Public Policy Brief

The Consolidated Assistance Program

Reforming Welfare by Synchronizing Public Assistance Benefits

Oren M. Levin-Waldman

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Preface

Nearly all policymakers agree that the current welfare system is badly in need of reform. Many argue that it offers too few incentives to work and almost no means by which to obtain employment. Moreover, the tax structure penalizes low-income workers so that those who can find a job have little reason to remain employed.

In this *Public Policy Brief*, Levy Institute Resident Research Associate Oren M. Levin-Waldman argues that the economic incentives in the current system provide little reason for many mothers receiving benefits to enter the work force, given that it is likely that they would be employed in low-paying jobs offering no benefits. Levin-Waldman suggests that the current array of benefits be restructured into a consolidated assistance program that would not eliminate benefits altogether, but would give welfare recipients the necessary economic incentive to work.

In order to evaluate the variety of measures that have been proposed and to gain perspective on the debate about welfare reform, we should recall the function the original welfare system was designed to perform. As Levin-Waldman notes, "the initial welfare state was not designed to encourage women with children to work, but rather, to keep them home." Today's emphasis on encouraging mothers to work is a drastically different goal, reflecting changes in the structure of the labor force, the family, and women's role in society. When we place welfare in this context, it comes as no surprise that the system does not contain the economic incentives espoused by many in the current debate.

As Levin-Waldman suggests, additional incentives to work could be instituted through a restructuring and coordination of existing programs such as the earned income tax credit (EITC). Recent hearings by the Senate Governmental Affairs Committee indicate that structural changes should be made to the EITC to address problems stemming from fraudulent claims. The existence of fraud does not imply that the EITC should be eliminated or benefits reduced; rather, restructuring efforts to address problems associated with fraud provide an excellent opportunity to redesign the EITC also to target its intended audience more efficiently and to coordinate better with other programs.

The issues surrounding welfare reform are complex, and many factors influence a mother's decision about whether she can or will enter the work force. Access to affordable health and child care, adequate education, and job training are all factors in the work decision. Lack of paternal responsibility, high rates of out-of-wedlock births and teenage pregnancy, and the trade-off (especially for single mothers) between time spent working and time spent rearing children must also be addressed before any effective reform of the current welfare system can take place. The proposals in this *Brief* address some of these issues, but they should be viewed as one part of a larger strategy that would deal with all the issues confronting the welfare system.

Dimitri B. Papadimitriou
Executive Director

May 1995

Reforming Welfare by Synchronizing Public Assistance Benefits

During the 1992 presidential campaign, candidate Bill Clinton pledged to end welfare as we know it. He made it clear that those who played by the rules and worked should not live in poverty. As president, Clinton proposed a two-year time limit on welfare benefits, after which beneficiaries would be required to work; for those unable to find work, the government would provide assistance in the form of a minimum-wage, public sector job. For low-income workers, additional assistance would be provided through an expansion of the earned income tax credit (EITC), a measure designed to reduce the cost of payroll taxes. The expansion of the EITC, legislated under the Omnibus Budget Reconciliation Act of 1993 (OBRA 93), was aimed not only at providing low-income workers with additional assistance, but also at complementing the president's plans for welfare reform by offering an additional incentive for those receiving public assistance benefits to enter the labor market.

However, the expansion of the EITC provides only a small amount of tax relief to lower-middle-class workers (those earning up to $27,000). As laudable as this relief might be, it is questionable whether it is sufficient to induce those on welfare to forsake public benefits for the world of work. Moreover, when the EITC interacts with other public assistance programs, it is questionable whether the entire array of benefits produces any added incentive to work.

In this *Brief* I intend to show that the current benefit package does not offer sufficient incentives for recipients to enter the work force. In view of this failure, we must ask what can be done to create a system that would offer such incentives. Will merely expanding the EITC or adding another program to the current package be sufficient to counteract its disincentives? I suggest that a synchronization of benefits—a plan consolidating existing programs into a more integrated system—is needed. The EITC, while not a bad program in and of itself, in conjunction with the current array of public assistance programs is simply insufficient to offer such incentives. I therefore offer a plan that would synchronize and consolidate existing benefit programs by combining elements of the EITC and other programs into one program, the consolidated assistance program (CAP). This paper intends to argue that a program composed of a two-tiered assistance component (one tier for working parents and the other for nonworking parents) and a child support component would assure minimal subsistence to those unable to work while providing positive incentives for those on welfare to work without in effect punishing them in the process. Such a program would accomplish welfare reform more efficiently and effectively than a plan that would simply expand the EITC and place a time limit on benefits.

Overview of the Major Existing Welfare Programs

Welfare for the poor consists of a wide array of programs, including Aid to Families with Dependent Children (AFDC), food stamps, the Women, Infants and Children (WIC) program, Medicaid (medical assistance for the indigent), public housing assistance, school lunch programs, nutrition programs, supplemental income programs, and, most recently, the EITC. This *Brief* focuses on AFDC, food stamps, Medicaid, and EITC benefits and attempts to establish whether the EITC as it is currently structured is sufficient to offset the disincentive effects of a welfare package consisting of AFDC, food stamps, and Medicaid.

Aid to Families with Dependent Children

AFDC is the basic welfare program and is the program we perhaps are most familiar with. It is a children's program that provides benefits through assistance to their mothers. AFDC is a cooperative program between the states and the federal government. The federal government establishes minimum benefit levels and provides funding to the states, and the states determine actual benefit levels and program eligibility.

In fiscal year (FY) 1993, 14.1 million recipients collected \$22.3 billion in AFDC benefits. Consolidated into family units, there were 4.981 million AFDC beneficiaries (U.S. House of Representatives 1994). In addition to benefit costs, total administrative costs for AFDC were \$3 billion (U.S. House of Representatives 1994). The Congressional Budget Office (CBO) estimates that in 1994 AFDC benefits will total \$23 billion (Congressional Budget Office 1994).

Originally titled Aid to Dependent Children (ADC), the program dates back to the Social Security Act of 1935, which created both a pension plan for the elderly and a public assistance program for dependent children. The pension plan was to operate as an insurance system in which individuals would receive benefits commensurate with payments into the system. Public assistance was intended for widows with children and operated as a public charity. The establishment of this dual operating system was based on conceptions of fairness and the social mores of the time. Social Security beneficiaries were thought to be "entitled" to benefits by virtue of having made payments into the fund. Public assistance was specifically for children. Predicated on the assumption that families with fathers had no need for assistance because the fathers would support the children, public assistance benefits were designed to aid families in which the father was no longer present (Weir, Orloff, and Skocpol 1988).

However, the depression of the 1930s undermined the assumption that living fathers would be able to work and support their children. One way in which the New Deal sought to address the problem of wide-scale unemployment was by creating public works programs. The public works were to furnish able-bodied men with work in an economy in which jobs were scarce and thereby enable them to fulfill their traditional role as providers.

Public works programs were based on the belief that by working in exchange for their relief, men would be able to maintain their moral integrity and self-esteem, which would be lost or impaired if they had to accept public assistance. Consequently, the moral fabric of society would not be undermined. Nor would it be undermined by women's staying home with their children, as that was precisely what society thought women were supposed to do. Hence the initial welfare state was not designed to encourage women with children to work, but rather to allow them to stay home. In fact, the system was structured so that women on ADC found it difficult to "marry off" of welfare. "Man-in-house" rules effectively discontinued benefits to any woman who either had or was presumed to have a man in the house. Moreover, it was a common assumption that mothers who were courting were neglecting their responsibilities to their children. Even though widows were considered "deserving" recipients, they were not above moral suspicion (Gordon 1994).

Food Stamps

The food stamp program is designed principally to increase the food purchasing power of eligible low-income households so that they can buy a nutritionally adequate, low-cost diet. Food stamp benefits are equivalent to the difference between the amount judged to be sufficient to buy an adequate, low-cost diet and a household's expected contribution to its food costs. The CBO estimates that more than $24 billion in food stamp benefits were paid in FY 1994; in an average month, benefits were paid to an estimated 27 million recipients (Congressional Budget Office 1994).

The food stamp program, administered by the U.S. Department of Agriculture, dates back to the early 1970s. Because food stamp benefit rates are based on a household's income and resource levels including AFDC benefits, households in states with lower AFDC benefit rates receive more food stamp benefits than households in states with higher AFDC benefit rates. The food stamp program therefore has had the effect of equalizing some of the state-to-state disparities in AFDC benefit levels.

Medicaid

Medicaid, authorized under Title XIX of the Social Security Act, is an entitlement program providing medical assistance to individuals or families with incomes under $9,000 who are "aged, blind, disabled, members of families with dependent children, and certain other pregnant women and children" (U.S. House of Representatives 1994, 783). The program is funded by federal funds that are matched at a set rate by state funds.

Recent Reforms of Welfare Programs

As demographics and our assumptions about who can or should work have changed, a greater emphasis has been placed on the need to get welfare mothers—previously encouraged to refrain from entering the work force—to work. Over the years AFDC has been amended several times to increase work incentives, but these incentives have often been negligible.

The most significant welfare reform in recent years has been the Family Support Act (FSA) of 1988. In addition to provisions aimed at enforcing paternal child support, the act provides for job training through the Job Opportunities and Basic Skills (JOBS) program. The 1988 act stipulated that mothers with children receiving AFDC benefits participate in training programs or risk losing their benefits. The goal of the legislation was to transform welfare into a transitional program aimed at helping an increasing portion of AFDC recipients get jobs and avoid long-term dependency. Through the JOBS program, states are supposed to (1) provide a broad range of educational, training, and employment-related activities, (2) increase the number of AFDC recipients participating in these activities, and (3) target resources to long-term and potentially long-term recipients.

The FSA did recognize that states might not be able to serve all who were required to participate. To ensure satisfactory participation in JOBS, the act therefore established minimum participation standards that attempted to go beyond including all AFDC beneficiaries in the participant base to including only those who would be required to participate in JOBS in the base. The minimum participation standards rose from 7 percent of all participants in FY 1991 to 20 percent of all participants in FY 1993. But due to exemptions, relatively low minimum participation standards, and the growth of the AFDC caseload, the share of AFDC recipients active in JOBS remains limited and has not increased (U.S. General Accounting Office 1994a). The General Accounting Office (GAO) also found that from FY 1991 through FY 1993, in an average month the JOBS program served only about 11 percent of the more than 4 million parents receiving AFDC. The GAO concluded that the current JOBS program has not served a large portion of the AFDC caseload and is not well-focused on employment (U.S. General Accounting Office 1994a).

Interaction of AFDC, Food Stamp, and Medicaid Programs

AFDC recipients usually qualify for food stamps and Medicaid. And, usually, the total value of the benefit package is greater than the value of the package would be if an individual worked full time at the minimum wage. Although a family supported by wages at or near the minimum wage will still qualify for some AFDC, food stamps, and Medicaid (the last so long as earned income is at or below $9,000), the family may not have much more disposable income than it would if it had no earned income, because for every dollar of earned income over $30 per month there is a corresponding reduction of AFDC benefits. The way the system is currently designed, then, provides little incentive to work.

Earned Income Tax Credit

The earned income tax credit is a refundable tax credit available to working households with a qualifying child (defined as a dependent child under the age of 18). The goal of the credit is to increase the incentive to work by offering a tax credit to offset the cost of federal payroll taxes. The credit is refundable in that claimants can receive a check for the amount of the credit that exceeds their federal tax liability. The EITC therefore acts as a government subsidy of low-wage labor.

Because the credit is completely dependent on family income, not individual circumstances, the EITC is unlike a negative income tax or some other type of minimum income floor. In order to receive the credit, one must work and must file a tax return. What distinguishes the EITC from other traditional welfare transfer payment programs is that it is dependent on both the number of qualifying children in a family and the family's amount of earned income.

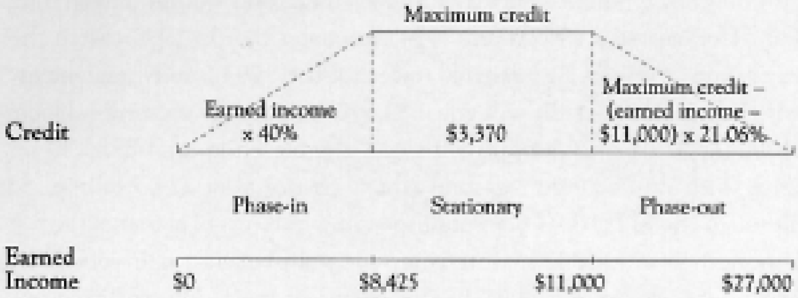
The Office of Management and Budget (OMB) estimates that the EITC will cost close to $16 billion by 1995; some estimates place the figure at around $22 billion (Office of Management and Budget 1994). The Joint Committee on Taxation (1994) estimates that in 1996 (when the expansion of the credit legislated under OBRA 1993 is fully implemented) the maximum credit will equal $3,370 for a family with two eligible children, $2,040 for families with one eligible child, and $382.50 for those with no children; the total cost is estimated at $24.5 billion. So although the EITC does not entail spending in terms of actual outlays, it is nonetheless a social maintenance program because it involves the expenditure of tax revenues. In this regard, it is no different from any other social program and thus warrants the same type of scrutiny as do others.

Introduced in 1975 as a means of offsetting the Social Security payroll tax, the EITC has come to be viewed by observers all along the political spectrum as one of the better mechanisms for assisting the poor. Because it is refundable and is tied to work, it is a means of assisting those who work. Consistent with the view that the nonworking poor need to be motivated to work, the expansion of EITC under OBRA 1993, in addition to offering assistance to the working poor, was designed to assist in overall welfare reform.

Operation of the EITC

The EITC is calculated in three income ranges: the phase-in range, the stationary range, and the phase-out range (see Figure 1). In 1996 (when the expansion under OBRA 1993 is fully implemented), families with two or more children will be eligible to receive a credit equal to 40 percent of the first $8,425 of earned income; for those with only one child, the credit equals 34 percent of the first $6,000 dollars of earned income. For a family of two or more children with income between $8,425 and $11,000 (or between $6,000 and $11,000 for a family with one child), the credit remains constant at the maximum credit level (hence, the term stationary for this income range). The maximum credit will be $3,370 for a family with two eligible children and $2,040 for a family with one child. For incomes above those in the stationary range, the EITC gradually declines. For a family with two or more children, the

Figure 1 Income Ranges of the Earned Income Tax Credit. The figure is based on earnings of a family with two or more children.



credit decreases by 21.06 percent for every dollar of earned income above $11,000; for a family with one child it declines by 15.98 percent for earned income above the stationary range. The Congressional Budget Office has estimated the maximum credit, when indexed to inflation, at $3,560 for taxpayers with adjusted gross incomes of up to about $11,600 (Congressional Budget Office 1994).

For example, a family with two children and with earnings of $10,000 (in the stationary income range) will receive the maximum credit of $3,370. A family with two children and with earnings of $17,000 (in the phase-out income range), will receive much less. This family's credit will be equal to the maximum credit of $3,370 minus 21.06 percent of the difference between its income and earnings at the end of the stationary range. Therefore, a family income of $17,000 would receive a credit of $2,106.[1]

Recipients can receive their credit in one lump sum paid upon filing their annual tax return, or they can request that their employers disburse the credit in advance through regular payroll checks. To receive the credit in advance, employees must fill out forms that allow their employers to pay them their credit over the course of the year, with employers reimbursed at the end of the year. The advance payment option is not widely familiar to either employers or eligible employees. The GAO estimated that less than 0.5 percent of those who received the EITC in 1989 received it in advance through the payroll option (U.S. General Accounting Office 1992). In a survey of 617 employers, the GAO found that 60 percent did not know about either the credit or the advance payment option. Although the IRS, through its outreach efforts, did publicize the credit, it did little to promote the advance payment option. President Clinton attempted to publicize the option by instructing federal agencies and departments to inform all federal employees who would qualify for the credit of the advance payment feature.

Problems with the EITC

Despite its popularity, there are some problems with the EITC. Because the EITC requires filing a tax return, many people who are eligible for the credit may not receive it. Many families who earn too little to pay taxes do not file returns and, hence, do not receive the credit that they are otherwise entitled to. Based on data from the Survey of Income and Program Participation (SIPP) and from special tabulations on files containing tax return data provided by the U.S. Census Bureau, Scholz (1994) estimated that in 1990 only 80 to 86 percent of eligible credit recipients filed for the credit. This means that about 2.1 million eligible taxpayers failed to receive the credit.

At the same time, many file for and receive the EITC who are ineligible on the basis of total income. The EITC is based solely on *earned* income (wages, tips, and salaries). A family can have substantial investment income (such as income from dividends, capital gains, or interest), but little earned income and thus still qualify for the credit. For instance, a family with a total income of $30,000 could conceivably qualify for the EITC if at least $3,000 of the total was investment income.[2] Based on the IRS's Individual Statistics of Income database, O'Neal and Nelsestuen (1994) found that approximately 10 percent of the EITC benefits paid in 1988 went to households with substantial accumulations of investment assets. One extreme example was a recipient who had portfolio income consisting of interest and dividends in excess of $299,000.

Further, as the EITC is currently structured, the bulk of claimed benefits go to families with earned incomes in the phase-out range. Based on adjusted gross income data from the Internal Revenue Service, in 1991 only about 5 percent of EITC returns had incomes that fell in the phase-in range, but more than 50 percent had incomes that fell in the phase-out range (see Table 1). Holtzblatt, McCubbin, and Gillette (1994) calculated that prior to OBRA 1993 4.1 million (28 percent) of all EITC claimants had incomes in the phase-in range, 2.8 million (19 percent) had incomes in the stationary range, and 7.6 million (53 percent) had incomes in the phase-out range. As a consequence of OBRA 1993, in 1994 the number of households with incomes in the phase-in and stationary ranges declined, and the number in the phase-out increased; 3.5 million (22 percent) of claimants had incomes in the phase-in range, 2.5 million (16 percent) in the stationary range, and 9.8 million (62 percent) in the phase-out range. Similarly, Hoffman and Seidman (1990) found that the typical EITC family had low-to-moderate income, placing it above the poverty line. Although 76 percent had incomes below $15,000 (in 1988 dollars), approximately 11 percent had incomes above $20,000, and some had incomes above $30,000.

On the whole, then, the EITC appears to be providing benefits primarily to lower-middle-class families who, although they are not much above the poverty line, would not be considered poor by official definitions. This is precisely the group excluded from most income transfer programs. The majority of families claiming the credit were single-parent families, of which 80 percent had a female as the head of household. More than 80 percent of claimants had only one or two children. Almost 60 percent of EITC recipients worked at least 1,500 hours a year, and almost 25 percent reported working more than 2,080 hours (Hoffman and Seidman 1990).[3]

If the majority of EITC recipients fall in the phase-out range, some of the intended purpose behind the expansion is called into question. The bulk of the total dollar value of EITC benefits is claimed by those who are not covered by current welfare programs. The poorest members of society (those earning between $0 and $11,000) do not benefit much from the EITC. And yet, this is the income range that welfare recipients would presumably be earning if they were to work. The problem with the EITC as a tool of welfare reform is that those whom the credit should be targeting are precisely those who derive no real benefit from it.

Table 1 Distribution of EITC Returns, by Income Level

Income Range	EITC Returns Number	EITC Returns Percent	Value of Credit (in thousands)	Average Credit
$5,000–10,000	332,636	5	$32,853	$98.76
$10,000–15,000	2,079,143	31	754,474	362.87
$15,000–20,000	3,056,909	50	1,238,448	405.13
$20,000–25,000	706,628	11	58,323	82.54

Note: Figures represent the EITC as it was used to offset taxes before the credit.
Source: Internal Revenue Service, *Statistics of Income—1991, Individual Income Tax Returns*, (Washington, D.C.: IRS, 1994).

Interaction of EITC with Welfare Programs

According to the Survey of Income and Program Participation (SIPP), in 1988 an average 27 million individuals collected AFDC and other cash assistance each month (Bureau of the Census 1990). Those who qualify for AFDC and food stamps and also work qualify for the EITC, earning incomes that fall primarily in the credit's phase-in and stationary ranges. Although some of the 4.981 million AFDC families are working and could be receiving some EITC benefits, most do not work and therefore cannot claim the credit. The question to be answered is how does the overall structure of existing welfare programs prevent those on welfare from moving to work and thereby deriving the full benefit of the EITC.

For families whose incomes fall in the phase-in and stationary ranges, the effect of the EITC is to raise wages by as much as 40 percent. Since this is also the range of income received for working at a full-time job for a salary at or near the minimum wage, it is presumably the same income range that those who are currently receiving AFDC benefits would be in were they to work and file for the credit. Because the EITC increases the rewards to work, the expansion of the credit legislated in OBRA 1993 should present a greater incentive to work.

The stated purpose of the EITC's expansion was to lift the incomes of poor working families above the poverty line. It would seem, then, that families who should receive the maximum credit are those earning incomes in the phase-in range, as they are the ones whose effective earnings the expansion was meant to target.

For example, consider a single parent who has two children and works full-time at the minimum wage. In 1996, when the EITC is fully implemented, the family's annual earnings would be $8,840 ($4.25 per hour x 40 hours per week x 52 weeks per year); the addition of the maximum credit of $3,370 effectively raises this family's annual income to $12,210 (or $5.87 per hour). Contrary to those who argue that the current welfare system encourages people to stay home and collect benefits (see, for example, Kaplan and Tausky 1972, Banfield 1974, Auletta 1982, Murray 1984, Mead 1986, and Freeman and Holzer 1986), the EITC would appear to provide the right incentive to work (see, for example, Ellwood 1988). Yet evidence seems to suggest otherwise.

Consider the example of a mother of two children who lives in Pennsylvania and has worked four months on a job. The economic trade-off between work and welfare for this mother is presented in Table 2. As the data show, as the mother works more hours (or as her wage rises) and she moves up the income ladder through the phase-in and stationary ranges of the EITC, her AFDC benefits decline. In addition, the value of the EITC is completely absorbed by work expenses such as child care. When her income reaches $9,000, combined Social Security and work expenses exceed the EITC.

Initially, then, there might be an incentive for this mother to work part-time and earn $2,000 a year for a gain in total disposable income of $1,375 (or $688 per $1,000 of earnings). But the net gain from earning an additional $2,000 (the difference between earning $2,000 and $4,000) will be only $367 (or $184 for each additional $1,000 of earnings). The marginal benefit of working for each additional $1,000 of earnings is only about $184 until earnings reach $7,000. When earnings rise to $8,000, the marginal benefit drops to $116. When earnings increase to $9,000, the marginal benefit of working rises to $567. When earnings reach $10,000, the marginal benefit of working drops again, to $414.

Still, at an income level of $10,000 this mother clearly has a greater disposable income than she would have if she were not working at all. At the same time, however, she no longer is eligible for Medicaid benefits. If

Table 2 Interaction of the EITC with Selected Public Assistance Programs

					Taxes					
Earnings	EITC	AFDC	Food Stamps	Medicaid	Social Security	Federal Income	State Income	Work Expenses	Disposable Income	Marginal Benefit
$0	$0	$5,052	$2,496	yes	$0	$0	$0	$0	$7,548	—
2,000	600	4,892	2,184	yes	153	0	0	600	8,923	$688
4,000	1,200	3,292	2,304	yes	306	0	0	1,200	9,290	184
5,000	1,500	2,492	2,364	yes	383	0	0	1,500	9,473	183
6,000	1,800	1,692	2,424	yes	459	0	0	1,800	9,657	184
7,000	2,100	892	2,484	yes	536	0	0	2,100	9,840	183
8,000	2,400	0	2,568	yes	612	0	0	2,400	9,956	116
9,000	2,528	0	2,388	yes	689	0	4	2,700	10,523	567
10,000	2,528	0	2,208	no	765	0	34	3,000	10,937	414
15,000	1,820	0	1,308	no	1,148	0	174	4,200	12,606	334
20,000	936	0	0	no	1,530	58	314	5,200	13,834	246
30,000	0	0	0	no	2,295	1,717	594	5,400	19,993	616
50,000	0	0	0	no	3,825	5,569	1,154	5,400	34,052	703

Notes: Figures reflect the earnings of a mother after four months on a job in Pennsylvania. A family of two children is assumed. "Work expenses" are estimated day care and other expenses related to working. "Disposable income" is the sum of total earnings, benefits, and any EITC less taxes and work expenses. "Marginal benefits" are the increase in disposable income per $1,000 of additional earned income (based on the data provided in the source).

Source: U.S. House of Representatives, Committee on Ways and Means, *Overview of Entitlement Programs: The Green Book, 1994* (Washington, D.C.: U.S. Government Printing Office, 1994).

the value of Medicaid—in Pennsylvania estimated to average $4,128 ($1,810 for an adult and $1,159 for each child)—were included as an expense, the working mother earning $10,000 would find herself considerably worse off than the nonworking mother (see Table 3). If we subtract the value of Medicaid benefits from the previous calculation of disposable income ($10,937), her new level of disposable income would total $6,809, $739 less than the level of benefits (excluding Medicaid) received by a nonworking mother.[4]

Hence, given the current structure of the welfare-EITC package, work incentives appear to exist for earnings at or below $9,000. The marginal benefit of $414 for earning an additional $1,000 is by no means sufficient to offset the cost of purchasing health insurance on the private market. No one knows exactly what it would cost to purchase a bare-bones policy, but even if a bare-bones policy could be obtained for half the value of average Medicaid benefits ($2,064), the working mother in this example would have a disposable income of only $8,873, which still would be less than the disposable income of a mother in similar circumstances who earned only $2,000. Unless an employer were to provide health insurance, working may actually be a more costly option than not working. Even though in terms of absolute income level the worker earning $2,000 has more "income" than the nonworker, it is clear that a worker is not necessarily better off than a nonworker. On the contrary, once earnings exceed $9,000 and a working mother loses her Medicaid, she may be much worse off than a nonworker.

On the face of it, then, it appears that Medicaid is the aggravating variable. But such an appraisal is too simplistic, because Medicaid varies with place and is an intangible, noncash benefit. In this example, the value of Medicaid could clearly alter the decision about whether to forsake welfare for work. However, in another state Medicaid could easily be half the amount and therefore a much less important factor in welfare-to-work decisions. In addition, a welfare recipient might not see any benefit in working if the difference between not working and working is that one receives Medicaid in the former case and does not in the latter.

To a large extent, Medicaid acts much like a dummy, or qualitative, variable and, as such, cannot be as easily quantified as the other assistance programs.[5] Blank (1989) has noted that the actual (dollar) value of

Table 3 Interaction of EITC with Other Assistance Programs (Including Medicaid Benefits and Health Expenses)

					Taxes					
Earnings	EITC	AFDC	Food Stamps	Medicaid	Social Security	Federal Income	State Income	Work Expenses	Disposable Income	Marginal Benefit
$0	$0	$5,052	$2,496	$4,128	$0	$0	$0	$0	$7,548	—
2,000	600	4,892	2,184	4,128	153	0	0	600	8,923	$688
4,000	1,200	3,292	2,304	4,128	306	0	0	1,200	9,290	184
5,000	1,500	2,492	2,364	4,128	383	0	0	1,500	9,473	183
6,000	1,800	1,692	2,424	4,128	459	0	0	1,800	9,657	184
7,000	2,100	892	2,484	4,128	536	0	0	2,100	9,840	183
8,000	2,400	0	2,568	4,128	612	0	0	2,400	9,956	116
9,000	2,528	0	2,388	4,128	689	0	4	2,700	10,523	567
10,000	2,528	0	2,208	0	765	0	34	7,128	6,809	(3,717)
15,000	1,820	0	1,308	0	1,148	0	174	8,328	8,478	334
20,000	936	0	0	0	1,530	58	314	9,328	9,706	246
30,000	0	0	0	0	2,295	1,717	594	9,528	15,865	616
50,000	0	0	0	0	3,825	5,569	1,154	9,528	29,924	703

Notes: Figures reflect the earnings of a mother after four months on a job in Pennsylvania. A family of two children is assumed. Medicaid benefits are the average benefits in Pennsylvania for one adult and two children. "Work expenses" are estimated day care, health care (assumed purchaseable at a price equivalent to average Medicaid benefits), and other expenses related to working. "Marginal benefits" are the increase in disposable income per $1,000 of additional earned income (based on the data provided in the source).

Source: U.S. House of Representatives, Committee on Ways and Means, *Overview of Entitlement Programs: The Green Book, 1994* (Washington, D.C.: U.S. Government Printing Office, 1994).

Medicaid benefits has little effect on AFDC participation. This is not the same as saying that because Medicaid is available only to AFDC participants, Medicaid will not have an impact on the decision about whether to work in the minimum-wage market or simply participate in AFDC. Rather, the meaningful factor is the availability of affordable health care. In other words, the value of the program may be of no consequence, but the program in and of itself is (Bane and Ellwood 1994).

This conclusion is supported by Moffitt and Wolfe (1992), who found that if 100 percent of workers received medical coverage, AFDC participation would fall by 7.3 percent and the employment rate would rise by 16 percent; medical coverage would actually reduce the AFDC caseload by 20 percent. The effect of Medicaid on the welfare-to-work decision cannot, therefore, be dismissed. The choice facing AFDC recipients is no longer whether there is a positive incentive to work, but whether they can afford to work given that Medicaid benefits are lost once earnings exceed $9,000. Unless an employer provides health insurance, there is an effective marginal tax on the worker, the size of which is contingent on what it would cost to purchase insurance in the private marketplace.

Although the combination of welfare benefits and the EITC does not appear to provide an AFDC recipient much incentive to leave welfare for full-time, minimum-wage employment, she would indeed be worse off if she did work and there was no EITC. Consider again the working mother living in Pennsylvania with two children. Without the EITC it makes sense for her to work only if she earns $2,000 (see Table 4). Earnings between $2,001 and $8,000 are associated with negative marginal benefits and falling disposable income. Although marginal benefits are positive for earnings over $8,000, the mother who works full time at the minimum wage (and therefore earns between $8,000 and $9,000 per year) would realize roughly the same amount of disposable income as if she were not working at all.

Even though comparing the world with the EITC to the world without it (Table 2 compared to Table 4) shows that a mother earning the minimum wage would have more disposable income with the EITC than without it, the EITC still does not make our working mother much better off than if she were not working at all. And any incentive that she

Table 4 Interaction of Work with Selected Public Assistance Programs (Without the EITC)

				Taxes					
Earnings	AFDC	Food Stamps	Medicaid	Social Security	Federal Income	State Income	Work Expenses	Disposable Income	Marginal Benefit
$0	$5,052	$2,496	yes	$0	$0	$0	$0	$7,548	—
2,000	4,892	2,184	yes	153	0	0	600	8,323	$388
4,000	3,292	2,304	yes	306	0	0	1,200	8,090	(117)
5,000	2,492	2,364	yes	383	0	0	1,500	7,973	(117)
6,000	1,692	2,424	yes	459	0	0	1,800	7,857	(116)
7,000	892	2,484	yes	536	0	0	2,100	7,740	(117)
8,000	0	2,568	yes	612	0	0	2,400	7,556	(184)
9,000	0	2,388	yes	689	0	4	2,700	7,995	439
10,000	0	2,208	no	765	0	34	3,000	8,409	414
15,000	0	1,308	no	1,148	0	174	4,200	10,786	475
20,000	0	0	no	1,530	58	314	5,200	12,898	422
30,000	0	0	no	2,295	1,717	594	5,400	19,993	710
50,000	0	0	no	3,825	5,569	1,154	5,400	34,052	703

Notes: Figures reflect the earnings of a mother after four months on a job in Pennsylvania. A family of two children is assumed. "Work expenses" are estimated day care and other expenses related to working. "Disposable income" is the sum of total earnings and benefits less taxes and work expenses. "Marginal benefits" are the increase in disposable income per $1,000 of additional earned income (based on data provided in the source).

Source: U.S. House of Representatives, Committee on Ways and Means, *Overview of Entitlement Programs: The Green Book, 1994* (Washington, D.C.: U.S. Government Printing Office, 1994).

might have to work is likely to be muted by the fact that if her earnings are slightly higher than the minimum wage (that is, more than $9,000), she will lose her Medicaid assistance.

The extent to which the current EITC-welfare package is able to provide incentives is complicated by the fact that no one knows how many people who enter the low-wage labor market will be lucky enough to find jobs providing health insurance benefits. Nor does anyone know how many of those who obtain employment but do not receive health insurance benefits will still be able to obtain medical care at affordable prices.

Another major obstacle to working for the poor and the near-poor is child care, so far only alluded to in the above example's computation of disposable income (as a portion of "work expenses"). The cost of child care alone will affect women's decisions about entering the labor market (Connelly 1992). According to the GAO, the provision of a full subsidy to mothers who must pay for child care could increase the proportion of poor mothers who work by 15 percentage points, from the current rate of 29 percent to 44 percent, and the proportion of near-poor mothers who work by 14 percentage points, from the current rate of 43 percent to 57 percent (U.S. General Accounting Office 1994b). Such a subsidy would increase the proportion of nonpoor mothers who work by 10 percentage points, from the current rate of 55 percent to 65 percent. The findings of the GAO study appear consistent with those of Berger and Black (1992), who estimated that subsidized child care programs would lead to a 12 percent increase in employment. These results suggest that among the factors encouraging low-income mothers to seek and keep jobs, affordable child care is a decisive one. And because most mothers do pay for child care while they work, their decision to enter the work force is therefore contingent on how much income they have after child care expenses have been paid. Admittedly, considering cost factors alone may miss the complexities involved in child care. While such complexities may not be quantifiable, they still are likely to enter into a mother's determination of whether to work or to continue receiving welfare benefits.

Analyzing the welfare-to-work decision is made even more complicated by the fact that under existing programs states (or localities) set benefit levels. Variations across regional and state boundaries mean that the

EITC (as currently structured) offers greater incentives to work in states in which AFDC benefits are considerably less generous. (The appendix provides an example of how variations in benefit levels across states might affect incentives to work.)

Given the variety of factors affecting the decision to work, it seems clear that, even at its projected 1996 level, the EITC alone cannot motivate those on welfare to go to work. Even though it offers relief, the credit is simply insufficient to provide an adequate income to mothers who may consider leaving welfare. Given the wages that most mothers who leave welfare would receive, the size of the credit in most cases would cover only the cost of child care. In a sense, the credit's only effect may be to lift the living standards of working mothers to levels comparable to those of welfare mothers; without the credit a working mother earning the minimum wage would clearly be worse off. Moreover, if a welfare recipient is faced with a low-skill labor market in which there is no dignity associated with work, there is really no incentive to work.

Implications for Welfare Reform

What is important to stress is that while welfare recipients who work are eligible for the EITC, the interaction between welfare programs and the credit ultimately leads to a situation where there is not much incentive to work. Yet, these recipients are the very people who should be targeted by the EITC as part of any welfare reform effort. It is clear that work incentives need to be stronger than they are under the current structure of welfare programs and the EITC. The current structure appears to provide an incentive to work only if incentive is measured in terms of absolute income. Greater absolute income, however, does not necessarily make a person better off (Bane and Ellwood 1994).

It would seem, then, that serious welfare reform requires more than just the addition of the EITC—even an expanded one—to the current array of welfare programs. An expanded EITC might enhance work incentives, but not enough to entice significant numbers to leave the welfare rolls. First, an expanded EITC may not be correctly structured to reach the correct targets to achieve that goal. Second, the value of the credit

Table 5 Demographics of the 1992 AFDC Population

Average family size (persons)	2.9
Number of child recipients (percent of AFDC cases)	
One	42.5
Two	30.5
Three	15.5
Four or more	10.1
Unknown	0.7
Basis for eligibility (percent of child recipients)	
Parents present in household	
Parent incapacitated	4.1
Parent unemployed	8.2
Parents absent from household	
Death	1.6
Divorce or separation	30.0
No marital tie	53.1
Other reason	2.0
Unknown	0.9
Age of mother (percent of mothers)	
Under 20 years	7.6
20 to 24 years	24.5
25 to 29 years	23.3
30 to 39 years	32.7
40 years or older	11.8
Unknown	0.1
Age of children (percent of recipient children)	
Under 3 years	24.6
3 to 5 years	21.7
6 to 11 years	32.4
12 years and older	21.2
Unknown	0.0
Race (percent of parents)	
White	38.9
Black	37.2
Hispanic	17.8
Native American	1.4
Asian	2.8
Other or unknown	2.0

(Continued on next page)

Table 5 *(Continued)*

Education of mother (percent of mothers)	
Eighth grade or less	4.9
One to three years of high school	18.8
High school diploma	22.4
Some college	6.8
College graduate	0.5
Unknown	46.6
Mother's employment status (percent of mothers)	
Full-time job	2.2
Part-time job	4.2
Presence of income (percent families)	
With earnings	7.4
No non-AFDC income	78.9
Father's relationship to youngest child (percent of fathers)	
No father	89.4
Natural father	na
Adoptive father	na
Stepfather	na
Other factors (percent of households)	
Living in public housing	9.2
Participating in food stamp or donated food program	87.3
Including nonrecipient members	38.9

na: not available

Source: U.S. House of Representatives, Committee on Ways and Means, *Overview of Entitlement Programs: The Green Book, 1994* (Washington, D.C.: U.S. Government Printing Office, 1994), 401–402.

(even when fully implemented in 1996) appears to be too low to make any significant difference in the decision to leave welfare for work.

The problem, however, is not the presence of the EITC, but the structure of the other programs. The question that perhaps should be addressed is what prevents AFDC recipients from entering the work force. That is, assuming that jobs exist (which is another issue altogether), why is this population unable to take advantage of work opportunities?

To answer this question, it is necessary to examine the composition of the AFDC population. Table 5 provides basic demographic information for the AFDC population in 1992. What stands out in the data is that a considerable percentage of mothers (46.3 percent) cared for young children (under 6 years of age) and that many (at least 46.1 percent) had only a high school education or less. With so few years of schooling, it is likely that these women would be able to find only low-skill jobs paying no more than minimum wages. Moreover, if they were to work, they would have to pay child care and have to find and pay for medical insurance. As tables 2 and 4 show, if a mother can make only the minimum wage and has to incur child-care expenses, she has little incentive to move off welfare, even given the benefit of the EITC.

Problem of Synchronization

Although there would be even less incentive to work without the EITC, even with the EITC there is little incentive at the low end of the earnings distribution to move from welfare to work. At the upper end of the distribution the credit may adversely affect labor incentive insofar as it enables workers to trade off some hours of work in exchange for greater leisure time (Hoffman and Seidman 1990, U.S. General Accounting Office 1992, and Kosters 1993). If the end result is that more people in the phase-out range receive the credit than people in the phase-in and stationary ranges, the EITC is, in effect, no more than tax relief for the lower-middle class.

What, then, are the advantages of the EITC? In light of the program's costs, this is by no means a trivial question. If the only goal of the credit is to reduce the poverty rate, there may be some evidence that the EITC does its job. The GAO estimated that the EITC reduced the poverty rate by as much as 0.7 percent in 1991, after having reduced the rate by a relatively smaller 0.1 percent in 1985 and 0.4 percent in 1988 (U.S. General Accounting Office 1992). According to the Center on Budget and Policy Priorities, the effect of the Clinton expansion of the EITC proposal was to reduce the number of people in poverty by over 2 million in 1994.[6] (Data on the number of families living in poverty are provided in Table 6.)

However, adding the 1993 maximum credit for a family of three of $1,511 to minimum-wage yearly earnings yields only $10,351 in total

Table 6 Families Living Below the Poverty Line, by Race, 1992 (in thousands)

Family	All	White	Black	Hispanic[a]
Population	68,144	57,858	7,888	5,318
Number in poverty	7,960	5,160	2,435	1,395
Percent of number in poverty	100.0	64.8	30.6	17.5
Percent of own group	11.7	8.9	30.9	26.2
Married-couple households	3,318	2,631	486	680
Percent of number in poverty	41.7	33.1	6.1	8.5
Female-headed households	4,171	2,202	1,835	604
Percent of number in poverty	52.4	27.7	23.1	7.6

[a] Those of Hispanic origin may be of any race.
Source: Bureau of the Census, U.S. Department of Commerce, "Poverty in the United States: 1992," *Current Population Reports*, P60-185 (Washington, D.C.: U.S. Government Printing Office, 1993).

income, as compared to the 1993 poverty line of $11,572 ($14,763 for a family of four). Even with the EITC such a family would still have lived below the poverty line, and even with food stamps it would not have risen much above the line. With the expansion of the EITC under OBRA 1993, a family with earnings of $11,368 in 1994 would still have found itself with less than a poverty-level income. Even though food stamps would have raised this family's total income above the poverty line, in net terms (that is, in terms of disposable income) the family would still have been living in poverty.

It may be that our expectations of the EITC are too high. As a form of tax relief, the credit does its job. But many now are viewing the EITC as a staple of welfare reform which, in the credit's current form, may be too much to expect from it. Reducing the number of people in poverty and motivating people to go from welfare to work are two different matters entirely. If 2 million people are assisted, there is no doubt that the EITC has some merit. But it does not follow that because the program is a benefit to the working poor, it will be a good vehicle for motivating the poorest members of society to forsake welfare for work. The EITC, then, should be targeted at the poorest in the market.

The first step in targeting this population is making employers and potential employees aware that this labor market subsidy exists; many potential beneficiaries do not take advantage of the credit because they simply are unaware of it. Both employers and employees must be made aware that eligible employees can receive the EITC through their regular paychecks and that the credit can be payable either during the working year or as a lump sum at the end of the year. They must also be informed that there are forms to be filled out and instructed how to do so, so the potential beneficiaries do not fail to take advantage of the credit because of the complexity of the forms (Nelson 1992).

But targeting the EITC at low-wage workers raises serious questions. For example, would widespread knowledge and use of the credit give employers an incentive to maintain low wage rates? At present, answering this question is almost impossible. The GAO found that 60 percent of the employers they surveyed between December 1990 and October 1991 knew little or nothing about the EITC (U.S. General Accounting Office 1992); given this lack of knowledge of the credit, it is hard to make a case that the EITC has up to this point kept wages artificially low. But if the Clinton administration successfully publicizes the advance payment option, might employers find themselves armed with a new mechanism for maintaining low wage rates? That is, if employers know that their employees are receiving higher effective wages as a result of the credit, would employers be encouraged to pay lower wages? The question of just who is being subsidized—workers, employers, or both—warrants attention.

Targeting also involves the coordination of the EITC with other public assistance programs. If there is little incentive for an AFDC recipient to work because she will be penalized by the loss of other benefits, of what value is a labor market subsidy? It is one thing to say the EITC is intended to assist the working poor and possibly offer a small incentive to move from welfare to work; it is quite another to show that the credit actually accomplishes these objectives.

For the EITC to offer a greater incentive for those on welfare to go to work, the program would have to be restructured; that restructuring would have to involve no less than the synchronization of benefits. One approach would be to eliminate the other assistance programs; if the EITC were the only assistance program, the poor would have no choice but to rely on it. But this option is essentially negative, as it would fail to foster the type of dignity work should have. Although it is true that simply cutting the other programs can make the EITC appear to be a positive inducement to work, such reductions would in reality be a form of "tough love" (Heclo 1994) based on the assumptions that the poor are lazy and that they do not work for what Mead (1992) calls "mysterious" reasons.

For an elimination of benefits to succeed, welfare mothers would have to be able to find types of jobs that would enable them to earn more than they are currently receiving through transfer programs. As the demographics of the AFDC population show, this is highly unlikely (Burtless 1994). Moreover, the private marketplace would have to be able to generate sufficient employment so that all who want to work can find a job, and it is not entirely clear that sufficient jobs exist. If there are not enough jobs, the end result would be more suffering and misery.[7]

Some believe that there are enough low-skill jobs for existing welfare mothers. For instance, Blank (1995) has argued that there is little evidence that jobs *per se* have become less available, especially for less-skilled female workers; in fact, women's unemployment rates have fallen relative to men's over the past decade. Burtless (1995) has observed that despite the existence of roughly 7 million jobless workers, most labor economists believe that employers have the ability to offer jobs to 2 to 3 million current AFDC recipients if the recipients were forced to leave the welfare rolls. Blank (1995) also notes, however, that substantial evidence indicates that the attributes of available jobs have deteriorated. So while the U.S. labor market has changed since the early 1970s, these changes have not led to the elimination of jobs for less-skilled workers, but rather to a reconfiguration of those jobs into lower-paid positions that provide fewer opportunities for advancement into higher-wage positions.

Although an able-bodied and moderately resourceful welfare recipient can almost certainly find employment if she is willing to accept low wages and a meager package of fringe benefits, it is those very working conditions that create her welfare-to-work dilemma. Jobs may exist, but they will not suffice to support a family unless accompanied by an array of support services. It is simply unrealistic to expect that all single women with young children will be able to work full-time, year-round. Many will choose to work part-time so as to make child rearing more feasible. Others will spend part of the year without jobs as a result of involuntary unemployment, illness, or difficulty in arranging child care (Burtless 1995).

Eliminating the major welfare programs would certainly make the EITC essential as a labor market subsidy. But the EITC alone is not enough to support a family given current labor market conditions. Those who advocate time limits for benefits simply fail to consider the "damper that the low end of the labor market places on opportunities for low-educated workers" (Haveman 1995). The decline in earnings opportunities for less-skilled workers needs to be addressed for welfare-to-work programs to lead recipients toward self-sufficiency.

The role of public policy, then, should be to further the goals of society in a positive and constructive way, as opposed to a negative and harmful way. A positive approach would be to offer an inducement to work by making work pay. Such an approach would involve a whole new way of thinking about how the welfare state is administered, what the goals of the welfare state ought to be, and how its various programs can be synchronized to achieve its goals.

A Program for Consolidated Assistance

The Congressional Budget Office estimated the 1994 cost of AFDC at $23 billion, food stamps at $24 billion, and Medicaid at $140 billion (Congressional Budget Office 1994). The total cost of the major public assistance programs is $187 billion. In addition, the 1996 cost of the EITC is projected at $24.5 billion. The federal government is spending in excess of $210 billion on these programs for the poor. The actual cost of the welfare state is considerably more, however, as the $210 billion does not even begin to take into account a number of other assistance programs, such as public housing, nutrition programs, educational programs, and school lunches. Despite their cost and number, there has been little coordination of existing welfare programs. And, there has been relatively little coordination of the parallel systems created by the tax programs and the public assistance programs. As a result, the current welfare system has become "inequitable, inefficient, overly complicated, and expensive to administer" (Forman 1993, 418).

Given that nonworking or minimum-wage-earning welfare recipients should derive the greatest benefit from the EITC, one solution to the current welfare problem is to find a way in which the program can be restructured or synchronized with other programs so that it (1) assists those who most need it and (2) creates a positive inducement to work so that individuals are able to achieve a degree of self-sufficiency. To put it another way, could the $210 billion currently spent on the major welfare programs and the EITC be spent on another, better-coordinated set of programs devised to accomplish these objectives? Such a positive interaction might be achieved through the consolidation of these programs into a plan offered through the tax code. Although the CAP does not take regional differences in the cost of living into account, its goals are to encourage work, to deliver fair and equitable benefits, and to do both efficiently.

Goals of Welfare Reform

Although welfare reform should seek to move people off the rolls by making work pay, it first should acknowledge the importance of providing basic assistance to those who, for whatever reason, will not be able to work. With this understanding, welfare reform should be predicated on four principles.

- Work allows people to be self-sufficient and confers dignity. It socializes people into the common project of society in which they all work together as equal citizens.
- Children should be adequately provided for. This support should, when possible, come from their family. Fathers have a responsibility to support their children; a welfare system should aim to ensure that fathers contribute to their children's support.

- A person who works should not be penalized economically for doing so.
- Positive incentives to work should not vary regionally, but should be uniform throughout the country.

The New Program: CAP

Return to the example of the mother who has two children and lives in Pennsylvania. If she did not work, she would receive $7,548 in benefits ($5,052 in AFDC and $2,496 in food stamps) plus health coverage through Medicaid. The program proposed here—the consolidated assistance program (CAP)—would do away with the distinctions between AFDC and food stamps and instead would consist of two basic components: a child support component and an assistance component.

The child support component would be modeled along the lines suggested by Garfinkel (1992). A minimum assured benefit for children—between $2,000 and $2,500 for the first child, $1,000 each for the second and third child, and $500 each for the fourth, fifth, and sixth child—would be provided through a child support assurance system (CSAS). The cost of the CSAS would be shared by known fathers and the government. For children whose paternal support is less than the minimum assured benefit, the government would pay the difference. Children whose paternal support exceeds the assured benefit would receive no assistance through the CSAS.

The assistance component of the CAP would be available to both those who cannot find work and those who are working. The assistance component for nonworkers would consist of a maximum benefit based on the existing annual median state AFDC benefit. (In 1994 the monthly median state benefit for a nonworking mother with two children was $366, or an annual benefit of $4,392.)

The assistance component of the CAP for workers would be modeled along the lines of the current EITC. It would provide a positive incentive to work by offering a maximum credit of $5,500 to anybody who worked and earned between $8,425 and $11,000. As such, this component of the CAP would be similar to the existing EITC. Total benefits would still be based on earnings in one of three income ranges, although

Table 7 Disposable Income Under the Proposed CAP

Income and Expenses	Nonworking Recipient	Working Recipient
Income		
Earnings	$0	$8,840
Assistance component	4,392	5,500
Child support component	3,500	3,500
Total	$7,892	$17,840
Expenses		
Taxes	$0	$(678)
Child care	0	(2,000)
Other	0	(700)
Total	0	$(3,378)
Disposable income	$7,892	$14,462

Notes: Earnings are those of one person working full-time at the minimum wage. The assistance component for the nonworking recipient assumes two children.

benefits in the phase-in range would be expanded and the level of qualifying income in the phase-out range would be narrowed from those under the existing EITC. Specifically, benefits would equal 65.1 percent of earnings in the phase-in range (earnings up to $8,425); $5,500 (the maximum credit in the phase-in range) for earnings in the stationary range (earnings between $8,425 to $11,000); and would decline at a rate of 61.1 percent on earnings in the phase-out range (earnings between $11,001 and $20,000). Unlike the current EITC (and the CSAS component), the assistance component of the CAP for workers would not be tied to the number of children in the household.[8]

Total benefits for a mother with two children, then, would be $7,892 for the nonworking family ($4,392 in assistance benefits and $3,500 in CSAS benefits). Working families would receive a maximum benefit of $9,000 ($5,500 in assistance benefits and $3,500 in CSAS benefits). Table 7 provides a comparison of effective incomes for a working and nonworking family with two children.

Under this benefit structure beneficiaries do not lose anything by going to work; the net income gain of almost $7,000 means that the person in our example is better off working. And although the maximum credit for working families under the CAP would be considerably larger than the maximum credit allowed under the EITC in 1996, the increase is partially offset by the narrowing of income parameters and the higher rate at which the credit declines in the phase-out ranges.

In addition, although the higher phase-out rate under this scheme as compared to the current EITC (61.1 percent versus 26.10 percent) does create a work disincentive for incomes at the higher range of the credit, any disincentive could be offset by maintaining the CSAS component for workers with incomes up to at least $27,000.

There are two reasons why the CSAS, or at least the government portion of the child support subsidy, should be extended to incomes above the maximum level at which the working assistance benefit is allowed. First, children simply deserve our support regardless of family income. If we are a nation purporting to uphold family values, we should be ready to support our most precious resource. This is simple justice.

Second, we do not want to take away all benefits from those at the upper end of the current EITC phase-out range, as they are not truly wealthy. As a matter of fairness, as part of the lower-middle class, they should still receive some relief following synchronization. As shown in Table 8, most single mothers with earnings at the upper end of the current EITC phase-out range will do as well under the new program as under the current scheme.

It is true that under the CAP marginal tax rates are rather high for earnings between $11,000 and $20,000; overall, however, a single mother with two children would have a higher income under the new program than she would under the old one. Even after food stamps are added to the incomes of mothers with earnings of, say, $16,000 under existing programs, these mothers still fare better under the new program. It should also be noted that mothers with more than two children would receive more under the new program (as a result of increased CSAS payments) than under the old program (as EITC benefits do not increase for families with more than two children). Moreover, CSAS is a minimum for child support; children whose court awards for paternal support were higher would receive more support.

Table 8 Comparison of the Disposable Income of a Working Mother Under Existing Programs and the CAP

	CAP			Existing Programs		
Earnings	Assistance	CSAS	Gross Income	Food Stamps	EITC	Gross Income
$11,000	$5,500	$3,500	$20,000	$1,974	$3,370	$16,344
12,000	4,899	3,500	20,389	1,733	3,159	16,892
14,000	3,667	3,500	21,167	1,250	2,738	17,988
16,000	2,445	3,500	21,945	775	2,317	19,092
18,000	1,223	3,500	22,723	293	1,896	20,189
20,000	0	3,500	23,500	0	1,475	21,475
22,000	0	3,500	25,500	0	1,053	23,053
24,000	0	3,500	27,500	0	632	24,632
26,000	0	3,500	29,500	0	211	26,211
27,000	0	3,500	30,500	0	0	27,000

Note: Calculation of benefits under existing programs assumes a family of a single mother with two children.

Finally, in order to address the issue of health care insurance, under the CAP Medicaid benefits would be extended for one year for those who go to work (as is currently the case under the Family Support Act of 1988). It should be pointed out that such an extension might not entirely solve the problem of health care for these families. Mothers with children might find that, despite the CAP benefits, once their Medicaid expires, they can no longer afford to work. On the other hand, it might well be that a year of consistent work might socialize these mothers into work patterns and provide them with an adequate work history so that if their employers were not providing private insurance, they might be in a better position to find jobs that did offer health benefits.

Extending benefits beyond a year raises the issue of fairness to people who have been working but have not been able to afford health insurance. Why should free health insurance be available to welfare mothers ready to go to work, but not to those who have been working? There is no easy way to answer this question. Certainly, health care reform would also contribute to welfare reform. The reason for not cutting off Medicaid for newly working welfare mothers is that they should not be penalized for doing what society has demanded of them;

fairness would dictate that the umbrella be extended to cover mothers who are currently working, rather than contracted so that it does not cover those who are not newly working.

Budgetary Effects and Financing Proposals

The estimated cost of the assistance component of the CAP for nonworking mothers is essentially the same as the current cost of the AFDC program. Because the food stamp program would be eliminated under this proposal, the $24 billion currently spent on food stamps could be transferred to offset government spending for the CSAS program.

The assistance component of the CAP for nonworking mothers would be administered through the same tax system as the assistance component of the CAP for working recipients, which would mean that nonworking mothers would have to file a tax return in order to receive basic assistance. Such a reorganization would eliminate the current AFDC bureaucracy, for a potential savings of $3 billion in federal administrative costs in addition to administrative cost savings associated with the elimination of the food stamp program.

A best guess of total expenditures for the CAP is that they would be somewhat less than the costs of the current, three-program system. The CSAS component would be paid for in part by fathers. The worst-case scenario—in which no father makes payments—would cost the government an estimated $17.5 billion.[9] (Benefit costs would, of course, run higher if the CSAS were extended to those with incomes up to $27,000 or if the average recipient family size were to increase.) Estimated costs for the assistance component of the CAP range from $22 billion (if nobody works and only nonworking benefits are paid) to $27.5 billion (if everyone works and only working benefits are paid).[10] Estimated costs for the entire CAP, then, would be a maximum of $45 billion (and likely less). This level of spending appears reasonable when compared to the $50 billion currently paid for the AFDC and food stamp programs ($47 billion in program costs plus $3 billion in administrative costs for AFDC).

It is true that some of those who already file for the EITC would have earnings that fall within the eligible range of income to receive working benefits under the CAP, which would add to the cost of that component. But capping the working component of the CAP at earnings of $20,000 eliminates perhaps one-third of those who currently are eligible for the EITC. The elimination of those with earnings between $20,001 and $27,000 would save at least $8.5 billion. Moreover, many who now file for the EITC and also receive food stamps would no longer be receiving food stamps, which would result in additional savings. However, as mentioned above, those eligible for benefits under the new program would receive more than under the current system.

In summary, the hodgepodge of current programs now costs around $210 billion. The consolidated assistance program would cost roughly the same as current programs, and possibly $3 to $5 billion less. Some additional administrative savings from the food stamp program might be realized. But even if this proposal were to cost more than the current programs, the new program for welfare reform would address in a positive and constructive way the issue of work incentives and disincentives present in the current system (Aaron 1973).

Conclusion

The goal of welfare reform is to make work pay. True welfare reform, then, will involve more than marginal changes of existing programs; it will require making work a more economically attractive option. If the EITC is to be a staple of such reform, the credit would need a more drastic alteration than a simple expansion coupled with a two-year time limit on AFDC benefits. Welfare reform requires a synchronization of benefits so that the system can move people from welfare to work and ensure that those who do so are not penalized because they chose to do what society wants and demands of them.

The consolidated assistance program collapses existing welfare and work incentive programs into one program without increasing the federal budget. The CAP offers a positive inducement to work while ensuring that those who cannot find work are still provided for. Its goal is to encourage work, to deliver fair and equitable benefits, and to do so efficiently.[11]

Efficiency is, of course, defined by many as spending less money; reducing spending often entails reducing and streamlining programs. The traditional means by which federal government programs have been cut have been consolidation into block grants and transfer of responsibility to the states. If as a result of the implementation of the program suggested here, the federal government spent less, the achievement of efficiency could be claimed by some. However, such a definition of efficiency may well be too narrow. Efficiency in government can also be defined as the best possible use of resources or the least costly way to achieve the objectives formally established in the policy-making process. In terms of welfare, many people believe that those objectives are to encourage people to work and not to wantonly allow children to starve. If, through the synchronization of benefits, these objectives can be accomplished (and in a positive manner), then, by definition, government will have become more efficient. Moreover, synchronization of benefits is in the spirit of President Clinton's program for reinventing government. This program, then, could serve as a major step in the effort to reform government as well as to reform the welfare system. The effect of synchronization of benefits along the lines of the consolidated assistance program should be greater efficiency and greater labor market activity, that is, more people applying for jobs and entering the private labor market.

Appendix. Regional Variation in Welfare Benefits

Under existing welfare programs, states (or localities) set benefit levels. Variation across regional and state boundaries means that the EITC (as currently structured) offers greater incentives to work in states in which AFDC benefits are considerably less generous.

Consider the following example. In the state of New York, a single, nonworking mother with two children receives $6,924 in AFDC benefits and approximately $1,934 in food stamp benefits, or $8,858 in total benefits.[12] If the value of Medicaid, which in New York is equal to $4,790 ($2,214 per adult and $1,288 per child), is added to this figure, our mother has an income value equal to $13,648 (see Table A1).

Table A1 Comparison of Benefit Levels for Nonworking and Working Mothers in New York and Texas

	Nonworking, New York	Nonworking, Texas	Working
Earnings (@4.35 per hour)	$0	$0	$9,048
AFDC	6,924	2,208	0
Food stamps	1,934	3,349	2,442
Taxes	0	0	–678
Child care	0	0	–2,000
Other expenses	0	0	–700
EITC	0	0	3,370
Medicaid	4,790	2,992	0
Total	$13,648	$8,549	$11,482

Sources: U.S. House of Representatives, Committee on Ways and Means, *Overview of Entitlement Programs: The Green Book, 1994* (Washington, D.C.: U.S. Government Printing Office, 1994), 761–769; "The Earned Income Credit—Integrating Tax and Welfare Provisions," *Tax Notes*, no. 7, July 1994; and Mary Jo Bane and David T. Ellwood, *Welfare Realities: From Rhetoric to Reform* (Cambridge, Mass.: Harvard University Press, 1994).

However, if this same mother worked full-time for slightly more than the minimum wage ($4.35 per hour), received food stamp benefits, and claimed the EITC, her gross annual income would equal $14,860. We must, however, account for the costs associated with work not borne by the nonworking mother. To recalculate net income, we subtract from gross monthly income the costs of taxes ($678), child care ($2,000), and other expenses ($700).[13] To this figure we add $2,442 in food stamp benefits {$295 – .30 [income – $131 – (earned income x .20) – child care]} and $3,370 from the EITC, which yields an annual net income of $11,482. Given the benefit structure in New York, then, the woman would have little incentive to work at a minimum-wage job.

Regional variation further complicates the issue of work incentives. For instance, as shown in Table A1, the monthly AFDC grant in Texas is $184, or $2,208 for a twelve-month period. The single, nonworking mother would also be entitled to $3,349 in food stamp benefits, yielding $5,557 in total benefits. If the value of Medicaid, which in Texas is $2,992 ($1,542 per adult and $725 per child), is added to this figure, our mother has an income value equal to $8,549. In Texas, then, a mother would receive a higher net income by working at the minimum wage, receiving food stamp benefits, and claiming the EITC than she would by not working at all.

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Notes

1. The difference between the family's earnings and earnings at the upper end of the stationary range is $17,000 – $11,000 = $6,000. Multiply this amount by the percentage applicable to the phase-out range, that is, $6,000 x .2106 = $1,263.60. Subtracting this amount from the maximum credit, $3,370 – $1,264 = $2,106, yields the amount of the family's EITC.

2. If, say, $3,500 of the total $30,000 is investment income, the family would be eligible for the EITC on $26,500 (the earned portion of their total income), still within the phase-out range.

3. The number of hours considered equivalent to full-time work is 2,080, that is, 40 hours per week, 52 weeks per year.

4. This assumes that the mother working at the minimum wage would not receive employer-paid health care benefits and that such benefits could be obtained at a cost equivalent to the average value of Medicaid benefits.

5. In a quantitative model dummy variables are used to quantify qualitative attributes. "Such qualitative variables usually indicate the presence or absence of a 'quality' or an attribute," such as male or female, black or white, AFDC recipient or nonrecipient, thought to be factors that influence the variable(s) being modeled (Gujarati 1992). These attributes are quantified by constructing "artificial variables" that take on values of 1 or 0, indicating the presence or absence of the attribute in question.

6. These figures were provided to me by the Center on Budget and Policy Priorities, whose source was the Congressional Budget Office.

7. It also should not be forgotten that the slow growth of the American economy since the early 1970s has been at least part of the cause of the rise of incomes at the top of the income distribution and the fall of those at the bottom (see, for example, Papadimitriou and Wolff 1993, Wolff 1994, Hungerford 1993, Phillips 1990, and Levy 1988). Had there been sufficient economic growth, the current discussion about welfare and the EITC might be unnecessary.

8. The benefits to working families suggested here would essentially be no different from the expansion of the EITC suggested by Bane and Ellwood, who would have tripled the 1992 value of the EITC from $1,800 to $5,400. Bane and Elwood also would have eliminated food stamps but, in addition, would have raised the minimum wage from $4.25 to $5.50 (Bane and Ellwood 1994, 148–150).

9. This figure is derived by multiplying the current number of AFDC families by the maximum CSAS benefit for a family with two children ($3,500).

10. These figures are derived by multiplying the entire current AFDC caseload by the maximum nonworking benefit of $4,392 (to arrive at the $22 billion figure) and by multiplying the entire caseload by the maximum working benefit of $5,500 (to arrive at the $27.5 billion figure).

11. These proposals are similar in spirit to those of Robert Haveman, who advocates reforming the welfare system to achieve equity and efficiency (Haveman 1988). His idea is to generate opportunities, offer effective incentives to work, and make individuals responsible for their own actions. The CAP's child support component flows from Haveman's uniform child support system, in which the message to fathers is that they must support their children.

12. The value of monthly food stamp benefits is equal to the maximum allowable benefit ($295 for households containing three people) minus 30 percent of monthly counted income. Counted income is defined as gross monthly income minus a standard deduction of $131 minus 20 percent of monthly earned income minus monthly dependent care expenses up to $175 per dependent over age two and $210 per child under the age of two (U.S. House of Representatives 1994, 761–769).

13. The tax figure is from *Tax Policy Note* (1994). The $2,000 expense for child care, based on the figures used in tables 2 and 4, is based on the assumptions many make with regard to what a mother with two children ought to expect to pay for these services (see, for example, Bane and Ellwood 1994, 146–147; and *Tax Policy Note* 1994).

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