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the LEGAL UPDATE

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Tax Update

Puerto Rico Government Issues Expenditure Report

On September 22, 2019, the Government of Puerto Rico issued its Tax Expenditure Report ("PRTER") for Tax Year 2017. The PRTER is intended to comply with requirements imposed on the Puerto Rico Government by GASB Statement No. 77 and the Puerto Rico Oversight, Management and Economic Stability Act ("PROMESA").

GASB Statement No. 77, *Tax Abatement Disclosures*, requires state and local governments to disclose key information about their tax abatement agreements. These are agreements whereby a government reduces—or abates—the taxes a company or person otherwise would owe. Information includes the following:

- The purpose of the tax abatement program
- The tax being abated
- Dollar amount of taxes abated
- Provisions for recapturing abated taxes
- The types of commitments made by tax abatement recipients
- Other commitments made by a government in tax abatement agreements, such as to build infrastructure assets.

In turn, Section 208(b) of PROMESA requires, within six months of the establishment of the Fiscal Oversight Board, the publication of a Report on Discretionary Tax Abetments or similar tax relief agreements to which the territorial government, or any territorial instrumentality, is a party.

The PRTER provides a definition for "tax expenditures" that includes revenue loss due to special exclusions, deductions, exemptions, credits, preferential rates of tax, or a deferral of tax liability measured as "foregone revenue". This method does not measure behavioral response to the potential elimination of tax expenditures. Further, the PRTER emphasizes that no judgment has been made about the desirability of any special tax provision as a matter of public policy.

The PRTER is also clear on the fact that it does not take into consideration the macroeconomic feedback or dynamic effects on the overall level of economic activity that investments in such "tax expenditures" could have. Lastly, it recognizes that approximately 98% of the income taxed under incentives acts such as Act 73-2008 and 20-2012 is income generated by foreign-owned incentive corporations whose potential behavior in response to elimination of tax benefits could have an impact that eliminates any potential gain in revenues resulting from the elimination of the tax expenditure; even that it may create significant dynamic reductions in the economy.

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The PRTER classified 302 separate items of tax expenditures that could be categorized in the following budget classifications:

- Art, culture, sport & recreation
- Business farming and fishing
- Business research and development
- Business – small business
- Donation, gifts, charities and non-profit organizations
- Economic development
- Education
- Employment
- Environment
- Families and households
- Health
- Housing
- Income support
- Intergovernmental tax arrangements
- International
- Retirement
- Savings and Investment
- Social

The PRTER promises to be a great tool in the Puerto Rico budgetary process and tax policy discussion. A full copy of the report can be found here: