Universal basic income and child allowances in California

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Abstract

California has a higher poverty rate than any other state, and also more UBI pilots than any other state. In 2020, state legislators took California's UBI momentum to a new level by introducing a bill, AB 65, to provide $1,000 per month to certain low- and middle-income adults.

I present an analysis of the distributional and budgetary impacts of AB 65, as well as an examination of perverse incentives its targeting apparatus creates. I estimate that it would dramatically reduce poverty, but also cost more than the entire state budget of California. I suggest child allowances and young child allowances (monthly payments for each infant or young child) as more tenable steps toward UBI that California and other US states can take.

Introduction

California is in many ways the center of the national universal basic income conversation. It has more completed and ongoing basic income pilots than any state, including perhaps the most famous one in Stockton. Silicon Valley firms and workers have funded many of these trials and supported other cash transfer efforts like GiveDirectly, which companies like Google have long backed, and Andrew Yang's presidential campaign.

Policymakers have also sought to bring elements of UBI to California. In 2017, two state senators proposed reforming the carbon pricing system and rebating the proceeds as a dividend. In 2018, the California Democratic Party added UBI to their party platform. In 2020, Assemblymember Evan Low (who served as a national co-chair for Yang's presidential campaign) introduced a "CalUBI" bill. In December 2020, Low reintroduced the bill for the 2020-21 legislative session, as well as a bill to exempt income from UBI pilots from benefit programs, and Senator Dave Cortese introduced legislation to create a three-year UBI pilot for 21-year-olds exiting foster care.

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Other than the foster care bill, which passed the Senate 31-4 and is now on its way to the Assembly, these efforts have all faltered. California has still made strides in cash assistance—it has expanded its Earned Income Tax Credit match in recent years, and Governor Gavin Newsom has called for targeted cash assistance and state funding of guaranteed income pilots—but pilots are not programs, and means-tested programs differ fundamentally from UBI.

The CalUBI bill, which would have provided $1,000 per month to most California adults, approximated the full UBI vision, though its extremely high cost made it untenable and its means-testing would have created problems for administration and incentives.

In this paper, I describe the quantitative effects of the CalUBI bill, and offer a different approach which doesn't require state and local lawmakers to compromise universality amid budget constraints. A child allowance, whether for all children or even only infants, is an affordable yet impactful policy that can feasibly provide universal monthly cash transfers. As a state with a large budget (and currently an enormous surplus), and the highest overall poverty and child poverty rates in the country, California is well poised to seize the idea.

California's extreme economy

California is both rich and poor. It ranks #8 among US states on GDP per capita, and #7 on median household income. It also ranks #7 on income inequality,1 and accordingly, its poverty rate is higher than its GDP would predict, ranking #25 based on the Official Poverty Measure (OPM).

When using the Supplemental Poverty Measure[2] (SPM), however, California ranks #1 on both overall poverty and child poverty: 17.2% of Californians are in poverty, compared to 12.5% of Americans. In fact, California has ranked #1 on SPM poverty every year since the Census Bureau first reported it by state in 2011. That's because the SPM, unlike the OPM, adjusts for taxes, in-kind benefits (like the Supplemental Nutrition Assistance Program), and, most importantly for California, local housing costs. As a result of its housing shortage (California has the fewest housing units per adult of any state), housing in California is notoriously expensive—second only to Hawaii.

California also stands out in terms of taxation. Due to Prop 13 (1978), a ballot measure that limits property taxes, it ranks #35 on local property taxes. The state offsets that revenue loss with high income taxes—its top marginal rate is 13.3%, the highest of any state—and high sales taxes—its state rate is 7.25%, the highest of any state, and its state and local combined rate ranks #9. It is among the 41 states that tax capital gains as ordinary income, which raises significant revenue given its residents claim 8.1% of their income in capital gains, a higher share than all but three states. The net result is a state and local tax burden of 11.5%, ranking #8 across states.

[2] Poverty researchers generally favor the SPM over the OPM.

The state deploys these higher-than-average tax revenues for generous transfers. It matches the federal Earned Income Tax Credit at 85% for low income workers, a higher rate than any other state, and adds a Young Child Tax Credit supplement for qualifying families with children under age 6. Due to generously funding the Aid to Dependent Families Children (cash welfare) matching grant in the 1990s, California today gets more per child from its replacement, Temporary Assistance for Needy Families (TANF), than all states but New York and Vermont. And while California has not yet eliminated asset limits for TANF, it is among the 33 states to have raised income and asset limits for SNAP. It expanded Medicaid as quickly as it could following the passage of the Affordable Care Act, and overall spends more per capita on public welfare than 43 states.

Lack of welfare spending doesn't explain California's highest-in-the-nation poverty rate, but more inclusive and generous welfare programs can nonetheless ameliorate it.

AB65: the CalUBI bill

AB65 creates the CalUBI program, which provides $1,000 per month to Californians meeting these eligibility conditions:

(A) Is a resident, and has been a resident for the three most recent consecutive taxable years.
(B) Is at least 18 years of age.
(C) Is not currently incarcerated in a county jail or the state prison.
(D) Reported gross income that does not exceed 200 percent of the median per capita income for the eligible recipient's current county of residence, as determined by the United States Census Bureau.

Using data from the 2017-2019 Current Population Survey March Supplements, I estimate that 58% of Californians would be eligible for CalUBI. 77% meet the age requirement, 83% meet the income requirement,[3] 97% meet the migration requirement,[4] and 99.5% meet the incarceration requirement.[5] Providing the $12,000 payment to each of the 23.6 million eligible recipients would cost $283 billion per year.

[3] We interpreted a county's "median per capita income" as the median personal income among people with income greater than zero.
[4] The Current Population Survey only includes migration data from one year ago. 1.0% of Californians lived in a different state one year ago. To approximate the three-year requirement, we tripled the observation weights for this 1%; this also served to "age" the data from the 2017-2019 period to 2021, as it produces a total population estimate of 40.1 million. The University of Virginia Weldon Cooper Center for Public Service projects that California's 2020 population was 40.4 million.
[5] The Current Population Survey omits prisoners, so we used data from the Prison Policy Initiative, which estimates that 213,000 Californians were in state prison or county jail as of 2018.

Enacting the policy would reduce poverty by 83%, to 3.0%; for context, Minnesota currently has the lowest poverty rate, at 6.5%. It would also reduce inequality by 26%.[6] For these calculations, we assume that the CalUBI would not be counted as income for tax liabilities or benefit eligibility, though this may be unrealistic: Alaska's Permanent Fund Dividend does not affect eligibility for programs like Supplemental Security Income, but the payments are subject to federal income tax (Alaska has no state income tax).

However, the program would cost significantly more than the entire state budget, and it includes no funding mechanism to close that gap.

Perverse incentives from means-testing

The CalUBI means-testing approach creates perverse incentives in two ways: its immediate benefit cliff discourages people from working, and its geographic cliff discourages people from residing in lower-income counties.

As an example, consider a single resident of Santa Clara County earning $100,000 per year, let's call them Alex. Santa Clara County is home to Google, Apple, San Jose, and Assemblymember Evan Low, and its median personal income is about $53,500, second only to San Francisco County ($55,000) in California. With income below twice the median, Alex would be eligible for CalUBI. Their net income would be $100,000 minus $28,743 in federal, FICA, and state income taxes,[7] plus $12,000 in CalUBI, totaling $83,257.

Now suppose Alex is offered a job that pays 10% more. At $110,000 income, they exceed the $107,000 CalUBI threshold for Santa Clara County, so they no longer receive the $12,000 payment. As a result of their raise, Alex's net income *falls 7%* from $83,257 to $77,162. To get back to their original net income, they'd have to earn more than $120,000; if Alex can't get at least a 20% raise, they're better off with their current income.

Suppose that instead of taking a new higher-paying job in Santa Clara County, Alex considers moving to neighboring Santa Cruz County for a job paying the same $100,000. Where the median income in Santa Clara County is over $53,000, it's under $33,000 in Santa Cruz County. Alex would lose CalUBI eligibility, and their net income would therefore fall $12,000—a full 14%—if they were to cross the county border.

These welfare cliffs and discontinuities harmfully distort behavior. People like Alex will avoid earning too much money, or perhaps they'll favor a job with deferred compensation plans to lower their income, or they'll defer capital gains themselves, all to stay under the threshold in their county. They'll also avoid moving to lower-income areas, maybe choosing to commute

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[6] We measure inequality as the Gini index of the ratio between a person's poverty unit's (similar to a household) resources and its poverty threshold. The current value is 0.42, and under CalUBI it would fall to 0.31.

[7] This and other calculations apply SmartAsset's calculator.

from a more expensive area instead to retain CalUBI eligibility. This would increase geographic inequalities by raising high-income people's demand to live in high-income areas. Just as school district boundaries determine housing prices, county boundaries would do the same under this policy.

Universal designs

AB65's cliff could be mitigated by phasing the benefit out with income, as programs like SNAP and the Earned Income Tax Credit do, and as the negative income tax cousin of UBI does. Depending on the design, this could avoid Alex's quagmire and ensure that any additional dollar they earn raises their net income.

However, this phase-out would be a hidden tax: if the benefit phases out at 50 cents per dollar of earnings, that's equivalent to a 50% marginal tax, on top of normal taxes and phase-outs of other benefits. The array of means-tested benefits explains why parents around the poverty line currently face higher marginal tax rates than any other group in the country, often exceeding 50% and sometimes exceeding 100%.

Further, if the benefit is means-tested but distributed monthly, recipients would be required to report changes to their income regularly. This costs recipients of existing benefits time and explains some of the high administrative overhead costs. To support income reporting requirements for the American Rescue Plan's monthly Child Tax Credit expansion, the IRS is building a portal, an endeavor that's slowing the delivery of funds to low and middle income parents. The alternative is how refundable tax credits work today: calculated from income often a year or more in the past, without the ability to meet real-time needs, especially when financial circumstances change.

Other AB65 targeting provisions have drawbacks, too. County-level income thresholds will induce migration even with phase-outs. A three-year residency requirement conflicts with Californians' pro-immigration sentiment (the Alaska Permanent Fund Dividend only has a one-year requirement). And as our other research shows, excluding children misses an opportunity to improve lifelong development, and to cost-effectively reduce poverty.

Universality bypasses all of these issues. Universal payments don't discourage work through hidden taxes or cliffs; they don't require recipients to report income more than once per tax year; they can be efficiently distributed; they demonstrate inclusiveness toward newcomers; and they provide kids the resources they need to thrive.

Of course, universality is more expensive. Expanding CalUBI to each person in California would raise the cost from $283 billion to $472 billion—a sixth of the state's GDP and more than twice the current state budget. If funds could be conjured to pay for it, it would drive down the poverty rate to 1.2%.

But given a fixed budget, poverty is often minimized by spreading it across more of the population in smaller amounts. Spreading the $283 billion across each person in California would give each about $590 per month, and this would have virtually the same antipoverty impact as the original proposal.[8] That is, excluding children and newcomers offsets the progressivity of excluding higher-income people (not to mention the distortions).

Nevertheless, the $283 billion price tag makes AB65 unworkable as written. What policies could make progress toward its goals?

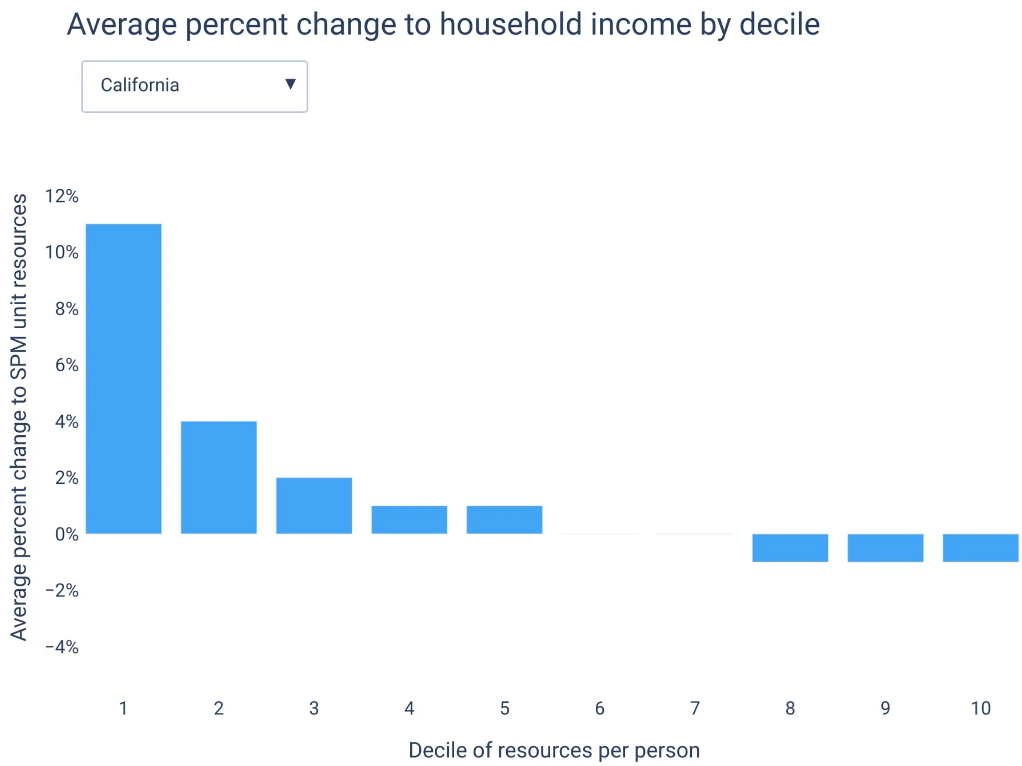
A California child allowance

Monthly cash transfers can efficiently relieve poverty and reduce inequality at the state level, but given to everyone, they're costly. Even a $100 monthly UBI would cost California $48 billion per year, more than a fifth of the current state budget.

A focus on children could be a tenable, effective starting point. Given 9 million of California's 40 million residents are under 18, a $100 monthly child allowance (cash payments given to parents for each child) would cost $11 billion annually. That's 0.4% of California's $2.9 trillion GDP or 5% of its proposed $227 billion budget.

Our child allowance simulation shows that this would be achievable and impactful in California. The state could fund a $100 monthly child allowance with a 1% income tax, cutting child poverty by 16%, adult poverty by 5%, and overall poverty by 7%. The bottom decile of Californians would see incomes rise by 11%, and on average only the upper three deciles would lose income, and only by under 1%.

[8] 3.08% vs 3.03%.



A number of revenue options could fund such a program:

- Adding to the income tax, as described in the above simulation.

- Applying California's expected $75 billion surplus in 2021. This wouldn't fund a permanent policy, but could fund a $100 monthly child allowance, plus a $100 monthly young child supplement, for a trial year.

- Taxing commercial property at market value would raise between $6.5 and $11.5 billion per year. A ballot measure to do this narrowly lost in 2020.

- Ending the mortgage interest deduction on second homes would raise $250 million per year. AB946 proposes to do this, though the revenue is used for a first-time home buyer program.

- Conforming parts of the state income tax code with federal tax code changes enacted as part of the 2017 Tax Cuts and Jobs Act; this would raise $1.7 billion per year.

- Replacing other benefit programs, such as CalWORKS (the state TANF program), Special Supplemental Nutrition Program for Women, Infants, and Children (WIC), the child component of CalEITC, and the Young Child Tax Credit.

- Instituting an estate tax, as was proposed in 2017 and which was estimated to raise between $500 million and $1 billion per year.

- Repealing other state tax deductions that primarily benefit high income households, such as the property tax deduction.

Or a California young child allowance

For greater affordability, California could focus on the group whose development is most sensitive to financial conditions, and whose needs are most costly due to childcare: young kids. Providing a young child allowance of $100 per month to each of California's 3 million Californians children under age 6 would cost $4 billion annually.

Washington and Sacramento have both already prioritized the needs of young kids: the American Rescue Plan's Child Tax Credit expansion provides an extra $50 per month to children under age 6 compared to older kids, and California provides a Young Child Tax Credit (YCTC) of up to $1,000 per year to families who qualify for the federal Earned Income Tax Credit and have at least one child under age 6.

Transforming the YCTC into a young child allowance of $100 per month per child would have several benefits, by:

1. Including families with no earned income who are ineligible for EITC
2. Providing more money for families with multiple young children
3. Avoiding adding a 20% marginal tax to qualifying families with income between the phase-out region of $25,000 and $30,000
4. Including children whose parents earn above $30,000
5. Enhancing the benefit by at least $200 per year for all current recipients
6. Meeting needs on a monthly basis
7. Potentially sending parents money proactively, rather than relying on families filing tax returns (many of whom don't have to file since they don't owe taxes)

Local effects

Young child allowances or infant allowances may appeal to local governments as well. With smaller budgets and limited capacity to verify income, local governments often lean on state and federal governments for social assistance, or provide services through ordeals (like food banks) as to proxy for need. Minimizing the touch points and administrative burden for distributing cash transfers will therefore benefit both the government and the recipients.

Infant allowances provide local governments opportunities to minimize those touch points by focusing them on places most infants go: hospitals. Rather than requiring recipients to enroll in human services agencies, local governments could partner with pediatricians, hospitals, and other pre- and post-partum care providers to provide new parents the information to enroll in the transfer. Without the need to verify income, all that would be needed is proof of birth and residency.

California has roughly one birth per 90 residents,[9] so a $100 monthly infant allowance for the first 24 months would cost an average of $2.7 million per year for a city of 100,000 people, where they would benefit over 2,000 infants at any given time. That's a cost on the order of guaranteed income pilots, and within the reach of local governments, especially if the state government provided grants to kick-start the concept.

Impacts of a $100 monthly child allowance

California's overall poverty rate is the highest in the country, and it's child poverty rate is as well: 20% of children are in poverty. Specific age groups also face extremely high poverty rates, such as 18% of infants and 19% of children under age 6.

A $100 monthly child allowance for all children in California would cost about $11 billion per year. This would reduce child poverty by over 25 percent, while also reducing adult poverty by 13 percent. More age-targeted options would have a lower cost, while still having significant impacts: $100 per month for children under age 6 (the group targeted with a larger Child Tax Credit in the American Rescue Plan) would lower poverty in that formative age group by more than 10 percent. And an infant allowance for the first 24 months would reduce infant poverty by 6 percent.

$100 monthly child allowance		Poverty cut (%)			
Age	Cost	0-1	0-5	0-17	18+

[9] 446,479 births divided by 39.51 million population.

0-1	$1.1 billion	-6.3	-6.3	-2.1	-2.0
0-5	$3.4 billion	-10.9	-10.6	-6.6	-4.2
0-17	$10.8 billion	-20.6	-21.2	-25.5	-13.1

Of course, more generous amounts would have larger effects. And just as the Affordable Care Act raised the age at which children could be on their parents' insurance, and as proposals to lower the Medicare age have become more prominent, child allowances that start at low ages could plausibly be expanded over time to include older ages. This is a fundamentally different foundation than starting with a means-tested program, which is politically difficult to expand later to specifically include higher-income people.

Conclusion

Many cash transfer studies show that they improve health, well-being, and educational outcomes, and that they don't reduce labor supply much or raise spending on vices. Guaranteed income pilots may add some precision to these estimates, but the policy conversation is ready to move beyond lotteries. If California is to make meaningful progress toward UBI policy, age-targeting may provide a clearer path than other ways of trimming cash down to size.