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by

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In the postwar period, and in the last few years in particular, we have made considerable progress against poverty. By means of broad economic growth and full employment policies, selective labor market programs, and income maintenance efforts, the number of poor households, as defined by the Social Security Administration, was reduced from 13.4 million (24 percent of all households) in 1959 to 11.5 million (19 percent of all households) in 1965.[1] The number of poor people fell from 39 million in 1959 to 30 million in 1966.[2] The poverty-income gap, that is, the difference between the money income of all poor households and what their money income would be if they were just over the poverty threshold, was $13.7 billion in 1959 and $11 billion in 1965.[3] By projecting these trends, we can estimate that in 1968 about 10.5 million households with 27 million people (14 percent of all people) will be poor. In that year the poverty-income gap will be about $10 billion, or 1.2 percent of the expected gross national product.

The Role of Transfers in Antipoverty Efforts

This progress in terms of the poverty rate and the poverty-income gap is due in some part to vigorous development of the American system of transfers. This is our public and private means for providing both money income and goods and services to persons on a basis other than their current productive activity. The grand total of such transfers in 1964 was $97 billion, $57 billion of which was in the form of health, education, and other services. The pre-transfer poor, who were 28 percent

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[1] Report of the Council of Economic Advisers, 1967, p. 140.

[2] Census study cited in U. S. News and World Report, Sept. 4, 1967, p. 64.

[3] CEA, *loc. cit.*

of the total population, received an estimated \$38 billion worth of fringes and transfers, over half of which came to them in the form of social insurance and public assistance. In return they paid \$8 billion in taxes and private contributions. Hence, they gained \$30 billion; this meant that while the pre-transfer poor started with only 5 percent of factor income, they ended up with 11 percent of factor income plus fringes and transfers net of the transfer costs.[4] This is a good measure of the size (though not necessarily the effectiveness)of our antipoverty effort in 1964. (Note that this was before the passage of Medicare, the new Federal aid to education provisions,and the Economic Opportunity Act.)

In 1964, money transfers of \$40 billion lifted 8.5 percent of all families out of poverty. It reduced the pre-transfer poverty-income gap by \$10 billion. Transfers were divided about equally between the poor and the non-poor; however, while they amounted to only 4 percent of the income of the non-poor, they were about half the income of the poor. The latter point is true even though only about half of the after-transfer poor families received a transfer. It is interesting that the several types of transfer payments differ widely as to their distribution. Most unemployment insurance and veterans benefits went to the pre-transfer non-poor, while public assistance went chiefly to those who remained poor after transfer. The benefits of the largest program, OASDI, were more evenly distributed, with relatively heavy emphasis upon those who became non-poor by receiving transfers. Money transfers do much more for small families than for large families. Persons in families of four or more persons are 55 percent of all persons poor before transfers and 62 percent

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[4] See the author's chapter, "How Much Does the American System of Transfers Benefit the Poor?" in Leonard H. Goodman, ed., Economic Progress and Social Welfare .(New York: Columbia University Press, 1966).

of those poor after transfers. They comprise only 36 percent of those taken out of poverty by transfers. Although such persons account for 51 percent of the poverty-income gap, they get only one-third of all transfers received by the pre-transfer poor.

Under this money transfer system the average payments, net of taxes, to pay for transfers, established a pattern that systematically related payment to pre-transfer income and family size. That is, for families with under \$1,000 of pre-transfer income, the average net transfer was \$810 for one-person families, \$1280 for two-person families, \$1650 for four-person families, and \$1935 for six-or-more-person families. The average net transfer fell off to zero at \$4000 for one-person families and \$5500 for four-person families. Those figures are averages. The idea of a guaranteed income plan is to assure a pattern something like this in terms not of averages, but of minimums. At the same time, it would be possible to correct the bias in the present system against the larger family. Note that the present system cut the pre-transfer poverty-income gap by \$10 billion. By adopting a carefully designed guaranteed income plan, we could cut the gap by another substantial sum and thereby hasten our progress against poverty.

The Guaranteed Income Idea

The guaranteed income is one name for a family of plans that includes such members as the reverse or negative income tax, the income-conditioned family allowance, and social dividends. It is a close relative of what some would call demogrants. The central idea of all these plans is that net benefits are payable on the basis of family size (or number of eligible family members) and the level of income. This is in contrast with both public assistance and social insurance.

Of the plans that have been discussed, the most sensible and purposeful is the one called "The Welfare-Oriented Negative Rates Plan."[5] Under this plan a family would receive 50 percent of the difference between its actual income and the poverty-line income for its family size. This means allowances would be paid as shown in Table 1.

Table 1

Net Allowances Received by Families of Three Different Sizes Under Negative Rates Plan

Family Income Before Allowance	Net Allowance Based on 50 Percent of Poverty-Income Gap: One-Person Family, Poverty Line of $1500	Four-Person Family, Poverty Line of $3000	Six-Person Family, Poverty Line of $4000
$ 0	$750	$1500	$2000
500	500	1250	1750
1000	250	1000	1500
1500	0	750	1250
2000	0	500	1000
2500	0	250	750
3000	0	0	500
3500	0	0	250
4000	0	0	0

A family would therefore be confronted by a new set of choices. The new choice situation is represented by Figure 1. Consider a four-person family earning $2000 (choice point A). After the plan is in effect that family would receive a net allowance of $500, and if it continued to earn $2000, would have an after-allowance income of $2500 (choice point B). On the other hand, if its income target was $2000, it could attain that by working less and earning only $1000 (choice point C). Or, if it decided to earn $2500, the after-allowance income would rise to $2750 (choice point D).

[5] See Christopher Green and Robert J. Lampman, "Schemes for Transferring Income to the Poor," Industrial Relations, Vol. 6, No. 2, February, 1967.

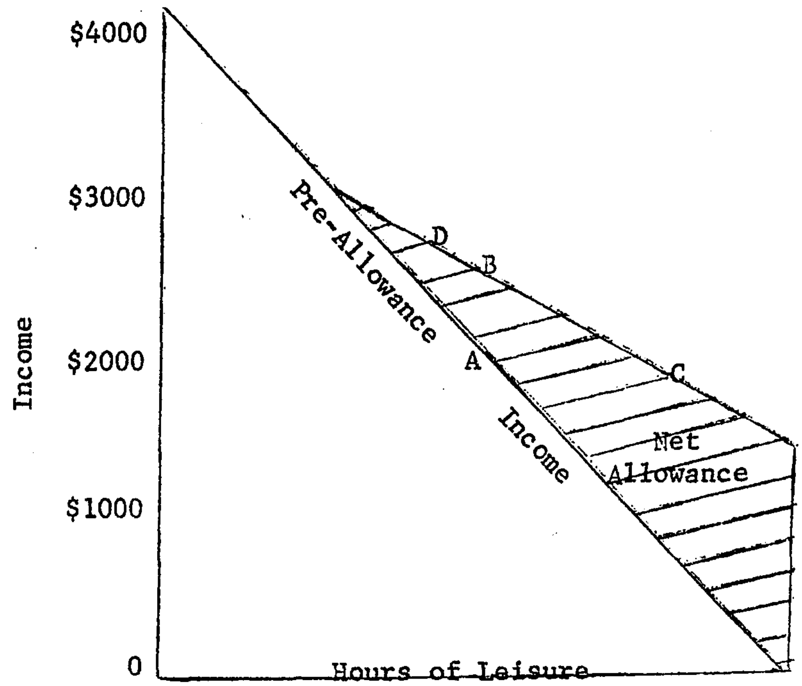

Figure 1

Income-Leisure Choice with Negative Rates Plan

Considerations in Designing a Guaranteed Income Plan

For purposes of calculating costs, we can assume that the typical family in this situation would elect choice point B, that is, the family members would do neither more nor less work because of the introduction of the 50 percent negative rates plan. However, it should be noted that there is a lively controversy among economists about what would actually happen, some maintaining that people would take more leisure, some that they would take less. There is very little controversy about the effect of a 100 percent rates plan, i.e., one that would fill 100 percent of the poverty-income gap. Such a plan would take away all monetary incentive for a low-income family to earn or receive income from property or transfer sources, and would thus make the pre-allowance poverty-income gap much larger than it now is and result in a greater than proportional increase in the cost of the plan. A 50 percent rates plan would have cost an estimated

$8 billion in 1964, without any correction for savings on public assistance. Doubling the rate to 100 percent of the poverty-income gap would more than double the cost. Indeed, in the opinion of this writer, it would more than triple the cost. For this reason, and because we don't want to penalize more severely than necessary work effort by either poor or non-poor people, it seems desirable to avoid tax rates on the poor of higher than 50 percent. That is, we would like to avoid allowances that amount to more than half the difference between pre-allowance income and the break-even income.

Another point to be noted about the benefit scheme shown in Table 1 concerns horizontal and vertical equity. Incomes after allowance would rise with family size. For example, one-member families earning $2000 would have $2000 post-allowance earnings, four-member families would have $2500, and six-member families $3000. Incomes would rise with earnings. In no case would a family that had a lower pre-allowance income end up with a higher rank in terms of post-allowance income, among families of the same size. In passing it should be noted that vertical equity is violated by the proposal of the Advisory Council on Public Assistance to allow relief recipients to receive a certain amount of income without reduction of relief payment. That proposal is reflected in the amendment to public assistance which recently emerged from the House Ways and Means Committee, that would "set aside" the first $30 a month ($360 a year) earned by a family on assistance and tax added earnings at 70 percent. This means that if a family of four has, say, an initial allowance of $2000, and wages of $2500, it can get a total income of $3002 at the same time that a non-relief-recipient family of four next door is working full time to earn $2500.

We have now referred to two considerations that are important in designing a guaranteed income plan. These are (1) preserving incentives to seek pre-allowance income, and (2) maintaining horizontal and vertical equity. Three other concerns are (3) paying money out only to the poor, (4) avoiding incentives to family disorganization, and (5) integrating the plan with the existing transfer-tax system.

We began this discussion by indicating that the goal was to close a substantial part of the remaining poverty-income gap, which is now on the order of $11 billion. In line with that, we may assert that the most efficient plan is the one that does the most to close the gap per dollar of expenditure. It is necessary to note that there is no plan that would close the $11 billion gap with $11 billion of expenditure. A 100 percent plan would close the gap, but would cost, as we have indicated, in the neighborhood of $25-$30 billion. A plan that sets the minimum allowance at the poverty line and taxes all pre-allowance income at a tax rate of 33 1/3 percent would close the gap completely, but at a cost of $50 billion, and would pay most of its benefits to people who are not poor. By contrast, the 50 percent negative rates plan would cost $8 billion, less about $3 billion reduction in public assistance (or a net cost of $5 billion), and would close half of the poverty-income gap.

To make sure that all of the benefits go to the poor, we need to be careful in defining the benefit-receiving unit and the income to be counted in determining the size of benefit. Spouses should be required to file jointly, and unmarried persons under 19 years of age and students under 22 years of age should be prohibited from filing separately. A person who files under this plan could not be claimed as a dependent on any other person's positive income tax return. Income to be counted in reducing the allowance should be broadly defined to include the total money income of all members of the recipient unit. Ideally, it should include not only earnings and property income, but also public and private transfers (but excluding public assistance) and imputed income from non-cash-yielding assets. One could exclude from eligibility families with a gross business or farm income of more than a certain amount, and perhaps families with very large assets or very high incomes in the previous year. This would preclude a certain number of "horror cases" in which benefits would go to rich people who, in some cases, presently pay no income tax.

We need to be alert to the possibility that even a carefully designed plan might encourage husbands to desert their families and might discourage widows from remarrying. For example, a father with a wife and three children, who earns $3000, presently pays no income tax and would get no allowance. If he deserted he would pay $394 in income tax, but, under the 50 percent rates plan, his wife might claim $1500. Or if a widow with two children who has no income but receives an allowance of $1250 marries a man earning $3000, which is $2606 after taxes, she would lose $1250 while he would save $394. The penalty is $856. While we do not know how much effect these incentives and penalties might have, they do act as a deterrent to considering rates higher than 50 percent, and recommend reducing the size of the guarantee for persons filing alone.

The other pertinent concern is to integrate the plan with the existing tax-transfer system. For example, what will happen to public assistance? We believe that the guaranteed allowances should be calculated without reference to public assistance and that public assistance benefits could be payable above the allowances as the states saw fit. At the present time, about 8 million of the total 30 million poor persons receive $6 billion in public assistance payments. Presumably, a substantial number of the 8 million persons would continue to get assistance payments, but in diminished amounts. The great innovation would not be with regard to these people, but rather with regard to the 22 million poor persons who do not now receive assistance.

Another integration problem exists in connection with the income tax. Where the poverty lines are higher than the combined exemptions and deductions under the income tax, a family might have to pay a marginal tax rate of 50 percent plus a marginal rate of 14 percent on earnings. This is an argument for raising exemptions and deductions for smaller families, but to do so would add to the cost of the plan to the Treasury.

Once the plan is in effect it would mean that a substantial part of the cost of increased expenditures of, for example, the Social Security program, would be offset by reduced allowances under the guaranteed income plan. Similarly, success in efforts to get increased employment at higher wages for the poor would be reflected in lower guaranteed income net allowances.

By this type of arrangement, the administration of the plan could be integrated with that of the income tax. A family would declare what it thought its next quarter's income was likely to be. If the expected income were so low as to justify an allowance, the Internal Revenue System would do two things: (1) it would mail out allowance checks to the family each month, and (2) it would withhold tax at the source at a rate of 50 percent. At the end of the quarter the family would make a new declaration, and either the allowance or the withholding rate could be changed to adjust for over- or under-payment in the previous quarter. A final settlement could be reached at the end of the year, at which time account would be taken of the fact that some people who started the year on one side of the poverty line ended up on the other and, hence, experienced both positive and negative rates under the income tax.

Alternative Proposals

A thoughtful person reviewing the proposal set forth above may very well ask: What are the alternatives? Among the more popular alternatives presently being discussed are: broadening and liberalizing public assistance, instituting a family or children's allowance, raising minimum social insurance benefits, and subsidizing employment of the poor by paying a wage subsidy to private employers or using the Government as the employer of the last resort. Each of these possibilities will be briefly discussed.

Extending public assistance--along with its 100 percent tax rate--to cover the working poor, would invite great difficulties. It must be emphasized that over half the poor families are headed by an employed person; 70 percent of poor families have one or more members in the work force. Most poor persons are poor because wage earnings are low relative to size of family.

Then is a family allowance the answer? Since only one-fifth of the children in the nation are poor, a straight family allowance would pay out most of its benefits to non-poor families. The plan reviewed above is more efficient and is, in effect, an income-conditioned family allowance.

Social insurance is not a promising route to early narrowing of the poverty-income gap because of the categorical nature and the wage-relatedness of benefits. If the minimum benefits are raised all benefits have to be increased, and most of the increased benefits would go to the non-poor.

Subsidizing employment of the poor opens a Pandora's box and is, if carried very far, perhaps the most radical of the proposals mentioned. It overlooks the fact that most of the poor are not unemployed and that most of the unemployed are not poor. It introduces the problem of equity--some persons having better incomes on publicly subsidized jobs reserved for the poor than others have on non-subsidized jobs. It would require a complicated system of selecting people for the jobs and of providing capital equipment and supervision. It is not clear how people would be separated from these jobs nor how subsidized employment would contribute to a reduced poverty problem over time.

Conclusions

For several reasons, then, we have tentatively concluded that a "welfare-oriented negative rates plan" compares favorably with some alternative next steps in the development of the American system of transfers. It would regularize the general income-family size benefit pattern in that system. It would correct the bias against larger families. It would preserve the incentive to receive pre-allowance income while maintaining horizontal and vertical equity. It would be efficient in the sense that all the benefits would go to the poor; hence all the proceeds would go toward a partial closing of the poverty-income gap, without significant encouragement of a widening of the pre-allowance poverty-income gap. Finally, it could be integrated with our existing tax-transfer institutions without undue difficulty and it could be managed by the Internal Revenue System.

Such a plan could be varied in several ways without making it a "fire-breathing monster." On the other hand, no variation could convert it into a panacea for all the nation's poverty and poverty-related problems. It is both the strength and the weakness of the plan that it offers a workable approach to partially closing the poverty-income gap.