Which Way Forward for a Basic Income in the United States—Expand the EITC or Social Security? Paper presented at the Fifteenth Basic Income Earth Network Congress, McGill School of Law, Montreal, June 27-29, 2014. Almaz Zelleke, Visiting Scholar, NYU Robert F. Wagner Graduate School of Public Service, az22@nyu.edu. Rev. 7/2/14.

Note: Not for citation. This is very much a work in progress, and I welcome feedback to improve the analysis and proposal.[1]

Abstract: Recent attention to basic income in the U.S. prompted by the successful petition for a basic income referendum in Switzerland suggests the time is ripe for concrete basic income proposals. In this paper, I consider ways forward based on the expansion of existing income support programs—the Earned Income Tax Credit for low-wage workers and Social Security for senior citizens, among others. The EITC is a household-based negative income tax paid annually, while Social Security benefits are partially-taxable individual grants paid on a monthly basis. I discuss the pros and cons of these approaches for a subsistence-level basic income in the U.S.

1. Introduction

Interest in a basic income in the U.S. is higher than at any time since the 1960s, largely due to the media attention around the petition for a basic income referendum in Switzerland. As is often the case, attention is focused on the amount of a potential basic income (with the amazing figure of $2,800 a month having been introduced by the conversion of the suggested Swiss figure of 2,500 Swiss francs a month into U.S. dollars) and its unconditionality. Little attention in these discussions has been paid to how a basic income might be implemented. In particular, a basic income is often conflated with a negative income tax (NIT). Are there other forms a basic income might take? Are there important differences? Does a specific goal, such as poverty elimination, or reduction of inequality, lead to a preference for a specific form? If so, are there grounds for preferring a different form to an NIT? In this paper, I explore the ways a basic income might be implemented and consider the pros and cons of each.

[1] I wish to thank Clay Shirky for comments on this paper, along with the participants of the session of the BIEN congress at which this paper was presented, especially Julius Nadas, Jack Wagner, Borja Barragué Calvo, and Mark Witham.

2. Four Models for Income Supplementation

When designing income supplements, there are several important questions related to eligibility, size, and funding of the benefit. In terms of the form the benefit will take, there are two essential questions: whether the benefits are phased in, and whether they are the phased out, in relation to other income or assets. This provides four basic models for designing income supplements (*table 1*).

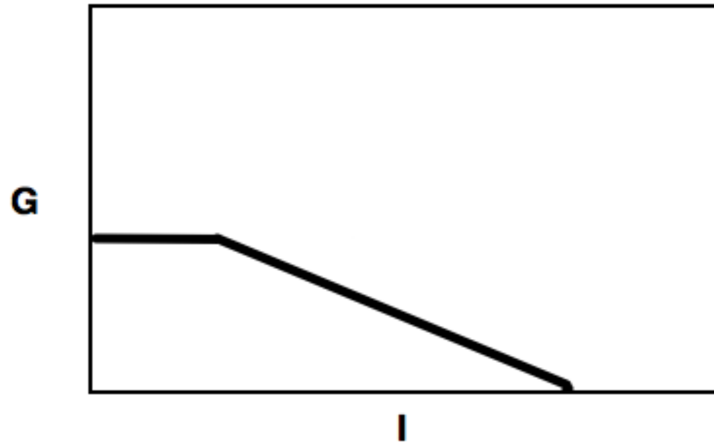
Table 1: Four Models of Income Supplementation

	No Phase In	Phase In
Phase Out	GMI (SSI, FAP, SS)	NIT (EITC)
No Phase Out	Flat Grant (Alaska PFD)	Tax Expenditures (Housing Mortgage Interest Tax Deduction)

SSI=Supplemental Security Income; FAP=Family Assistance Plan; SS=Social Security; EITC=Earned Income Tax Credit; Alaska PFD=Alaska Permanent Fund Dividend

2a. No phase in, phase out (*figure 1*) Under the first model, the maximum benefit is available to those with no other income, but phases out as income rises. Supplemental Security Income (SSI) in the U.S. is an income supplement in this form with no phase in, but a phase out as earned income rises. President Nixon's proposed Family Assistance Plan (FAP) also had this structure. Social Security benefits follow a version of this structure, with no phase in but with phase out of 50-85% of benefits as other income rises. Since this structure guarantees a certain amount of income before benefits phase out, let's call it the Guaranteed Minimum Income, or *GMI model*.

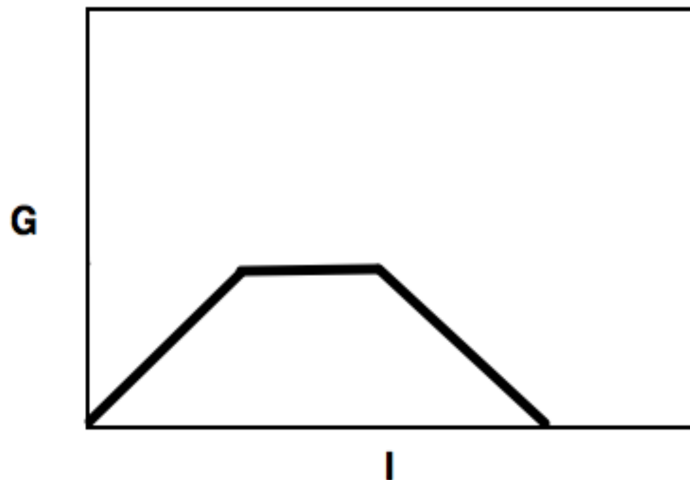
Figure 1: The GMI model



G=grant, I=income. Under the *GMI model*, G is a fixed amount that phases out at a flat tax rate as income increases.

2b. Phase in and phase out (*figure 2*). In this model, the benefit builds slowly along with earned income, plateaus once it reaches its maximum, and then phases out as earned income continues to rise. The Earned Income Tax Credit (EITC) in the U.S. is an income supplement in the form of an NIT that phases in and phases out. Let's call this the *NIT model*.

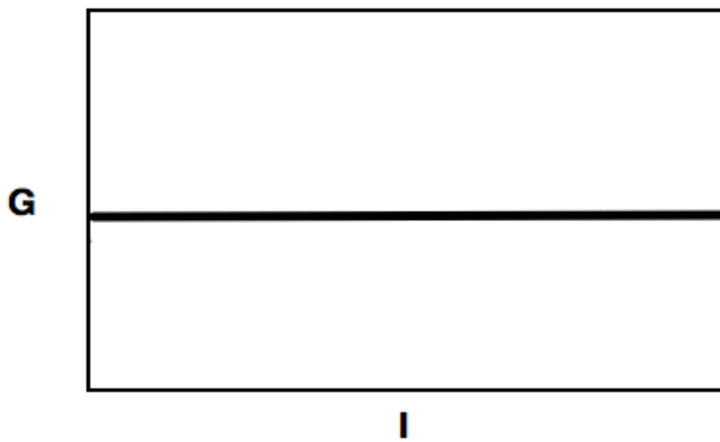
Figure 2: The NIT model



G=grant, I=income. Under the *NIT model*, G rises at a flat rate as income increases, plateaus, and then phases out at a flat tax rate as income continues to increase.

2c. No phase in, no phase out (*figure 3*) An income supplement in the form of a flat grant neither phases in nor phases out, but is available to all eligible recipients regardless of other income or assets. *The Alaska Permanent Fund Dividend* (PFD) is a flat grant with no phase in and no phase out. All Alaska residents receive the same amount regardless of other resources. Let's call this the *Flat Grant model*.

Figure 3: The Flat Grant model

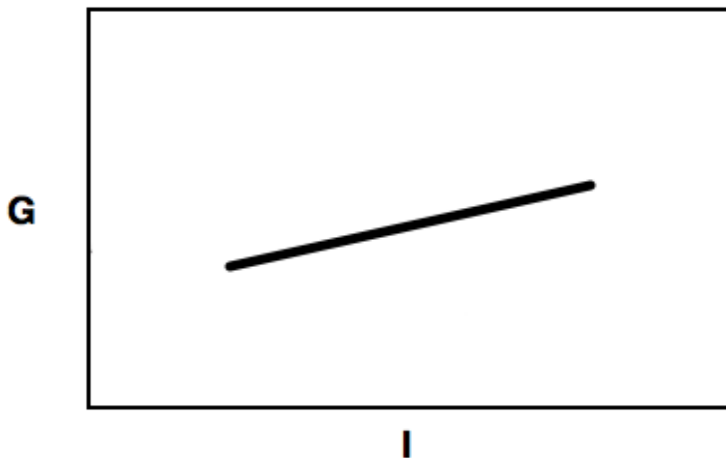


G=grant, I=income. Under the flat grant model, G is a fixed amount unrelated to other income.

2d. Phase in, no phase out (*figure 4*) Although we tend not to think of them in the same category as other income supplements, non-refundable tax deductions and credits can be considered an income supplement with a phase in, since income has to be high enough to be subject to taxation and, in the U.S., high enough to make itemizing deductions, rather than taking the standard deduction, worthwhile. Some tax deductions

in the U.S. are clawed back by the Alternative Minimum Tax (AMT), which could be considered a phase out, but the deduction for housing mortgage interest used to buy or improve a home (rather than for other expenses) is not subject to the AMT, and does not phase out, regardless of how high the taxpayer's income is. Let's call this the *Tax Expenditure model*. And since it clearly doesn't fit with the goals of a basic income, we can end our consideration of this model here.

Figure 4: The Tax Expenditure model



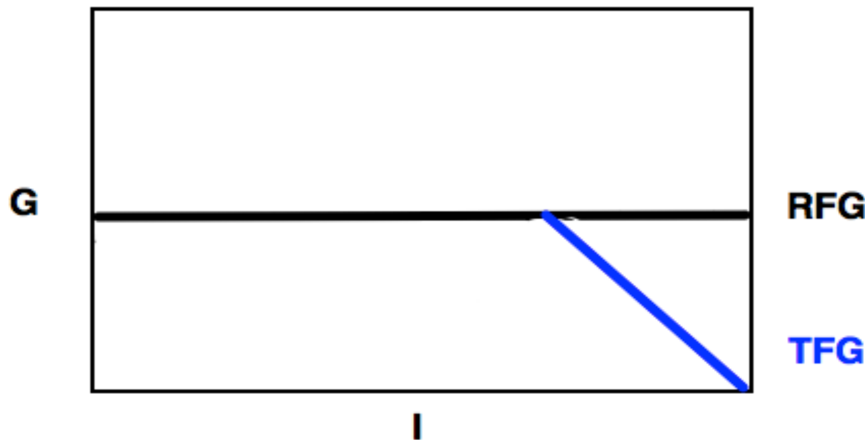
G=grant, I=income. Under the tax expenditure model, tax deductions and credits phase in at variable rates as income surpasses a threshold level, and may or may not phase out as income increases.

3. Variations on the Models

A further distinction is to separate those benefits for which increasing income causes a reduction in *benefits*, as in the case of the *NIT* and *GMI models*, and those for which the supplement itself is untouched, but *other income* is taxed at a higher rate to cause an *effective* phase out of the underlying benefit. For example, although Alaska has no state income tax, one could imagine a similarly flat grant benefit that is *effectively*

phased out for recipients with high income with, say a tax surcharge for incomes over $100,000 or $200,000 a year. At the federal level, there is unlikely to be an asset on the scale of the Alaska Permanent Fund that could fund a basic income. Therefore, let's refine the *Flat Grant model* into two variations (*figure 5*)—the *Resource-Financed Flat Grant (RFG)*, which is a flat grant that does not require taxation higher than the status quo ante to finance it, and the *Tax-Financed Flat Grant (TFG)*, which is itself untaxed but is wholly or partially funded by taxes on income above the flat grant itself. (Those taxes could be flat taxes of a certain percentage on all income or consumption, as under a VAT tax, or progressive taxes whose rates increase as incomes, assets, or consumption increases.)

Figure 5: Flat Grant Variations



RFG=resource-financed flat grant; TFG=tax-financed flat grant. Under the RFG model, the grant is a fixed amount independent of other income or assets; under the TFG model, the grant is a fixed amount that is *effectively* phased-out through taxes on other income, assets, or consumption once they increase past a certain level.

Finally, income supplements can vary according to whether they are scaled to family or household size, as with the EITC and SSI, or whether the benefits are

individually paid and the amounts are uniform, as with the PFD. Basic income is generally defined as an individual benefit, but given the family and household basis of the U.S. income tax code, it's worth considering whether this is an essential feature of basic income implementation, or whether it could be set aside for transition purposes, if not on a permanent basis. This question is beyond the scope of this paper.

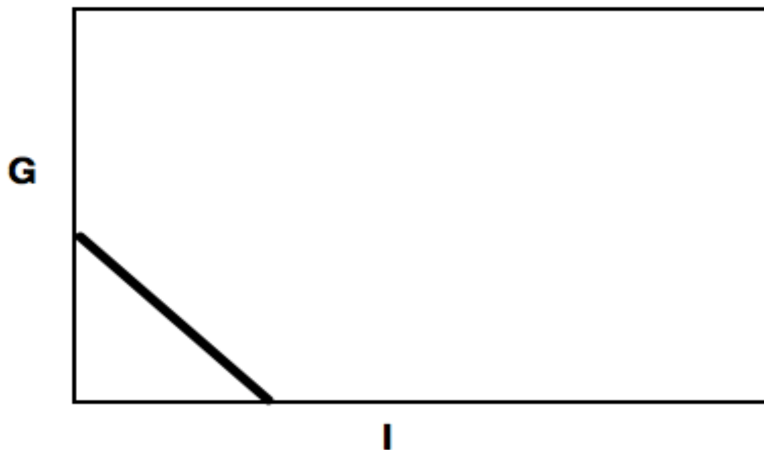
Now that I've outlined the basic distinctions, let's take a closer look at the various forms a basic income might take. While a basic income in the form of a flat grant like the PFD might be the preference of basic income advocates, without a sovereign wealth fund or other large and well-defined asset on hand to fund it, any significant basic income in the U.S. is likely to involve raising or reallocating tax revenue, and will lead to a desire to keep total costs down in order to keep taxes as low as possible. That will likely push the debate in the direction of a *GMI* or an *NIT*—an income supplement with a phase out, as incomes rise, and with or without a phase in. So let's take a closer look at the *GMI* and *NIT models* first.

4. A Guaranteed Minimum Income (GMI) or Negative Income Tax (NIT)

GMIs and NITs, as they were first discussed in the U.S., were designed to address the problems created by the structure of social assistance programs at the time. Social assistance benefits, because they were tied to a standard of need, were often more generous than what could be earned by wages by the lowest waged workers. And yet, because social assistance was meant to be a *substitute* for wages, rather than a *supplement* to them, social assistance beneficiaries faced dollar-for-dollar benefit reductions, or effective 100% marginal tax rates, when they began to earn income (*figure 6*). The problem was how to provide benefits in a way that encouraged, rather than discouraged,

employment, and the proposed solution was to phase out benefits at a lower marginal tax rate. This approach was termed a negative income tax (NIT), which at the time referred to both variants—what I'm calling the *GMI model*, with no phase in (*figure 1*), and what I'm calling the *NIT model* (*figure 2)*, with a phase in.

Figure 6: The Social Assistance model

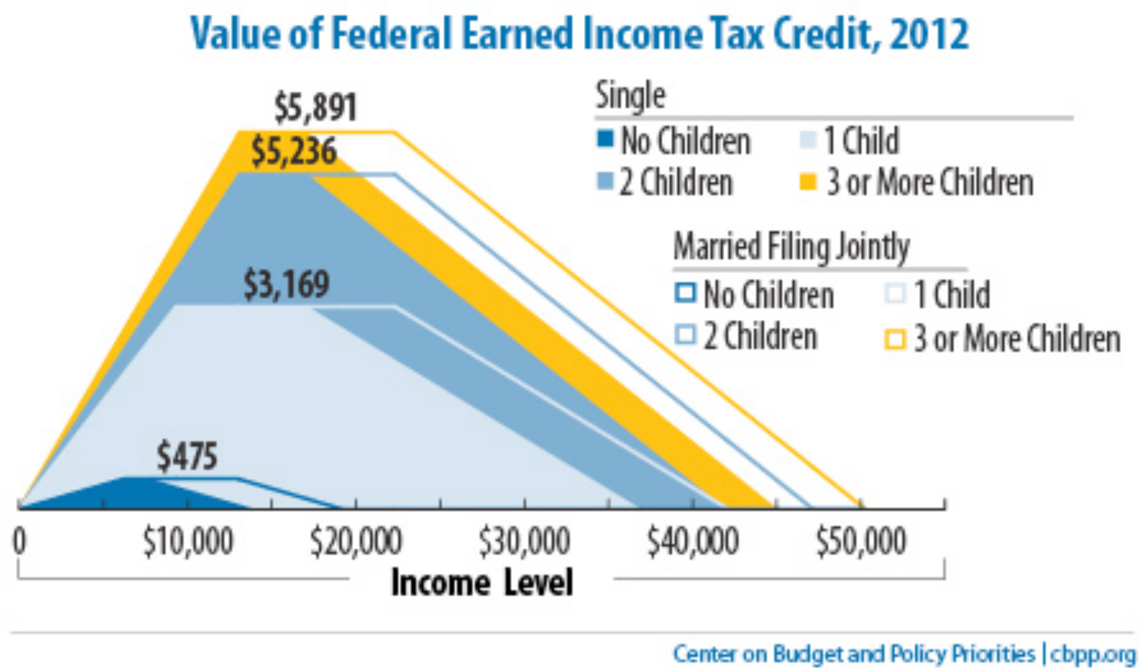


G=grant, I=income. Under the *social assistance model*, the grant is reduced by $1.00 for every $1.00 of other income.

President Nixon proposed a GMI in the 1960s that would have guaranteed a family with children a minimum income of $1,600, about half the poverty threshold for a family of four at the time. The phase out rate would have been about 40%, meaning a reduction of 40¢ for every dollar earned—a significant improvement over 100% tax rates, but still a much higher marginal tax rate than faced by low-income earners who did not receive the grant. FAP generated considerable opposition and did not pass Congress, but after its defeat Congress did enact the Earned Income Tax Credit (EITC), an NIT for low-income workers with children, which has been increased and expanded repeatedly in the decades following.

The inherent dilemma of the NIT is that the more generous the benefit and the lower the rate at which the benefit phases out, the higher the cost of the program and the more taxpayers fall under the program. On the other hand, targeting the benefit to only the neediest keeps costs lower, but requires steeper phase-outs, back in the direction of the 100% marginal tax rates. This dilemma is illustrated by the EITC (*figure 9*), which phases in slowly, increasing as earned income increases, and then phases out slowly, as income surpasses the poverty line adjusted for family size. The irony of its NIT design is that some benefits continue to be paid until income approaches, or even (for families with 3 children) surpasses, $50,000, but the amount of the benefit at that point is trivially small.

Figure 9: The Earned Income Tax Credit



This tradeoff is well known to basic income advocates, but it's worth parsing out the underlying assumptions of the *GMI* and *NIT* approach. Both models are based on a particular theory of economics, which holds that

- Employment alone provides fair or adequate income to *most* workers and their families
- Income subsidies can be limited to a relatively *small* group of workers for whom the market mechanism does not work (for reasons of racial discrimination, geographic location, preference for childrearing over work, etc.)
- The poor need to be incentivized to work for *more* than a subsistence level benefit
- This cash benefit is superior to other forms of subsidy (such as a higher minimum wage, a jobs program, etc.) because it is *either cheaper or less distorting to the market*.

This theory holds today for the EITC, which is widely heralded as having encouraged single mothers—a population that is thought to need incentives to go to work rather than remain on social assistance benefits—to enter the workforce and leave what is left of welfare in the U.S. SSI, on the other hand, acknowledges the lower likelihood of its eligible population—seniors and the disabled of any age—to earn enough to live on, but its meager benefit level (75-80% of the poverty threshold) and high phase out rates of 100% on unearned income, and 50% on earned income (above modest exclusion amounts) serves as a deterrent to feigning disability, failing to save for retirement, or shifting from low-wage work to SSI benefits.

5. The Flat Grant Models (RFG and TFG)

In contrast, the *Flat Grant* models are based on very different theories of economics. The *RFG* is based on the theory that

- All members of a political community are entitled to share in the resources of that community, regardless of their work effort or other income
- Work disincentive effects are either small, shared by all recipients regardless of their work effort or other income, or irrelevant, given that funding is independent of employment and the tax base.

The size of the benefit is based on the size of the asset, along with the time horizon over which the community wishes the asset to hold value and pay a benefit.[2]

The *TFG*, on the other hand, is based on a theory that is more directly in conflict with the theory underlying the *GMI* and *NIT models*. This theory holds that

- Employment alone *does not* provide a fair or adequate income to most workers and their families
- The market mechanism fails *many* workers for reasons unrelated to their own efforts or desert
- The poor need *no greater incentives* to work for more than a subsistence level (or even higher) benefit than those with higher incomes need to remain employed in high-paying jobs
- This cash benefit is superior to other forms of subsidy (a higher minimum wage, a jobs program, etc.) *because it maximizes the freedom of the individual recipients* to choose how to live.

None of this comes as news to basic income advocates. However, it does suggest that it makes strategic sense to explicitly distinguish basic income from the *NIT* and *GMI models*. While it is in theory possible to construct a GMI with a much lower phase out rate and a much longer "tail" of progressively increasing tax rates and decreasing benefit amounts, which might appear to make it indistinguishable from a progressive *TFG*, the rationales underlying the two models, at least as they have developed in the U.S., suggest that it would be strategically sound for U.S. basic income advocates to choose a model that makes its underlying rationale clear. As Brian Steensland argues in his exhaustive

[2] The *RFG* can also be a way of protecting an asset like clean air, by taxing those who pollute it in order to limit and, at the same time, share the profits of the negative externalities of polluting activities. In the U.S., a carbon tax and dividend seems like the most likely form of *RFG* that could be enacted, given the state laws that at least currently govern the exploitation of other natural resources such as oil and water. Contemporary Georgists have also suggested the use of land taxes to fund an *RFG*.

history of the U.S. guaranteed income debates of the 1960s,[3] and Karl Widerquist echoes in his review of the literature on the guaranteed minimum income experiments of the 1960s and 70s,[4] it is easy for the general idea of an income supplement to mean different things to different people, and then to generate opposition from across the political spectrum. For this reason, it might be best for basic income advocates to work as hard to distinguish basic income from the *NIT* and *GMI models* as advocates of those programs worked to distinguish them from social assistance, or the much maligned "welfare."

If I'm right about this, then part of our strategy has to be continuing to highlight the structural and systemic factors that lead to poverty and economic insecurity, as the left has long done. We now have more evidence than ever about this, thanks in large part to the kind of long-term analysis of income trends undertaken by Thomas Piketty[5] and his colleagues. Another part of the strategy has to be confronting the rhetoric about work incentives embedded deep in the *NIT* and *GMI models*. Charles Karelis provides a theoretical argument against the way marginal utility theory has been used against the

---

[3] Brian Steensland, *The Failed Welfare Revolution: America's Struggle over Guaranteed Income Policy* (Princeton University Press, 2008). See also Felicia Korhnbluh, *The Battle for Welfare Rights: Politics and Poverty in Modern America* (University of Pennsylvania Press, 2007).

[4] Karl Widerquist, "A Failure to Communicate: What (If Anything) Can We Learn From the Negative Income Tax Experiments," *Journal of Socio-Economics*, 34: 49-81.

[5] Thomas Piketty, *Capital in the Twenty-First Century* (Harvard University Press, 2014).

poor,[6] and Sendhil Mullainathan and Eldar Shafir recently published psychological research to back up Karelis' intuitions.[7]

On the other hand, after the instinctive resistance to the idea of unconditionality and the concern about work incentives, the next line of resistance to a basic income is inevitably the high cost of a universal grant, so the question of financing has to be addressed as well. Assuming that the *TFG* model is the way to go, what would a basic income look like?

6. The Tax-Financed Flat Grant (TFG)

The *TFG* form of basic income designed to eliminate poverty and maximize work incentives should look more like Social Security, and less like either the EITC or SSI. While the Social Security benefit amount varies from recipient to recipient, based partly on their earnings history (or that of their spouse or parent), once it is set it does not change according to income or assets, until other income reaches a threshold.[8] This reflects Social Security's structure as a contributory program whose benefits feel "earned" by those who receive them, and preserves incentives for covered workers to save additional funds for retirement and for those seniors who are able to keep working and earning income.

---

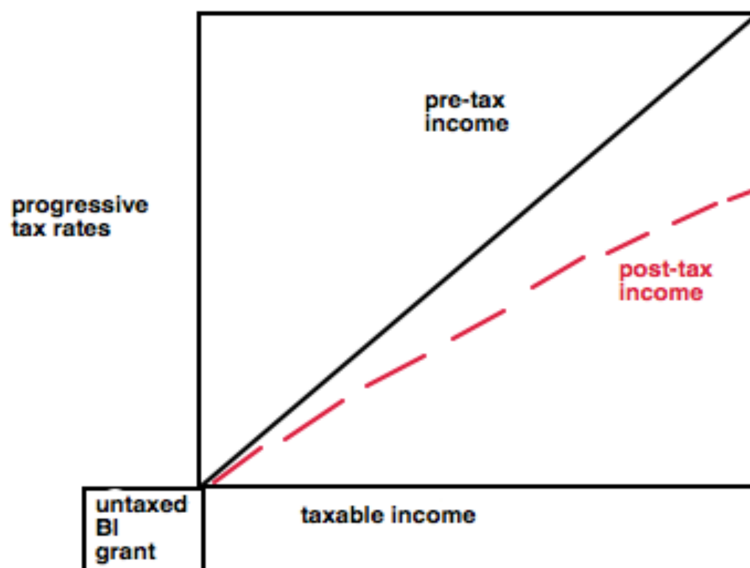
[6] Charles Karelis, *The Persistence of Poverty: Why the Economics of the Well-off Can't Help the Poor* (Yale University Press, 2007).

[7] Sendhil Mullainathan and Eldar Shafir, *Scarcity: Why Having Too Little Means So Much* (Times Books, 2013).

[8] Once other income reaches $25,000 for single tax filers, or $32,000, 50-85% of Social Security benefits are taxable at the same progressive tax rates that apply to income for all taxpayers.

A basic income designed on the *TFG* model would be a uniform, tax-exempt flat grant financed not by past contributions but by progressive taxes on all other income, earned or unearned (*figure 10*). Current tax rates on the first dollar of earnings are limited to the flat Social Security and Medicare payroll taxes of 7.65%, but with the income floor of an untaxed subsistence level basic income, progressive income taxes could begin on the first dollar of earnings as well; the basic income could replace the personal exemptions and standard deduction income disregards. This has two advantages. It would raise funds, but it would also make all workers contributors to the financing of the basic income as well as recipients of its benefits—the contributory model that is one of the elements of Social Security's political durability.

Figure 10: The Tax Financed Grant model



The basic income grant forms an income floor exempt from taxation; all other income is subject to progressive tax rates.

The advantages of this structure are

- The benefit remains in place as income fluctuates, maintaining the economic security of the benefit for precarious workers

- It removes the disincentive effects of the high marginal tax rates the GMI and NIT forms impose on low-income earners
- It restores progressivity to the tax and benefit system, under which marginal tax rates rise as income increases, rather than the other way around, as is currently the case in the U.S.

Following the Social Security approach, the *TFG* could be administratively separated from the tax system, and integrated only at the point of the annual tax filing, when the receipt of the grant is reported and used to determine the first dollar of taxable income. (High earners who know that their taxes due will be greater than their basic income grants will likely prefer to forgo the monthly payment in favor of claiming it as a tax exemption on their tax returns.) But there are reasons to prefer a full integration with the tax code.

One advantage of the tax-integrated approach is that it invites a reform of the tax code in the direction of simplification. If all citizens receive what is essentially a refundable personal exemption and standard deduction tied to an adequate minimum, what is the rationale for the myriad tax exemptions and deductions that complicate the U.S. tax code and that redistribute benefits *up* the income ladder? Some of the exemptions, like the lower rate on capital gains, are clearly designed to privilege the income streams particular to the politically powerful, but others, including the home mortgage interest deduction, the child tax credit, and of course, the EITC, are designed—but poorly so—to subsidize socially-approved investments on the part of low- and middle-income taxpayers. These tax exemptions are now estimated to cost the U.S. Treasury $1 trillion in foregone revenues. It is true that in the current political culture in the U.S. any reduction in exemptions is viewed as a tax increase by anti-tax activists like

Grover Norquist, author of the "Taxpayer Protection Pledge"[9] signed by the majority of Congressional Republicans. But the strategy of linking economic security for all Americans with tax simplification for all taxpayers might have the chance of breaking through the current political stagnation in Washington by uniting progressive Democrats on the left and classically liberal Republicans on the right.

7. How High Should the Basic Income Be?

For a basic income that eliminates poverty—which should be the first priority in the U.S.—the poverty thresholds present themselves as a target amount for a basic income. While there is widespread agreement that they are outdated and inadequate, it seems unrealistic that in the current climate a basic income could be set at a higher level, and evidence from the NIT experiments in the U.S. and Canada in the 1960s and '70s, along with more recent evidence from a study of Native Americans who received dividends from casino profits, suggests that even less than poverty threshold-level income supplements can have significant effects on well-being and opportunity.[10]

---

[9] The pledge requires Congressional representatives to "one, oppose any and all efforts to increase the marginal income tax rates for individuals and/or businesses; and two, oppose any net reduction or elimination of deductions and credits, unless matched dollar for dollar by further reducing tax rates." See atr.org/take-the-pledge.

[10] See Widerquist, "Failure to Communicate;" Evelyn L. Forget, "The Town with No Poverty: The Health Effects of a Canadian Guaranteed Annual Income Field Experiment," *Canadian Public Policy*, vol. 37, no. 3 (2011), pp. 283-305; E. Jane Costello et al, "Relationships Between Poverty and Psychopathology: A Natural Experiment," *Journal of the American Medical Association*, vol. 290, no.15. (2003), pp. 2023-29; and E. Jane Costello et al, "Association of Family Income Supplements in Adolescence with Development of Psychiatric and Substance Use Disorders in Adulthood Among an American Indian Population," *Journal of the American Medical Association*, vol. 303, no. 19 (2010), pp.1954-60.

The *TFG model* suggests a salient amount as a starting point for a basic income in the U.S. The current value of the personal exemption is $3,900, and the standard deduction, which applies not to individuals but to tax units, is $12,200 for married couples filing jointly. Dividing the standard deduction by 4, to get at a rough per person amount for a typical family, yields a little over $3,000 per person. A $7,000 per person basic income that goes to adults and children would not provide an income sufficient to meet the poverty threshold for a single person living alone, but it would exceed it for couples or joint householders and all families with children. The experience of Social Security suggests that popular universal benefits that start out at a low level will increase over time. Of course, the basic income could be targeted to the poverty threshold for individuals who live alone, or about $12,000 per person, but it seems unlikely that a basic income at that level would also go to children, which would leave our most vulnerable families—single-parent families—at disproportionate risk for poverty. [11]

To achieve a higher level basic income probably requires a rationale in addition the one based on poverty elimination, and a source of funding. Growing inequality in the U.S. is a problem that can also be alleviated by a basic income. Thomas Piketty provides compelling evidence that inequality cannot be reduced by the redistribution of income from earnings only, but requires a tax on capital as well. This could be addressed in one (or both) of two ways. The first may appeal to some of the same potential allies on the

[11] I make the argument for a basic income that goes to adults and children at an amount targeted to the poverty threshold for single-parent families with 2 or 3 children in "Targeting Benefit Levels to Individuals or Families?" *Basic Income Studies*, vol. 2, no.1 (June 2007), article 7.

right for whom income tax simplification is a goal. The second won't appeal to many on the right, but it's worth trying anyway.

The first option is a tax on the imputed income of capital. There is widespread agreement among tax specialists that the U.S. system of taxation of capital gains, even at a lower rate than earned income, distorts the behavior of owners of capital—particularly in a political regime like ours in which tax rates are changed fairly frequently.[12] Taxation of capital *gains*—the amount earned when assets are sold—but not of the value or earnings of the capital if they are unrealized—induces owners of capital to hold on to assets that might be better (in the sense of economic efficiency) sold. (It also taxes owners on gains that might be illusory—based on inflation, but not real gain.) Owners of capital are more likely to sell when capital gains taxes are decreasing, and to hold when they are increasing, encouraging them to lobby for reductions, even if they are for short windows only. A way around this problem that encourages the circulation of capital and its allocation to the highest yielding investments, is to tax on an annual basis an imputed earning of, say, 4% or 5% on the value of capital assets.[13] The other way is to forget about taxing capital gains and to impose a tax on the value of the capital itself, as Piketty has proposed.[14] Higher, progressive rates of taxation on capital could fund a higher basic income aimed at reducing economic inequality—something a subsistence-level basic income would have little effect on.

---

[12] See, e.g., Bruce Bartlett, *The Benefit and the Burden: Tax Reform—Why We Need It and What It Will Take* (Simon and Schuster, 2012); and C. Eugene Steuerle, *Contemporary U.S. Tax Policy*, 2nd ed. (Urban Institute Press, 2008).

[13] See Bartlett, *Benefit and Burden*, chap. 9.

[14] Piketty, *Capital in the Twenty-First Century*, chap. 15.

The second option would be to restore meaningful taxation of estates—or better yet, of inheritances. Ideally, the full amount of revenue from estate or inheritance taxation should be devoted to the redistribution of wealth through a basic income. Under the current U.S. tax code, estates valued at under $5.25 million face no estate tax at all. With the median inheritance for the baby boom generation estimated to be only $64,000,[15] it's clear that the high threshold for estate taxation benefits a small minority of inheritors. To have the strongest effect on inequality, taxation of estates should shift to taxation of inheritances, with lifetime exclusion amounts high enough to exclude most inheritances from taxation and to encourage bequests that distribute accumulated wealth more broadly.

8. Conclusion

A *TFG* financed by progressive taxes on income, capital, and inheritances would eliminate poverty and, depending on how progressive the tax rates are, have the potential to stop the trend of rising inequality in the U.S. and even reverse it. If the *TFG model* seems like a plausible approach to the implementation of a basic income in the U.S., the next step would be to estimate the tax rates required to finance a basic income at this level, but that is beyond the scope of this paper.

[15] Alicia H. Munnell et al, "How Important are Inheritances for Baby Boomers?" Boston College Center for Retirement Research, Brief no. 11-1, January 2011. The mean inheritance is estimated to be more than 4 times the median, at $292,000.