

(H. B. 4723)

(No. 400)

(Approved September 22, 2004)

AN ACT

To amend Act No. 121* of October 31, 1994, as amended, known as the “Puerto Rico Internal Revenue Code of 1994,” to incorporate the tax exemptions allowed in the International Insurers and Reinsurers Act of Puerto Rico, which are necessary to promote the development of Puerto Rico as an International Insurance Center, and for other purposes.

STATEMENT OF MOTIVES

Through this legislation, the Legislature proposes several amendments to the Puerto Rico Internal Revenue Code of 1994, with the purpose of compiling the tax incentives provided in the International Insurers and Reinsurers Act of Puerto Rico in said Code. The International Insurers and Reinsurers Act of Puerto Rico provides the necessary legal structure to establish and promote Puerto Rico as an International Insurance Center to strategically place our island in the global insurance industry.

The insurance industry has become an increasingly important component in the global financial services sector, which has promoted the development of International Insurance Centers. Countries such as the Bermudas, Barbados, and the Cayman Islands have gained prominence as important International Insurance Centers by offering insurers a favorable tax system, experienced service infrastructures, and a regulatory framework that facilitates a free market.

On the other hand, Puerto Rico has more attractive and ideal features to offer these international markets. Outstanding among said features are an experienced service infrastructure, a highly developed and predominantly bilingual financial services industry, a reliable and qualified regulatory framework, a modern communications infrastructure, access to the monetary system of the United States, and a privileged geographical location.

Moreover, Puerto Rico has a solid and experienced insurance industry that shall be able to converge with the international insurance market and provide services thereto. In the last few years, the Puerto Rico insurance industry has been undergoing an accelerated growth, having reached a total amount of subscribed insurance premiums of more than five billion (5,000,000,000) dollars by 2002. This represents approximately three times the volume of subscribed premiums for 1990, and an increase of thirty (30) percent compared to 1998. The Puerto Rico insurance industry generates approximately twelve thousand (12,000) direct employment positions with a payroll of three hundred forty million (340) dollars and an average annual salary of twenty-nine thousand (29,000) dollars. This growth has positioned Puerto Rico as the fourth largest insurance market in Latin America, surpassed only by Brazil, Mexico, and Argentina.

Notwithstanding these attributes and the efforts of previous legislatures, Puerto Rico has not been able to project itself as an alternative for international insurance markets. To successfully enable the establishment of these markets in Puerto Rico, it is necessary to enact vanguard laws that take into account the needs of modern businesses and fulfill the expectations of international markets within a framework of trust and prestige.

*TRANSLATOR'S NOTE: Should read Act No. 120

The International Insurers and Reinsurers Act of Puerto Rico proposes the adoption of Chapter 61 of the Insurance Code of Puerto Rico, Act No. 77 of June 19, 1957. The proposed new Chapter 61 establishes the International Insurer, as the entity authorized to underwrite insurance to cover risks outside Puerto Rico and to underwrite reinsurance to cover risks both, outside and within Puerto Rico. Furthermore, said Chapter provides, among other things, organizational and authorization requirements, minimum capital requirements and the tax incentives to be received by these international insurers.

The tax incentives allowed in the International Insurers and Reinsurers Act of Puerto Rico include, among others, the exemption on the income derived by the International Insurers and by some qualified holding companies of an international insurer, the income tax exemption on the dividends and other distributions of income made by them and the exemption on the payment of municipal license taxes, and on personal and real property.

Said law also exempts International Insurers and some qualified International Insurer Holding Companies from withholding at the source of income the taxes on some of the dividends and income distribution payments made to third parties and filing an income tax return at the Department of the Treasury of Puerto Rico.

The approval and implementation of the International Insurers and Reinsurers Act of Puerto Rico shall help in the creation of direct and indirect employment positions in the financial services area. The employment thus generated shall be specialized and highly compensated. Likewise, the establishment in Puerto Rico of these international entities shall create new reinsurance facilities, particularly property insurance for catastrophic risks,

and shall have a positive impact on the financial industry in general, mainly due to increased liquidity of the capital markets and the demand for financial services that these international entities would generate. Insofar as Puerto Rico gradually establishes itself as a leading jurisdiction in the international insurance market, the number of entities that shall establish operations on the island shall increase, and therefore, the number of direct and indirect employment positions generated shall also increase.

This Legislature considers that the International Insurers and Reinsurers Act of Puerto Rico, together with this bill, shall be extremely beneficial, since they shall achieve a substantial extension and growth of the Puerto Rico insurance industry in the economy of our Island and in the international markets.

BE IT ENACTED BY THE LEGISLATURE OF PUERTO RICO:

Section 1.- Section 1022 of Act No. 120 of October 31, 1994, as amended, known as the “Puerto Rico Internal Revenue Code of 1994,” is hereby amended to add clauses (45), (46) and (47) to subsection (b), to read as follows:

“Section 1022.- Gross Income

(a) General Definition ...

(b) Exclusions from Gross Income...

(1) ...

(2) ...

...

(53) Income derived by International Insurers or by International Insurer Holding Companies which are in compliance with Section 61.040 of the Insurance Code of

Puerto Rico, as well as income derived from the liquidation and/or dissolution of the operations in Puerto Rico by International Insurers or by International Insurer Holding Companies which are in compliance with referred Section 61.040.

- (54) Distributions of dividends and distributions of benefits received by a corporation or partnership that are International Insurers or International Insurer Holding Companies which are in compliance with Section 61.040 of the Insurance Code of Puerto Rico.
- (55) Income derived from the distributions in a total or partial liquidation of International Insurers or International Insurer Holding Companies which are in compliance with Section 61.040 of the Insurance Code of Puerto Rico.”

Section 2.- Section 1052 of Act No. 120 of October 31, 1994, as amended, known as the “Puerto Rico Internal Revenue Code of 1994,” is hereby amended to read as follows:

“Section 1052.- Corporations and Partnerships Returns” - “Every corporation or partnership subject to taxation under this Subtitle shall file a return stating specifically the items of its gross income and the deductions and credits allowed by this Subtitle and such other information for the purpose of carrying out the provisions of this Subtitle as the Secretary may by regulations prescribe. The return shall be sworn to by the president, vice-president or other principal officer and by the treasurer or assistant treasurer, in the case of a corporation, or by a managing partner in the case of a partnership. In cases where receivers, trustees in bankruptcy, or assignees are

operating the property or corporation or partnership business, such receivers, trustees, or assignees shall file returns for such corporations or partnerships in the same manner and form as corporations or partnerships are required to file returns. Any tax due on the basis of such returns filed by receivers, trustees, or assignees shall be collected in the same manner as if collected from the corporations or partnerships of whose business or property they have custody and control. The provisions under this subsection shall not apply to any International Insurers or to any International Insurer Holding Companies which are in compliance with Section 61.040 of the Insurance Code of Puerto Rico. However, International Insurer Holding Companies which are in compliance with Section 61.040 of the Insurance Code of Puerto Rico shall submit the certification required pursuant to Section 61.040(6) of the Insurance Code of Puerto Rico to the Secretary of the Treasury.”

Section 3.- Section 1054 of Act No. 120 of October 31, 1994, as amended, known as the Puerto Rico Internal Revenue Code of 1994, is hereby amended to add clause (4) to subsection (e) to read as follows:

“Section 1054.- Records and Special Returns

- (a) By Taxpayer
- (b) ...
- (c) ...
- (d) ...
- (e) Individual Corporate Returns”
 - (1) General Rule
 - (2) ...
 - (3) ...

- (4) The provisions in this subsection (e) shall not apply to International Insurers or International Insurer Holding Companies which are in compliance with Section 61.040 of the Insurance Code of Puerto Rico. However, International Insurer Holding Companies which are in compliance with Section 61.040 of the Insurance Code of Puerto Rico shall submit to the Secretary of the Treasury the certification required pursuant to Section 61.040(6) of the Insurance Code of Puerto Rico.”

Section 4.- Clause (2) of subsection (p) and clause (3) of subsection (q) of Section 1112 of Act No. 120 of October 31, 1994, as amended, known as the Puerto Rico Internal Revenue Code of 1994, are hereby amended to read as follows:

“Section 1112.- Recognition of Gain or Loss.

- p) Nonrecognition of gain or loss on distribution (not in complete liquidation) of property

(2) Distribution of Appreciated Property

The provisions of this clause shall not apply to a distribution of property by: (i) a corporation that is a party to a reorganization in pursuance of a reorganization plan, (ii) a corporation that has an election in effect under Section 1342 or 1391 for the taxable year of the distribution, or (iii) any International Insurers or International Insurer Holding Company which are in compliance with Section 61.040 of the Insurance Code of Puerto Rico.

(q) Gain or loss recognized on property distributed in complete liquidation of a corporation

(3) Exception. - No gain or loss shall be recognized to a corporation that: (i) is party to a reorganization on the distribution of property to its shareholders pursuant to a plan of reorganization or (ii) to a corporation that has an election in effect under Section 1342 or 1391 for the taxable year of the distribution, or (iii) any International Insurers or International Insurer Holding Companies which are in compliance with Section 61.040 of the Insurance Code of Puerto Rico.”

Section 5.- Subsection (a) of Section 1147 of Act No. 120 of October 31, 1994, as amended, known as the “Puerto Rico Internal Revenue Code of 1994,” is hereby amended to read as follows:

“Section 1147.- Withholding of Tax at the Source of Income of Nonresident Individuals

(a) Obligation to Withhold.- All persons, in whatever capacity they may hold... ..The provisions in this subsection shall not apply to dividends or shares in the benefits of partnerships received from International Banking Entities organized under the provisions of Act No. 52 of August 11, 1989, known as the “International Banking Center Regulatory Act,” nor to the interest (including the origination fee discount, letters of credit and other financial guarantees), dividends, shares in the benefits of a partnership, distributions in a total or partial liquidation or other income items similar to these received

from International Insurers or from International Insurer Holding Companies which are in compliance with Section 61.040 of the Insurance Code of Puerto Rico.”

Section 6.- Subsection (a) of Section 1149 of Act No. 120 of October 31, 1994, as amended, known as the “Puerto Rico Internal Revenue Code of 1994,” is hereby amended to read as follows:

“Section 1149.- Withholding at the Source of Income Tax Attributable to the Distributive Share of a Nonresident Alien Individual Partner of a Special Partnership or Stockholder of a Corporation of Individuals.

- (a) **Obligation to Withhold.-** The partner or stockholder to whom the administration of the special partnership or of the corporation of individuals has been delegated, or any other persons to whom the obligation to deliver to the partners or stockholders the report described in clause (2) of Section 1054(c) has been delegated, must deduct and withhold an amount equal to twenty-nine (29) percent of the distributable share of a partner in the income of the special partnership, or an amount equal to thirty-three (33) percent of the distributable share of a stockholder in the income of the corporation of individuals, of a partner or of a stockholder who is a foreign individual, an estate or a nonresident trust. The distributable share in the income of the partnership shall be understood as distributed pursuant to the provisions in Sections 1346 or 1393(j), as may be applicable. The provisions in this subsection shall not apply to the share attributable to a nonresident stockholder engaged in industry

or business in Puerto Rico of International Insurers or of International Insurer Holding Companies which are in compliance with Section 61.040 of the Insurance Code of Puerto Rico.”

Section 7.- Subsection (a) of Section 1150 of Act No. 120 of October 31, 1994, as amended, known as the “Puerto Rico Internal Revenue Code of 1994,” is hereby amended to read as follows:

“Section 1150.- Withholding of Tax at the Source on Foreign Corporations and Partnerships not Engaged in Trade or Business in Puerto Rico.

- (a) **Obligation to Withhold.-** In the case of foreign corporations and partnerships subject to taxation under this Subtitle not engaged in industry or business in Puerto Rico, there shall be deducted and withheld at the source, in the same manner and on the same items of income that are provided for in Sections 1147 (including its subsection (g)) and 1149, a tax equal to twenty-nine (29) percent of said income, except that in the case of income from dividends or profits of partnerships, the deduction and withholding shall be made in an amount equal to ten (10) percent thereof. In the case of dividends referred to in Section 1231(a)(2)(D), the withholding shall be of seven (7) percent. Dividends received from industrial development income that arise from interest on obligations of the Commonwealth of Puerto Rico or any of its instrumentalities or political subdivisions, on mortgages insured by the Puerto Rico Housing Finance Agency and Bank acquired after March

31, 1977, and on loans or other assets with mortgage security granted by any pension or retirement system of a general nature established by the Legislature of Puerto Rico, the municipalities, agencies, instrumentalities and public corporations of the Commonwealth of Puerto Rico that were acquired after March 31, 1977, as well as dividends or benefits of partnerships received from international banking entities organized under the provisions of Act No. 52 of August 11, 1989, known as the International Banking Center Regulatory Act, and the interest (including the origination fee discount, letters of credit and other financial guarantees), dividends, shares in the benefits of a partnership, distributions in a total or partial liquidation or other income items similar to these received from International Insurers or from International Insurer Holding Companies which are in compliance with Section 61.040 of the Insurance Code of Puerto Rico shall not be subject to withholding.”

Section 8.- Subsection (a) of Section 1221 of Act No. 120 of October 31, 1994, as amended, known as the “Puerto Rico Internal Revenue Code of 1994,” is hereby amended to add subsection (a)(1)(B), to read as follows:

“Section 1221.- Tax on nonresident alien individuals

(a) Income Not Related to Trade or Business in Puerto Rico

(1) General Rule

(A) Imposition of Tax.- There shall be levied, collected and paid for each taxable year, in lieu of the tax imposed by Section 1011.

- (B) The provisions of this subsection shall not apply to the interest (including the origination fee discount, letters of credit and other financial guarantees), dividends, benefits of a partnership, or other income items similar to these received from International Insurers or from International Insurer Holding Companies which are in compliance with Section 61.040 of the Insurance Code of Puerto Rico.”

Section 9.- Subsection (a) of Section 1231 of Act No. 120 of October 31, 1994, as amended, known as the “Puerto Rico Internal Revenue Code of 1994,” is hereby amended to add subsection (a)(4), to read as follows:

“Section 1231.- Tax on Foreign Corporations and Partnerships

(a) Tax on Foreign Corporations and Partnerships on Income not Related to an Industry or Business Within Puerto Rico

- (1) General Rule
- (2) ...
- (3) ...
- (4) The provisions of clause (1) of this Section shall not apply to the interest, (including the origination fee discount, letters of credit and other financial guarantees), dividends, benefits of a partnership, or other income items similar to those received from International Insurers or from International Insurer Holding Companies which are in compliance with Section 61.040 of the Insurance Code of Puerto Rico.”

Section 10.- Subsection (f) of Section 1232 of Act No. 120 of October 31, 1994, as amended, known as the “Puerto Rico Internal Revenue Code of 1994,” is hereby amended to add clause (4) to subsection (f) to read as follows:

“Section 1232.- Tax or Amount Equivalent to Dividend or Distribution of Benefit

(f) Limitation.

- (1) The provisions of this Section 1232 shall not apply
- (2) ...
- (3) ...
- (4) The provisions in this Section shall not apply to income derived by an International Insurer, as defined in Section 61.020(4) of the Insurance Code of Puerto Rico.”

Section 11.- Subchapter G of Chapter 3 of Act No. 120 of October 31, 1994, as amended, known as the “Puerto Rico Internal Revenue Code of 1994,” is hereby amended to add Section 1212 to read as follows:

“Section 1212.- Exceptions

The provisions in this Subchapter G shall not apply to International Insurers as defined in Section 61.020(4) of the Insurance Code of Puerto Rico.”

Section 12.- Severability of the Provisions

The provisions in this Act are independent and severable. Therefore, if any of the provisions were to be found unconstitutional by a court with jurisdiction and competence, the remaining provisions thereof shall not be affected and the law thus modified by the decision of said court shall continue to be in full force and effect.

Section 13.- Effectiveness

This Act shall take effect immediately after its approval for the sole purpose that the Secretary of the Treasury, together with the Insurance Commissioner of Puerto Rico, adopt the necessary regulations for its implementation. For any other purpose, this Act shall take effect one hundred eighty (180) days after its approval.

CERTIFICATION

I hereby certify to the Secretary of State that the following Act No. 400 (H.B. 4723) of the 7th Session of the 14th Legislature of Puerto Rico:

AN ACT to amend Act No. 121* of October 31, 1994, as amended, known as the “Puerto Rico Internal Revenue Code of 1994,” to incorporate the tax exemptions allowed in the International Insurers and Reinsurers Act of Puerto Rico, which are necessary to promote the development of Puerto Rico as an International Insurance Center, and for other purposes,

has been translated from Spanish to English and that the English version is correct.

In San Juan, Puerto Rico, today 19th of October of 2006.

Francisco J. Domenech
Director

*TRANSLATOR’S NOTE: Should read Act No. 120