entity affiliated to the exempted business or its assets.

(3) Credit Usage - The exempted business may use the credit for eligible investment in order to satisfy up to fifty percent (50%) of the income tax provided in subsection (a) of Section 3 of this Act, or income tax applicable under the previous incentives act pursuant to which the grant was issued to the exempted business, for the taxable year of the exempted business. Provided, that said limitation shall not apply with respect to the operational costs of the exempted business related to electricity, water, and sewage.

(4) Credit Carry Forward- Every credit for eligible investment, including the credit in excess of the percent established in subsection (a) of this Section 3, not used in a taxable year may be carried forward to subsequent taxable years until exhausted. This credit shall not generate a refund.

(5) The exempted business may not claim this credit with respect to the portion of the eligible investment in strategic projects over which it takes or has taken the deduction established in subsection (b) of Section 4 of this Act, or claims or has claimed any of the credits provided in this Section or in Section 6 of this Act.

(6) Adjustment to Basis- The basis of any asset for which the credit provided in this subsection is claimed shall be reduced by the amount of the credit claimed.

(7) Transfer of Credit for Eligible Investment for Strategic Projects

(A) The investment credit provided by this paragraph may be transferred, sold or in any way disposed of by the exempted business to any other person, totally or partially, and it will be governed by the provisions of subsections (1) and (3) of this Section, except , if that the assignee is not an exempted business, it will be able to claim the credit against the income tax provided in Subtitle A of the Puerto Rico Internal Revenue Code.

- (B) The money or the value of the property received in exchange for the investment credit shall be exempt from taxation under Subtitle A of the Puerto Rico Internal Revenue Code, and from the “Municipal License Tax Act”, up to an amount equal to the amount of the investment credit transferred.
- (C) Purchasers of investment tax credits shall be exempt from taxation under Subtitle A of the Puerto Rico Internal Revenue Code or the difference between the amount paid to acquire said credit and the value thereof, and such buyers shall not be subject to the provisions of Chapter 1 of Subtitle F of the Puerto Rico Internal Revenue Code.
- (D) Basis Adjustment- The basis of any assets for which the credit provided in this Section is claimed shall be reduced by the amount of the credit transferred.

(h) Credit Usage and Minimum Tax.-

The usage of the tax credits provided in this Section and in Section 6 of this Act, shall be subject to the following rules:

- (1) Tentative Tax.- The exempted business shall first calculate its tax obligation in accordance with the fixed income tax rate applicable provided in Subsection (a) of Section 3 of this Act.
- (2) Credit Usage.- The sum of the tax credits granted in Section 6 of this Act and subsections (a), (b), (c), (d), (e), (f) and (g) of this Section 5, subject to the limitations applicable to each one, claimed by the exempted business shall be subtracted from the tax liability calculated in paragraph (1) of this subsection (h).
- (3) Minimum Tax.- The tax determined on industrial development income computed after applying the credits in accordance with paragraph (2) of this subsection, shall never be less than the amount that, added to the amounts deposited under Subsection (b) of Section 3 with respect to a taxable year, results in:
 - (A) In the case of a small or medium sized business, one percent (1%) of the net industrial development income from the exempt business;

- (B) In the case of a local investment business, three percent (3%) of the net industrial development income from the exempt business;
 - (C) In all other cases, the fixed income tax rate provided in Subsection (a) of Section 3 of this Act that may be applicable to the exempted business multiplied by the net industrial development income from the exempted business, not including income described in Subsection (j) of Section 2 of this Act.
- (4) The exempted business with a grant issued under this Act, shall pay the greater of paragraph (2) or paragraph (3) of this subsection (h).

In the cases described in sub-paragraphs (A) and (B) of paragraph (3) of this subsection (h), the minimum tax provided therein shall cease to apply, and subparagraph (B) or (C), whichever is applicable, will apply for the taxable years in which the exempted business ceases to qualify as a small or medium sized business or a local investment business, as the case may be.

An exempted business with a grant issued under a previous incentives act, that claims special deductions or credits under such previous incentives act, may not claim tax credits analogous to those provided in Sections 5 and 6 of this Act.

Section 6 - Industrial Investment Credit

- (a) For purposes of this Section, the following terms will have the following meaning:

- (1) Investor.-

Means any person that makes an eligible investment.

- (2) Eligible investment.-

For purposes of this paragraph, any of the following investments will be considered an eligible investment:

- (A) The amount of cash used in the purchase of a majority (fifty percent (50%) or more) of the equity interests, or of the operational assets of an exempted business with a grant issued under this or previous acts, that is in the process of closing operations in Puerto Rico, to continue operating it, or the cash contributed to such business in exchange for corporate stock or partnership interest that is used by the exempted business for: (i) construction or improvements of the physical facilities and (ii) purchase of machinery and equipment.

(B) The amount of cash contributed in exchange for corporate stock or partnership interest in the establishment of an exempted business with a grant issued under this Act or previous acts, considered as a small or medium business, according to Subsection (i) of Section 2 of this Act, that is used by the exempted business for: (i) construction or improvements of the physical facilities; and (ii) purchase of machinery and equipment to be devoted exclusively to industrial development.

The amount of cash contributed in exchange for corporate stock or partnership interest of an exempted business that is considered as a small or medium business, according to Subsection (i) of Section 2 of this Act, that is used by the exempted business for: (i) construction or improvements of the physical facilities; and (ii) purchase of machinery and equipment to be devoted exclusively to industrial development in a substantial expansion. In order to qualify as a substantial expansion under this subparagraph, the investment must be equivalent to, at least fifty percent (50%) of the book value of the operational assets of the Exempted Business as of the closing of its accounting books for the year previous to the date of the expansion.

Any other investment that is not used directly and totally for the purposes described in this subsection will be excluded from the definition of eligible investment of this Act.

The term eligible investment will not include an investment made with cash proceeds from a loan that is guaranteed by the exempted business or by its assets.

(3) Operational assets.- Means any land, structure, machinery, equipment, and intellectual property, such as, copyrights, patents, trade names, and licenses. Accounts receivable, cash, goodwill, and inventory expressly excluded from this term.

(4) Corporate stock or partnership interest - the stock of a corporation that is issued in exchange of a cash contribution may be common stock, preferred stock, or preferred stock convertible to common. The cash contribution made in exchange for corporate stock or partnership interests, with rights so restricted that they are not more than an evidence of the debt of the corporation, will not be admitted as an Eligible Investment.

(b) General Rule.-

(1) Subject to the provisions of paragraph (2) of this subsection, any investor may claim a credit for industrial development equal to fifty percent (50%) of his eligible investment made after the approval of this Act, to be taken in two (2) or more installments: the first half of such credit in the year in which the eligible investment is made and the balance of such credit, in subsequent years. Any eligible investment made before the date for filing the income tax return, according to the

provisions of the Puerto Rico Internal Revenue Code, including any extension granted by the Secretary of the Treasury for the filing thereof, shall qualify for the tax credit in this section in the tax year for which the aforementioned tax return is being filed, provided all the requirements of this Section are met. Such industrial development credit may be applied against the investor's tax determined under Subtitle A of the Puerto Rico Internal Revenue Code, including the alternative minimum tax of Section 1017 and the individual's alternative tax of Section 1011(b) of the Puerto Rico Internal Revenue Code. If the investor is an exempted business, it may claim this credit against the tax imposed by Subsection (a) of Section 3 of this Act.

(2) **Maximum amount of credit.**- The maximum amount of credit for industrial investment shall not exceed eight million (8,000,000) dollars per exempted business with a grant issued under this Act.

(3) The Secretary of Treasury shall authorize the investment credits claimed by investors up to a limit of twenty million (20,000,000) dollars per fiscal year. Nevertheless, in order to attend to the best interests of the Commonwealth of Puerto Rico, the Executive Director may request that the Secretary of the Treasury to authorize a higher amount of credits during a fiscal year, or in excess of the limit provided for a particular business.

(c) **Credit Carryover.**- The industrial development credit not used in a tax year may be carried over to subsequent tax years, until fully exhausted.

(d) Any investors interested in requesting an administrative ruling from the Secretary of the Treasury, to generate a credit under subsection (a)(2)(A) of this Section, shall previously obtain a Certification from the Executive Director, by means of a Sworn Statement stating that the investment to be made relates to the acquisition of an exempted business in the process of closing, so that he determines if the investment made, or intended to be made, qualifies for the tax credit. The Secretary of the Treasury may require, as a condition for endorsement or approval that the investor post a bond or another type of guarantee, in favor of the Secretary of the Treasury to respond in the event that the credits are revoked.

(e) **Basis Adjustment and Recapture of the Industrial Investment Credit.**-

(1) The basis of any eligible investment shall be reduced by the amount of industrial investment credit claimed, but may never be reduced to less than zero.

(2) If any exempted business which originates an industrial investment credit under subsection (a)(2)(A) of this Section, ceases its operations as such before the end of a ten (10) year period, beginning on the date of the eligible investment, the investor shall owe, as income tax, an amount equal to the industrial investment credit claimed by such investor, multiplied by a fraction the denominator of which shall be ten (10) and the numerator of which shall be the balance of the ten (10) year period

as required by this subsection. The amount of income tax due shall be paid in two (2) installments, beginning with the first tax year following the date on which the industrial activity ceased.

(f) **Transfer of the Industrial Investment Credit.-**

(1) The credit for industrial investment provided by this Section may be transferred, sold or otherwise disposed of, totally or partially, by an investor to any other person.

(2) The basis of the eligible investment shall be reduced by the value of the industrial investment credit transferred, sold or otherwise disposed of.

(3) The investor that transferred the industrial investment credit, totally or partially, as well as the person acquiring the industrial investment credit, shall notify the Secretary of the transfer through a statement to that effect to be attached to their income tax return for the year in which the transfer of the industrial investment credit takes place. The statement shall include all the information that the Secretary may deem necessary through regulation adopted to that effect.

(4) The money or value of the property received in exchange for the industrial investment credit shall be exempt from taxation under Subtitle A of the Puerto Rico Internal Revenue Code, and from any municipal taxes, up to an amount equal to the amount of the industrial development credit transferred.

(5) The purchasers of industrial investment credits shall be exempt from taxation under Subtitle A of the Puerto Rico Internal Revenue Code or the difference between the amount paid to acquire the credit and the value thereof.

Section 7 - Real and Personal Property Tax

(a) **In General.-**

(1) The personal property of the exempted business with a grant issued under this Act, used in the development, organization, construction, establishment or operation of the activity covered under the grant, shall enjoy ninety (90) percent exemption from municipal and Commonwealth personal property taxes during the exemption period provided by Section 10 of this Act.

(2) The real property of the exempted business with a grant issued under this Act, used in its development, organization, construction, establishment or operation, shall enjoy ninety (90) percent exemption from the municipal and Commonwealth property taxes during the exemption period provided by Section 10 of this Act.

(3) The real property of an exempted business described in Section 2(h)(12) of this Act shall be totally exempt from the payment of property taxes during the first

five (5) years starting on the date of commencement of operations determined pursuant to Section 10 of this Act. Once such period expires, the provisions of the previous paragraph shall apply.

(b) Term.-

The real property of an exempted business with a grant issued under this Act shall be totally exempt during the period authorized by the grant to carry out the construction or establishment of the exempted business and during the first fiscal year of the Government of Puerto Rico in which the exempted business would have been subject to property taxes for having been in operation as of the 1st of January preceding the commencement of such fiscal year had it not been the exemption herein provided. Likewise, the property of such exempted business which is directly related with any expansion of the exempted business shall be totally exempt from property tax during the period authorized by the grant to carry out such expansion. Once the total exemption period established by this paragraph expires, the partial exemption provided in this Section shall commence.

(c) Assessment.-

(1) Taxes on real property shall be assessed, levied, notified and administered pursuant to the provisions of Act 83 of August 30, 1991, as amended, ("Municipal Property Tax Act"). Notwithstanding, an exempted business may choose to avail itself of the self-assessment method provided by paragraph (2) of this subsection.

(2) Optional Self-Assessment Method.-

(i) An exempted business under this Act or previous incentives acts may use the self-assessment method established in this paragraph to determine the classification and the real property tax on property that has not been assessed pursuant to the "Municipal Property Tax Act". In such cases, the exempted business will comply with the procedures established in the "Municipal Property Tax Act", as long as it has complied with the notification requirements established in such act or in the tax exemption grant.

(ii) The self-assessment method provided in this paragraph may be used exclusively for that property which should be properly considered as real property because of the use and location to which it is destined and that is used in the development, organization, construction, establishment or operation of the exempted business. Provided that the method herein established shall not be used to assess land or structures (including the real property permanently adhered to a structure and that exclusively serves such structure, such as lighting equipment).

(iii) The assessment value of the property classified as real property by the exempted business to be assessed under this paragraph, shall be equal to thirty-five percent (35%) of the depreciated book value of the exempted business. Provided that such assessed value will not be less than a percent of cost, calculated based on the useful life of the property, as hereinafter provided:

Useful Life	Cost
2-5 years	25%
6-10 years	17%
11-15 years	15%
16 years or more	10%

(iv) The exempted business shall also enjoy the exemption established in the subsection (a) of this Section on the value assessed pursuant to subparagraph (iii) of this paragraph. Provided that the provisions of the "Municipal Property Tax Act" will apply with respect to the rate, date and methods of payment of this tax as if it was assessed under such Act.

(v) Any exempted business that has chosen to use the self-assessment method established in this paragraph will file a self-assessed real property tax return on or before May 15 of every year, in which it will identify the property to be considered as real property and will determine its obligation to pay real property taxes for the Government's fiscal year according to subparagraph (iii) of this paragraph. Provided that, once an exempted business adopts the assessment method established in this paragraph, it will file and pay on the date of the filing of first tax return, in addition to the tax corresponding to the current fiscal year, the tax corresponding to the four (4) previous fiscal years, or for the number of years that it has operated, whichever is smaller. The exempted business will be able to make the payment corresponding to its tax liability for the four (4) previous fiscal years, or the corresponding number of years, as previously provided, in two (2) installments. The first of such payments will be made when filing the corresponding tax return and the second payment must be made within six (6) months following the filing of the First Return in which it has opted for this method. In ten (10) working days from the time in which the exempted business files the tax return provided in this subparagraph, the Municipal Revenues Collection Center (CRIM) will notify the municipalities concerned of the election by the exempted business to avail itself of the optional self-assessment method.

(vi) Once the property classified and assessed under the optional method established in this paragraph is classified and assessed by the Municipal Revenues Collection Center ("CRIM") pursuant to the "Municipal Property Tax Act", and the revision procedures established in such act are exhausted, the value of the property of the exempted business will be the one established by the CRIM instead of the value determined under the self-assessment method established in this paragraph. In such cases, the exempted business will comply with the procedures established in the Municipal Property Tax Act. Provided that the classification and assessment made by the CRIM pursuant to such act will only have prospective effect for all legal purposes, as a result of which no determination of deficiency shall be made with respect to the method used or the classification of the property as real property for the years in which the optional self-assessment method was used.

- (d) The investments that qualify under Subsection (j) of Section 2 of this Act will be totally exempt from payment of property tax.

Section 8 - Municipal License Tax and Other Municipal Taxes

- (a) Exempted businesses that hold a grant under this Act, shall enjoy a sixty percent (60%) exemption from municipal licenses, municipal excises and other municipal taxes imposed by any municipal ordinance, during the periods established in Subsection (b) of Section 10 of this Act.
- (b) Notwithstanding what is provided in subsection (a) of this Section, the following exempted businesses that hold a grant under this Act shall enjoy the percent of exemption on said municipal licenses, municipal excises and other municipal taxes, hereinafter provided:
- (1) Exempted businesses under this Act that operate in the special industrial development zone constituted by the municipalities of Vieques and Culebra. Shall enjoy ninety percent (90%) exemption.
- (2) Exempted business under this Act that are considered as small or medium sized businesses as established in Subsection (i) of Section 2 of this Act, but only during the period that they are small or medium sized businesses. Shall enjoy a seventy-five percent (75%) exemption. In the case of exempted businesses that are small or medium sized business, and that have operated before requesting a grant under this Act, this paragraph will apply solely to the volume of business in excess of the average volume during the three (3) years previous to the date of the request.

The volume of business not covered by this paragraph shall enjoy a sixty percent (60%) exemption, in agreement with subsection (a) of this Section.

(3) Exempted business described in Paragraph (12) of Subsection (h) of Section 2 of this Act. Shall enjoy one hundred percent (100%) exemption during a period of five (5) years from the date when the exemption begins.

- (c) The taxable portion under subsections (a) and (b) of this Section shall be subject, during the grant's effective term, to the tax rate in force at the time the grant is issued, regardless of any later amendment made to the grant to cover operations of the exempted business in one or several municipalities.
- (d) The exempted business that holds a grant under this Act shall enjoy full exemption of municipal taxes or municipal licenses that apply to the volume of business of said exempted business during the semester of the fiscal year of the Government of Puerto Rico in which the exempted business commences operations in any municipality, pursuant to the "Municipal License Tax Act of 1974", as amended. In addition, the exempted businesses that hold a grant under this Act shall be fully exempt from the municipal taxes or licenses on their volume of business attributable to such municipality for the two (2) semesters of the fiscal year or years of the Government following the semester in which it commenced operations in the municipality.
- (e) Exempted businesses that hold a grant under this Act and their contractors and subcontractors shall be fully exempt from any tax, levy, fee, license, excise, rate or tariff imposed by any municipal ordinance on the construction of works to be used by said exempted business within a municipality, without it being understood that said taxes include the municipal license tax levied on the volume of business of the contractor or subcontractor of the exempted business during the term authorized under the tax exemption grant.
- (f) Income obtained from investments that qualify under Subsection (j) of Section 2 of this Act, shall be totally exempt from municipal licenses, municipal excises and other municipal taxes.
- (g) All exempted businesses under this Act, or previous act, will be able to renounce the benefit of the discount of five percent (5%) for down in agreement with Section 11 of the "Municipal License Tax Act", and to make the total payment of its municipal patent in the date arranged by this Act. Provided that, in the case of the exempted businesses that choose to make the down payment and to renounce the discount, the statute of limitations for the appraisal and collection of the patent imposed under the "Municipal License Tax Act" will be three (3) years from the date in which the Declaration on the Volume of Business is filed, instead of the terms established in Section 19 (a) and (b) of the "Municipal License Tax Act".

- (h) In housing project the municipalities may give a partial or total credit for the municipal construction tax on the total cost of the infrastructure works that fulfill the partially sustainable or the self- sustainable criteria, as defined in this Act.

Section 9 - Commonwealth Excise Tax and Sales and Use Tax

(a) In addition to any other excise or sales and use tax exemption granted under Subtitles B and BB, respectively, of the Puerto Rico Internal Revenue Code, the following articles introduced or acquired directly or indirectly by an exempted businesses holding a grant under this Act will be totally exempt from such taxes, during the exemption period established in Section 10 of this Act.

(1) Any raw material to be used in Puerto Rico for manufacturing or finished products, excluding hydraulic cement, crude oil, partially finished or partially finished derivative products of oil, and any other blend of hydrocarbon. For purposes of this paragraph and the applicable provisions of Subtitles B and BB of the Puerto Rico Internal Revenue Code, the term "raw material" shall include:

(A) Any product in its natural state derived from agriculture or mining.

(B) Any by-product, residual product, or partially processed or finished product; and

(C) Sugar in bulk or in units of fifty (50) pounds or more to be used exclusively in the manufacture of products.

(2) Machinery, equipment and accessories thereof, used exclusively in the manufacturing process, or in the construction, or repair of vessels, within or outside the premises of a manufacturing plant, machinery, trucks or lifts used exclusively and permanently in hauling raw material within the exempted business circuit; machinery, equipment and accessories used to carry out the manufacturing process or those that the exempted business is obligated to acquire by requirement of federal or Commonwealth laws or regulations for the operation of an industrial unit.

The above notwithstanding, the exemption shall not cover machinery, devices, equipment or vehicles used in whole or in part in the administrative or commercial operations of the exempted business, except in those cases in which these are also used in at least ninety percent (90%) in the manufacturing process or in the construction or repair of vessels, in which case they shall be deemed as being used exclusively in said manufacturing process.

(3) All machinery and equipment that must be used by an exempted business, that holds a grant under this Act to comply with environmental, safety and health requirements, shall be fully exempted from the payment of Commonwealth excise taxes, as well as from the sales and use tax.

- (4) The machinery, equipment, parts and accessories used in experimental or reference laboratories.
 - (5) The machinery, equipment, parts and accessories used in the preliminary phase of region exploration geared to the mineralogical development of Puerto Rico, and the dry docks and shipyards for the construction or repair of vessels.
 - (6) Fuel used by the exempted business covered by this Act in the cogeneration of electric power for its own use or for the use of its affiliates.
 - (7) Chemicals used by the exempted business in sewage treatment.
 - (8) Energy efficient equipment, properly certified by the Administration of Energy Issues.
- (b) Exceptions.- The following articles of use and consumption used by the exempted business that holds a grant under this Act, regardless of the area or place where they are located, or their use, shall not be deemed as raw material, machinery or equipment for the purposes of paragraphs (1), (2), and (3) of subsection (a) of this Section:
- (1) all construction materials and prefabricated buildings;
 - (2) all electrical materials and water pipes installed in the buildings;
 - (3) lubricants, grease, waxes and paints not related to the manufacturing process;
 - (4) lamp posts or spotlights installed in parking areas; and
 - (5) treatment plants and electric power substations.

Section 10 - Exemption Periods

- (a) Exemption.-

An exempted business that holds a grant under this Act shall enjoy tax exemption for a fifteen (15) year period.

- (b) Flexible Tax Exemption.-

Exempted businesses that hold a grant under this Act shall have the option of choosing the specific taxable years to be covered under their grants with regard to their industrial development income, as long as they notify the Secretary of Treasury and the Executive Director no later than the due date provided by law to file their income tax returns for said taxable year, including extensions granted for said purpose. Once the exempted business opts for this benefit, its exemption period shall be extended for the number of taxable years it did not enjoy said benefit under the exemption grant.

(c) Provisions That Apply to Tax Exemption on Businesses of Property Devoted to Industrial Development.-

(1) The period during which a property devoted to industrial development belonged to any political subdivision, agency or instrumentality of the Government shall not be deducted from the period referred to in subsection (a) of this Section. Provided that in such cases the property shall be deemed, for purposes of this Act, as if it had not been previously devoted to for industrial development.

(2) When the exempted business that holds a grant under this Act is for property devoted to industrial development, the period to which reference is made in subsection (a) of this Section shall not cover those periods in which the property devoted to industrial development is in the market to be leased to an exempted business, or is vacant, or is leased to a nonexempted business, except as provided below. Said period shall be computed on the basis of the total period during which the property was at the disposal of an exempted business, as long as that the total number of years is not greater than that provided under said subsection (a) of this Section, and the exempted business that qualifies as property devoted to industrial development informs the Secretary of Treasury and the Executive Director, in writing, of the date in which the property is leased to an exempted business for the first time, and the date in which the property is vacated and is again occupied by another exempted business.

In the event that the exemption of the exempt business for property devoted to industrial development expires while it is in use under a lease by a manufacturing exempted business, said exempt business for property devoted to industrial development shall enjoy a fifty percent (50%) exemption on property taxes while the exempted manufacturing business continues to use said property under a lease.

(3) When the exempted business that holds a grant under this Act is one of property devoted to industrial development, the period referred to in subsection (a) of this Section shall continue its normal course, even when the exemption grant of the exempted business using said property, as a result of the termination of its normal period or by revocation of its grant, expires before the exemption period of the property devoted to industrial development, unless, in the case of revocation, it is established that at the time said property was made available to the exempted business, the owners thereof had knowledge of the facts that later caused the grant to be revoked.

(d) Establishment of Operation in Other Municipalities.-

An exempted business that holds a grant under this Act, can establish additional industrial units as part of the operations covered by a valid grant, in the same municipality where the main office is located, or in any other municipality of Puerto Rico, without having to apply for a new grant, as long as it notifies to the

Office of Exemption within thirty (30) days of the commencement of operations of the additional industrial unit. The additional industrial unit will enjoy the exemptions and benefits established by this Act for the remainder of the exemption period of the grant in effect.

(e) Interruption of the Exemption Period.-

In the event that an exempted business which holds a grant under this Act has ceased operations and later wishes to resume the same, the time during which no operations were conducted shall not be discounted from the corresponding exemption period, and the exempted business may enjoy the remaining exemption period while the tax exemption grant is in effect, as long as the Secretary of Development determines that the ceasing of operations was justified and that reopening said exempted business shall be for the best social and economic interests of Puerto Rico.

(f) Fixing the Date of Commencement Operations and the Exemption Periods.-

(1) The exempted business that holds a grant under this Act may select the date of commencement of operations for purposes of Section 3 of this Act by filing a sworn statement before the Exemption Office, with copies to the Secretary of Treasury, stating the unconditional acceptance of the grant approved for the exempted business under this Act. The date of the commencement of operations for purposes of Section 3 of this Act may be the date of the first training or production payroll of the exempted business that holds a grant under this Act, or any date within a period of two (2) years after the date of the first payroll.

(2) The exempted business that holds a grant under this Act may postpone the application of the fixed rate provided in Section 3 of this Act for a period which shall not be greater than two (2) years from the date of commencement of operations fixed under paragraph (1) of subsection (f) of this Section. During the postponement period, said exempted business shall be subject to the applicable tax rate under Subtitle A of the Puerto Rico Internal Revenue Code.

(3) The exemption period provided in Subsection (a) of Section 7 of this Act for the exemption on real and personal property, will begin the first day of the fiscal year of the Government of Puerto Rico following the last fiscal year in which the exempted business was fully exempted, pursuant to the provisions of subsection (b) of Section 7 of this Act. The partial exemption for said fiscal year shall correspond to the tax on the property owned by the exempted business on the 1st of January which precedes the beginning of said fiscal year.

(4) The partial exemption period provided in subsection (d) of Section 8 of this Act for purposes of exemption from municipal license taxes and any other municipal tax, shall commence on the first day of the first semester of the fiscal year of the Government of Puerto Rico following the expiration of the full-exemption period

provided in that subsection. Provided that, in the case of exempted businesses that had been operating in a commercial scale before applying for the benefits of this Act, the date of commencement of operations for the purposes of municipal license taxes shall begin the first day of the semester after the date of filing of the tax exemption application.

(5) In the case of exempted businesses that hold a grant under this Act and which have been operating in a commercial scale before applying for the benefits of this Act, the date of commencement of operations for purposes of the fixed rate provided in Section 3 of this Act shall be the date of filing an application with the Office of Exemption, but the commencement date may be postponed for a term of not more than two (2) years from said date.

(6) The exempted businesses that holds a grant under this Act shall commence operations in a commercial scale within a one (1) year term from the date that the grant is signed, which term may be deferred per request of the business by just cause, but deferments that extend the date of commencement of operations by a term greater than five (5) years from the date of the approval of the grant will not be approved.

Section 11 - Industrial Development Zones

(a) In General.-

The Secretary of Economic Development and Commerce of Puerto Rico, according to the procedure established in subsection (b) of this Section, will classify the different regions or municipalities of Puerto Rico under one of the following industrial development zones:

High Industrial Development Zone

Intermediate Industrial Development Zone

Low Industrial Development Zone

Provided, however, that the Municipalities of Vieques and Culebra will constitute a Special Industrial Development Zone, different from the zones herein established.

(b) Procedure and Criteria.-

(1) From July 1, 2008, the Secretary of Development will make the classification provided for in subsection (a) of this Section by means of an Administrative Order, in consultation with the Executive Director, the President of the Planning Board and the Secretary of the Treasury. This classification will be based on the employment level in the municipality or region and the need of the establishment of industrial operations in the particular area. In addition, he will take into consideration the

nature to the area, the availability of the working labor force, the existing infrastructure and any other factors that affect the economic and social development of the municipality or region to be classified. The Secretary of Development shall include as an exhibit to the Administrative Order provided for in this subsection, a report that details the specific criteria used to make such classifications.

(2) The Secretary of Development shall make a general revision of the classifications made under subsection (a) of this Section every five (5) years, starting on the first classification made under this Section.

(c) Special Designation.-

Notwithstanding the provisions of subsection (b) of this Section, the Secretary of Development may, by means of an Administrative Order and in consultation with the officials mentioned in subsection (b) of this Section, reclassify any municipality or geographic area from one zone to another, prior to the general revision required by paragraph (2) of subsection (b) of this Section, when the factors that justified the inclusion of the municipality or region in the previous zone, have varied substantially. Provided, in addition, that the Administrative Order through which the special classification provided in this subsection is made, must indicate the specific criteria that motivated the change in classification.

(d) Special Rules.-

The reclassification of a municipality or geographic area from one zone to another will not affect the exemption of the exempted businesses already established in such municipality or region. However, a business that has applied for a grant of tax exemption to establish operations in a municipality or particular region, but has not yet established operations, or has obtained it before the date in which such municipality or area has been reclassified from one zone to another, that as a result of the change in designation qualifies for benefits inferior to those it would have under the old classification, will have right to enjoy the exemption benefits in effect before the reclassification if it establishes operations in it within one (1) year starting on the date in which the area was reclassified. For purposes of this Act, the date of the first payroll for training or production will be considered as the date of establishment of the business.

(e) Transitory Provisions.-

Until the Secretary of Development makes the initial classification of the municipalities or regions in the industrial development zones provided for in this Section, those in effect as of the effectiveness date of this Act will apply to the grants of exemption issued under this Act, [as established by the provisions of Act 135 of December 2, 1997, as amended.] Provided, however, that during such transitory period, the municipalities or regions will maintain their present designations as zone of low, intermediate or high industrial development.

Section 12. - Office of Industrial Tax Exemption -

(a) In General -

The Office of Industrial Tax Exemption shall be ascribed to the Department of Economic Development and Commerce. This office shall be directed and administered by a Director, who shall be appointed by the Secretary of Development. The Director shall exercise the powers inherent to his office, shall appoint the necessary personnel to perform their duties and shall comply with the duties and obligations imposed by this Act.

(b) Sworn Statements Required by the Office of Industrial Tax Exemption -

The Office of Exemption may require tax exemption grant applicants to submit those sworn statements needed to establish the required or appropriate facts, in order to determine whether the operations or proposed operations of the applicant qualify under the provisions of this Act.

(c) Hearings -

The Director may hold as many public and/or administrative hearings as he deems necessary to comply with the duties and obligations imposed by this Act. In addition, he may require the applicants for tax exemption grants to present any evidence that may justify the requested tax exemption.

The Director, or any Special Examiner of the Exemption Office designated by the Director, with the approval of the Secretary of Development, may receive the evidence presented in connection with any application for a grant, and shall have the power to summon witnesses and take their statements as to the facts alleged or in any way related to the tax exemption applied for, to administer oaths, to any person testifying before him, and to submit a report to the Secretary of Development regarding the evidence presented, together with his recommendations on the case.

(d) Penalties -

Any person who makes or attempts to make on his own behalf or on behalf of any another person, any false or fraudulent statement regarding any tax exemption application or grant, or any violation of the provisions regarding predecessor or successor exempted businesses, shall be deemed guilty of a third degree felony and if convicted thereof shall be punished according to the penalty provided for such type of felony in the Puerto Rico Penal Code of 2004, as amended.

It is also established that, in these cases, the exemption grant shall be retroactively revoked and the grantee and/or its shareholders shall be responsible for all the taxes that were totally or partially, exonerated under this Act.

(e) Special Account of the Office of Industrial Tax Exemption -

The fees, charges and penalties prescribed in subsection (d) of this Section 12, shall enter into a Special Account created for such purpose in the Department of the Treasury in order to defray the ordinary operating expenses of the Exemption Office. Before using the resources deposited in the Special Account, the Exemption Office shall submit annually a budget of expenses chargeable to the funds of the Special Account for the approval of the Office of Management and Budget of the Government of Puerto Rico. The resources of the Special Account set aside to defray the ordinary operating expenses of the Exemption Office may be complemented with appropriations from the General Fund of Puerto Rico, whenever necessary.

(f) The Exemption Office shall establish the necessary systems to facilitate electronic filing and transmittal of the exemption applications and related documents, in order to expedite the Interagency consideration of exemption applications and the processes, in general.

Section 13. - Proceedings -

(a) Ordinary Proceedings. -

(1) Tax Exemption Applications. -

Any person that has established or intends to establish an eligible business in Puerto Rico may request from the Secretary of Development the benefits of this Act by filing the corresponding duly sworn application with the Office of Exemption.

At the time of filing, the Director shall collect the applicable processing fees, which shall be paid by certified check, postal or bank money order, payable to the Secretary of Treasury.

The Secretary of Development shall establish by regulation the processing fees to be charged. Provided, that such regulation must be revised every three (3) years after its approval.

The fees in effect under Act 135 of December 2, 1997, as amended, will continue in effect until the first regulation under this provision is approved.

(2) Interagency Consideration of the Applications. -

(A) Upon receipt of any application under this Act by the Office of Exemption, the Director shall remit, within a period of five (5) days from the date the application is filed, a copy thereof to the Secretary of Treasury and the Executive Director for this latter to issue an eligibility report regarding the activity to be carried out and on other facts related to the application. When evaluating the application, the Secretary of Treasury shall verify compliance by the stockholders or partners of the applicant business with their tax obligation under the Puerto Rico Internal Revenue Code.

This verification will not be necessary in the case of non-Puerto Rico resident stockholders or public corporations. Noncompliance with such tax obligation shall be basis for the Secretary of Treasury not to endorse the application of the applicant business.

(B) Once the Executive Director submits his Eligibility Report and recommendation, the Director shall remit copy of the draft grant, within five (5) working days after having received all the documentation needed to process the case, to the agencies concerned, including the applicable municipality and the Municipal Revenue Collection Center (CRIM) for their evaluation and recommendation, provided no petition in opposition thereof has been filed. Any unfavorable recommendation to the draft grant shall include the reasons thereof.

The agencies and municipalities consulted by the Director will have thirty (30) days to submit their report or recommendation to the remitted draft of the grant. Should the recommendation of the agency or municipality be favorable, or if the same is not received by the Office of Industrial Tax Exemption within the aforementioned period of thirty (30) days, said draft of grant shall be deemed to have received a favorable recommendation and the Secretary of Development shall take corresponding action with regard to such application.

In the case that the municipality raises any objection regarding the draft of the grant remitted, the Office of Exemption shall proceed to consider such objection, as it deems necessary, whereby the Office of Exemption shall notify the parties and the corresponding agencies for the administrative action or revision of the draft grant deemed pertinent. Once the controversy is elucidated, the Director shall make the decision he deems appropriate and shall submit the case to the Secretary of Development for his final consideration.

(C) In the case of amendments to grants approved under this Act, the period for the concerned agencies and municipalities to submit a report or opinion to the Director shall be twenty (20) days.

(D) Once the reports have been received, or the periods to prepare such reports have expired, the Director shall submit the draft of the grant and his recommendation to the consideration of the Secretary of Development within the following five (5) days.

(E) The Director may rely on the recommendations furnished by those agencies or municipalities that issue reports or opinions and may request them to supplement the same.

(F) The Secretary of Development shall issue a final determination in writing within a period not to exceed five (5) days from the date the draft grant was submitted for his consideration.

(G) The Secretary of Development may delegate on the Director those functions that in his judgment he deems convenient in order to facilitate the administration of this Act, except the function of approving or denying original tax exemption grants, other than exemptions granted under clause (b) and subparagraph (E) of paragraph (1) of subsection (d) of section 2 of this Act.

(b) Renegotiations and Conversions. -

(1) Renegotiation of Grants in Effect. -

(A) Any exempted business covered by a grant issued under this Act or under previous acts, may request that the Secretary of Development consider renegotiating its grant in effect if said exempted business shows that it will increase the average employment it has had during the last three (3) taxable years prior to the date of filing the request, by twenty-five percent (25%) or more; or that it will make a substantial investment in its existing operation to help maintain the economic and labor stability of the industrial unit represents an increase of twenty-five percent (25%) or more in the existing investment in property devoted to industrial development as of the effective date of this Act. If the exempted business shows to the satisfaction of the Secretary of Development that it is unable to comply with the afore mentioned to increase average employment or investment, it shall submit the necessary evidence to the Office of Exemption. The Secretary of Development, prior favorable recommendation of the Secretary of Treasury and the Executive Director, and prior recommendation of the agencies that issue tax exemption reports, may, in his discretion, consider the renegotiation taking into account any other factor or circumstance that reasonably shows that the renegotiation will be in the best social and economic interests of Puerto Rico.

For purposes of this Section, the employment of the aforementioned exempted business shall consist of the number of individuals residing in Puerto Rico who work on a permanent basis in full-time regular shifts in the exempted business rendering services as employees, even if they are not directly in the payroll of the exempted business (such as persons working under personnel leasing contracts, but not including persons such as consultants or independent contractors).

For purposes of this Section, the investment of the exempted business covered by a grant issued under this Act or under previous acts, in its existing operation shall be determined according to the book value of the property devoted to industrial development, computed with the benefit of the allowable depreciation under the straight-line method, taking into account the useful life of said property determined according to Subtitle A of the Puerto

Rico Internal Revenue Code, in lieu of any other accelerated depreciation allowable by law.

Should the Secretary of Development agree to the requested renegotiation after receiving recommendation of the agencies that issue reports on tax exemption, he shall take into account the number of jobs of the exempted business, the place in which it is located, the investment and additional jobs, as well as the remaining period of its grant, the tax benefits already enjoyed and its financial capacity, so that the exempted business may obtain a new grant with tax benefits adjusted under this Act.

The Secretary of Development shall establish the terms and conditions he deems necessary and convenient for the best interests of Puerto Rico, within the limits provided in this Act, and may, in his discretion, prior recommendation of the agencies that issue reports on tax exemption, impose special employment requirements, limit the period and percentage of exemption, limit the taxes to be exempted, levy a fixed tax rate on industrial development income higher than that provided in subsection (a) of Section 3 of this Act, and require and provide any other term or condition needed for the industrial and economic development purposes proposed by this Act.

When the exempted business, interested in renegotiating its grant does not meet the requirements of increase in employment or investment provided for in this subsection, the Secretary of Development may, prior favorable recommendation of the Secretary of Treasury and the Executive Director and the agencies that issue reports on tax exemption, levy a fixed tax rate on industrial development income greater than that levied in the grant of the exempted business.

(B) The Secretary of Development may not grant a fixed tax rate on industrial development income under this subsection that is less than four percent (4%) without the approval of the Secretary of Treasury. Except in the case of businesses described in paragraphs (2) to (6) of subsection (a) of Section 3 of this Act, the fixed rate established in renegotiation under paragraph (1) of subsection (b) of this Section shall be applicable only with respect to annual industrial development income, computed under this Act, excluding income from investments described in subsection (j) of Section 2 of this Act, in excess of the base period income.

For purposes of this subparagraph, "base period income" means the highest amount resulting from comparing the industrial development income for the last taxable year prior to the date of the application for renegotiation, excluding income derived from investments described in subsection (j) of Section 2 of the previously applicable act, with the annual average industrial

development income computed under the act applicable to the grant issued under previous incentives acts, but excluding the income derived from investments described in subsection (j) of Section 2 of such previous incentives acts, for the three (3) taxable years with the highest industrial development income, (excluding income derived from investments described in subsection (j) of Section 2 of such previous acts) of the five (5) taxable years prior to the date of the application for renegotiation under this Section, or shorter applicable period. In the case of exempted businesses that have been in operation for a period of three (3) years or less as of the date of the application for renegotiation, the base period income shall be the annual average industrial development income, excluding income derived from investments described in subsection (j) of Section 2 of such previous incentives acts, earned during such period, determined under the act applicable to the previous grant.

(C) An amount equal to the base period income shall be subject to tax every taxable year under the provisions of the grant issued under the previous act renegotiated under this subparagraph, including, but not limited to the tax on dividends or distributions of profits from industrial development income, and the tax on liquidation applicable under such previous act, for the remainder of the exemption period of the renegotiated grant, provided the industrial development income, excluding income derived from investments described in subsection (j) of Section 2 of this Act, for the taxable year, determined under this Act exceeds the base period income. If the industrial development income, excluding income derived from investments described in subsection (j) of Section 2 of this Act, for any taxable year determined under this Act is less than the base period income, the industrial development income, excluding income from investments described in subsection (j) of Section 2, shall be determined for such year under the provisions of the act under which the previous renegotiated grant was approved, and such amount shall be subject to tax under the provisions of the preceding act, provided that it does not exceed the base period income.

In addition, the industrial development income derived from the investments described in subsection (j) of Section 2 ("2(j) income") shall also be subject to the provisions of the previous act applicable to the grant renegotiated under this subsection, for the remainder of the exemption period of the previous renegotiated grant, up to an amount not exceeding the 2(j) income of the base period, including, but not limited to, the tax on dividends or distributions of profits from industrial development income and the tax on liquidation applicable to the distributions of such 2(j) income.

For purposes of this subparagraph, “base period 2(j) income” means the annual average industrial development income derived from the investments described in subsection (j) of Section 2 of the act applicable to the grant issued under previous acts, for the three (3) taxable years with the highest income from such 2(j) investments, of the five (5) taxable years prior to the date of the renegotiation application under this Section, or the shorter applicable period. In the case of exempted businesses that have been operating for a period of three (3) years or less on the date of the application for renegotiation, the base period 2(j) income shall be the annual average income earned from such investments during such period, computed under the act applicable to the previous grant.

Once the exemption period under the previous grant expires, the fixed rate provided in paragraph (1) subsection (a) of this Section shall apply to all industrial development income earned by the exempted business, excluding income from investments described in subsection (j) of Section 2 of this Act, which shall be totally exempt from tax.

(D) Exempted businesses that renegotiate their grants under the provisions of this subsection and which as of the date of the renegotiation had been operating under Act No. 135 of December 2, 1997, as amended, or previous acts, may distribute the profits accumulated prior to the effective date of the renegotiation at any later date, but such distributions shall be made according to the tax treatment provided in the grant issued under each such act under which such profits were accumulated.

(E) Exempted businesses that renegotiate their grants under this subsection shall be taxed upon total liquidation with respect to their industrial development income according to the tax treatment provided in each of the acts under which such profits were accumulated.

(F) The remaining terms, conditions and benefits contained in this Act which are not in conflict with to the provisions of this subsection shall apply to the exempted businesses covered hereby.

(2) Conversion of Businesses Exempted under Former Acts. -

Any of the following businesses exempted under preceding acts may request to avail itself of the provisions of this Act, subject to the limitations provided below, provided it shows that it is in compliance with all the applicable legal provisions. The exemptions granted in the converted grants shall not be greater than those provided under this Act.

(A) Exempted businesses that have not commenced operations as of the effective date of this Act, may apply to convert their grants for the remainder

of the period originally granted, in which case their exemption shall be adjusted as provided in Sections 3, 7, 8, 9 and 10 of this Act.

(B) Exempted businesses whose grants were granted on or before January 1, 2008 and had not been enjoying exemption before such date, except under such grants, may apply to convert their grants in which case their exemption shall be adjusted as provided in Sections 3, 7, 8, 9 and 10 of this Act. The fixed rate under subsection (a) of Section 3 of this Act shall apply to the industrial development income, as provided in subsection (g) of Section 3 of this Act.

(C) In considering any application for conversion under this subsection, the Secretary of Development, prior recommendation of the agencies that issue reports on tax exemption, shall establish the terms and conditions that he deems necessary and convenient for the best interests of Puerto Rico, within the limits provided in this Act, as well as impose special employment requirements, and/or limit the percentage of exemption, the taxes to be covered under the grant, provide a fixed tax rate on industrial development income higher than that provided in subsection (a) of Section 3 of this Act, but never higher than seven percent (7%), and/or require and provide any other term or condition necessary and convenient in accordance with the purposes of this Act.

(D) Exempted businesses that convert their grants under the provisions of this subsection, and which as of the effective date of the conversion had been operating under Act No.135 of December 2, 1997, as amended, may distribute the profits accumulated before the effective date of the conversion at any later date, according to the tax treatment provided in such act under which such profits were accumulated.

(E) Exempted businesses that avail themselves of the provisions of this subsection shall be taxed upon total liquidation, with respect to their industrial development income, according to the tax treatment provided in each of the acts under which such profits were accumulated.

(F) The benefits of this subsection may be requested within twelve (12) months from the date of approval of this Act and the effectiveness of its provisions may be fixed from the first day of the taxable year in which the same are requested, but never before July 1, 2008, and until the first day of the next taxable year, at the option of the exempted business.

(G) The remaining terms, conditions and benefits contained in this Act which are not in conflict with the provisions of this subsection shall be applicable to the exempted businesses covered hereby.

(c) Refusal of Applications. -

(1) Refusal if not for the benefit of Puerto Rico. - The Secretary of Development may refuse any application when he determines that such concession is not in the best social and economic interests of Puerto Rico, after considering the nature of the physical facilities, the number of jobs, the amount of the payroll and the investment, the location of the project, its environmental impact, or other factors which in his judgment merit such a determination, as well as the recommendations of the agencies that issue reports on tax exemption.

The petitioner, after being notified of the refusal, may request reconsideration from the Secretary of Development within sixty (60) days after receipt of the notice, presenting the facts and arguments regarding its application which he believes to be pertinent, including the offer of any consideration for the benefit of Puerto Rico which he deems will render meritorious his request for reconsideration.

In the event the application is reconsidered, the Secretary of Development may accept any consideration offered for the benefit of Puerto Rico and may require and impose any other term or condition that may be necessary to ensure that such concession is in the best interests of Puerto Rico and the industrial and economic development purposes of this Act.

(2) Refusal for Conflict With the Public Interest or Due to Substitution for Competition With Established Businesses. -

The Secretary of Development may refuse any application when he determines, based on the facts submitted for his consideration and after the applicant has been afforded the opportunity to make a thorough presentation of the issues in dispute, that the application is in conflict with the public interest of Puerto Rico on any of the following grounds:

(A) That the applicant business has not been organized as a bona fide business of a permanent nature or, in view of the moral or financial reputation of the persons that constitute it, the plans and methods for obtaining financing for the distribution and sale of the product to be manufactured or the services to be rendered, the nature or intended use of such a product or services, or any other factor that may indicate that there is a reasonable possibility that granting the exemption will be harmful to the economic and social interests of Puerto Rico, or

(B) That the product to be manufactured by the applicant will substitute or compete at a substantial advantage by reason of the benefits provided in this Act, with products manufactured by industries established in Puerto Rico that are not eligible businesses. Notwithstanding the above, the Secretary of Development may grant the exemption when he determines that the applicant eligible business shall be of substantial benefit to the general economy of Puerto Rico due to anticipated increases in the production to supply markets

outside of Puerto Rico, or to meet a substantial existing demand in Puerto Rico that has not been previously met, and in view of the investment, technology and new job opportunities involved.

If exemption is granted to any industry under the aforementioned circumstances, the Secretary of Development, upon request of an interested party, may also grant exemption to existing industries manufacturing such articles which in his judgment may be substantially harmed due to such substitution or competition.

(d) Transfer of Exempted Business. -

(1) General Rule. - The transfer of a tax exemption grant or of the stock, property or other proprietary interest in an exempted business with a grant issued under this Act must be previously approved by the Director. If the same is carried out without approval, the tax exemption grant shall be annulled as of the date the transfer occurred, except in the cases listed in paragraph (2) of this subsection. Notwithstanding the above, the Secretary of Development may retroactively approve any transfer made without his prior approval when in his judgment the circumstances of the case so justify it, taking into consideration the best interests of Puerto Rico and the economic and industrial development purposes of this Act.

(2) Exceptions. -

The following transfers shall be authorized without the need of prior consent:

(A) The transfer of the assets of a decedent to his estate or the transfer by bequest or inheritance.

(B) The transfer within the provisions of this Act.

(C) The transfer of stock or any partnership interest when such a transfer does not directly or indirectly result in a change in the ownership or control of an exempted business with a grant issued under this Act.

(D) The transfer of stock of a corporation that owns or operates an exempted business with a grant issued under this Act, when the same occurs after the Executive Director has determined that any transfer of the stock of such corporation shall be allowed without his prior approval.

(E) The pledge, mortgage or other guarantee with the purpose of providing security for bona fide debt. Any transfer of control, title or interest pursuant to such contract shall be subject to the provisions of subsection (a) of this Section.

(F) The 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 person other

than the same debtor or former bankrupt, shall be subject to the provisions of subsection (a) of this Section.

(G) The transfer of all the assets of an exempted business with a grant issued under this Act to an affiliated business. For purposes of this subparagraph, affiliated businesses are those whose stockholders or partners hold in common eighty percent (80%) or more of the participations in or voting stock issued and outstanding of such exempted business.

(3) Notice. -

Every transfer included in the exceptions of subsection [sic - should be paragraph (2)] of this Section shall be reported to the Director by the exempted business with a grant issued under this Act, with a copy to the Executive Director and the Secretary of Treasury, within thirty (30) days, except those included under subparagraph (D) of paragraph (2) that do not make the stockholder a holder of ten percent (10%) or more of the outstanding capital of the corporation, and those included under clause (G) of paragraph (2), which shall be reported to the Director by the exempted business, with a copy to the Secretary of Treasury, prior to the date of the transfer.

(e) Procedures for Permissive and Mandatory Revocation. -

(1) Permissive revocation. -

(A) When the grantee fails to comply with any of the obligations imposed by this Act or its regulations, or by the terms of the exemption grant.

(B) When the grantee does not commence or does not complete the construction of the facilities needed for the manufacture of the products it intends to manufacture, or the rendering of the services it intends to render, or fails to commence the production of such products or the rendering of such services within the period fixed for such purposes in the grant.

(C) When the grantee discontinues production on a commercial scale or suspends its operations for more than thirty (30) days without the express authorization of the Secretary of Development. The latter may authorize such suspensions for periods of more than thirty (30) days when the same are motivated by extraordinary circumstances.

(D) When the grantee fails to comply with its tax obligations under the Puerto Rico Internal Revenue Code and other Puerto Rico tax laws.

(2) Mandatory Revocation. -

The Secretary of Development shall revoke any grant issued under this Act if it was obtained by false or fraudulent representations concerning the nature of the eligible business, or the nature or extent of the manufacturing process or of the

production performed or to be performed in Puerto Rico, or the use that has been given or shall be given to property devoted to industrial development, or any other facts or circumstances which wholly or partially motivated the concession of the exemption.

An additional cause for revocation under this paragraph shall be when a person commits or attempts to commit, personally or on behalf of any other person, a violation of the provisions regarding successor businesses or predecessor exempted businesses.

In the event of such a revocation, all the net income determined, previously reported as industrial development income, whether it has been distributed or not, as well as any distribution thereof, shall be subject to the taxes levied under the provisions of the Puerto Rico Internal Revenue Code. In addition, the taxpayer shall be deemed to have filed a false or fraudulent tax return with intent to avoid the payment of taxes, and shall therefore be subject to the penal provisions of the Puerto Rico Internal Revenue Code. The tax due in such case, as well as any other taxes theretofore exempted and unpaid, shall become due and payable from the date when such taxes would have become due and would have been payable had it not been for the exemption grant and shall be levied and collected by the Secretary of Treasury pursuant to the provisions of the Puerto Rico Internal Revenue Code.

(3) Procedure. -

In the cases of revocation of a grant issued under this Act, the grantee shall have the opportunity to appear and be heard before the Director or before any Special Examiner of the Exemption Office appointed for such a purpose, who shall report his conclusions and recommendations to the Secretary of Development, prior recommendation of the agencies that issue reports on tax exemption.

(f) Limitation of Benefits for the Production for Export.

The Secretary of Development, from time to time, and upon consultation with the agencies that issue reports on tax exemption, may designate from eligible products, those whose benefits of this Act shall be limited to the production for export, when he determines the existence of the following factors:

- (1) That the production in Puerto Rico of such products for the local market already satisfies the existing demand and that the capacity of such local production may satisfy the demand foreseen for a period of five (5) years, or
- (2) That there is an active competition in Puerto Rico in the production and marketing of the particular product. Those products which, although similar in name, appearance and use, differ among themselves with regard to their quality, size, price or other factors which affect the market for the product,

and consequently, its demand, shall be deemed as distinct manufactured products which require a separate designation.

When the aforementioned conditions cease to exist, the Secretary of Development may, upon consultation with the agencies that issue reports on tax exemption applications, cease the imposition of said limitation or resume its designation when such conditions reappear.

This limitation shall apply to the tax exemption applications that have not been granted as of the effective date of such limitation

Section 14. - Nature of the Grants

(a) In General. -.

The tax exemption grants under this Act shall be considered a contract between the grantee, its stockholders, partners or owners, and the Government of Puerto Rico, and such contract shall be law between the parties. Said contract shall be interpreted liberally, in accordance with the purpose of this Act to promote the socio-economic development of Puerto Rico. The Secretary of Development shall have discretion to include, on behalf of and in representation of the Government of Puerto Rico, such terms and conditions that are in accordance with the purposes of this Act and that foster job creation through the socio-economic development of Puerto Rico, taking into consideration the nature of the petition or action requested, as well as the related facts and circumstances that may apply.

(b) Obligation to comply with statements in application.

Every exempted business with a grant issued under this Act shall conduct its exempted operations substantially as stated in the application, except when these have been changed through amendments authorized by the Secretary of Development upon request of the grantee, pursuant to the provisions of this Act.

(c) Administrative decisions shall be final

- (1) All decisions and determinations of the Secretary of Development under this Act, with respect to the issuance of the grant and its contents, shall be final and no judicial or administrative appeal or other action shall proceed against them, unless otherwise specifically provided. Provided, that once the grant is issued under this Act, no agency, public instrumentality, political subdivision, public corporation, or municipality, whether autonomous or not, of the Government of Puerto Rico, except for the Secretary of Development or the Governor, shall challenge the legality of such grant or any of its provisions.
- (2) Any grantee adversely affected or injured by any action taken by the Secretary of Development to revoke and/or cancel a tax exemption grant

under paragraph (2) of subsection (e) of Section 13 of this Act, shall be entitled to judicial review thereof by filing an appeal for review with the Court of Appeals of Puerto Rico within thirty (30) days after the final decision or adjudication by the Secretary of Development. Pending judicial review, the Secretary of Development is authorized, when in his judgement justice so requires, to postpone the effective date of any action taken by him, under such conditions as may be required and to the extent needed to prevent irreparable damage. When such postponement is applied for and denied, the reviewing court, including the Supreme Court of Puerto Rico, shall order, through a writ of certiorari, any procedure necessary and appropriate to postpone the effective date of any action taken by the Secretary of Development, to preserve the status or rights of the parties until termination of the review proceedings, after posting bond payable to the Secretary of Treasury in the amount of unpaid taxes to date, plus interest and penalties, plus interest computed for a period of one (1) year at the prevailing legal rate.

- (3) Any decision or judgment of the Court of Appeals of Puerto Rico shall be subject to review by the Supreme Court of Puerto Rico upon application by any of the parties of a writ of certiorari in the manner provided by law.

Section 15. - Periodic reports to the Governor and the Legislature

- (a) In General. - Annually, and regardless of any other report required by law, the Secretary of Development, in consultation with the Secretary of Treasury, the Director of Office of Exemption, the Executive Director, and the Planning Board, shall render a report to the Governor and the Legislature on the economic and fiscal impact of this Act, and Act No. 135 of December 2, 1997, as amended. Such report shall be filed within one hundred eighty (180) days after the close of each fiscal year.
- (b) Required Information. - The Secretary of Development shall request the following information from the Government agencies, municipalities or exempted businesses, as applicable, in order to prepare the report provided in subsection (a) of this Section:
- (1) number of grant exempt applications filed and approved, classified by type of business and industrial activity classification;
 - (2) total investment in machinery and equipment, projected payroll and employment of the exempted business;
 - (3) a description of any additional incentive the exempted business receives, whether from local Government or municipal funds;
 - (4) firm's total assets, liabilities and equity;

- (5) income taxes, withholding on royalty payments, and other taxes paid by exempted businesses, and usage of benefits, such as tax credits and special deductions;
 - (6) municipal taxes paid;
 - (7) comparison of commitments made by exempted businesses with respect to the level of employment and other conditions established by grant; and
 - (8) any other information needed to inform the Governor and the Legislative Assembly the scope and effect of the implementation of this Act.
- (c) Additional Information. - These reports shall include an analysis and evaluation of the issues affecting the industrial development of Puerto Rico, such as: the impact of government processing of permits, licenses, authorizations, grants and any other similar matters; the availability of property for industrial purposes and of skilled workers.
- (d) Report by the Secretary of Treasury. -

Annually, and regardless of any other report required by law, the Secretary of Treasury shall render a report to the Legislature on the tendencies identified with respect to tax payments by exempted businesses, with a comparison to the previous year and a forecast of said conduct for the next three (3) years following that of the report. Said report shall be submitted within one hundred eighty (180) days after the close of each fiscal year.

The Department of Treasury, together with the Industrial Development Company, shall establish questionnaires and regulations needed to achieve the objectives of this Section.

- (e) Cooperation among the agencies. - Government agencies and municipalities shall provide the information required in this Section to the Secretary of Development and the Secretary of Treasury. The Secretary of Development may establish through regulation the forms and processes needed to ensure the exchange of information required by this Section.
- (f) The Secretary of Development, with the assistance of the Industrial Development Company, the Department of Treasury and the Government Development Bank shall establish an electronic database that allows storage and updating of information on the exempted businesses, as well as access to relevant agencies, taking measures to protect the confidentiality of said information. This information shall be used to oversee the fulfillment of conditions imposed on exempted businesses and develop promotional compliance intelligence system that allows the Industrial Development Company to identify and assist in a timely manner exempted businesses in precarious situation, as well as establish promotional strategies.

Section 16 - Successor Business

(a) General Rule. -

A successor business may avail itself of the provisions of this Act, provided that:

- (1) The predecessor exempted business has not ceased operations for more than six (6) consecutive months before filing the application for exemption of the successor business, nor during the exemption period of the successor business, unless this is due to extraordinary circumstances.
- (2) The predecessor exempted business maintains its average annual employment for the three (3) taxable years ending with the close of its taxable year prior to filing the application for exemption of the successor business, or the applicable part of said period while the grant of the successor business granted under the provisions of this Act is in effect, unless such average cannot be maintained due to extraordinary circumstances;
- (3) The employment of the successor business after its first year of operations is greater than twenty-five percent (25%) of the average annual employment of the predecessor business referred to in paragraph (2) above;
- (4) The successor business does not use the physical facilities, including land, buildings, machinery, equipment, inventory, supplies, trademarks, patents, marketing outlets having a value of fifty thousand (50,000) dollars or more and which have previously been used by the exempted predecessor business. The foregoing shall not apply to additions to property devoted to industrial development, even when said additions are physical facilities with a value of fifty thousand (50,000) dollars or more and which are being used or have been used by the main unit or predecessor exempted business. Nevertheless, the Secretary of Development may determine, upon recommendation of the agencies that issue reports on tax exemption, that the use of physical facilities or acquisition of any industrial unit of a predecessor exempted business that is or was in operation will be in the best economic and social interests of Puerto Rico, in view of the nature of said facilities, the number of jobs, total payroll, the investment, the location of the project or other matters that in his/her judgment justify said determination.

(b) Exceptions. -

Notwithstanding the provisions of subsection-section (a) of this Section, its conditions shall be deemed as met, when:

- (1) The successor business assigns to the predecessor exempted business such portion of its annual employment as may be necessary so that the annual employment of the predecessor exempted business is maintained at, or is equivalent to, the annual employment that said predecessor exempted business must maintain. The assignment provided herein shall not be covered by the grant of the successor business, but it shall enjoy the exemption, if any, with respect to the portion so assigned which the predecessor exempted business would have enjoyed thereon, as if such portion had been its own annual production. If the exemption period of the predecessor exempted business has expired, the successor business shall pay the applicable taxes on such portion of its annual production as it may assign to the predecessor exempted business.
- (2) The successor business declares as not covered by its grant such portion of its facilities as may be necessary for property tax purposes so that the investment in physical facilities of the predecessor exempted business is maintained at or is equivalent to its total investment in physical facilities at the close of the taxable year of such predecessor exempted business prior to filing the application for exemption of the successor business, less depreciation thereof and less any decrease in the investment in physical facilities that may have occurred as of the date the provisions of this paragraph are used as a result of an authorization to use them under the provisions of paragraph (4) of subsection (a) of this Section. In those cases in which the tax exemption period of the predecessor exempted business has not expired, the successor business shall enjoy the exemption which the predecessor exempted business would have enjoyed with respect to the portion of its investment in said physical facilities that for purposes of this paragraph it declares as not covered by its exemption, if said facilities had been used in producing its industrial development income;
- (3) The Secretary of Development determines, upon recommendation of the agencies that issue reports on tax exemption, that the operation of the successor business is in the best economic and social interests of Puerto Rico, in view of the nature of the physical facilities, the number of jobs, total payroll, the investment, the location of the project or any other factors that in his/her judgment justify said determination, including the particular exempted business' economic situation, and relieves it fully or partially from complying with the provisions of subsection (a) of this Section, imposing such conditions to the operations as may be convenient and necessary in benefit of the best interests of Puerto Rico.

Section 17 - Special Fund for Economic Development

In General.-

(a) The Secretary of Treasury shall establish a special fund called "Special Fund for Economic Development," into which there shall be deposited, during the first four (4) years of effectiveness of this Act, five percent (5%) of the income tax paid by exempted businesses under this Act or under prior incentives acts with respect to industrial development income, as well as the government revenues from payments of withholding tax on royalty related to exempt operations under this Act or prior incentives acts. Beginning on the fifth year of effectiveness of this Act, seven point five percent (7.5%) of the afore stated items shall be deposited to the fund, instead of the five percent (5%) provided for the first four (4) years. Provided, that beginning on the ninth year of effectiveness of this Act, ten percent (10%) of the afore stated items shall be deposited to the fund, instead of the seven point five percent (7.5%) previously stated.

The money in the Special Fund herein established shall be administered by the Executive Director and shall be used exclusively for the following purposes:

- (1) Special incentives for scientific and technical research and the development of new industrial products and processes, which may be carried out, among others, directly or in agreements with government agencies or public and private universities or with any natural or juridical persons with knowledge and experience; as well as the Industrial Incentives Program administered by the Puerto Rico Industrial Development Company in furtherance of its industrial promotion efforts, including the improvement and development of industrial property.
- (2) The development and establishment of special programs of self-employment or micro-enterprises directed to counteract the problems facing those persons or families that, due to chronic unemployment or any other considerations, are economically straggled or are alienated and whose rehabilitation requires government action beyond the traditional services of the Executive Branch in order to integrate them to the mainstream of modern socioeconomic development.
- (3) Provide special incentives for the establishment in Puerto Rico of industries of strategic importance to the Government, including the investment in venture capital

funds that promote this type of industry, upon authorization by the Economic Development Bank.

- (4) Provide special incentives for the acquisition of exempted businesses by their management.
- (5) Provide special incentives for establishing programs to further and promote investment, technology and training of small and medium business.
- (6) Provide financial support to community businesses, as defined in Subsection (r) of Section 2 of this Act.
- (7) Provide special incentives for the establishment and development of the Strategic Projects in this Act.
- (8) Provide special incentives for research and development directed to bio-science, information technology, bio-medics, and aeronautical engineering.
- (9) Twenty percent (20%) of the moneys deposited in the Special Fund shall be destined to the Science, Technology, and Research Trust created by Act 214 of August 18, 2004, of which no less than forty percent (40%) shall be used for research projects at private non profit institutions of higher learning.
- (10) Support entities or programs dedicated to further the following initiatives:
 - (A) The establishment of networks of public Internet access and other initiatives directed to reduce the digital divide in Puerto Rico.
 - (B) Rendering consulting services in information systems for small or medium businesses.
 - (C) The establishment of incubation centers that provide a support structure and a proper framework for the establishment and development of new companies through specialized resources.

- (D) The establishment of centers and training programs in information and communication systems for unemployed people throughout the Island.
 - (E) The establishment of educational programs at all levels with emphasis on languages, sciences and mathematics.
- (11) Support regional initiatives, as defined in Subsection (v) of Section 2 of this Act, or other entities, for purposes of developing companies, research and development, construction and operation of incubation centers, and other purposes included in this Section.

The Executive Director shall have the necessary and sufficient discretion to use the moneys in the Special Fund, provided said use leads to achievement of the purposes previously stated. Likewise, the Executive Director, in consultation with the Secretary of Development, shall establish through regulation the criteria for disbursing the moneys in the Special Fund for Economic Development established herein. All allocation of money on the Special Fund shall be approved by the Board of Directors of the Puerto Rico Industrial Development Company.

- (b) The Secretary of Treasury may require that returns and forms of income tax, income tax on royalty payments, and any other tax related to this Act, be filed with two payments (checks, or electronic transfers, or others) that separate the portion of the income to the Special Fund described in this Section. and the portion corresponding to the General Fund.

Section 18. Reports required from exempted businesses and their stockholders or partners.

- (a) Every exempted business with a grant issued under this Act shall file an annual income tax return with the Secretary of Treasury, regardless of its gross or net income, separate from any other return that for any other reason it may be required to file with regard to the industrial operations covered by the benefits provided in this Act, and pursuant to the Puerto Rico Internal Revenue Code. The Secretary of Treasury may share with the Puerto Rico Industrial Development Company the information thereby received, as long as the confidentiality of said information is protected.

- (b) Every stockholder or partner of an exempted business with a grant issued under this Act shall file annually with the Department of Treasury an income tax return pursuant to the provisions of the Puerto Rico Internal Revenue Code, provided they have the obligation to do so under said Code.
- (c) The exempted business with a grant issued under this Act shall also be required to keep in Puerto Rico on a separate basis, the accounting for its operations, as well as the necessary records and files, and submit sworn statements and comply with the rules and regulations in force for proper compliance with the purposes of this Act and which the Secretary of the Treasury may prescribe from time to time in connection with levying and collecting all kinds of taxes.
- (d) Every exempted business with a grant issued under this Act shall file annually a report with the Office of Tax Exemption, with a copy to the Secretary of Treasury and the Executive Director, no later than thirty (30) days after the date prescribed by law for filing the corresponding income tax return, including extensions granted to this effect, authenticated by the signature of the President, managing partner, or authorized representative. Such report shall contain a breakdown of data reflecting compliance with the conditions established in the grant for the taxable year immediately preceding the filing date, including, without it being construed as a limitation, the following: the average employment; the products manufactured or services rendered as well as any other information that might be required in the form that may be issued for these purposes or required by Regulation. This report shall be accompanied by such fees as are established by regulations, which shall be paid through a post or bank money order or a certified check for three hundred dollars (\$300.00) payable to the Secretary of Treasury. The information provided in this annual report shall be used for statistical purposes and economic studies, as provided in this Act. Likewise, the Puerto Rico Industrial Development Company shall conduct, at least every two years, a compliance audit of the terms and conditions of the grant issued under this Act.
- (e) All exempted business with a grant issued under this Act shall file the duly completed reports that may be requested by the Commissioner.
- (f) The Director, after being so advised by the corresponding agency, may impose an administrative fine of ten thousand dollars (\$10,000.00) to any exempted business with a grant under this Act that fails to file any of the reports required by the

Secretary of Treasury, the Executive Director, the Director or the Commissioner, pursuant to the provisions of subsections (a) through (e) of this Section, or that files said reports after their due date. The Office of Exemption may initiate a civil action to collect said administrative fines in the Court of First Instance of Puerto Rico, Superior Section, San Juan Part, which shall have exclusive jurisdiction over this proceeding, or may consider the case for the corresponding sanction pursuant to the provisions of subparagraph (A) of paragraph (1), of subsection (c) of Section 12 of this Act. An incomplete report shall be considered as not filed if the corresponding agency notifies the exempted business of any omission in the required report and said exempted business does not furnish the missing information within fifteen (15) days of having been notified thereof, or fails to reasonably justify its omission.

Section 19 - Regulations Under this Act

The Secretary of Development shall draft, in consultation with the Secretary of Treasury and the Executive Director, such regulations that may be needed to implement the provisions and purposes of this Act. The Secretary of Treasury shall approve regulations, after consulting with the Secretary of Development and the Executive Director, dealing with the concession and transfer or sale of tax credits under Sections 5 and 6 of this Act. Said regulations shall also be subject to the provisions of Act No. 170 of August 12, 1988, as amended, known as the "Uniform Administrative Procedures Act of Puerto Rico." The regulations under Act No. 135 of December 2, 1998 shall continue in effect until new regulations are approved, except when they are inapplicable or inconsistent with the provision of said Act. The lack of any regulation alluded in this Act shall not prevent its application. Any regulation required or allowed under this Act shall be submitted to the Secretaries of the Puerto Rico House of Representatives and Senate for their approval. Both Bodies shall consider such regulation with thirty (30) days from receipt thereof. In the case both Bodies do not issue a determination within the time period provided, the Regulation shall be considered approved.

Section 20 - Grants under Preceding Laws.

No applications for exemption under Act No. 135 of December 2, 1997, as amended, shall be received after the effective date of this Act. However, grants approved thereunder or under similar previous acts may be amended pursuant to their respective provisions. Applications for new grants filed under said act which have not been approved before the effective date of this Act may, at the petitioner's election be processed under this Act.

Section 21 - Applicability of the Puerto Rico Internal Revenue Code.-

The Puerto Rico Internal Revenue Code shall apply to this Act in a supplemental manner to the extent that its provisions are not in conflict with the provisions of this Act.

Article 2.- Section 1232(f)(2) of Act No. 120 of October 31, 1994, as amended, known as the Puerto Rico Internal Revenue Code is amended so that it reads as follows:

“Section 1232.- Tax on dividend or profit distribution equivalent amount

(a) ...

(f) Limitation.-

(1) ...

(2) Industrial development income [as defined in Act 135 of December 2, 1997], industrial development income as defined in Section 2(a) of the Economic Incentives for the Development of Puerto Rico Act, the tourism development exempt income, pursuant to the provisions of the “Puerto Rico Tourism Development Act of 1993” and income derived by the International Banking Entities, organized under the provisions of Act No. 52 of August 11, 1989, “International Banking Center Regulatory Act,” shall not be subject to the provisions of this Section.”

Article 3.- Subparagraph (S) and subparagraph (T) are added to Section 1022(b)(4) of the Puerto Rico Internal Revenue Code of 1994, as amended, so that it reads as follows:

“Section 1022.- Gross Income

(a) ...

(b) ...

(1) ...

(4) ...

(A) ...

(B) ...

...

(S) Loans to Small and Medium Businesses.- interest on loans of up to two hundred fifty thousand dollars (\$250,000) in the aggregate per exempted business considered small or medium businesses as defined in the “Economic Incentives for the Development of Puerto Rico Act”, for their establishment or expansion, provided the loan complies with the requirements established in the act known as “Community Reinvestment Act of 1977”, as amended, "Pub. Law 95-128, 91 Stat. 1147", and the requirements that the Commissioner of Financial Institutions establishes by regulation.

(T) Loans for the Capitalization of Small and Medium Businesses.- interest on loans up to two hundred fifty thousand dollars (\$250,000) in the aggregate per exempted business issued to shareholders of exempted businesses to be used in the initial capitalization or the subsequent capitalization of exempted businesses that are considered small or medium businesses, as defined in Section 2(I) of the Economic Incentives for the Development of Puerto Rico Act.

...”

Article 4.- Energy Affairs Administration

Section 1.- Creation of the Energy Affairs Administration

(a) The Energy Affairs Administration shall be created as part of the Puerto Rico Department of Economic Development and Commerce.

(b) The Secretary of Economic Development and Commerce of Puerto Rico shall have the following authority:

(1) Appoint the Executive Director of the Energy Affairs Administration, with the consent of the Governor, and recommend to the Governor the compensation that said officer shall receive.

(2) Authorize increases in the electric energy generation capacity of Puerto Rico in excess of two (2) megawatts from non-renewable sources, with the public policy on energy as reference.

(3) Recommend, develop, and implement Puerto Rico's public policy on energy.

(c) A Committee is created composed by the Secretary of Natural and Environmental Resources, the Administrator of Energy Affairs, the Administrator of Natural and Environmental Resources, the Executive Director of the Solid Waste Authority, and the Secretary of Economic Development, or their authorized representatives to define a new plan for the reorganization and transfer of all the powers, duties, and functions of the Energy Affairs Administration. This Committee shall submit a report, ninety (90) days after the approval of this Act to both Legislative Bodies. This reorganization shall consider:

(1) The transfer of the Energy Affairs Administration to the Department of Economic Development, without limitation, duties, functions, powers, positions, property, equipment, files and documents, available funds and remainders of any origin, contracts, commitments, exemptions, and privileges originating under Act No. 128 of June 29, 1977, as amended. This transfer shall be effective no later than September 1, 2008.

(2) Adjusting the operational structure of the Department of Natural and Environmental Resources, the Administration of Natural and Environmental Resources, and the Solid Waste Authority, exclusively for purposes of activities the necessary changes to transfer the functions of the Energy Affairs Administration to the Department of Economic Development.

(d) No later than September 1, 2008, a transfer shall be made of all functions of the Energy Affairs Administration of the Department of Natural and Environmental Resources, created under the Reorganization Plan No. 1 of December 9, 1993, to be part of the Energy Affairs Administration

hereby created, along with its funds and assignments. Said transfer includes, without this being understood as a limitation, the following:

(1) All of its powers, duties, functions, positions, properties, equipment, files and documents, available funds and remainders of any origin; contracts, obligations, exemptions, and privileges originated under Act No. 128 of June 29, 1977, as amended.

(2) Any regulation that governs the operation of the Puerto Rico Office of Energy, in effect when the transfer authorized under this Act becomes effective. These shall continue in effect until they are amended or revoked by the corresponding administrative authority.

(3) Personnel of the Energy Affairs Administration that upon approval of this Act occupied regular positions with permanent functions of Career Service will be transferred with regular career status. Appointed employees that on said date had a right to be reinstated, in harmony with the applicable provisions of law, shall be transferred with said appointed status and shall remain in their positions with that status until the appointing authority reinstates them to career status. Temporary employees that on said date had a right to permanency, as provided in Act No. 56 of August 16, 1989, as amended, shall continue with the corresponding procedures. Similarly, any collective agreement in effect shall prevail until its expiration.

(e) In addition to the functions transferred by the Energy Affairs Administration of the Department of Natural and Environmental Resources, the Energy Affairs Administration shall have the following functions:

(1) To implement the final report to be filed to the Wheeling Committee created under subsection (e) of this Section, establishing the mechanism for energy wheeling in Puerto Rico provided in Article 4 of this Act and any other initiative that fosters reduction in energy costs and maximizes energy efficiency.

(2) To determine, approve, and establish the rates that the exempted businesses described in Section 2(d)(1)(H) of this Act shall pay the Electric Power Authority to purchase energy; should it not have been agreed to between the parties.

(3) To establish and approve regulations to perform its functions.

(4) To determine, approve, and establish the rates the Electric Power Authority shall pay the exempted businesses described in Section (2)(d)(1)(H) to purchase energy on a commercial scale; should it not have been agreed to between the parties.

(5) To impose fees for the filing of applications for the purchase of energy from plants of up to one thousand dollars (\$1,000) per megawatt hour capacity.

(f) The Wheeling Committee ascribed to the Energy Affairs Administration is created. The Committee shall be composed of seven (7) members, including the following: one (1) representative of the Puerto Rico Department of Economic Development and Commerce, one (1) representative from the Department of Consumer Affairs, one (1) representative from the Department of Treasury, one (1) representative from the Electric Power Authority, one (1) representative from the Energy Affairs Administration, and two (2) members from the private sector to be appointed by the Governor. The Governor shall appoint the president of the hereby established Committee from within the members of the public sector.

The Executive Director of the Energy Affairs Administration may delegate the Committee through regulation any of the functions provided in subsection (e) of this Section.

Section 2.- Wheeling of Energy

(a) The public policy of the Government of Puerto Rico shall be to establish aggressive strategies to achieve efficiency in electric power generation, transmission and distribution to guarantee its availability and supply at a competitive cost.

(b) The Electric Power Authority shall identify and implement within a non-extendable term, ending on January 2, 2010, a system that allows the exempted businesses described in Section 2(d)(1)(H) of the Economic Incentives for the Development of Puerto Rico Act, or analogous provisions in previous incentives acts, to contract the sale of electric power to other entities by means of energy wheeling.

(c) Upon establishing the wheeling service provided in this Section, the Electric Power Authority shall consider the following matters, among others:

- (1) The condition of the transmission and distribution networks, the loss of power related to this phase of the operation and its cost. The Electric Power Authority shall develop a plan (or review the plan already developed, if any), on or before May 1, 2009, to strengthen such networks and minimize said losses. The best practices of other jurisdictions that have implemented this mechanism and the convenience of applying them in Puerto Rico shall be considered.
- (2) The criteria to be considered when determining the fees to be collected for the transmission and distribution service, so that costs premainained at a reasonable level that allows the mechanism's feasibility, that promotes energy generation and competitiveness of Puerto Rico with respect to cost and availability of this service, protecting the best interests of the people of Puerto Rico, including the distance between energy producer and consumer.
- (3) The reasonable conditions that shall be established to guarantee the protection and the adequate and efficient maintenance of the transmission and distribution infrastructure.
- (4) In case the Electric Power Authority cannot reach an agreement with an energy producer about costs, terms, or other covenants related to energy wheeling services within sixty (60) calendar days from filing a request, the Executive Director of the Energy Affairs Administration shall appoint an arbitrator to decide over the controversy among the parties. The arbitrator in the process provided herein shall issue a determination according to law, within sixty (60) days from the beginning of the arbitration process. Said term may be extended for an additional thirty (30) days if the parties agree. Arbitration costs shall be paid in equal portions by the parties.

Section 3.- Purchase of Energy

- (a) Exempted businesses with a grant issued under this Act, that establish a system of electric transmission and distribution and of electricity net metering with the Electric Power Authority by installing an electric solar equipment, windmills, or any other equipment able to generate electric power from renewable sources of energy in compliance with the net metering program under Act No. 114 of 2007, and applicable federal regulations, shall resolve any controversy as provided herein.
- (b) Should a controversy arises between the producer and the purchaser of energy, over costs, terms, or other conditions related to purchasing energy by the Electric Power Authority from commercial scale energy producers that are exempted businesses, the Executive Director of the

Energy Affairs Administration shall appoint an arbitrator within sixty (60) calendar days from filing a request to decide the controversy between the parties. The arbitrator shall issue a determination within sixty (60) days from the beginning of the arbitration process. Said term may be extended up to an additional thirty (30) days if the parties agree. Arbitration costs shall be paid by the parties in equal proportions.

Article 5.- Separability and Rules for Interpretation in Case of Other Conflicting Acts.-

If any Section, subsection, paragraph, subparagraph, clause, or subclause of this Act is declared unconstitutional by a court of competent jurisdiction, the judgment to that effect shall not affect, harm or invalidate the remainder of this Act, its effects being limited to the section, subsection, paragraph, subparagraph, clause or subclause of this Act so declared unconstitutional.

Article 6.- Effectiveness

This Act will shall take effect on July 1, 2008.

