In our modern, interconnected world, we are continually bombarded with new concepts, policies, methods, and initiatives. How do we make sense of these new ideas? Are they viable? Are they worth pursuing? In this column, guest authors will describe, analyze, and evaluate new ideas emerging in their areas of expertise.

**Universal Basic Income**

Entrepreneur Andrew Yang has proposed a Universal Basic Income (UBI) benefit as part of his presidential campaign. His proposal would give every citizen over age 18 a benefit of $1,000 per month, providing an income guarantee close to the individual poverty level. While many like the idea of a minimum income guarantee, others have raised concerns over work disincentives and how the program would be financed. This column explores some of the positive and negative impacts of Yang’s UBI proposal.

**Motivation for Universal Basic Income**

Andrew Yang points out that our labor force participation rate is currently 62.7%, lower than we have experienced since the 1970s. He further claims that a third of all working Americans will lose their jobs due to automation during the next 12 years.

The labor force participation rate is somewhat misleading. It measures the percent of the population over the age of 16 that is either working or actively seeking employment. Those that are not working or actively seeking employment include retired individuals, homemakers, and those that have given up seeking employment. As more and more baby boomers retire, this naturally causes the participation rate to fall.

If Yang’s predicted job losses are true, that could lead to an increase in those who give up seeking employment. Economists call this structural unemployment, meaning that there has been a structural shift in the types of jobs available, with displaced workers lacking the skills needed for these new jobs. These workers can re-enter the labor force, but it often requires education and training to develop the skills currently in demand, so it is often a slow transition. Historically, this is not a new claim. We have seen similar concerns dating back to the innovations of the industrial revolution. While each wave of innovation does create employment shifts, labor markets seem to recover more quickly than expected.

**Work Incentives**

One of the problems with traditional welfare programs is that they naturally create some disincentives to work because employment leads to reductions in not only cash assistance, but other forms of assistance such as food stamps and Medicaid. By making the benefit available to everyone, this would remove such disincentives as well as any welfare stigmas that might reduce participation.

However, providing a benefit to all that is not currently available would create new disincentives to work. Consider a two-income household where one partner is the primary earner, and the other partner works primarily to afford extras such as children’s activities or vacations. If the couple is able to receive a $24,000 benefit, that could lead the secondary earner choosing to leave their job.
Financing
Andrew Yang has proposed a 10% value-added tax (VAT) to fund the program. Other current welfare programs such as food stamps and disability would be replaced by UBI. Funds currently flowing to those programs would be used to fund UBI. There would also be some administrative savings as UBI would not require any form of screening to verify who is eligible for benefits.

Many Americans don’t know exactly what a VAT is, aside from the fact that they are widely used in other countries. VATs are essentially the same thing as a sales tax, and a federal sales tax would be easier to implement since many states already have sales taxes in place. A 10% sales tax would cause prices to rise, but by less than the full 10%. Prices for necessities would rise by nearly the full 10% as these are products that we will continue to purchase even when prices increase. Prices for luxuries would see much more modest increases as many consumers would simply stop buying them as they become more expensive. Because prices increase more sharply on necessities, sales taxes tend to place a greater burden on low-income groups. As is done in most states, Yang would exempt food and clothing from the VAT to reduce some of the negative impacts.

On the positive side, sales taxes tend to increase saving, which is consistently lower than most economists consider appropriate. Because the tax is only made for purchases, it rewards savings by avoiding the tax on that portion of your income. However, this also forces a greater burden on low-income groups. As is done in most states, Yang would exempt food and clothing from the VAT to reduce some of the negative impacts.

Alternative Policy: Earned Income Tax Credit expansions
While there are certainly some positive impacts of UBI, I do not support Yang’s proposal primarily because of the high cost of providing a benefit to everyone. In addition, it isn’t clear what the net benefit would be for different income groups. Clearly, low income groups would benefit. It also seems that high income groups would have a lower burden from the tax due to higher savings rates. If the program is self-funding, this implies that there would be a higher relative burden on the middle class.

Instead, I would propose an expansion of the Earned Income Tax Credit (EITC), which currently provides benefits to single individuals with earnings up to $15,270 and families with 3 or more children with earnings up to $49,194. The EITC supplements earnings, creating positive work incentives for participants. It also would not have the disincentives for work for partners earning secondary incomes. However, there are still some potential disincentives as the benefits are reduced or phased out as earnings increase.

Another benefit of the EITC is that it doesn’t have welfare stigmas that are associated with traditional welfare programs. All the paperwork flows through the federal income tax returns and makes filing taxes only slightly more complicated.

Further information on Andrew Yang’s UBI proposal can be found at www.yang2020.com/what-is-freedom-dividend-faq.

Further information on the EITC can be found at www.taxpolicycenter.org/briefing-book/what-earned-income-tax-credit.