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Welfare Reform in the United States

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Abstract

This paper reviews the structure and trends of the U.S. welfare system and the U.S. Administration's reform proposals. It shows that, despite the attention the program receives, the welfare program is actually quite small and has experienced moderate rates of growth. However, the system does face serious problems. In particular, its structure sets up strong financial disincentives to paid employment and saving at the same time that its low level of benefits fails to lift low-income children and their families out of poverty.

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Summary

The U.S. Administration has called for reform of the welfare system and last year introduced the Work and Responsibility Act of 1994. This paper, which reviews the structure and trends of the U.S. welfare system and the reform proposals, shows that the welfare program, despite the attention that it receives, is actually quite small. Spending on welfare represents just 1 percent of the federal budget and 2 percent of state budgets and has experienced only moderate rates of growth. Excluding the effects of the recent recession, virtually all of the increase in expenditure in the past decade was due to general inflation. An increase in the number of recipients was in line with growth in the general population and was offset by a decline in real benefits.

Moreover, the paper finds that few recipients become "trapped" in the system. Most recipients use welfare as a means of temporary assistance--not as a permanent alternative to employment--and leave welfare within two years. However, the system does face serious problems. In particular, its structure sets up strong financial disincentives to paid employment and saving at the same time that its low level of benefits fails to lift low-income children and their families out of poverty.

I. Introduction

The U.S. Administration has called for reform of the welfare system and last year introduced the Work and Responsibility Act of 1994. This paper reviews the structure and trends of the U.S. welfare system and the reform proposals. It shows that, despite the attention the program receives, the welfare program is actually quite small. Spending on welfare represents just 1 percent of the federal budget and 2 percent of state budgets and has experienced moderate rates of growth. Excluding the effects of the recent recession, virtually all of the increase in expenditure in the last decade was due to general inflation. An increase in the number of recipients was in line with growth in the general population and was offset by a decline in real benefits. Moreover, few recipients become "trapped" in the system. Most recipients use welfare as a means of temporary assistance, not as a permanent alternative to employment, and leave welfare within two years. However, the system does face serious problems. In particular, its structure sets up strong financial disincentives to paid employment and saving at the same time that its low level of benefits fails to lift low-income children and their families out of poverty.

II. The U.S. Welfare System

1. Aid to Families with Dependent Children

The main welfare program in the United States and the focus of the current welfare reform debate is Aid to Families With Dependent Children (AFDC), a joint federal-state program which is the major source of cash assistance to low-income children and their families. Recipient families typically also receive support in the form of food stamps, health insurance through Medicaid, subsidized day care, and housing assistance. The system of benefits is fragmented, and eligibility requirements and the federal-state division of administrative and financial responsibilities differ across these programs.

The AFDC program originally was created in 1935 in part to provide financial assistance to fatherless families so that mothers could devote full time to raising their children. Those eligible for the program continue to be needy children (and certain members of their household) who have been deprived of parental support or care because their father or mother is absent from the home continuously, is incapacitated, is deceased, or is unemployed. 1/ In recent years, efforts have been made to redesign AFDC and tighten eligibility requirements in order to encourage adult recipients to search for and accept paid employment. The current welfare reform debate follows in this trend.

1/ U.S. House of Representatives (1993), p. 615.

2. Expenditure at the federal and state levels

The AFDC program is administered by the states within broad federal guidelines and financed jointly by the federal and state governments. States set their own benefit levels and establish limits on income and other resources. The federal government pays from 50 percent to 80 percent (55 percent on average) of benefit costs in a state depending on state income, and 50 percent of administrative costs. The AFDC program itself represents a small share of the federal and state budgets (see tabulation below). In 1992, the federal government provided 54 percent of total AFDC expenditure, representing just under 1 percent of the federal budget. 1/ The states financed the remainder, representing about 2 percent of their budgets.

AFDC Expenditure 2/

(In billions of dollars, unless otherwise noted)

	1970	1975	1980	1985	1988	1990	1991	1992
Total expenditure	4.8	9.2	13.0	16.4	19.0	21.2	23.0	24.9
Federal	2.8	5.2	7.2	8.7	10.3	11.5	12.5	13.6
Percent of total	57.0	56.1	55.3	53.2	54.3	54.3	54.3	54.4
Percent of federal budget	1.3	1.4	1.2	0.9	0.9	0.9	0.9	0.9
State	2.1	4.1	5.8	7.7	8.7	9.7	10.5	11.4
Percent of total	43.0	43.9	44.7	46.8	45.7	45.7	45.7	45.6
Percent of state budgets	3.2	3.6	3.0	2.5	2.3	2.2	2.1	2.2

3. Welfare caseload and benefits

In 1992, 4.8 million families (13.6 million persons) received benefits under the AFDC program (see tabulation below). AFDC recipients represented just under 5 percent of the total population in that year (compared with a 20-year average of 4.7 percent) and represented less than one half of the pre-welfare poverty population. 3/ In 1992 two thirds of the total AFDC caseload were children, a share that has been relatively stable since 1980 when, following trends in the general population, the average family size declined to 3 persons (from 4 in 1970). However, although the AFDC program is targeted at poor children, only 60 percent of children in the pre-welfare

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1/ An additional 6 percent of the budget is devoted to other income support and related programs, such as housing assistance, food and nutrition assistance, and the Supplemental Security Income (SSI) program which provides cash payments to low-income aged, blind, and disabled persons.

2/ Sources: U.S. House of Representatives (1993); Survey of Current Business; Tax Foundation (1993); and staff estimates.

3/ The number of families on AFDC rose in 1993, but projections by the Department of Health and Human Services show the number of families on AFDC falling during 1994-95 as the effect of the economic downturn dissipates. Subsequently, the number of recipients is projected to increase at about the rate of population growth.

poverty population received benefits under the program. Those children who did receive benefits represented about 13 percent of the total child population, reflecting the higher percentage of children who are poor (22 percent in 1991) compared to the share of the general population which is poor (14 percent).

AFDC Caseload and Benefits 1/

	1970	1975	1980	1985	1988	1990	1991	1992
Annual average (thousands)								
Families	1,909	3,269	3,574	3,692	3,748	3,974	4,375	4,769
Recipients	7,429	11,067	10,597	10,813	10,920	11,460	12,596	13,626
Children	5,494	7,821	7,220	7,165	7,326	7,755	8,515	9,225
Percent of recipients	74.0	70.7	68.1	66.3	67.1	67.7	67.6	67.7
Average family size	4.0	3.2	3.0	3.0	3.0	2.9	2.9	2.9
Average monthly benefit per family								
In current dollars	178	208	269	329	370	389	388	388
In 1992 dollars	644	542	458	429	439	417	399	388
Percent of poverty threshold income	53.8	58.1	49.2	46.1	47.1	44.8	42.9	43.4

The vast majority of adult AFDC recipients are women caring for children. Of the total number of eligible children in 1991, 11 percent had both parents present, but one parent was incapacitated or unemployed. Most of the remaining children were eligible for AFDC because a parent was absent from the home (33 percent because of divorce or separation and 53 percent because of lack of a marriage tie). Most eligible mothers are in their 20s or 30s (80 percent) and have 1 or 2 children (72 percent). About half of adult recipients have graduated from high school and about 10 percent also have some college education. In 1991, 38 percent of welfare recipients were non-Hispanic white, 39 percent were black, and 17 percent were Hispanic. 2/ Most lived in metropolitan areas, with about half of all recipients living in six large, highly urbanized states: California, New York, Illinois, Ohio, Michigan, and Pennsylvania. 3/

Contrary to a commonly-held view, only a small share of AFDC recipients remain on welfare continuously for long periods of time. 4/ Half of all spells on welfare last two years or less and only 14 percent last 10 years or more. 5/ However, of those who leave welfare, one quarter return within two years and one third return eventually. When return spells are taken into account, the percentage of recipients that will be on welfare for two years or less declines to 37 percent and the percentage that will be on

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1/ Source: U.S. House of Representatives (1993), p. 616.

2/ U.S. House of Representatives (1993), pp. 696-697 and DeParle (1994), p. E4.

3/ Bane and Ellwood (1994), pp. x-xi.

4/ Bane and Ellwood (1994), pp. 28-66.

5/ Analyses using monthly rather than annual data show that 70 percent of all welfare recipients leave within two years.

welfare for ten or more years rises to 25 percent. In general, the analysis of welfare dynamics shows that most recipients use welfare not as a permanent alternative to paid employment, but as a means of temporary assistance during times of economic difficulty. 1/

The average monthly benefit per family in 1992 was $388 ($4,656 a year), representing 43 percent of the poverty threshold for a family of three. In real terms, these benefits have fallen 40 percent since 1970. The decline is less pronounced, but still substantial, when combined AFDC-food stamp benefits are considered, as food stamp benefits have been adjusted for food price inflation in almost all years. Between 1972 and 1992, the maximum level of these combined benefits offered by the median state declined by 26 percent in real terms. 2/

4. Shortcomings of the current welfare system

Whether viewed as a longer-term income support program or as a transitional program geared to encouraging paid employment, the current welfare system in the United States suffers from some serious shortcomings. The cash benefits paid under the AFDC program, even when combined with food stamp benefits, do not lift low-income children and their families out of poverty. At the same time, the program is structured in a way that sets up strong financial disincentives to paid employment and saving.

As a means of income support, AFDC benefits fall far short of the poverty line (as noted above) and vary widely across states. The poverty threshold set by the Bureau of the Census in 1992 was an annual income of $11,187 for a family of three. 3/ Only a few states provide AFDC benefits which, combined with food stamps, would bring a family of three close to the poverty line. In January 1993, the median state paid $367 (39 percent of the poverty line) in monthly AFDC benefits and $652 (70 percent of the poverty line) in combined AFDC and food stamp benefits. Moreover, AFDC benefits can vary by more than a factor of five across states. At the low end, a family of three in Mississippi received $120 (13 percent of the poverty line) in monthly AFDC benefits and $412 (44 percent of the poverty line) in combined benefits. At the other extreme, a family of three in Connecticut received $680 a month (73 percent of the poverty line) in AFDC and $866 (93 percent of the poverty line) in combined benefits.

1/ Because recipients who experience longer spells tend to accumulate in the system, the dynamics of welfare look quite different if one looks at expected total spell duration for the welfare caseload at a point in time. According to the authors' estimates, less than 15 percent of all current recipients will be on welfare for two years or less and 48 percent will be on welfare for ten years or more (Bane and Ellwood (1994), p. 29).

2/ U.S. House of Representatives (1993), p. 665.

3/ Alaska and Hawaii are excluded from the following discussion since their poverty lines are set 25 percent and 15 percent higher, respectively, than that for the continental United States.

It might be expected that this low level of benefits would create strong economic incentives to work. However, the eligibility requirements and administrative rules and practices of AFDC create a number of equally strong disincentives to work and save. In particular, although AFDC recipients are permitted to earn up to a specified amount before benefits are reduced ($120 a month plus some child care costs), benefits are reduced dollar for dollar against earned income once these "income disregards" are reached. Eligibility is also determined by the value of the family's assets, with upper limits set at $1,500 for the value of a car and $1,000 in savings. These low limits on savings increase the likelihood that those who leave welfare will return at the first interruption in their flow of earnings.

Another factor discouraging work is the eligibility-compliance culture that characterizes the current welfare system. 1/ The focus of welfare agencies is determining eligibility for benefits rather than encouraging job-search or training. The Family Support Act of 1988 caused some shift in emphasis, but the job training program it introduced was implemented on a limited scale because of underfunding (see further discussion below). Moreover, those who work while still eligible for welfare face burdensome reporting requirements and they are considered by caseworkers to be problem cases if their earnings vary over time, for example because of part-time employment. 2/

An additional important disincentive to seeking paid employment is the loss of health care coverage through the Medicaid program that results from leaving welfare. Most welfare recipients have few skills and accept low-paying jobs that do not offer private health insurance coverage. Since 1990, states have been required to offer transitional Medicaid coverage for 12 months to persons who leave AFDC assistance because of an increase in earnings. Notwithstanding this transitional coverage, the loss of health insurance is estimated to cause up to 25 percent of welfare recipients to remain on AFDC and may also contribute to the high percentage of recipients who return to welfare once they leave. 3/ The loss of subsidized child care after a one-year transition introduces similar financial disincentives to those trying to leave welfare.

1/ Bane and Ellwood (1994), pp. 1-7.
2/ Bane and Ellwood (1994), p. 6.
3/ Council of Economic Advisors (1994), pp. 134 and 165-66.

Earnings and Benefits for a Mother with
Two Children with Daycare Expenses after Four Months
on Job (January 1993) (Pennsylvania) 1/

Earnings	EITC	AFDC	Food Stamps	Medicaid	Taxes: Social Security	Taxes: Federal Income	Taxes: State Income	Work Expenses	Disposable Income
--	--	5,052	2,445	Yes	--	--	--	--	7,497
2,000	390	4,892	2,133	Yes	153	--	--	600	8,662
4,000	780	3,292	2,253	Yes	306	--	--	1,200	8,819
5,000	975	2,492	2,313	Yes	383	--	--	1,500	8,897
6,000	1,170	1,692	2,373	Yes	459	--	--	1,800	8,976
7,000	1,365	892	2,433	Yes	536	--	--	2,100	9,054
8,000	1,511	--	2,521	Yes	612	--	--	2,400	9,020
9,000	1,511	--	2,341	Yes	689	--	--	2,700	9,463
10,000	1,511	--	2,161	No	765	--	--	3,000	9,907
15,000	1,121	--	1,261	No	1,148	--	112	4,200	11,922
20,000	424	--	--	No	1,530	125	252	5,200	13,317
30,000	--	--	--	No	2,295	1,785	532	5,400	19,988
50,000	--	--	--	No	3,825	5,812	1,092	5,400	33,871

The tabulation above illustrates these financial disincentives for persons leaving welfare for work. It shows the effect of increased earnings on disposable income (net of child care and other work expenses), once taxes, the phasing out of the Earned Income Tax Credit (EITC), 2/ and reductions in AFDC and food stamp benefits are taken into account. Throughout the range of earnings between $4,000 and $8,000, effective marginal tax rates approach 100 percent. 3/ The effective marginal tax rate slightly exceeds 100 percent at the point when the person would leave the welfare rolls (i.e. at earnings of $8,000 when AFDC benefits would fall to zero). Chart 1 shows that disposable income changes relatively little over a wide range of earnings.

A final problem with the design of the AFDC program is that it penalizes two-parent families by imposing additional eligibility requirements. The AFDC-UP program, which is designed to assist two-parent families, requires that the principal wage earner be unemployed and have worked at least 6 of the last 13 quarters. In part because of these restrictions, the AFDC-UP program is relatively small--only 7 percent of AFDC families in 1992 were participants in this program.

Some have argued that these additional eligibility requirements for the AFDC-UP program discourage the formation of two-parent families. In the

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1/ Source: U.S. House of Representatives (1993), p. 647. The calculations of AFDC benefits assume that benefits are reduced in proportion to earnings increases after disregarding the following: $120 a month, plus child care costs equal to 20 percent of earnings (up to a maximum of $350 a month for two children). For purposes of calculating disposable income, work expenses are the sum of child care costs and 10 percent of earnings (up to a maximum of $100 a month).

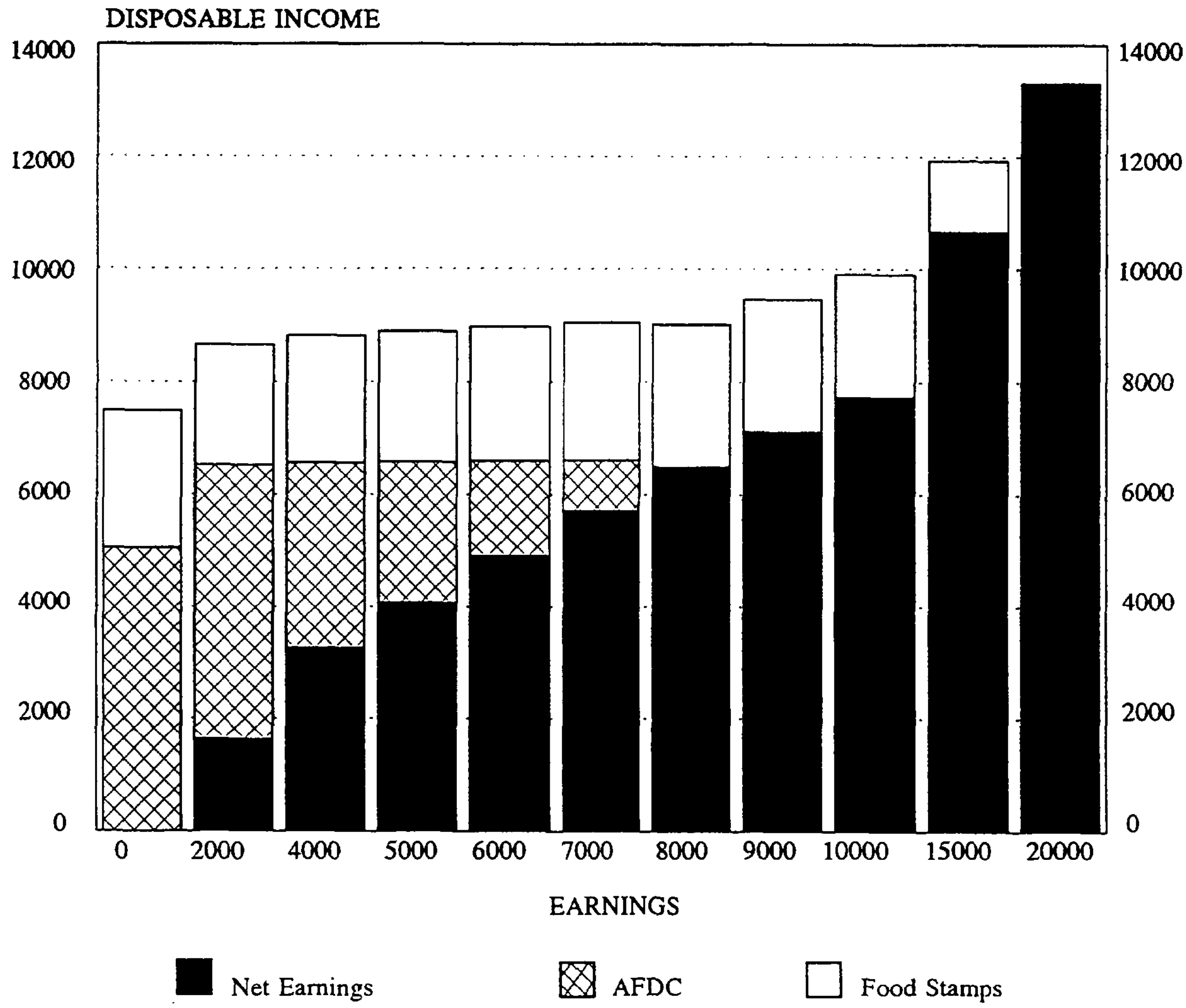
2/ The EITC is a refundable tax credit to low-income families with children.

3/ For comparison, a full-time job at the minimum wage ($4.25 an hour) would pay $8,840 a year.

Chart 1

UNITED STATES

Disposable Income at Various Earnings Levels for a Family of Three Receiving AFDC



Source: U.S. House of Representatives (1993), p. 648.

same vein, some argue that in general AFDC influences family structure by encouraging recipients to have additional children since benefits increase with family size. However, this view and the reform proposals (family caps) that derive from it are difficult to justify. The average AFDC family has the same number of children as the rest of the population. Moreover, as of early 1993, the median state provided approximately $65 in additional monthly benefits ($2.15 a day) for an additional child, far short of the costs of raising a child. 1/ On an annual basis, this increase in benefits of $780 compares to the tax deduction received by taxpayers of $2,350 per child.

III. The Administration's Proposals for Reform

The Administration's proposals for reforming the welfare system contain four main elements: (1) replacing welfare with transitional assistance and work through an expansion of the federal Job Opportunities and Basic Skills (JOBS) training program, followed by a mandatory employment program at the end of two years (WORK program); (2) supporting working families through an expansion of the EITC, health care reform, and increased child care subsidies; (3) promoting parental responsibility and preventing teen pregnancy, in particular through child support enforcement; and (4) changing administrative rules with a view to improving work and saving incentives and achieving greater coordination with other benefit programs.

1. Training and employment

The Administration's welfare reform plan builds on the initiatives under the Family Support Act of 1988 (FSA) to shift the focus of welfare offices away from determining eligibility and compliance toward encouraging paid employment. The JOBS program created by the FSA is generally viewed as a significant step in this direction, but it is insufficiently funded. Under the FSA, all states were required to establish JOBS programs, which include education, training and job placement, and supportive services such as child care. However, participation rates have fallen short of expectations largely on account of state budgetary constraints (which have limited the availability of the required state matching funds). In 1992, states claimed only two-thirds of $1 billion in federal funds and only 10 states drew their full allocation. 2/ As a result, only 7 percent of all adult AFDC recipients were participating in JOBS programs.

The Administration would expand the current program through increases in funding (to $1.5 billion in FY 1996 from $1 billion currently) and by raising the federal share of the cost (federal match) to a minimum of 65 percent in FY 1996 and 70 percent in FY 2000, from the current minimum rate of 60 percent. The expanded JOBS program would be closely linked with Job Training Partnership Act (JTPA) programs and other mainstream training

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1/ U.S. House of Representatives (1993), p. 660.
2/ White House (1994b), p. 16.

programs and educational resources, rather than creating an employment training system for welfare recipients alone. 1/

In the Administration's view, enhanced funding for training and education programs will be effective in shifting welfare recipients into paid employment only if it is coupled with time limits on cash assistance. The proposed reform therefore includes a two-year lifetime limit on cash assistance, with deferrals only for those people caring for infants or children with disabilities, or those with disabilities themselves.

Coupled with the time limit on cash assistance will be a new program called WORK, which will provide subsidized private sector jobs and positions with local nonprofit organizations and the public sector--all of which are likely to be at the minimum wage. Both JOBS and WORK will be financed at the federal level as capped entitlements based on expected caseload. Individual WORK assignments will be limited in duration and search for unsubsidized employment will be emphasized in order to prevent long-term stays in the WORK program. In fact, both JOBS and WORK program participants will be required to accept any offer of an unsubsidized job, provided safety standards are met and the family is not made worse off financially if the job is taken. Persons refusing such job offers will not be eligible for a WORK position and the entire family will lose AFDC cash benefits for a period of six months. 2/

The training and employment offered under the proposed expansion of the JOBS program and the proposed WORK program are significantly more expensive than cash benefits under AFDC. In order to limit the cost of these programs as well as the administrative burden on the states, the Administration has proposed a gradual phasing in of the plan. The time limits on cash benefits and required participation in JOBS and WORK initially would only apply to recipients born after 1971 (the youngest third of the projected adult caseload in FY 1996), resulting in a combined five-year cost of $4 billion (see tabulation below). States would have the option of phasing the program in faster.

1/ White House (1994b), p. 12.
2/ White House (1994b), p. 21.

Administration Welfare Reform Plan:
Five-Year Cost

(In billions of dollars)

JOBS (education, training, and job placement)	2.8
WORK slots for those who reach the two-year limit	1.2
Child care for JOBS and WORK participants	2.7
Child care for the working poor	1.5
Child support enforcement	0.6
Teen pregnancy prevention	0.3
Other 1/	1.7
Total cost	10.8
Net savings from reduced caseload and fraud	-1.5
Total net cost	9.3

The Administration projects that 2.4 million adults would be affected by the proposed requirements by FY 2000 (when those born after 1971 would represent one half of the projected adult caseload). Using the results of JOBS programs in various states, the Administration projects that of those, 40 percent would be working or otherwise off welfare; 37 percent would be receiving education, training, and/or job search assistance through the JOBS program; and 23 percent would be deferred or exempted because of illness or because they are caring for an infant or disabled child (see tabulation below). Of those working, many would continue to receive public support: 9 percent of the affected caseload would be combining AFDC benefits with part-time work and 17 percent would be working at subsidized or public sector jobs through the WORK program (requiring about 400,000 subsidized or public sector jobs); 14 percent would be completely off welfare. Part-time workers and participants in the WORK program would receive sufficient AFDC benefits to ensure that they were no worse off than if they were not working.

1/ Includes state option to reduce AFDC-UP eligibility requirements; investments in automation; and incentives to work and save.

Projected Welfare, Work, and Training Status
of Affected Caseload Under Reform

	FY 1997	FY 2000	FY 2004
	(Thousands of persons)		
Affected caseload	1,641	2,376	3,349
Off welfare	45	331	860
Working part-time with partial AFDC benefits	166	222	271
WORK participant	--	394	566
JOBS participant	904	873	965
Deferred or exempted	526	556	777
	(In percent of affected caseload)		
Affected caseload	100	100	100
Off welfare	3	14	25
Working part-time with partial AFDC benefits	10	9	8
WORK participant	--	17	17
JOBS participant	55	37	28
Deferred or exempted	32	23	23
Approximate share of caseload affected by reform requirements	33	50	67

State experimental programs that offer job search assistance, education, and training have shown mixed results both in terms of their ability to increase participants' earnings and reduce welfare outlays. Two large statewide programs that have shown some positive results include California's Greater Avenues for Independence (GAIN) program and Florida's Project Independence. 1/ California's GAIN is a large, relatively comprehensive program that emphasizes job search assistance for those with a high school diploma, and education for those without a diploma or its equivalent. Its cost per participant during 1988-90 was $4,415, compared to a projected $2,220 per JOBS participant in 2004 ($1,375 in 1990 dollars) under the Administration's reform proposal. 2/ Three years into the program, average earnings for the (randomly-selected) experimental group were $636 (25 percent) higher than the average for the control group and average AFDC payments were $331 (8 percent) lower. However, the program had little effect on the welfare caseload: in the last quarter of the three-year

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1/ See MDRC (1994a) and MDRC (1994b).

2/ These calculations are based on the following assumptions: $1.5 billion in federal funding for JOBS; the minimum federal match rate of 70 percent; 965,000 JOBS participants in 2004; and a projected rate of inflation of 3.4 percent during 1995-2004.

period, over half of the experimental group was still on AFDC, only 3 percentage points lower than for the control group.

The first year evaluation of Florida's Project Independence showed smaller effects, but the effects were not significantly different from GAIN's first-year results. 1/ Other state programs have failed to produce any discernible benefits. The Urban Institute's assessment of Washington's Family Independence Program (FIP), which ran from 1988 to 1993, concluded that FIP had no positive impact on employment and average earnings. This failure reflected the inability of the financial incentives offered by FIP to increase participation in education and training programs (which in turn was related to limited funding), the absence of clear guidelines, and an increase in caseload that overburdened the FIP staff. 2/

2. Other aspects of the reform plan

The second element of the Administration's reform plan focuses on improving the conditions of the working poor, both to assist in the movement from welfare to paid employment and to help prevent some persons from going on welfare in the first place. Although not part of the proposed welfare legislation, two important initiatives include the 1993 expansion of the EITC and the proposed reform of the health care system. The expansion of the EITC will more than double the maximum credit when fully phased in (at a cost of $21 billion over 5 years) and will help raise the incomes of families with a full-time worker closer to the poverty line. A reformed health care system with guaranteed universal coverage would provide low-income workers the same health benefits currently received by welfare beneficiaries and therefore further reduce the disincentives to leave welfare for paid employment.

The principal new initiative to help the working poor (as well as welfare recipients) would be an expansion of child care subsidies. Currently, AFDC recipients receive a child care subsidy of $175 a month per child; the plan would require that states supplement this amount. Additional federal funding would cover subsidies for participants in the JOBS and WORK programs at a five-year cost of $2.7 billion. The five-year expenditure for expanded child care for the working poor would be $1.5 billion. Financing constraints caused this measure to be scaled back significantly from the $5 billion need estimated by the Administration's task force on welfare reform. 3/ The plan would also simplify rules specifying the amount of earned income that AFDC recipients can receive before their benefits are reduced and give states the option of setting income disregards at levels above the federal minimum.

The third element of the Administration's proposed reform attempts to encourage parental responsibility by funding teen pregnancy prevention

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1/ Stanfield (1994), p. 112.
2/ Urban Institute (1994), p. 17.
3/ Stepp (1994b), p. E5.

programs, requiring that minor parents live with their parents and attend school, giving states the option of imposing family caps on benefits, and increasing the number and enforcement of child support awards. Approximately $1 billion over five years would be spent in these areas. With regard to child support enforcement, the Administration's proposal cites estimates by the Urban Institute suggesting that potential child support collections are about $48 billion a year. Of that amount, only $20 billion in child support has been awarded by the courts and only $14 billion is actually paid. 1/ The extent to which increased child support collections can assist AFDC recipients may be limited, however; the Urban Institute research shows that 90 percent of uncollected child support is owed by middle- and upper-income fathers. 2/

The final element of the reform proposal focuses on streamlining administration and changing certain eligibility requirements in order to improve incentives to work and save, at a five-year cost of $1.7 billion. In particular, the limit on allowable savings would be increased from $1,000 to $2,000; the limit on the value of a car would be increased from $1,500 to $3,500; and the types of income that would be disregarded in determining AFDC benefits would be expanded somewhat (for example, to include non-recurring lump sum payments) to conform more closely with eligibility rules for the food stamp program. Eligibility rules would be simplified further by permitting states to eliminate the additional eligibility requirements for the AFDC-UP program geared to two-parent families.

3. Financing

About half of the $9.3 billion five-year cost of the reform would be financed by tightening eligibility rules for AFDC, food stamps, and Supplemental Security Income (SSI) for legal immigrants and tightening SSI rules for recipients with drug addictions. State spending for the AFDC emergency assistance program which, among other things, assists homeless families, would be capped, generating an additional $1.6 billion in savings. Another $1.6 billion would be diverted from the Superfund program for toxic waste cleanup by extending the Superfund tax.

1/ White House (1994b), p. 35.
2/ Stepp (1994a), p. C5.

Administration Welfare Reform Plan:
Five-Year Financing

(In billions of dollars)

Tighten eligibility rules for SSI, AFDC, and food stamps for non-citizens and SSI for drug and alcohol-addicted recipients	4.5
Cap state spending in the AFDC Emergency Assistance program	1.6
Income test meal reimbursements to family day care homes	0.5
End agricultural subsidies to farmers with more than $100,000 in non-farm income	0.5
Shift excess savings from corporate Superfund tax	1.6
Deny EITC to non-resident aliens	0.3
Other	0.3
Total financing	9.3

The size of federal financing required for welfare reform is contingent on a number of assumptions: the size of the projected future welfare caseload; the imposition of caps on the number of deferrals from the two-year time limit; the assumed effectiveness of training, education, and job search programs in moving welfare recipients into unsubsidized, private employment; and the availability of state funds to match federal funds. Whether these assumptions are consistent with one another is open to question. In the past, states have not had the matching funds required to use the entire federal allotment and although the minimum federal match rate would be raised under the proposal, almost half of AFDC recipients reside in only six states. If states are able to raise matching funds, there is a question whether the federal financing for JOBS and WORK will be sufficient to meet enrollment demand, particularly given the limited deferrals that will be granted under the reformed program. In particular, given the uncertainties surrounding projected welfare caseloads and the effectiveness of training, education, and job search programs, the demand for subsidized and public sector jobs through WORK may be greater than projected. The current plan minimizes the risk to the federal fiscal finances since both JOBS and WORK are financed as capped entitlements. However, the effects of the reform would also be more limited since those for whom WORK slots are not available would continue to receive cash welfare benefits.

IV. Concluding Remarks

The Administration's proposal to reform the welfare system addresses a number of the shortcomings of the AFDC program, particularly when combined with the 1993 expansion of the EITC and the proposed reform of the health care system that would provide universal health insurance coverage. In particular, the proposal would increase resources devoted to the JOBS program and child care subsidies; raise asset limits and thereby allow welfare recipients to become more self-sufficient; make eligibility rules more transparent and consistent across programs; and attempt to change the culture of welfare offices to one that encourages self-sufficiency. However, the proposal does not address the steady erosion of real benefits over time, the resulting shortfall in benefits compared to a subsistence level of income, or the wide disparity of benefits across states. In addition, benefits continue to be reduced dollar-for-dollar with increases in earned income, producing extremely high effective marginal tax rates as AFDC recipients shift from welfare to work.

Central features of the proposal include mandatory work requirements and a two-year lifetime limit on cash assistance. Allowable exemptions from the mandatory work requirement have been reduced significantly. Under current guidelines, mothers of children under the age of three are exempt. Under the Administration's proposal, the deferral will be limited to mothers of infants under the age of one; for a second child, the deferral will be reduced to 3 months. Within the two-year time limit, the plan would deny benefits under certain circumstances. In particular, states will have the option of denying additional benefits for children born on welfare; and if a WORK participant turns down an offer for an unsubsidized job, the entire family will be denied benefits for six months.

The two-year limit on cash assistance is based on the assumption that education and training programs can successfully move a significant share of welfare recipients into self-sufficient paid employment within that time period. However, California's GAIN Program and Florida's Project Independence, which are considered relatively comprehensive and successful programs, failed to reduce significantly welfare rolls. Moreover, the earnings gains they generated were concentrated among those recipients who were considered "job ready" from the outset or were parents whose youngest child was age six or older. By contrast, the Administration's proposal is targeted to adult recipients in their 20s, the age group that has proved most difficult to employ, and would spend a fraction of the funds allocated to relatively successful training programs.

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