The factors which contribute to the inadequacy of welfare reforms and welfare programs of the past

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THE FACTORS WHICH CONTRIBUTE TO THE INADEQUACY
OF WELFARE REFORMS AND WELFARE PROGRAMS
OF THE PAST

A THESIS
SUBMITTED TO THE FACULTY OF ATLANTA UNIVERSITY IN
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BY
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DEPARTMENT OF ECONOMICS
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Finally, this paper is dedicated to the late Keathen Wilson, Sr. and to all people who are downtrodden for any reason but who have learned how to be survivors.
INTRODUCTION

The factors which contributed to the failure of welfare reforms and welfare programs of the past are well documented. After two decades of various welfare reform proposals it is clear that the welfare reforms and welfare programs of the past have fallen short of our major welfare reform goals. There may be several reasons for this assessment including high expectations, the conflicting nature of our welfare reform goals and inadequate funding. However, some of the problems of the current system are glaring. They include the following:

1. The present system provides inadequate coverage for both the working poor and the poor who are unable to work.

2. The present system is plagued by administrative inefficiency.

3. Twenty-five million people are still below the poverty level.

4. The cost of the present system has become a burden to state and local governments.¹

In recent years incremental and comprehensive reforms have been advanced to improve the efficacy and efficiency of the welfare system. Comprehensive reforms such as work-welfare approaches, and comprehensive cash assistance approaches (which includes guaranteed incomes) have gained some support in recent years. The work-welfare approaches focus on the often neglected demand side of the labor market and the

comprehensive cash assistance approaches focus on providing a basic income support level and an equitable distribution of benefits. Both types of welfare reform try to deal effectively with the tradeoffs that are involved in meeting our welfare reform goals. Some of the proposed welfare reforms could offer some improvements to the efficacy and efficiency of the welfare system.

This thesis explores the following:

- The welfare system and an assessment of it in terms of our major welfare reform goals.

- The two major types of welfare reform approaches - the work welfare approaches that focus on the demand side of the labor market and the comprehensive cash assistance approaches that focus on a basic income support level.

- The effect of income guarantees on work - some of the potential economic consequences.

- An assessment of the 1977 Carter administration's program for Better Jobs and Income (PBJI) an unsuccessful welfare reform proposal that incorporated both a demand side of the labor market focus (a guaranteed jobs program) and a comprehensive cash assistance approach for those who were unable to work.
CHAPTER I

BACKGROUND AND RELATED LITERATURE

The Welfare Reform Goals

The literature on welfare reform consists of a myriad of proposals and/or approaches and analyses of their effects. In addition, the problems of the welfare system and the resultant effects are often analyzed. The fundamental goals of welfare reform are based realistically on problems of the welfare system.

The perceived problem areas that make up the 'welfare mess' and how welfare reform should proceed are dependent on the goals established for the welfare system. Though there is not complete agreement on priorities, goals, and strategies, several goals are often mentioned as desirable.

The welfare reform goals most often cited are:

1. Adequacy (an adequate level of support that will allow families to subsist);

2. Horizontal Equity (recipients in corresponding situations should receive corresponding benefits);

3. Vertical Equity (the more one earns, the more he or she keeps; the most needy are to receive the most benefits);

4. Work Incentives (those able to work are effectively motivated to do so);

5. Family Stability Incentives (family structure should only be minimally affected by welfare programs);

6. Administrative Efficiency (the operation of the system should be done at the lowest cost); and

7. Target Efficiency (benefits should go to those most in need).

In the real world, the basic goals must be compromised to varying extents to create welfare reform plans that are
integrated* and practical given the conflicting character of these goals.1

The concept of adequacy is built on the idea that the poor receive some minimum level of benefits and/or income that is adequate to live on from an income-tested transfer system. Ideally, this "income-tested transfer system should work in conjunction with employment and social insurance systems."2 The concept of adequacy is not easily measured and is a topic of debate. The increasing difficulty of evaluating the concept of adequacy can be based on two factors. First, there is no consensus as to how adequacy should be defined, and second, measurement of adequacy has been complicated by the advent of the numerous in-kind programs.3

The major issue is whether an absolute or a relative definition of adequacy is appropriate. An absolute definition treats adequacy as that level of income required to provide an individual or family the bare minimum food, clothing, shelter, and related services necessary to avoid severe deprivation. A relative definition views poverty in terms of a comparison between income available to the less well off and that available to others in the society.4

*The meaning of the word integrated as used in this discussion is to unite the various and interrelated programs of the welfare system into effective systems.


2Ibid.


4Ibid.
The concept of target efficiency advocates that benefits should be directed to the most "needy."¹ "Within a given budget constraint, greater benefits should be transferred to those of lower incomes."² Categorization of recipients is used to provide target efficiency since categorization is supposed to assure that benefits of a given program are received by the most needy groups of people to the greatest extent possible. This approach excludes certain groups according to the programs' standards.³ The categorical nature of the need-tested welfare programs requires that recipients not only be needy but additionally requires that recipients are in a particular demographic category such as aged, disabled, blind, or in a family with dependent children headed by a woman or in some states an unemployed male. Thus, if individuals or families do not fall in these categories they will be excluded. The most needy are individuals and families with low incomes, especially those groups having a higher than average incidence of poverty such as blacks, families with children, and the aged.

The concept of administrative efficiency says a system should achieve its goals at a minimum cost. Ideally, simplicity should be characteristic of the system's operation for both administrator and recipient. Integration and coordination should be attained with multiple programs to control costs and to make the system manageable. Administrative efficiency is difficult to obtain when there is a lack of

¹"Needy" is used throughout this paper to mean families or individuals with incomes below the poverty level, adjusted for inflation. In 1981 that level was $8,414 for a family of four.


³Ibid.
The equity concept or issue of fairness is two interrelated issues: horizontal equity and vertical equity. Horizontal equity states that people in similar circumstances should receive similar benefits. Categorization with its accompanying shortcomings is used to determine similar circumstances. Differing program rules and wide interstate differentials lead to inequities. The wide interstate differentials are caused by each individual state determining benefit levels, eligibility, and other program criteria. As a consequence of such wide administrative discretion, differences in state benefit levels cannot be explained by income differences or cost of living differences when states are compared. Also, gaps in the categorization process can lead to some families or individuals being eligible to receive assistance while other families or individuals are ineligible to receive assistance even though their situations are similar. Another cause of inequity is a notch, a point in the public assistance benefit scale where one additional dollar of earnings makes a recipient ineligible for other programs.

Vertical equity stresses that families and/or individuals "who earn more income should receive more total income." Concurrently, those who need the most assistance should receive the most assistance. One underlying principle of vertical equity is to circumvent any

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1 Ibid.
2 Ibid.
3 Ibid.
4 Ibid.
delimitating effect of the welfare system on the functioning of the labor market. The idea that the welfare recipient should not be better off than the working poor is one basis of the political controversy of vertical equity.\(^1\)

The concept of work incentives states that individuals who are employable should have strong motivation to work. The welfare system should not promote dependency on its assistance. Higher disposable income should reward those who work and earn more. The notches and high cumulative benefit reduction rates in the present welfare system have a negative effect on work incentives.\(^2\)

The idea of family stability incentives is an important concept. It is desirable that a system should keep to minimum incentives that would lead to the break up of the family. The effect of this system of programs on children, women, female-headed families, working fathers, the aged, etc. has been a cause of some concern and some intensive research. The fact that some families would be better off in terms of their eligibility for welfare benefits if the parents were separated or divorced has been a major concern. A serious problem that can accompany the categorical nature of the programs is that people may be encouraged to make themselves part of the target group to receive greater benefits\(^3\) via separation or divorce.

\(^{1}\)Salamon, Welfare: The Elusive Concensus, pp. 46-47.


\(^{3}\)Ibid.
Incremental and Comprehensive Reforms

The essential issue is how to implement these basic welfare reform goals:

1. What approaches should be utilized and why?
2. What advantages and disadvantages do these approaches have?
3. What are the trade-offs of these approaches?

In recent years, there have been two basic types of approaches advanced, the incremental change approach and the comprehensive restructuring approach. Discussion and analyses of these approaches and plans are based on how well these plans work toward reaching welfare reform goals as well as how feasible they are in a given political climate with philosophical and budgetary restraints. Important or key features are the cost of the plan, the effectiveness of work incentives in the plan, and the level of assistance for recipients in the plan.

The incremental change approach entails step by step modifications of the system to eradicate its problems. The form of the welfare system would remain intact and thus allow for only categorical changes. The financial responsibility for the programs would remain with state, federal, and local governments.1 In the past, the welfare system has been developed by the incremental approach and these revisions have increased and broadened the benefits but have distributed them unevenly.2


The cited advantages of this approach are its political feasibility and its relative low cost when compared with the other approaches. Disadvantages of this approach are that this type of change does nothing to improve the system's faulty structure and that the welfare recipients and the public's dislike for the system will remain. Advocates of comprehensive restructuring assert that piecemeal reforms are being oversold as a strategy.\textsuperscript{1} However, many economists and social theorists feel that after reviewing the current difficulties associated with welfare reform policy, the incremental approach is the only realistic approach. They think that comprehensive restructuring is not only politically impossible, it is unnecessary and undesirable.\textsuperscript{2}

Advocates of a comprehensive restructuring approach have advanced a number of possible approaches to meet many of the welfare reform goals. These include the work-welfare, multi-track approaches for those who are able to work and a comprehensive cash assistance approach for those who cannot work. The latter entails the use of a single cash payment system that would replace many of the current programs. Each one of these types of approaches have trade-offs to be considered. Advocates of sweeping change have proposed widely divergent plans.

Work-welfare plans to provide public service employment for those who are able to work but not able to secure the needed


employment with the private sector. Concurrently, the work-welfare approaches provide training and placement services for those who can work to better enable them to be absorbed into the private sector. Advantages of these approaches are that taxpayers are more willing to reward work than to provide welfare and that the government provides work opportunities. Disadvantages are that job creation is costly and no mechanisms or strategies have been developed to create a large number of public service jobs.1

Guaranteed Incomes

Proponents of comprehensive welfare reform have advanced many guaranteed income plans over the years. Guaranteed income plans advocate the government providing a minimum level of income for those who are unable to earn enough by working. These plans would increase welfare payments for millions of Americans and increase the cost of the welfare system. Advocates of this type of plan hope that a single system of cash benefits would eliminate the administrative complexity of the existing system.2

To be feasible, a guaranteed income must meet three basic criteria: (1) the cost of the plan must be reasonable, (2) the plan should have effective work incentives, and (3) the plan should provide an adequate level of support. Ideally, these three conditions should be achieved simultaneously and herein lies a major problem. Benefit levels, the marginal rate of taxation, and overall program costs are


tightly interwoven factors, to adjust one of these factors you must adjust the others.\textsuperscript{1} Thus, meeting the basic criteria of reasonable cost, adequate levels of support, and effective work incentives simultaneously is difficult to achieve.

The marginal tax rates of a guaranteed income plan provide the work incentives of the plan. The marginal tax rate is based on the schedule of reduction in benefit payments as a welfare recipient's income increases. This tax has the same effect as normal taxes on the incentive to work. A high marginal tax rate placed on welfare recipients would negate the financial motivation for working. Some welfare experts assert that it is impossible to have low welfare tax rates and give substantial benefits to the working poor while maintaining a low cost. Obtaining any two objectives conflicts with a third.\textsuperscript{2}

\textbf{The Effect of Income Guarantees on Work}

The research on the effects of guaranteed income plans on work is inconclusive. The results of the most well known guaranteed income experiment, the New Jersey Income Maintenance Experiment, indicated that the work effort of employed males was only marginally affected by the availability of an income guarantee regardless of the tax rates.\textsuperscript{3} Other studies conclude that guaranteed income plans produce a work reduction effect among low income workers. Some studies estimated a

\textsuperscript{1} Ibid., pp. 37 and 39.


work reduction effect of 50 percent.¹

Program for Better Jobs and Income

The 1977 Carter administration proposal called the Program for Better Jobs and Income utilized both a comprehensive assistance approach and a guaranteed jobs approach to help those who could not work and those who could. It proposed cashing out AFDC, SSI, and food stamp benefits and combining these with a jobs program. This proposal, which was not passed by Congress, provided improvements such as a national minimum benefit level and administrative improvements. Some of the proposal's perceived shortcomings were its relatively high cost, its administrative complexity, and its level of work disincentives.²

Chapter two provides an overview of the system of welfare programs and an assessment of the welfare system in terms of the major welfare reform goals. A description of the various programs' functions and costs is provided. An assessment of the welfare system in terms of adequacy, equity, administrative efficiency, target efficiency, work incentives, and cost is also provided. This assessment provides insight into the magnitude of the welfare system's problems.

Chapter three examines the two major welfare reform approaches, the incremental change approach and the comprehensive restructuring approach. This chapter includes an assessment of these approaches and the work-welfare approaches, comprehensive cash assistance approaches,


and the multi-track approach. This chapter also closely examines the guaranteed income approach.

Chapter four examines the effect that income guarantees have on the work effort of the recipients. It also explores some potential economic consequences of income guarantees. Also, this chapter reviews three types of studies and some of their findings on the effect that income guarantees have on work. The chapter also explores the economic theory of work and leisure.

Chapter five examines the 1977 Carter administration proposal Program for Better Jobs and Income (PBJI). This chapter illustrates how some welfare reform proposals fail to effectively deal with the trade-offs involved with welfare reform. An assessment of the PBJI in terms of the welfare reform goals is also included. Further, the chapter provides insight into the difficulties of welfare reform.

Chapter six is a summary of findings and recommendations. The findings and recommendations of this study provide an analysis of the problems of the welfare system and welfare reform approaches to improve it. This study also should provide insight into the difficulties of welfare reform.
CHAPTER II

AN ASSESSMENT OF THE WELFARE SYSTEM

The welfare system was designed to address the survival problems of the low income population and, though it has succeeded in helping many people, welfare experts think that the welfare system has major problems. The welfare system consists of programs that offer cash assistance including: Aid to Families with Dependent Children (AFDC) which offers support to needy families with children; Supplemental Security Income (SSI) which offers assistance to needy people who are aged, blind, and disabled; The Earned Income Tax Credit (EITC) which gives aid through a tax break to low income workers; and The General Assistance program (GA) which is a set of state programs that provide assistance to needy persons who are ineligible for the federal programs. In-kind benefits which consist of goods and services for the needy are currently available through the Food Stamp program, Medicaid, the Child Nutrition program, and housing assistance programs.1

The Cash Assistance Programs

AFDC

AFDC and its related programs offer cash assistance to low income female-headed families with dependent children and to families

where the father is unemployed, disabled or incapacitated (twenty-six states have an unemployed parent program (AFDC-UP) which include the male-headed households). The federal outlays for this program in fiscal year 1981, as proposed by the Carter Administration, would have been $7.8 billion. Nearly eleven million people receive AFDC benefits. 1 AFDC does not have a national minimum or basic needs standard. Eligibility for AFDC is determined by the individual states and thus benefits vary widely from state to state. Financial responsibility for the program is divided among federal, state, and local governments. In recent years, the states and localities have assumed about 45 percent of the cost while the federal government has assumed about 55 percent of the cost of this program. 2

SSI

The SSI program provides cash assistance to needy aged, blind or disabled individuals. Some states supplement the basic federal grant with state payments. The federal outlays for this program in fiscal year 1981, as proposed by the Carter Administration, were $7.3 billion. This program has automatic cost of living increases in benefit levels and has 4.2 million recipients. 3 In recent years, benefit levels for SSI recipients have reached 73 and 83 percent of the


poverty threshold for one and two member families, respectively.\footnote{U.S. Department of Health, Education and Welfare, \emph{Welfare Reform: Issues, Objectives and Approaches}, p. 6.}

\textbf{EITC}

EITC aids low income workers by providing a tax credit that reduces the amount of income tax they are required to pay. If the credit amounts to more than the taxes owed, the workers get the amount of the difference rebated to them. In 1979, the credit was 10 percent of the first $5,000 of income and reduced at a rate of 1.25 percent of each $110 earned above $6,000 of income.\footnote{U.S. Congressional Budget Office, \emph{The Budget of the United States, Fiscal Year 1981}, p. 258.} The cost of this proposal as proposed by the Carter administration was $1.9 billion in fiscal year 1981.\footnote{\textit{Ibid.}, pp. 260-272.}

\textbf{General Assistance (GA)}

General Assistance is provided by states to aid needy persons who are ineligible for the federal programs. These programs are entirely financed by state and local governments in thirty-three states. Benefit levels provided vary widely from state to state and are limited in nature.\footnote{Vee Burke, \emph{Federal and State-Local Expenditures for Income Transfers to Persons with Limited Income, Fiscal Years, 1975 and 1976} (Washington, D.C.: Government Printing Office, 1976), p. 11.} In fiscal year 1981 the cost of these programs to the states will be over $1.1 billion.\footnote{U.S. Department of Health, Education and Welfare, \emph{Program for Better Jobs and Income (PBJI)} (Washington, D.C.: Government Printing Office, 1978), p. 20.
In-Kind Programs

The Food Stamp Program

The Food Stamp Program helps needy families purchase food by providing a monthly allotment of coupons that can be exchanged for food. These monthly allotments of coupons are adjusted twice a year for changes in food prices. The amount of the monthly allotment received is determined by earned income and household size. A profile of food stamp recipients in 1976 indicated that a majority of the recipients had incomes below the poverty level, some 68 percent of the households were headed by females and 17 percent of the participating households had one or more member over age sixty-four. In fiscal year 1981, the cost of the program, as proposed by the Carter administration, would have been $9.7 billion. This program had 20.4 million recipients in fiscal year 1981. The federal government and the state governments equally share all of the administrative costs.

The School Lunch and Other Nutrition Programs

The school lunch and other nutrition programs provide indirect subsidies to needy and non-needy children through food assistance programs. There are fifteen separate federal programs that assist states in feeding children and other needy persons. Some of these programs are the National School Lunch program, the School Breakfast program, the Summer Feeding program, the Child Care program, and the Women, 

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Infants, and Children program (WIC). The WIC program is a special feeding program for women, infants, and children. In fiscal year 1981, over twenty-five million participants would have received $3.6 billion in subsidies, as proposed by the Carter administration for the school lunch and other nutrition programs. Also, over two million recipients would have received $903 million in benefits from the WIC program as proposed by the Carter administration in fiscal 1981.¹

**Housing Assistance Programs**

Housing assistance provided by the Department of Housing and Urban Development (HUD) offers economic assistance to support housing. Emphasis is on rental housing assistance for low income families and individuals. In fiscal year 1981 these programs would have cost $6.6 billion as proposed by the Carter administration. Also, HUD provided subsidies for subsidized housing which would have cost $914 million as proposed by the Carter Administration. Two major HUD rental housing programs are lower income rental assistance (Section 8) and public housing. The basic objective of these programs is to improve housing conditions for low income families and individuals. As of 1981, 1.1 million families occupied public housing and 1.3 million families received assistance from the Section 8 program.²

**The Medicaid Program**

The Medicaid program provides health care at little or no cost to the needy. In fiscal year 1981, Medicaid outlays of $15.9 billion

¹Ibid.
²Ibid.
would have financed care for twenty-three million people as proposed by the Carter administration. The funding for this program is divided among federal, state, and local governments. The states have responsibility for the administration of the program.¹

The Need for Welfare Reform

An assessment of the welfare system is necessary to evaluate the efficacy and efficiency of the system. This assessment of the welfare system will focus on the conceptual issues of adequacy, horizontal and vertical equity, target efficiency, work incentives, administrative efficiency, and cost. From this assessment we can determine how well the welfare system achieves its objectives. It is from this process that welfare reform proposals can be designed or improvements can be made to minimize waste and errors.

Adequacy

A comprehensive assessment of the distribution of income in the United States is provided by the Census Bureau's yearly analysis of the poverty population. According to the Census Bureau, in 1978, 24.5 million persons were below the poverty level, some 11.4 percent of the total U.S. population. The present system of cash assistance not withstanding, many remain below the poverty level. White families had a much lower rate of poverty (6.9 percent) than black families (27.5 percent). Groups having a higher than average incidence of poverty are

¹Ibid.
The Persistence of Poverty

The economic and social conditions of a country are major determinants of the extent of poverty experienced by citizens. There were several significant developments that affected the level of poverty in the United States in the past decade. One such development was a significant reduction in real economic growth. The recession of 1973/74 and the accompanying unemployment increased the incidence of poverty and negated, somewhat, the effectiveness of the income transfer programs. It is clear, however, that the impact of the recession and the ensuing unemployment would have been more severe without the benefits provided by the income transfer programs.

Changes in family composition were another important development. The proportion of female headed families in the population increased. When compared to other families female-headed families have a higher incidence of poverty. In 1977, 31.7 percent of all female-headed families were in poverty compared to 5.5 percent of other families.

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The low benefit levels of the welfare programs are also a factor in the persistence of poverty. An assessment of average monthly benefit levels in major cash assistance programs in a 1976 study indicated that between 1965 and 1975 social security was the only program whose average benefit level rose consistently.\(^1\) This explains why the proportion of the aged poverty population declined between 1965 and 1975. However, some programs like AFDC had a different experience. In the AFDC program, the average benefits increased significantly between 1965 and 1970 and then leveled off or declined in constant dollar terms between 1970 and 1975.\(^2\) This could explain why the proportion of female headed families in poverty increased despite the availability of a cash assistance program.

Leaks and Gaps in the Programs

The presence of gaps and leaks in the structure of the welfare programs are often cited as factors that explain the persistence of poverty.\(^3\) Most of these problems are caused by the categorical nature of the programs. Categories used to identify segments of the needy population such as the blind, disabled, and aged, exclude more people than they include creating huge gaps in coverage. This fault limits the assistance offered to segments of the poor population.

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\(^2\)Ibid.

The impact of the gaps and leaks as well as variations in benefits mitigate the effectiveness of the welfare system in raising the poor above the poverty level. A 1976 study indicated that only 44 percent of all pretransfer poor families rose above the poverty level as a result of benefits from the major income transfer programs. In addition, the public assistance category of the major income transfer programs aided only 5 percent of the poor in getting out of poverty.\(^1\)

Inequity

**Horizontal Inequities in Cash Assistance Programs.** Another major problem of the welfare system is the difficulty it has been having in addressing itself to the issue of basic fairness or equity. This is evidenced by the disparities faced by different segments of the poor population that are called horizontal inequities. Horizontal inequities are a pervasive problem in the welfare system. The combination of the categorical needs standards and the broad discretion left to states produces these inequities.\(^2\)

In particular, the eligibility standards of the need-tested programs have allowed large sections of the needy population, especially the working poor, to be excluded from federal cash assistance subsidies. Even though state general assistance programs are available for the poor who are ineligible for the federal programs, the general assistance programs provide only limited benefits and coverage.\(^3\) Another illustration of the horizontal inequities in the system are the

\(^1\)Plotnick and Skidmore, *Progress Against Poverty*, p. 147.


\(^3\)Ibid.
state variations in benefits and coverage. In the AFDC program, for example, the individual states are allowed to determine the benefit levels, eligibility, and other program criteria. Thus, there are wide variations in benefits, eligibility, and other program criteria from one state to another. A 1975 study by the Joint Economic Committee of Congress indicated that the differences in state benefit levels cannot be explained by income differences or cost of living differences when states were compared. For example, while Louisiana paid a maximum of $122 to an AFDC family in 1974, neighboring Mississippi, with per capita income three-fourths as high as Louisiana, was paying only half as much; nearby Oklahoma, with per capita income only 10 percent higher than Louisiana, provided twice as much.¹

Horizontal Inequities in the In-Kind Benefit Programs. Horizontal inequities are also found in the in-kind benefits program. Even though some programs such as the Food Stamp program have reduced horizontal inequities by providing additional benefits and coverage, other in-kind benefits programs have added to the problem. Mainly, participation in many of the in-kind benefits programs required participation in the categorical programs.² For example, AFDC recipients with incomes above poverty level (as a result of combined AFDC payments and Medicaid) can receive food stamps, whereas those with similar incomes from sources other than AFDC cannot. In addition, AFDC recipients, regardless of the presence of other post transfer income, are automatically eligible

¹Ibid.

for Medicaid while similarly situated non-AFDC families may not be.\footnote{Ibid.} Thus, pre-existing inequities are increased by the in-kind benefits programs. In addition to these inequities, the limitations inherent in the in-kind benefits program such as funding limitations and disparities in participation increase the problem.

**Vertical Inequities.** The issue of vertical inequity focuses on the advantages the welfare system sometimes provides for the poor versus the non-poor. A major concern that arises when addressing the issue of vertical inequity is that the welfare system may be enabling welfare recipients to live better than the working poor. One example of this concern is the effects of the provision that allows AFDC recipients to deduct work expenses from their income. Suppose there are two workers who earn $5,300 per year on the same job and one of them was on AFDC and one was not. If the worker on AFDC claimed work-related expenses (taxes, child care, etc.) of $1,000, then she/he could end up with $2,173 more than the non-AFDC worker. The bonus of $2,173 includes the amount of AFDC benefits entitled after work expenses and the additional flat $30 per month plus one-third of all remaining earnings from income before calculating the AFDC benefits.\footnote{Salamon, *Welfare: The Elusive Consensus*, p. 47.}

**Target Efficiency.** Target efficiency is the concept based on the idea that benefits should be directed to the most needy. In the welfare system, categorization is used to target benefits to the most needy and this causes some problems. The problem is that categorization has
excluded large portions of the needy population. Thus, leaks of bene-
fits to the non-poor and the exclusion of portions of the needy popula-
tion, which include the aged, families with children, the working poor,
and blacks, are major problems.\textsuperscript{1}

**Work Incentives and Marginal Tax Rates**

Work incentives are a major issue in the welfare system. The
goal of the public assistance programs is to avoid causing any negative
impact on the welfare recipients' incentive to work. The AFDC program,
for example, was fitted with a work incentives provision in 1967. This
provision permitted the states to deduct work expenses and $30 plus one-
third of the remaining income when computing benefits of recipients.\textsuperscript{2}

**Marginal Tax Rates.** The efforts to provide work incentives in
the welfare system have been somewhat mitigated by another factor, the
cumulative marginal tax rates of the programs.\textsuperscript{3} The marginal tax rates
are based on the schedule of reduction in benefit payments as a welfare
recipient's earned income increases. This tax has the same effect as
normal taxes on the incentive to work, the higher the tax the less the
motivation to work. Marginal tax rates differ from notches. With a
notch, one additional dollar of income can make a person ineligible for
other programs but in the case of marginal tax rates an additional
dollar in income results in only a partial reduction in benefits. The
size of that reduction in relation to the increase in income is the

\textsuperscript{1}Ibid., p. 38.

\textsuperscript{2}Ibid., p. 52.

\textsuperscript{3}U.S. Congress, Joint Economic Committee, *Welfare in the
Seventies, Studies in Public Welfare*, 93rd Cong., 2d sess, No. 15,
marginal tax rate.

In many instances, marginal tax rates of one program are added to the marginal tax rate of other programs in their effect on welfare recipients. The in-kind benefit programs that supplement AFDC have their own marginal tax rates, thus these tax rates combine with the marginal tax rates of the AFDC program and result in a greater loss in benefits. For example, while the AFDC program taxes net earnings at a 67 percent rate (benefits decline $2 for every $3 in earnings in excess of expenses and $30 per month), if an AFDC recipient participates in the Food Stamp program, they are taxed an additional 30 cents per dollar.

In a study of operations in 100 areas, the Joint Economic Committee concluded that in practice it was possible that the income remaining after work expenses and benefit reductions for employed AFDC and food stamp recipients can average as little as 20 cents per dollar earned.

A Series of Notch Problems

The welfare system's benefit scales have a series of problems called notches that also mitigate efforts to provide work incentives. A notch is a point in the public assistance benefit scale where one additional dollar of earnings makes a recipient ineligible for other programs. Ideally, programs like AFDC and food stamps have benefit levels that gradually decrease thus avoiding this problem. However, what happens in some programs like Medicaid is that an additional dollar of income can cause a family to be ineligible for $1,000 to $1,500

1 Ibid.
2 Ibid.
in medical care.¹ Notch problems not only affect AFDC recipients, but many others not on cash assistance.

**Impact of Work Disincentives.** Most analysts conclude that work disincentives such as cumulative marginal tax rates and notches in benefit scales do have a negative work effect on welfare recipients. However, this conclusion is not considered to be definitive² as the effects of welfare on work is still being studied. Some experts think that the strength of a negative work effect caused by disincentives is subject to factors such as age, sex, and marital status. Some research indicates that the negative work effect is small for working age males but somewhat stronger for married women, female family heads, and older men.³

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¹Salamon, Welfare: The Elusive Consensus, p. 50.
³Ibid.
including earnings, gifts, rent, child support, and social security. ¹

The level of benefits and eligibility for assistance can be affected by how income is defined.

The definition of countable income affects program costs both directly by affecting the number of recipients and the amount of benefits they receive and indirectly by necessitating increased administrative complexity. Under a broad definition of income, countable income would include all earned and unearned income as well as public and private transfer benefits. Some experts feel that a broad definition of income would minimize program eligibility and costs.

In some welfare programs certain expenses may be deducted from income to achieve increased equity or to provide financial incentives. For example, AFDC allows child care and work deductions. The food stamp program allows deductions for medical and shelter expenses.²

Asset tests (assets are cash, savings, checking accounts, and other resources (a car or home) that can be converted to cash for current consumption) establish limits on the amount of assets a recipient may have and remain eligible for benefits. Various welfare programs allow different assets to be excluded from the assets test.

For example, in the SSI program a limit is placed on the amount of cash a recipient may have on hand. In 1978 under the SSI program a recipient could exclude the value of household goods and personal effects up to $1,500, exclude the value of an automobile up to $1,200, and exclude entirely the value of an owner-occupied home.³

Lines of Authority. An additional problem is that the lines of authority of the system are not clearly demarcated among federal, state, and local agencies. Often, for the states, the administrative authority at the federal level becomes an additional complication. The

¹Salamon, Welfare: The Elusive Consensus, p. 53.
³Ibid.
states often must try to integrate federal regulatory changes with on-going state administrative practices. For example, when federal rules on the treatment of income of stepfathers in AFDC changed, state social service departments had to revise their data intake forms accordingly. Many states point out that there can be a large number of federal changes in a year.¹

Procedures and Structures. Other features that add to the administrative burden are: separate programs have both separate eligibility procedures and definitions of income; elaborate certification procedures must be repeated many times; and the programs have separate administrative structures.² AFDC, food stamps, and Medicaid eligibility, for example, are all determined by different procedures. Also, the definitions of income differ among these programs. For example, AFDC exempts the income of full and part-time students who are not full-time employees (as well as deducts one-third of all earnings above $30 a month plus work expenses). However, a program like the Food Stamp program does not differentiate between full and part-time students and provides deductions that include medical expenses and shelter costs in excess of 30 percent of nonexempt income.³

The elaborate certification procedures contribute to the administrative burden because of the dynamic nature of the welfare population. For example, most AFDC recipients are participants for less than two years at a time. The situations of recipients can change even in this

¹Ibid.
²Ibid.
period of time. Consequently, eligibility must be determined repeatedly. Elaborate recertification procedures are necessary, entailing complete affidavits and verifications.\(^1\)

The fact that separate administrative structures are designed for separate programs adds to administrative complexity. For example, aged food stamp recipients must locate not just the SSI intake office, but the food stamp office as well to participate. In addition, the in-kind programs require additional administrative apparatus to dispense benefits and verify results. Also, the Food Stamp program requires participants to make monthly or bi-monthly visits to stamp dispensing centers.\(^2\)

**Administrative Costs.** The cost of administration is increased by the administrative complexity throughout the system. For example, the direct cost of administration consumes approximately 12 percent of program costs in both AFDC and food stamps. Direct costs have increased rapidly on an absolute, per participant, and per $1,000 in benefit bases.\(^3\) The direct administrative costs are for personnel, including the extra personnel needed for the checking and rechecking of eligibility. For example, administrative costs in the AFDC program increased from $88.45 per $1,000 in benefits in 1971 to $123.90 in 1975 and to $147.93 in fiscal year 1977. Table 1 gives administrative costs for three programs for the years 1971, 1975, 1977.

\(^1\)Ibid.

\(^2\)Ibid.

TABLE 1

ADMINISTRATIVE COSTS IN MAJOR PUBLIC ASSISTANCE PROGRAMS,
FISCAL YEARS 1971, 1975, 1977

<table>
<thead>
<tr>
<th>Program</th>
<th>Total (millions of dollars)</th>
<th>Per Participant</th>
<th>Per $1,000 of Benefits</th>
</tr>
</thead>
<tbody>
<tr>
<td>AFDC</td>
<td>485</td>
<td>1,042</td>
<td>1,496</td>
</tr>
<tr>
<td>Food Stamps</td>
<td>104</td>
<td>592</td>
<td>689</td>
</tr>
<tr>
<td>SSI(^b)</td>
<td>-</td>
<td>460</td>
<td>592</td>
</tr>
</tbody>
</table>

\(^a\)Projected.
\(^b\)Includes federal costs only.

A major indirect cost is the cost caused by the number of errors in the system. This indirect cost of administration have increased because of the number of errors made in administering the programs. A 1973 HEW National Survey of AFDC errors, indicated that nearly 41 percent were in error either because of overpayment, underpayment or ineligibility. Further, despite a quality control program that was initiated in 1974 to correct these errors, 27 percent of the cases were still found to be in error by the end of 1975. Many welfare experts feel that the complexity of the welfare programs invites errors.¹

The Growth in Welfare Expenditures

In fiscal year 1981, the major income tested assistance programs; AFDC, SSI, Food Stamps, EITC, and General Assistance, as proposed by the Carter administration, would cost over $30 billion for over 40 million recipients.² The growth of expenditures for welfare benefits and coverage has been the focus of some concern. One example of this growth is that the federal income assistance expenditures grew at a rate that was two-thirds higher than the rate of growth of the federal budget between 1965 and 1975.³ Inflation, expansion of coverage, and policy changes all contributed to the rapid growth of welfare costs. A significant series of eligibility extensions, the creation of new programs or major revisions of in-kind programs

¹Ibid.
³Plotnick and Skidmore, Progress Against Poverty, p. 110.
dramatic expansions in program costs.\(^1\)

The way in which costs of income assistance programs are distributed has become a burden to state and local governments as total costs have increased due to inflation and expansion of benefits and coverage. All of the major need based assistance programs (AFDC, SSI, EITC, etc.), with the exception of food stamps, require state/local financial participation.\(^2\) The state and local governments are required to pay up to 50 percent of the costs of some programs, and the costs of the programs have been rapidly increasing over recent years.\(^3\)

Despite a general increase in the relative size of the federal contribution, state and local spending on needs-tested programs increased more than four-fold in actual dollars, and two and one-half times in constant dollars from 1965 to 1975.\(^4\) One study of state spending determined that public welfare consumed 18.5 percent of all state spending in 1975, up from 13.2 percent in 1965. Table 2 gives the state spending percentages on welfare for selected states and compares them for years 1965 and 1975. The escalation of state and local costs as prompted by expanded AFDC participation, increased AFDC benefit levels, and the Medicaid program. As a result of these factors, welfare spending has been increasing at a rate 40 percent faster than the rate of growth of overall state spending. Added to this burden is the fact that thirty-three states finance general assistance programs

\(^1\)Ibid.


\(^3\)Ibid.

for needy persons who are ineligible for federal assistance.¹

TABLE 2
STATE SPENDING FOR PUBLIC WELFARE AS A PROPORTION OF ALL STATE SPENDING, 1965 AND 1975, SELECTED STATES (PERCENTAGE)

<table>
<thead>
<tr>
<th></th>
<th>All Sources 1965</th>
<th>All Sources 1975</th>
<th>State Sources Only 1965</th>
<th>State Sources Only 1975</th>
</tr>
</thead>
<tbody>
<tr>
<td>California</td>
<td>17.3</td>
<td>24.3</td>
<td>10.9</td>
<td>17.4</td>
</tr>
<tr>
<td>Connecticut</td>
<td>14.8</td>
<td>19.9</td>
<td>10.7</td>
<td>12.3</td>
</tr>
<tr>
<td>Georgia</td>
<td>13.6</td>
<td>18.2</td>
<td>5.7</td>
<td>8.0</td>
</tr>
<tr>
<td>Louisiana</td>
<td>19.4</td>
<td>12.4</td>
<td>8.0</td>
<td>5.6</td>
</tr>
<tr>
<td>Michigan</td>
<td>9.5</td>
<td>27.1</td>
<td>5.6</td>
<td>20.2</td>
</tr>
<tr>
<td>Mississippi</td>
<td>14.4</td>
<td>12.5</td>
<td>6.9</td>
<td>5.7</td>
</tr>
<tr>
<td>New York</td>
<td>14.2</td>
<td>23.7</td>
<td>7.6</td>
<td>10.2</td>
</tr>
<tr>
<td>Oregon</td>
<td>10.2</td>
<td>15.5</td>
<td>8.7</td>
<td>11.8</td>
</tr>
<tr>
<td>Texas</td>
<td>12.1</td>
<td>13.9</td>
<td>4.2</td>
<td>5.2</td>
</tr>
<tr>
<td>All</td>
<td>13.2</td>
<td>18.5</td>
<td>7.5</td>
<td>11.8</td>
</tr>
</tbody>
</table>


In conclusion, the welfare system fails to achieve many desired goals. The welfare reform goals of adequacy, equity, target efficiency, administrative efficiency, and work incentives are being inadequately met. Waste and error, inequities, poor coordination, inadequacies, and complexity prevent the welfare recipients and society from obtaining maximum benefits from the system. The continuing search for welfare reform ¹Ibid.
strategies must center on effectively dealing with the trade-offs and conflicting character of our welfare reform goals.
The basic controversial issue of welfare reform focuses on how to change the welfare system to more optimally provide assistance to the low income population given budgetary and political restraints. The major questions are: (1) Should the present system be modified (an incremental change approach)? (2) Should the present system be abolished in lieu of an entirely new one (a comprehensive restructuring approach)? The alternatives are still being debated and examined. The alternative that is selected must deal with the trade-offs that are involved in meeting our major welfare reform goals.

The Incremental Change Approach (Incremental Reform Approach)

The incremental change approach entails step by step modifications of the welfare system to eradicate its problems. The categorical system of benefits would be retained and administrative obligations would remain divided among the federal, state, and local governments. The incremental change approach has been used to make improvements and address problems of the welfare system in its development. Thus, it is in keeping with the traditional modus operandi of the welfare system to use an incremental change approach to eliminate its problems.¹

Proponents of the incremental change approach state that this approach could improve the efficacy and efficiency of the welfare system in the following ways: (1) Improve program administration through new designs and rules; (2) Standardize the benefits of existing programs; and (3) Broaden and liberalize eligibility standards. Ultimately these modifications would lead to a more equitable distribution of benefits, reduced program expenditures, and better targeting of benefits on the most needy.\(^1\) If all necessary reforms are implemented experts think that the incremental change approach can lead to a system that is very similar to types proposed by advocates of the comprehensive restructuring approach without its uncertainty and greater initial costs.\(^2\)

Advantages of the Incremental Change Approach

Advocates of the incremental change approach cite economic and political advantages of this approach over the comprehensive restructuring approach. First, the initial cost of an incremental change approach is estimated to be low when compared with the cost of initiating an entirely new system as sought by advocates of the comprehensive restructuring approach. Second, experts predict that comprehensive reform proposals will cost more than the existing system on the average because most of the comprehensive reform proposals will considerably expand the eligibility of the existing system and thus increase the number of participants.\(^3\) In the present political climate, with its

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\(^1\) Ibid., p. 33.


emphasis on fiscal restraint and budget reductions, low costs are important.

The incremental change approach is also more acceptable than a comprehensive restructuring approach to the welfare bureaucracy and those with welfare interests because the effects of a wide sweeping change have not been determined. Although there have been a number of social experiments and a considerable research effort, not enough is known about the effects of a totally restructured system on labor markets, industry, and family and social patterns. Early in the Carter administration, the then Secretary of the Department of Health, Education, and Welfare (HEW), Joseph Califano, leaned toward the incremental approach for similar reasons. He stated that, "...millions of Americans have come to depend on existing programs and would face the possible disruption of their lives if the benefits system was subjected to extensive and untested change." Many congressional leaders also favor an incremental change approach in improving the welfare system.

Disadvantages of the Incremental Change Approach

Many critics of the incremental change approach point out that this approach does not correct the defects of the welfare system's structure. The welfare system's complexity, overlapping programs, and ill-coordination will remain. Thus, all of the defects of piecemeal design will remain. Without integration and coordination of the programs and functions, the effectiveness of this approach would be

1 Ibid.

Finally, advocates of the incremental change approach assert that this approach is a more viable means of reform. Many economists and social theorists feel that after reviewing the current difficulties associated with welfare reform policy, the incremental approach is the only realistic approach. These experts assert that not only is comprehensive restructuring politically impossible, but it is unnecessary and undesirable.  

The Comprehensive Restructuring Approach
(Comprehensive Reform Approach)

The comprehensive restructuring approach offers a number of proposals to improve the efficacy and efficiency of the welfare system. Proposals fall in two basic categories: (1) A work-welfare approach or multi-track system for the needy who are able to work and those who are not able to work, and (2) A comprehensive cash assistance approach or negative income tax that would provide a single program of cash benefits and eliminate the present system of cash and in-kind benefits. These proposals would implement new strategies and phase out all or most of the present systems' structures.

The Work-Welfare Approach - The Demand Side of the Labor Market

The most unique feature of recent and pending work-welfare reform approaches is their explicit focus on the demand side of the labor market.

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market. The immediate objective of these reforms is to create jobs that welfare recipients can fill immediately. Thus, work habits and skills acquired can lead to financial independence. This approach offers hope of increasing the employment of the poor and reducing welfare caseloads.1

Many previous reforms such as the 1967 Work Incentive Program (WIN) emphasized investments in human capital that focused on the supply side of the labor market. The goal of these reforms was to alter the characteristics of welfare recipients by making them more attractive to employers on the theory that a skilled worker creates his own demand. Thus, the demand side of the labor market was not focused on. It was implicitly assumed that jobs for welfare recipients were already there in the form of standing vacancies or would soon be created when employers saw the transformed labor supply entering the market. The importance of these recent reforms is not the availability of job opportunity (WIN and WIN II were job oriented programs), but the focus on these types of opportunities and the level of funding for these programs. Ultimately, these reforms and some recent experiments seek to expose more welfare recipients to these opportunities while reducing or eliminating supply side services.2

The work-welfare approach makes working or a willingness to work a condition for program participation. This approach separates the low-income population into two groups: those who are employable and those who are not employable (includes the aged, the disabled, and


2Ibid.
those who care for small children). Those who are not employable would receive benefits through categorical programs (AFDC, SSI, etc.) or a comprehensive cash assistance plan. Those who are employable would receive assistance in one of three forms: work conditioned benefits which are connected to earned income, a guaranteed job program providing public or private sector employment, and benefits that would be tied to training, educational, and employment programs. The work-welfare approach also has a major goal of providing training and placement services for those who are employable to better enable them to be absorbed into the private sector and thus reduce long-run costs for the total program.1

The Guaranteed Jobs Approach

An important alternative within the work-welfare approach is the guaranteed jobs program. The objective of the guaranteed job program is to provide either public or private sector jobs to low-income families with an employable member. Government extension of tax credits and wage subsidies is designed to encourage employers to create private sector jobs. The guaranteed jobs programs would offer job opportunities to welfare recipients, who may not ordinarily get this opportunity.2

The Work Equity Project. One recent demonstration program testing the guaranteed jobs approach that has received much attention is The Work Equity Project (WEP). WEP is a guaranteed, mandatory jobs program that has been underway since mid-1978 in Minnesota. This


2Ibid.
program requires that all employable AFDC, General Assistance, and Food Stamp recipients in participating counties accept jobs in community work projects, if other suitable employment cannot be secured. WEP is funded and designed to supply jobs for all employable welfare recipients. A distinguishing feature of this program is that unlike WIN, CETA, Supported Work, Mr. Reagan's welfare reform in California, and other similar programs, it is in a position to serve all eligible recipients. WEP therefore is testing a program's ability to create jobs.  

Though preliminary assessment of the work-welfare demonstration projects indicate that participants did go on to find more and better employment, the overall net results have been only modest. One predominant problem in the several work-welfare demonstration projects examined was that there was a high early drop-out rate of participants. Administrators found that providing jobs in the public sector was not difficult but providing welfare recipients with skills, services, and confidence was a formidable task.

Trade-Offs of the Guaranteed Job Approach. Advocates of the guaranteed job approach cite two major advantages over the other alternatives: (1) Taxpayers are more willing to reward work than to provide welfare, and (2) A government guarantee of the right to work. Critics of this approach cite many perceived drawbacks. Mandatory work-welfare reforms have the drawback of not offering any provisions for child care or transportation costs. In addition, participants are not allowed to choose their employer which can be an important decision. Other major

\footnote{Schiller, "Welfare: Reforming Our Expectations," p. 59.}
problems are:

1. Whether it will be possible to create the necessary number of jobs (one to two million)? The question becomes more difficult in times of sluggish economic growth.

2. How could it be ensured that jobs are distributed in the areas of the eligible population and that these jobs would match the skills of the recipients?

3. Would mass public service employment provide meaningful work experience that would lead to private sector employment?

4. Will guaranteed public jobs undermine the low wage private sector of the economy by being more attractive than low wage private sector jobs?

5. Will guaranteed public sector jobs displace state and local employees?

6. Will the cost of a guaranteed jobs program be exorbitant (one million jobs could cost as much as $8.3 billion)?

Work-Conditioned Benefits Programs

Work conditioned benefits programs reward work by providing a wage subsidy to overall earnings that is tied to the number of hours worked or by an earned income tax credit. Work conditioned programs seek to direct benefits to the working poor. These programs focus on assisting the employable population. For example, in one work conditioned program proposal the participants would lose only a fraction of their AFDC benefits with an increase in earnings, leading to an increase in total income, but one that was less than the additional earnings. In other words, if earnings were increased by $1,000, income would increase by less than $750 because of a partial but not equivalent reduction in welfare payments. With the exception of the EITC,

most current programs do not focus on the working poor and work conditioned programs could increase their coverage and benefits.\(^1\)

Trade Offs of Work Conditioned Programs. Advocates of this approach cite these advantages: (1) Those working full-time but earning an inadequate income would have their earnings supplemented; (2) this approach strengthens the attachment of the low income population to the labor market because participants are rewarded for having job and benefits rise with additional work effort; (3) these financial incentives encourage job searching and independence.\(^2\)

Critics of work conditioned benefits cite these problems: (1) This type of reform could further complicate administrative procedures instead of simplifying them; (2) this approach could inefficiently target benefits on the poor because wage subsidies and tax credits are difficult to relate directly to need as determined by family characteristics; and (3) there is no provision in this approach to aid those who are employable but are not fortunate enough to obtain jobs.\(^3\)

A Multi-Track Approach

A multi-track approach entails the utilization of different types of separate programs to meet the various needs of the low income population. Each track is a different program to meet different needs. One track that would aid workers with low paying jobs is a work-conditioned benefits program. Other tracks include a welfare benefits

\(^1\)Ibid.
\(^2\)Ibid.
\(^3\)Ibid.
program for those who are not employable and an unemployment insurance program for the unemployed not eligible for the regular insurance benefits.

Trade-Offs. Advocates of the multi-track approach cite these advantages over the other work-welfare approaches: (1) The multi-track approach acknowledges that potential recipients may not have enough training for needed public or private sector jobs; and (2) This approach also allows for the possibility that a guaranteed jobs program may be difficult to set up on a large enough scale. Critics of the multi-track approach cite two basic problems: (1) The complexities of administering a multi-track program, and (2) potential problems that are associated with the guaranteed jobs approach, such as job creation, job distribution, etc.

Comprehensive Cash Assistance

The comprehensive cash assistance approach would provide a single cash system that would replace many of the current programs of the welfare system. This approach would be universal in nature as opposed to the categorical format for current programs. Other characteristics of this approach are: (1) benefits would be available to those who meet simplified criteria; (2) criteria would stress the incomes and assets of applicants rather than their family situations or potential for employment; and (3) work incentives would stem from benefits and would phase out gradually so that those who worked would be better off than those who did not. Comprehensive cash assistance

1 Ibid.

2 Ibid.

3 Ibid.
approaches include the Negative Income Tax programs (NIT) and the
guaranteed income proposals.

Trade-Offs. Advocates of the comprehensive cash assistance
approach cite several advantages this approach has over the others:

1. This approach would be more equitable because it would
provide a more uniform treatment of low-income persons.

2. The recipients could decide how to best meet their
particular needs because all of the assistance would
be provided in cash as opposed to in-kind benefits.

3. This approach could simplify the administration of the
welfare system and reduce administrative costs by
eliminating duplication.

4. Recipients would not be induced to alter their family
situations or labor market behavior because of cate-
gorization or work requirements.¹

Critics, however, cite shortcomings of this approach:

1. Providing universal treatment for all could be unfair
and excessively costly because different solutions
may be needed for different causes of poverty.

2. The administrative simplicity and cost savings anti-
ipated for the comprehensive cash assistance approach
may be mitigated because of the dynamic nature of the
welfare population.² The normal flow of families off
and onto welfare is continuous due to changing personal,
family, and economic circumstances. As people move on-
to and off of welfare their eligibility status must be
determined repeatedly. Many administrative dollars are
spent in this process. In addition, savings thought to
come from utilizing the income tax system to determine
need is questionable because circumstances of recipi-
ents can change from month to month. Thus, a compro-
hensive cash assistance plan cannot be grafted onto the
income tax system.

The Guaranteed Income Approach

Another of the comprehensive restructuring approaches that has
been seriously considered and supported is the guaranteed income

¹Ibid.

²Ibid.
approach. The guaranteed income approach advocates the government providing a minimum level of income for those who are unable to work and for those who are unable to earn enough by working. This approach has three basic tenets: (1) that everyone has a right to a basic level of income, (2) that the government should guarantee to every citizen a level of cash income that is high enough for an individual or family to live in moderate comfort, and (3) that there should be no restrictions on the use of the money. This approach would automatically provide benefits for every needy person and in some special cases of dire need, this basic income guarantee could be supplemented.\(^1\)

Presidential advisors, economists, and social theorists have proposed various guaranteed income plans. These have included Milton Friedman's Negative Income Tax (1962), Robert Theobald's guaranteed income (1965), James Tobin's guaranteed income plan (1965), R. J. Lampman's subsidy plan (1967), Edward Schwartz' guaranteed income (1967), President Johnson's Income Maintenance Commission Proposals (1969), President Nixon's Family Assistance Plans (1969), George McGovern's $1,000 a year Demogrant plan (1972), The Great Britain credit income tax (1972), and HEW's Income Supplementation plan (1974).\(^2\) Each of the plans would require the government to provide minimum income guarantees that ranged from $1,500 to $6,000 for the average family of four. The marginal tax rates of these plans have ranged from 50 percent to over 100 percent. The costs of the plans ranged from a low of several billion to a high of over $50 billion. These

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\(^1\) Tobin, "The Case for an Income Guarantee," p. 34.

proposals would add millions of participants to the welfare structure.  

Benefit Levels (Adequacy), Marginal Tax Rates and Cost

A major goal of the guaranteed income plans is to provide a package of adequate support levels, effective work incentives, and a program cost that is reasonable. A major problem in reaching this goal is that it is difficult to reach the objectives of adequate levels of support, effective work incentives, and a program cost that is reasonable simultaneously. Benefit levels, marginal rate of taxation, and overall program cost are tightly interwoven factors. For instance, if the level of benefits is increased and the tax rate is held constant, the overall program cost must increase or if the overall cost is held constant, the tax rate must increase and so on. For every guaranteed income plan the mathematical relationship between the benefit levels, marginal tax rates, and costs are fixed. Additional problems in initiating a guaranteed income plan revolve around determining an adequate level of support, determining effective work incentives via marginal tax rates and financing the costs of the plan.

1 Ibid.
4 Ibid., p. 80.
An Assessment of Some Selected Guaranteed Income Plans

The guaranteed income proposals discussed here were proposed in the decade of the sixties. These proposals or plans are models and standard bearers of the more recent guaranteed income plans and illustrate some of the best ideas to be developed in this area. An assessment of these five plans will be given in terms of the conceptual issues to offer insight into the potential effectiveness of the guaranteed income approach. In addition, this assessment will give some indication as to the effects of a hybrid plan.

The five plans reviewed in Table 3 show the basic features of: (1) eliminating all or most of the present welfare programs, (2) the use of federal income tax reporting to determine the amount of benefits to be received, and (3) varying benefit levels, marginal tax rates, and annual cost.

These plans also included such features as adjustable income guarantees, a subsidy to help those in the middle income groups with the problem of job displacement and universal medical coverage.

When these plans are reviewed in terms of adequacy we find that the Friedman and Lampman plans provide very low benefit levels of support. The Friedman plan would provide only $2,000 for a family of four. The Lampman plan reduces its subsidy as income rises to $3,000. Also, the Tobin plan provides a low level of support at the bottom of the earnings scale. However, the Theobald and Schwartz plans provide the best income levels of this group $3,200 and $3,000 respectively, making these plans the most expensive in terms of cost.¹

¹Berliner, Programs to Prevent Poverty, pp. 468-470.
## Table 3: Major Provisions of Selected Guaranteed Income Proposals*

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<td></td>
<td>Eliminates SS, unem-</td>
<td>Eliminates some existing welfare</td>
<td>Old age, survivors and</td>
<td>Phase out welfare programs</td>
<td>This plan would substitute for</td>
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<td></td>
<td>ployment compensation</td>
<td>welfare programs but retains</td>
<td>disability insurance</td>
<td>file statement of income</td>
<td>Medicare, old-age survivors and</td>
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<td></td>
<td>subsidies and other</td>
<td>old-age, survivors and disability</td>
<td>would be continued for</td>
<td>and dependents.</td>
<td>disability insurance, old-age</td>
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<td></td>
<td>assistance. Requires</td>
<td>insurance. Federal income tax</td>
<td>those not eligible for</td>
<td></td>
<td>assistance and other measures of</td>
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<td></td>
<td>universal medical</td>
<td>reporting will indicate the</td>
<td>the income allowances.</td>
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<td>assistance. A tax should</td>
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<td></td>
<td>coverage.</td>
<td>amount of subsidy payment.</td>
<td>would gradually phase</td>
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<td>be paid only when family</td>
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<td>out medical care and</td>
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<td>income is greater than total</td>
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<td>housing subsidies. All</td>
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<td>exemptions and deductions.</td>
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<td>adjustments would be</td>
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<td>made at income tax</td>
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<td></td>
<td>filing time.</td>
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<tr>
<td>Benefits</td>
<td>Basic economic security:</td>
<td>A family of 4 would receive $1,500</td>
<td>Every taxpayer would</td>
<td>This plan has 3 different yearly</td>
<td>A family of 4 has a total of $4,000</td>
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<tr>
<td></td>
<td>$1,000 for each</td>
<td>if they earned zero income (the</td>
<td>receive $400 payment</td>
<td>income levels, $3,000, $4,000, $5,000.</td>
<td>in deductions &amp; exemptions. If the</td>
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<tr>
<td></td>
<td>adult, $600 for each</td>
<td>breakeven level is $3,000. If this</td>
<td>for each family member.</td>
<td>For the minimum level, for example,</td>
<td>family has no income the family</td>
</tr>
<tr>
<td></td>
<td>child. Thus, a family</td>
<td>family earned $500 they would</td>
<td>A family of 4 would</td>
<td>a family of 4 that earned zero</td>
<td>would receive $2,000 or 50% of $4,000-6. A family</td>
</tr>
<tr>
<td></td>
<td>of four receives $3,200</td>
<td>receive $1,625; if they earned</td>
<td>receive $1,600. Each</td>
<td>income would receive $5,000. As</td>
<td>with income of $3,000 would receive</td>
</tr>
<tr>
<td></td>
<td>If a family of 4 earns</td>
<td>$1,000 they would receive $1,750.</td>
<td>family is allowed to</td>
<td>earnings rose the percent of</td>
<td>$500 or 50% of ($4,000-$3,000).</td>
</tr>
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<td></td>
<td>$2,000, they would</td>
<td></td>
<td>keep two-thirds of its</td>
<td>earnings retained would</td>
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<tr>
<td></td>
<td>receive $1,200.</td>
<td></td>
<td>income.</td>
<td>decrease.</td>
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<tr>
<td>Costs</td>
<td>$25 to $30 billion per</td>
<td>Depends on level of income</td>
<td>$12 &amp; $15 billion</td>
<td>$11 to $38 billion depending on</td>
<td>About $10 billion annually.</td>
</tr>
<tr>
<td></td>
<td>year funded by general</td>
<td>guarantee &amp; number of recipients.</td>
<td>annually.</td>
<td>expenditure level.</td>
<td></td>
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<tr>
<td></td>
<td>revenues.</td>
<td>Income guarantees are adjustable.</td>
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The Friedman, Lampman, and Tobin plans have the best work incentives in terms of their marginal tax rates. The Friedman plan allows recipients to retain 50 percent of their earnings. The Lampman plan allows recipients to retain 25 to 50 percent of their earnings. For example, if earned income is $2,000 which is $1,000 below the break-even point of $3,000, then the rate of subsidy would be 25 percent of $1,000 or $250 for a total income of $2,250; if earned income decreased to zero, with the same break-even point of $3,000 then the rate of subsidy would be 50 percent of $3,000 or $1,500, a total income of $1,500. Thus, the marginal tax rate varies inversely with income levels. The Tobin plan allows recipients to retain two-thirds of their earnings.¹

The Theobald and Schwartz plans have higher marginal tax rates though they provide the best level of support. The Theobald plan allows a family of four to retain only 10 percent of their income above $3,200 level. In the Schwartz plan, income above $3,000 is taxed at a rate of 60 percent on $1,000 of earnings and it increases as earnings increase. Thus, these two plans cause concern about a possible work disincentive effect.²

The federal tax laws pose problems for both the Friedman and Lampman plans because of a double exemption. For instance, in the Friedman plan, a family that earns less than the sum of its exemptions, deductions would be taxed at a rate of 50 percent. However, when earnings exceed this sum, the tax would apply at 14 percent of the lowest

¹Ibid.
²Ibid.
bracket. The resultant effect is that of a regressive tax. Also, in the Lampman plan when earnings exceed $3,000, the tax would apply at the lowest bracket.\textsuperscript{1}

\textsuperscript{1}Ibid.
CHAPTER IV

THE EFFECT OF INCOME GUARANTEES ON WORK

Some Potential Economic Consequences of a Guaranteed Income

A great deal of concern has been voiced about the effect of an income guarantee on an individual's incentive to work. Economists have written extensively on the effect of increased income on work effort. The theory of consumer behavior of the choice between leisure and income points out that each consumer is confronted with a fundamental trade off between the consumption of goods and services (income) and the consumption of leisure. The amount of income received by a consumer depends upon the amount of time allocated to work. The more one works, the greater is his or her income. However, the more one works the less time one has for leisure which has utility for most people.1

This trade off between work and leisure is the focal point of the concern surrounding the economic consequences of a guaranteed income (See Figure 1). "Suppose the wage rate is represented by the slope of ZA. In absence of a guaranteed minimum income, an individual whose indifference map is given by I, II would attain equilibrium at b, working CZ hours and receiving income OYo. If a minimum income of OY min is guaranteed by the government this individual might still work CZ hours, earn income OYo, and receive supplementary payment from the government

Fig. 1 Demand for General Assistance Payments

\[ Y_{\text{min}} \]

\[ Y \]

\[ O \]

\[ G \]

\[ C \]

\[ Z \]

\[ Y_0 \]

\[ Y_1 \]

\[ F \]

\[ H \]

\[ D \]

\[ B \]

\[ E \]

\[ I \]

\[ II \]

\[ \text{Income} \]

\[ \text{Leisure} \]

\[ \text{Ferguson and Gould, Microeconomic Theory, p. 74.} \]
of \( BD = Yo - Y_{min} \). In this case, however, the individual can attain a greater level of satisfaction by doing no work at all — by moving to point \( E \) on indifference curve II and receiving the minimum guaranteed income from the government. From point \( E \) the individual can be induced to work. In terms of Figure 1, if the wage rate should rise to \( ZF \) (or higher), he or she would forego his government payment, work \( GZ \) hours, and receive income of \( OY \). The exact result, however, depends upon the leisure-income preference of individuals, the level of the minimum income, and the wage rate available to each individual in question.\(^1\)

Reduced work effort can afford advantages in the long run, if this time is used for gaining skills via education and training. "A predominant theory has been that 'a national increase in education reduces the dispersion of labor income.'" Jan Tinbergen, in the study, *Income Distribution: Analysis and Policies*, presents an impressive body of evidence on the responsiveness of differentials between the wages of the skilled and unskilled to increases in the supply of educated workers. Tinbergen asserts,

>a policy of saturation of human capital-investment in human capital that is over-investment relative to any efficiency criterion may be an important option for reducing the inequality of labor income.\(^2\)

\(^1\)Ibid.

Marginal Tax Rates

A major component that guaranteed income plans use as a work incentive is the marginal tax rates of the plans. Every guaranteed income plan has a schedule of benefit reductions as the recipients' earned income increases. This tax has the same effect as normal taxes on the incentive to work, the higher the tax the less the motivation to work. The marginal tax rates of the existing welfare programs are in the range of 70 percent and greater, a rate that would cause reductions in work effort. However, many who propose welfare reform plans with marginal tax rates of 50 to 60 percent consider their rates to be relatively low. Some welfare experts estimate that the marginal tax rates of welfare reform plans should be 30 percent or lower to have only a minimal effect on work effort of recipients.¹

Psychological Aspects

Advocates of a guaranteed income such as psychologist Eric Fromm, suggest that people may initially prefer not to work for a short period of time, but that the vast majority would have a great desire for work. Fromm feels that exploitation of the guaranteed income would stop after a short period of time, just as people would not overeat sweets after a short period of time. His premise is based on the fact that Americans are preoccupied with the work ethic. He feels that this preoccupation is not likely to disappear.² However, Fromm does not


determine how long it would take for people to increase their work effort.

Research on the Effects of a Guaranteed Income

Over the last decade, a great amount of research and data have been accumulated by scholars and government analysts on the effects of a guaranteed income. These studies have mostly focused on the behavior of welfare recipients and low income workers under conditions that approximate conditions which would exist under a guaranteed income. While the results of these studies are inconclusive, they merit close consideration.

Three major types of research studies have been used in an attempt to estimate the effect of welfare reform plans on the work effort of the poor and near poor. The first type is based on an analysis of existing welfare programs and examines if welfare recipients have changed their attitudes toward work. The second type, called the cross-section approach involves a statistical and economic analysis of large quantities of survey data, illustrating the behavior of recipients who cope with increasingly high marginal tax rates and cash transfer payments. The third type consists of a series of direct experiments in which selected families were given a form of guaranteed income and their behavior was closely studied. The objective of these studies was to ascertain the effect of guaranteed income payments on work effort.

First Type: An Analysis of Existing Welfare Programs and Recipients' Work Effort

An example of the first type of study is one by Larry Orr and Irwin Garfinkel on the work effort of AFDC mothers receiving an annual
guaranteed income. The Orr and Garfinkel research indicated that on the average the employment rates of AFDC mothers decreased by 4.5 percent as the annual guarantee increased by $1,000. In addition, their research indicated that a $1,000 increase in the guarantee had a larger effect, the smaller the initial guarantee. For example, an increase from $500 to $1,500 led to a decrease in employment rates of about 14 percent.¹

An earlier study by Leonard Hausman analyzed a survey of 50,000 AFDC families in 1967 who lived in the states of Alabama, Kentucky, and Mississippi, each of which guaranteed different levels of income in the absence of non-welfare income. Hausman's findings indicated that an increase in monthly AFDC payments from $82 to $162 caused a decline of 36 percent in the market work effort of these female headed families. Hausman concluded that if AFDC mothers can reach income targets with less effort they will reduce that effort. Both studies indicate that female heads of households would reduce their work effort with guaranteed income plans and that the work reduction effect is greater the higher the marginal tax rate.²

Second Type: The Cross Section Approach

The cross section studies were based on aggregate statistical data that were used to predict the economic behavior of the low income worker. These studies focused on possible changes in the work effort of low income male workers. Research institutions, distinguished


economists, and the federal government have conducted many studies in this area. Most of these studies used aggregate statistical data which can increase the opportunity for inaccuracy in the results. However, these studies are valuable for estimating the direction and order of magnitude of changes in the work effort of low-income male workers.¹

A cross section approach study by Greenburg and Kosters attempted to simulate the effects of a welfare reform similar to President Nixon's Family Assistance Plan. This study used an income guarantee of $3,500 for a family of four and a marginal tax rate of 75 percent. They estimated that working men with family responsibilities would reduce the number of hours they worked by 29 percent. Thus, they concluded that married male heads of participating families (in an income guarantee program) would substantially reduce their work effort.²

Another cross section approach study by Kalanchek and Kaines called "Labor Supply and the Negative Income Tax" developed an economic model that would simulate the effects of a guaranteed income of $2,400 (for a family of four) and a marginal tax rate of 50 percent. They estimated in this study that male family members would reduce their labor supply by 37 percent. Also, they estimated that such a plan would produce a 46 percent reduction in the labor supply of the eligible population. They note that the income guarantee and the marginal tax rate of


²Ibid.
this plan were relatively low.¹

The findings of these studies are that a guaranteed income would reduce the work effort of male low-income workers. The economic simulations suggest that reductions in work effort would accompany even low level guarantees. Some welfare experts think that the opportunity costs associated with low paying jobs are greater than those associated with welfare. One such expert, Nathan Glazer, points out that the welfare system offers advantages far in excess of those available from low paying jobs open to the inner city poor. Welfare offers medical coverage, security, stability, and other benefits that are lacking or inadequate in many low paying jobs. Glazer proposed a solution to this problem—offer sufficient benefits to those in low-wage and seasonal labor markets. This would make traditionally low paying jobs more attractive by offering the needed benefits to these workers.²

Third Type: Experimental Demonstration Programs

The third group of studies consisted of experimental programs. First, a relatively large group of people with similar backgrounds (including age, income, education, family size, economic, and social characteristics) was selected. Then the selected group was divided into a control group and an experimental group. The control group continued their usual life cycle while the experimental group embarked on a life style of new and varied conditions. The new and varied conditions were


as follows: the experimental groups were guaranteed a certain amount of income for a certain period, whether they worked or not; the amount of this income guarantee and the marginal tax rate applied to the experimental groups' earnings varied.

The most well known study, the New Jersey Income Maintenance Experiment, began in August 1969 and ended in 1972. The total cost was $7.8 million, and it was the first large scale social experiment in the United States. Some 1,357 households participated, 725 in the experimental group and 632 in the control group. The participants were from five cities, four in New Jersey and one in Pennsylvania. Each participating family had to have one male (age 18-58) who was able to work and the family's income had to be less than 150 percent of the poverty level. The income guarantee varied from 50 to 125 percent of the poverty level and the marginal tax rate varied from 30 to 70 percent. There was no work requirement for the participants.¹

Preliminary data from the New Jersey experiment indicated that there was no evidence that work effort declined among those receiving income support payments. However, the final results indicated that the number of employed family members decreased 9.5 percent, but not for the control group.² The experimental and political credibility of this experiment were challenged by those who thought the experiment was being used to promote the political feasibility of a negative income tax. Also, some doubted the experiment's objectivity as it was discovered that its administrators, designers, and sponsors were for income


²Ibid., p. 4.
guarantees.¹ Charges by the press that the experiment was rigged were denied. In Daniel Moynihan's book, The Politics of a Guaranteed Income, Moynihan relates that, "the charge was a lie but was probably believed!" It did not help the experiment when the General Accounting Office audited the initial findings and declared them "premature."²

The New Jersey Experiment examined the work effort of various members of the experimental families. The most important group or key group of the experiment was non-aged, able-bodied males with family responsibilities because it was feared "that given an income alternative, they would decide not to work."³ "Over the central two years of the experiment,...the employment rate for male family heads in the experimental group was only 1.5 percent less than for the controls."⁴ The next most important group as determined by policy interests were wives. The wives on the average were mothers of four children (the average family size was six). For wives, the difference between the experimentals and the controls was significant. The experimental wives worked, "23 percent fewer hours per week and their employment rate was 24 percent less than the control group of wives."⁵ In that wives in six-person families work hard inside the home, this can be a desirable outcome. Thus, "this work could be more beneficial or cost effective

¹Ibid., p. xix.


⁴Ibid.

⁵Ibid.
from a national viewpoint than the low-wage market labor." Finally, when the total family labor supply (a composite of market work by the husband, the wife, and other adult family members) was examined over the central two years, the number employed per family was 9.5 percent less for experimental families than for controls. The disincentive effect can be considered socially useful in that the secondary earners could benefit. Wives could decide to work more in the home, teenagers could stay in school longer because of the payments (guaranteed income), and older workers could take it a bit easier. "These benefits represented a net increase in family income,...a greater command over material goods and services and enhancing their economic well-being."1

At the same time, six other major guaranteed income experiments were initiated. The New Jersey experiment analyzed the work effort of husbands and wives of various ethnic groups living in an eastern urban environment. Two other guaranteed income experiments were set up expressly to analyze the work behavior of poor families living in rural areas. These "Rural Income Maintenance Experiments" were carried out in Iowa and North Carolina.2 Another experiment was the "Gary Income Maintenance Experiment," which focused on black families and included

1Ibid.

female-headed families previously on welfare in urban, Gary, Indiana.\(^1\)

The Seattle and Denver Maintenance Experiments analyzed the work effort of husbands, wives, and female headed families in Seattle, Washington and Denver, Colorado.\(^2\)

Many feel that the three most significant guaranteed income experiments in terms of measuring the national impact of a guaranteed income were the New Jersey, the Seattle, and the Denver experiments. The results of the New Jersey, Seattle, and Denver experiments were similar for husbands. The measured reduction in hours of work by white husbands in New Jersey was 6 percent and for black and white husbands in the Seattle and Denver experiments, it was 6 percent also.

Critics of the guaranteed income experiments and others cite a number of methodological biases that could have underestimated the reduction in work effort as measured by the guaranteed income experiments. Three examples of the cited biases are the Hawthorne effect, the windfall effect, and the small size effect. The Hawthorne effect is characteristic of socio-economic experiments. "Merely by asking participants for their cooperation in the guaranteed income experiments, the investigators had stimulated a new attitude among the participants who now felt themselves part of an important group."\(^3\) Martin Anderson, economist and presidential advisor, notes that participants were subjected to an


unusual and extensive amount of personal attention. Thus, participants were made to feel important which ultimately influenced their behavior. Participants quickly learned what the investigators liked and would then try to please them by acting accordingly. Mordecai Kurz, professor of economics at Stanford University and Robert Spiegelman of Stanford Research Institute pointed out that Hawthorne effects have become well known. "If for example families on the income maintenance experiment develop a sense of 'experimental responsibility,' they may behave quite differently than a control group without such a sense of responsibility."¹

The windfall effect is the effect caused by participants viewing income guarantees as windfalls, a small fortune that would not last long. Economist Jacob Mincer characterized it, "the short run response of a particular part of the population to a temporary flow of cash grants."² Henry Aaron observed, "...the brief duration of the experiment is likely to lead to estimates of the sensitivity of labor supply to guarantee levels that are too low."³ In addition, experts point out that it is difficult to estimate the size of the windfall bias.

The small size effect is an effect that makes it difficult to project what might happen if a guaranteed income were instituted on a nation wide basis. Aaron states, "the thinness of the sample and the brevity of the experiments make it impossible to observe the impact of a negative impact on the mores of the entire group."⁴ The results of


³Ibid.

⁴Ibid.
such small-scale experiments make it difficult to anticipate the behavior of all the low-income population. It must be noted that an effort was made to correct for this bias in the Seattle-Denver experiments.¹

The Seattle and Denver experiments were larger and more comprehensive than the New Jersey experiment. According to Michael Keeley of the Stanford Research Institute, the most important advantages of the Seattle and Denver experiments were the larger sample size (5,000 families) and the more generous negative income tax plans which were designed to dominate welfare programs such as AFDC and Food Stamps. Further, the Seattle and Denver experiments' results were adjusted to expand the information gained into a national focus. The analysts of the Seattle and Denver experiments constructed an economic model that allowed them to infer from their small sample what would happen if the experiment was conducted on a national scale. The report of the analysts states that "to provide meaningful predictions of the effects of a particular national program, a labor supply response model...must be used." Subsequently, their economic model predicted when using an income guarantee of $3,750 in 1974 and a marginal tax rate of 70 percent that the national effect of a guaranteed income program would be to cause husbands to reduce their work effort by 11.2 percent, wives by 32.2 percent, and females who head families by 9.4 percent.²


²Ibid., p. 21, Table 6, p. 23, Table 8.
These studies were not considered definitive and there is every possibility that a host of biases could have understated the results. The results of the studies of existing welfare programs, economic simulations, and six major guaranteed income experiments indicate that there will be a reduction in the work effort as a result of income guarantees. How much of a reduction depends upon the leisure-income preferences of individuals, the level of minimum income, and the wage rate available to each individual or group in question. However, this reduction in work effort can be used to benefit society via greater opportunities for education, training, and improved life styles.
CHAPTER V

AN ASSESSMENT OF THE 1977 CARTER ADMINISTRATION
PROPOSED PROGRAM FOR BETTER JOBS
AND INCOME (PBJI)

An Assessment of the Program for Better Jobs
and Income

The Carter administration proposal, Program for Better Jobs and Income (PBJI) of 1977, illustrates a comprehensive reform approach that utilizes both a comprehensive cash assistance program and a guaranteed jobs program. The focus of this proposal was both on the demand side of the labor market (for those who are employable) with the guaranteed jobs program and expanded benefits and coverage for those who are unable to work. This proposal was unable to attract the broad coalition of support needed to pass the legislation. There were doubts about the adequacy, equity, level of work incentives, administrative efficiency, the ability to create jobs, and the proposal's cost. Though this proposal received praise for important reforms such as a national minimum benefit level and expanded coverage for many groups, this proposal also demonstrated how many welfare reforms fail to deal effectively with the trade-offs inherent in the welfare reform goals.

An Overview of the Carter Administration Proposals

Carter's PBJI was offered as a comprehensive reform proposal that would increase job opportunities for the low-income population
and consolidate our major income programs into one simple and efficient system. The PBJI had six basic objectives:

1. To divide the poor into two groups, those who can work and those who cannot because of child care responsibilities, age, and disabilities.

2. To create up to 1.4 million minimum wage jobs for those who can work and who are unemployed.

3. To consolidate AFDC, SSI, and Food Stamp benefits into a single income maintenance program open to all who are needy including childless couples, low wage workers, and single first time applicants.

4. To aid the working poor by expanding EITC as well as paying cash benefits to those who are eligible.

5. To increase the federal share of welfare costs and provide state and localities with $2.1 billion (1978 dollars) in fiscal relief in the program's first year with the promise of more relief in years to come.

6. To potentially reduce the number of people eligible for welfare benefits from 40 million to 36 million; while increasing those receiving benefits from 30 to 32 million by reforms such as expanding the EITC and the guaranteed jobs program.

The Carter administration calculated that their proposal would require an outlay of $2.8 billion over and above the costs of the continuing and existing programs for a projected cost of $31.1 billion in fiscal 1981.¹

Points of Controversy

The basic points of controversy surrounding Carter's PBJI were the cost of the proposal, its complexity, the equity and benefit levels of the cash program; the feasiblity and the effects of the jobs program; and the scope of the program.

Cost

The Congressional Budget Office (CBO) cast some doubt on the actual cost of the Carter administration's proposal. The CBO projected that the Carter proposal would cost the government about $10 billion more a year than the Administration estimated or $13.9 billion more in fiscal 1982. When the CBO translated their estimate for fiscal 1982 ($13.9 billion) into 1978 dollars (that's what HEW and the Carter administration used for their estimates) they arrived at a net additional cost of $12.4 billion for the Carter proposal. The Carter proposal appeared to be more expensive than was first suggested and many Congressmen found that aspect undesirable.¹

Administrative Complexity

Administrative complexity is a major problem of the existing welfare system and many felt that it was a major problem of Carter's PBJI proposal. Even though the cash assistance program would have consolidated some of the existing programs, wide variations in benefit levels and high marginal tax rates would have remained. Moreover, the multitude of program categories and work requirements would constitute a complex system. The proposed procedures of retrospective accounting and monthly income reporting would add to the administrative burden. Others voiced a concern that the PBJI might well have been too complex for the welfare administrators, recipients, and the public to understand.²


Adequacy and Equity of Benefit Levels

The benefit levels in the PBJI caused concern because of the amounts, inequity, and the breadth of coverage. Liberals thought that $4,200 for a not expected to work family of four was hardly a dignified standard of living. Some conservatives felt the benefits were overly generous. An additional concern for some liberals was that recipients on the lower tier of benefits ($2,300 annually for an expected to work family of four) could not possibly afford the additional expenses of the job search required for those who are expected to work. A CBO study estimated that 1.8 million families below the poverty level would lose benefits under the PBJI. Other inequities inherent in the PBJI included disparities in benefits from state to state and disparities among groups such as female headed families with children and individuals and couples under 65 receiving much less than those over 65.

Feasibility of Job Program

Some welfare experts questioned the feasibility of the PBJI's job program. What mechanism or strategy would be developed to create a large number (1.4 million) of public service jobs for the needy population? In a research paper by Sheldon Danziger, Robert Haveman, and Eugene Smolensky of the Institute for Research on Poverty, doubts were raised concerning the feasibility of creating the number of public service jobs needed for unskilled labor in a relatively short period.

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2 Ibid.

of time. Furthermore, the PBJI failed to develop a mechanism and/or strategy that would transplant participants in the job program into private sector jobs. The PBJI did not focus on developing marketable skills that would be crucial for the participants of PBJI to gain private sector jobs.¹

Two more areas of concern were the wages to be paid to subsidized workers (minimum wage) and the impact of the subsidized workers on state and local job markets. Labor leaders advocate the use of the prevailing wage levels as opposed to minimum wage for the participants of the PBJI. Labor leaders viewed the use of minimum wage for PBJI participants as discriminatory and stigmatizing. In addition, labor groups wanted some type of protection against public and private employers lowering wages or firing workers because of the PBJI's job program.²

Fiscal Relief for State and Local Governments

The state and local officials found that the fiscal relief offered by the PBJI was somewhat less than they had hoped for. One major criticism was that the PBJI did not provide the immediate fiscal relief sought by many state and local government officials. The PBJI provided for gradual relief over a period of time. Others were disappointed because the PBJI did not provide total federal financing. An analysis by John P. Keith and Joseph M. Thomas for the Regional Planning Association stated that the PBJI failed to adjust benefit levels in response to inflation. Consequently, the state and local contribution to basic benefits would rise as the cost of living and


²Ibid., p. 1770.
poverty threshold rose. Under these circumstances, states and localities would have realized the greatest fiscal relief the initial year the proposed programs became effective.¹

Ceilings on state marginal tax rates in the PBJI posed problems for some states. The designers of PBJI, in an effort to be consistent, provided work incentives for those expected to work and those not expected to work as well as set marginal tax rates for both groups. The PBJI proposed a 50 percent basic benefit reduction rate. The states were restricted to a 52 percent benefit reduction rate for those who could not work. Critics of the PBJI such as the AFL-CIO pointed out that if you are not expected to work you would not have earned income and further you would not need any work incentives. Those states with high benefit levels would be faced with increased welfare rolls. "If welfare benefits are reduced too rapidly as earnings increase there is little incentive to work; yet if the benefit reduction rate is too gradual work incentives remain strong but families remain eligible until they reach high income levels."² For example, if New York maintained its existing benefit levels, the 52 percent benefit reduction rate would force it to continue cash aid to working families with incomes up to $11,923 a year, thus increasing the number of families eligible.³


²Ibid.

³Ibid.
Scope of Proposal

Another major issue was the fact that the PBJI did not fold in health and social service activities. The PBJI included a tax measure such as EITC and a jobs program but excluded health care and social services. Many felt that health care and social services were important areas which should have been integrated with welfare reform. Thus, some experts suggested that a health insurance package and/or Medicaid reforms should have accompanied the PBJI. Another perceived shortcoming of the PBJI was that it made no provisions for the increasing demand for social services such as child care, that the expanded eligibility of programs will create. ¹

Though the PBJI offered improvements to the welfare system, it was perceived as a proposal that did not deal with the trade-offs of welfare reform effectively. Again, the conflicting nature of the welfare reform goals is illustrated in this comprehensive reform approach. Both the demand side of the labor market approach and the comprehensive cash assistance approach have practical problems. The guaranteed jobs approach can affect labor markets and job creation is costly and complex. The cash assistance approach needs to define an adequate level of support and still provide work incentives. A demonstration project using these approaches might be instructive.

CHAPTER VI

SUMMARY AND RECOMMENDATIONS

The current macroeconomic policies and employment programs of the federal government do not provide an adequate level of income for all members of the society. The current welfare programs were developed to bridge this gap. However, these programs are beset with a host of major problems as outlined in this review. The current welfare programs have failed to meet the fundamental goals sought: Adequacy, Equity (horizontal and vertical), Effective Work Incentives, Family Stability Incentives, Administrative Efficiency, and Target Efficiency. Poverty has persisted despite the current welfare programs.

In terms of adequacy it was found that despite the current welfare programs 25 million persons were below the poverty level, about 11.5 percent of the total U.S. population in 1978. Blacks, female-headed families, families with children, and the aged had a higher than average incidence of poverty when compared to others. Economic and social conditions worked together to render the welfare programs less effective in combating poverty. Occurrences such as the recession of 1973/74 and others in the last decade caused a significant reduction in the rate of real economic growth. The increased number of female-headed families in our society in the last decade has produced an added strain. Female-headed families have a higher incidence of poverty when compared to other families. In 1977 31.7 percent of all
female-headed families were in poverty compared to 5.5 percent of other families.

Low benefit levels have also contributed to the persistence of poverty. For example, between 1965 and 1975, social security was the only major cash assistance program whose average benefit level rose consistently. Other programs experienced both increases and decreases in average benefits. The AFDC programs benefits on the average increased significantly between 1965 and 1970 and then leveled off or declined in constant dollar terms between 1970 and 1975.

Gaps and leaks in the coverage of the welfare programs also reduce the programs' effectiveness in combating poverty. Many experts point to the categorical nature of the programs as the source of the problem. Categories used to determine eligibility for the programs sometimes exclude more needy people than they include. A 1976 study indicates that the public assistance category of the major income transfer programs aided only 5 percent of the poor in getting out of poverty.

The current welfare programs fail to distribute their benefits equitably. Horizontal inequities (disparities faced by different segments of the poor population) are a pervasive problem. The broad discretion left to states leads to widely diverging state standards for benefits and coverage. Categorical needs standards allow large segments of the needy population, especially the working poor, to be excluded from the federal cash subsidies. Many of the in-kind benefits programs require participation in categorical programs and can thus exclude the needy who are not participants. Add to these problems funding limitations and disparities in participation and inequity grows.
Vertical inequity is also a problem. Vertical inequity focuses on the advantages the welfare system sometimes provides for the poor versus the non-poor. A major concern is that the welfare system may enable welfare recipients to live better than the working poor. For example, AFDC recipients are allowed to deduct work expenses from their income and thus are better off than a worker at the same income level but who is not an AFDC recipient.

Target efficiency is not always realized by the current welfare programs. Target efficiency is the concept that benefits should be directed to the most needy. Again, the categorical nature of the program is a source of inefficiency. Significant portions of the needy population are excluded. Leaks of benefits to the non-poor and exclusion of some portions of the needy population, which include the aged, families with children, the working poor, and blacks reveal the programs' inefficiency.

Most welfare experts agree that work incentives are vital if the welfare system is to achieve its goals. The welfare programs should avoid causing any negative impact on the welfare recipients' incentive to work. Programs like AFDC inserted work incentive provisions in their structure. Under the AFDC program when recipients' benefits are calculated the states can deduct work expenses and $30 plus one-third of recipients remaining income.

The effort to provide work incentives in the welfare system has been adversely affected by the cumulative marginal tax rates of the programs. These marginal tax rates have the same effect as regular taxes on the incentive to work. The higher the tax rates the less the motivation to work.
In many instances, the marginal tax rates of one program are added to the marginal tax rate of other programs. For example, the in-kind benefit programs that supplement AFDC have their own marginal tax rates. Thus, these tax rates combine with the marginal tax rates of the AFDC program and result in a greater loss in benefits. If an AFDC recipient participates in the food stamp program then the recipient is subject to tax rates of 67 percent under the AFDC program and a 30 percent rate for the food stamp program. One study indicated that recipients can average as little as 20 cents per dollar.

Another factor is a series of notches in the benefit scales that also work against the work incentive provisions. A notch is a point in the benefit scale where one additional dollar of earnings makes a recipient ineligible for other programs. Ideally programs have benefit levels that gradually decrease to avoid this. However, in some programs like Medicaid an additional dollar of income can cause a family to be ineligible for $1,000 to $1,500 in medical care.

Most analysts conclude that work disincentives such as cumulative marginal tax rates and notches in benefit scales do have a negative work effect on welfare recipients. Some experts think that the strength of a negative work effect caused by disincentives is subject to factors such as age, sex, and marital status. Some researchers have concluded that the negative work effect is small for working age males but somewhat stronger for married women, female family heads, and older men. The effects of welfare on work are still being evaluated.

The concept of administrative efficiency is the idea that a system should achieve its goals at a minimum cost. Unfortunately the welfare system is characterized by overlapping programs, financial cost-
liness, and undue complexity. Each program has its own set of rules and each program is separately administered. Both demographic (categorical) and needs-tested standards are used for establishing eligibility and are major causes of the systems' complexity.

The definition of countable income affects program costs both directly by affecting the number of recipients and the amount of benefits they receive, and indirectly by necessitating increased administrative complexity. In some welfare programs like AFDC, certain expenses can be deducted from income to achieve increased equity or to provide financial incentives. Assets tests (includes cash, savings, checking accounts, cars or homes) establish limits on the amount of assets recipients can have and still receive benefits. Various welfare programs allow different assets to be excluded from the assets tests. This all adds to the complexity.

An additional problem is that the lines of authority in the welfare programs are not clearly established between the federal, state, and local agencies. States often must try to integrate federal regulatory changes with on-going state administrative practices. States point out that there can be a large number of federal changes in a year.

The cost of administration has increased as a result of the administrative complexity throughout the system. Direct costs of administration have increased rapidly; consuming about 12 percent of program costs in both AFDC and food stamps. The indirect cost of administration has increased because of the number of errors in administering the programs.

The growth of expenditures for welfare benefits and coverage has been the focus of some concern about the dramatic increases in the cost of the welfare system. Federal income assistance expenditures grew at
a rate that was two-thirds higher than the rate of growth of the federal budget between 1965 and 1975. Inflation, expansion of coverage, and policy changes all contributed to the rapid growth of welfare costs. Eligibility extensions, new programs, and major revisions of old programs caused significant increases in program costs.

The way in which costs of income assistance programs are distributed has become a burden to state and local governments as the costs have increased due to inflation and expansion of benefits and coverage. Most major need based assistance programs require state/local financial participation. Up to 50 percent of the cost of some programs is required, and the costs have increased rapidly over recent years. Thirty-three states finance general assistance programs for needy persons who are ineligible for federal assistance.

Goals of adequacy, equity, efficiency are not being met by our present welfare programs. Waste, error, inequities, inadequacies, and complexity prevent the recipients and society from obtaining maximum benefits. The major questions are: (1) should the present system be revised (an incremental change approach)?, or (2) should the present system be abolished in lieu of an entirely new one (a comprehensive restructuring approach)? The alternatives continue to be examined.

The incremental change approach entails step by step modifications of the welfare system to eradicate its problems while retaining the categorical system of benefits and the federal, state, and local assumption of administrative obligations. Advocates of this approach cite these advantages over comprehensive restructuring:

1. Low initial cost
2. More acceptable to the welfare bureaucracy.
3. Thought to be one of the most realistic approaches. Critics point out that this approach retains all of the systems' structural faults.

The comprehensive restructuring approach proposes to replace the current system with an entirely new one. A number of comprehensive proposals have been offered. A work welfare approach, guaranteed job approach, work condition approach, a multi-track approach, a comprehensive cash assistance approach, and a guaranteed income approach. The proposals would implement new strategies and phase out all or most of the present systems' structure. In addition, various approaches can be used in tandem.

The work-welfare approach makes working a condition for program participation. Those who are employable would receive assistance in one of three ways:

1. Work conditioned benefits
2. A guaranteed job program providing public or private sector employment.
3. Benefits tied to training, educational or employment programs.

Work-welfare has a major goal of providing training and placement service for participants to enable them to be absorbed into the private sector. Those who are not employable would receive benefits through categorical programs or comprehensive cash assistance. The focus is on the demand side of the labor market.

The objective of the guaranteed jobs program is to provide either public or private sector jobs to low income families with an employable member. Employers are encouraged to participate via government extensions of tax credits and wage subsidies. Though these types of programs
have met with some success, there are no provisions for child care or transportation expenses. In addition, job creation is expensive and difficult.

Work conditioned benefits programs reward work by providing a wage subsidy to overall earnings that is tied to the number of hours worked or by an income tax credit. The focus is on assisting the employable population. Earnings are supplemented, attachment of the poor to the labor market is strengthened. However, administrative procedures would be complicated and there is no provision to aid the non-employable. Benefits would go to the working poor.

The comprehensive cash assistance approach would provide a single cash system to replace many of the current welfare programs. The format would be uniform rather than the categorical format of the current programs. This approach would be more equitable and recipients could decide how to best meet their needs. However, providing uniform treatment for all could be unfair and costly.

The guaranteed income approach has been a subject of intense research and it has gathered some support. This approach requires that the government provide a minimum level of income for those unable to work and for those who are unable to earn enough working. A major objective of this approach is to provide a package of effective work incentives, an adequate level of support and reasonable program costs. However, welfare experts point out it is impossible to change the levels of any one of these three without changing the levels of the remaining factors.

There is much concern over the effect of income guarantees on work. Economic theory says that the exact result would depend on the
leisure-income preferences of individuals, the amount of income guarantee, and the wage rate available to each individual in question. A great amount of research and data have been accumulated on the effects of a guaranteed income. Three major types of research studies have been used to estimate the effect of welfare reform plans on the poor and near poor:

1. An analysis of existing welfare programs and an examination of recipients' attitudes toward work.

2. Statistical and economic analysis of large quantities of survey data illustrating the behavior of recipients called the cross-section approach.

3. A series of direct experiments in which families received guarantees and their behavior was closely studied.

Though the results varied from study to study, there were some important findings. The strength of a negative work effect is subject to factors such as age, sex, and marital status. Males in the New Jersey Experiment that were prime age and able bodied with family responsibilities were only marginally affected. Secondary earners such as wives who were most significantly affected could decide to work more in the home, teenagers could continue their education, and older workers could take it a bit easier. Thus, the disincentive effect could have beneficial and socially useful consequences.

The 1977 Carter administration proposal of the Program for Better Jobs and Income (PBJI) offered much needed reforms such as a national minimum benefit level and expanded coverage. The PBJI was a comprehensive reform that utilized both comprehensive cash assistance and a guaranteed jobs program. The focus of this proposal was primarily on expanded benefits and coverage for many groups and for those who were employable, a demand side of the labor market via the guaranteed jobs
program. However, high costs, administrative complexity, and high levels of work disincentives were seen as PBJI's shortcomings.

**Recommendations**

Given that the welfare system has major problems, welfare reform proposals that attempt to deal with these problems either in an incremental approach or comprehensive approach should be thoroughly examined for possible implementation.

The comprehensive restructuring approach offers the greatest opportunity via alternatives for changing the welfare system. With the comprehensive approach you could start anew with a coherent system. However, it is the least feasible politically.

The work-welfare approach focuses on the often neglected demand side of the labor market, provides an opportunity to work and possibly gain some skills and thus could be utilized to some advantage. However, provisions would have to be made for child care and transportation expenses.

The guaranteed income approach offers a great improvement over the current system in terms of equity and recipients' control of benefits. This might be compatible with the current "free market" philosophy and would decrease administrative costs. A demonstration project utilizing both could be instructive.


Nathan, Richard P. "Modernize the System, Don't Wholly Discard it." The Los Angeles Times, February 27, 1977, Section VI.


