The government's New Fiscal Plan proposes reestablishment of a new locally funded Earned Income Tax Credit (EITC) in order to:

- stimulate the percentage of participation in the labor market
- reduce poverty
- increase participation in the tax system
- shrink the informal economy
- reduce dependency on public assistance

To underwrite this new work credit, the plan proposes that the government reassign some $204 million per year, an amount that would be generated from economies and a revision of other incentives and credits. In addition, the plan projects some 288,000 tax units per year from among eligible taxpayers.

Proposal of a local Earned Income Tax Credit (EITC) is not new in Puerto Rico. In 2006, legislation was passed for an EITC to take effect in 2007, but it was eliminated in 2014. That credit was broadly applied, and it granted benefits to a large number of taxpayers. In its last year (2013), credits totaled $151.6 million to 505,962 tax units, some 48% of all taxpayers. The average credit was $299.70. it must be noted that there was very little stability in the parameters for the credit during the years it was in effect. For example, initially, in 2007, the maximum income for eligibility was $20,000, but by 2013 it was $27,500. The maximum benefit also rose, from $150 in 2007 to $450 in 2013. The constant changes that were made to increase the credit (five changes in seven years) had adverse effects: great variability in the program's cost and uncertainty among taxpayers.

The Tax Reform that has been presented includes a new Earned Income Tax Credit. For an evaluation and analysis of the previous EITC and this latest one, Espacios Abiertos commissioned a study from Dr. María Enchautegui. The study suggests seven important improvements over the previous EITC:

- Increase the maximum income for eligibility, to range from $20,500 to $42,000, depending on whether the taxpayer is married or not and whether there are dependents;
- Increase the range of maximum benefits, from a minimum of $300 per year to a maximum of $2,000;
- Increase the average benefit per participant, which according to the government's projections will be $525.30 per year;
- Focus on distinguishing beneficiaries by civil status (married or single) and the number of dependents, with the work credit increasing as the number of dependents increases;
- Allow a range of income rather than a single point at which the taxpayer can receive the maximum benefit (in this way there are fewer incentives for recipients to report lower income

than they actually earned or even to work less than they potentially could in order to receive the maximum benefit);
- Grant a higher EITC than the previous one for tax units with dependents;
- Allow self-employed individuals to qualify for the EITC when authorized by the Secretary of the Treasury (thereby allowing individuals transitioning toward self-employment to continue to qualify for EITC benefits).

The design and implementation of the new EITC promises to be a step in the right direction in achieving the public policy objectives of this incentive, and for the island's working class.

However, given the current financial crisis faced by Puerto Rico, it is important that the new earned income tax credit incorporate the lessons learned from the prior EITC. Among these lessons, the first is that:

- Although the objective of the EITC proposed now, like that of the prior one, is to reach a large majority of taxpayers, the credit actually has a potentially lower impact. This is because the average credit will be less (though for a larger number of people) than if it were concentrated—with the important objective of reducing poverty among children—on social groups such as families with dependents. This more concentrated application would provide relief to those working families and, in turn, would incentivize participation in the labor force among a sector in which the effectiveness of an EITC has been demonstrated in a wide range of academic studies and scientific evidence.

Other important lessons are the following:

- Possible interactions with other proposed changes in the current tax reform should be taken into account in order to precisely determine the program's costs and benefits;
- The incentive's design should be stable, so that individuals who might possibly receive it are able to plan their labor offering with greater certainty;
- It is important to have accurate projections of the program's costs in order to guarantee its continuance; and, lastly
- There should be recognition of objectives similar to those pursued by the government, such as avoiding the regressivity of the IVU, or tax on goods and services; encouraging participants in the PAN (nutritional assistance program,) and Temporary Aid to Needy Families programs to transition into the labor market; and trying to focus and intensify the incentive on single mothers with children.

Having identified the most significant lessons learned from the previous local EITC, the study includes six design recommendations in order to (1) ensure the program's sustainability; (2) achieve the greatest impact possible on the labor force, and (3) provide relief to the current levels of poverty faced in Puerto Rico. Those recommendations are:

- Concentrate the EITC on families with dependents under 18 years of age;
- Reduce the eligible range of income for single individuals without dependents in order to more strongly favor families with dependents;
- Adapt the salary parameters and structures to the income distribution in Puerto Rico;
- Establish a minimum income of approximately $3,000 to evidence attachment to the labor force;
- Ensure that single individuals without dependents qualify for the EITC if they are between 25 and 64 years of age; and, lastly
- Establish a plateau or wider range of income for the maximum benefit of taxpayers with dependents.

Lastly, the study concludes that in order for the new EITC to be successful and able to remunerate behaviors that the government wishes to incentivize, it is important that its design ensure its sustainability or budgetary viability over the next few years and that its potential impact be maximized in order to achieve the objectives that inspired it.