

The personal exemption and the minimum standard deduction for a family of four amounts to only \$3,000. Thus, the two systems would overlap in the range between \$3,000 and \$4,000.

The answer to this problem is to give the family the option to choose the system under which its disposable income is higher. In the above example, it is obvious that all families with incomes of \$4,000 or less would choose the negative income tax. It turns out that some families with incomes above \$4,000 would also choose the negative income tax because the switch from the negative to the positive income tax precisely at \$4,000 would raise the tax rate on an additional dollar of income above 100 percent. At \$4,001, the positive tax for a family of four (according to the simplified tax table) would be \$144, leaving it with a disposable income of \$3,857 instead of the \$4,000 it would have had without the additional dollar of income. Paradoxically, the option to pay the higher negative income tax rate would yield a family of four a higher disposable income until its income exceeded \$4,400 in this example (see Figure 1). The exact location of this "tax breakeven point" need not concern the individual taxpayer because the final tax return would provide a reconciliation between the positive and negative income tax.

Figure 1. Illustration of a Negative Income Tax Plan for a 4-Person Family with a \$2,000 Basic Allowance and a 50 Percent Tax Rate

