

Internal Revenue Service
memorandum

CC:INTL:0334-95
Br1:RACadenas

date:

to:Sharese Stevens, Examination Division CP:IN:E:2111
Office Of Assistant Commissioner (international)

from:George M. Sellinger, Chief Branch 1,
Associate Chief Counsel (International) CC:INTL:Br1

subject:Application of Earned Income Tax Credit to Puerto Rico Residents

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This in response to your memorandum dated March 13, 1995, concerning the I.R.C. § 32 earned income tax credit (EITC). Your memorandum states that wealthy individuals from Puerto Rico who may exclude Puerto Rico source income for federal income tax purposes under I.R.C. § 933, could appear to unjustifiably benefit from the EITC. We believe that there are some safeguards within the statute that prevent abuse of the EITC.

I.R.C. § 32 is intended to give an incentive to individuals of modest means to engage in income earning activity, i.e. to have a job and work. An "eligible individual's" principle place of abode¹ must be in the United States for more than one half of the Taxable year in which the EITC is claimed. I.R.C. § 32(c)(1)(A)(i)(A). Our hypothetical wealthy Puerto Rican, (assuming no children) must earn less than \$5,000 during his presence in the United States in order to get the EITC. I.R.C. § 32(b)(2).

We would question whether the I.R.C. § 933 exclusion would be applicable in a case where an individual lives and works in the United States for more than one-half of any given year. I.R.C. § 933(i) ~~applies to an individual who is a "bona fide resident of Puerto Rico during the entire taxable year**."~~ Without the I.R.C. § 933 exclusion, an individual's Puerto Rico source income will be used in the EITC "earned income phaseout" computation under I.R.C. § 32(b).

¹32(c)(3)(E) if the basis for claim the EITC is a "qualifying child" of the taxpayer, then such child's principal place of abode must be the United States.

I.R.C. § 32 and the regulations are silent on whether amounts excluded by Puerto Rico residents under I.R.C. § 933 are to be considered in the EITC income ceiling computations. I.R.C. § 32(c)(1)(D) prohibits individuals claiming the I.R.C. § 911 foreign earned income exclusion from also claiming the EITC².

There are various Code provisions that specifically cause Puerto Rico income excluded under I.R.C. § 933, to be included in income for other tax purposes, for example:

(1) I.R.C. § 86(b)(2) concerning the taxability of Social Security benefits provides for a special definition of "modified adjusted gross income" that requires accounting for amounts otherwise subject to exclusion from income under sections 135, 911, 931 and 933.

(2) I.R.C. § 135(c)(4) concerning exclusion of amounts received in redemption of United States Savings Bonds used to pay educational expenses likewise provides for a special definition of "~~modified adjusted gross income~~" that requires accounting for amounts otherwise subject to exclusion from income under sections 911, 931 and 933.

Since I.R.C. § 32 does not contain an analogous provision that refers to the I.R.C. § 933 exclusion, we conclude that the EITC computations would not include amounts excluded from United States gross income by Puerto Rico bona fide residents under that provision. This matter is assigned to attorney Ricardo A. Cadenas, who may be reached at (202) 874-1490 if you have any questions.

GEORGE M. SELLINGER

²A similar disqualification provision appeared in an earlier version of the statute that referred to I.R.C. § 931, but that section was repealed by the 1986 Act. Because of this change, it would appear that residents of Guam, American Samoa and CNMI who may exclude income under I.R.C. § 931 are not automatically barred from claiming the EITC.