

THE RECENT DEBATE OVER WELFARE REFORM, which is sure to continue in the next Congress, is far reaching and complex. I have chosen to focus on the relationship between government assistance to the needy and the low wage labor market. This focus addresses the heart of the problem, the fact that we as a country want to find a way to help those in need without undermining the value of work and the idea that we are each responsible for ourselves. The current system does not achieve this difficult goal, but there are ways that government assistance could be changed to make it more compatible with our goals for society as a whole.

The work-related aspects of welfare reform clearly display some of the mixed feelings that the public has toward welfare and welfare recipients. Most Americans seem to have genuine compassion for those in need, but they also seem to feel strongly that anyone who can, should work for what they get. Thus the general notion that welfare causes erosion of the work ethic is very troubling, and should be a primary concern of new reform efforts. The primary program that is being considered for reform is Aid to Families with Dependent Children (AFDC), however

there are other programs that fall under the heading of welfare and are as important as AFDC. The two most important of these are food stamps and Medicaid, these two, along with AFDC, will be hereafter referred to as welfare.

First, it is important to understand the ways in which welfare may discourage work, and if these effects are significant. The most basic way that welfare may discourage work is that it provides some individuals with the option of choosing not to work and to receive welfare payments instead. While many people on welfare are unable to find work and have little choice, it is undeniable that it is possible for some people to choose to receive welfare rather than work. Other people may continue to work, but work less as a result of the availability of government support. The size of the work disincentive will be partially determined by the size of welfare payments. It is hard to generalize about such payments because they vary greatly by state, however the median combined AFDC and food stamp level of payment is \$7,525 per year, which is less than the \$8,840 that someone could earn working full time at minimum wage (United States Department of Health and Human Service 10).

Another important consideration is the rate that AFDC payments are reduced if a recipient chooses to earn some income. This is referred to as the benefit reduction rate (BRR), and it is currently 100 percent. In other words, if a recipient earns an extra dollar, his or her benefit will be reduced by one dollar, leaving him or her no better off. Food stamp benefits also

decrease as income increases, and eventually Medicaid will be cut off. The combined effects of these three welfare programs is equivalent to a tax rate of over 100%. However, some income is exempted before the BRR takes effect and exact state policies on how to count income vary. Despite these complications, this policy clearly discourages work, however, the magnitude of this effect will depend on many factors and cannot be determined a priori.

A reasonably large amount of work has been done to determine the size of the welfare system's effect on work incentives. There are basically two ways to approach this problem: one can compare data from different time periods, or one can compare modern data from different states. One can look at the overall level of work among female heads of households and compare it to changes in welfare policy over time. Such a comparison

yields mixed results. There was significant variation in benefit levels over the past 30 years, however, the hours of work by female heads of households did not vary considerably, only between 17 and 20 hours per week (Moffitt 7-12). Also there was not an obvious effect on work from changes in the BRR (Moffitt 13).

Welfare, Reform, and the Low-Wage Labor Market

Society hopes to eliminate work disincentives; but because the problem involves much more than the welfare system, so must the solution.

By Eliot Jamison

On the issue of the BRR, the changes in question may not have been large enough to evoke a significant response, especially when one considers that a further "tax" on extra earnings is imposed through the food stamp program. Thus the actual BRR that a recipient faced may have remained near 100 percent even between 1967 and 1981 when it was only 67 percent for AFDC by itself.

The data from the past thirty years is not conclusive in terms of the existence and size of the welfare program's work disincentive. When evidence from inter-state comparisons is added, one finds a real but rather weak work disincentive created by the AFDC program. Different studies have widely varying results; the decrease in estimates of average hours worked by female heads ranges from 1 to 9.8 hours per week (Moffitt 16). If one takes a middle result from this range, one can see that the work income lost from reduced work due to welfare would average approximately \$1000 per year. This is significant, but certainly not enough to lift many families out of poverty. A complete picture of the work disincentive, however, should include the effects of other programs. The food stamp program, by one estimate, is calculated to reduce work by 1 hour per week (Moffitt 18). Medicaid, and health care policy more generally, appears to be important in work and welfare decisions. One study found that the existence of Medicaid only significantly altered the AFDC participation and employment decisions of families with high expected medical expenses, but that it was quite a significant effect for those families (Wolfe and Moffitt 625).

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CLINTON'S REFORM

The existence of perverse incentives in the welfare system is fairly widely acknowledged, and President Clinton's reform proposal attempts to increase greatly work among welfare recipients. One way of doing this is by requiring recipients to find work after two years or face termination of their benefits. It should be noted that this provision will not apply to mothers with infants, people with disabilities, or people caring for disabled children (US Dept. of HHS). This imposed time limit may affect private sector work decisions by welfare recipients by making welfare less "attractive." Nevertheless, as detailed above, welfare policies are not major determinants of female head's work decisions and so requiring work after two years will probably only induce a small number of people to choose work over welfare. If recipients are forced into public sector jobs after two years, the amount they work will obviously increase. However, it is unclear if public sector work programs are as valuable, to the recipient as well as to the country, as private sector jobs. The President's plan also proposes to change the maximum amount of savings that a recipient may have and remain eligible for AFDC. Finally, it gives states increased flexibility to reduce the BRR (US Dept. of HHS). These changes should decrease work disincentives, but again, the empirical evidence suggests that their effects may be limited. Furthermore, the expansion of the Earned Income Tax Credit, which is essentially a negative income tax, should have a positive effect on work incentives by reducing the effective BRR that recipients face.

Perhaps part of the reason for lack of work among welfare recipients is that given the skills they possess there is not enough demand for their labor at prevailing wage rates. This possibility is supported by the success of some job training programs around the country. One of the most successful is the GAIN program in Riverside County, California. If this is an important part of the reason for lack of work, then the President's proposed increase in funding for job training programs and new participation requirements may be helpful.

Problems with Clinton's proposal

The President's reform plan will likely have a modest but positive impact on welfare recipients' private sector work decisions. Despite the efforts to correct

past perverse incentives, there may be new undesirable incentives in the President's plan. The first set of such incentives that would be created would come from changes that make welfare more attractive. Welfare, under the President's reforms, will offer free education and job training as well as assistance in job searches. These services could be quite valuable to people with relatively low skills who are hoping to improve their skills in order to obtain work. So, while it is unlikely that someone with a good job is going to quit and go on wel-

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fare just to get some extra training, it is possible that someone who is just on the margin between receiving and not receiving welfare will be more likely to opt for welfare if its benefits are greater. This would not be entirely bad; it would provide useful skills to those who need them. However, if the government's goal is to provide job training for those who could benefit from it, it is inefficient to provide such training through the welfare system.

Also, there is the possibility that subsidies to private employers to hire welfare recipients, which President Clinton has proposed as one way to create more jobs for welfare recipients (US Dept. of HHS), could adversely affect others in the low-wage labor market. For instance, it will be cheaper for an employer to hire a welfare recipient than someone who is not receiving welfare. This could increase unemployment among low-wage non-recipients; it possibly would force them onto public assistance and begin a process whereby, in the extreme case, a large percentage of low wage workers are circulated through the welfare system in order for employers to receive subsidies.

The President's proposal includes specific language that forbids such practices by employers (US Dept. of HHS). However, it is hard to imagine how such rules could be enforced. Presumably,

employers will not be able to fire a current employee and immediately hire a welfare recipient at a subsidized wage; but less blatant practices could be feasible. For example, if a firm is planning to hire a new worker and it decides to hire a recipient rather than a non-recipient, the non-recipient will be hurt and the government will probably be unable to prevent it. It would be impossible to determine if a firm would have hired a non-recipient if the subsidy had not been in place, or if the firm would not have hired anyone. Government efforts to enforce proper use of subsidies would probably be expensive and would be unlikely to be successful.

The new perverse incentives created by President Clinton's proposal, for the most part, involve the creation of discrepancies in the treatment of low-wage workers who are on welfare as compared to those who are not. The most straightforward remedy to this is to implement various reforms in the entire low-wage labor market as opposed to just the welfare system. Specifically, government subsidized job training could be made available outside the welfare system, both to those who do and those who do not need income support.

Furthermore, the idea of government support to encourage creation of jobs for those with only marginal skills is a good idea, but it should not be done through the welfare system. The government could offer to supplement the wages of all workers whose wages from their employers were below a certain level. This reform needs to be coupled with elimination of the minimum wage in order to allow employers to hire even workers whose skills are so limited as to not be worth even \$4.25 per hour, possibly a quite large group. This reform could be done through further expansion of the Earned Income Tax Credit, a popular program, and federal legislation banning minimum wage laws. Admittedly, this new tax credit could be expensive, but partial funding could come from using the money that would otherwise go to administering public jobs under the President's reform plan.

In addition, the flexibility granted to states could be increased more than envisioned in the President's proposal in order to encourage experimentation. Specifically, states could be encouraged to experiment with wide ranges of minimum guaranteed incomes and BRRs. If states were free to implement quite different welfare systems, we could learn a

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lot more about what is and is not effective. Another possible reform is to split AFDC into two separate programs based on recipients' ability to work. One program would be aimed at those recipients whom society does not expect to work, such as disabled recipients and mothers with very young children. This program could simply consist of providing enough money for the family to live decently. The program would not have to concern itself with work incentives because its recipients would be explicitly not expected work, and this would make this program simpler and less expensive to administer. The other program, for those who would be expected to work, could be designed along the lines of the President's proposal or the reforms suggested above.

Finally, the President's emphasis on health care reform as being necessary for welfare reform is entirely correct. It is very plausible and understandable that a

young mother would hesitate to accept a job that had no medical benefits if she would lose Medicaid and possibly have no way to pay for health care for her children. It has been estimated that providing health insurance with benefits as generous as Medicaid to all working female heads of households would result in an AFDC caseload 25 percent smaller and 18 percent higher employment probabilities for female heads of households (Wolfe and Moffitt 625). Thus, it is clear that universal coverage in our health care system is essential to increasing work among welfare recipients.

It now appears that President Clinton may have to proceed with welfare reform without a plan passed to provide universal health coverage. Despite this limitation, there is the potential for much progress in improving assistance to the needy. Hopefully the final proposal that comes out of congress will look at the low-wage labor market as a whole,

rather than just focusing on welfare recipients. IS

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Barry Goldwater on Hubert Humphrey:

He talks so fast that listening to him is like trying to read "Playboy" magazine with your wife turning the pages.