

FILM INCENTIVE PROGRAMS IN PUERTO RICO

Puerto Rico has been promoting the development of the film and television industries since 1999 when it first enacted a law providing incentives to encourage the investment in film production and related infrastructure projects. Moreover, Puerto Rico's strategic location and close-ties with the United States position it as a desirable venue for filming. As a Commonwealth of the United States, Puerto Rico "offers all of the benefits and protections available on the mainland, including applicability of U.S. labor, safety and minimum wage laws, U.S. intellectual property and banking protections and U.S. Dollar currency. No U.S. passport is required for United States citizens."¹ Accordingly, Puerto Rico not only benefits from its close-relationship with the United States, but it directly competes with the states for the film market. State legislatures have been enacting competitive incentive regimes for the past decades thus, leaving Puerto Rico at a disadvantage. To parallel current competitive conditions, including tax incentives, the Puerto Rico Legislature enacted the Puerto Rico Film Industry Economic Incentives Act of 2011, as amended (the "Act"). Through the Act, Puerto Rico aims to attract foreign capital and foster the economic development as well as to create infrastructure for the development of the film industry in the island. The incentives provided through the Act are discussed in the following paragraphs.

In general, to benefit from the provisions of the Act, it is necessary to obtain a grant from the Secretary of the Department of Economic Development and Commerce of the Government of Puerto Rico (the "Secretary"). Such grants may be effective before the grant application filing and, except for some cases, will have a term equal to the life of the project. In terms of application fees, the Film Projects² shall pay to the Secretary a fee equal to 1% of the Puerto Rico Production Expenditures³, not to exceed \$250,000. Additionally, grantees must contract an auditor to determine and render a report to establish the Puerto Rico Production Expenditures, to

¹ Puerto Rico Film Commission. <http://puertoricofilm.org/shooting-in-pr/puerto-rico/>.

² Film Project means: feature length films, short films, documentaries, television series, miniseries, music videos, national and international commercials, video games, recorded live performances, original soundtrack and dubbing recordings for the previously mentioned, television programs, and the post-production of any of the previously listed projects.

³ Puerto Rico Production Expenditures are, in general, payments made to residents of Puerto Rico and/or Nonqualified Residents for services physically rendered in Puerto Rico, directly attributable to the development, preproduction, production, and post-production of a Film Project. Please refer to the Act for further guidance since there are additional requisites.

compute the approximate tax credit, and to certify certain expenditures. The grants under the Act are usually conceded in connection with Film Projects or Infrastructure Projects⁴.

Film Projects

Film Projects include feature length films, short films, documentaries, television series, miniseries, music videos, national and international commercials, video games, recorded live performances, television programs, and the postproduction of any of the previously listed projects, among others. The requirements to obtain a grant in connection with a Film Project are: 1) the production and/or postproduction is to be carried out in whole or in part in Puerto Rico; 2) the Film Project is intended for airing, commercial distribution or exhibition to the general public outside of Puerto Rico by any means and media; and 3) a minimum expenditure requirement of \$25,000 or \$50,000 depending on the Film Project.

No tax exemption grants will be issued under the Act to any of the following Film Projects: pornographic material productions; productions that primarily consist of religious or political advertising; productions that primarily market a product or service other than a national or international commercials (such as infomercials); radio programs; productions with the primary purpose of fund-raising; employee training or in-house corporate advertising productions; and, productions that receive substantial support in the form of subsidies, donations or appropriation from the Commonwealth of Puerto Rico, among others.

Tax credits in cases of Film Projects include a 40% credit of the amounts disbursed for Puerto Rico Production Expenditures, excluding payments made to Qualified Nonresidents⁵, which only qualify for a 20% credit. In addition, a recent amendment to the Act includes additional tax credits which, depending on the Film Project, may be up to 50% of the Puerto Rico Production Expenditures, excluding payments to Qualified Nonresidents. These additional credits encourage the participation of Puerto Rico residents in Film Projects. For example, a 7% additional tax credit is granted if the director of the Film Project is a Puerto Rico resident.

⁴ Infrastructure Project means the development or substantial expansion in Puerto Rico of studios, Studios, Large-Scale Studios, laboratories, post-production facilities, facilities for the international transmission of television images or other media, or other permanent facilities to carry out Film Projects (regardless of whether said projects avail themselves of the provisions of this Act) whose hard costs budget, as certified by the Auditor, exceeds one million dollars (\$1,000,000).

⁵ Qualified Nonresidents include producers, directors, writers, any talent in front of the cameras (except extras), including stuntmen, known as *Above the Line*, and any person of technical or creative character behind the cameras, known as *Below the Line*, and any other similar person that, according to the general accepted practice in the entertainment industry, may be considered *Above the Line* or *Below the Line*, as determined by the Secretary, that is not a resident of Puerto Rico.

Moreover, an additional credit of 10% of the Puerto Rico Production Expenditures, excluding payments to Qualified Nonresidents, is available to grantees engaged in feature films, television series or miniseries, whose story is centered in Puerto Rico and Puerto Rico is expressly mentioned. However, all the above-mentioned credits combined may not exceed 90% of the Puerto Rico Production Expenditures. And, except for national and international commercials, music videos and original soundtrack and dubbing recordings, all Film Projects must include a certain Puerto Rico Screen Credit⁶ to receive production tax credits under the Act. The Puerto Rico Screen Credit must be placed in a prominent position within the credit roll of the finished Film Project.

Tax credits pursuant to Film Projects are generally subject to a \$50 million annual cap. However, under certain circumstances, Film Projects may apply for credits in excess of this annual limit when any portion of the Puerto Rico Production Expenditures has been incurred within a Film Development Zone⁷. The \$50 million annual cap does not apply to the 20% credit for the Puerto Rico Production Expenditures consisting in payments to Qualified Nonresidents. Furthermore, none of the previously mentioned credits are refundable.

Film Projects' tax credits may be taken in two different ways. First, 50% of the granted tax credit will be available in the taxable year in which 50% or more of the Puerto Rico Production Expenditures have been disbursed. Alternatively, a 50% of the tax credit may be granted in advance if a bond is posted designating the Secretary of the Treasury of Puerto Rico as beneficiary. The remaining 50% of the tax credit, or the full tax credit if no advance was authorized, will be available in the taxable year in which all Puerto Rico Production Expenditures have been paid.

⁶ According the Puerto Rico's Film Commission Circular Letter No. 13-02, a Puerto Rico Screen Credit is a requirement establishing that, excluding commercials, music videos and soundtrack and dubbing recordings, all grantees shall be required to include a screen credit in connection with Puerto Rico's Film Incentive Program. The Puerto Rico Screen Credit shall read as follows: "Filmed on location in Puerto Rico, thanks to the Commonwealth of Puerto Rico, the Puerto Rico Film Commission and its Film Incentives Program" and must also include the "Puerto Rico Film Commission" logo and website "www.puertoricofilm.com."

⁷ Film Development Zones are those designated by the Secretary. Such geographical areas shall consist of real property for the development, construction, and operation of Large-Scale Studios and other related developments consistent with the purposes of and as provided in this Act, irrespective of who is the owner of such property. Notwithstanding, the Act established the Autonomous Municipality of San Juan as a Film Development Zone.

Infrastructure Projects

Infrastructure Projects, in general, refer to the development or substantial expansion in Puerto Rico of studios, laboratories, and other facilities to carry out Film Projects whose hard costs budget exceeds \$1 million dollars. To qualify as a substantial expansion, the investment must be equal to at least 25% of the fair market value of the existing physical facility.

Tax credits granted in cases of Infrastructure Projects shall be equal to 25% of the amounts disbursed in connection with the development and/or expansion of the Infrastructure Project in question. Tax credits pursuant to Infrastructure Projects are generally subject to a \$10 million-dollars aggregate annual cap and subject to a \$150 million dollars' lifetime cap. None of these credits are refundable.

As a general rule, all or any portion of tax credits issued in accordance with the Act may be transferred to other persons, subject to the same use limitations imposed by the Act. Prior to any tax credit transfer, the transferor shall submit to the Secretary of the Treasury of Puerto Rico a statement that describes the amount of tax credit for which the transfer of tax credit is eligible. The proceeds from the sale of tax credits granted pursuant to the Act are exempted from the payment of any tax imposed by the Government of Puerto Rico. Moreover, it should be noted that no subsidies are provided under the Act.

Tax Treatment of Grantees

Generally, grantees may also enjoy the following tax benefits under the grant: 1) a fixed 4% income tax rate on net income directly derived from the exploitation of activities covered under a grant; 2) 100% exemption on dividends; 3) 90% exemption on municipal and Puerto Rico taxes on real or personal property; and 4) 100% exemption on municipal license taxes, excise taxes and other municipal taxes.

Currently, Puerto Rico has strongly positioned itself in the growing and international film industry market, allowing it to capture a growing share of such market. Along with its location, geographical, and political characteristics, Puerto Rico now offers competitive incentives in the film industry. It fosters the development and production of film projects and infrastructures through various incentives while, at the same time, capitalizing on the economic impacts of the film industry, making Puerto Rico a well-positioned player in the film and television industry.