

Dr. Mike Walden: You Decide, Should We Look At A Negative Income Tax?

By Administrator

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Income inequality, poverty, hunger, unemployment – these are all issues that have been with us for a while but became worse during the pandemic. The various stimulus bills tried to help, and currently Congress is considering legislature that would make more permanent changes to addressing the challenges.

However, it's not as if we haven't been engaged in helping alleviate economic stress. In my recently published book, *Real Solutions: Common Sense Ideas for Solving Our Most Pressing Problems*, I identified 92 individual poverty programs operated by 52 different agencies of the federal government and collectively spending almost \$1 trillion annually. Unfortunately, each program has its own rules and there can be little coordination among the programs.

There are also major administrative costs with these programs, usually at the rate of 15% to 20% of the total agency budget, with some as high as 40%! Obviously, this means less money going to recipients.

Another problem with several of the programs is the existence of a "tax cliff." A tax cliff occurs when additional income earned by the recipient results in a big drop in help from the program. Sometimes the value of assistance drops more than 100% for every extra dollar earned by the recipient. In other words, if the recipient earns an additional \$1000 by working more, they may lose more than \$1000 in program benefits. Obviously, a tax cliff reduces the incentive of the recipient to become economically self-sufficient.

What all this means is that not only do we need a commitment to helping households in poverty, but we also need to have a logical and coordinated process for delivering that help, and in a way that still leaves an incentive for the recipient to ultimately become self-supporting.

Fortunately, many say there is such a system, the idea of which has been around almost fifty years. It's called a "negative income tax," or NIT. Maybe it's time to revive that idea.

Here's how an NIT works. All households file an income tax return that lists their earnings and members of the household including dependents. The IRS compares the household

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earnings against the income deemed necessary to achieve some agreed-upon standard of living for the household. If the household's earnings exceed the minimum income standard, then they pay income taxes as usual.

However, if the household's earnings are less than the minimum income standard, then the IRS *sends* money to the household. The money could be sent in one lump sum, although a better approach would be monthly payments. Notice, this money is *not* a tax refund. A refund occurs when a household has paid too much taxes and has the excess returned.

Importantly, the NIT would be structured to preserve financial incentives for the household. This means if the household earns more, the amount of the funds received from the IRS would drop, but by much less than the extra earnings. Some plans recommend a reduction of 50 cents for every additional dollar of earnings.

Preserving the incentive to earn more would mean more households would qualify for payments from the IRS than are receiving some form of poverty assistance today. However, with the incentive to earn more, over time many of these households would move to self-sufficiency.

Two big plus points for the NIT are its low administration costs and flexibility. A similar program the IRS currently operates has administrative costs of only 1.5%. The NIT could be set up to quickly adjust to a household's circumstances. When a household's earnings change – either up or down – an interim income tax form could be filed allowing the NIT payments to be adjusted. Alternatively, employers could be required to send information about hirings, firings, and payment adjustments to the IRS.

Financial help via the NIT could be brought into the 21st century by issuing debit cards to recipients. The cards could be replenished each month, and when adjustments to the amounts are needed, they can quickly be reflected in the cards.

One reason there are so many federal poverty programs is that each addresses a different aspect of poverty, such as hunger, housing, energy costs, etc. The simplest NIT program would eliminate these categories and just provide households cash via the NIT debit cards. It would then be up to households to decide how to use the cash.

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While this would be the simplest and most straightforward approach, there are some who think controls should be placed on how recipients use public financial assistance. Such control could be accomplished by issuing several NIT debit cards, with the amounts on each card limited to certain expenditures, like food, housing, transportation, etc.

How does the NIT compare to a universal guaranteed income (UGI)? While there are many versions of the UGI, the most common gives recipients a certain amount of cash with no strings attached. Some versions provide almost everyone the cash regardless of their income. Obviously, the NIT is more restrictive as well as directed to those with the most need.

The political environment seems to be set for a renewed focus on economic challenges faced by a large part of our society, but in particular those who live in or near poverty. Now might be the perfect time to restructure how we provide help to those households. Should the idea of a negative income tax be part of that restructuring? You decide.

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