Wages are stagnating, robots are taking our jobs. This Democrat has a $1.4 trillion solution.

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Northern California Rep. Ro Khanna (D-CA) plans to unveil Wednesday legislation that will give substantial tax credits to low- and middle-income Americans. His goals include combating two of the most troublesome aspects of the American economy: income stagnation within the working class and rising instability caused by a shift from secure jobs with benefits to jobs (or gigs) lacking them.

More broadly, he's motivated by surging interest in Silicon Valley in using income redistribution as compensation for the costs imposed on workers by increasing automation.

The ambitious proposal from the freshman representative, which could cost $1.4 billion over 10 years, would turbocharge a program that has enjoyed an unusual amount of bipartisan support since it was introduced in 1975: the Earned Income Tax Credit.

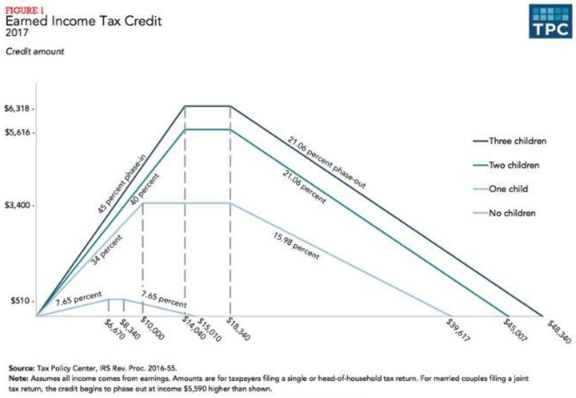
Sen. Sherrod Brown (D-OH) will introduce similar legislation in the Senate.

The EITC supplements the pay of low-earning households and incentivizes low-income people to work. (It's designed "to make work pay," as President Bill Clinton famously put it.) For tax year 2016, 26 million people received about $65.6 billion in credits.

The program works by providing refundable credits that begin with a small subsidy for the first dollar of earned income and gradually rise until — for a two-parent family with two kids — the subsidy reaches a maximum of about $5,600 for an income of $14,000. It stays at that level till income hits about $18,300, then begins to phase out.

Families with three kids get a little more, those with one a little less. Childless families get a very skimpy credit.

It's a little tricky to describe in words; below is a graph from the Tax Policy Center showing how the current credit phases in and out with various family sizes.

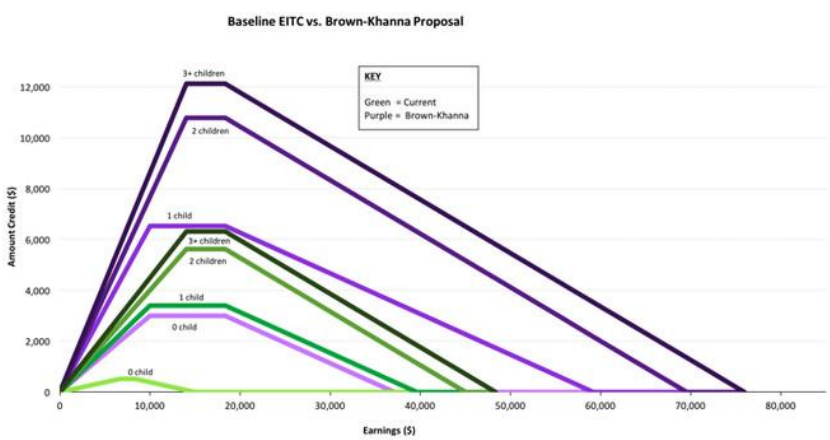


The current Earned Income Tax credit *Tax Policy Center*

The Khanna-Brown proposal, the Grow American Incomes Now Act (GAIN), would roughly double the current EITC for families with two kids, bringing it to a maximum of about $10,800. The proposal would continue the policy of being less generous to childless workers, but it would quintuple their maximum credit, taking it from $510 to $3,000.

"The large expansion of the EITC I am proposing would compensate for the loss of wages of the bottom 20 percent of wage earners since 1979," Khanna told me, before his official announcement, scheduled for 12:30 pm Wednesday.

To give a sense of the level of subsidy we're talking about, under Khanna's proposal, a family with two kids earning a salary of $18,000 would get a credit worth more than $10,000 — a salary bump of some 55 percent.



How the Khanna-Brown plan compares to the current EITC (proposed credits are rendered in purple)

Khanna knows the bill isn't likely to pass a Republican-controlled Congress, but he's hopeful that it could be serve as the basis of a Democratic plan to tackle inequality and the challenges of the new economy as we head toward the 2020 presidential race. And he thinks it will resonate with voters more than Republican tax cuts.

"There are a variety of ways to pay for such a large expansion of the EITC, including a financial transaction tax, closing special interest tax loopholes, and raising revenue from the top 1 percent of earners," he recently explained. "I'm happy to have that conversation with my colleagues in Congress. I also look forward to learning more about the House Republican offsets to pay for their $5 to $7 trillion worth of tax cuts for corporations and the very wealthy."

The general idea of expanding the EITC is not new: **House Speaker Paul Ryan and President Barack Obama last year both floated EITC increases**, though both were much more modest.

The EITC began as a small experiment in the 1970s. Now it's a major anti-poverty program.

The EITC has undertaken an amazing journey from a wonky program introduced as a way to subsidize low-wage earners in the 1970s to one of the pillars of the American welfare state. It lifts an estimated 65 million people out of poverty. And Khanna's proposal would take it to an entirely new level.

The tax credit enjoys broad bipartisan support: Liberal economists like its impact on reducing poverty through redistribution, while libertarian economists like it both because it spurs some people — particularly single parents — to enter the workforce and because it is inexpensive to administer. Overhead costs are under 2 percent, compared to 20 to 25 percent for a program like food stamps.

The policy grew out of debates in the 1960s over the best ways to combat poverty. The libertarian economist Milton Friedman championed a negative income tax, which he thought could outright replace many welfare programs of the day. A negative income tax would have, like the EITC, boosted the pay of low-income workers, but it would have gone farther by issuing payments to people with no income. (It would therefore, unlike the EITC, be a form of guaranteed income.)

President Richard Nixon went so far as to include a negative income tax — for families with children only — in his Family Assistance Plan of 1969. It passed the House but died in the Senate.

The idea of a negative income tax was fought by legislators who worried about subsidizing the "undeserving poor" as well as discouraging work. They pushed instead for a "work bonus" that would be reserved only for the employed. The Earned Income Tax Credit was passed and signed under President Gerald Ford. It has been expanded several times since — most notably during the 1986 tax reform, under President Ronald Reagan, and during President Clinton's first term.

Economists and other analysts have identified several benefits of the program:

- One study found that a $1,000 increase in the EITC **boosts** employment a sizable 7 percentage points, and reduces the proportion of families below the poverty level, after taxes and other transfers, by 9.5 percentage points.
- A review of several studies of the effect of the EITC **found** that its approach of giving low-income parents a cash transfer "produces substantially larger gains in children's school achievement per dollar of expenditure than a year of preschool, participation in Head Start, or class size reduction in the early grades."

- The liberal think tank Center for American Progress **estimates** that an EITC increase, even one on a scale much smaller than Khanna's, could produce knock-on societal benefits of $1.7 to $3 billion, including crime reduction.

There is a body of research suggesting that giving the poor, or working poor, cash rather than specific services can be a more effective form of support. One longstanding concern about the EITC, however, has been that it delivers its payment in one lump sum, as a tax refund. That could invite splurges (or lead to challenges with respect to "income smoothing," in the economic jargon). But one study by the Federal Reserve Bank of Chicago found that the poor used their windfall wisely: They bought cars they needed for work, for instance.

"Given the crucial role of access to transportation in promoting work, this leads to the conclusion that recipient spending patterns support the program's prowork goals," the study found.

On the other hand, some economists find that the EITC discourages work for lower-earning spouses in families that are in the "phase-out" part of the tax-credit curve. It also does not help people who either can't find work or whose work involves nonmarket activities, like child care or elder care.

Some conservative critics point to a fairly high rate of error in EITC claims (20 to 25 percent), some of which surely includes some fraud: Determining which children count as "qualifying" can be tricky, particularly in nontraditional families, and the IRS is not well equipped to vet such claims.

"The credit creates a modest increase in workforce participation by single mothers," write the Cato Institute's Chris Edwards and Veronique de Rugy, "but that benefit is outweighed by the work disincentives during the phase-out range, billions of dollars of errors and fraud … and the damage caused by the higher taxes needed to fund the program." They conclude that the program should be cut back, not expanded.

A proposal tailored for modern — or post-industrial — economic challenges

Silicon Valley these days is full of heady talk about basic income programs, spurred by worries about automation, under which the government would guarantee a certain floor salary even for people who cannot find work. Khanna's program is not a basic income, but it could conceivably be a first step in that direction.

A vastly bigger EITC would not help if you lost your job to a robot, but it could help if automation relegated you to a lesser-paying job.

"Robots and automation may lead to new jobs, but these jobs often pay less or are not unionized or are part time," Khanna told me.

A foreshadowing of the automation trend can be seen in the offices of large tech companies, which tend to produce less employment than a previous generation of employer. Facebook has a workforce **roughly 5 percent the size of General Electric's**, for example (17,000 versus 300,000). Uber may have given millions of drivers gainful employment, but they lack the protections of worker benefits.

Khanna presents his program as combating a range of modern economic ills, with wage stagnation near the top of the list. From 1948 to 1973, productivity rose by 97 percent and hourly compensation rose about 91 percent, according to the Economic Policy Institute. Over that period, workers were capturing an impressive share of productivity gains.

From 1973 to 2015, however, productivity slowed a bit, rising at 73 percent, but hourly compensation cratered, rising 11 percent.

A bigger EITC, or a similar kind of work-conditional cash transfer, could counterbalance some of those losses.

Andrew McAfee, an MIT economist and author of a new book on automation, ***Machine, Platform, Crowd***, has expressed enthusiasm for a larger EITC. “The EITC is a direct incentive to enter the labor force, and to work more hours — up to a limit. The research is pretty clear that it works as designed,” he told me. “So I support expanding it: making it both bigger and available to more people.”

Khanna also presents his plan as a response to the rise of the “gig economy” an issue that overlaps with, but is not identical to, both the automation and wage-stagnation questions. It would help the growing legions of independent contractors, like Uber drivers, who aren't protected by minimum wage laws.

The economists Alan Krueger and Lawrence Katz **estimate** that almost all new net jobs have come in the gig economy, expanding from roughly 9 million to 14 million jobs between 2005 and 2014. Though gig workers are earning a paycheck, they are stranded without with the safety net that benefits can provide.

Supplementing the income of such workers could lead not just to a better quality of life: They also might use the money to pay for the schooling or training they need to land more substantial work.

That is, a large EITC and gig work could help people respond to automation.

The MIT economist Daron Acemoglu **has a new paper** examining the thesis that automation will end employment as we know it. He finds that things aren’t nearly that dire. Indeed, over the long run, he argues, it's possible that robots will create entire new categories of jobs for complex work. But the transition between destruction and new job creation could take a long time.

"What I would take away from [my] model is that there are some forces that might still make human labor relevant for the future, but they are slow acting," he says by email. "So indeed, given the costs of displacement by automation technology and robotics for the people, there is a very strong case for policies to facilitate the transition."

So, workers may experience more frequent bouts of unemployment as robots take their jobs, and then lower wages as they enter a new occupation. The gig economy, plus the EITC, would help them earn money and pay for retraining.

Asked recently about basic income, Bill Gates expressed skepticism — but he suggested the EITC served a similar purpose at less cost. "Even the US isn't rich enough to allow people not to work," **he wrote, in a Q&A session on Reddit**. "Some day we will be, but until then things like the Earned Income Tax Credit will help increase the demand for labor."

But is it politically or financially viable?

Khanna's plan isn't cheap. Elaine Maag of the Tax Policy Center **estimates** that Khanna’s EITC plan could add $1.4 trillion dollars to the federal deficit over the next decade, depending how much is given to singles versus families and how generous the phase-in rate is. (Full disclosure: I had a hand in formulating the bill; after Khanna told me of his interest of a tax credit expansion last year, I helped convene experts to discuss it, **as part of ongoing effort** to bring Congress members and thinkers from Silicon Valley together. I was not paid.)

Yet it’s a serious response to serious economic challenges. It could be intellectually worthwhile to prompt a showdown between the Democrats and Republicans over whether corporate tax cuts or a larger EITC is a more sensible expenditure.

"The EITC, in addition to being good economics and encouraging more low-income people to work, gives Democrats an entree into the [tax-policy debate] that doesn't focus on the groups at the top that don't really need more tax cuts," said Austan Goolsbee, former chair of Obama's Council of Economic Advisers, now a University of Chicago economics professor. “In my view, that makes a large expansion of the EITC a realistic policy goal for the Democratic Party."

As a freshman Congress member, Khanna will also need the leadership of the Democratic Party to make this a priority in negotiations. Getting Sherrod Brown to sign on helps; and as of Wednesday morning there were 50 co-sponsors. Given Republican sympathy for the program, there could be room for compromise: smaller tax cuts in exchange for a version of the Khanna-Brown plan.

The next few months will be crucial for the bill as Congress takes up tax reform. At the very least, Silicon Valley's ambitious ideas now have a seat at the table.