

BACK TO WORK:

Freeing Puerto Rico's Labor Market from Stifling
Federal Intervention

1. Headed Toward A National Debt Crisis, Puerto Rico's Decline is Rooted In Decades Of Mismanagement

- Puerto Rico's debt now exceeds a staggering 100 percent of Gross National Product.

2. Without Reform, Puerto Rico's Economic System Could Be Driven Near Collapse

- Puerto Rico's outstanding public debt is one-half that of perennially distressed California, a state with more than ten times the population, earning several multiples of Puerto Rico's wages per capita.
- The population, economy, and assets to back up the pension system are all shrinking faster than the budget cuts can keep up with.
- A lack of economic opportunity is increasing the number of people dependent on government or leaving the island altogether.
- As the tax base shrinks and the proportion of dependents grows, more pressure is put on the island's already bloated and mismanaged public sector. More than \$60 billion of Puerto Rico's \$70 billion Gross National Product is public sector.

3. Puerto Rico's Troubles Have Been Perpetuated By High Minimum Wages And Welfare Benefits

- The combination of high minimum wages and welfare benefits appears to have frozen increases in productivity and income, killed the investment rate, and left Puerto Rico with one of the world's lowest rates of employment and labor force participation.

3. Puerto Rico's Troubles Have Been Perpetuated By High Minimum Wages And Welfare Benefits *(Continued)*

- This imposition of the federal minimum wage – which was set high in relation to Puerto Rico’s average wages – had the effect of dramatically diminishing the opportunities for employment in the formal economy.
- The simultaneous expansion of federal welfare benefits also reached levels that were far higher in relation to average wages than on the U.S. mainland, leading to far higher levels of welfare dependency.
- Within a few years of the introduction of food stamps, for example, half the population of Puerto Rico used them, accounting for 7.5 percent of personal income. In recent decades, federal welfare has accounted for nearly 30 percent of average income in Puerto Rico.
- Puerto Rico’s labor force participation rate is now less than 40 percent, and its employment rate is less than 30 percent, much of which is represented by public sector jobs.

4. The Implications For Puerto Rico Are Clear: Officials In The U.S. And Puerto Rico Alike Must Seriously Consider Ways To Make Both Minimum Wage And Welfare Benefits More Flexible

Recommendations

- **Relief from Federal Minimum Wage:** The government of any state or territory of the United States should have the authority to petition the U.S. Department of Labor for relief from minimum wage restrictions for areas where the employment rate is unusually low. The waiver should be granted except in unusual circumstances.
- *Any oversight board proposed in such a financial crisis should have the power to grant broad waivers from application of the federal minimum wage, and it should have the power to recommend policy reforms, including the reorganization of government institutions.*
- **Encourage Work Alongside Welfare:** Welfare benefits should be “flattened” by lowering benefits for those who are not working, and increasing benefits for those working at the bottom of the income ladder, so as to eliminate the “welfare cliff.”
- **Replace Income Tax with Sales Tax:** Until such time as federal transfer payments can be reduced to levels commensurate with mainland United States, the Puerto Rican government should transition from income tax to sales tax, so that its finances are not restricted to the current artificially constricted tax base.