



TAX INSIGHTS

Understanding Private Equity Funds in Puerto Rico: Structures, Tax Incentives, and Compliance Considerations under Act 60-2019

Collaborators:

Vanessa Rodríguez, CPA, Tax Senior Manager

Jennifer Mercedes, Tax Senior

Puerto Rico has positioned itself as a competitive jurisdiction for private equity funds through Act 60-2019, known as the Puerto Rico Incentives Code (“Incentives Code”). This article provides a high-level overview for fund managers, investors, and advisors of how private equity funds are structured, taxed, and regulated in Puerto Rico, with a focus on preserving tax incentives and mitigating compliance risks.

We highly recommend reading this article alongside our recent tax alert on Private Equity Funds, which discusses new requirements and rules set by the Department of Economic Development and Commerce: [Tax Alert: New Administrative Order Governing Private Equity Funds](#).

What is a Private Equity Fund?

A Private Equity Fund (PEF) is an investment vehicle formed to invest in non-publicly traded securities and is treated as a partnership for Puerto Rico tax purposes. To qualify for the tax incentives available under the Incentives Code, a fund must meet specific eligibility requirements and obtain a tax exemption decree from the Puerto Rico Department of Economic Development and Commerce (DDEC). Qualification is not automatic; funds must not only satisfy eligibility requirements at inception but also maintain ongoing compliance with the terms and conditions of the exemption decree and applicable regulations.

Types of Funds and Eligibility Requirements:

- Private Equity Fund (PEF)
- Puerto Rico Private Equity Fund (PRPEF)

PEF	PRPEF	Eligibility Requirements
✓		Within four years of organization and annually thereafter, at least 15% of the fund’s capital (excluding cash) must be invested in qualifying private securities or debt of Puerto Rico entities or government instruments, or foreign entities that during the last three years derive at least 80% of their gross income from Puerto Rico sources or from income effectively connected to a Puerto Rico trade or business (“80% test”).
	✓	Within four years of organization and annually thereafter, at least 60% of the fund’s capital (excluding cash) must be invested in qualifying private securities or debt of Puerto Rico entities or government instruments, exempt investment trusts, foreign entities that meet the 80% test, or foreign entities that transfer operations to Puerto Rico within six months and after such transfer meet the 80% test.
✓	✓	All investors must be Accredited Investors.
✓	✓	The fund must employ one or more Registered Investment Adviser (“RIAs”), with at least one maintaining an office in Puerto Rico, conducting a trade or business in Puerto Rico, and registered with the relevant regulatory authorities.
✓	✓	Within four years of organization, and annually thereafter, no more than 50% of the fund’s capital may be invested in a single business or group of affiliated entities.
✓	✓	The fund must reach a minimum of \$10 million in capital (including documented commitments) within 24 months of issuing ownership interests and subsequently.
✓	✓	The fund must appoint at least one investor to an advisory board to discuss matters of interest and concerns related to the fund.
✓	✓	For foreign funds, the general partner or RIA must conduct a trade or business in Puerto Rico and derive at least 80% of gross income from Puerto Rico sources or effectively connected income.

Tax Benefits:
Income Tax

	Accredited Investors	General or Managing Partners, RIA and Private Equity (“PE”) Firm
Distributive share from Interests and Dividends *	Subject to income tax at a flat rate of 10% in lieu of any other tax imposed by the Puerto Rico Internal Revenue Code (“PRIRC”).	Subject to income tax at a flat rate of 5% in lieu of any other tax imposed by the PRIRC.
Distributive share from Capital Gains	Shall be fully exempt from income tax and shall not be subject to any other tax imposed by the PRIRC.	Subject to income tax at a flat rate of 2.5% in lieu of any other tax imposed by the PRIRC in the taxable year in which that sale occurs.
Sale of Ownership Interest	Capital gains realized on the sale of an ownership interest in a PEF or PRPEF are subject to income tax at a flat rate of 5% in the taxable year in which the sale occurs, in lieu of any other tax imposed by the PRIRC. If the entire gross proceeds are reinvested in a PRPEF within ninety days from the date of sale, such capital gains are fully exempt from income tax.	
Distributive Share from Net Capital Losses	May deduct their distributive share of net capital losses provided that such losses are attributable to legal entities that meet the 80% test. These losses may be offset against other income and capital gains if certain requirements are met, with any unused losses carried forward indefinitely.	

* Exempt interests or dividends generated by a PEF or RPEF shall maintain their exemption when held by the investors.

Property Taxes

- A PEF and PRPEF shall have a 75% exemption from property taxes imposed under the “Municipal Property Tax Act,” including the real and personal property, tangible and intangible, belonging thereto.
- PEFs and PRPEFs are exempt from filing the personal property tax return.

Municipal Taxes

- Income earned by a PEF and PRPEF and distributions made to investors are not treated as gross income and are excluded from the definition of “volume of business” for purposes of the Municipal License Tax Act.
- PEFs and PRPEFs are exempt from filing the volume of business declaration.

Special Deductions

- PEF – Resident accredited investors may deduct up to 30% of the adjusted basis of their investment over 10 years, subject to an annual cap of 15% of their net income before the deduction.
- PRPEF – Resident accredited investors may deduct up to 60% of the adjusted basis of their investment over 15 years, subject to an annual cap of 30% of their net income before the deduction.

Structures

In the case of PEFs and PRPEFs that are series Limited Liability Companies (LLCs), said LLC may elect to be treated as a single fund regardless of the number of series, if the fund meets said eligibility requirements. These structures may offer:

- Segregation of assets and liabilities by investment strategy or investor group
- Centralized management and compliance oversight
- Flexibility to manage multiple portfolios within a single legal entity

Disclosure of Information

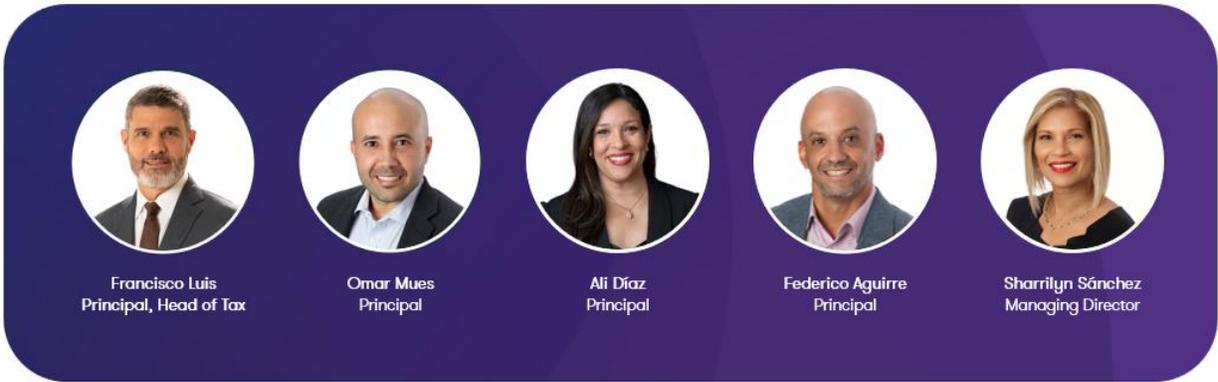
Every Fund shall:

- Register any offer of participation or investment in such Fund with the OCIF and must comply with all applicable provisions of the U.S. and Puerto Rico Federal Securities Laws.
- Provide to its investors quarterly unaudited results and annual audited financial statements prepared by a Puerto Rico licensed CPA.
- Disclose material risks, events, and provide a sworn certification of compliance by the CEO.
- Hold an annual general meeting to update investors on fund operations.
- Be subject to examination by the OCIF for compliance with costs borne by the fund.

Failure to comply with tax or regulatory obligations may result in penalties, loss of tax incentives, or revocation of tax exemption decree.

Puerto Rico's private equity incentives under Incentives Code offer meaningful tax and operational advantages. However, these benefits depend on proper structuring, timely compliance and ongoing adherence to statutory and decree specific requirements. Professional tax and legal guidance are essential to navigating the evolving regulatory environment and preserving available incentives.

We are committed to keeping you informed of all the latest developments in laws and regulations that affect businesses in Puerto Rico. We can help you navigate the complex tax landscape to ensure that you are taking advantage of all the available benefits. Contact us today to learn more about how we can help you.



DISCLAIMER: This update and its content do not constitute advice. Clients should not act solely on the basis of the material contained in this publication. It is intended for information purposes only and should not be regarded as specific advice. In addition, advice from proper consultants should be obtained prior to taking action on any issue dealt with this update. The information provided in this publication may change in the future and such changes may be applied