Navigating the Tax Incentive Landscape and Policy

University of the Virgin Islands Research & Technology Park Business Attraction Summit 2019

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U.S. Virgin Islands Tax System

- Unincorporated territory of United States
- Not covered by U.S. Tax Treaties
- Covered by U.S. Treaties of Friendship, Commerce & Navigation and Bilateral Investment Treaties
- Special competent authority procedure for Territorial-IRS Disputes
- Tax Implementation Agreement (Feb. 24, 1987) governs exchange of information between USVI and U.S.

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U.S. Virgin Islands Tax System

- Uses Internal Revenue Code under “Mirror System”
- Residents file one Form 1040 with the Virgin Islands Bureau of Internal Revenue (“BIR”), regardless of source of income
- Foreign to the U.S. for corporate tax purposes, so the rules for Controlled Foreign Corporations, Passive Foreign Investment Companies and Foreign Personal Holding Companies, and Global Intangible Low-Taxed Income apply
- USVI corporations file Form 1120 with the BIR and foreign corporations (including U.S. corporations) file Form 1120F with the BIR

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U.S. Virgin Islands Tax Incentives

- USVI offers economic development incentives to targeted businesses
- Authorized by the U.S. Congress under Section 934 of the Internal Revenue Code of 1986; Amended by the JOBS Act of 2004
- Similar incentive programs in place for over 50 years
- USVI currently can reduce or remit so much of the tax liability incurred to the USVI “as is attributable to income derived from sources within the Virgin Islands or income effectively connected with the conduct of a trade or business within the Virgin Islands.”

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U.S. Virgin Islands Research and Technology Park Program

- RTPark – University of the Virgin Islands ("UVI") St. Croix headquarters and "virtually" available throughout the Territory
- Development and growth of technology sector in the USVI
- Targeted Businesses
  - "Knowledge-Based" businesses engaged in:
    - E-Commerce
    - Software Solutions
    - Development, commercialization or licensing of IT-based products and services
    - Creation, use, distribution or management of digital content
    - Technologies related to RT Park mission

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U.S. Virgin Islands Research and Technology Park Program

- **Tax Incentives**
  - Income tax credit equal to 90% of tax
  - Exemption from local taxes
  - Reduced withholding on dividends, interest, and royalties to foreign recipients
  - No withholding on payments to U.S. persons/entities
- Negotiated joint venture with RTPark – the “Cell” concept
- Park-Tenant Agreement

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U.S. Virgin Islands Research and Technology Park Program

- Park Tenant Agreement financial terms:
  - Application Fee
  - Initial Certificate Fee
  - Annual Management Fee
  - Equity Stake
  - Buyout Fee
  - UVI Partnership Commitment
- Timeline
  - 60-180 days to admittance

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Other USVI Economic Development Programs

- 1. Economic Development Program – Title 29, Chapter 12, Virgin Islands Code
  - Provides benefits for initial benefit period of 20 years in St. Thomas and St. John and 30 years in St. Croix
  - Benefit extension available including 10-year extension and 5 to 10 year extensions for capital investment meeting certain criteria
  - Exemptions from gross receipts tax, certain excise taxes, property taxes
  - Income tax rate equal to effective 10 percent of statutory rate
  - Local employment, procurement, and investment requirements

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Other Economic Development Programs

- 2. Sustainable Tourism through Art-based Revenue Stream Act – Subchapter II, Chapter 12, Title 29 of the Virgin Islands Code – Provides tax incentives for music and film businesses operating in the USVI
- 3. Enterprise Zone Tax Incentives – Provides tax benefits for businesses located in historic USVI towns
- 4. Tax Incremental Financing
- 5. Hotel Development Act
- 6. Exempt Insurers and Exempt Companies
- 7. Benefits for Farmers and Fishermen
- 8. Benefits for Renewable Energy in Act 7075
- 9. Qualified Opportunity Zones

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Source and Effectively Connected Income Rules for USVI

- April 2008 – IRS issued Final Regulations for determining whether income is derived from sources within a U.S. possession under Code section 937 or whether income is effectively connected with the conduct of a trade or business within the possession
- Fees for services are sourced where the work is performed, so allocation may be required
- Effectively connected rules are those in IRC Section 864(c)(4)
- No U.S. source income can be effectively connected with a USVI trade or business except certain income from inventory sales
- Special consideration for transfers of Intellectual Property to USVI
- IRS Notice issued in September 2006 provided examples for determining possession source and effectively connected income
    - Examples indicate that development and sales of computer software and operation of application service providers can meet source of income and effectively connected requirements under Code section 937

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Entity Selection Post Tax Cuts and Jobs Act of 2017

- Individuals who reside in the USVI obtain benefits on their dividends or distributions from RTPark beneficiaries
- Investment structures involving non-USVI investors need to consider changes made by the Tax Cuts and Jobs Act of 2017 (TCJA)
- Investments by U.S. residents into USVI corporations need to be carefully structured to avoid current taxation of USVI corporate earnings

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Residency Rules for USVI

- There are five alternative ways that a person can meet the physical presence component of the bona fide residency test for U.S. possessions:
  - A person is present in a possession for at least 183 days during a tax year
  - A person spends no more than 90 days in the U.S. during the tax year
  - A person has no significant connection to the U.S. during the tax year
  - A person has no more than $3,000 of earned income from U.S. sources and is present for more days in the territory than in the U.S. during the tax year
  - A person is present in the possession for a simple, non-weighted 3-year average of 183 days per year (or 549 days for 3 years), provided that a minimum of 60 days of presence is met in each of those 3 years

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Residency Rules

- August 2015 – IRS published proposed amendments to Treasury Regulations, adding 30 international travel days (non-USVI/non-U.S. mainland days) that will count as days of presence in the USVI
  - However, the proposed amendments require that the taxpayer’s actual days in the USVI exceed those spent in the U.S.
  - Proposed amendments are designated as “reliance regulations” and therefore the amendments were applicable beginning in the 2016 tax year
  - Proposed amendments are in line to be issued in final form

Residency Rules

- Bona Fide residents must also meet “tax home” and “closer connection” tests
- Tax home test requires that taxpayer not have a tax home outside the possession for the taxable year
- Closer connection test requires that taxpayer demonstrate that he/she does not have a closer connection to the U.S. or a foreign country than to the possession
- IRS requires Form 8898 be filed by persons who move to/from possession for the year of move

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