The mirage of welfare reform

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PRESIDENT Carter has promised to submit a welfare-reform package to Congress in the not too distant future. The time seems right. The welfare explosion of the late 1960's has subsided, as have the echoes of anti-welfare hysteria. A new wave of research has dramatically increased our understanding of the current welfare system. As a result, the President's analysts should find it easier to design an intelligent proposal with favorable political prospects. But this is not to say that any drastic "overhaul" of the system is a foregone conclusion. Indeed, that is unlikely—and probably undesirable.

Many critics have charged that the current system is replete with problems, all of them very serious and none of them amenable to a solution, short of total reform. Consider the list of indictments: The welfare system is inequitable; it often pays inadequate benefits; it breaks up families; it places too heavy a financial burden on local governments; it tolerates massive fraud; it intrudes too greatly into recipients' lives; it offers no incentives to work; it bypasses the working poor; it is an inefficient tangle of separate programs. In the face of all these difficulties, it might seem foolish for the President to squander political capital on proposals that only tinker with the status quo.
Yet, upon reflection, tinkering is almost surely what is required, what is actually possible. From a political perspective, the current welfare system is a web of vested interests; any program change will be met by political opposition. If the President’s plans are to receive Congressional approval, he will have to limit opposition by limiting the extent of his reform. And such restraint is also desirable on programmatic grounds. As we shall argue, welfare—as it now exists in some areas and could exist everywhere—is already more “reformed” than most people realize. Most of the remaining gaps in the system can be filled by specific incremental legislation. The result will not resemble the efficient, uniform system that many writers describe. But it is the beginning of welfare wisdom to recognize that such idealized systems cannot be achieved, no matter how ambitious the legislation.

A look at the current scene

The cornerstone of the current welfare system is Aid to Families with Dependent Children (AFDC). AFDC began life as a minor title in the Social Security Act of 1935, with the purpose of extending aid to “children deprived of parental support or care by reason of death, continued absence from home, or physical or mental incapacity of a parent.” There were certain program guidelines, including the restriction of aid to female-headed families and to two-parent families where the father was disabled. But most matters, including payment levels, were left to the states. Congress tried to encourage adequate benefits through its cost-sharing formula, but explicitly refused to mandate minimum benefit levels.

State administration of the federal program continues through the present—creating, in essence, 51 AFDC programs. The state programs differ most markedly in the level of benefits: In 1975, a family of four could receive a maximum of $60 per month in Mississippi, $153 in Georgia, $170 in Florida, $317 in Illinois, $349 in California, and $400 in New York. Depending upon a state’s per-capita income, the federal government picks up between 50 and 83 per cent of these benefit payments, and between 50 and 90 per cent of other administrative costs.

Some of the variation among the states reflects regional differences in the cost of living, but most results from their varying ability and willingness to pay. Federal law requires each state to publish an annual “needs standard,” an estimate of a family’s minimum financial requirements. By these estimates, an AFDC payment for a
family of four in Georgia represents 67 per cent of its "need"; in Florida, 74 per cent; in Ohio, 59 per cent; in Alabama, 60 per cent. In only 21 states do "needs" and payments coincide.

The states have also differed in their responses to federal program reforms. In 1961, Congress passed legislation creating AFDC-U (Aid to Families with Dependent Children—Unemployed Parent). AFDC-U was an attempt to counter the most serious criticism of AFDC: that by denying benefits to families with able-bodied men, AFDC encouraged family disintegration. But as with AFDC, AFDC-U was offered on a federal cost-sharing basis, at a state's option. Today AFDC-U exists in 26 states and the District of Columbia. The remaining 24 states, mostly in the South and Southwest, continue to deny federal welfare benefits to most two-parent families.

In 1967 Congress addressed itself to the charge that AFDC provided a disincentive to work. This criticism, voiced by such economists as Milton Friedman and James Tobin, was based on the way benefits were calculated under AFDC. In each state, an eligible family was entitled to a certain maximum payment according to the number and (in some cases) ages of the family members. This maximum payment was then reduced, supposedly dollar for dollar, by the amount of family earnings. In a world where recipients abhorred charity and would seize any opportunity to work, this formula was sensible enough. But in the economists' world, where one dollar is as good as the next, this arrangement was equivalent to a 100-per-cent tax on earnings: If earnings increased by a dollar, welfare payments would decrease by a dollar, so income would stay the same.

In actuality, this "tax" was both more complicated and more liberal than was popularly supposed. When a state paid maximum benefits below its needs standard, it often allowed a recipient's earnings to fill the gap, with only a fractional reduction in benefits or no reduction at all. Moreover, studies of welfare records by Leonard Hausman and Michael Wiseman now indicate that caseworkers often allowed large, unverified deductions for work expenses, which kept effective tax rates below 60 per cent.

But Congress responded to the popular impression of a 100-per-cent tax by adding the "$30 and one-third" rule to the guidelines for benefit calculation. This rule instructed caseworkers to ignore the first $30 of a recipient's earnings and one third of all additional earnings, when computing benefits. At the margin, an extra dollar of earnings would result in an extra 33 cents of income. Although
clear in the abstract, this rule had different effects in different state systems. Today, the precise relationship between earnings and benefits is calculated according to one of eight different formulas, depending upon the state. In all of them, however, an extra dollar of earnings reduces AFDC payments by significantly less than a dollar.

Not being satisfied with the "disregard" (as it is called) provided by the "$30 and one-third" rule, Congress at the same time added the Work Incentive Program (WIN). As a condition of continued welfare eligibility, WIN currently requires fathers in the AFDC-U program, and mothers and some older children in AFDC families, to register for work with the state employment service and to be engaged in active job search or training programs. WIN began as an administrative nightmare, requiring the cooperation of the Department of Labor and of Health, Education, and Welfare at the federal level, and welfare departments and state employment services at the local level. As a result, the number of placements in either training or jobs grew very slowly at first. WIN was substantially strengthened in 1971 (under the Talmadge amendments to the Social Security Act), and participation among welfare recipients has grown rapidly since.

The recipient explosion

But the intricacies of benefit calculation and work registration are primarily the concern of administrators, social scientists, and a few recipients. To the public at large, the most interesting (and frightening) aspect of AFDC has been the growth of the recipient population. In 1950, AFDC covered 2.2 million people. By 1960, the number had increased to 3.0 million; by 1967, to 5.3 million; by 1971, to 10.6 million. After 1971, growth slowed dramatically, so that today the rolls stand at 11.3 million people. But this still means that one out of every 20 citizens receives AFDC, at an annual total cost of almost $10 billion.

The recipient explosion of 1967-71 was the subject of a good deal of popular writing, offering a variety of explanations. Daniel P. Moynihan attributed part of the increase to a new wave of family breakups among poor blacks. Francis Fox Piven and Richard Cloward saw the explosion as the product of a heightened political consciousness among the poor. According to the Piven-Cloward thesis, large numbers of female-headed families had long been eligible for AFDC, but had refrained from applying because of
the stigma and the bureaucratic humiliation. During the late 1960's, these women, encouraged by legal-aid offices and welfare-rights groups, changed their minds and decided to claim what was legally theirs.

In retrospect, it appears that Piven and Cloward explained the increase better (although the family disintegration to which Moynihan pointed was real enough). Independent calculations by Barbara Boland of the Urban Institute and Dorothy Projector of the Social Security Administration confirm that, as late as 1966, more than one third of female households eligible for AFDC were not receiving benefits. By 1971, this proportion had fallen below one tenth. Meanwhile, AFDC had become a guaranteed income for female-headed households (though not necessarily an adequate one), in the sense that those eligible for benefits received them as a matter of course: They did not regard the program as providing only emergency assistance.

The "big three"

Although AFDC once stood alone in providing broad-scale public assistance, it is now part of a "big three" with Medicaid and food stamps. Food stamps have always served two functions—providing relief to the poor and thus stimulating demand for agricultural products. The program began in 1939 as a supplement to the direct distribution of agricultural commodities. It affected a limited number of people (who were already on relief), and was terminated in 1943. President John Kennedy revived food stamps as a pilot program in 1961 in certain depressed areas, including Appalachia. In 1964, President Lyndon Johnson raised the program to the federal level, but as with AFDC, it continued to be at the option of the states. The federal government specified the maximum benefits a family could receive (i.e., the face value of the stamps), but the counties decided whether to administer the program, and the states set the eligibility criteria.

In 1971, the food-stamp program was liberalized and extended nationwide. Today, a family of four can buy a monthly package of stamps worth $166 in food. Eligibility criteria are uniform across the country, and stamp distribution is mandated in all jurisdictions. The value of the stamp package is recalculated annually to compensate for changes in the price of food. The amount the family pays for these stamps is adjusted for its income, but in no case exceeds 30 per cent of family income. As with AFDC benefits, a
dollar increase in earnings results in less than a dollar reduction in benefits.

With the 1971 changes and the growing participation rates, the food-stamp program has become, in Richard Nathan's phrase, a "mini-negative-income tax." The liberalization of the food-stamp program arrived just in time for the 1973-74 inflation in food prices—33 per cent in two years—which substantially increased the face value of the monthly food-stamp package and the number of families eligible for food stamps. In fiscal year 1970, the program reached 4.3 million people, at an annual federal cost of $550 million. By 1975, the program reached 17.1 million people, at a cost of $4.4 billion. (A third of this expansion resulted from phasing out commodity distribution.) About 80 per cent of the recipients are poor. (If the government were to count the net value of food stamps as income—which it doesn't—the official poverty count would be reduced by one sixth.)

Medicaid was passed by Congress in 1965 as Title 19 of the Social Security Act. Its purpose was to provide medical care to the non-aged poor (the elderly were covered by Medicare), but as with AFDC, most of the specifics of the program were left to the states. Today, every state except Arizona has a Medicaid program of some kind. In 26 states, coverage is restricted to AFDC and AFDC-U recipients. In the remaining states, some coverage is also extended to the medically indigent—families whose income (net of medical expenses) falls below a state-established threshold. The state programs also vary widely in the specific services they will reimburse. Altogether, the state programs serve a total of 25 million recipients, at a cost of $12 billion.

For an AFDC recipient, Medicaid operates in a straightforward fashion. Each month the recipient automatically receives a Medicaid card. If the recipient requires care that is covered by the program, he goes to a doctor or hospital and presents the card in lieu of payment. The doctor then bills a financial intermediary, like Blue Cross, which in turn bills the state government. If the recipient leaves AFDC because of increased earnings, he remains covered by Medicaid for four additional months. After 1965 AFDC became substantially more attractive, because it was tied to Medicaid in this fashion. There is thus reason to believe that Medicaid significantly accelerated the welfare explosion.

For someone not receiving AFDC, or someone who has exhausted post-AFDC Medicaid eligibility, coverage is more problematic. A state may not cover such persons at all. Where they are covered,
eligibility must be established at the time of illness—there is no card provided in advance. In some cases it is possible to establish eligibility by incurring enough medical expenses to force net income below the eligibility threshold, but there may be a problem of paying for services in the meantime. The range of covered services for the medically indigent is often more restricted than the range of services for AFDC recipients in the same state. For all of these reasons, relinquishing Medicaid represents a real loss, and going off welfare poses a real risk.

Beyond the "big three," the federal government aids the poor through a number of secondary programs, including public housing, housing subsidies, free school lunches, legal assistance, scholarships for higher education, day care, and so on. Unlike the "big three," these secondary programs are often funded by fixed budgets that are too limited to serve more than a small fraction of eligible families.

What needs to be reformed?

Where has the system failed? The answer depends on whom you ask. Thoughtful people have been writing about AFDC for a number of years, and they have produced an exhausting and exhaustive catalogue of the system's faults. Nonetheless, some problems are more important than others, and there is general agreement that the new Administration will have to address itself to four major questions.

1. How generous should the system be? Twenty-six states pay a family of four cash benefits equal to less than two thirds of the federal poverty standard—i.e., less than $68 per week. Ten of these states pay a combination of cash benefits and food stamps totalling less than $68 per week. Twenty-four states have no AFDC-U program and thus simply deny federal cash benefits to two-parent households. Where AFDC-U does exist, it has a variety of eligibility restrictions that preclude some portion of the needy from receiving aid. Chief among these is the definition of an unemployed parent as someone who works fewer than 100 hours a month. Under this "100 hours rule," a family with a father who works more than 100 hours a month is ineligible for aid, even if family income falls below the needs standard.

At the same time, some critics—including those sympathetic to the poor—have suggested that benefits in some jurisdictions may be too great. The most direct statement of this problem was made
by Blanche Bernstein, in a study of the New York City welfare system for the Subcommittee on Fiscal Policy, chaired by Congresswoman Martha Griffiths. Bernstein demonstrated how the City's standard benefits—AFDC, Medicaid, food stamps, and free school lunches—produced a package valued at $5,500. Because these benefits were tax-free, they were equivalent in value to a job with a gross annual pay of $7,000—far more than what could be gained from many of the City's low-skilled jobs.

2. What work should be required of recipients? AFDC is regularly criticized as a haven for cheaters and frauds. At times, these charges focus on actual violations of the law, such as nonreporting of income. But more often the claim is that some people on welfare could really work for a living if they had to, but prefer to avail themselves of substantial welfare benefits instead. This issue is complex because it is bound up with all kinds of value judgments. The evidence does show that a female AFDC recipient is more likely to work in a low-benefit state like Florida than in a higher-benefit state like Illinois. But if the work is that of a farm laborer at $1.50 per hour, is it good or bad that she should leave her children for such a job?

Despite these ambiguities, all writers on welfare reform have addressed the question of work, though in two different ways. One group, including almost all economists, advocates financial incentives to encourage welfare recipients to work. Ten years ago, they argued that AFDC discouraged work through the 100-per-cent tax. Today, economists like Henry Aaron argue that the 100-per-cent tax has in fact been recreated through the interaction of several benefit programs. Because a typical AFDC recipient receives food stamps, Medicaid, and perhaps other aid, a dollar of extra earnings can (under the "$30 and one-third" rule) reduce AFDC benefits by 67 cents, increase the cost of food stamps by another eight cents, increase public-housing rent by an additional amount, and so on—leading once again to a situation where a welfare recipient is no better off for having worked. There is a real question as to whether recipients make such marginal calculations, but in the extreme cases disincentives obviously exist. The clearest example, already mentioned, is the loss of Medicaid after leaving AFDC.

Although economists want to encourage work through incentives, a second group of reformers wants to mandate work through direct legislation. This group argues that low tax rates on earnings are weak incentives at best, and that provision of an adequate income is an invitation not to work. To offset that, reformers want to tie
welfare benefits more strictly to work, at least for certain kinds of welfare families. This approach lay behind the 1971 Talmadge amendments that made the "work search" requirements in the WIN program more rigorous.

3. Can the system be administered more efficiently? The question of administrative efficiency has several aspects. One is how well program administrators now do their jobs. Television audiences in New York were recently enraged (though probably not surprised) to see two reporters with hidden cameras bribe a welfare worker to give them benefits for which they were ineligible. This episode came on the heels of revelations concerning massive fraud in the Medicaid program: Doctors and hospitals gave services far in excess of patient needs, and then billed the government for even more services than were delivered.

Another aspect of efficient administration involves the number of programs that now deliver aid. Many economists and government officials believe substantial savings could be achieved if the budgets for AFDC and in-kind programs like food stamps, free school lunches, public housing, and so on were all combined, and the benefits disbursed as cash.

Finally, there is the issue of target efficiency. Every welfare system distributes some money to persons less needy than others. This happens because of the need to preserve work incentives, because of loopholes in program legislation, because of the management failures cited above, or because of fraud. Progress in eliminating these inefficiencies would be beneficial both in terms of distributing the present welfare-benefits "pie" and in terms of the amount of transfers the public will be willing to support in the future.

4. How should the system be financed? The combined cost of food stamps, Medicaid, and AFDC is less than two per cent of GNP. Nonetheless, the distribution of that cost creates heavy fiscal burdens, particularly in some urban areas. The classic case is, of course, New York City, which has a large welfare population and bears about 23 per cent of its welfare costs. By national standards this is quite high; indeed, in only 14 other states do local governments contribute more than one per cent of AFDC and Medicaid costs, and in only four other states does the local contribution exceed 10 per cent. In those few states sharing the New York tradition of local contributions to AFDC and Medicaid, local welfare costs are frequently spread across a county base extending beyond fiscally pressed central cities. There is growing Congressional agreement that program costs should be shifted to higher levels of government.
There are additional issues beyond these four questions. Some critics charge that the current system is too intrusive and that case-workers exercise too much discretionary control over the lives of recipients. Others claim the system is too slow in responding to emergencies. Still others say the system abounds with inequities—the most obvious being the interstate differences in benefits and eligibility, although intrastate inequities exist as well. Congresswoman Griffiths' subcommittee made headlines in 1972 with its survey showing that certain welfare families received benefits from as many as six or seven programs (e.g., legal aid, school lunches, public housing, as well as food stamps and AFDC), while other welfare families in the same city benefited from only one or two. Another technical but important inequity arises from the operation of the "$30 and one-third" rule. For a family to become eligible for AFDC, its income must fall below the needs standard of the state. Only after establishing eligibility does the family qualify for the "$30 and one-third" deduction. With this deduction, the family income can rise above the initial needs standard, although the family continues to qualify for benefits. This creates the peculiar situation whereby two families may have identical current incomes, but one receives additional AFDC benefits (because it established eligibility in an earlier "bad" month) while the other does not.

What are the options?

Clearly, no new program can solve everything, if only because many of the problems have conflicting solutions. It is, for example, hard to imagine any new program that is both tougher on fraud and less intrusive into recipients' lives.

From the perspective of those concerned about fundamental human needs, the greatest failing of the welfare system lies in the inadequate benefits provided many dependents and the incomplete coverage of poor families with children. But it would be naive to assume that the issues of adequacy and coverage can be addressed in isolation. Since 1960, Congress has considered various welfare reforms on five different occasions. Each time, legislators were responding more to public concern over the rising number of recipients and the fiscal consequences of growth in the rolls than to the human suffering caused by Mississippi's $60 monthly benefit.

Recently, welfare reform has been in the news because the National Governors' Conference and Mayor Beame requested fiscal relief. Last fall, candidates on the stump, including the President,
received their most enthusiastic applause when they talked about putting welfare recipients to work and rooting out fraud. In this climate, any liberal welfare reform must be based on exchanging an extension of benefits for a redistribution of costs and/or a toughening of work requirements. Three proposals for such a trade-off now appear to be under consideration.

The first and most widely discussed is a *Negative Income Tax* (NIT), which was first proposed in the 1940’s and 1950’s by several economists, including George Stigler and Milton Friedman. They argued that if society were committed to reducing poverty, the appropriate mechanism was a downward extension of the positive tax system, whereby those with substandard incomes would receive payments from the government—i.e., receive “negative taxes.”

Compared to the AFDC system of that time, NIT offered several advantages. It would be open to all households—two-parent as well as female-headed—and so would not offer incentives for family disintegration. It would also be integrated with the Internal Revenue system. Under NIT, a dollar of earnings would not result in an equal loss of benefits. Work incentives would thus be restored to the welfare system.

Today, the partial acceptance of AFDC-U and the variations of the “$30 and one-third” rule have reduced these advantages. Nevertheless, Paul Samuelson, former HEW official Laurence Lynn, and other economists continue to argue for NIT, for a variety of reasons. They see NIT as a total replacement for all current welfare programs except Medicaid: AFDC, food stamps, housing supplements, and so on would all be abolished in favor of a single uniform cash payment, scaled to family size, with a tax rate on earned income below the current multiple-program rate. The consolidation of programs would reduce administrative costs, while the uniformity of the program would eliminate current inequities and inadequacies. As far as possible, recent advocates want the program run as Stigler and Friedman first conceived it—as an extension of the Internal Revenue Service. This would eliminate intrusive social workers. In exchange for all this, the federal government would assume the total cost of the program.

The second option is a *Two-Track Transfer System*. This term describes a variety of specific proposals, all of which emphasize separating poor families into those whose household heads are employable and those whose household heads are not. Whereas NIT tries to encourage work through a low tax on earnings, two-track options mandate work through threat of benefit withdrawal.
Families without employable heads (families headed by a disabled person, and female-headed families with preschool children) would be put in a program similar to AFDC, with a federally funded minimum benefit. But employable family heads would be given job training coupled with low-level unemployment compensation, tied to a strict work test. If a recipient failed to take a job to which he was referred, the family benefits would be cut off. In some versions, the plan would include public-service employment to provide jobs of last resort to those unable to find work in the private sector.

The two-track work test allows circumvention of the central problem of NIT—what became known five years ago as "McGovern's Dilemma." If NIT is to have a substantial "guarantee" (the payment made to families with no other income) and a low tax rate to promote work, in many cases payments will be made to families having what appear to be astonishingly high incomes. To provide a simple example: A NIT system with a $5,000 base payment, a $100-per-month standard deduction for work expenses, and a 50-per-cent tax rate will cease making payments to families only when earnings exceed $11,200 per year. Although payments to non-poor families may be modest, many such families will receive them, because the number of families with children in the $5,000-to-$12,000 income range exceeds the number of families with children in the less-than-$5,000 range by 150 per cent. By contrast, a two-track system is free to impose high tax rates to insure target efficiency, even with a high guarantee, at the same time that the work incentive is preserved administratively, through the work test.

The proposals for two-track systems also include reform of the Unemployment Insurance Benefits (UIB) system, in particular the procedures now followed to grant extended benefits to jobless persons for periods in excess of normal coverage. The two-track procedures represent a method of imposing requirements on long-term UIB recipients similar to those imposed on welfare recipients. It is true that this change could be accomplished within the current UIB system itself; no "welfare reform" is required. Proponents are loath, however, to separate the UIB problem from other elements of the transfer system.

Two-track systems in one form or another have received the support of officials within the Department of Labor, as well as Eli Ginzberg and other manpower authorities. More recently, they were the topic of a Ford Foundation continuing seminar on welfare policy. The trade-off involved is this: In exchange for increasing
the benefits in the poorest states and extending the benefits at some level to all families, the federal government would increasingly—and perhaps totally—assume the costs, as well as forcefully and publicly declare that malingerers on the AFDC and UIB rolls will not be tolerated.

The final option is tinkering, more eloquently described as incremental reform. Incremental reform requires working for one or more specific improvements in the current welfare system. The first item on the list is a federally mandated minimum benefit level in all states. The second is extending AFDC-U to all states. The third is liberalizing AFDC-U eligibility regulations, including dropping the 100-hours rule. The fourth is separating Medicaid eligibility from AFDC. In exchange for one or more of these, the federal government would offer to increase its share of program costs and, if deemed desirable, further strengthen the WIN program.

Variations on an incremental strategy are almost as old as AFDC itself. In 1969, Richard Nathan, then a Nixon aide, responded to a Presidential request to “do something about welfare” with a proposal that included the first two items. His proposal was briefly considered, but subsequently discarded in favor of the Family Assistance Plan.

It is somewhat unfair to call such changes incremental, since any of them would significantly change the existing system. Yet the changes are incremental because even if they were all adopted, many features of the current system would remain intact. Wide variations in state benefit levels would continue. Food stamps would remain as a separate program. Cumulative (from multiple programs) marginal tax rates on earnings of welfare recipients would remain high. Programs would continue to be administered by the states through local offices, with long eligibility checks, social workers, and so on. The fact that the changes can be described as increments to the existing system is a great advantage. To see why, it is useful to review a bit of history.

The political lessons of FAP

How should the President choose among his options for welfare reform? One obvious criterion is the probability of Congressional passage. No one would suggest that every plan managing to get through Congress is worthwhile. But it seems foolish to spend much time on programs with highly dubious political prospects.
Fortunately, the President has some political experience to learn from: the history of the Family Assistance Plan (FAP). FAP, a program of the Nixon Administration, was the last serious attempt at national welfare reform. It was twice passed by the House of Representatives, in 1970 and 1971, and twice defeated in the Senate, largely through the actions of the Senate Finance Committee. By now, both the program and its history have been described in several good books by M. Kenneth Bowler, Vincent and Vee Burke, and Daniel Patrick Moynihan.

The defeat of FAP is often described in terms of political perfidy: The liberals, who should have supported it, did not; or the Administration introduced it, and then walked away from it. But the history in these books suggests a more systemic problem—the inability of the Administration to clarify the relationship of FAP to the existing welfare system. Without such clarification, the many vested interests of the welfare system could not know whether to support or oppose FAP.

President Nixon introduced FAP in a nationally televised speech in August 1969. The program he described was a kind of negative income tax (though he avoided that term), designed for families with children. Its maximum payment for a family of four was $1,600, and recipients would lose 50 cents of benefits for every dollar they earned over $50 per month. The program had certain overtones of a two-track system: There was to be a work test for employables, and some public-service jobs. But these were not the central focus of the program. Throughout his speech, President Nixon emphasized the way in which the universal, uniform FAP would replace the archaic AFDC system with a streamlined income-support program, whereby work would be profitable and encouraged.

In reality the proposal was—or soon became—more mundane. Early in the year, Administration analysts had considered proposing FAP as a replacement for AFDC. But by the August speech, officials agreed that AFDC recipients should not lose benefits under any reform. If a state paid AFDC benefits above FAP’s payment, it would have to supplement FAP’s payment to keep the level of benefits unchanged.

In practice then, FAP would have provided the first three items of incremental reform. In the poorest states, benefit levels would have been raised, and benefits would have been extended to two-parent families with children. But in a state like Illinois, little would have changed. The 100-hours rule on AFDC-U would have been
eliminated. The federal government would have assumed a greater share of program costs. But the typical welfare recipient would not have noticed much difference.

Had the Administration presented FAP as a set of minimum standards, it just might have received smoother passage. But it described FAP as total welfare reform, and thereby made FAP vulnerable on a number of grounds.

Burke and Burke describe how Senator John Williams, a fiscal conservative, lectured the Senate Finance Committee on FAP’s work disincentives. Using charts requisitioned from HEW, he showed how the interaction of tax rates on FAP, AFDC state supplements, food stamps, Medicaid, and public-housing benefits created extremely high cumulative tax rates on earned income and, in some cases, left recipients worse off as earnings increased. His points were well taken—but they could have applied equally well to the then-existing welfare system without FAP. Because FAP was purported to be a total welfare reform, however, conservative opponents could attack it for not curing all of the problems of welfare.

At the same time, liberals—including Senators Eugene McCarthy and Fred Harris, spokesmen from the National Council of Churches, and members of the National Welfare Rights Organization—attacked FAP because its annual payment of $1,600 was below the AFDC payment in more than half of the states. Some of this attack was disingenuous—it was known that the Administration wanted to mandate state supplements to FAP’s payment, so that no welfare recipient would lose by the law. But some of the critics were honestly confused by the Administration’s insistence on the uniform nature of its program. In President Nixon’s August speech, the only reference to state supplementation was a phrase, inserted at the last minute, that no current welfare recipients would lose benefits. Even then the point remained unclear, and within 72 hours Administration spokesmen had to clarify it at a press conference. Over time, the issue came alive again, as the Administration backed away from its earlier position. When FAP was reintroduced in 1971, the language requiring state supplementation was ostentatiously missing from the bill, and this helped kill any remaining liberal interest in the plan.

We should not rely too heavily on hindsight. Given the then-existing hostility to the welfare explosion, it is remarkable that FAP’s proposal to increase benefits in low-payment states progressed as far as it did. Nonetheless, it appears that the Nixon Administration underestimated the complexity of its political task. Welfare
politics in the United States involves a delicate balance of interests: Russell Long, black welfare mothers in Los Angeles, mayors, governors, social workers, the United States Chamber of Commerce—the list is long. Even the most irrational features of the system benefit someone, and so every reform will arouse opposition.

Normally, one deals with a political opponent through compromise—or by outvoting him. In the case of welfare, a compromise strategy is problematic because the issues are so intense. Consider the level of benefits: How can a Congressman from Detroit or Baltimore be persuaded to vote for a national benefit level that might—or might seem to—cut his constituents’ AFDC payments by 20 per cent? Conversely, how can a Congressman from the rural South be persuaded to support a proposal that would cause a sharp rise in the wages of low-skilled labor? Similarly, requiring welfare recipients to accept public-service employment attracts so much support because it is discussed in the abstract. But federal officials conceive of such jobs as paying something close to the minimum wage, while union officials expect remuneration to be set at prevailing wages. In many urban areas, the difference between minimum and prevailing wages for even routine jobs can be more than $8,000 per year. With the tight federal budget and municipal layoffs, it is hard to see a common ground.

If compromise cannot work, there remains the possibility of outvoting the opposition. But as the scope of reform grows larger, more and more interests will be adversely affected—and all the votes will move to the other side. This is what happened to FAP. By purporting to reform the entire welfare system at once, the Nixon Administration created an enormous list of opponents and guaranteed its defeat.

Earlier we suggested that any serious welfare-reform proposal must balance liberal and conservative elements—an extension of benefits together with a redistribution of costs or a toughening of work requirements. The lesson of FAP suggests something stronger: Those committed to improving the well-being of the poor must insure that the debate is confined to a narrow range of issues—in the language as well as the substance of the proposals. Any suggestion of “total welfare reform” will expose every aspect of the existing system to new debate, guaranteeing political stalemate. If the President is seriously concerned with the adequacy of the current system, he is politically constrained to pursue an incremental strategy of trading mandated minimum standards and other reforms for greater federal assumption of costs and an expansion of WIN.
Moreover, all of this trading should be described in suitably modest language.

**The system in Alameda County**

An incremental strategy may improve the system somewhat and achieve a better distribution of costs, but what about the remaining problems—work incentives, administrative problems, fraud, inequities, intrusions into recipients' lives? These should be addressed serially, if at all, rather than attempting to solve them simultaneously.

The President should be cautious. Selling a new program is like selling a new car: In both cases it is useful to exaggerate the shortcomings of previous models. But although some of the remaining problems are serious, realism suggests that the negative-tax and two-track systems may not solve them—if only because these programs also have shortcomings that even the most prescient have yet to identify. Compared to textbook descriptions of comprehensive reform, the existing welfare system is a hopeless hodgepodge, the result of years of devious political compromise. According to a more charitable interpretation, however, the complexity of the system substantially reflects the complexity of the problems to which it is a response. In fact, some of these problems involve trade-offs that preclude their simultaneous solution. If proposals for comprehensive change are to receive serious consideration, they must come to grips with the same complications that confronted AFDC.

Consider as an illustration a system that exists not in HEW position papers or popular descriptions, but in a major urban area—Alameda County, California. The system there has a relatively generous AFDC program, including AFDC-U, and serves a major poverty area, Oakland. An incremental reform will not substantially increase the current level of benefits for recipients there, so Alameda County is as good a place as any to assess whether the proposed changes make for an acceptable compromise. If the details that follow seem mundane, remember that any social program has a day-to-day impact on the lives of individuals. Program reform is merely a change in the nature of the impact or a change in the people involved.

When an Oakland mother with three children wants to apply for AFDC, she comes to one of the seven welfare offices in the county. After being given a number, she must wait in a rather un-
pleasant room until her number is called. She is then given a package of application forms, which she is told to take home and complete to the best of her ability. She is also told to return the next day for a group eligibility meeting, and to bring some positive identification for every member of the family, i.e., a birth certificate or a driver’s license.

The AFDC application form is 12 pages long and requires detailed information concerning the composition of the family, the parentage of family members, the amount of income available, and the assets of the family, including automobiles, real estate, and other personal property valued in excess of $100 per item. If the woman has a job, she will also be asked to provide information about her work and transportation expenses, deductions for social security, and so on. In addition, she must fill out a five-page application for food stamps, which requires similar information.

The next day, in the group meeting, an eligibility worker (not a social worker) will help her finish any questions that she could not understand or answer. The worker will explain the regulations of the system, the right to appeal administrative decisions through a fair hearing, the responsibility to report immediately any change in earnings or family composition, and so on. After the meeting, the completed forms will be assigned to an “intake” worker, who will check them during the next seven days for missing information, and will phone the applicant if more information is required. Finally, an eligibility worker will visit the applicant at home to inspect living conditions, the welfare of the children, and so on.

This whole process usually takes about 15 days. In emergency situations the time can be reduced substantially, or aid can be provided through other channels. Eligibility will be determined according to whether the woman’s income (net of work expenses and certain other deductions) is below the needs standard of the county ($420), and whether the total value of her assets (cars, furniture and other household goods, and real-estate equity) is less than the specified limits for each category ($1,500, market value, for cars; $1,000 in personal property; $20,000 in real estate). If she qualifies for welfare and has no other income, she will receive a biweekly check for $174. If she has other income, her check will be reduced accordingly. Unearned income (like child support from an absent father) will reduce the amount of the benefit check dollar for dollar. Earned income will reduce benefits according to the “$30 and one-third” rule. She will also receive authorization to buy a maximum of $166 dollars of food stamps per month, at a cost of $95. She will
be given a Medicaid card entitling her family to free medical care and reduced prices on prescriptions.

Each month on welfare, the woman will be required to fill out a two-page WR-7 form to report any changes in family income or family composition. Failure to submit this form on time will first bring a warning letter, and eventually benefits will be suspended.

If all of her children are at least six years old, she will be required by the Talmadge amendments to register at the local state-employment-service office for job training and job placement under the WIN program. This registration is arranged automatically by the welfare department. Over time, a WIN service worker will encourage her to enter training, or to undertake a search for a job if she has none. In practice, at any one time, fewer than 10 per cent of AFDC families are receiving WIN or other employment services, and fewer than 17 per cent report earnings from work. All eligible recipients, save those who have just come onto the rolls, have been exposed to WIN services, but in some cases this amounts to merely an interview with an employment counselor.

If the recipient is not receiving these services, if she is not suspected of fraud, and if she is not having difficulties of some other kind, the WR-7 form will be her only contact with the system for one year: She will not be visited by a caseworker. At the end of the year, she will have to return to the welfare office and go through a complete reapplication process.

Now consider two-parent families who apply for AFDC-U. They must go through the same process, with two exceptions. If the father in the household is employed, he must work fewer than 100 hours per month. And regardless of the ages of his children or his employment status, the father must register for WIN services.

What will happen to these families over time? Suppose we define a “case closing” as occurring when a family leaves AFDC and remains off aid for at least a year. This definition is meant to exclude closings that involve moving from AFDC to, say, SSI, or closings where the family is off welfare for only a month or two before returning. On average, a single-parent family like the one described above will be on the rolls 44 months before its case closes by this definition. If the mother has more than a high-school education, her time on the rolls will shrink, on average, to 36 months. If she is currently working, her average time will be still less—18 months. If she has more than three children, or if she is black, or if she has fewer than 12 years of education, her expected time on welfare will expand to as many as 60 months.
Movement off the AFDC-U rolls parallels movement off the AFDC rolls, with two exceptions. First, everything happens much more quickly under AFDC-U. Whereas a typical AFDC family might be on the rolls 44 months before its case is really closed, a typical AFDC-U family will be on the rolls only 12 months before leaving. Second, families on AFDC-U experience substantial rates of disintegration. If a typical AFDC-U case were followed for a year, the odds would be almost one in five that the family would move over to the AFDC rolls within that time. Over two years, the odds would rise to two in five. In some cases, this is because the father in the family is reclassified as disabled (which technically qualifies the family for AFDC, rather than AFDC-U). But in most cases, this shift occurs because the family splits up. This should not be surprising: Most families come onto welfare because they have serious problems. Providing aid can mitigate some of these problems, but it would be naive to anticipate eliminating all of them.

**Four questions**

Does the system in Alameda County need “reform”? As should be clear, reform has too many meanings for an unambiguous response. It is nonetheless useful to examine the system by confronting the four major questions now facing the President.

1. *How generous is the system?* If a family qualifies for aid, the amount of the AFDC grant plus food stamps and Medicaid substantially exceeds the federal poverty standard. Indeed, if Medicaid benefits are valued at either the average cost of services provided or the cost of a comparable health-insurance policy, the total annual benefit package exceeds $6,500. This may not be generous, but no current plan for comprehensive reform proposes a larger benefit.

The system is obviously not generous for poor, two-parent families made ineligible for AFDC by “overemployment” of adults. Such families are eligible for food stamps and perhaps limited medical assistance (under the medically-indigent provisions of Medicaid in California), but not for cash payments of any kind. These families are the working poor to whom any welfare reform proposal must, in part, be addressed.

2. *What work should be required of recipients?* The system is best described as schizophrenic: On the one hand, work is encouraged by WIN employment-search requirements, and support is provided for employment preparation, counseling, and training; on the other hand, there are three potentially serious work disincentives—Medic-
aid eligibility, AFDC-U eligibility, and the high marginal tax rate on benefits.

For both AFDC and AFDC-U families, loss of Medicaid benefits is a significant barrier to leaving welfare. Families with children regularly need both normal and emergency health care. Possession of a Medicaid card frees such families from budgeting for normal care, and in the event of an emergency, care can be obtained quickly through established and accessible procedures. But a low-income, non-welfare family cannot get assistance in a medical emergency—a major operation for a child, for example—except through a lengthy process of establishing medical indigence. Hence a family leaving welfare subjects itself to considerably more uncertainty as well as considerably lower quality health care. This is surely a legitimate area for reform.

AFDC-U regulations automatically cut off aid to the families of men who work more than 100 hours per month on a regular basis, regardless of the wage earned. At the same time, an AFDC-U father is required to take a job only if it pays, after standard deductions for work expenses, more than his AFDC-U grant. For men with large families, this provision can rule out any job paying less than $5.00 per hour. Few entry-level positions pay this much, even though some offer excellent prospects of income advancement over time, once employment is established.

What common sense might suggest about the effects of these regulations is borne out by the data. Analysis of a sample of Alameda County recipients indicates that, all other things being equal, the likelihood of an AFDC-U case closing is inversely related to the number of children in the family. The data also indicate that tightening the definition of unemployment under AFDC-U (at one time families headed by men who were involuntarily employed fewer than 172 hours per month were eligible) has reduced the likelihood that jobs will be taken. The 100-hours rule and the first-job wage requirements thus seem to be good targets for reform.

The high cumulative tax rate on earnings results from the interaction among AFDC, food stamps, and other benefit programs. The typical families described earlier appeared relatively immobile: Once on welfare, they tended to remain for many months. An economist might speculate that their low mobility was caused by the high tax rate, which created a low incentive to take a job. But this speculation seems to be incorrect. Because of various administrative and court decisions over the past 10 years, California's AFDC system has had four different tax rates, including the old
100-per-cent tax as well as a system under which the first $70 to $100 of the monthly earnings of most recipients were not taxed at all. Yet analysis of the data in California indicates that these tax-rate variations had no impact on the likelihood that an AFDC mother would take a job. Roughly similar findings about male-headed households emerged from the federally sponsored New Jersey Negative-Income-Tax experiment, in which sample households were assigned to negative-income-tax plans with a variety of different guarantee levels and tax rates. Analysis of the New Jersey data shows that variations in the tax rate had no significant impact on the hours worked by the household members.

All of these results are tentative and require further verification. Nonetheless, they suggest that reductions in the current AFDC tax rates on earnings are not a high-priority item for reform. This is especially the case because such reductions will substantially increase overall program costs by extending welfare eligibility further up the income distribution (recall McGovern's Dilemma).

3. Can the system be administered more efficiently? Perhaps. From the perspective of a recipient, an efficient system is one that delivers the benefits it is supposed to. In Alameda County, for each AFDC office there is a food stamp office in the same building. Case records show that all AFDC recipients receive Medicaid, while about 85 per cent receive food stamps. Recipient access to other programs—e.g., public housing—is more problematic.

From an administrative perspective, the minimal requirements for efficiency are that administrators be able to identify quickly the number and identities of people receiving aid, that reliable records of costs be maintained, and that control be exercised over the training and activity of eligibility workers and social workers. The Alameda County welfare system certainly meets all these requirements. At the same time, it probably tolerates a significant amount of fraud. The county maintains a fraud-inspection unit that primarily operates on two kinds of information: phone tips from recipients' neighbors, who call on a "welfare hotline" to report incidents of fraud; and cross-checks with the state tax system, whereby social security numbers of recipients are matched against those of workers whose taxes have been withheld by the state. Both sources reveal a significant amount of fraud, and about five per cent of the total number of cases are under investigation for fraud at any one time. But the fraud unit itself feels that it cannot uncover other kinds of fraud—the small amounts of unreported income, the AFDC-U father who "disappears" when he finds a job and "reappears"
when he is unemployed, and so on. Whether the rate of welfare fraud is any different than the rate of tax fraud is unclear. Nonetheless, administrators believe that better control of fraud is a legitimate concern.

4. How is the system financed? In California, the non-federal share of the cost of the welfare system is divided between the counties and the state. Overall, the state pays about 33 per cent of AFDC costs, and the county picks up 17 per cent; the remaining portion is covered by Washington. California is atypical—it is a wealthy state, and both the county and the state could probably afford to pay more. Both would be delighted to pay less.

The existing system creates substantial incentives for the state, and at least modest incentives for the county, to be concerned about administrative efficiency. These financial incentives clearly affect administrative behavior and are backed up by the federal government through a regular system of audits, to assure state compliance with its regulations. However, in negotiations over welfare procedures, the federal government has few “sticks” with which to force efficiency; in the end, it is the financial incentives and the resulting local political pressures that seem to count in bringing about administrative improvements.

In addition to these four major areas, Alameda County’s system has a number of secondary problems. About eight per cent of the Alameda caseload is in public housing; the rest of the families are not. The vacancy rate in the county’s public housing is effectively zero, so one can assume that having a public-housing apartment is an advantage distributed arbitrarily among low-income families. Eliminating this inequity, however, requires phasing out public housing, or providing it to everyone, or adopting a different program—not “welfare reform.” Similarly, about five per cent of AFDC recipients have gross incomes above the needs standard. They remain eligible for aid because of the “$30 and one-third” deduction; if they tried to apply for aid, they would be refused. It should be noted, however, that such inequities are usually of short duration, since anyone with income that high has an excellent probability of leaving AFDC in the near future. The “$30 and one-third” procedure was originally regarded by Congress as a transitional device, intended to help people work their way off welfare. In Alameda County, it does seem to do this. Where it does not—in cases where families remain on welfare, despite having an income in excess of need—it is frequently Medicaid that provides the disincentive for leaving AFDC.
What is to be reformed (again)?

Few would say that the welfare system in Alameda County needs no improvement—least of all the administrators of the system. But little of the necessary improvement seems to require total welfare reform. It is worthwhile to sort the problems of Alameda County into four categories: problems that do not really exist (e.g., the routinely intrusive social worker), problems that could be solved through either incremental or total welfare reform, problems that can only be solved through total reform, and problems that cannot be solved at all, because we lack the knowledge to solve them.

The relative importance of these categories can be seen by supposing that the President succeeded in passing a Negative Income Tax. How would daily life in Alameda County be changed? NIT, modeled on the Internal Revenue Service, would be more remote administratively, and would make certain aspects of the welfare system more automatic. Recipients would no longer have to wait for eligibility examinations. There would be no more multiple applications required for AFDC, food stamps, and other programs. Recipients would cease to have even limited contact with social workers.

If NIT were a true replacement for AFDC, then both county benefit levels and the current tax rate on recipient earnings would probably be lowered. If (as is more likely) NIT were supplemented by AFDC (as FAP was supposed to be), both benefit levels and the tax rate would remain unchanged. In either case, full program benefits would be extended to those working-poor families now excluded from AFDC-U. In addition, certain small inequities—the uneven distribution of public housing, for example—would somehow be eliminated.

But these improvements in efficiency and equity would be at the expense of other program goals. The new system would be less responsive to recipients in financial emergencies. Most allowances for exceptional needs of families would be lost. Moreover, by its remoteness, the new system would be more vulnerable to recipient abuse.

Most of these changes would be modest. The daily life of a current AFDC recipient would largely remain unchanged, because welfare as it now operates in Alameda County is already a kind of Negative Income Tax. It covers most poor female-headed households, it pays a fairly decent benefit level, and it is not particularly intrusive. True, the tax rate on earnings is high, but this seems to have little effect on work effort. The greatest work disincentive of
the system—the relationship between welfare and Medicaid—is typically not addressed in NIT proposals. The greatest virtue of NIT—extending aid to the working poor—can be obtained by extending AFDC-U, and does not require a new national program.

A similar conclusion results from comparing the current system in Alameda County with any of the two-track proposals. Little would be changed under a two-track arrangement, because the combination of WIN and AFDC has already produced a kind of two-track system. The current system does not place heavy formal emphasis on separating employable and unemployable families, but this is as it should be. Because both tracks are given income support from the same building, the system is flexible enough to deal with the frequent changes in family composition by simply relabeling the case folder—a “flip-flop,” in county parlance. If employables and unemployables were serviced in truly separate programs, such transfers would be much harder.

Supporters of two-track systems may object that the current WIN program is insufficiently energetic in providing recipients with jobs. To an extent, the slow (but increasing) rate of job placement under WIN arises from identifiable causes with specific remedies: the requirement for high entry-level wages, the low program budget that limits the number of training slots, and the difficulty in coordinating WIN with other training activities. More generally, the program may be weak because we do not know all that much about how to train unskilled people for available jobs. But if the problem results from a failure of knowledge, a national two-track system based on the same knowledge will be of no help.

Failures of knowledge bring us to the fourth category of problems—those that we do not know how to solve. They occur throughout the welfare system, and impose serious constraints on what the President can hope to accomplish. Two recent examples illustrate the point. The new welfare commissioner of New York City, an executive on leave from an insurance company, was quoted by the New York Times (October 30, 1976) as rejecting a program of semi-annual caseworker visits to recipients’ homes. He acknowledged that such visits would cut down fraud, and admitted that reducing fraud was a high public priority. But he rejected the program because he felt that certain of the City neighborhoods were too unsafe for caseworkers to enter—a real and dangerous situation. It is not clear how such a problem would become easier to solve if it were passed on to the Internal Revenue Service or the Department of Health, Education, and Welfare as part of a total “reform.”
On November 18, 1976, the General Accounting Office (GAO) released a highly critical report on the Supplemental-Security-Income program, which represented a partial federal takeover—a “reform”—of state-operated programs for the aged, blind, and disabled. Since its inception in 1971, the program has been charged with delays in disbursing checks, and other administrative inefficiencies. To these charges, the GAO added the results of a survey showing that significant numbers of recipients had unreported incomes (including income from other federal programs), which made them ineligible for all or part of their benefits. The GAO estimated that had benefits been calculated properly, the program budget would have been reduced by $56 million.

These recent anecdotes, the description of the Alameda County system, and the political history of FAP lead to a single conclusion: The uniform, efficient welfare system of the economic textbooks is nothing but a mirage. Even the most comprehensive welfare reform will leave a system with many of the current problems, and much of the current public unhappiness. Plans for complete reform are distinguished not so much by the improvements they produce as by the risks they entail—most notably, the risk of political stalemate that will preclude any welfare reform for at least the rest of the decade.

Rather than pursue comprehensive reform, the President can present Congress with a program for incremental reforms: a minimum level of AFDC benefits; an extension of AFDC-U to all states; the relaxation of AFDC-U eligibility rules; and the untying of Medicaid from AFDC. If all these reforms were passed, the result would approximate a comprehensive welfare reform in most respects. But the individual proposals do not have to rise or fall together. The President can push for as many as the public will encourage and the budget will permit. And because the proposals work within the existing AFDC system, the President's political strategy can develop without raising the thorniest questions of total welfare reform: the appropriate level for a uniform national benefit, the ways in which marginal tax rates on earnings should be lowered, and so on.

Some will call the proposed measures only half a loaf. But in the welfare system as it now stands, this is certainly better than no bread at all. Given the uncertainties surrounding the outlook for and consequences of more dramatic proposals, a solid half loaf can be viewed as a real accomplishment.