



By Eva Lloréns Vélez pages 16-20

TOP STORY

Prepa 'roadshow' looking to raise \$500M; meetings with investors in Boston, New York
page 2

INSIDE

SAIC: Natural gas a more than \$500M offset to EPA compliance costs

page 6

Smooth sailing for Crowley; hammers out collective bargaining agreement in record time

page 8

Toyota to the rescue: Will expanded Prius line kick-start hybrid sales in 2012?

page 50

SPECIAL REPORT



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Back in the saddle

Armed with new, attractive tax and wage credits, and promotion incentives, Puerto Rico is ready to once again become one of the world leaders in attracting investment. The Puerto Rico Economic Development & Commerce Department, combined with the Labor Department, has secured a more than \$1 billion investment and helped more than 200 businesses—both local and foreign—set up new operations on the island. Here's how it works.



BY EVA LLORÉNS VÉLEZ
eval@caribbeanbusiness.pr

Puerto Rico, called the showcase for industrialization and democracy under the U.S. flag in the 1950s and 1960s—a pedestal it has slid from in the past decade—has once again become the talk of the investment community, through an aggressive incentives program designed by Gov. Luis Fortuño's administration to help companies set up operations on the island.

The incentives engine driving Fortuño's economic-development plan is turbocharged, running the gamut from promotion and marketing

to electric power and job-creation credits for companies opening new businesses.

The new model is helping Puerto Rico to transition from a manufacturing-driven economy to a multisectorial model that has new businesses and exports driving job creation across many industries.

KNOWING WHERE TO LOOK

The incentives, say private industry sources interviewed by CARIBBEAN BUSINESS, significantly offset onerous labor laws and high energy costs that were once seen as overwhelming deterrents by potential investors.

Two members of the private sector who specialize in helping businesses become established and expand on the island see a change in perspective in the business community beyond Puerto Rico's shores. Although significant credits exist, businesses often don't know where to look for them.

Bettye Baldwin, managing principal at Retention Strategies, and Janine Guzmán, a lawyer at Pietrantonio, Méndez & Álvarez, say potential investors and employers are often overwhelmed by the maze of Puerto Rico's statutes when trying to establish themselves here, but emphasized that there is help.

"If they get people who are knowledgeable, there is a way through the maze," Baldwin said. "They can work on an action plan."

There is now a general recognition by the administration and the leadership of both houses of the Legislature that to pull out of the negative economy we are in, local labor laws must be changed.

2012 should see an effort by the Legislature and the administration to become more competitive with economies in the states and around the world. The final solution may very well be not to take anything away already acquired by present

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Continued from previous page

employees—what's referred to as a grandfather clause—but rather to subject everyone hired after the new labor laws are passed to these more competitive laws. This will be especially attractive for new companies considering investing in Puerto Rico. All employees hired would be subject to the more competitive labor laws.

Guzmán added that there are all kinds of federal and local programs, based on annual earmarks, that provide funding for businesses. Local Law 52, for example, and the federal Work Investment Fund can provide up to 50% in wage incentives, she said.

IT STARTS WITH PRIDCO

The Puerto Rico Industrial Development Co. (Pridco) offers a host of incentives for businesses, manufacturing, agriculture, apparel, green companies, hotels, cruises and banks. The Industrial Film Commission oversees incentives for off-island producers looking to film their projects here. The commonwealth Department of Labor & Human Resources oversees all wage subsidies for businesses, while the Economic Development Bank offers financial support and consulting to small and midsize businesses. The Puerto Rico Commerce & Export Co. also helps out small businesses and provides support for the exportation of local products.

There are credits for the use of electric power by businesses that open in urban centers. The subsidy, however, is only about \$40 a month. The low participation rate brings the total annual amount provided by the Puerto Rico Electric Power Authority (Prepa) to just \$3,204 for all small businesses in urban centers.

More recently, the government enacted the Export Services Act, which is aimed at exporting services. The tax benefits include a 4% corporate tax rate, which may be reduced to 3%; 100% tax exemption on dividends or profit distribution from export service businesses; 100% exemption on property taxes for certain export services; a decree of 20 years, renewable for 10 more, guaranteeing these rates.

There is even the Housing Incentives Act, which was enacted in 2010 to help jump-start the ailing real



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managing principal at Retention Strategies

estate business, just to mention a few. The Housing Incentives Act, in essence, exempts homebuyers from paying property taxes for a determined period and provides discounts on the notary fees, registration and some mortgage fees.

MORE THAN \$1 BILLION IN INVESTMENT

The benefits available to businesses can be enormous. William Rivera,

owner of Cheesecake and Company, said he received a marketing incentive from Pridco's promotions program that has allowed his Guaynabo company to reinvest 15% to 17% in company operations.

“It was easy to get the help for the incentive,” he said.

The promotions program in the past four years has promoted more than 200 companies, yielded a commitment of more than \$1 billion

in investments and created 14,000 jobs.

The marketing incentive program, one of the many incentives given by Pridco, is for companies whose sales are greater than \$100,000 a year. Through this incentive, Pridco will reimburse 50% of the costs incurred, up to \$50,000, for publicity, publications, promotional material, market research and special promotional activities.

Porfirio Díaz of Old Harbor Brewery, an Old San Juan restaurant that brews craft beer, said the promotions incentives will allow his company to export its beer. Right now, the special beer is available in more than 80 restaurants and hotels.

The incentives have also allowed the business to save money and rent space in Carolina for a brewery that will add 12 jobs to the current 49, he said.

Pridco Executive Director José Ramón Pérez-Riera said the promotions program helps businesses dedicated to biotechnology, information systems, telecommunications, food, textiles and manufacturing.

The incentives offered by Pridco are numerous because it is the entity in charge of promoting industry and direct foreign investments.

Chief among them is the Economic Incentives for the Development of Puerto Rico Act, which provides attractive tax and other incentives to foster investments. In general terms, eligible businesses include those established to manufacture products on a commercial scale, and businesses established to render services on a commercial scale for foreign markets or for other eligible businesses in Puerto Rico. The law, known as Act 73, operates through a tax decree issued for a period of 15 years.

The law provides a host of other tax incentives for eligible businesses. For instance, with the approval of the Economic Development & Commerce Department, businesses can get an 8% income tax rate coupled with a 2% withholding tax rate on royalties, instead of a 4% income tax rate and 12% withholding tax rate on royalties.

An eligible business engaged in a novel pioneer activity—i.e., socially or economically beneficial activities that haven't been carried

Continued from page 17

out in Puerto Rico during the previous year—will be subject to a 1% income tax rate.

Under the law, businesses that purchase products manufactured in Puerto Rico will be permitted to claim a credit of 25% of the purchase cost, up to a maximum of 50% of its tax liability, for products made from recycled materials. The credit is equal to 35% of total purchases up to the 50% limit.

In addition, businesses that set up shop on the island towns of Vieques and Culebra get \$5,000 per job created in a high industrial area. In a low-industrial-development zone it is \$2,500 per job, and in an intermediate zone it is \$1,000 per job.

Businesses can also receive a credit of 50% of the costs for investments in research and development (R&D), clinical trials, toxicology tests, infrastructure, renewable energy and intangible property.

Under the law, businesses can also get a tax credit of 50% of costs for investments in machinery and equipment for the generation and efficient use of energy. For instance, all eligible businesses that are industrial clients of the Puerto Rico Electric Power Authority can receive a tax credit of 3% of their electricity payments, among a host of other power incentives.

Eligible businesses that obtain a decree are also eligible for a 90% exemption from municipal and commonwealth property taxes on personal property used in the businesses' development, organization, construction, establishment or operation, among other uses.

They are also eligible for full exemption from municipal taxes or municipal licenses that apply to the volume of their business generated during the quarter of the government fiscal year in which the exempted business commences operations, and continuing for the following four quarters. They also get municipal tax exemptions on certain works or construction.

JOB CREATION

Pridco also provides incentives to encourage the establishment and retention of local and foreign investors. They include a basic incentive for job creation—\$400 per employee



“In all sectors, jobs have been created...What we have to look at is the numbers that have come out of the Labor Department.”

—José Ramón Pérez Riera,
Economic Development and Commerce Secretary

for new businesses and \$250 per employee for expansions of existing businesses.

In addition to the basic incentives, companies can receive a location-based incentive for job creation outside of the San Juan metropolitan area.

There is also a special incentive for the rescue of a business. When a Pridco-promoted business intends to cease operations or reduce its

workforce by 50% or more, a new owner committed to keeping at least 25% of the employees who are working at the moment of the rescue may be entitled to assistance.

Companies engaged in projects deemed to have extraordinary importance for the economy of Puerto Rico—because they create and maintain a large number of jobs or a lesser number of higher-paying jobs, promote new technology, transfer

technology business knowledge, or are otherwise considered highly meritorious by the executive director and the board of Pridco, can also benefit from incentives.

Companies promoted by Pridco may be eligible for an incentive to improve buildings belonging to Pridco that are necessary for the companies' operations.

There is also an incentive for the manufacturing of furniture and related products, and another applying to the apparel industry and its related products.

This final incentive is available for Puerto Rican businesses that have been operating for at least one year in the manufacture of furniture or related products, or in the manufacture of apparel or similar products that qualify for the economic incentives provided by Act 8 of 1986. Businesses that qualify for the incentive will receive a cash incentive of 3% of eligible sales, up to a maximum amount of \$150,000 per business a year.

Companies may be eligible for a cash incentive of up to \$100,000 for establishing and operating a business in Vieques or Culebra. This incentive can be used for maritime, land and aerial transportation of raw materials and finished products, including labor costs, tolls and other expenses related to transportation.

SCIENTIFIC RESEARCH INCENTIVES

As part of Puerto Rico's focus on attracting R&D to the island, Law 73 established a Special Fund for Economic Development (FEDE by its Spanish acronym). This fund can be used for scientific and technical research and the development of new industrial product businesses, among other purposes.

Similarly, the Puerto Rico Science, Technology & Research Trust (the Trust)—an autonomous entity that receives funding from FEDE and the Scientific Research Fund of the University of Puerto Rico, among other sources—provides a financing option for research, development and infrastructure projects in the fields of science and technology. From 30% to 40% of the Trust's annual budget is used to finance corporate activities and projects that have an impact on science and technology R&D in Puerto Rico.

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Puerto Rico also provides incentives to promote the sustainable growth of the island's agriculture sector. These include a wage subsidy as well as incentives for working farmers, and an annual bonus to other agricultural producers that maintain farms or are involved in the storage, transportation, distribution and marketing of farm produce.

BANKING AND INSURANCE

The banking and insurance industries have their own incentives as well. Puerto Rico's International Banking Center law permits the creation of international banking entities (IBEs), which are essentially banks located in Puerto Rico that provide financial services to clients outside of Puerto Rico.

Puerto Rico is considered a foreign jurisdiction under the U.S. International Banking Act of 1978; therefore, all IBEs in Puerto Rico are exempt from International Banking Association requirements for domestic financial institutions.

In the area of insurance, the recently enacted Act 98 of 2011 facilitates the establishment of entities that export insurance and reinsurance services, allowing Puerto Rico to compete with jurisdictions such as Bermuda, the Cayman Islands and Vermont, which for years have successfully engaged in promoting this type of activity.

ARTS

The Puerto Rico Film Commission (PRFC) was created in 1999 to develop the film industry on the island, in part by offering incentives to off-island producers looking to film their projects in Puerto Rico.

The PRFC's primary incentives are a 40% tax credit on local production expenditures, and a 20% tax credit for production expenditures on nonresident talent, provided they are subject to income taxation in Puerto Rico.

In addition, the PRFC also provides incentives for film industry-related infrastructure projects. These include a 25% tax credit on costs for development or expansion of infrastructure projects. People engaged in qualifying media and infrastructure projects as well as the operation of a large-scale studio within



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—Miguel Romero,
Labor Secretary

the film-development zone, a special area designated for movie making, are eligible for favorable tax treatment. These incentives include a 4% fixed income tax rate, 100% exemption on dividends, 90% exemption from municipal and state taxes on property, and 100% exemption from municipal licensing, excise and other municipal taxes.

HOTELS AND CRUISESHIPS

The Puerto Rico tax incentive package offers hotel developers a

competitive advantage over other destinations to attract luxury-class hotels, theme parks and golf courses as well as promote the use of natural resources as a source of entertainment. Tax exemptions under this law remain valid for a period of 10 years from the starting date of the eligible tourism-related project, and the business operation will be entitled to a 10-year extension.

The cruise industry also has a host of incentives. Act 113 of 2011, known as the Law for the Promotion

& Development of the Cruiseship Industry in Puerto Rico, further strengthens Puerto Rico's competitiveness in the cruise industry.

The new law provides a string of incentives to promote transit and homeport cruise visits, spur travel agencies to sell packages to non-residents that include both a cruise and a stay in a hotel in Puerto Rico, promote the purchase of products in Puerto Rico, promote the local procurement of ship maintenance and repair services, and promote excursions for cruiseship passengers.

BUSINESSES CAN SAVE, CREATE JOBS

Pérez-Riera said he wasn't sure yet how many jobs the incentives have created in Puerto Rico, nor how much businesses have been able to save.

However, he said the film industry incentives have created some 10,000 temporary jobs, while the tourism incentives may have created more than 5,000 new jobs in construction alone.

“In all sectors, jobs have been created,” he said. “What we have to look at is the numbers that have come out of the Labor Department.”

Those numbers show that total employment for Puerto Rico in January reached 1,095,758, an increase of 21,975 people working compared with January 2011.

Senate President Thomas Rivera Schatz, in a recent editorial board interview with CARIBBEAN BUSINESS, said some 34,000 jobs have been created in the private sector.

WAGE SUBSIDIES

The Labor Department also offers incentives in the form of wage subsidies. The Puerto Rico Human Resources & Occupational Development Council (HRODC) administers funds received by Puerto Rico under the federal Workforce Investment Act (WIA).

The program offers workforce training incentives to businesses through on-the-job training, customized training, combined programs and retraining. In essence, WIA reimburses up to 50% of the salary of the participant for the duration of the training.

Labor Secretary Miguel Romero

Continues on page 20



Continued from page 19

said that although Puerto Rico lost some \$15 million in WIA funds, it was able to replace the funds using American Recovery & Reinvestment Act (ARRA) funds to promote labor.

"Through WIA, we were able to impact 6,000 jobs," he said. "Since 2009, we have impacted 11,000 jobs."

This year, the agency granted up to \$30 million in wage subsidies through Law 52, creating some 9,000 jobs since 2009. He said that some of the employers that have received the wage subsidy include the San Juan Beach Hotel and Metzgermeister, a food products firm in Mayagüez.

More recently, the Labor Department launched a program that helps former convicts find employment.

Romero noted that not all businesses can offset labor and energy costs using the island's incentives.

"Not everyone participates," he said.

However, the Labor chief noted that some 14,000 new corporations

have been created in a year's time, which means the incentives are helping promote new business.

SMALL BUSINESS

Puerto Rico also offers incentives to small and midsize enterprises (SMEs) to facilitate their growth.

Two government agencies are particularly focused on SMEs: the Economic Development Bank (EDB) and the Puerto Rico Commerce & Export Co. The EDB offers financial support to SMEs through asset-based loans, participation loans with private financial institutions or under the SBA 504 loan guarantee program, mezzanine financing or capitalization loans, tourism project loans, management buyout loans, and credit lines for operational capital.

The Puerto Rico Commerce & Export Co. (CCE by its Spanish initials) is a public corporation that fosters the development of trade, with special emphasis on small and midsize businesses, and the export of Puerto Rican products and services to other countries or regions. It provides educational courses and consulting services.

CCE's real estate division can provide storage facilities for product distribution using its warehouses and commercial facilities in San Juan, Ponce and Mayagüez. It also helps businesses in the area of exports.

To help small businesses, Prepa is authorized to grant a 10% credit, up to a maximum of \$40 a month or \$480 a year, to small retailers or non-professional personal logistics facilities with seven or fewer employees that are located in urban centers.

GREEN ENERGY INCENTIVES

There are also incentives in the area of renewable energy.

The Green Energy Incentives Act of 2010 creates a Green Energy Fund (GEF) through which the government of Puerto Rico will co-invest \$290 million in renewable-energy projects over the next 10 years. Initial funding of \$20 million began July 1, 2011 and steps up to \$40 million by fiscal year 2016. Through the GEF, the P.R. Energy Affairs Administration will offer cash rebates of up to 60% on the cost of installing Tier 1 or small projects (0-100 kW) for residences and small businesses,

and up to 50% on the cost of Tier 2 projects (100 kW-1 MW) for commercial or industrial use.

In the area of housing, the government created Act 132 of 2010, known as the Housing Incentives Act, to reduce the inventory of housing and other properties and jump-start the real estate market. The program was extended to December 2012 due to its success. Under the housing incentives, homebuyers are eligible for benefits including: exemption from payment of stamps and vouchers at the time of purchase; exemption from property taxes for five years; tax exemption on capital gains realized on the sale or purchase of existing residential and commercial properties, provided their value doesn't exceed \$3 million; tax exemption on future capital gains on the sale of a new property; and other types of incentives.

More recently, the government also passed the Export Services Act of 2011 to attract foreign talent and foreign capital, and create a special fund for promoting the establishment of new businesses to export services from Puerto Rico. ■