

Welfare Reform in the United States*

Robert Haveman
John Bascom Professor of Economics
Department of Economics, La Follette Institute of Public Affairs and
Institute for Research on Poverty
University of Wisconsin – Madison
1180 Observatory Drive
Madison, Wisconsin 53706-1393
haveman@lafollette.wisc.edu

John Karl Scholz
Professor of Economics
Director, Institute for Research on Poverty
University of Wisconsin – Madison
1180 Observatory Drive
Madison, Wisconsin 53706-1393
jkscholz@facstaff.wisc.edu
phone: (608)265-5367
fax: (608)265-3119

April 15, 2001

* This paper is prepared for the 2001 East-West Center, Korean Development Institute conference on “A New Paradigm for Social Welfare in the New Millennium,” Honolulu, Hawaii. We are grateful for the guidance and assistance of Professor Yoon H. Kim and staff at the East-West Center for their hospitality.

There are inevitable tensions among the three primary goals of any nation's social safety net. These three goals are adequacy (providing a socially acceptable minimum level of living to those unable to attain it on their own), targeting (the provision of support to the neediest at the lowest public cost), and desirable incentives (providing financial and other encouragement for socially desirable behaviors in the structure of programs). Generous programs are costly. Costs can be limited by targeting benefits on the most needy, but doing so implies rules that reduce public support when private income increases, or rules that restrict benefits to those with income or assets below some threshold, or rules that limit benefits to adults with children. Such rules tend to inhibit work, skill development, and asset accumulation, and encourage nonmarital childbearing. Targeting becomes easier if benefits are low, but low benefits may come with the cost of consigning the poor to lives of deprivation.

The safety net in the U.S. has resolved the inherent tensions in a way that is quite different than other industrialized countries. By international standards the size of the U.S. safety net is small. Moreover, the safety net is composed of many programs, each with different target groups and eligibility requirements. And, it has a variety of other characteristics that give taxpayers concern. By the late 1980s, American citizens of all political persuasions were calling for reform of this system.

The first two sections of this paper briefly describe the key safety net programs in the U.S. prior to 1996 and the tensions associated with this system. These tensions led to the 1996 Personal Responsibility, Welfare and Opportunity Reconciliation Act (PRWORA). The next two sections of the paper describe, and then provide brief appraisals of, the two major—and complementary—changes to the U.S. safety net in the past decade: PRWORA and the sharp expansion of the earned income tax credit (EITC). The final section of the paper offers lessons

for other countries, drawn from the U.S. experience with antipoverty policy.

I. The Structure of the Social Safety Net in the U.S. Prior to Reform¹

Programs in the U.S. safety net can broadly be broken into two groups: social insurance and means-tested transfers. The distinguishing characteristics of social insurance programs are that they are universal, in that all individuals or their employers make contributions to finance programs and all people can receive benefits when specific eligibility requirements are met. Most of these programs have dedicated funding mechanisms in which social insurance taxes are remitted to trust funds from which benefits are paid. Means-tested transfers, on the other hand, are financed by general revenues and tend to be categorical, in the sense of being restricted to those who satisfy some set of personal (e.g, single parents) or resource characteristics (e.g., disabled who are poor). All such programs provide benefits only to those judged on income or asset levels to be needy and they generally reduce public support as recipients' incomes increase. In most industrialized countries, means-tested transfers have a smaller budgetary cost than social insurance programs.

Social Insurance Programs in the U.S.

The largest social insurance program is social security, formally known as the Old-Age, Survivors, and Disability Insurance program (OASDI). It is a massive program and pre-tax and -transfer poor families receive half of its benefits. Consequently it has a major effect on poverty rates among the elderly and disabled who are the primary beneficiary groups.

The elderly receive the bulk of cash benefits from social insurance. Aggregate retirement income payments were \$334.4 billion in 1999, and averaged \$750 per month for a retired worker

¹See Scholz and Levine (2000) for a more complete discussion of antipoverty programs and their evolution.

(\$1,300 for couples). The elderly also receive substantial benefits from Medicare (hospital insurance and for some households, supplementary medical insurance), which covers almost all people over age 65 and most people under 65 who are receiving Social Security disability benefits (DI). Real Medicare outlays have increased more than tenfold from \$16.9 billion in 1967 (the year the program started) to \$233.4 billion in 1999, and average over \$5,800 per enrollee in 1998. In recent years, the elderly have typically received between 85 and 90 percent of all payments for both Medicare and social security.²

Three smaller social insurance programs, unemployment insurance (UI), workers' compensation, and disability insurance (DI), target prime-age workers. Unemployment insurance (\$21.4 billion in 1999) provides temporary and partial wage replacement to recently employed workers who become involuntarily unemployed. Workers' compensation (\$42.6 billion in 1998) provides cash and medical benefits to some persons with job-related disabilities or injuries, and to their survivors. Disability Insurance (DI) (\$51.3 billion in 1999) is part of the OASDI program, and provides income support to covered workers who are permanently and totally disabled.³ Over time, the enormous increase in the aggregate value of the five social insurance programs have been driven largely by increases in social security and Medicare.

Means-tested Transfer Programs in the U.S.

Medicaid (\$188.8 billion in 1998) is the largest means-tested transfer program, providing medical assistance to low-income persons who are aged, blind, disabled, members of families with dependent children, and certain other pregnant women and children. Asset and income

² Authors' calculations from data provided by the Health Care Financing Administration and Social Security Administration. Other Social Security and Medicare benefits go to families with a disabled member.

³ A covered worker is totally disabled if they are unable to engage in "substantial gainful activity" and permanently disabled if the condition is expected to last more than one year or result in death.

tests that vary across states determine eligibility. Supplemental Security Income (SSI, \$29.7 billion in 1999) is a federally-funded but state administered means-tested safety net program for the aged, blind and disabled whose income and assets are below threshold levels. The disabled comprise nearly 80 percent of SSI recipients.

Aid to Families with Dependent Children (AFDC) was the central safety net program for poor families with children from 1936 to 1996, and was the primary target of the 1996 welfare reform. This program was directed at single-parent families, though some two-parent families with an unemployed parent also received benefits. The program was a means-tested entitlement, meaning that all applicants whose income and assets were below the stipulated levels could receive benefits. States determined benefit generosity that varied widely, and states and the federal government shared the costs of the program according to a federal matching formula. AFDC benefits were \$24.1 billion in 1995. Expenditures for its post-reform successors are difficult to determine, but appear to be around \$13.4 billion, reflecting the precipitous drop in welfare caseloads over this period.

The largest federal cash or near-cash antipoverty program is the earned income tax credit (EITC). Since its introduction in 1975, the EITC has been expanded in Republican and Democratic administrations. The credits most rapid growth has occurred in the last 15 years, with phased-in expansions legislated in 1986, 1990 and 1993.

The EITC is administered through the federal personal income tax, and is directed primarily to working poor and near-poor taxpayers with dependent children. In 1999, taxpayers with two or more children could get a credit of 40 percent of income up to \$9,540, for a maximum credit of \$3,816. Taxpayers (with two or more children) with earnings between \$9,540 and \$12,460

receive the maximum credit. Their credit is reduced by 21.06 percent of earnings between \$12,460 and \$30,580.⁴ The credit is refundable, meaning that if the EITC exceeds the taxpayer's other liabilities, the U.S. Treasury writes a check to the taxpayer for the difference. In fiscal year 1999, the credit cost \$31.9 billion, providing support to 19.5 million taxpayers. In comparison, the credit cost roughly \$3.8 billion in 1975 (in 1999 dollars) and gave benefits to 6.2 million taxpayers.

Two other major means-tested program are the Food Stamps program (\$15.8 billion in 1999) and housing assistance (\$27.6 billion in 1999). Food stamps are designed to enable low-income households to purchase a nutritionally adequate low-cost diet. The program is the country's single, almost-universal entitlement for those with low income and assets.⁵ Housing aid is primarily a federal government function, and comes through public projects rented to low-income families and via income-conditioned subsidies for securing private rental housing. Waiting lists for support are common in housing programs.⁶

Public Expenditures on Safety Net Programs

Figure 1 summarizes the evolution of spending on social insurance and means tested transfers. The cost of social insurance—the largest category—has risen steadily because of rapid increases in the cost of social security and Medicare. Total social insurance expenditures (in real

⁴Table 1 lists the evolution of EITC parameters since the inception of the credit.

⁵ Families receiving SSI or TANF payments are generally automatically eligible for Food Stamps.

⁶The remaining, smaller means-tested programs are Head Start (providing enriched day care to children from poor families, \$4.7 billion in 1999), and two nutrition programs: school nutrition programs (\$7.4 billion in 1999) and the special supplemental nutrition program for women, infants and children (WIC, \$3.9 billion in 1999). In addition, roughly \$5.5 billion is allocated to states through a block grant, called the Child Care and Development Fund (CCDF), designed to assist working poor families with child care needs.

dollars, excluding workers' compensation because of data limitations) rose at an annual rate of 6.9 percent in the 1970s, 3.1 percent in the 1980s and 4.0 percent in the 1990s (through 1998).

The bottom two lines of Figure 1 show total spending on in-kind transfers (without Medicaid, which is roughly the same size as the combined value of the other in-kind transfers), and cash transfers. In-kind transfers (including Medicaid) grew at an annual rate of 12.3 percent in the 1970s, 3.7 percent in the 1980s and 8.9 percent in the 1990s. Cash transfers—the sum of AFDC/TANF, the earned income tax credit (EITC) and SSI—grew at an annual rate of 4.7 percent in the 1970s, 1.8 percent in the 1980s, and 4.2 percent in the 1990s.

II. The Reform of Safety Net Policy in the 1990s

For many years there was widespread dissatisfaction with one key component of the safety net—the AFDC program, which was known as ‘welfare.’ Figure 2 plots the responses to a question drawn from the General Social Survey (GSS), a large and regular household survey.⁷

The question is:

We are faced with many problems in this country, none of which can be solved easily or inexpensively. I'm going to name some of these problems, and for each one, I'd like you to tell me whether we're spending too much money on it, too little money, or about the right amount. Are we spending too much money, too little money, or about the right amount on [...].

The two lines beginning in 1973 highlight American's schizophrenic attitudes toward the safety net. They plot the percentage of respondents saying “too little on welfare” (the bottom series) and “too much on welfare” (the top series). In 1984, the GSS started asking an identical question on “assistance to the poor.” The lowest line (that starts in 1984) shows the percentage

⁷The GSS has been conducted by the National Opinion Research Center (NORC) at the University of Chicago since 1973.

that says we are spending “too much on assisting the poor.” The highest line (that starts in 1984) shows the percentage that says we are spending “too little.”

The GSS responses are striking. First, a near majority of respondents appear to simultaneously believe we are spending too much on welfare and too little on assisting the poor. The conflicting responses to welfare and assistance to the poor highlight tensions that arise when crafting the safety net between an instinct to help disadvantaged families and an unwillingness to do so through welfare programs. Second, there was a sharp increase, starting in 1993, in the percentage of respondents who said spending on welfare was too high. The increase coincides with President Clinton’s 1992 campaign pledge to “end welfare as we know it.” There was a comparable decline in the percentage of respondents who said we were spending too little. These patterns both influence and are influenced by public debates, but they document Americans’ longstanding antipathy toward welfare.

Many factors probably contribute to American’s dislike of welfare. The first is the stubborn persistence of poverty, despite years of anti-poverty spending. Figure 3 shows trends in the official (cash income) measure of poverty for persons older than 64, children under 18, persons 18 to 64, and for the full population.⁸ Poverty rates for children are very high – nearly 20 percent of children are being raised in a poor family.⁹ The 1998 child poverty rate (18.9 percent)

⁸Since the early 1960s, official poverty in the United States has been gauged by an absolute measure. This measure established a set of family-size-specific poverty thresholds, based on of the cost of a minimum adequate diet multiplied by three (to allow for other expenses). The one-third ratio of food to total income was based on studies of consumer expenditures. To determine a family’s poverty status, its cash income before taxes is compared with the appropriate threshold. The U.S. Census Bureau publishes the official annual statistics on the number and proportion poor (the poverty rate) by comparing the thresholds to estimates of families’ cash income before taxes, using income information collected in March of each year in a nationally representative survey, the Current Population Survey. The thresholds are updated annually for price inflation, but are not changed in real dollar terms. The 1997 poverty threshold value for a family of four (two adults and two children) was \$16,050.

⁹ Poverty rates are even higher for families with children under six, where nearly one quarter of U.S. children are being raised in poverty (Green Book, 1998, page 1293).

is only 8.4 percentage points lower than the 1959 child poverty rate and is almost 5 percentage points *higher* than its lowest point in the late 1960s and early 1970s.¹⁰

The second pressure point on the social safety net is the perceived disintegration of the American family. Figure 4 shows the sharp upward trend in the fraction of U.S. children being raised in single-parent families. While research has found, at most, a minor link between welfare benefits and the prevalence of single-parent families, the welfare system in the U.S. does contain incentives that encourage such changes in family structure. Because benefits are family-size conditioned, the incremental cost of children to recipients lies below that faced by nonwelfare families; the system is “pro-natalist.” Moreover, because eligibility for AFDC benefits depends on having dependent children, continued childbearing by single-mother recipients insures continued eligibility and enables long-duration dependency.¹¹ These incentives—when combined with large family sizes of some recipients, and a sizable number of long-term recipients—led some to conclude that the system fosters both excess childbearing by recipients, and dependency. Similarly, because it historically has been difficult for two-parent families to receive AFDC, the cost of both marital separation and nonmarital childbearing is reduced. Again, the high rates of divorce and nonmarital childbearing (especially among teenagers) in the

¹⁰The second striking feature of Figure 3 is the decline in poverty rates for the elderly. In 1959, the elderly poverty rate was 35.2 percent; by 1998, it was 10.5 percent, equal to the poverty rate for prime-age workers. A complete explanation for the strikingly different patterns of child and elderly poverty rates would require analysis of saving behavior of prime-age workers, retirement decisions of the elderly, marriage and fertility patterns of workers with low human capital and the operation of low-wage labor markets. A substantial contributing factor is the rapid expansion of social security since 1959.

¹¹Concern with this pronatalist incentive led 21 states to cap the benefits provided a family at the level indicated by its family size upon entering the rolls. Hence, the birth of another child would not lead to more income support. This provision is referred to as the “family cap.” This policy was first introduced in 1992 in New Jersey.

U.S. have fueled the belief that the welfare system has played an important causal role in encouraging these unattractive behaviors.¹²

A third factor contributing to the dislike of the welfare system is also related to incentives, in particular disincentives to work. These effects are reflected in the high marginal (and average) tax rates placed on the earnings of households that receive benefits. Figure 5 illustrates the budget constraint faced by a single parent with two children in a typical state, under a variety of hours of work and hourly wage rate assumptions. Total annual family income is plotted on the y-axis; family earnings on the x-axis.¹³ The 45° line indicates the annual income-earnings relationship in the absence of all tax and transfer programs.

The lowest (dotted ••••) line shows the income-earnings relationship if the family received only AFDC benefits available in the state. As earnings increase from \$0 per month, the first \$30 plus one-third of monthly earnings is set aside in the calculation of the benefit entitlement, as well as an allowance for travel and work-related expenses. In the earnings range from \$2500-\$7000, income is virtually unchanged at about \$7500 per year. Through this range, then each dollar of earnings results in a nearly equivalent reduction of benefits—a marginal tax rate of 100 percent.

¹²Numerous research studies have failed to confirm quantitatively large or economically significant effects of these incentives, though some response in the expected direction has been found (See Moffitt, 1997). During the same period that these trends in family structure and childbearing are observed, the generosity of AFDC benefits—and hence the asserted incentives—fell.

¹³This figure is constructed from estimates from a micro-data simulation model reported in Giannarelli and Steuerle (1996). In Figure 5, annual earnings from 0 to 2080 hours per year are determined by assuming the welfare recipient earns the pre-reform minimum wage of \$4.25 per hour. (The minimum wage is \$5.15 per hour now.) Working full-time at this wage yields \$8,840 of annual earnings. Earnings beyond this level are assumed to come from increases in the wage rate. For example, the earnings level of \$13,260 in Figure 5 assumes that the recipient works full-time at \$6.35 per hour, which some estimates suggest is close to the expected wage rate of the typical welfare recipient. Also see Dickert, Houser and Scholz (1995) for a similar analysis.

The triangle line ▲▲▲ reflects the relationship between work and income were the family to be eligible for Food Stamps, public housing and Medicaid benefits, as well as AFDC. (It also takes into account payroll and federal income taxes, except for the EITC.) Benefits fall as earnings increase in all of these programs, and starting at zero earnings up to the poverty line (nearly \$13,000 of earnings) the line is nearly horizontal at a total net income, including the in-kind benefits, of roughly \$15,500. Additional earnings are nearly entirely offset by reductions in benefits, again implying the marginal tax rate is close to 100 percent.

The top line (with squares) indicates the effect of the EITC, as it interacts with these other benefits. When earnings are low, the marginal tax rate of the EITC is negative, and offsets the benefit reduction rates in the Food Stamp and AFDC programs. After the earnings level at which the credit is maximized (around \$8,500 for a family with 2 children in this figure), the credit remains constant for a range of earnings, during which the program has no marginal effect on work incentives. Beyond this range, the available credit falls as earnings increase, at about a 20 percent rate. We have indicated the overall marginal tax rates that apply to the various segments of this final income-earnings relationship. As can be seen in the figure, because of the EITC, marginal tax rates are below 75 percent until earnings reach about \$10,000. However, after that level and up to about \$18,000, earnings again get ‘taxed away’ by the reductions in program benefits (and increases in taxes) at a 100 percent rate.

Figure 5 can also be used to illustrate the average tax rate for the welfare family. Assume that the woman faces the choice of either welfare reciprocity or full-time work at a \$6.35 wage rate. As a welfare recipient, her position is shown as point A on the diagram, reflecting a total income (including AFDC, Food Stamps, housing subsidies and Medicaid) of \$15,137. However,

if she were to work full-time at \$6.35 an hour, she would earn \$13,260. This level of earnings exceeds the eligibility limit for AFDC benefits. Annual Food Stamp benefits at this income level are very small, \$572, but the woman receives \$2,428 in EITC benefits, and housing subsidy benefits valued at \$2,430 (plus Medicaid). Taking account of taxes and other offsets to income, the woman's position is shown as point B on the diagram, indicating annual income of \$18,828. Although her market wage rate is \$6.35 for each of the 2080 hours per year that she works, her *net* wage rate (her total income from working full-time less her income should she not work at all, divided by 2080 hours) is only \$1.78.¹⁴ Such a meager hourly return to work is a strong deterrent to entering the labor force and seeking work. Taken together, the high benefit-reduction rates and very low net average wage rates tend to lead some recipients to cease job search completely, and others to reduce hours worked.¹⁵

The fourth pressure point arose from a broad perception in the general public that well-intentioned anti-poverty interventions had few positive effects, and often made things worse. Corbett (1993), for example, discusses a policy dynamic that contributes to cynicism about policy. For policy ideas to become enacted, they must be aggressively marketed, to the point where their likely effectiveness becomes exaggerated. Once enacted, public attention shifts elsewhere and little attention is placed on implementation of the often underfunded policy. Subsequent evaluation then may reveal that the policy failed to live up to promised expectations,

¹⁴ $\$18,828 - \$15,137 = \$3,691 \div 2080 = \$1.78.$

¹⁵In addition to high marginal and average tax rates on earnings, the AFDC and Food Stamps programs contained enforced "assets tests," eliminating eligibility for assistance if assets (including a car) exceed some very low level. For example, in the 1995 AFDC program, those families eligible for benefits cannot hold assets valued at more than \$2,500: \$1,000 in equity value plus a car worth up to \$1500. In the Food Stamp program, the asset limit is \$2,000 for households without an elderly member and \$3,000 for those with an elderly member.

feeding a recurring cycle of cynicism. The following passage from a prominent journalist writing in the *New York Times* (Lemann, 1994) is revealing.

“... Think for a minute why most people believe that the Great Society was a failure. What’s the evidence? It is the enduring physical and social deterioration of poor inner-city neighborhoods. The Government promised to turn these places around, and instead they got worse; *ipso facto*, Government can’t do anything right. This is exactly the button that Marlin Fitzwater tried to push [in 1992] when he blamed the Great Society for the Los Angeles riots... Voters are absolutely certain that social services cost a lot and don’t work, so political support for them is hard to come by.”

The fifth pressure point arises from a possible discrepancy between the objectives of the system and citizens’ judgments regarding the nature of the poverty problem. While the system sought to offer collective support to supplement poor people’s own income, many Americans see the poverty problem as something quite different from the simple need for income assistance. With the rapid growth in the number of women with children who work outside the home, able-bodied women with children became expected to contribute to their own well-being through work. And with most young and low-education people experiencing eroded real earnings, concern with maintaining the incomes of similar people who did not work waned. These concerns have been reinforced by perceptions of counterproductive behaviors and choices by some of those receiving benefits—to bear children out of wedlock as teenagers, to not complete high school, to refuse minimum-wage employment when it is available, to abuse drugs and sell them.

III. The 1996 Welfare Reform Act (PRWORA/TANF)

Pressures on the safety net have made welfare reform a near-quadrennial event. Since the 1960s every U.S. president other than Gerald Ford had a highly publicized plan for reforming welfare, though only one of these, the Family Support Act of 1988 (FSA) became law. The FSA

shifted the nation's welfare system by requiring states to establish a Job Opportunities and Basic Skills Training (JOBS) program to "help needy families avoid long-term welfare use." JOBS provided job search assistance, education, work experience, vocational training, and other employment-related services, and required all parents except those with small children to participate in these work-related activities or face a reduction in the amount of assistance received. Unfortunately, evaluations of the JOBS program were mixed at best.

Along with JOBS, and in anticipation of a major reform, the federal government had, throughout the decade of the 1990s, encouraged states to come forward with demonstrations designed to test proposed reforms. States responded in force: by 1995 proposed demonstration projects had been approved for 43 states, covering three-fourths of AFDC recipients. The range of demonstration proposals mirrors the set of problems that have been associated with the welfare system. For example, 36 states implemented some form of work requirement; 31 states proposed time limits on the receipt of benefits; 41 states adopted (positive or negative) financial incentives to encourage the move from welfare to work; 39 states proposed either "encouraging parental responsibility" by education or imposing 'sanctions' for having another child while on welfare,¹⁶ for teenage recipients who lived apart from their parents, or for failing to attend mandated education/training programs.¹⁷ The move from this free-for-all potpourri of program waivers to comprehensive reform is not as large a leap as it might first appear; already states had been thinking about new ways of doing business in this area.

¹⁶"Sanctions" refer to warnings followed by reduction of benefits, or removal of some persons in the family from benefits, or (at the limit) denying eligibility for benefits.

¹⁷See Wiseman (1997). In addition, numerous states required mothers to identify their children's fathers, and implemented tough child support enforcement efforts (U.S. Department of Health and Human Services, 1996).

PRWORA/TANF–The 1996 Legislation

Beginning in the early-1990s, welfare reform was debated within Congress, within the Clinton administration, and between the two. It was clear that reform would be far-reaching and not incremental. The resulting legislation, signed by President Clinton after vetoing two prior Congressional packages, abolished AFDC and in its place, established Temporary Assistance for Needy Families (TANF).

As stated in the legislation, TANF has four primary objectives:

1. To assist a central target group—needy families—to care for children;
2. To promote job preparation and work (that is, to reduce “dependency”);
3. To reduce out-of-wedlock childbearing; and
4. To promote mother-father families.

These goals clearly reflect some of the primary concerns with the pre-reform system. However, rather than changing the structure or assuming control of the AFDC program and correcting its structural and incentive problems, Congress instead removed the program from federal jurisdiction and assigned responsibility to individual states for accomplishing these goals. Along with the responsibility, the federal government also provided financing to accomplish the objectives—pre-reform federal expenditures for welfare were packaged into a fixed “block grant” and assigned to individual states depending on their previous AFDC expenditures.¹⁸ The legislation granted wide discretion to states in the use of the block grant monies, permitting

¹⁸States must continue to spend at least 80 percent of their pre-TANF expenditures on the new program (or 75 percent, if they meet the mandatory work requirement goals of the program). This is known as the “maintenance of effort” provision. The use of the pre-TANF program as a basis for the block grant freezes the prior discrepancies in state spending and favors those states which have greater ability to pay and have chosen to have more generous programs historically. The federal government continues to fully fund the EITC and Food Stamp programs and continues the federal matching program for Medicaid.

allocations to child support enforcement, child care assistance, job subsidies, medical care assistance, training/education, and the creation of asset accounts to encourage saving. Although states were given substantial freedom in designing their own approach to assisting poor families, the federal legislation also imposed restrictions and requirements on states.

The new restrictions and requirements embody defining characteristics of the new legislation. They are:

- The new state TANF laws can not establish a right (or “entitlement”) for families to receive cash income support, even if they meet certain eligibility requirements. Indeed, states must impose limits on the length of time that families can receive services; in particular, no family can be given any help that involves federal funds after it has received a maximum of five years of assistance.¹⁹
- States must meet targets for the proportion of assisted families that have full-time workers; in turn, states are encouraged to impose additional work requirements on families.²⁰
- States are required to develop comprehensive programs for enforcing the collection of child support payments from noncustodial parents. Mothers who refuse to identify the father(s) of their children are denied all (or part) of the assistance package.
- States must implement programs designed to reduce the prevalence of teen nonmarital childbearing.²¹ Unmarried teen parents who receive help must be in school and living with parents (or under alternative adult supervision).
- No one convicted of a drug-related crime is permitted to receive help unless the state enacts legislation specifically authorizing such assistance; legal immigrants admitted to the country after the passage of TANF (except refugees) cannot be assisted by a state

¹⁹TANF does permit states to exempt 20 percent of the people receiving benefits or services from this time limit, and states may provide benefits or services out of their own funds.

²⁰By 2002, 50 percent of all one-parent families must have a worker employed at least 30 hours per week, and 90 percent of all mother-father families must have a worker employed at least 35 hours per week. With recent sharp caseload reductions, states have easily met existing requirements.

²¹TANF provides funding for ‘abstinence education’, requires that states be annually ranked on their performance in reducing teen nonmarital birth rates, provides \$1 billion over 5 years for performance bonuses to states that achieve reduced nonmarital birth and increased two-parent family prevalence rates, and provides \$400 million in bonus payments to states that reduce rates of nonmarital childbearing.

under the new program (or receive Food Stamps) for their first five years in the country.²² Families whose income is above the former eligibility limit for AFDC, may not be eligible for Medicaid benefits.²³

Though financed as a block grant, TANF and its accompanying restrictions, represents a major restructuring of federal-state fiscal and administrative relations in U.S. social policy.²⁴

Emerging Models for Assistance to Needy Families

As is clear from these provisions, a wide variety of new, diverse, and hand-tailored individual state programs targeted on the low-education, unskilled, working-age population with children will evolve. It will be several years before the complete dimensions of this new and uncoordinated arrangement will be known. Nevertheless, several potential models for the future of welfare have emerged.

The Wisconsin Works (W-2) Program

Wisconsin eliminated the AFDC cash income support welfare program, and did so on its own prior to the passage of the national TANF legislation. In its place, the Wisconsin Works (W-2) program was established. While W-2 ends the entitlement to cash income support, it does ensure that all working-age people with income at or below 115 percent of the poverty line (and not just single parents) have—and do—*work*. And support for work activities, such as child care assistance and subsidized health care, is made available.

²²However, states may use their own funds to provide such benefits. The 1997 balanced budget act restored disability and health benefits.

²³Children in families with incomes up to 200 percent of the poverty line may be covered under a new initiative passed in 1997, the Child Health Insurance Program (CHIP). Similar to TANF, CHIP provides states a block grant and flexibility to design their own programs.

²⁴While federal expenditures for AFDC were diverted into block grant form, benefits and expenditures for Food Stamps and the EITC were maintained, with minor changes. The Food Stamps change reduced benefits somewhat and established a new work requirement under which prime-age, healthy individuals without dependent children lose Food Stamps if they do not work at least 20 hours per week or participate in a workfare or approved training program.

Poor people who appear at a W-2 office—now called “job centers” rather than welfare offices—are guided into a work-oriented regime. They meet with a “Financial and Employment Planner,” no longer a welfare caseworker, who advises them of their work options and assists them to make the best choice among these options. Counseling is provided and clients are told of the job-finding support offered by the program and the child care and health care subsidy arrangements that are available. Because several program offices are housed in the center, the client is told of the other programs for which she may be eligible, and especially of the work supports (e.g., child care subsidies) that may be available. Each is told to expect being employed full-time, full-year, and that their income will depend on their work efforts, not on their family size or needs.

This is a major change in approach. In the old AFDC system, the main task of the case worker was to see if the family met the eligibility rules of the program (single parent status, no assets, no other income source), and if they did, to determine the amount of the monthly check that would be sent to the recipient. The larger the family, the bigger the check. There was no counseling, no planning, and little emphasis on work.

Wiseman (1999) identified five features that are at the heart of W-2. (1) It focuses on adults, rather than children. (2) It denies core cash assistance to most adults if they do not work full time. For those unable to find employment in the private sector, it provides public sector jobs, albeit at low wages. (3) Eligibility for other services (health care, child care, transportation, child support enforcement) are not tied to receipt of TANF cash benefits. Indeed, only roughly 20 percent of the W-2 budget now goes to cash assistance. The balance funds ancillary services such as child care, health care and transportation that enable W-2 recipients to work. (4) There

is an emphasis on responsibility and reciprocity. The state provides W-2 as an opportunity; those in need assume responsibility, with assistance, for taking advantage of it. (5) Program provision and administration are separated: non-governmental organizations are frequently responsible for running W-2 programs.

The most well-publicized aspect of W-2 is its 4-tier job ladder. Upon entry into the program, clients are assessed by the W-2 Planner, and are assigned to one of four categories of work options. The most qualified are allocated to the top category of work options—*regular jobs in the private economy*—and given information and advice on how to find such a job. If they are successful, they will earn income and support themselves; they will cost the state very little, except for the day care and health care subsidies they receive. They will also be eligible for Food Stamps and the EITC. It is expected that most of these people have the skill and experience necessary to be self-sufficient, to earn enough to be ineligible for cash income support.

The second tier is *trial jobs*, which are directed at individuals with basic skills, but are not ready for unsubsidized employment. With the trial jobs, employers are paid up to \$300 a month to train and supervise workers for up to 6 months. Employers must pay at least the minimum wage. This component of the job ladder has not been used very much.

Those with fewer skills or other work qualifications may be placed in a *community service job*. These jobs pay \$673 per month and require 40 hours of participation per week. However, 10 hours of education/training can be substituted for 10 hours of work. Provision of these jobs is costly to the state; all of the wage costs plus the supervision and job arrangement costs are paid by the state, and again day care and health care subsidies are available. Clients in this category are penalized the national minimum wage rate of \$5.15 for every hour of the 40 hours missed

without good cause, and are not eligible for the EITC. The harsh terms in this option are expected to provide the incentive to move up the job ladder, making this a temporary stopping point.

Finally, the least well-off, are placed in *W-2 Transitions*, where they engage in activities including treatment for alcohol or drug abuse, community rehabilitation (generally for a disability), counseling, or obtaining shelter or safety from domestic abuse. Individuals in *W-2 Transition* will also be paid, but not much—about \$630 per month plus the health and child care subsidies. Again, forty hours of participation per week are required, 28 hours of work and 12 hours of education/training. No EITC support is available and the same minimum wage penalty applies for time missed without good cause. As with community service jobs, the meager level of available benefits in *W-2 Transitions* provide a strong incentive to move up the job ladder.

Consistent with TANF, *W-2* will only provide services and employment assistance to any client for a maximum of five years. Teen parents are required to live with parents who will provide them support; they are mandated to attend high school, and *W-2* only provides some in-kind support for child care. Similarly, *W-2* adopts the TANF restrictions on providing services to legal immigrants, and aggressively seeks child support from noncustodial parents, passing this support directly through to the children's caregivers.

As a result of these changes and the ending of the entitlement, the culture of state-assisted support has been fundamentally changed, and with it the expectations of the state's low-income population. Supported by a robust economy, the number of people seeking support has decreased substantially. By 1997, the number of recipients of *W-2* services was only about 30 percent of the number receiving AFDC benefits three years earlier. And, by early 1999 only about 10,000

cases receiving cash assistance remain open, which is about 10 percent of the peak number in 1994

W-2 is distinctive, not only because the precipitous drop in caseloads induced, at least in part, by the program (the State's strong economy and expansions of the EITC also likely played a role), but by its strong focus on work. Studies of people who recently left Wisconsin's welfare system suggest that people formerly on the caseload are indeed working, but, not surprisingly, a large fraction of these families are living with incomes at or below the poverty line.²⁵ For example,

- Fifteen months after leaving welfare, about 30 percent of all who left were receiving no public assistance. The majority received some form of public assistance, mainly Medicaid, over the entire 15 month period.
- For all the leavers, median annual earnings were around \$7,800 in the year after exit—\$9,100 for those who never went back on welfare.
- About 36 percent of women with one child, and only 17 percent of women with three children, had measured incomes greater than the poverty line in the first year after they left welfare.
- As the caseload fell after the passage of W-2, those remaining on the welfare roles appear to be more difficult to employ.

No studies have yet tried to directly measure the effect of W-2 relative to a counterfactual world in which W-2 had not been implemented.

The Minnesota Family Investment Program

The Minnesota Family Investment Program (MFIP) has many of the same rhetorical points of emphasis as W-2, but appears to rely more on incentives as opposed to sanctions to achieve its

²⁵See Cancian *et al.* (1999a, 2000). There is no reason to think that the statistics that characterize the experiences of Wisconsin families leaving welfare are any worse than those that apply to families from other states, and given the states strong economy and extensive work supports provided by W-2, they may be better.

goals. Rather than abolishing AFDC, as is done in W-2, MFIP reforms welfare into a work-oriented program.

MFIP has four major parts (Knox, Miller and Gennetian, 2000). (1) It enhances financial incentives as a supplement to earned income, which encourages people to work. Welfare benefits are received by participants until their income is 40 percent above the poverty line. (2) Child care payments are made to providers, rather than being paid by MFIP participants up front. (3) Public assistance rules and benefits (including food stamps) are simplified and put into a single cash benefit program. And (4) employment-focused activities are mandatory for all MFIP participants unless they are already working 30 hours or have a child under the age of one.

The evaluation of MFIP conducted by the Manpower Development Research Corporation (MDRC) suggests it substantially increased employment and earnings relative to the AFDC program, and the effects continued for at least three years (the last year of the evaluation, to date). The higher earnings and larger welfare payments reduced poverty. MFIP appeared to also reduce domestic abuse, modestly increased marriage rates, and, for children, improved school performance and reduced behavioral problems. For two-parent families, MFIP appeared to increase marital stability. Knox, Miller and Gennetian (2000) noted “Because MFIP increased support for working families – through financial incentives and, for two-parent families, less restrictive eligibility rules – the program cost between \$1,900 and \$3,800 more per family per year than did the AFDC system.” The MDRC evaluation results for MFIP are among the most promising of any welfare reform.

The Oregon TANF Program

The Adult and Family Services Division (AFS) of the Oregon Department of Human Services has transformed their approach to welfare in a direction somewhat different than W-2 and MFIP: it too may be a harbinger of the future of welfare.²⁶ Like other states, the mission of Oregon's AFS is "to help low-income families become self-sufficient. In the past, the emphasis was on determining eligibility and providing benefits." Responsibility for programs has been pushed down from the state to county and even local agencies. This results in considerable variation within the state in services offered to clients. The model in the words of AFS, is

Beginning with their first contact with AFS, clients hear a message of self-sufficiency. Staff members of AFS and partner agencies help families find employment or other resources, and people who come onto public assistance are expected to participate in activities that move them to their employment goals. When clients find work, they receive help in keeping their job and advancing to better employment, through services designed to meet their needs.

When operating well, the program will find resources to strengthen families. These may include community colleges and JTPA agencies that provide "life skills," basic education, training and vocational programs; job placement resources; crisis support services for domestic violence, food needs, and housing services; mental-health, alcohol and drug programs; disability-related services; child care services; and volunteer and mentoring services. The rhetoric and, it appears, the practice of the program is notably softer than what is heard in MFIP and W-2, and seems to emphasize ancillary services that facilitate work and programs to attack domestic violence, prevention of teen pregnancy and juvenile crime, and family case management.

²⁶Material for this section comes from the Web page, <http://www.afs.hr.state.or.us/>.

In some respect the Oregon model seems to harken back to a time when the social work profession dominated the development and conduct of anti-poverty policy. While we are not aware of any rigorous evaluation of Oregon's welfare policy, caseloads fell by 60 percent between 1994 and July, 1999, and, in the words of the AFS, "not by keeping people out of the program, but by moving them to employment or obtaining other resources such as child support. More than 1500 clients find work each month, and they earn an average of more than \$7.00 per hour. Nine-tenths of them are off welfare 18 months later."

The Future of TANF

TANF was launched at an unusually propitious time. The country was in the midst of the longest economic expansion in history. Labor markets were tight, and the earned income tax credit (see below) had been expanded both in 1990 and 1993. With the strong economy and sharp reductions in caseloads, the TANF block grants (the funding mechanism from the federal government to the states) was considerably larger than the amount states would have received under AFDC, given the size of their (declining) caseloads. This provided the resources, along with the flexibility inherent in the block grants, to adopt programs that differ in significant ways from past practice and from programs adopted by other states.

It is too early to tell how welfare nationwide will evolve. Clearly new ways of doing business have emerged. Some appear quite promising. Yet few strictures are put into place that would prevent a state from eviscerating its safety net and TANF policies have evolved in the strongest economy in decades. Welfare reform is clearly not eradicating poverty. A recent study of families leaving welfare showed that despite substantial work effort and varied sources of income, 19 percent of the women were poor in all of the five years, and just 22 percent had

incomes above poverty in every year.²⁷ Only about 5–10 percent *earned* enough to pull their families above the poverty line. At the same time, solid research comparing the effects of TANF relative to alternative ways of structuring the safety net is in its infancy.

IV. Making Work Pay: The Effects of the Earned Income Tax Credit

The EITC has become a very important federal antipoverty initiative. It is well targeted. By its structure, the credit is limited in 1999 to taxpayers with earned income and adjusted gross income less than \$30,580 if they have more than one qualifying child, \$26,928 if they have one qualifying child, and \$10,200 if they have no qualifying children. Hotz, Mullin and Scholz (2000) report that more than half of EITC payments go to families with incomes below the poverty line.²⁸ In 1997 and 1998 the EITC removed 4.3 million persons from poverty (Council of Economic Advisors, 1998, 2000).

Because the EITC is based on annual family income and not wages, it is possible that people with high hourly wages who for some reason or another, choose to work relatively few annual hours could receive the credit. In fact, the evidence suggests that in low-wage labor markets, incomes and wages are tightly linked. Hotz, Mullin and Scholz (2000) report tabulations from Survey of Income and Program Participation (SIPP) data from April, 1997 show that 40 percent of EITC payments go to taxpayers with wages in the bottom 25 percentile of all workers with children (below \$6.25 per hour) and 80 percent of all EITC benefits are paid to workers with

²⁷See Cancian *et al.* (1999a).

²⁸The HHS poverty guidelines for 1999 are \$8,240 for a one-person family, \$11,060 for two-person families, \$13,880 for three person families, and \$16,700 for four-person families. Scholz and Levine (2000), for example, calculate using the April, 1997 SIPP that over 60 percent of EITC payments go to taxpayers with pre-EITC incomes below the poverty line and roughly half of total payments directly reduce the poverty gap. In unpublished calculations by Richard Bavier at OMB, 49 percent of EITC payments were made to taxpayers with pre-EITC incomes below the poverty line in the 1998 CPS.

wages below the median of \$9.78 per hour. If monthly hours are extrapolated to annual totals, 86.9 percent of EITC recipients worked at least 1,000 hours and 68.1 percent worked more than 1,500 hours per year.

Though the evidence is now somewhat dated, it appears that the EITC gets high marks for reaching its intended beneficiaries. Scholz (1994) used matched data from tax returns and the SIPP to calculate that 80 to 86 percent of taxpayers eligible for the EITC appeared to receive it in 1990. Developments since 1990 have an ambiguous effect on EITC participation rates. The maximum credit has increased sharply since then, from \$1,207 to \$3,756 in 1999 dollars, and the credit extends further up in the income distribution, where filing propensities are high. However, there has been a steady increase in labor force participation of single women with children (Meyer and Rosenbaum, 1999), and new workers in this group presumably have lower filing propensities than the typical worker in the population. In addition, the IRS no longer will intervene and award the credit when taxpayers file and appear eligible, but do not take the credit. Instead they send a letter to taxpayers encouraging them to consider filing an amended return.

Several papers have examined the effects of the EITC on labor market participation (see Hotz and Scholz, 2000, for a comprehensive survey). In a recent study Meyer and Rosenbaum (1999) find that EITC changes account for 63 percent of the increase in the employment rate of single mothers from 1984 to 1996 and 37 percent of the increase from 1992 to 1996. There is broad agreement in the academic literature that the EITC significantly increases the labor market participation of low-income, single parent families.

Eissa and Liebman (1996) examine the hours worked of taxpayers who were already in the labor market when 1987 EITC phase-outs were extended to additional workers. They find no

declines in hours worked as a result of the higher phase-outs. Liebman (1997) also shows that there is no bunching of taxpayers at the beginning and end of the phase-out range, as might be expected with the discontinuity in the implied marginal tax rates. As Liebman notes, it is not surprising that negative effects on hours for people already in the labor market are small because the precise relationship between the EITC and hours worked is likely to be poorly understood by most taxpayers. The majority of EITC recipients pay a third party to prepare their tax returns and it is difficult to infer the implicit tax rates embodied in the credit from the look-up table that accompanies the EITC instructions. This confusion is less likely to mitigate positive participation effects, since for this to be operative, taxpayers only need to understand there is some tax-related bonus to work. There is abundant anecdotal evidence that taxpayers have this understanding (see, for example, DeParle, 1999).

Compared to alternative delivery mechanisms, the EITC is inexpensive to administer. As noted above, most EITC recipients would be required to file a tax return even in the absence of the credit, so the costs imposed on taxpayers of filling out Schedule EIC (a 6-line schedule that gathers information about qualifying children) is small. The cost to the IRS is also quite small. The entire IRS budget in FY1995 was \$7.6 billion and the IRS served 116 million individual taxpayers and 15 million corporations. The incremental cost of administering the EITC is surely a very small fraction of this total. The costs of administering two other major income support programs for low-income families are much higher. Administrative costs for food stamps were \$3.7 billion in FY1995, and AFDC administrative costs were \$3.5 billion.

While a system based largely on self assessment (like the U.S. income tax) will have lower administrative costs than a more bureaucratic approach, it will also have higher noncompliance.

The most recent study of EITC noncompliance examined returns filed in 1997 and found that of the \$30.5 billion claimed in EITC, \$7.8 billion, or 25.6 percent of the total exceeded the amount to which taxpayers were eligible (Internal Revenue Service, 2000).

The rate of EITC noncompliance appears higher than the overall U.S. tax gap, where it is estimated that 17 percent of total taxes are not paid.²⁹ While compliance appears to be very high for wage and salary income, presumably because of third-party information reporting, compliance rates on self-employment income, certain types of capital income and income earned in the informal sector are worse than the EITC. Nevertheless, EITC noncompliance appears to be the single most important threat to the credit's political viability.

The EITC and Other Countries

As suggested by the preceding, the EITC appears to be an effective, beneficial policy for U.S. low-wage workers. But its effectiveness is enhanced by several features of low-wage labor markets in the U.S. The EITC might be a less useful tool in countries with different policy environments.

- Relative to other OECD countries, the U.S. has few employment regulations that constrain the ability of employers to alter the size of their work force and few mandated benefits. The relative absence of labor market rigidities reduces barriers to hiring low-skill workers and presumably enhances the effectiveness of the EITC in stimulating labor force participation.
- The family is the unit of taxation in the U.S. The target efficiency of the EITC is enhanced by limiting it to families with incomes below roughly \$30,000. Countries whose tax systems are based on individual, rather than family income will have a difficult time limiting the EITC to low-income families.

²⁹Internal Revenue Service, *Federal Tax Compliance Research: Individual Income Tax Gap Estimates for 1985, 1988, and 1992*, Publication 1415 (Rev. 4-96) Washington, D.C.: 1996

- The U.S. has a relatively effectively administered individual income tax. Consequently, a very large fraction of EITC-eligible families would file tax returns even in the absence of the EITC.³⁰ This leads to high EITC participation rates and low administrative costs.
- By OECD standards, the U.S. is a low-tax country (only South Korea, Mexico and Turkey have lower ratios of taxes to GDP among the OECD countries). While cumulative marginal tax rates in the phase-out range of the credit are high, they do not appear to be so onerously high as to stifle work (or create an employment trap).³¹
- The U.S. has a fairly low minimum wage of \$5.15 per hour. While in perfectly competitive markets employer-based and supply-side subsidies (like the EITC) will have the equivalent effects, with a binding minimum wage, employer-based subsidies will be more effective policy. A binding minimum wage limits the ability of employment and wages to adjust to an increase in labor supply prompted by the supply-side subsidy.

V. Is the U.S. System of the EITC and TANF a Model for Other Nations?³²

With the expansion of the EITC, the abolition of AFDC and implementation of TANF, the U.S. is undergoing a sharp change in philosophy regarding society's support and treatment of those citizens with the least earnings capacity. Work, self-sufficiency, economic independence, and responsibility have replaced income support cum education/training. Does this welfare-to-work approach hold potential for other nations, which—like the U.S.—continue to struggle with how best to cope with their least productive citizens?

Drawing from research findings and our own interpretation of the advantages and disadvantages of other nation's approaches, we offer some reflections on this question.

³⁰Low-income families would generally file returns because their incomes exceed filing thresholds or to get back withheld taxes. With the new \$500 child credit along with personal exemptions and the standard deduction, a married couple with two children will not have a positive tax liability until their earnings exceed \$24,600, even without the EITC, but they will be required to file if their incomes exceed \$12,500.

³¹In the phase-out range of the credit, some families may face marginal tax rates exceeding 50 percent. If workers bear the full burden of social security payroll taxes, combined marginal rates may be 14.2 percent for payroll taxes (15.3/1.0765) plus 15 percent from the individual income tax plus 21.06 percent for the EITC phase-out. Families also likely to bear some of the burden of state sales taxes, income and property taxes.

³²The following discussion draws from Haveman and Wolfe (1999).

First, the strategies of “diversion,” restricting the concept of “entitlement,” and imposing time limits on the receipt of income support appears to fundamentally change the perspective of potential clients regarding expectations of what they need to do for themselves relative to what the state will do for them. To the extent that “dependence” on public transfers is a major problem for many nations, such a change in expectations and perspective may be attractive. Since the passage of TANF, more persistent job search activities are in evidence, and numerous potential transfer recipients have become self-sufficient earners. For those generous welfare states of Western Europe currently struggling with high unemployment (particularly of youth) and costly and generous income support systems that erode pressures to seek and accept employment, this element of the U.S. reform should be given close scrutiny. While the recognition that normal, private sector work requires the provision of associated health care and child care services seems to have been a revelation to many Americans, such arrangements are already in place in many European nations and other developed countries, making the application of pressure to seek and accept work more feasible for them.

Second, the emphasis on job finding rather than on training/education does seem to rest on difficult-to-refute research evidence. Adults with low skills do seem to accumulate needed human capital on the job as well as in structured (largely institutional/classroom) education/training programs.³³ The lesson for “active labor market” states such as Sweden could be an important one, especially in the face of growing suspicions regarding the cost-effectiveness of extensive public sector training/education programs for low-skilled unemployed workers.³⁴

³³This conclusion must remain a tentative one, as the ultimate employment and earnings success of clients who have secured jobs is not yet known.

³⁴See discussions in Freeman, Topel, and Swedenborg (1997), and *Swedish Economic Policy Review* (1998).

Third, the U.S. approach toward its citizens of lowest earnings capacity reflects acceptance of a labor market that generates high-variance wage and earnings distributions, and an expectation that families should become and remain self-sufficient within this market framework. While this tolerance for inequality has unattractive side-effects, it has also fostered an enviable record of job creation and employment. Placing much of the responsibility for income support for low-earnings-capacity families on their own efforts in the private labor market also reduces demands on the fisc and associated pressures for high taxes and employment-related charges. The advantages of income support through employment seem clear, especially if income receipt associated with one's own efforts carries with it more self-esteem and satisfaction than reliance on public assistance or social security payments. In fact, there is a trade-off between the inequality consequences of the U.S. arrangement (especially as reflected in TANF) and the adverse employment and economic growth consequences of generous and accessible benefits (and the very large wedge between the employer costs of using labor services and the net return to workers from supplying labor) in the most advanced welfare states. Both systems could benefit by considering still other arrangements to secure a more optimal position on the collective-individual responsibility continuum.

In this regard, there is one additional aspect of the reformed U.S. welfare system that nations would do well to consider. The effort to “make work pay” in the United States has resulted in the implementation of a large and effective program which subsidizes the work efforts of low-earnings individuals—the EITC. If both wage flexibility in the interest of employment growth and low rates of income poverty are to coexist, some means of supplementing market returns associated with work must be found. Many such measures in addition to a U.S.-style EITC have

attractive efficiency characteristics and are administratively feasible. They would seem natural complements to efforts designed to shift the emphasis from public transfers with their adverse incentives for labor supply and other behaviors to work-related policies.

Finally, the increased emphasis in the United States on parental responsibility for one's children as embodied in its child support system is one that other nations are likely to find attractive. Increased numbers of children are being born out of wedlock in nearly all developed countries. To the extent that this implies that more children are being raised by a single parent, a well-enforced child support system can both reduce the need for state provision for children's well-being and encourage greater parental involvement with their nonresident offspring.

While some of these aspects of the U.S. reform may serve as models for other nations, there are other aspects of this policy that would appear either irrelevant or unworthy of emulation. As we have emphasized, the U.S. reform was in part stimulated by aspects of family structure or behavior—high rates of teen nonmarital childbearing, high birth and low marriage rates among the recipient population—that do not seem to characterize most other developed European or Asian nations. Those attributes of TANF that are targeted on these issues seem hardly transferable.

The devolution of social responsibility for the support for low-earnings-capacity citizens from the national government to lower units (states and counties) is another characteristic of the U.S. reform that also seems less exportable to other nations. The lack of concern with the large variance among regions in terms of resources and attitudes toward poor people and minorities that is implicit in TANF runs quite counter to European Community efforts to harmonize policies and reduce inequalities among regions. Providing incentives to work and earn would

seem possible in that environment without the risk of interjurisdictional competition and a “race to the bottom” that U.S. policy carries.

In addition to these reflections, we conclude by noting two additional concerns raised by the U.S. reform, which deserve careful reflection by other nations as they embark on social policy reform. Because the amount of federal block grant support is fixed, TANF requires states to bear full costs of any expansion of program costs, reducing the incentive to expand coverage or increase support, and increasing the incentive to shift increased costs to county and local governments.³⁵ This, along with the elimination of support as an “entitlement,” also raises questions regarding the adequacy of the likely responses of governments to the circumstances of poor families when less favorable macroeconomic conditions ensue. Other countries would do well to ensure that policy is not designed in a way that provides incentives for decision-makers to cut the safety net when macroeconomic conditions deteriorate.

Second, there is no firm federal mandate in the U.S. for rigorous evaluation of the state-based reforms, and without such impetus, individual states appear to have little incentive to require and pay for serious evaluation efforts. Given that many participants will not be able to earn enough to escape poverty, effective policy making should ensure that the impacts of reform on affected citizens be objectively assessed and reported. The absence of a rigorous evaluation

³⁵Understanding how states will respond to the new incentives incorporated in the 1996 legislation is essential in assessing the ultimate economic impact of the reform. Chernick (1998) sets out a conceptual framework for studying these fiscal responses and provides rough estimates of the impacts of the reform based on quite divergent econometric estimates available in the literature. In attempting to answer the question regarding the overall impact of the reform on public spending on the poor, Chernick identifies several margins of state and individual response that are relevant, including the relationship between state TANF spending and spending on other programs targeted on the poor (see Table 1 in Chernick), state fiscal responses to both “price” and “income” effects contained in the reform, enforcement of “maintenance of effort” requirements on states, client entry to and exit from the new programs that will be developed, and interstate migration responses to state differences in these new TANF programs.

component to state TANF reforms is surely an undesirable feature of U.S. policy that other nations contemplating major policy changes should not emulate.

References

- Chernick, Howard. (1998). "Fiscal Effects of Block Grants for the Needy: An Interpretation of the Evidence." *International Tax and Public Finance*, 5 (2, May), 205–233.
- Corbett, Thomas, 1993, "Child poverty and welfare reform: Progress or paralysis?" Focus: Institute for Research on Poverty, 15:1
- Council of Economic Advisers, 1998, "Good News for Low Income Families: Expansions in the Earned Income Tax Credit and the Minimum Wage," Washington, D.C., December
- Council of Economic Advisers, 2000, Economic Report of the President, Washington, D.C., February
- Cancian, Maria, Robert Haveman, Thomas Kaplan, Daniel Meyer, and Barbara Wolfe. 1999a. "Work, Earnings, and Well-Being After Welfare." In Sheldon Danziger, ed., Economic Conditions and Welfare Reform. Washington, DC: Urban Institute Press.
- Cancian, Maria, Robert Haveman, Daniel Meyer and Barbara Wolfe. 1999b. "Post-Exit Earnings and Benefit Receipt among Those Who Left AFDC in Wisconsin" Institute for Research on Poverty Special Report no. 75 Madison, WI.
- Cancian, Maria, Robert Haveman, Daniel Meyer and Barbara Wolfe.. 2000a. "Before and After TANF: The Economic Well-Being of Women Leaving Welfare" Institute for Research on Poverty Special Report no. 77. Madison, WI.
- DeParle, Jason, 1999, "Once a Forlorn Avenue, Tax Preparers Now Flourish," New York Times, 3/21, p. 1
- Dickert, Stacy, Scott Houser and John Karl Scholz, 1995, "The Earned Income Tax Credit and Transfer Programs: A Study of Labor Market and Program Participation," *Tax Policy and the Economy*, James M. Poterba (ed.), National Bureau of Economic Research and the MIT Press, 9, 1-50
- Eissa, Nada and Hilary Williamson Hoynes, 1998, "The Earned Income Tax Credit and the Labor Supply of Married Couples," NBER Working Paper #6856.
- Eissa, Nada and Jeffrey B. Liebman, 1996, "Labor Supply Response to the Earned Income Tax Credit," *Quarterly Journal of Economics*, May, 605-637
- Freeman, Richard B., Robert Topel, and Birgitta Swedenborg, eds. (1997). *The Welfare State in Transition: Reforming the Swedish Model*. Chicago, IL: University of Chicago Press.

- Giannarelli, Linda, and Eugene Steuerle. (1996). "The True Tax Rates Faced by Welfare Recipients." 1995 Proceedings of the Eighty-Eight Annual Conference on Taxation. National Tax Association.
- Green Book, 1998, "Background Material and Data on Programs Within the Jurisdiction of the Committee on Ways and Means," U.S. Government Printing Office, May 18.
- Haveman, Robert, and Barbara Wolfe. 2000. "Welfare to Work in the U.S.: A Model for Other Developed Nations?" International Tax and Public Finance.
- Hotz, V. Joseph, Charles H. Mullin and John Karl Scholz, 2000, "The Earned Income Tax Credit and Labor Market Participation of Families on Welfare," Paper prepared for the Joint Center on Poverty Research Conference on Means-Tested Transfers, December
- Hotz, V. Joseph and John Karl Scholz, 2000, "The Earned Income Tax Credit," forthcoming in *Means Tested Transfers*, Robert Moffitt (editor), July
- Internal Revenue Service, 2000, "Compliance Estimates for Earned Income Tax Credit Claimed on 1997 Returns," September, Washington, D.C.
- Liebman, Jeffrey, 1997, "The Impact of the Earned Income Tax Credit on Incentives and Income Distribution," Tax Policy and the Economy,
- Knox, Virginia, Cynthia Miller and Lisa A. Gennetian, 2000, "Reforming Welfare and Rewarding Work: A Summary of the Final Report on the Minnesota Family Investment Program," Manpower Development Research Corporation, September.
- Meyer, Bruce D. and Dan T. Rosenbaum, 1999, "Welfare, the Earned Income Tax Credit, and the Labor Supply of Single Mothers," NBER Working Paper 7363, September.
- Moffitt, Robert A. (1997). "The Effects of Welfare on Marriage and Fertility: What Do We Know and What Do We Need to Know?" Institute for Research on Poverty, Discussion Paper no. 1153-97, University of Wisconsin-Madison.
- Scholz, John Karl, 1994, "The Earned Income Tax Credit: Participation, Compliance, and Antipoverty Effectiveness," *National Tax Journal*, March, 59-81.
- Scholz, Karl, and Kara Levine. Forthcoming. "The Evolution of Income Support in Recent Decades." in Robert Haveman and Sheldon Danziger, eds. Understanding Poverty: Progress and Policy Prospects. Cambridge, MA: Harvard University Press.
- Swedish Economic Policy Review*. (1998). Special issue on the Welfare State, ed. Jonas Agell and Anders Björklund. Vol. 5, no. 1, Spring.

U.S. Department of Health and Human Services, Administration for Children and Families.
(1996). "State Welfare Demonstrations." HHS Fact Sheet, August 22, Washington, D.C.
[<http://www.acf.dhhs.gov/programs/opa/facts/stdemo1.htm>] (3 Feb. 1998)

Wiseman, Michael, 1997, "Welfare Reform in the United States: A Background Paper." Institute
for Research on Poverty, Special Report no. 70, University of Wisconsin–Madison.

Wiseman, Michael, 1999, "In Midst of Reform: Wisconsin in 1997," Assessing the New
Federalism Working Paper 99-03, The Urban Institute, June

Table 1: Earned Income Tax Credit Parameters, 1979-1999 (in nominal dollars)					
Year	Phase-in Rate (%)	Phase-in Range	Maximum Credit	Phase-out Rate (%)	Phase-out Range
1975-78	10.0	\$0-\$4,000	\$400	10.0	\$4,000 - \$8,000
1979-84	10.0	0-5,000	500	12.5	6,000 - 10,000
1985-86	11.0	0-5,000	550	12.22	6,500 - 11,000
1987	14.0	0-6,080	851	10.0	6,920 - 15,432
1988	14.0	0-6,240	874	10.0	9,840 - 18,576
1989	14.0	0-6,500	910	10.0	10,240 - 19,340
1990	14.0	0-6,810	953	10.0	10,730 - 20,264
1991 ^a	16.7 ¹ 17.3 ²	0-7,140	1,192 1,235	11.93 12.36	11,250 - 21,250 11,250 - 21,250
1992 ^a	17.6 ¹ 18.4 ²	0-7,520	1,324 1,384	12.57 13.14	11,840 - 22,370 11,840 - 22,370
1993 ^a	18.5 ¹ 19.5 ²	0-7,750	1,434 1,511	13.21 13.93	12,200 - 23,050 12,200 - 23,050
1994	23.6 ¹ 30.0 ² 7.65 ³	0-7,750 0-8,245 0-4,000	2,038 2,528 306	15.98 17.68 7.65	11,000 - 23,755 11,000 - 25,296 5,000 - 9,000
1995	34.0 ¹ 36.0 ² 7.65 ³	0-6,160 0-8,640 0-4,100	2,094 3,110 314	15.98 20.22 7.65	11,290 - 24,396 11,290 - 26,673 5,130 - 9,230
1996	34.0 ¹ 40.0 ² 7.65 ³	0-6,330 0-8,890 0-4,220	2,152 3,556 323	15.98 21.06 7.65	11,610 - 25,078 11,610 - 28,495 5,280 - 9,500
1997	34.0 ¹ 40.0 ² 7.65 ³	0-6,500 0-9,140 0-4,340	2,210 3,656 332	15.98 21.06 7.65	11,930 - 25,750 11,930 - 29,290 5,430 - 9,770
1998	34.0 ¹ 40.0 ² 7.65 ³	0-6,680 0-9,390 0-4,460	2,271 3,756 341	15.98 21.06 7.65	12,260 - 26,473 12,260 - 30,095 5,570 - 10,030
1999	34.0 ¹ 40.0 ² 7.65 ³	0-6,800 0-9,540 0-4,530	2,312 3,816 347	15.98 21.06 7.65	12,460 - 26,928 12,460 - 30,580 5,670 - 10,200

Source: 1998 Green Book, Committee on Ways and Means, U.S. House of Representatives, U.S. Government Printing Office, page 867. 1998 and 1999 parameters come from Publication 596, Internal Revenue Service

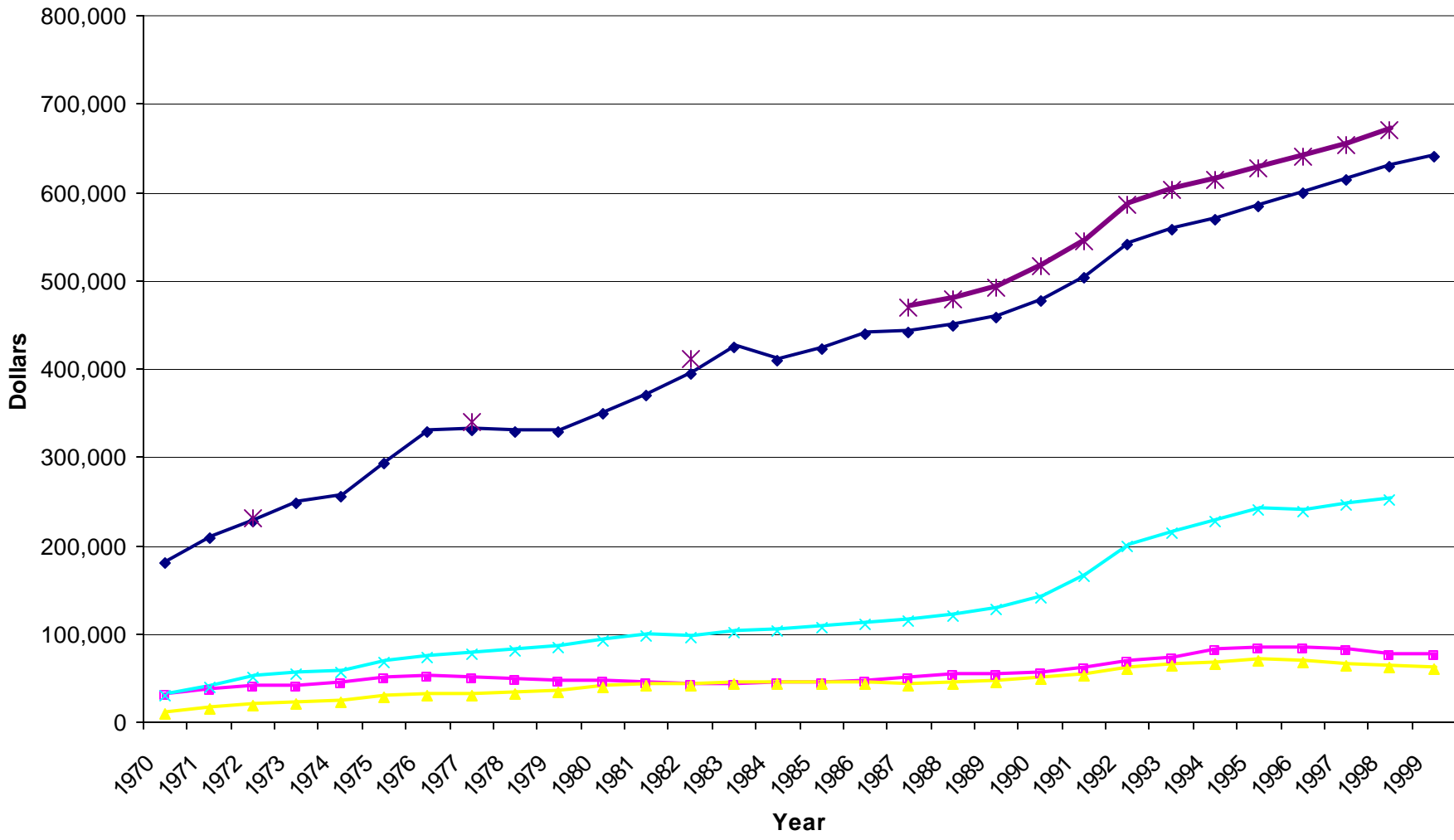
^a Basic credit only. Does not include supplemental young child or health insurance credits.

¹ Taxpayers with one qualifying child.

⁴² Taxpayers with more than one qualifying child.

³ Childless taxpayers.

Figure 1: Total Social Insurance, Cash and In-Kind Means-Tested Transfers (1999 dollars)



◆ Social Insurance w/o WC
 ■ Cash Transfers
 ▲ In Kind, no Medicaid
 × In Kind, w/ Medicaid
 ✱ Social Insurance w/ WC

**Figure 2: Public Attitudes on Welfare and Assistance to the Poor:
GSS Data (no survey in 79, 81, 92 and 95)**

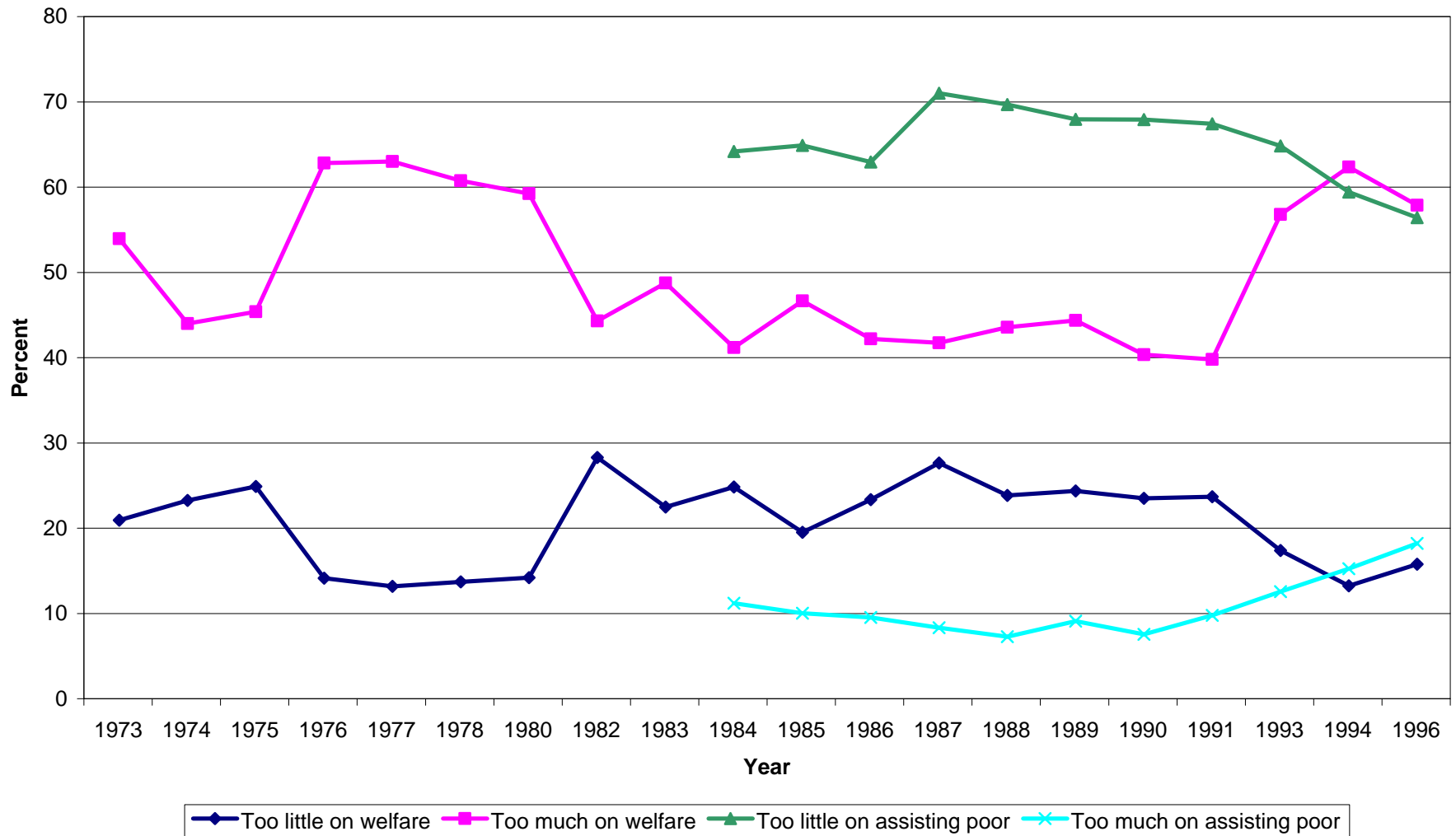


Figure 3: Child, Elderly and Aggregate Poverty Rates, 1959-1998

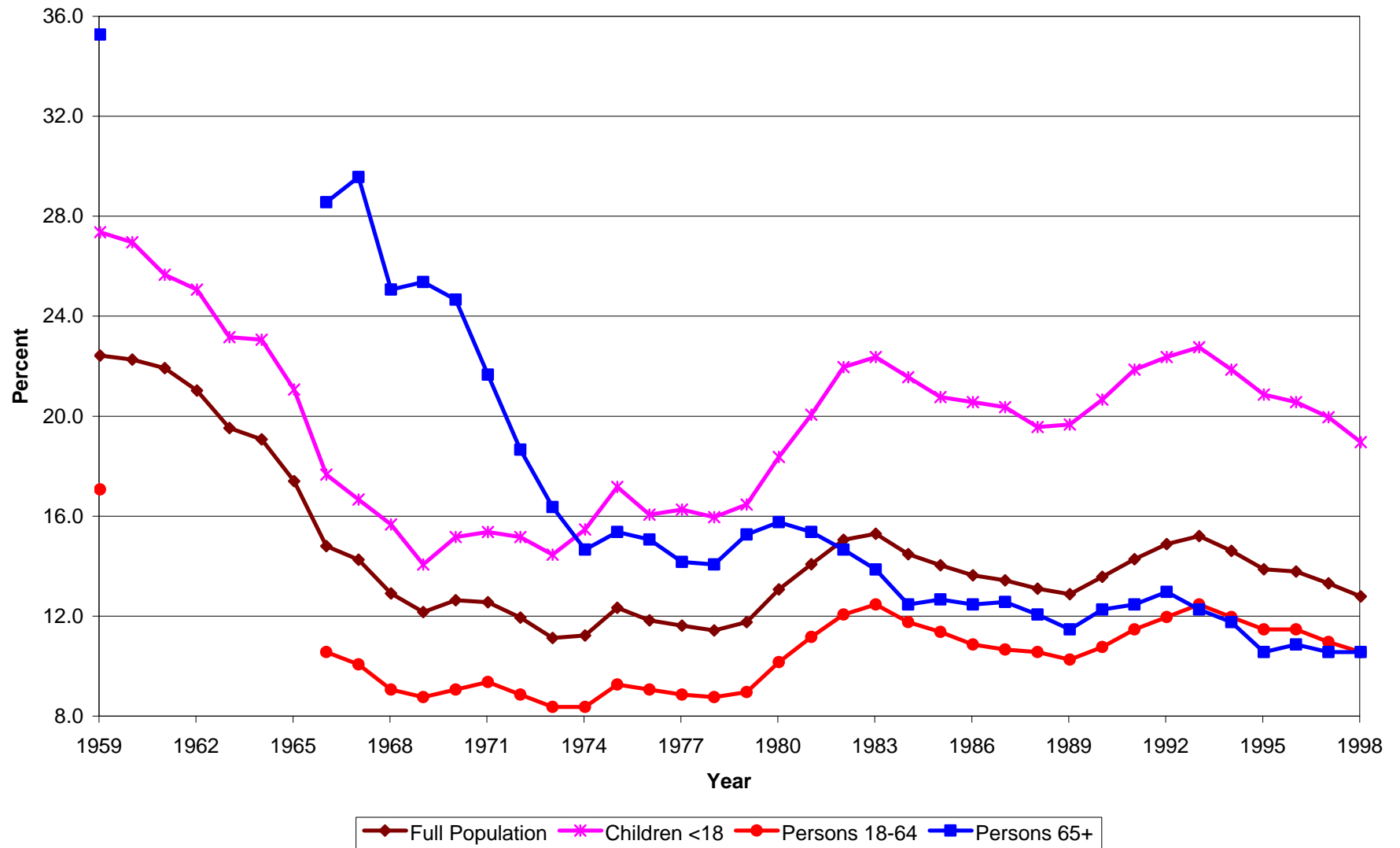


Figure 4: Percent of children in single-parent families, 1960-98

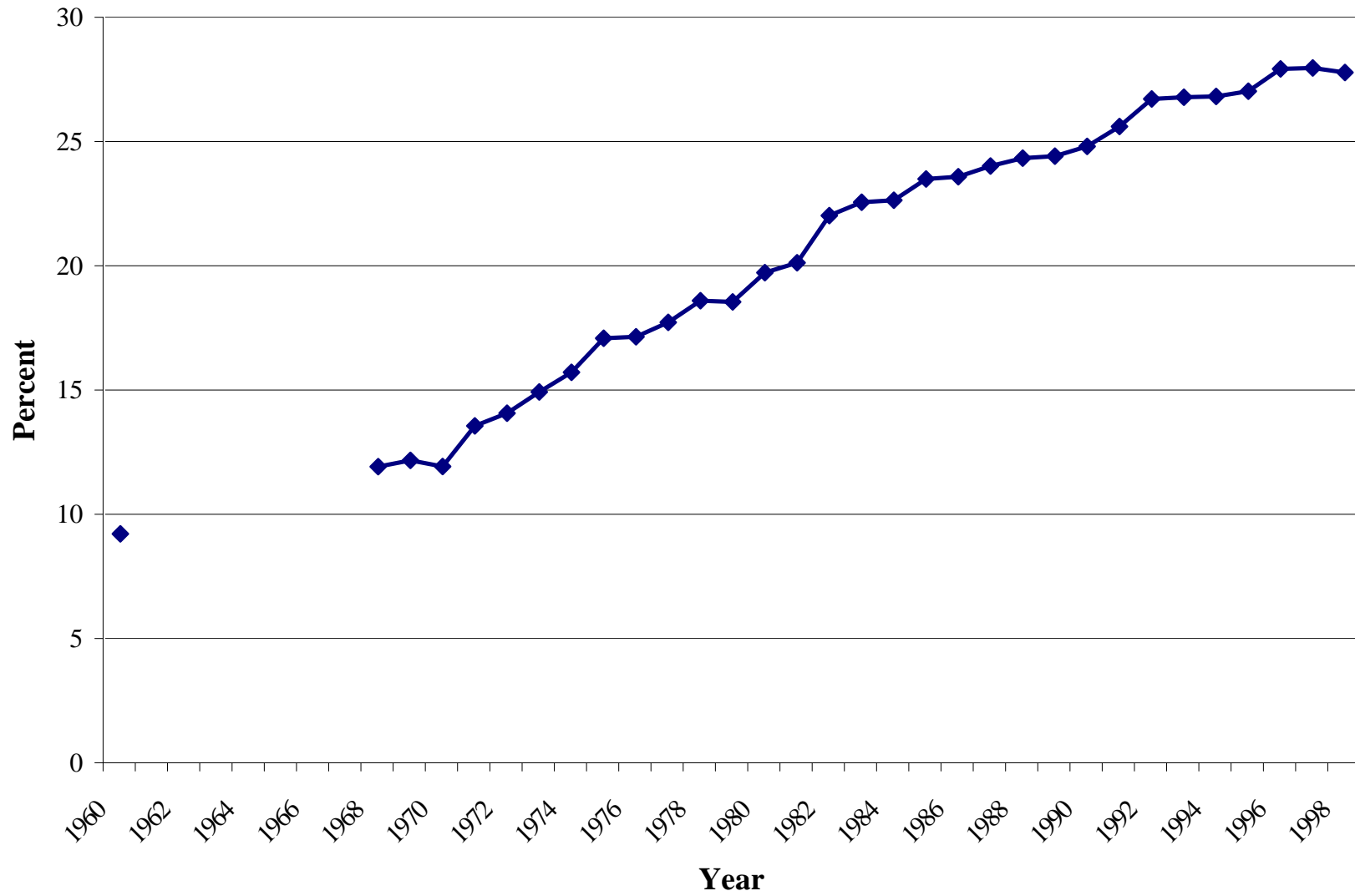
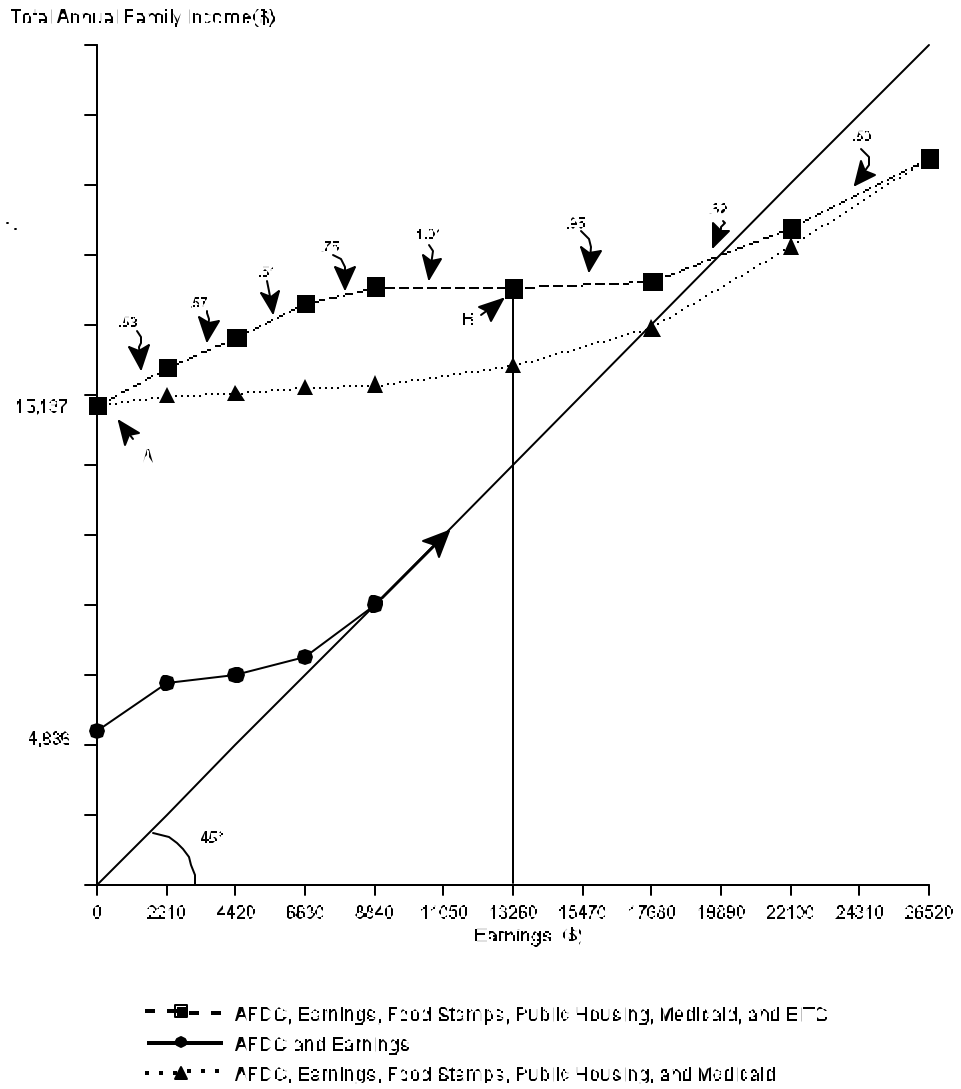


FIGURE 5
 Annual Income-Earnings Relationship Facing a Typical Family on AFDC as They Shift into the Labor Force



Source: DiMarcello and Steuerele, 1996, Table I.