

APPENDIX 16

FALLACIES OF THE NEGATIVE INCOME TAX

(By Henry Hazlitt*)

There is talk about guaranteeing every family an income of at least \$3,200 a year. If a family earned less than this, the government would make up the difference. The Gallup Poll recently asked people whether they favored or opposed such a plan. Only 36% of those questioned answered yes; 58% were opposed outright.

Their principal objection to the plan is that it would destroy incentives to work and earn. But some social reformers believe they could escape this result by what they call a "negative income tax." Instead of guaranteeing every family \$3,200 a year, they would pay every family \$1 for every \$2 that its own earned-income fell short of the \$3,200. To put it another way, they would give \$1,600 a year to every family with no earned-income, and then tax the family's first \$3,200 of self-earnings at a rate of 50%.

The advantage claimed for the negative income tax (NIT) is that it would not, like the straight guaranteed income, completely destroy the incentive of people to work and earn money for themselves. But the NIT merely substitutes a dilemma of its own. Either it must pay only half an adequate income to a family that earns no income, or it must pay twice an adequate income to a family that already earns an almost adequate income.

An orthodox relief program would pay the jobless head of a family, say, \$60 a week. If he then started to earn something, he would be paid simply the difference between that amount and \$60. Under the NIT principle a man who was earning nothing would also receive a relief payment of \$60 a week. But if he then earned \$30 a week on his own he would still get a \$45 payment (reduced by only \$1 for every \$2 earnings), bringing his total income to \$75 a week. If he was later able to earn the full \$60 for himself he would still be getting a relief payment of \$30 a week, bringing his total income to \$90. In fact, even if he succeeded in bringing his total self-earnings to \$118 a week he would still be getting \$1 a week in relief payment.

He would then be almost twice as well off economically as he would if he had always earned enough—say \$61—not to get on the relief rolls in the first place. This would be clearly inequitable to those who had never got on relief. The incentive to get on relief, and certainly to stay on relief, would be enormously greater under NIT than under the present system.

If we tried to escape this result by using the NIT formula only in part, and taking the man off relief, say, as soon as he was himself earning \$60 a week, we would get an even more absurd result. When he was earning \$58 a week under NIT, he would still be getting \$31 a week from the government, making his total income \$89. But if he then made the mistake of earning only \$2 more he would end up with a net loss of \$29 a week. So the negative income tax would create a tremendous positive incentive to get and stay on relief permanently.

The NIT scheme could avoid this preposterous result by paying a man with zero income only, say, \$30 a week, or only half as much as its own logic assumes that he needs to live on.

In addition to this special dilemma, the NIT has the fatal defects of the straight guaranteed income. By neglecting the careful applicant-by-applicant investigation of needs and resources made by the ordinary relief system, it would open the government to massive fraud, cheating and swindling. And it would also force the taxpayers to support a man regardless of whether he was making any effort to support himself.

*The Henry Hazlitt Column, Los Angeles Times Syndicate, Los Angeles, Calif.