

New Benefits and Tax Credits for the Development of Residential Projects in Urban Centers

ATTORNEYS

- Isis Carballo-Irigoyen
- Yamary I. González-Berríos
- Rubén Muñiz-Bonilla
- Lillian Toro-Mojica
- Mariana M. Contreras-Gómez
- Leyla González-Ibarría
- Xenia Vélez

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An McV Tax Alert

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Act 182, enacted on August 27, 2024 (“Act 182”), amends the Puerto Rico Incentives Code (the “Code”) to include the development of a “Project in an Urban Center” as a new eligible activity qualifying for tax benefits and credits. The activity consists of the development of real estate for residential use, either for sale or lease, located in an Urban Center of a Municipality of Puerto Rico, if the following requirements are met:

1. The eligible investment in the Urban Center is at least \$1,000,000 (excluding the acquisition cost or fair market value of the real property); or the real property is in a “State of Abandonment,” which generally is defined to include any structure that is an unoccupied, abandoned or unused lot inadequate for use or living because it needs repairs, has structural defects, or is a health or security hazard to the public; or is declared as a “Public Nuisance” pursuant to the Puerto Rico Municipal Code; and
2. The Urban Center Project must consist of at least 7 residential units.

Tax Incentives

Under the Code, the holder of a tax incentives grant for this eligible activity can enjoy the following tax benefits:

- A 4% income tax rate on income generated from the sale or lease of the Urban Center Project
- 100% income tax exemption for shareholders or partners/members on dividends or benefits distributed from exempt income
- 75% exemption on real and personal property taxes
- 50% exemption on municipal license taxes, excise taxes and other municipal taxes
- 75% exemption on any tax, right, license, excise, rate or tariff imposed by any municipal ordinance in connection with construction work

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Tax Credits

Similar to the tax credit granted to eligible tourism activities pursuant to Section 3010.01(a)(2) of the Code, the exempt business that qualifies for this new activity can request a Tax Credit for Eligible Investment in an Urban Center equal to 40% of the lesser of the Eligible Investment or the Total Project Cost (the “Credit”).

The Credit can be claimed in three installments: the first part can be claimed in the second year after the exempt business commenced operations, and the remaining balance in equal parts over the next two years. Any unused portion of the Credit can be carried over until exhausted.

The Credit may be sold or otherwise transferred by the exempt business.

An Eligible Investment in an Urban Center is generally defined as:

- The amount of cash or value of land and existing structures contributed to an exempt business or eligible business under Section 2071.01(11) of the Code in exchange for: (i) shares of a corporation; or (ii) participation or increase in participation of a limited liability company, partnership or common enterprise.
- A loan that is guaranteed by the exempt business, or eligible business that later receives a grant, or by its assets, or by other entity, parent or affiliate of the exempt business.

Only eligible investments that are made on or after July 1, 2024 will be considered an “Eligible Investment in an Urban Center”, unless the Secretary of the Department of Economic Development and Commerce (“DDEC”) (“Secretary”), exercising his discretion, in consultation with the Secretary of the Treasury, and considering the best interests of Puerto Rico, determines a prior date, which can never be prior to July 1, 2019 (i.e., the effective date of the Code).

Total Project Costs include:

- Construction hard and soft costs incurred by the exempt business in the development of the Urban Center Project;

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- Expenses related to the purchase of furniture, fixtures and equipment and operating supplies and equipment during the first 12 months of operations;
- Expenses related to issuance of debt to obtain capital for the exempt business;
- Expenses related to the construction and development of infrastructure and utilities necessary for the construction and development of the Urban Center Project;
- Acquisition costs or fair market value at the date of contributing the real property; and
- Any other expense, disbursement or investment that the Secretary determines by regulation, circular letter, administrative order or similar document.

Other Requirements

- An application for a grant of tax exemption must be submitted on or before December 31, 2025.
- The development of the real property must have commenced construction on or after July 1, 2024.
- If the development commenced before July 1, 2024 and the Secretary, in his discretion, grants a prior commencement date, the construction could not have been finalized by July 1, 2024. For this purpose, a project is considered finalized if it is 80% completed.
- In the case of real estate leased for residential use in an Urban Center, the lease agreement between the exempt business and the lessee must have a minimum duration of six months.
- Every exempt business that claims a tax credit must request an accreditive certificate issued by DDEC that certifies the Eligible Investment in an Urban Center.

Act 182 became effective immediately for taxable years commencing after 2024.

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PUERTO RICO 787.759.9292

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