
Institute for Research on Poverty

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IRP SPECIAL REPORT

Welfare Reform in the 104th
Congress, Congressional Forum III

**Strategies for Self-Sufficiency: Jobs,
Earnings, Child Support and the
Earned Income Tax Credit**

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***Welfare Reform in the 104th Congress:
Goals, Options and Tradeoffs***

Lessons from Research and State Experience

**Forum III: Strategies for Self-Sufficiency:
Jobs, Earnings, Child Support and the Earned Income Tax Credit**

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**Welfare Reform in the 104th Congress:
Goals, Options, and Tradeoffs**

BACKGROUND AND CONTEXT FOR THE FORUM SERIES

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Three Congressional briefings have been conducted by the Institute for Research on Poverty (IRP) and Family Impact Seminar (FIS). Why another set of briefings? The two organizations launched these sessions because the debate about how to reform welfare had become highly contentious, being largely defined by raw opinion rather than empirical evidence.

Virtually all observers believe the existing welfare system needs to be changed. Conservatives believe that AFDC destroys initiative and discourages work and marriage. Liberals argue that it offers inadequate benefits while robbing individuals of their dignity and self-esteem. Recipients feel degraded and trapped by a system that offers no reward for their efforts to be self-sufficient and that gives them little control over their lives. Taxpayers criticize spending what appears to be an increasing amount on a program from which they see few positive results.

Specific proposals to change welfare, however, inevitably arouse passion and rhetoric. Arriving at a consensus regarding solutions has proven extraordinarily difficult. These briefings will not provide such solutions. Rather, IRP and FIS are endeavoring to introduce a more reflective discussion into an all-too-often passionate and partisan debate. They do so by drawing upon the better research in given areas and upon the experiences of practitioners struggling with the challenges of doing reform on a daily basis.

Why welfare again?

Once again, we are engaged in a debate about reforming welfare. The necessity for change stems, in part, from the nature of a welfare program: benefits can be received in the absence of work and the "tax" rate at which benefits are reduced in the face of earnings substantially exceeds the rate imposed on other members of society. A closer look suggests that the problems with welfare result from efforts to apply commendable policy principles: (a) the narrow **targeting** of benefits to the income and asset poor and to children, but in ways that clearly punish work and may tacitly encourage unwise decisions regarding the formation of families; (b) by permitting some degree of state **flexibility**, which fosters interstate competition to lower program benefits; and (c) the introduction of program **accountability** systems, which define the mission of welfare offices in terms of getting the checks out accurately rather than moving recipients into mainstream society.

These flaws (and others) might be excused if the major welfare programs for children lifted them out of poverty. That seldom happens. The cash guarantee for an average family in a typical state comes to less than 40 percent of the poverty threshold, less than 70 percent if food stamps are included. Moreover, only about 60 percent of poor children received help from AFDC in 1993, down from 80 percent in 1973. Meager benefits, spotty coverage of the target population, and the high rate at which benefits are reduced in the face of earnings cause AFDC to be a very ineffective antipoverty strategy. In 1993, 15.7 million children were classified as living in poverty; fifteen years earlier, less than 10 million were considered poor. By the mid-1980s, child poverty in the United

States was more than twice that of the United Kingdom and Canada, four times the French rate, and over ten times the Swedish rate.

Despite the shortcomings of welfare, reform remains elusive, for several reasons. First, we cannot agree on goals. Are we trying to reduce the economic insecurity of children, the dependence on public transfers of their parents, or is the purpose to reduce public spending?¹ Second, we cannot agree on the nature of the problem. Some locate the problems of dependency and poverty within the individual; others emphasize institutional and structural factors that affect the individual. And we cannot agree on the solutions. Over twenty separate welfare reform bills were introduced in the 103rd Congress, and welfare appears no less contentious in the 104th Congress.

Who is right in this seemingly endless dialogue? Despite the fact that the debate is cast in oppositional terms, welfare is one area where both sides are right and both sides are wrong. The disputants engage in what might be called perceptual reductionism—taking part of the welfare population and assuming it represents the whole. For some, the never-married, African-American teen mother lacking motivation to move into the labor force represents welfare; others, when thinking about welfare, see women doing their best to raise a family in a world where opportunities are scarce and where the rules are stacked against them. From simple images, we are led through simple theories to "silver bullet" solutions. The welfare population is actually quite heterogeneous in terms of age, education, social and vocational skills, family situations, and motivation. In consequence, answers to the welfare dilemma are likely to be similarly complex. These briefings were organized as one way to inform the debate and replace the rhetoric found on both sides of the issue with a more reasoned discussion.

We have structured the sessions around three dimensions of the problem. The first is the internal dimension: problems stemming from the structure of national welfare policy and the accumulated frustrations generated by prior attempts to alter those structural problems. The second is the individual dimension: concerns about critical decisions some young people make that affect their economic well-being and the well-being of their children. The third is the institutional dimension: issues involving the prospects for self-sufficiency as determined by the nature of the labor market and strategies for supplementing private earnings.

1. The Internal Dimension²

The internal structure of AFDC, the program most closely associated with national welfare policy, has long been disparaged. It was observed above that welfare can be defined as public transfers with two distinguishing characteristics: (1) benefits can be received in the absence of work, and (2) the rate at which benefits are reduced in the face of earnings substantially exceeds the rate we would dare impose on other members of society. Yet if an AFDC client works long enough but does not earn enough to get off assistance, she can lose one dollar in benefits for every dollar she earns. Economists call this a 100 percent marginal tax rate.

Furthermore, an AFDC recipient who works may lose access to health care for her children if she is successful in working her way off assistance through employment that does not provide health benefits. She may face difficulties in finding or keeping quality child care. And a working recipient must continually (usually monthly) report a variety of work-related data to a system obsessed with the accuracy of the benefits issued.

When potential applicants walk into a welfare office, they often confront a hostile "culture." Staff are neither trained nor rewarded for helping welfare applicants or recipients achieve economic self-sufficiency and personal independence. Rarely does anyone ask clients what they need or how the system can help. The interaction between worker and client is routine and adversarial.

Information is processed and institutional antennae are tilted toward screening out the unworthy and detecting fraud and abuse. It is difficult to integrate the roles of cop, or protector of the public purse, and people-changer, even in a "tough love" program.

Reformers have been struggling both with the internal logic of welfare and with management options for years. Virtually every president since Eisenhower has made welfare reform a domestic priority. Since 1980, an explosion of state and local experimentation has occurred—over half the states currently are engaged in at least one reform demonstration that required prior federal approval. Despite the attention, many remain frustrated. The accumulated frustrations with decades of marginal reforms has led to a feeling of resignation—perhaps Washington will never be able to prescribe suitable answers appropriate to various parts of the country. This has led to a renewed interest in devolving social welfare programs to states and local governments—the new federalism, or "block grant," approach to reform. If the federal government cannot, or will not, reform welfare, perhaps the states can.

The first briefing (February 13, 1995) dealt with the history, challenges, and some probable outcomes associated with this approach to reform.

2. The Individual Dimension³

The welfare debate of the last three decades largely focused on moving adult recipients from welfare dependency to self-sufficiency by increasing their labor force participation. That debate encompassed a broad set of supply (characteristics of the individual) and demand factors (characteristics of the labor market). Gradually, policies and programs to ensure that the absent parent met his or her financial responsibilities to his or her offspring were added to the agenda.

Recently, the policy focus increasingly has shifted to a concern with those **individual** choices and behaviors that have adverse longer-term consequences. In particular, policy attention has narrowed in on teen and nonmarital births. There is increasing concern that young women having children before they are emotionally and economically prepared to raise them has adverse consequences both for society and the parties involved.

Some of the numbers are comforting. The number of teen births fell from 587,000 in 1960 to 505,000 in 1992 and the birth rate (number per thousand females ages 15-19) fell from 89.1 in 1960 to 60.7 in 1992. Still, observers note that the proportion of teen births outside of marriage increased from 15 percent in 1962 to over 70 percent in 1992.

These numbers, however, do not fully convey the nature of the issue. Teenage childbearing means young mothers face major difficulties in fulfilling goals for their children. It often results in a life of poverty for both mothers and children. Five years after giving birth, 43 percent of teen mothers are living in poverty. Poverty rates are especially high among those living on their own (81 percent) and those not employed (62 percent); yet poverty rates are still relatively high among those employed (27 percent); and those living with a spouse (28 percent) or adult relative (34 percent). Teenage parents consume a large share of all welfare dollars. Teen childbearing is estimated to cost over \$34 billion a year for the major income support programs alone. Nearly half of all recipients are current or former teenage parents.

If welfare were primarily responsible for these observed trends, the solution might well be found in altering the welfare system. If, however, the relationship between welfare and basic fertility or family formation decisions is more complex, the results of reform efforts might be disappointing. In the meantime, other promising interventions might be ignored.

The second briefing (March 24, 1995) examined the empirical evidence on a range of relevant individual decisions: whether to initiate sexual activity; whether to give birth; whether to marry; and so forth. It also explored some of the prospects and problems associated with altering these behaviors.

3. The Institutional Dimension⁴

Individual decisions are informed by the larger economic and social trends that structure the environment in which choices are made. The structural changes that have taken place in the economy over time might be termed **institutional** changes, since they reflect trends in such major institutional systems as the labor market, which ultimately shape the opportunity structures available to low-income families.

In the post-World War II period, the U.S. economy boomed and opportunity appeared unlimited. Real wages (after inflation) grew by 40 percent per decade. Even those at the bottom of the income and skill distribution witnessed significant gains. Children could expect to do better than their parents and, in fact, typically did so.

Striking changes in the macroeconomy began in the early 1970s and accelerated over the 1980s. Earnings inequality increased, and those at the lower end of the skill distribution fared quite badly. In 1973, the median male with one to three years of high school had \$24,079 in income (1989 dollars); by 1989 the median male with the same level of education had only \$14,439 in income. The trend is nearly as dramatic for males with only a high school degree: in 1973, the median male had an income of \$30,252; this had fallen to \$21,650 by 1989. Overall, average hourly earnings in private nonagricultural industries peaked in 1973 at \$8.55 per hour (in 1982 dollars), before declining to \$7.40 per hour in 1994.

The decline in labor market opportunities for people with low levels of education has placed an enormous strain on the nation's antipoverty programs. But it may also alter the choices people perceive they have. Young men with limited education and skills may not feel that they can adequately contribute meaningfully to a family. Young women may despair of finding a suitable husband who can contribute financially. Despair and futility may have a rippling and counterproductive effect across a number of life decisions.

Strategies are available for improving the economic well-being of low-income families. The Earned Income Tax Credit (EITC) is an income supplement to low-income families. The real value (in 1993 dollars) of the maximum EITC credit has grown from \$739 in 1975, the year the program was initiated, to \$1,068 in 1990. By 1996 the real value of the EITC will be roughly three times its 1993 level, as a consequence of legislative changes in 1990 and 1993. For single-parent families, the child support enforcement system plays a critical role, attempting to ensure that the absent parent continues to support their offspring. The child support system has been improved over the past two decades but much still remains to be done. Some estimate that as much as \$34 billion additional dollars could be collected for eligible children if the system could be perfected.

The third briefing (April 28, 1995) examines changes in the low-wage labor market and how those changes may contribute to problems of dependency and poverty as well as how they might complicate the task of reform. It also examines public efforts to offset these trends through income supplements.

Wicked Public Policy Challenges

These briefings will not provide easy answers; none exist. Despite widespread dislike for the program, AFDC endures because changing it raises very difficult policy choices. Every dialogue on welfare reform inevitably confronts two policy challenges—how to alleviate poverty, particularly among children, and how to minimize welfare dependency, a concern particularly directed at their adult caretakers. This dilemma makes the debate hard to resolve. Society is concerned about the condition of poor children, to whom no blame is assigned for their plight. At the same time, society has mixed feelings about the parents, toward whom some responsibility for the family's economic situation is assigned.

AFDC also endures because, as noted, we have multiple ends in mind. If the issue were only reducing welfare dependency, the policy challenge would be quite simple: end welfare. Short of that, one could reduce the generosity of benefits and make access to those benefits more difficult, a tack that captures the drift of much of contemporary welfare policy. Think of the reaction that a proposal to simply cut AFDC benefits by 47 percent across the board might engender. Yet this is how much benefits have fallen in real terms since the early 1970s.

Generally speaking, however, society is concerned about the degree of economic insecurity experienced by some children. As AFDC guarantees (the amount of benefits a family with no other income would receive) have steadily declined, the number of poor children has climbed to levels not seen since the War on Poverty was launched thirty years ago. If reformers were concerned only with reducing dependency, then cutting benefits would be a simple policy solution. But when child poverty becomes part of the equation, the policy challenge becomes more daunting.

The real reform challenge is to reduce dependency and poverty at the same time. The welfare reform debate has largely ignored this more difficult challenge of dealing with both poverty and dependency, focusing almost exclusively on the question of dependency. Moreover, thinking has often been couched in oppositional terms—the "hards" versus the "softs."⁵ The hards situate the cause of poverty within the individual, and the softs emphasize institutional and structural factors bearing upon the individual. Conventional wisdom would place most liberals in the soft camp, where they are likely to stress the deleterious effects of poverty. Conservatives are more likely to emphasize the dangers of welfare dependency. Acceptance of one position or the other leads observers toward quite divergent explanations for both poverty and dependency as well as toward radically different solutions.

Among the softs are those who believe that it is incumbent upon the state to provide its citizens with enough to enable them to subsist, whether they work or not. Among the hards are those who argue that proactive government effort to reduce poverty is causally linked to increases in social disorganization and personal dysfunction, and that everyone would be better off if public interventions were minimized. Between these positions are those who believe that a myriad of factors contribute to and perpetuate poverty and dependency, including both institutional and individual factors. But the reform dialogue too often assumes the contours of a formal debate—with little real communication and with a seeming obsession with scoring political points.

Must one choose one side or the other? Both positions reveal part of the truth, because no one image of the poor captures the full reality of this diverse population, no single theory explains poverty and dependency in a compelling way, and no one strategy is likely to eradicate these social challenges.

Back to the future: Recognizing the "Columbus complex"

The culture of welfare we are dealing with now has not been the norm throughout history. The normative frameworks and institutional arrangements through which we have helped the poor have evolved and changed throughout time. That change is not always linear. Rather, old arguments and solutions reappear from time to time. Like Columbus discovering a "new" world, policy explorers keep discovering old problems and old solutions (see Appendix A for a review of recent reform themes). Knowing where we have been is essential to determining where we ought to be headed.

Early relief. The history of welfare reform is a story of "novel" ideas launched with high anticipation and exaggerated rhetoric, typically succeeded by dissipated hopes and disappointing (or unanticipated) outcomes.

The crafters of the Elizabethan Poor Laws, the precursor to the modern welfare state, recognized that the poor were not a homogeneous population and that public policy must remain sensitive to that fact. Only the truly destitute—the "lame, impotent, old, blind"—were considered appropriate recipients of public support. The able-bodied were provided what amounted to public service employment, a version of Elizabethan workfare, in order to secure for the local parish some return on its investment. And where possible, children in impoverished families were apprenticed so that they might acquire the skills necessary to obtain employment as adults.

The provision of income support without some obligation on the recipient has generally been viewed with disfavor. A series of reforms in the 1820s and 1830s in the United States and Britain attempted to replace "outdoor" relief—the giving of cash to the poor—with institutions (workhouses) that were intended to rehabilitate the unworthy poor and deter frivolous welfare use. A half-century later, individual failings once again were seen as a basic cause of destitution. The Scientific Charity movement focused on moral suasion and primitive casework techniques (among other things) to enhance the functioning of impoverished families and to minimize the granting of cash assistance. In some locales (e.g., Brooklyn, N.Y.), opponents of welfare were temporarily successful in proscribing all cash assistance.

Children became an object of distinct social concern just before the Civil War. The legal and other resources of the Society for the Prevention of Cruelty to Animals were used to protect children because no other institutional recourse was available. By the second half of the nineteenth century, however, a concerted "child saving" movement had been mounted.

The initial focus was on removing disadvantaged children from their problem homes and neighborhoods. Thousands of children from the slums of eastern cities were shipped to midwestern farms as an exercise in social hygiene. Slowly the emphasis shifted to mechanisms to keep children in their homes. Mothers' pensions (the antecedent of the federal AFDC program) emerged early in this century. They represented a modest effort by a number of states to support disadvantaged children. It was then deemed good policy to provide income support to certain mothers rendered destitute by, in most cases, the death of a spouse. This emerged as a benign and preferred alternative to removing children from what were considered unsafe environments. The recipient's obligation was, in effect, to be a good caretaker of the children in her charge.

A federal role. AFDC (then ADC) was included in the 1935 Social Security Act virtually without debate. The program provided federal support to financially strapped states trying to maintain their systems of mothers' pensions during a national depression. AFDC was specifically designed to keep certain impoverished mothers (widows) out of the labor force so they would not compete with men for scarce jobs and could tend to their childrearing responsibilities. The program

served the public purposes of that era. In many places, obtaining ADC was taken as a sign of public recognition that a mother was carrying out her childrearing responsibilities well. In any case, it was assumed that the need for welfare would diminish as the economy recovered from the Great Depression of the 1930s and as the social insurance provisions of the Social Security Act matured.

It was not long before the tests associated with being designated an appropriate caretaker were strengthened. AFDC benefits typically were conditioned on the behavior of the recipient. A host of criteria were applied to determine whether beneficiaries of public largesse were "fit" to receive help. Ties to the local community were examined; sexual practices were monitored; in some jurisdictions, school attendance and performance were reviewed. In the 1950s, nineteen states enacted or proposed laws or policies to exclude children solely on basis of birth status (e.g., being born to an unmarried woman on assistance). Eleven states had some form of work-related eligibility requirement in 1952, another ten added similar requirements over the subsequent decade.⁶

By the 1960s it was clear the welfare rolls were growing, not shrinking. The caseload no longer was dominated by widows, but by mothers who had less claim on society's compassion. In response, cash welfare assistance often was available only in concert with intensive services designed to help the caretaker parents achieve self-sufficiency. It should not be forgotten that the strategy of the War on Poverty was a "hand up," not a "hand out." The dominant goal for most of that decade was to change how people functioned rather than simply give them money.

Rise and fall of entitlements. Between the late 1960s and mid-1970s, an "income definition" of poverty emerged. Poor people were perceived as differing from the rest of society primarily in their lack of money, and the solution was to correct the income shortfall in a simple and standardized manner. Services were separated from cash assistance. Flat grants (benefit calculations based primarily on family size) as opposed to individualized budgets (benefit calculations based on a number of separate consumption decisions) were introduced. Client protections were strengthened. AFDC became an "entitlement"; benefits were based almost solely on categorical status (e.g., raising children as a sole parent) and economic need and were issued to recipients absent any obligation upon their part.⁷

This transformation had several motives, some well intentioned and others born of frustration. It was generally agreed that behavior-conditioned assistance was labor intensive and costly. It was also argued that services were ineffective and social workers intrusive and abusive. In any case, rising caseloads—a trend abetted by a series of court decisions and administrative rulings that made welfare assistance more accessible to poor children—rendered moot any further discussion of individualized treatment of recipient families.

This income solution to child poverty came under serious attack by the late 1970s. By the early 1980s, explanations of poverty shifted once more toward individual factors (i.e., dysfunctional behaviors) and away from institutional factors (i.e., market failures). The challenge of chronic and geographically concentrated poverty, ambiguously referred to as the "underclass" problem, gained scholarly (though not necessarily policy) attention. And the locus of action shifted away from Washington to the states.

Slowly at first, and then with increasing celerity, state-sponsored welfare demonstrations were undertaken. These demonstrations drew from the tapestry of reform themes that had accumulated. Ancient issues and concerns were discussed as if they were being revealed for the first time. Time-worn solutions were rehabilitated as if they were pristine insights. Under the sobriquet of the new "social contract," the basic welfare structure that prevailed as recently as two decades earlier was partially restored.

From the Colonial period onward, reform has oscillated between compassion and caution, depending on which competing concept or paradigm held sway: individual (personal failings) versus institutional (market or societal failings) explanations for poverty and dependency; assured (based on need) versus attained (based on worthiness) benefits; the focus on outcomes (minimally adequate incomes) versus opportunities (the ability to compete in society); and so forth. These tensions remain as strong today as they were 300 years ago.

And Next?

We have been searching for solutions to the issues of dependency and poverty for a long time. Despite the long search, the task of reform remains daunting. As the search continues, we suggest four simple principles:

1. Clarity. A clear vision is needed concerning the direction in which reform is headed and how success will be defined and measured.
2. Consensus. Welfare reform should not be a partisan issue. Children are too important an asset to sacrifice for short-term political advantage. Although agreement on all issues is probably not feasible, the process of developing a reform plan should embrace a variety of views.
3. Continuity. Complex social problems such as welfare dependency and child poverty do not lend themselves to quick legislative fixes. The conceptual and operational challenges are fraught with theoretical and management uncertainties. Years of attention, experimentation, and refinement are required.
4. Confidence. Those involved in the reform challenge should not engage in unsubstantiated claims. We yet have much to learn and unwavering devotion to rigorous experimentation is fundamental. Even modest effects, if confirmed through credible evaluations, will constitute an invaluable contribution to the debate.

In the debate about welfare, we often forget that the issue is children. Welfare is merely one strategy for helping them, and not a particularly good one at that. We must keep our focus on the real goal—how to best support children and the families in which they reside.

Notes

¹At the same time that child poverty is getting worse, more children and their adult caretakers are depending on AFDC.

- The number of children receiving AFDC benefits remained relatively stable between 1971 and 1989, at 7.3 million. By July 1993, that number had increased by almost one-third, to about 9.6 million.
- In any month, about one child in seven receives AFDC. Longitudinal studies indicate that four African American children in ten receive AFDC during their minority years. Among poor white children, one in three experience persistent use of welfare; for African-American children the rate is three in five.
- For the first time in history, the number of families receiving AFDC benefits exceeded the five million mark early in 1993. Spending on AFDC benefits increased by over 30 percent between 1989 and mid-1993 (in current dollars) to an annualized rate of \$22.6 billion.

These numbers are a bit misleading. While the proportion of all children getting AFDC rose from about 4 percent in the early 1960s to 14 percent in the early 1990s, the proportion of poor children getting help was falling from 80 percent in 1973 to about 60 percent in 1993.

²See the material presented as part of the February 13, 1995, Congressional briefing. Parts of this discussion are drawn from Thomas Corbett, "Changing the Culture of Welfare," FOCUS (newsletter of the Institute for Research on Poverty), Vol. 16, number 2 (Winter 1994-95) pp. 12-22.

³See materials presented at the March 28, 1995, Congressional briefing. Parts of this section of the paper were drawn from "Teenage Childbearing and Welfare Reform: Lessons from a Decade of Demonstration and Evaluation Research," in Welfare Reform: Can Government Promote Parental Self-Sufficiency while Ensuring the Well-Being of Children, Karen Bogenschneider and Thomas Corbett (eds.), School of Family Resources and Consumer Sciences: University of Wisconsin: Madison (January 1995) pp. 17-28.

⁴See material that will be presented at the April 28, 1995, Congressional briefing. Part of this section was drawn from Robert Haveman and John K. Scholz, "The Clinton Welfare Reform Plan: Will It End Poverty as We Know It?" FOCUS, Volume 16, number 2 (Winter 1994-95), pp. 1-11.

⁵A good deal of this material is drawn from Thomas Corbett, "Child Poverty and Welfare Reform: Progress or Paralysis?" FOCUS, Volume 15, number 1 (Spring 1993), pp. 1-17.

⁶Pamela H. Holcomb. "Welfare Reform: The Family Support Act in Historical Context" (Washington D.C.: Urban Institute, 1993).

⁷This is not entirely accurate. There remained considerable faith that behavior could be influenced and shaped by tinkering with the economic incentives created by public policies, e.g., changing the labor supply of welfare recipients by manipulating the marginal tax rates they faced or improving the demand for low-skilled labor by offsetting a portion of the labor cost to the employer (wage-bill subsidies). The performance of these incentive strategies never quite matched their theoretical promise.

Appendix A: Major Reform Strategies

Social service strategies. Modestly undertaken in 1956 and greatly expanded in 1962, the concept was that social workers would counsel recipients out of poverty and dependency. The credibility of this approach evaporated when caseloads began to increase at an accelerating rate. This approach can be traced back to the "friendly visitors" of the scientific charity movement in the late 19th century. It reemerges as part of the tough-love and social-contract initiatives discussed later.

Institutional strategies. As part of the War on Poverty and Great Society effort, programs were initiated to revitalize social and political institutions at the local level. It was an attempt to empower individuals and neighborhoods, a strategy consistent with the "blocked opportunity" thesis that informed and shaped the War on Poverty. These initiatives (e.g., model cities and community action programs) encountered severe political problems and most were short-lived. In the 1980s, enterprise zones and public housing "ownership" initiatives were suggested to counter disinvestment and disorganization in disadvantaged areas.

Human capital strategies. By the early 1960s, it was argued that some were poor because of insufficient skills and education. The remedy was to enhance their earnings capacity and improve their competitiveness in the labor market. That is, their human capital was to be increased. Undertaken in the early 1960s with the Manpower Development and Training Act (for the disadvantaged in general) and the Community Work and Training programs (for welfare recipients), this approach was greatly expanded for AFDC clients with the introduction of the Work Incentive Program (WIN) in 1967. Since then, there have been numerous shifts in program design and administration (as well as names), but the approach continues under the federal JOBS initiative as well as residual initiatives from the War on Poverty, such as Head Start. A second human capital strategy involved enhancing the motivation of welfare recipients to enter the labor market. The marginal tax rates imposed on AFDC recipients (the rates at which their benefits were cut as their earnings increased) were reduced to allow working adults to keep part of their grant after securing employment (between 1967 and 1981) and by providing income help to the working poor through the tax system (e.g., the Earned Income Tax Credit).

Job creation and subsidization strategies. Public Service Employment (PSE) jobs were used to offset deficient demand for disadvantaged job seekers. At the height of the New Deal of the 1930s, some 4.6 million jobs were created, covering about a third of the jobless. PSE strategies continued to be in favor, at least sporadically, until the 1980s, when private sec-

tor solutions to insufficient demand for labor gained favor. Unpaid public employment as a condition for getting welfare (i.e., Workfare) was introduced in the mid-1960s and has been employed sporadically since. A variety of subsidies to employers (wage-bill subsidies) to offset the costs of hiring disadvantaged job seekers have been tried—becoming a major strategy in the late 1970s. The Targeted Jobs Tax Credit and WIN Tax Credit are two such subsidies. Yet another variant of this approach is the AFDC grant diversion program.

Income strategies. The best example of the income approach to reducing poverty was found in the several comprehensive federal mega-plans proposed during the 1970s: Nixon's Family Assistance Plan, Senator George McGovern's universal demogrant proposal, and Carter's Program for Better Jobs and Income. Their roots can be traced back to proposals for a negative income tax, initially suggested by Milton Friedman and others during the 1960s. A more subtle expression of this approach is found in the rather unplanned increase in the generosity of welfare guarantees and the easing of restrictions to obtaining benefits that took place in the 1960s and early 1970s.

Child support strategies. The changing composition of the AFDC caseload—proportionately fewer widows with children and more women with children whose other parent was alive but absent from the home—eventually led to a series of initiatives designed to ensure that both legally liable parents contribute to the economic well-being of their children, whether or not they were living with them. Although some federal activity was taken as early as 1950, substantive reforms were not carried out until the creation of the federal Office of Child Support Enforcement (OCSE) in the mid-1970s. This reform strategy was strengthened by federal legislation in 1984 and 1988 (the Family Support Act).

Macroeconomic strategies. For several decades, monetary and fiscal policy has been used as a tool for addressing poverty. The Kennedy tax cuts of the early 1960s, and their alleged positive effects on a sluggish economy, were seen as evidence that the economy could be fine-tuned and used as a weapon against economic want. Until the 1980s demand-focused approaches (e.g., increasing the money supply or increasing spending on public works projects) were favored. Since then, so-called supply-side approaches (e.g., lower marginal tax rates on individuals and businesses) came into favor. The principle remained the same: A strong economy is essential to lowering poverty and dependence. That is, a rising tide will lift all boats.

The "make work pay" strategy. This approach has been supported by an increasing number of economists who trade in poverty policy. (The phrase "make work pay" is found in *Working but Poor* by Sar Levitan and Issac Shapiro, 1987, Baltimore: The Johns Hopkins University Press, and popularized in *Poor Support: Poverty in the American Family* by David Ellwood, 1988, New York: Basic Books.) The approach is conceptually

similar to some aspects of the job creation and subsidization initiatives introduced as far back as the 1960s. The underlying principle is simple: Work ought to be a rational option; those adult AFDC recipients who work more ought to have more income, and those who really play by the rules and work full time ought to be able to get their families out of poverty.

The “make ‘em suffer” strategy. The “make ‘em suffer” label refers to a broad set of proposals to impose penalties on what are classified as inappropriate or counterproductive behaviors. (This label is used in *Rethinking Social Policy* by Christopher Jencks, 1992, Cambridge: Harvard University Press). Benefits are conditioned on such positive activities as attending school, partaking in work-preparation activities, immunizing children in the care of the recipient, not having more children while on public assistance, avoiding certain felonious activities such as illegal drug use or dealing, or paying the rent. The recipient is obliged to engage in specific activities to get full benefits. In reality, the “tough love” innovations of the 1980s did little more than resurrect provisions widely used in the “fit home” criterion of the preentitlement era.

Social contract strategies. The term “social contract” is used to describe a current approach to reform. (A good introduction to this principle can be found in *Beyond Entitlement* by Lawrence Mead, 1986, New York: Free Press). In principle, this approach balances both institutional and individual explanations for poverty/dependence as well as both liberal and conservative approaches to reform. That is, it would borrow elements from both the “make work pay” and the “make ‘em suffer” approaches noted earlier. The recipient is obligated to work toward self-sufficiency, and government is obligated to provide the instruments and opportunities that will enable the individual to reach that goal.

The “thousand points of light” strategy. The “thousand points” strategy means, essentially, that there are to be no more “solutions from the center.” Each state is encouraged to seek its own solutions to the problem of welfare.

**FORUM III: *Strategies for Self-Sufficiency: Jobs, Earnings,
Child Support and the Earned Income Tax Credit***

AGENDA

Job Availability for Long-Term AFDC Recipients
Harry J. Holzer, Ph.D.

Preparing Welfare Recipients for Employment
Rebecca A. Maynard, Ph.D.

The Low-Wage Labor Market
Robert H. Haveman, Ph.D.

Alternatives to Welfare Income: The EITC
John Karl Scholz, Ph.D.

The Current Child Support System--Status, Problems, and Prospects
Daniel R. Meyer, Ph.D.

The Limits of Private Child Support and the Role of an Assured Benefit
Irwin Garfinkel, Ph.D.

The Panelists

Harry J. Holzer, Professor of Economics at Michigan State University and an affiliate of the Institute for Research on Poverty, has special research interest in the employment problems of disadvantaged workers, minority youth in particular. He is the author of Unemployment, Vacancies, and Local Labor Markets (Kalamazoo: Upjohn Employment Institute, 1989) and Employers, Jobs, and Hiring of Less-Educated Workers (New York: Russell Sage Foundation, forthcoming 1995).

Rebecca A. Maynard is Trustee Professor of Education, Social Policy, and Communication at the University of Pennsylvania, a Senior Fellow at Mathematica Policy Research, Inc., and a member of the IRP National Advisory Committee. She served previously as senior vice-president and director of the Princeton research office of Mathematica. Her work has included numerous studies and evaluations of employment and training programs for welfare recipients. A recent article of hers in Family Planning Perspectives concerns the causes and consequences of repeat pregnancy among teenage mothers on welfare.

Robert H. Haveman is John Bascom Professor of Economics and Public Affairs at the University of Wisconsin-Madison, where he chairs the Economics Department. He is also a former Director of the Institute for Research on Poverty. He has long experience with social policy analysis, especially that concerning labor market problems of the low-income population. The effect of children's circumstances on their later achievement is the subject of his most recent book, Succeeding Generations: On the Effects of Investment in Children, co-authored with Barbara Wolfe.

Karl Scholz, Associate Professor of Economics and an affiliate of the Institute for Research on Poverty at the University of Wisconsin-Madison, is an expert in tax policy. He has served as Senior Staff Economist for the President's Council of Economic Advisers and has published a number of articles in professional journals on the condition of the working poor, tax issues affecting the low-income population, and assets and savings behavior.

Daniel R. Meyer is a faculty member of the School of Social Work and an affiliate of the Institute for Research on Poverty at the University of Wisconsin-Madison. Welfare reform and child support are the principal subjects of his research. He has also served as a visiting staff member at the U.S. Department of Health and Human Services, where in 1993 he helped develop a model to predict the costs and effects of welfare reform. He has published a number of articles on the child support system and on the Supplemental Security Income program.

Irwin Garfinkel, Mitchell Ginsberg Professor of Contemporary Urban Problems at Columbia University, has special expertise in the area of child support. A long-time affiliate and former Director of the Institute for Research on Poverty, he designed the pioneering Wisconsin reform of the child support system that began in 1982. Among his books are Assuring Child Support: An Extension of Social Security (New York: Russell Sage, 1992), and an edited volume, Child Support Assurance: Design Issues, Expected Impacts, and Political Barriers as Seen from Wisconsin (Washington, D.C.: Urban Institute Press, 1992).

JOB AVAILABILITY FOR LONG-TERM AFDC RECIPIENTS

Harry J. Holzer, Professor of Economics, Michigan State University

If all AFDC recipients were required to seek work, how many would actually be able to find some type of private-sector job within a reasonable period of time?

The answer to such a question depends partly on the total number of jobs in the economy, which will reflect factors such as the business cycle (i.e., whether or not the economy is in recession). It will also depend on the skill needs and geographic locations of available jobs, relative to the personal skills and residential locations of welfare recipients.

To date, economists have had little direct evidence on job availability among employers. To remedy this data deficiency, I recently administered a phone survey to over 3000 employers in several large metropolitan areas. The survey focused on job characteristics and employer hiring behavior for jobs that are available to less-educated workers.

Among my principal findings (Holzer, 1995) are the following:

1. The vast majority of jobs, even among those that do not require college degrees, involve daily interactions with customers, reading/writing of paragraphs, computation of arithmetic, and/or use of computers. Most also require that applicants have high school diplomas, previous experience in the particular line of work, references and/or formal job-related training.
2. Job requirements at firms located in central cities are even higher than they are for those located in the suburbs of major cities. Thus, only 5–10 percent of non-college jobs in the central cities do not involve any of the cognitive tasks listed above, and less than 5 percent do not require any of the credentials listed.
3. On jobs that do not involve much reading/writing or do not require the above credentials, employers often seem to prefer less-educated white or Hispanic applicants (including immigrants) to African Americans. The preference for whites is particularly strong in clerical/sales jobs that involve direct contact with a predominantly white clientele. The preference for Hispanics is strongest in blue-collar or manufacturing employment.

What are the numbers and characteristics of long-term AFDC recipients who might soon have to seek employment? In the largest American cities, 10–15 percent of household heads at any point in time are relatively long-term AFDC recipients (i.e., those who have been on the rolls for more than just a few years). Few of these women will bring any kind of meaningful recent work experience or job training to the labor market.

Furthermore, most of these longer-term recipients are concentrated in low-income, inner-city neighborhoods, with little access to private transportation or to the information and social contacts that are often needed to obtain jobs. About 60 percent of these women are high school dropouts, who frequently score poorly on tests of cognitive ability; some have other physical or emotional disabilities; and over half are African Americans. In addition, they will be competing for any available jobs with a fairly large pool of less-skilled individuals who are already in the labor market and looking for work (at least intermittently).

All of these data strongly suggest that a significant fraction of long-term AFDC recipients will not be able to find employment quickly, if at all, and will therefore suffer lengthy (and sometimes

permanent) periods of nonemployment. Even among those who do find work, many will experience high job turnover (owing to problems with their child care, transportation, or work performance), thus adding to their high unemployment rates. Indeed, the fraction of these women employed at any point in time is likely to be well under one-half in the absence of major policy interventions (Danziger et al., 1981).

As time goes on, the labor market will partially adjust to the added labor supply of these individuals, and perhaps more low-wage jobs will be created. But given the very lengthy spells without work experienced by inner-city, minority young people over the past few decades, it seems unlikely that enough jobs will be created for all who want them, even in the long term.

In addition to job placement/transportation assistance and job training, there will therefore be some need for longer-term public job creation if most of these women are to be moved from welfare to work rolls. This job creation might involve some type of targeted subsidies for employers, though these have their limitations. Alternatively, some degree of public sector employment may be necessary if strict time limits on AFDC are enacted, or if major work requirements are imposed on those who remain on the welfare rolls beyond some time period.

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PREPARING WELFARE RECIPIENTS FOR EMPLOYMENT

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April 28, 1995

My remarks will focus on three main messages. First, even if states succeed in implementing exceptionally strong employment and training programs for welfare recipients and welfare is time limited, many current and "would be" welfare recipients can look forward to, at best, low wage and episodic employment. Second, welfare recipients vary significantly in their employment potential and, indeed, in the likelihood that they will participate in and benefit from the types of education and training services that form the cornerstone of the JOBS program. Third, the success of employment programs for welfare recipients depends critically on public policies regarding the support services, wage supplements, and time limits.

Most welfare recipients, including first-time teenage parents, have some prior work experience, and even under current welfare policy, most are expected to have a job sometime within the next three years. For example, over half of all new applicants registered in California's GAIN program were employed some time during the three years after coming onto welfare (Friedlander et al. 1993), and 40 percent of first-time teenage parent welfare recipients were employed at some time during a thirty month follow-up period (Maynard et al. 1993). Yet, these jobs tend to be low paying and short tenure. Even under a dramatically reformed welfare system, it is unlikely that the majority of them will be economically self sufficient within two years. Indeed, a large portion of them will not even be economically self-sufficient within a five year time limit (CBO 1990).

The past fifteen years of social experimentation with employment and welfare policies suggest some avenues for state and federal policy makers to pursue in the next generation of welfare reform--options that will improve, albeit modestly, the likely outcomes for poor and single parent families under a radically transformed welfare system. These lessons derive from myriad state and federal welfare demonstration projects--some large-scale demonstrations of programs operated in lieu of the regular welfare system and some that operated as small scale, high intensity interventions; some with participation mandates and many that served primarily or exclusively volunteers; some that concentrated on long-term recipients and some that focused on the new applicants; and some that targeted adults, while others targeted teens (Burtless and Friedlander 1995; Maynard 1994, 1993; Hershey and Nagatoshi 1989; Quint et al. 1994; Bloom et al. 1994; Bloom et al. 1993; and Cave et al. 1993).

Barriers to Economic Self-Sufficiency Through Employment

The single biggest barrier to economic self-sufficiency for current and prospective welfare recipients is their **limited basic skills and work experience**. Large portions of welfare recipients fail to meet the basic skills requirements of the lowest occupational categories--service (40%), crafts and construction (37%), household workers (33%) and manual operatives (31%) (Zill and Nord 1994). Currently, there is a limited demand for workers in these jobs; they pay low wages and have limited or no fringe benefits; and they are characterized by high job turnover (Burtless 1994; Blank 1994). In part the high job turnover is a function of instability in the labor demand, but the poor job performance of many workers in this end of the job spectrum also contributes (Burtless 1994). Time and again, welfare recipients who have improved their basic and job skills to meet job demands lose their job after a short time, due to other complicating factors, including inadequate social skills and/or adaptability.

A second barrier relates to the **low economic and social rewards** to employment in the current environment--factors that could improve substantially under welfare reform. Under current policies where welfare is neither time-limited nor for most recipients, contingent upon serious work effort, there are relatively modest financial pay-offs to taking a full-time job at near minimum wage over the financial benefits and income security afforded by public assistance (Ellwood 1988; U.S. House of Representatives 1993). For many recipients, the strong desire for a better life and a life of economic independence is simply not strong enough to overcome the anxiety over the "failure" or "rejection" that most who brave the transition experience. Indeed, over half of those who leave welfare for employment lose their jobs within two years and return to welfare (Figure 2) (Gleason et al. 1994; Pavetti, 1995). One striking example of the challenge in moving welfare recipients into long term employment is illustrated by the experience of the Teenage Parent Welfare Demonstration in Newark, New Jersey, which trained several classes of teenage parents to work as sales clerks in a suburban mall. All successfully completed the training and were placed in jobs; all also quit or were fired from their jobs within a matter of a few weeks from placement (Hershey and Rangarajan 1993). They simply had not acquired the social skills and adaptability necessary to work in these relatively low-skill service jobs.

A third barrier to employment relates to real and perceived problems finding employment, finding and paying for child care, and accessing reliable transportation. Typical responses of welfare recipients to questions about the reasons they are not working include "can't find a job," "child care is not available," and "lack of transportation" (Figure 1). Yet, the reality is that the underlying problems are much more subtle. Many welfare recipients (and perhaps most) lack the self confidence, job search skills, and social support to engage in a prolonged and productive job search. Most also have limited or no experience with the child care market--having neither role models nor knowledge as to how to approach the market. And, most have limited experience with public transportation beyond their immediate neighborhood.

Indeed, welfare reform initiatives that have sought to attain high rates of JOBS participation and that have been willing to invest in case management and social support services have found all of these

problems to be highly tractable. Moreover, the cost of addressing them generally is substantially less than anticipated. Work mandates, with sanctions, are especially powerful in promoting aggressive service provision by local welfare offices--with the aim of avoiding imposition of sanctions (Maynard 1993). Providing child care resource and referral services and a willingness to subsidize child care on a sliding fee basis results in significant numbers of welfare recipients with young children engaging the services of relatives while their children are very young (Kisker et al. 1990; Schochet and Kisker 1992). However, most do switch to paid care as their children approach toddler age. The result of this pattern of child care use suggests quite clearly that sites are not minimizing costs by exempting mothers of young children from JOBS participation. For example, in a large scale study of teenage parents on welfare, even when child care subsidies were universally available to JOBS participants, two-thirds of mothers with very young children opted to rely on free relative care. However, over time, reliance on free care diminished as a result of both the unwillingness of many grandmothers to continue to care for the children as they became toddlers and the interests of the mothers in getting the children into more developmentally focused and more reliable care (Schochet and Kisker 1992; Kisker et al. 1990). By the time these mothers are mandatory for the program, they not only have been a recipient for over two years, on average, but they have an average of two children to be put in care, not one (Maynard and Rangarajan 1994).

Finally, transportation is a challenge, particularly when child care drop-offs are factored into the equation. However, there is evidence that areas that take seriously the goal of serving large fractions of their caseload in JOBS can succeed in working out public transportation or van pool options at reasonable costs (see for example, Hershey and Nagatoshi 1989). What is less well tested is the feasibility and cost of addressing child care and transportation needs in suburban and rural areas.

Effectiveness of Employment-Focused Interventions

The current array of education and training programs focused on welfare recipients and other disadvantaged populations have typically not been very effective in improving employment outcomes. The majority of welfare recipients, who have low levels of education and limited basic skills, generally have three **educational options** for improving their basic skills. First, the teenage parent recipients can return to or remain in the comprehensive high schools, which in inner city areas, in particular, frequently fail half or more of their students and turn out graduates with skills only marginally better than the typical welfare recipient (Committee for Economic Development 1994). Second, they can enroll in alternative schools, which often have limited academic expectations for their students, but do offer more accommodating schedules. This option, too, is available only to the younger welfare recipients. The third and most accessible option is the General Educational Development (GED) preparation programs. These programs are short-term and tightly focused on preparing students for the GED high school equivalency exam. Indeed, most of the work-welfare demonstrations have demonstrated modest impacts on GED attainment, but limited or no gains in completion of regular high school. The exception is that the mandatory learnfare programs targeted at teenage parent welfare recipients have had modest impacts on regular school retention and completion, even though their largest gains are in GED completion (Long et al. 1994; Quint et al. 1994; Maynard et al. 1993).

There has been only limited research on both of the alternative educational programs, which are the focus of most of the work-welfare educational components. However, the accumulating evidence suggests that neither contributes significantly to the basic skills and employability of participants. The evidence on alternative schools derives from a limited number of recent and ongoing random assignment evaluations sponsored by the U.S. Department of Education. The evidence on the limited effectiveness of the GED programs derives from two sources. One is the nonexperimental research by noted labor economists, who have estimated that there are at best, very modest employment and earnings gains associated with the GED (Murnane et al., 1993; Cameron and Heckman 1993). The second source of evidence comes from results of many work welfare demonstrations which have included education, job training, and job placement services and have been evaluated using experimental designs. Looking across the various outcomes of these demonstration programs, there generally is no correspondence between the likelihood that a program will increase GED attainment and the likelihood it promotes earnings gains of participants (Cohen et al. 1994; U.S. Department of Labor 1995). For example, while 4 of the 5 sites within the GAIN demonstration had positive impacts on GED attainment, none of these sites demonstrated a significant impact on earnings. In contrast, the one site that had a significant impact on earnings did not have a significant impact on GED attainment. (Table 1). Further evidence of the inability to increase earnings through promotion of the GED is found in the New Chance demonstration. In 5 of the 16 sites there were positive impacts on GED attainment with correspondingly negative impacts on earnings in 4 of those sites (Table 2). When we look across work-welfare programs for teenage parents, we see a similar lack of correlation between success in promoting GED attainment and success in employment outcomes (Maynard 1994).

We have tested a wide range of **job training programs** in a variety of organizational settings, ranging from those operated by the local JOBS programs, JTPA programs operated through public or community based organizations, community based job training providers, proprietary schools, and post secondary vocational schools and community colleges (which often provide contract services to JOBS and/or JTPA). These programs vary in the degree to which they emphasize general versus specific job skills, the setting in which the training is provided (classroom, on-the-job, or a combination), the duration and intensity of the training, the eligibility requirements and targeting strategies, and the extent of transitional employment support (including job placement assistance).

Despite this high variability in program design, the research on effectiveness has been fairly consistent over numerous demonstration and evaluation efforts. Job training programs generally have modest impacts on the employment and earnings of participants. These impacts are due primarily to their impacts on employment rates, rather than to productivity gains (as measured by wage rates).

Beginning with the National Supported Work Demonstration in the late 1970s, the dozens of random assignment evaluations of employment training programs have generally found that they increase employment rates between 5 and 10 percentage points and earnings by 10 percent, plus or minus. Often the results are statistically significant, but in a number of settings they have not been. For example, Supported Work increased significantly the employment and earnings of long term

volunteer AFDC recipients overall but in only two of the seven demonstration sites (Hollister, Kemper and Maynard 1984).

The positive overall impacts measured for California's GAIN program derive from positive impacts on employment and earnings in 3 sites and no impacts in 2 sites (Riccio et al.). The JTPA program had modest impacts for women (most of whom were welfare recipients), but again with high variability across sites (Bloom et al. 1993). In another demonstration targeted at minority female single parents, most of whom were welfare recipients, only one of the four programs had positive employment and earnings impacts. The impacts in that site were somewhat larger than typically found, but still modest relative to the magnitude of the employment problems faced by the target population (Burghardt and Gordon 1990).

The one large scale demonstration of mandatory work-welfare programs for teenage parent recipients resulted in significant employment and earnings gains in all three demonstration sites (Maynard et al. 1993). However, in smaller scale voluntary programs for this target population, there have been no employment and earnings effects for the full study sample and any positive gains limited to only a small proportion of the sites (Quint et al. 1994).

It is also notable that programs that emphasize aggressive job placement assistance have tended to have impacts that are similar in magnitude to the impacts of job training programs. For example, the most successful of the California GAIN programs, Riverside, offers little training relative to the other GAIN sites studied (Friedlander et al. 1993). Similarly, the JTPA evaluation results suggest only modestly greater effectiveness of job training over job search assistance (Bloom et al. 1994).

The Bottom Line

The bottom line is that, currently, we do not have model education and training programs that are capable of preparing many welfare recipients for economic self-sufficiency through private sector employment. Most welfare recipients simply will not pick up sufficient skills through these programs to obtain and retain jobs paying wages sufficient to lift them off welfare, let alone out of poverty. We clearly ought to continue to experiment with new methods preparing welfare recipients and other low-skilled workers for more productive and higher paying jobs. Moreover, we ought to consider some bold experiments in innovative basic skills and job skills training programs.

In the short-run, the bulk of our scarce work-welfare budgets might be better spent supporting welfare recipients in whatever types of jobs they can get--support them through the provision of child care and transportation, as well as possibly through liberalized earnings and asset disregard policies. We also could improve outcomes substantially through policies that make our public schools more accountable for retaining students and increasing their basic skills. As we move through the next round of deliberations on welfare reform, we should consider the following four facts:

Although some job training programs, such as that operated by the Center for Employment Training in San Jose, California, produce handsome pay-offs for both the participants and for society, we likely will not have the luxury of promoting such programs widely under the next generation of welfare reform. These types of job training programs entail substantial up-front investments at a time when resources are dwindling. Moreover, few job training providers achieve the strong results observed in some of the most successful demonstration projects. Indeed, many training providers have had no impact on employment outcomes of participants. In a world of capped funding for welfare and strict time limits on cash assistance, it seems prudent to place priority on ensuring universal access to child care and other employment supports that will enable families to at least maintain their access to earnings and those aspects of the social safety net that support the working poor indefinitely. We should also consider policies that make our public schools more accountable for retaining students and increasing their basic skills.

Work-welfare programs will not substitute for a good educational system. Once youths leave school either having graduated with poor basic skills or dropped out prior to graduation, their prospects for self-sufficiency and an above-poverty income are severely limited. Even the best second chance education and training programs have modest impacts on employment and earnings prospects.

As many as one fourth of welfare recipients--teenage parents and adults--could probably move directly into post secondary education that could yield "large" economic rewards to the recipient. However, the costs of this would be a minimum of two to four years of dependency. One question for policy makers is whether the student financial aid system could be adapted to provide the necessary economic support for this segment of the population

For many, the key to promoting employment is "making work pay" and making jobs available. Not only does work not pay for many welfare recipients (especially in high benefit states), but leaving welfare for work introduces substantial financial as well as personal risks--job loss, performance failure, and income fluctuations. The recipient also assumes increased burdens associated with finding child care and dealing with child care breakdowns.

Most welfare recipients will not participate in work programs, unless required to do so. One reason is the lack of a perceived pay-off. However, other reasons are fear of the unknown (including the unknowns of child care, of job training, and/or of employment).

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TABLE 1

EDUCATION, BASIC SKILLS AND EARNINGS IMPACTS FOR GAIN PARTICIPANTS
(Two to Three Years After Enrollment)

Site	GED/HS Diploma ^a		Test of Applied Literacy		Monthly Earnings (\$) ^b	
	Control Group Mean	Estimated Impact	Control Group Mean	Estimated Impact	Control Group Mean	Estimated Impact
Alameda	1.2	7.7*	480	2.3	\$101	\$9
Los Angeles	0.5	2.2*	445	3.7	98	0
Riverside	3.6	2.6	507	-19.0*	113	73*
San Diego	2.6	4.2*	454	33.8*	159	14
Tulare	1.8	19.0*	478	-10.2	120	12
Total (N=1,115)	2.0	7.1*	475	1.8	na	na

SOURCE: Martinson and Friedlander (1994, Tables 1 and 2) and Friedlander, *et al.* (1993, Table 4).

^a Obtained after referral to GAIN.

^b Estimates pertain to the subgroup determined to need basic education.

* Significantly different from zero at the .10 level.

TABLE 2

ESTIMATED IMPACTS OF THE NEW CHANCE PROGRAMS
ON GED ATTAINMENT AND EMPLOYMENT AND EARNINGS, BY SITE

Site	GED/High School Diploma (%)	Earnings (18 Month Total)	Cost per Participant (\$1,000)
One	3.8	-\$1,276**	\$11.3
Two	10.8	481	4.4
Three	8.0	840	4.7
Four	0.3	-904	8.8
Five	18.0**	357	7.6
Six	-0.1	-351	8.5
Seven	4.2	-781	9.8
Eight	30.4**	-171	10.8
Nine	18.5	-249	6.9
Ten	14.0	-849	10.3
Eleven	24.4**	-140	10.8
Twelve	2.4*	-238	8.1
Thirteen	24.9*	-110	9.1
Fourteen	12.6*	-1,454**	17.7
Fifteen	8.8	807	6.4
Sixteen	25.1	-818	10.3
Average Impact	13.1**	-\$342	\$9.1
Control Group Mean	30.0	1,708	--
Median Impact	12.7	-238	8.8
Range	0 to 30%	-\$1,454 to +\$818	\$4 to \$17

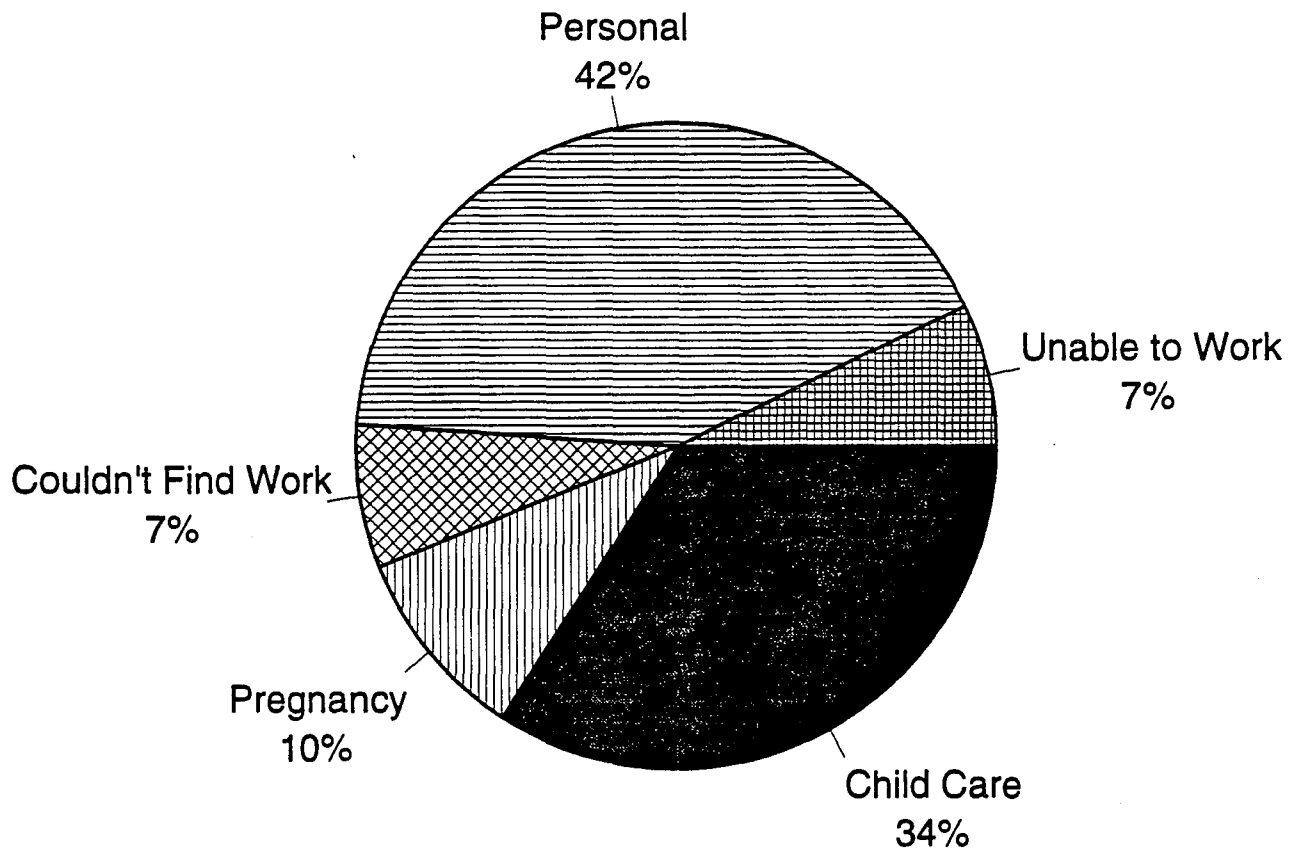
SOURCE: Quint, Polit, Bos, and Cave (1994, Tables 3.9, 5.3, 6.5, 7.3, and 8.5).

NOTE: All of the impacts on high school completion/GED are due to GED attainment. Indeed, the program led to significant reductions in the acquisition of a high school diploma (-2.6 percentage point reductions) and large increases in GED attainment (Cave et al., Table 5.1).

* Statistically Significant at the 10 percent level.

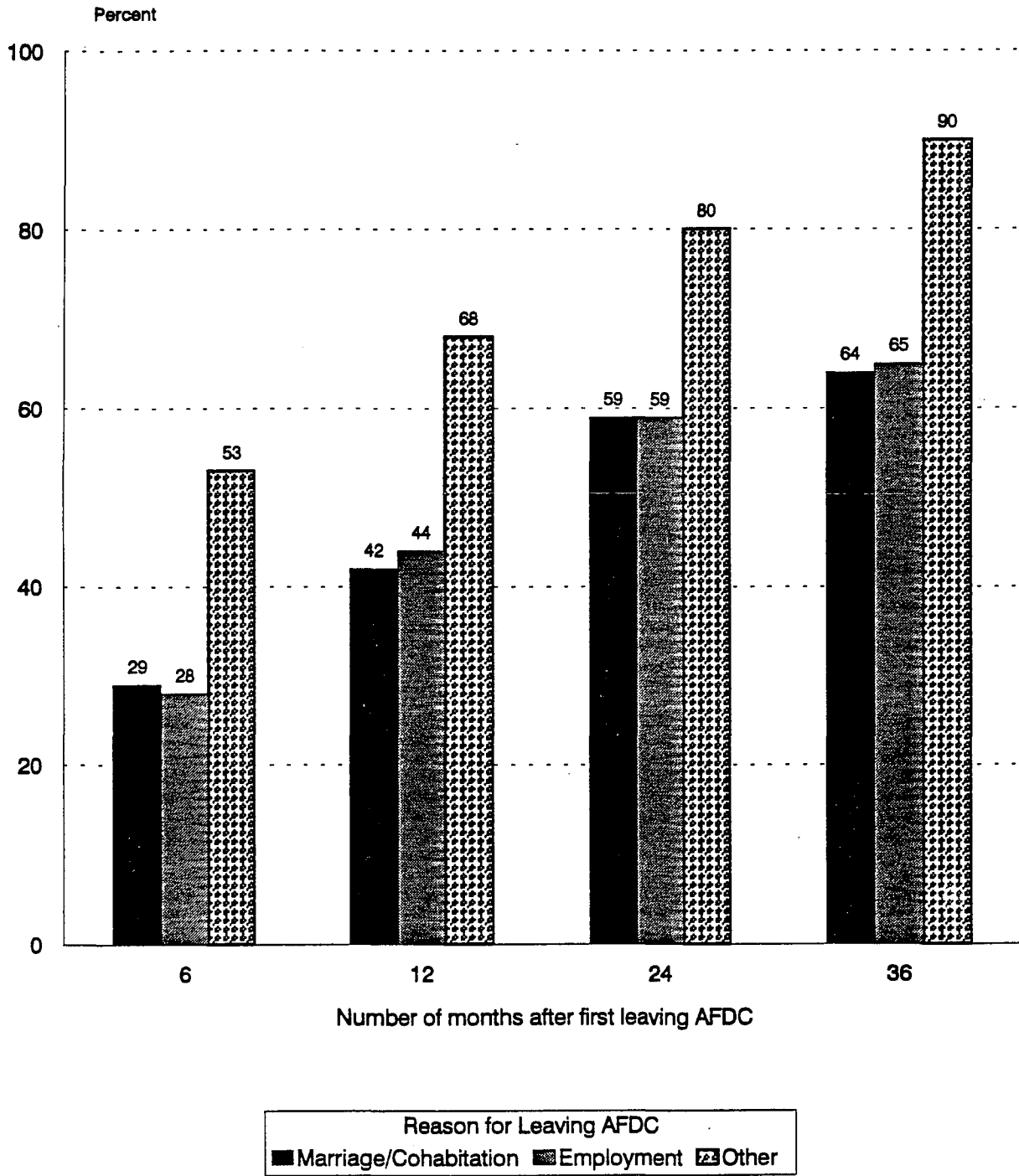
** Statistically Significant at the 5 percent level.

FIGURE 1
REASONS AFDC RECIPIENTS WERE NOT WORKING



Source: Zill et al. (1991: table 18).

FIGURE 2
CUMULATIVE % RETURNING TO AFDC



Source: Gleason, Philip, Anu Rangarajan, and Peter Schochet. *The Dynamics of AFDC Spells Among Teenage Parents.* Princeton, NJ: Mathematica Policy Research, Inc., 1994.

THE LOW-WAGE LABOR MARKET

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The welfare reform debate of 1995 is fueled by both the proposed "time limits" to be imposed on poor families who secure benefits and by the elimination of benefit eligibility for some groups who are entitled to benefits today. If policy changes in either of these dimensions are enacted, a greater share of families headed by people with low levels of education and skills will have to rely on the labor market--on their own earnings--for income and well-being.

Will the additional low-skilled workers excluded from income support and welfare services be able to get work? Can the bottom end of the labor market absorb them? If they are able to find work, will they be able to achieve self-sufficiency on the basis of their own earnings? If these workers least able to cope cannot achieve self-sufficiency through working and earnings, what will happen to them? The picture, I believe, is not a pretty one. Perhaps we should concentrate on reform of the bottom end of the labor market rather than on welfare reform. Let us review some of the facts.

FACT 1: Wages and earnings at the bottom end of the labor market—that serving low-skilled workers—has collapsed over the past two decades. For example, the hourly wage rate for a man with a high school degree but no more has fallen in real dollars by about 35 percent since the early 1970s. The decrease has been even more severe for workers with less schooling—namely, high school dropouts.

FACT 2: The deterioration in wages and earnings for women has been less severe than the collapse for men, but even so the earnings potential for low-skilled women has fallen substantially. The attached Table 1 shows the comparisons in earnings and income deterioration for both men and women with various amounts of schooling.

FACT 3: Implementation of the proposal for a five-year time limit on welfare will confront a very large stock of recipients who have already exceeded the five-year maximum. Hence, the number of welfare recipients who would be forced into the labor market could be substantial if the five-year maximum proposal were to be implemented suddenly, and applied to these women. About 20 percent of the current stock of recipients have been recipients for more than five years during their current reciprocity period. Moreover, evidence suggests that nearly double this number—almost 40 percent—have accumulated more than the **60-month limit**, when all of their spells on welfare have been taken into account. The adult recipients whose current spell exceeds the 60-month limit total about 1 million people. This would be a large bite to swallow. Subsequent annual flows of women who bump into the five-year limit will be smaller, of course.

FACT 4: Ignoring the large potential stock of long-term recipients, there will probably be sufficient jobs created over time to absorb the annual flow of recipients likely to be forced from beneficiary status by any plan now being discussed. The growth of low-wage jobs in the U.S. economy over the past two decades has been nothing short of spectacular. The attached Table 2 shows the strength of job creation in the United States relative to our industrialized competitors.

FACT 5: The characteristics of AFDC recipients suggest that they will be competing for jobs with the least demanding characteristics of any available in the market, and as we have seen from Professor Holzer's comments, even these jobs have substantial cognitive and social requirements. AFDC recipients have very low levels of education, major young child care responsibilities, and

sparse work experience and job readiness. Moreover, over 60 percent of them are African-American or other racial minority, which carries its own burden in terms of competing successfully for those jobs for which they qualify. The attached Table 3 shows the characteristics of AFDC recipients, and illustrates the enormous disadvantages that they bring to the labor market. It would be accurate to state that many welfare recipients will stand far back in the queue of applicants for the available low-skill jobs that are created.

FACT 6: Even if these recipients do obtain jobs—and many will—the upper-bound estimate of their earnings should they work **full time-year round (FTYR)** is no more than \$12,000–\$14,000; given their family sizes, this level of earnings will not remove them from poverty. Moreover, should they work at this level, who will support the required care of their children? The attached Figure 1 follows a group of women who were recipients in the late 1970s, and asks about their labor market performance in subsequent years. It shows that at the limit—working 2000 hours per year—these women have the capability of perhaps earning as much as \$14,000. But many of them, in fact, find their way into temporary jobs paying less than the average wage and end up earning far less than their FTYR potential. Indeed, the typical former recipient earns about one-half of this "outer limit" earnings level.

Given these facts, what are a couple of the implications of the current policy debate regarding welfare reform? In particular:

What Will Happen to Those Recipients Who Lose Their Benefits?

While no one really knows, if I were pushed into a corner I would speculate that 10–15 percent of them would make a successful transition into the world of work and become self-sufficient, but at a low level. Another 70 percent or so would "cope"—they and their children would be severely disadvantaged, but they would adjust by combining households or moving in with relatives, or work some in intermittent and informal jobs. They would be poorer and even less capable of nurturing their children, but we wouldn't be vividly confronted by their hardships. We would only see the effects on their children a decade or two down the road. The remainder—say, 10–15 percent of those losing benefits—would become truly destitute; the effects on them would be obvious: homelessness would be only the most visible effect. The stock of recipients who now face benefit cutoff because of a five-year rule is about 1 million; 10–15 percent of this number is about 100,000 to 150,000. On average, each of these recipients has two children; hence, we are considering 300,000 to 450,000 people who would be visibly destitute. Surely, some of them would find their way onto the rolls of the Supplemental Security Income program—at federal government expense—or into the foster care system, at state and local expense.

Is the Real Problem "The Welfare System," or is it the Collapse of the Bottom End of the Labor Market?

Surely the deterioration of the bottom of the labor market is a major culprit; for my tastes, it is THE problem. If this is so, why do we hear nothing about the need for policy reform regarding the low end of the labor market. Policy instruments do exist—a wage rate subsidy and a marginal employment tax credit both have characteristics that would increase the number of low-skill jobs, and raise the take home pay associated with them. Assessments of these approaches indicate that each has substantial potential for increasing the work and earnings of low-skilled workers. Surely these suggestions should not be excluded from any serious national debate on poverty and poverty policy.

Related Readings

Buron, Lawrence, Robert Haveman, and Owen O'Donnell. 1995. "Recent Trends in U.S. Male Work and Wage Patterns: An Overview." Institute for Research on Poverty, Discussion paper no. 1060-95.

_____. 1995. "The Utilization of U.S. Male Labor, 1975-1992: Estimates of Forgone Work Hours." Institute for Research on Poverty, Discussion Paper no. 1059-95.

Haveman, Robert. 1988. Starting Even: An Equal Opportunity Program to Combat the Nation's New Poverty. New York: Simon and Schuster.

Levy, Frank and Richard Murnane. 1992. "U.S. Earnings Levels and Earnings Inequality: A Review of Recent Trends and Proposed Explanations." Review of Economic Literature, 30(3): 1333-1381.

Nightingale, Demetra and Robert Haveman eds. 1995. The Work Alternative: Welfare Reform and the Realities of the Job Market. Washington: Urban Institute Press. See esp. Chapter 4, "Employment Prospects of Welfare Recipients," by Gary Burtless.

TABLE 1

Median Income of Persons 25 and Over, by Educational Attainment and Gender,
Selected Years, 1989 Dollars

Year	Males			Females		
	High School		College 4+ Years	High School		College 4+ Years
	1-3 Years	4 Years		1-3 Years	4 Years	
1967	\$22,858	\$26,894	\$39,186	\$7,574	\$10,800	\$19,205
1970	23,442	28,034	40,527	7,629	10,866	19,735
1973	24,079	30,252	41,065	7,920	11,087	19,667
1979	18,697	26,416	36,626	6,726	9,085	16,923
1983	15,138	21,932	35,188	6,531	9,326	18,427
1989	14,439	21,650	37,553	6,752	10,439	21,659

Source: U.S. Bureau of the Census (1990), for 1967-1983 figures, and U.S. Bureau of the Census (1991), for 1989 figures.

TABLE 2
Jobs Created in 10 Countries, 1979-92

Country	Total Created 1979-89 (000)	New Jobs as Percent 1979 Employment
Australia	1,617	26.5
Canada	2,091	20.1
France	550	2.6
West Germany	1,730	6.8
Italy	840	4.2
Japan	6,460	12.0
Netherlands	730	13.7
Sweden	364	8.7
United Kingdom	1,410	5.7
United States	18,518	18.7

Source: Lawrence Mishel and Jared Bernstein, The State of Working America (Armonk, N.Y.: M. E. Sharpe, 1994).

TABLE 3. CHARACTERISTICS OF AFDC CASELOAD, 1979-1991.

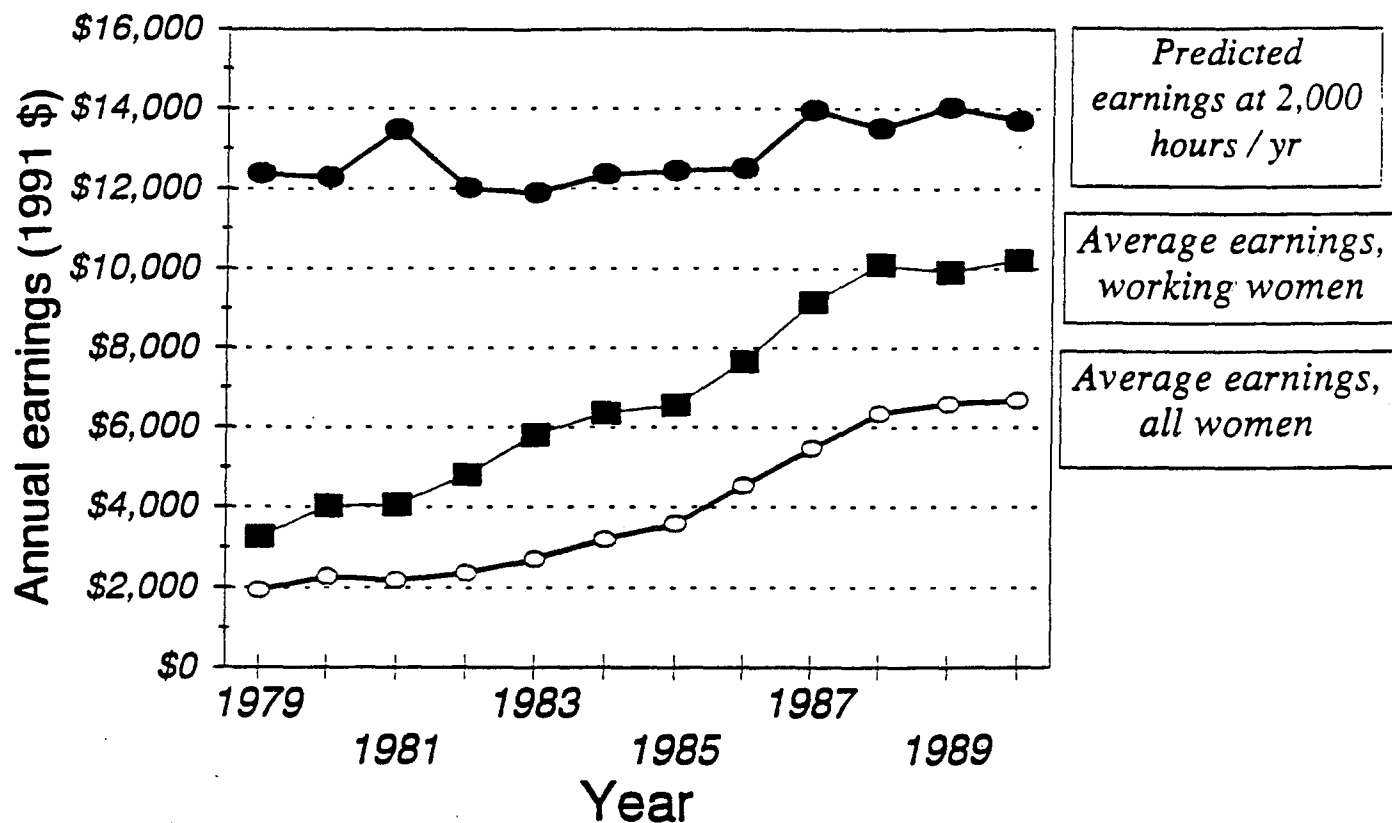
Percent

CHARACTERISTIC	MARCH 1979	1986	1991
Ages of children			
Under 3	18.9	21.0	24.8
3 to 5	17.5	21.1	21.4
6 to 11	33.0	32.4	32.6
12 and over	29.8	24.3	21.4
Education of mother			
8th grade or less*	18.2	11.9	11.2
1-3 years high school*	39.8	35.5	35.1
4 years high school*	36.0	42.9	40.7
Some college*	5.2	8.4	12.2
College graduate*	0.8	1.2	0.8
Unknown	47.8	59.7	49.9
Mother's employment status			
Full-time job	8.7	1.6	2.2
Part-time job	5.4	4.2	4.2
Cases with reported earnings			
	12.8	7.5	7.9

* Percentage distribution among mothers whose educational attainment is known.

Source: Committee on Ways and Means, *1993 Green Book*, pp. 696-97.

Figure 1.
Actual and Predicted Earnings among
Women Who Received AFDC in 1979-81



Source: Author's tabulations of NLSY.

ALTERNATIVES TO WELFARE INCOME: THE EITC

John Karl Scholz, Associate Professor of Economics, University of Wisconsin-Madison

As its name suggests, the earned income tax credit (EITC) is a credit on the federal income tax available to working poor families with children. In 1995 the credit equals 34 percent of earned income (wages, salaries, self-employment income, and farm income) for taxpayers with one child, up to an earned income of \$6,000; hence, the maximum benefit is \$2,040 (34 percent of \$6,000) for families with one child. Taxpayers with one child and incomes above \$6,000 but below \$11,000 receive the maximum benefit. Taxpayers with one child whose incomes exceed \$11,000 are in the phase-out range of the credit: their \$2,040 credit is reduced by 16 cents for every dollar of income earned over and above \$11,000. Taxpayers with two or more children are entitled to a larger credit (36 percent of earnings up to \$8,455, for a maximum credit of \$3,033). Credit parameters are summarized in Table 1. Unlike most credits and deductions in the federal individual income tax system, the EITC is refundable—that is, if the amount of the credit exceeds what the taxpayer owes, he or she receives a payment from the U.S. Treasury for the difference.

The earned income tax credit (EITC) plays a central role in policy affecting the working poor. Over the past 20 years a striking change has occurred at the lower end of the nation's earnings distribution. In 1973, the average man lacking a high school diploma earned \$24,079 (in 1989 dollars); by 1989 his counterpart earned \$14,439. The trend is nearly as dramatic for men with only a high school degree (comparable figures for women are more difficult to obtain because of the striking increase in women's labor force participation). The erosion of labor market opportunities for people with low levels of education has placed enormous strain on the nation's antipoverty programs. Against this backdrop, the EITC has provided an important supplement to the earnings of low-skill workers.

A family receives the EITC by filing a tax return, but many low-income families are not legally required to file returns. A married couple with two children, for example, was required to file a tax return in 1994 only if they had income above \$16,150, although with an income considerably less than that, the couple would be entitled to an EITC of over \$3,000. If the EITC is to be successful at meeting the objective of "making work pay," families who are eligible for the credit should receive it. The best available evidence suggests that this indeed happens, to a large extent, because the EITC participation rate is around 80 to 86 percent.

The participation rate of the credit is strikingly high when compared to the AFDC and food stamp participation rates. The United Kingdom has an EITC-like program called the Family Credit, administered through the transfer system and directed toward families with children. Official estimates place the participation rate of the Family Credit at only around 50 percent. Thus, both compared to other in-kind transfers in the U.S. and comparable work-related benefits in the United Kingdom, the EITC gets high marks for reaching those who are eligible for the benefit.

Labor Market Effects: Does the EITC Discourage or Encourage Work?

The EITC has different labor supply incentives depending on the taxpayer's income relative to the subsidy, flat, or phase-out range of the credit. The subsidy, or phase-in, range of the credit provides mixed incentives to work. The flat and the phase-out ranges provide an unambiguous incentive to reduce hours of work, and most EITC recipients are in those ranges, which raises the concern that the EITC may lead to a net reduction in the work effort of low-income workers.

Although, in aggregate, the credit is likely to reduce the hours worked by workers, the economic significance of these effects is small. The estimates that I deem most reliable suggest that the average reduction in hours worked will be around 11 per year. This average reflects a mixture of

a 38-hour per year increase for households in the phase-in range of the credit and a 3- and 21-hour per year reduction for households in the flat and phase-out range, respectively. Moreover, to the extent that taxpayers are unaware of the effects of the credit on after-tax wages, both the positive effects of the credit in the subsidy range and the negative effects of the credit on taxpayers in the phase-out range are overstated. In sum, the best available empirical evidence suggests that the EITC has a small, but detrimental, effect on the hours of workers.

The credit exerts unambiguously positive labor market incentives on the decision of whether or not to work. These effects can be important, as there is widespread agreement among economists that the strongest effects of wages, and hence of the EITC, are on labor force participation, rather than on hours worked.

The empirical work on this topic shows that net wages positively affect labor market participation and negatively affect public assistance participation, particularly among single parents. This increase in participation is likely to offset (or more than offset) the reduction in hours worked. So the evidence suggests that the EITC probably will increase the hours worked by low-income people, but the positive effect is likely to be small. At the same time, the modest positive labor market effects of the EITC should be contrasted to the detrimental effects on both labor market participation and hours of work associated with other income transfer programs.

The Antipoverty Effectiveness of the EITC

Table 2 presents evidence on the "target efficiency" of the EITC prior to, and the changed EITC resulting from, OBRA93, once the new law is fully phased in. Under both policies more taxpayers with incomes above the poverty line than below the poverty line are eligible to receive EITC payments, but because of the progressive benefit structure of the EITC, roughly half the credit payments go to households with incomes below the poverty line. The new law increases substantially the credit payments going to taxpayers with incomes above the poverty line, primarily as a consequence of extending the break-even level of income to \$27,000 from \$23,760 for taxpayers with two or more children. It increases by over 33 percent the number of taxpayers with incomes below the poverty line who will be eligible for the EITC, primarily as a consequence of extending the credit to low-income, childless taxpayers between the ages of 25 and 65. Under current law roughly \$5.6 billion of total EITC payments help close the "poverty gap"—the difference between total cash income and the poverty line.¹ Under the new law \$6.4 billion of EITC payments close the poverty gap. However, because the new law sharply increases overall expenditures on the credit, one measure of target efficiency—the fraction of total EITC payments that directly reduce the poverty gap—falls to 36 percent from 47 percent.

Compliance Issues

In past years a large number of ineligible taxpayers claimed the EITC, according to unpublished data from the IRS Taxpayer Compliance Measurement Program (TCMP). In 1988 10.4 million taxpayers claimed the EITC, whereas the TCMP for that year estimates that only 7.1 million people were entitled to the credit, meaning that over 30 percent of EITC claimants were ineligible. Of the \$5.6 billion in EITC claims, the 1988 TCMP estimates that nearly \$2 billion (33.6 percent) were claimed inappropriately. A General Accounting Office official testified in 1993 that "the credit has been the source of more taxpayer mistakes than any other individual income tax provision."

¹This reduction in the poverty gap will not be reflected in official government statistics, as the EITC is not included in the most widely publicized pretax, post-transfer income concept used to measure poverty.

The future viability of the EITC depends on the ability of the IRS to reduce noncompliance. Doing so requires two distinct tasks. First, programs must be put in place to detect accurately and report the degree of noncompliance and its causes. Current policy is being debated in an environment where solid evidence concerning the magnitude of compliance problems is scanty. Without credible numbers on EITC noncompliance and evidence about the source of noncompliance, it is difficult to design policy to address the problem.

The Internal Revenue Service has now taken the second step needed to address noncompliance: giving greater scrutiny to verifiable items on tax returns. The IRS has created an uproar this year due to refund delays as it reviews social security numbers more closely. Nevertheless, this effort, together with matching employee and employer W-2 reports, seem to be the best way of combatting the noncompliance that jeopardizes the program. As long as the credit is based on items the IRS is able to verify, there is nothing inherent in the credit that would lead to unusually high levels of noncompliance. Moreover, other areas of the tax code, for example Schedule C, also have large amounts of noncompliance associated with them. As a matter of sound policy, the costs of reducing noncompliance in every aspect of the tax code should be compared to its benefits, so the IRS uses taxpayer resources in as efficient a way as possible.

Additional Policy Considerations before Congress

Congressional staff have offered several proposals that could enhance the targeting of the credit. I have two brief comments on various proposals. First, the EITC is already well-targeted to low-wage workers. For example, more than 75 percent of EITC benefits go to taxpayers with wages that would place them in the bottom 25 percent of the wage distribution for all workers with children (below \$7.30 per hour). More than 95 percent of all EITC benefits are paid to workers with wages below the median of \$11.11 per hour. This "target efficiency" accounts for much of the appeal of the EITC.

Second, the Administration has introduced a proposal to deny the EITC to taxpayers with assets (based on dividend and interest income) above some threshold. This proposal would be relatively straightforward to administer and consequently could, in an effective manner, enhance the targeting of the EITC. I would not oppose such a proposal, though two things should be kept in mind when debating it. First, it will be relatively easy to manipulate portfolios so as to avoid the asset income thresholds without altering the value of the portfolio. Hence, the asset test will in all likelihood exclude fewer families than expected. Second, it may be counterproductive to implement a very restrictive asset test. While asset tests of any kind enhance targeting in a static sense, they also can make it nearly impossible for recipients to legally accumulate the assets necessary to take a wide range of choices leading to greater independence—helping a child attend college, acquiring additional training, or moving away from a dangerous neighborhood. Just as with high tax rates on labor earnings, asset tests can exert perverse incentives on low-income households and hence may reduce the efficiency of antipoverty policy.

Third, the Administration has announced its interest in increasing the minimum wage. By 1996, when the 1993 expansion of the EITC is fully phased in, the EITC will raise the effective minimum wage for a low-income taxpayer with two or more children to \$5.95 an hour (the comparable figure for taxpayers with one child is \$5.70). Economists have traditionally been concerned that increases in the minimum wage reduces employment of low-skilled workers, though this view has been challenged in some recent research. The EITC will not reduce employment of the lowest-skilled workers. The EITC is also more tightly targeted to low-income workers than the minimum wage, which also benefits earnings of secondary workers and teenagers from affluent families. Increasing the minimum wage may supplement the incomes of low-skilled workers in a

more timely fashion than the EITC, however, as most taxpayers receive the EITC in a single annual lump-sum payment, rather than incrementally throughout the year.

The erosion of the bottom of the nation's labor market imposes a pressing policy problem. The EITC is a sensible, well-targeted policy to address the problem. The credit is threatened by noncompliance. I now sense that the Internal Revenue Service is taking strong steps to attack this problem. Their efforts should be given time to work. The reason for this is that in other respects the credit is working well: (i) a high fraction of eligible taxpayers receive the credit, (ii) its labor market effects are probably, in aggregate, beneficial, and without a doubt, they are less pernicious than alternative ways of assisting the working poor, (iii) the credit is well-targeted toward poor and near-poor families, and (iv) families receiving the EITC are working, an action that, in my opinion, should be encouraged.

TABLE 1

EITC Parameters under Law Prior to OBRA93 and under OBRA93, Selected Years (figures for 1994 and beyond are in 1994 dollars)

	Credit Rate	Flat Range		Max. Credit	Phase-out Range	
		Beginning Income	Ending Income		Phase-out Rate	Income Cutoff
Prior Law						
1990 (1990 \$)						
All taxpayers	14%	\$6,810	\$10,730	\$953	10%	\$20,264
1993 (1993 \$)						
1 qualified child	18.5	7,750	12,200	1,434	13.21	23,050
2+ qualified children	19.5	7,750	12,200	1,511	13.93	23,050
Young child ^a	5	7,750	12,200	388	3.57	23,050
Health credit ^b	6	7,750	12,200	465	4.285	23,050
1994 and after						
1 qualified child	23	7,990	12,680	1,838	16.43	23,760
2+ qualified children	25	7,990	12,680	1,998	17.86	23,760
Young child ^a	5	7,990	12,680	400	3.67	23,760
Health credit ^b	6	7,990	12,680	479	4.285	23,760
Omnibus Budget Reconciliation Act of 1993 (OBRA93)						
1994						
1 child	26.3	7,750	11,000	2,038	15.98	23,760
2+ children	30.0	8,425	11,000	2,528	17.68	25,300
No qualifying child ^c	7.65	4,000	5,000	306	7.65	9,000
1995						
1 child	34.0	6,000	11,000	2,040	15.98	23,760
2+ children	36.0	8,425	11,000	3,033	20.22	26,000
No qualifying child ^c	7.65	4,000	5,000	306	7.65	9,000

TABLE 1, continued

	Credit Rate	Flat Range		Max. Credit	Phase-out Range	
		Beginning Income	Ending Income		Phase-out Rate	Income Cutoff
1996 and beyond						
1 child	34.0	6,000	11,000	2,040	15.98	23,760
2+ children	40.0	8,425	11,000	3,370	21.06	27,000
No qualifying child ^c	7.65	4,000	5,000	306	7.65	9,000

Source: Figures for the August 1993 budget agreement (OBRA93) were kindly provided by Janet Holtzblatt at the Office of Tax Analysis, U.S. Department of Treasury. The other figures are from U.S. House of Representatives (1993).

^aThe young child (or "wee tots") credit was for taxpayers who had a child under the age of one in the tax year and incomes in the ranges designated in the table.

^bThe supplemental health insurance credit goes to taxpayers with incomes in the range designated in the table who paid health insurance premiums that include coverage for one or more qualifying children. The taxpayer cannot take advantage of the supplemental health insurance credit on expenses used for the medical expense deduction or health insurance deduction for the self-employed (and vice versa).

^cThe taxpayer must be between the ages of 25 and 65.

TABLE 2

**Antipoverty Effectiveness of the EITC under the Law Prior to OBRA93
and under OBRA93 When Fully Phased in by 1996^a**

	Prior Law ^b	OBRA93 ^c
EITC-eligible taxpayers with incomes above the poverty line (millions)	6.211	7.582
EITC payments to these households (millions \$)	\$6,224	\$8,994
EITC-eligible taxpayers with incomes below the poverty line (millions)	4.084	5.451
EITC payments to these households (millions \$)	\$5,820	\$9,020
Pre-EITC poverty gap ^d	\$20,156	\$23,982
Post-EITC poverty gap	\$14,544	\$17,574
Number of households taken out of poverty by the EITC	0.909	1.380

Source: 1990 Survey of Income and Program Participation.

^aAll dollar amounts are given in 1994 dollars. 1990 SIPP data are converted to 1994 dollars assuming a 3 percent rate of inflation. Thus, the table shows the effect of the 1996 law (pre- and post-OBRA93), applied to the 1990 population, where dollars amounts are given in 1994 dollars. The fact that the population size is held constant at 1990 levels accounts for the smaller 1996 EITC expenditure than what is given in the Budget.

^bPrior law calls for a 23 (25) percent EITC subsidy for one (two) children households with earned income under \$7,990 in 1994. The credit is the maximum amount for earned income between \$7,990 and \$12,680. The credit is phased out at a rate of 16.43 (17.86) percent for incomes between \$12,680 and \$23,760.

^cOBRA93 (see Table 1) adds a 7.65 percent credit for childless taxpayers between the ages 25 and 65 with earned income below \$4,000, a 34.0 percent credit for one-child taxpayers with earned income below \$6,000, and a 40.0 percent credit for taxpayers with two or more children with earned income below \$8,425. The flat range of the schedule stops at \$5,000 for childless taxpayers and \$11,000 for taxpayers with one or more children. The phase-out rates are 7.65 percent, 15.98 percent, and 21.06 percent, so the credit is fully phased out at \$9,000, \$23,760, and \$27,000.

^dThe poverty gap is defined as the difference between cash income (the sum of earnings, dividends, interest, social security, public assistance, SSI, veterans payments, pensions, unemployment, and alimony) and the poverty line.

The Current Child Support System—Status, Problems, and Prospects

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Substantial policy attention has been paid to the child support system in the last 20 years, and a new round of reforms has recently passed the House. I will describe the current system, discuss what research tells us on whether the system is working, and close with discussion of potential policy changes that might make it more effective.

The Current System

I structure the description by dividing the child support system into three components:

1. whether custodial parents receive a child support order;
2. the level of the order, both initially and over time;
3. whether the order is collected.

Whether custodial parents receive a child support order. National data from 1990 (U.S. Bureau of the Census, 1991) show that between 75 percent and 80 percent of divorced and remarried custodial mothers have orders. Only about half of all separated mothers have orders, but for many of them the lack is a temporary problem because their separation is fairly recent. The percentage is much lower for never-married women, about one-quarter of whom have orders, and is also much lower for custodial fathers, who comprise about 10–15 percent of custodial parents (Meyer & Garasky, 1993). AFDC recipients are generally no less likely to have an order than nonrecipients, once other characteristics are taken into consideration.

Most of the recent policy attention has been focused on increasing the percentage of never-married women who have orders, and indeed the percentage of those women who have orders more than doubled from 1978 to 1989 (U.S. Bureau of the Census, 1991; Sonenstein et al., 1994). Establishing paternity is the first step toward gaining a child support order, and historically the lack of paternity establishment has been a major reason that never-married women fare so poorly in the child support system.

The Family Support Act of 1988 set performance standards for the states in their rates of paternity establishment. The first estimates showed that the paternity establishment rates varied dramatically across states and sometimes within states (Sonenstein et al., 1994). Recent reforms seek to make paternity establishment easier and more automatic, and the House bill continues this thrust.

The level of child support orders. As a result of the Family Support Act, each state has established a numerical guideline that is to be used to determine the child support order in each case, unless found to be inappropriate. Data from Wisconsin show that guidelines make orders much more consistent across families (Meyer et al., 1994). Data from several states show small increases in the level of initial orders as a result of guidelines (Williams, 1994). However, the variation across states in required order amounts is fairly high, especially for low-income families (Pirog-Good, 1993). Other problems are that the guidelines are still not fully implemented (Meyer et al., 1994), and substantial disagreement exists on the type of guideline that is most appropriate (see Williams, 1994).

Perhaps more important, orders do not keep pace with changing circumstances. Welfare cases are required to be reviewed every three years to see if they can be updated, but this process is

somewhat cumbersome. State experiments found that only about one-fourth of the orders are changed, but the ones that are changed show dramatic increases (averaging \$100/month) (Meyer et al., 1994). Nonwelfare cases are to be given the opportunity to have their orders reviewed every three years, but few take advantage of this.

Whether orders are collected. National data show that about half the orders are fully paid, about one-fourth are partially paid, and for about one-fourth nothing is paid. In all cases entering the system after January 1994, the child support order is supposed to be withheld from the income of the obligor as soon as the order is issued. Research on immediate withholding shows that this increases the percentage collected (Garfinkel & Klawitter, 1990). However, its effectiveness declines over time (Meyer et al., 1994), in part because we have a hard time tracking obligors when they change jobs. Other problems include differential use of immediate withholding across states and even within states (Meyer et al., 1994) and obligors who are self-employed or do not have earnings.

Putting all three factors together, could we collect more child support? Research suggests that we could collect substantially more. A recent estimate by Elaine Sorensen of the Urban Institute (1995) suggested that a perfect child support system would collect \$48 billion annually, compared to the \$14 billion we are currently collecting, or a "gap" of \$34 billion.

Who is not paying, and what could be done about it?

There clearly are obligors who are not paying their current orders. Sorensen (1995) estimates that non-payment of current orders accounts for 21% of the gap between what is currently paid and what could be paid. Part of this problem lies in obligors who could pay but do not. Immediate withholding of child support orders from wages could decrease the number of nonpayers if withholding orders were issued in every case and if they followed obligors when they changed jobs. A national registry of new hires (a part of the House Bill) is clearly a step in the right direction, as is a national registry of child support orders (also in the House bill), which should help with problematic interstate cases. But part of the problem for some groups is also a lack of ability to pay. One of these groups includes fathers in paternity cases, who some argue do not earn much and will not ever earn much. Research evidence here is mixed. Some recent findings show that even if these fathers do not have much income at the time paternity is established, many of them experience dramatic income increases over time, and much more could be collected (Phillips & Garfinkel, 1993; Meyer, 1995). Other research shows that a sizable group of the nonmarital fathers who are not paying have incomes below the poverty line (Bartfeld & Meyer, 1994). Perhaps we need to think about strategies for increasing the earnings potential of some nonresident parents so that they can support their children.

The House bill adds new penalties for failure to pay child support, including a new limitation that an individual with unpaid child support cannot receive food stamps. The merit of this provision depends on whether the problem of nonpayment is related to willingness to pay or ability. If the obligor is able to pay, new sanctions could be appropriate. But if the problem lies in the very low incomes of the obligors, then perhaps not allowing them to receive food stamps may make them more destitute. I believe further research is needed in this area.

Another group consists of those who are paying the amount ordered, but the order is quite low; for some of these obligors the order does not reflect their current circumstances. Sorensen's

estimate (1995) is that 21% of the gap between what is paid and what could be paid is due to orders that are too low. Her research and other recent research shows that moderate-income and high-income fathers have very low orders and could afford to be paying more, and should be asked to pay more under almost all guidelines currently in use. Clearly, full implementation of the guidelines is important. But perhaps a larger problem is that orders do not remain current; we need to look for ways to make the updating of orders much more automatic.

A third group not paying contains those without orders, primarily paternity cases. Cases without orders result in the final 58% of the gap between what is paid and what could be (Sorensen, 1995). Current law requires that AFDC recipients cooperate with the child support office as they attempt to establish paternity. One incentive to establish paternity among AFDC recipients has been to permit them to keep up to \$50/month of any child support that would be paid. The House bill deletes this provision, thus limiting this incentive to cooperate and replacing it with a more punitive approach. It penalizes recipients who do not have paternity established, even if they are cooperating fully with the child support agency. This is of particular concern: if a mother is cooperating fully, why should she bear costs for the state's difficulties in establishing paternity? While there is little recent research, one study found that in the late 1980s in Arizona, paternity establishment among AFDC recipients took from 9 to 16 months (Nichols-Casebolt, 1992).

Finally, I would like to comment on the interaction of the child support and welfare systems. Consider a father working full-time, full-year at \$5.00/hour. If he had two children, his child support order in Wisconsin would be about \$220/month. (Of course, if he were working less, this number would be smaller, and there is no guarantee that he would pay the full amount.) But even if he did pay the full amount, the amount paid would be less than half the AFDC grant that a Wisconsin mother of two children would receive (\$517). Thus perhaps it is not surprising that research has shown that the amounts of child support typically received by welfare recipients in Wisconsin are not associated with an increased likelihood of leaving AFDC. However, research has shown that typical amounts of child support (even small amounts of child support) decrease the likelihood of returning to welfare once a woman has left the rolls (Meyer, 1993).

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THE LIMITS OF PRIVATE CHILD SUPPORT AND THE ROLE OF AN ASSURED BENEFIT

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Strengthening public enforcement of private child support is good public policy because it will increase the economic security of children eligible for child support, will reduce dependence on welfare, and will reinforce the widely shared value of parental responsibility. But there are limits to what private child support enforcement can accomplish.

If we achieved perfection in enforcement—that is, if child support awards were established in all cases, the awards were equal to the Wisconsin percentage-of-income standard (17 percent of the nonresident parent's income for one child, 25 percent, 29 percent, 31 percent, and 34 percent for two, three, four, and five or more children), and 100 percent of all obligations were collected—we would reduce the poverty gap for children potentially eligible for child support by 24 percent and AFDC caseloads by 20 percent. That still leaves 76 percent of the poverty gap and 80 percent of welfare caseloads.

Moreover, perfection is unlikely to be achieved in our lifetimes. More realistically, if child support award rates and collection rates improved halfway between current performance and perfection and award levels were established and updated to the Wisconsin guideline, as depicted in the last panel labeled intermediate run in Table 1, the poverty gap would be reduced by 12 percent and AFDC caseloads by 9 percent.

Private enforcement is limited by the ability of nonresident fathers to pay support. Reversing the trend of declining earnings for working-class males described by Professor Haveman will increase the efficacy of child support enforcement. We should reverse that trend. But even if the earnings of the lower 50 percent of males on the earnings scale had kept pace with the earnings increases of the top 20 percent, the efficacy of enforcement would probably improve by no more than 50 percent.

The limits of private child support enforcement create a case for an assured child support benefit, the third component of a new system of child support assurance. Under child support assurance, child support awards are set by a legislated formula—based on a percentage of the nonresident parent's income—and payments are deducted from the absent parent's earnings, just like social security deductions. The government guarantees a minimum level of child support to all children legally entitled to private child support—an Assured Benefit. The Assured Benefit is financed from welfare savings and from a very small addition to the social security payroll tax.

Like Survivors' Insurance, child support assurance aids children of all income classes who suffer an income loss due to the absence of a parent. Survivors' Insurance compensates for the loss of income arising from widowhood. Child support assurance compensates for the loss arising from divorce, separation, and nonmarriage. Withholding a flat percentage of the nonresident parent's income makes the bulk of the financing of child support assurance similar to a proportional payroll tax, which is used to finance all of our social insurance programs. In the child support assurance case, however, the "tax" applies only to those who are legally liable for child support. The assured-benefit component of child support assurance makes the benefit structure of the system like all other social insurance programs in that it provides greater benefits to low-income families than are justified on the basis of the family's contributions or taxes.

Like other social insurance programs, child support assurance is based on a partnership of responsibility between parents and government. Parents are responsible for sharing income with their children. Government is responsible for enforcing private support and for insuring a steady flow of income to all children with a nonresident parent.

The 1984 Child Support Enforcement Act and the 1988 Family Support Act took giant strides on the collection side toward a new system of child support assurance by requiring states to adopt numerical child support guidelines for determining child support awards and universal wage withholding of child support obligations. Congress took very small strides on the benefit side in 1984 and 1988, directing the Secretary of DHSS to grant waivers to Wisconsin and New York permitting use of federal funds that would otherwise have been devoted to AFDC to support a version of an assured child support benefit. Two bipartisan national commissions, one on children, the other on Interstate Child Support Enforcement, as well as the Republican House Wednesday group welfare reform plan and President Clinton's welfare reform plan, all propose federally financed state demonstrations of an assured benefit. Although Representatives Roukema (H.R. 195) and Kennelly (H.R. 95) have proposed demonstrations, the House Republican welfare reform bill does not contain federal funding for child support assurance demonstrations. Senators Dodd and Rockefeller (S. 642) have reintroduced legislation calling for assured benefit demonstrations. The rest of my comments focus on the benefits and costs of an assured benefit.

An assured benefit promotes economic security. Because many nonresident fathers have low and irregular incomes, their private child support payments, at best, will be low and irregular. An assured benefit sets a secure floor under payments.

Because child support assurance is available to all families legally entitled to support, irrespective of income, it prevents poverty and dependence on welfare. Families need not become impoverished to qualify. As illustrated in the last panel of Table 1, the intermediate improvement in enforcement of private child support by itself reduces the poverty gap by 12 percent and AFDC caseloads by 9 percent. In conjunction with an assured benefit of \$3000 for the first child, the poverty gap is reduced by 24 percent and AFDC caseloads by nearly one-third.

Compared to AFDC, which is a substitute for earnings because it is so highly income tested, an assured benefit complements work, because the benefit is not reduced as earnings increase.

An assured benefit also increases the incentive to establish paternity. To qualify for an assured benefit, the child must be legally entitled to receive private support, which in the case of out-of-wedlock birth presupposes paternity establishment. Paternity establishment is a critical weak link in private child support enforcement.

Finally, an assured benefit is an equitable method of reinvesting the savings in welfare costs that arise out of improved enforcement of private child support obligations. If the welfare savings are used to reduce taxes, improved enforcement redistributes money from low-income nonresident fathers to middle- and upper-income taxpayers. Using these savings to help finance an assured benefit will reinvest the savings in low-income communities in a form that promotes work and parental responsibility.

Of course, an assured benefit also has costs. As the last panel of Table 1 indicates, the cost of the assured benefit alone would be equal to \$3.2 billion. The net cost of the child support assurance

system as a whole (the collection as well as the benefit side) would be only \$2.1 billion because improvements in collections save \$1.1 billion.

How can a government program not limited to poor families be so cheap?

First, the collection-side aspects of child support assurance save money. Second, despite the fact that it insures children of all income classes, the assured benefit per se is not very costly. Men and women tend to mate with people from the same sort of backgrounds. This assortative mating guarantees that only a small proportion of government expenditure for the assured benefit will go to a child living with a wealthy parent, because in the overwhelming majority of such cases, the nonresident parent will be equally wealthy and there will be no public subsidy. In rare cases, of course, there will be a poor nonresident parent of a child residing with a wealthy parent. Counting the public portion of the assured benefit for income tax purposes substantially reduces this already small leakage.

To date, the only American jurisdiction to conduct a major trial of a version of an assured child support benefit is New York State. The New York Child Assistance Program (CAP) limits the assured benefit to families that qualify for welfare, provides intensive social services along with the assured benefit, and includes no attempts to strengthen private child support enforcement. Experimental findings include increases in family income, work, and private child support awards, decreases in welfare dependence and costs, and no improvements in support payments. The cost savings are growing over time. Some, indeed possibly all, of the benefits may be attributable to the social services rather than the assured benefit. Moreover, limiting the assured benefit to the poor undermines the principle of universality that is critical to preventing poverty and dependence on welfare.

A non-income-tested assured benefit will cost more in benefits than the New York CAP program. But it will also cost much less to administer than the CAP version. Indeed, the administrative costs of a universal assured benefit will be quite small. Once income withholding is fully implemented and states or the federal government receive and disburse all child support payments, the additional costs of administering an assured benefit will consist primarily of modifying computerized record-keeping systems.

An assured benefit creates adverse incentives with respect to paying support and marriage. Nonresident parents who would pay less than the assured benefit and are motivated to pay out of concern for their children will lose this motive, because their children are guaranteed the support whether they pay or not. Because the assured benefit is available only to families with a nonresident parent, it subsidizes marital splits. Improved enforcement may dominate any adverse incentive to pay, however, and it is possible to design an assured benefit that rewards private payments of support. Moreover, evidence from studies of the effects of welfare on marriage suggest that adverse effects on marriage will be small.

The potentially adverse effects provide a rationale for limiting the generosity of the assured benefit. They also provide another rationale for beginning its implementation with state demonstrations. The major rationale, however, is to test whether in practice the costs are as small and the benefits as low as the micro-simulation estimates suggest, and to gain practical experience.

TABLE 1

**Estimated Benefits and Costs of a National Child
Support Assurance System over Time, in 1985 Dollars**

Assured Benefit Level ^a	Reduction in Poverty Gap (%)	Reduction in AFDC Cases (%)	Net Cost (in Billions)
Perfect System			
0	24	20	-2.7
1,000	25	23	-2.5
2,000	30	33	-1.4
3,000	40	49	+0.7
Short Run I^b			
0	0	0	+0.0
1,000	2	3	+0.5
2,000	5	8	+2.1
3,000	9	14	+4.7
Short Run II^c			
0	2	2	-0.1
1,000	3	4	+0.1
2,000	5	8	+0.9
3,000	9	14	+2.7
Intermediate Run^d			
0	12	9	-1.1
1,000	13	12	-0.8
2,000	17	20	+0.1
3,000	24	32	+2.1

^aThe benefits are those for the first child. In all other plans, the benefits for the second and third child are \$1,000 each, and \$500 each for the fourth, fifth, and sixth child.

^bNo increase in child support award rates, award levels, or payment rates.

^cAwards now set according to Wisconsin standard; no change in award rates or payment rates.

^dAward rates and collection rates halfway between current levels and perfection; award levels equal to the Wisconsin standard.

APPENDIX

**Testimony before the
Senate Committee on Governmental Affairs**

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Wednesday, April 5, 1995

Mr Chairman and Members of the Committee:

Thank you for inviting me to testify on the effectiveness and design of the earned income tax credit (EITC). The EITC plays a central role in policy as it affects the working poor. Over its history, the EITC has received strong bipartisan support, as reflected by the fact that it was increased sharply in 1990, under President George Bush, and again in 1993, by President Bill Clinton. The real value (in 1993 dollars) of the maximum EITC varied between \$739 and \$1,068 between 1975 – the year the EITC was adopted – and 1990. By 1996 the real value of the EITC will be roughly three times its 1990 level as a consequence of the 1990 and 1993 legislative changes.

The effectiveness of the EITC depends on (i) whether or not people eligible for the credit actually receive it, (ii) the labor market effects of the policy, and (iii) ensuring that those not eligible for the credit do not receive benefits. The first part of my testimony focusses on these aspects of policy design. The final section discusses a variety of EITC-related policy options.

Labor markets for low-skilled workers in the U.S.

To understand the role of the EITC, and in particular, its charmed existence over the past 20 years, a couple of facts about the labor market for low-skilled workers in the U.S. are useful. As Table 1 shows (next page), there has been a striking change in the bottom of the nation's earnings distribution, beginning in the 1970s, but accelerating over the 1980s. In 1973, the median male without a high school diploma earned \$24,079 (in 1989 dollars), by 1989 the median worker with the same level of education earned \$14,439. The trend is nearly as dramatic for males with only a high school degree. In 1973, the median male had an income of \$30,252, by 1989 the median male with a high school degree had an income of \$21,650. Average hourly earnings in private nonagriculture industries peaked in 1973 at \$8.55 per hours (in 1982 dollars) and, in 1994 was \$7.40 per hour. The erosion of labor market opportunities for people with low levels of education has placed enormous strain on the nation's antipoverty programs. Against this backdrop, the EITC has provided an important supplement to the earnings of low-skill workers.

The participation rate of the credit

A family receives the EITC by filing a tax return, but many low-income families are not legally required to file returns. A married couple with two children, for example, was required to file a tax return in 1994 only if they had income above \$16,150, though with an income considerably less than

that, the couple would be entitled to an EITC of over \$3,000. If the EITC is to be successful at meeting the objective of "making work pay," families who are eligible for the credit should receive it.

Table 1: Median Income of Persons 25 and Over, by Educational Attainment and Gender, Selected years, 1989 Dollars

Year	Males		
	High School		College
	1-3 Years	4 Years	4+ Years
1967	\$22,858	\$26,894	\$39,186
1970	23,442	28,034	40,527
1973	24,079	30,252	41,065
1979	18,697	26,416	36,626
1983	15,138	21,932	35,188
1989	14,439	21,650	37,553

Source: Robert Haveman and John Karl Scholz, "Transfers, Taxes, and Welfare Reform," National Tax Journal, June, 1994, 417-434

It is surprisingly difficult to estimate the percentage of EITC-eligible taxpayers who receive the credit – the EITC participation rate. Household surveys generally collect the information needed to determine eligibility but do not provide information on EITC reciprocity. Tax data are best for estimating EITC reciprocity, but not all households file tax returns so they are unsuited for estimating EITC eligibility. In an earlier paper I used unique data that allowed me to determine EITC eligibility and EITC reciprocity in the same data set: specifically, I use data from the 1990 Survey of Income and Program Participation (SIPP) matched by social security number to selected items from individual income tax returns.² The paper describes, in great detail, the steps needed to calculate participation rates. Of the roughly 10 million taxpayers eligible for the credit in 1990, I estimate that between 75 to 90 percent received the credit. For reasons given in the paper, my preferred estimates place the participation rate at 80 to 86 percent.

The high participation (or take-up) rate of the credit is striking when compared to the AFDC participation rate of 62 to 72 percent and the food stamp participation rate of 54 to 66 percent.³ The

²For a more detailed discussion of participation rates, see John Karl Scholz, "The Earned Income Tax Credit: Participation, Compliance, and Anti-poverty Effectiveness," National Tax Journal, 47(1) (March, 1994): 59-81.

³These figures are calculated from the 1986 and 1987 panels of the Survey of Income and Program Participation (SIPP) by Rebecca M. Blank and Patricia Ruggles, in their paper "When Do Women Use AFDC and Food Stamps? The Dynamics of Eligibility Versus Participation," mimeo, Northwestern University and the Urban Institute, Washington, D.C., June, 1993.

United Kingdom has an EITC-like program called the Family Credit. It is administered through the transfer system and directed toward families with children. Official estimates place the participation rate of the Family Credit at around 50 percent. Thus, both compared to other in-kind transfers in the U.S. and comparable work-related benefits in the United Kingdom, the EITC gets high marks for reaching those who are eligible for the benefit.

The EITC's labor market incentives

The EITC has different labor supply incentives depending on the taxpayer's income relative to the subsidy, flat, or phase-out range of the credit. The subsidy range of the credit increases the worker's marginal return to labor. For taxpayers with incomes in the subsidy range, the wage subsidy is thought to encourage work. At the same time, the income supplement provided by the EITC is thought to decrease recipients' labor supply because more money in hand means that they will choose to work less. The net effect is ambiguous. Households in the flat range of the credit receive the maximum EITC payment and no marginal subsidy for increased work, so these households have no marginal incentive to increase their hours of work, and the EITC supplement provides incentive to work less. In the phase-out range, the EITC is reduced as additional income is earned, which is akin to an additional tax on earnings. Thus the additional tax and the additional income both encourage workers to decrease their hours of work. For households that are not working, it is hoped that the wage subsidy provided by the EITC will encourage participation in the labor market.

The aggregate labor market effects of the credit depend on the distribution of taxpayers within the credit's ranges and the degree to which they respond to incentives. In my National Tax Journal paper I estimate that 77 percent of EITC recipients will have incomes that fall in the flat or phase-out range of the credit in 1996, which raises the concern that the EITC may lead to a net reduction in the labor supplied by low-income workers. The fact that an incentive exists, however, does not necessarily mean that people act on the incentive in an economically significant manner. In the following sections I describe work performed with Stacy Dickert and Scott Houser on the likely effect of the EITC on labor market behavior.⁴

The effect of the EITC on hours of workers.

A large body of work in economics examines the effect of taxes and transfers on the hours worked by those in the labor market. Dickert, Houser and I survey this literature and use the empirical results from these studies to simulate the effects of the OBRA93 EITC expansions from 1993 to 1996.

Table 2, which is drawn from our paper, shows the effect of the 1993 EITC expansion, using 3 sets of labor supply estimates from studies using kinked budget sets because (i) they provide a consistent treatment of taxes and (ii) between the estimates of MaCurdy, Green, and Paarsch on the low end, and Hausman on the high end, the estimates appear to span the range of estimates found in the literature.

⁴The following discussion of the tax treatment of low-income households and the effects of the EITC on labor market participation and hours of work is described in more detail in Stacy Dickert, Scott Houser, and John Karl Scholz, "The Earned Income Tax Credit and Transfer Programs: A Study of Labor Market and Program Participation," Tax Policy and the Economy, James M. Poterba (ed.), National Bureau of Economic Research and the MIT Press, 1995.

As expected, we find that the EITC will reduce hours for every group except those in the subsidy range of the credit. Studies of labor supply find that secondary earners are more responsive to changes in taxes and wages than are primary earners. Accordingly, our estimated labor supply responses are larger for secondary-earners in two-parent families than they are for primary earners or single-parent families.

Table 2: Simulated Labor Supply Responses to Changes in EITC Law from 1993 to 1996

	Estimated Percent Change in Annual Hours Worked		
	Kinked budget set simulations ²		
	MaCurdy et al.	Triest	Hausman
All Recipients (160)	-0.09	-0.54	-4.04
By credit range			
Subsidy (80)	1.88	3.92	13.46
Flat (140)	-0.09	-0.19	-1.79
Phaseout (160)	-0.53	-1.11	-4.73
By marital status			
Husbands (180)	0.00	-0.34	-3.17
Wives (140)	-1.47	-3.03	-11.36
Single female heads (160)	-0.53	-1.11	-4.02
Single male heads (160)	0.00	-0.18	-1.56
By sex			
Male (180)	0.00	-0.34	-3.15
Female (160)	-0.57	-1.17	-4.33

Note: See Dickert, Houser, and Scholz (1995) (the complete citation is in footnote 3) for further detail. Median monthly hours are in parentheses.

Our reading of the literature suggests Triest's estimates most closely reflect consensus estimates from various branches of the literature. Triest's estimates imply that taxpayers in the subsidy range of the credit will increase hours by roughly 38 hours per year, while taxpayers in the flat and phaseout range will reduce hours by 3 and 21 hours per year, respectively. When aggregated, EITC recipients are estimated to reduce hours by an average of 11 per year. Hausman's estimates are roughly 8 times as large, while the MaCurdy et al. estimates show virtually no response. Our estimates are consistent with, but update earlier estimates from a 1993 study by the General Accounting Office.

While the credit, in aggregate, is likely to reduce the hours worked by workers, the economic significance of these effects is small. Moreover, to the extent that taxpayers are unaware of the effects of the credit on after-tax wages, both the positive effects of the credit in the subsidy range, and the

negative effects of the credit on taxpayers in the phase-out range, is overstated. Thus, the best available empirical evidence suggests that the EITC has a small, but detrimental, effect on the hours of workers.

The effect of the EITC on labor market participation

What's missing from the literature and our calculations from Table 2 are estimates of the EITC's effect on labor market participation. The credit has unambiguously positive labor market incentives on the decision of whether or not to work. Few papers provide guidance for thinking about the size of the effects of the EITC on labor market participation. This is somewhat surprising, as there is widespread agreement among economists that the strongest empirical labor market effects of wages and nonlabor income are on participation, rather than hours of work.

We identify the effects of the EITC on labor market participation by making use of the striking variation across states in the after-tax return to work.⁵ The typical low-income family in Texas, for example, faces relatively low cumulative tax rates – this calculation reflects both explicit tax rates from the federal income and payroll taxes, and implicit tax rates from benefit-reduction rules of food stamps and AFDC. Low tax rates are primarily a consequence of the low levels of AFDC benefits available to families in Texas. A household in similar circumstances in New York faces considerably higher rates, primarily because of the higher level of AFDC benefits. We find, for example, that average tax rates can exceed 85 percent for New York families receiving AFDC that enter the labor market and work anywhere from 8 to 35 hours per week. This implies that this family, when making labor market participation decisions, will receive no more than 15 cents for every dollar earned in the labor market over a broad range of hours. If tax rates affect labor market participation, we expect labor market participation to be higher in low-benefit states than in high-benefit states, holding other observable characteristics constant.

Our empirical work shows that net wages positively and significantly affect labor market participation and negatively affect transfer program participation, particularly for single parents. Moreover, this result is not an artifact of our particular empirical specification, but clearly emerges in the underlying data even when we do not control statistically for other factors. If we classify one-parent families by their predicted wage rate and then plot their probability of working, it appears, looking across wage groups, that the probability of working generally rises with wage rates. Even after crudely controlling for human capital by looking within wage categories, tax rates appear to exert a strong negative effect on the probability of labor force participation.

The empirical evidence on the effects of the OBRA93 EITC expansion on labor market behavior is summarized in Table 3. We model the effect the EITC increase on net-of-tax wages, and calculate the implied change in the probability that individuals work. At the mean, the EITC increases the net wage of single-parent families by 15 percent. This leads to a 6.2 percent increase in their probability of working. If each new labor market entrant works an average of 20 hours per week for 20 weeks a year, the hours of single parent families would increase by roughly 72 million hours per year. Similar

⁵We characterize this variation using a detailed, microsimulation model we have developed that uses monthly data for the 1990 calendar year drawn from the Survey of Income and Program Participation (SIPP). The model is coded in the computer language C, runs on a personal computer, and contains detailed modules for SSI, AFDC, food stamps, the federal income tax, state income taxes, and payroll taxes. See Dickert, Houser, and Scholz (1995) for further details.

calculations show that the annual hours of primary earners in two-parent families would increase by roughly 12 million hours.

Table 3: Labor Market and Transfer Program Effects of the OBRA93 EITC Expansion, 1993 to 1996

	New Labor Force Participants		Families in the Labor Market	
	Percent Change in Net Wage	Annual Hours Change Due to Labor Force Participation (million) ¹	Annual Hours Reductions of Workers (million) ²	Average Annual Reduction in Hours
Single Parents	15.0	72.8	26.4	10.1
Primary Wage Earners	19.6	12.1	13.6	7.7
Secondary Wage Earners	-5.0	-10.4	14.5	30.3
Total		74.4	54.5	11.2

Transfer Program Participation Effects

	Number Leaving Program	Mean Annual Benefit	Mean EITC Payment
Single-Parent Families	398,384	\$6,844	\$2,040
Two-Parent Families	117,757	\$4,702	\$2,842

Source: Dickert, Houser, and Scholz (1995).

¹The estimation of the change in hours from new labor force participation assumes that, on average, these persons work 20 hours per week for 20 weeks per year.

²We use the estimated net wage and virtual income elasticities from Triest (1990).

The EITC will probably discourage labor force participation of secondary workers in two-parent families, as entering the labor market is likely to place the family's income in the flat or phase-out range of the credit. Specifically, on average we calculate that the after-tax return to work for secondary earners will fall by nearly 5 percent as a consequence of OBRA93. We expect that to decrease labor market participation of secondary earners, leading to a reduction of roughly 10 million

hours when using the same assumptions as above. Thus, we estimate that the aggregate increase in hours generated by increased labor force participation would be roughly 74 million hours.

The increased hours resulting from higher rates of labor force participation can be compared to the reduction in hours caused by the credit shown in Table 2. We use Triest's (1990) labor supply parameters for the simulation. We estimate that the annual hours of work for single-parent families in our sample will fall by 26.4 million hours, for primary earners they will fall by 13.6 million hours, and for secondary earners they will fall by 14.5 million, leading to an aggregate reduction of 54.5 million hours.

Taken together, the simulations suggest that the aggregate reduction in hours supplied by working households, 54.5 million, would be more than fully offset if new labor force participants work an average of 20 hours per week, 20 weeks per year. If either hours, or weeks worked are lower the offset will be smaller, while if new labor market entrants work more than 400 hours a year, the aggregate effect will be a larger positive number. The important point, however, is that one cannot forget about the participation margin when thinking about the labor market effects of the EITC.

Our evidence, like other papers before us, show that labor market participation appears to be sensitive to changes in wages and taxes. Hence, a policy like the OBRA93 EITC expansions that substantially increases the after-tax return to working for those not in the labor market are likely to elicit greater labor market participation. This increase in participation is likely to offset (or more than offset) the reduction in hours among those who work. The modest positive labor market effects of the EITC should be contrasted to the detrimental effects on both labor market participation and hours of work associated with other income transfer programs.

Compliance Issues

In past years a large number of ineligible taxpayers claimed the EITC, according to unpublished data from the IRS's Taxpayer Compliance Measurement Program (TCMP). In 1988 10.4 million taxpayers claimed the EITC, whereas the TCMP for that year estimates that only 7.1 million were entitled to the credit, indicating that over 30 percent of EITC claimants were ineligible. Of the \$5.6 billion in EITC claims, the 1988 TCMP estimates that nearly \$2 billion (33.6 percent) were claimed inappropriately. A General Accounting Office official testified in 1993 that "the credit has been the source of more taxpayer mistakes than any other individual income tax provision."

EITC rules were changed in 1990 and a 2-page schedule was added to the tax forms because of the widespread perception of compliance problems, but there is little publicly-available evidence that the 1990 changes significantly reduced noncompliance. The IRS did a special study during last year's filing season, examining returns filed electronically during the first two weeks of the filing season, and found that roughly 30 percent of EITC claims were inappropriate. It is not clear that this number is representative of the universe of filers, and getting information on this whole general topic is very difficult, but the limited available evidence indicates that noncompliance is still a major problem. - -

Noncompliance takes many forms, though one of the frustrations with thinking about this topic is in assessing the relative importance of different circumstances. Parents that are separated (or even living together) may file separate returns and both claim the same child as a dependent. Taxpayers may make up children. Taxpayers may misreport earnings or AGI. Some of these cases may not reflect the intent to commit fraud, others clearly do.

The future viability of the EITC depends on the IRS being able to reduce EITC noncompliance. Doing so requires two distinct tasks. First, programs must be put in place to detect accurately and report the degree of noncompliance and its causes. Current policy is being debated in an environment where solid evidence on the magnitude of compliance problems is scanty. The IRS study for last year reported that 29 percent of EITC claimants requested too large a credit, and 13 percent appear to be intentionally inflating their claims. The press release for this hearing cited a 40 percent fraud rate. Without credible numbers of EITC noncompliance and evidence about the source of noncompliance, it is difficult to design policy to address the problem.

The Internal Revenue Service has, perhaps belatedly, taken the second step needed to address noncompliance. This involves giving greater scrutiny to verifiable items on tax returns. The IRS has created an uproar this year due to refund delays as they give social security numbers greater scrutiny. Nevertheless, this and matching employee and employer W-2 reports, seem to be the best ways of combatting the noncompliance that jeopardizes the program. As long as the credit is based on items the IRS is, in principle, able to verify, there is nothing inherent in the credit that would lead to unusually high levels of noncompliance. Moreover, other areas of the tax code, for example, Schedule C also have large amounts of noncompliance associated with them. As a matter of sound policy, the costs of reducing noncompliance in every aspect of the tax code should be compared to its benefits, so the IRS uses taxpayer resources in as efficient a way as possible.

Even if the IRS is able to perfectly verify social security numbers and wage and salary income, future compliance problems may arise with self-employment income. Between 1975 and 1990 the subsidy rate of the EITC was roughly the same as the combined employee and employer share of the payroll tax. In this period, as long as the payroll tax and EITC subsidy are about the same, taxpayers will not overstate self-employment income in order to increase their EITC. Doing so would increase the taxpayer's EITC but would obligate the taxpayer to pay social security taxes on the self-employment income, eliminating any advantage to falsely reporting income.

With the sharp increase in the EITC, there are now stronger incentives to manipulate income. A taxpayer who does not work and has two children could receive a payment from the IRS of \$3,370 in 1996 (in 1994 dollars) by reporting self-employment income of \$8,425 ($\$8,425 \times .40$). Doing so would require the taxpayer to pay \$1,289 ($\$8,425 \times .153$) in social security taxes, leaving a net benefit to the transaction of over \$2,000. The IRS is not well-equipped to uncover overreporting of incomes, and the payoffs to monitoring compliance in this area are certainly small relative to other areas of compliance. Of course, the taxpayer's claims need not be illegal. Two families could care for each other's children or watch each other's houses. They could exchange payments of \$8,425 for doing so and both receive a net benefit of more than \$2,000 if neither had any other sources of taxable income.

It is, of course, not yet clear how people will respond to these incentives to manipulate income, as there is no comparable situation in the tax code. My guess is that over time taxpayers or paid tax preparers will begin to take advantage of the incentive to overstate income in the subsidy range of the credit. The IRS will surely monitor closely the amount of income reported by low-income taxpayers that occurs in forms not subject to information-matching procedures (i.e., income from self-employment). An increase in the proportion of income occurring in these forms will be an early signal that a problem may be developing.

A solution to the potential problems associated with self-employment income would be to restrict the expanded EITC to income reported on W-2s (and only allow an EITC equivalent to the employer and employee share of payroll taxes for other sources of income), though that would create an inequity

between low-income wage earners and self-employed households.

Additional policy considerations before the Committee

In my National Tax Journal paper, I estimate that roughly 50 percent of EITC payments by 1996 will go to taxpayers with incomes below the poverty line and that roughly 36 percent of total EITC payment will directly reduce the "poverty gap" – the difference between total cash income and the poverty line. Because of the design of the credit, however, all benefits (other than those obtained fraudulently) go to taxpayers with incomes that are no more than 73 percent of the median family income in 1993. Put differently, the highest income an EITC-eligible taxpayer can have is \$27,000 while the median family income in 1993 was \$36,959. In this sense, the EITC is fairly well targeted to working poor or near-poor families. Nevertheless, the EITC could be more tightly targeted to lower income taxpayers by increasing the phase-out rate of the credit. Given the previous evidence on labor market incentives, doing so would probably not have particularly large deleterious labor market effects.

Place an hours requirement on the EITC

There are additional ways that EITC benefits could be more tightly targeted. For example, Congress could establish a minimum annual number of hours of work to qualify for the EITC. This would require employers to report hours of work to the IRS. The purpose of the proposal would be to target the credit to low paid workers as opposed to highly paid part-time or part-year workers. My sense is that this proposal would be problematic. It would significantly increase compliance burdens of the income tax to require employers to report the hours of work of their employees. Moreover, there is little evidence that a significant number of EITC recipients are high-wage, part-time employees. Based on tabulations from the Survey of Income and Program Participation, I calculate that more than 75 percent of EITC benefits go to taxpayers with wages that would place them in the bottom 25 percent of all workers with children (below \$7.30 per hour). More than 95 percent of all EITC benefits are paid to workers with wages below the median of \$11.11 per hour. Given the extremely small gain in targeting and the very large increase in administrative burden from this idea, it should not be pursued.

Require the identification of both parents on tax forms claiming the EITC

A second proposal would require taxpayers to identify both parents of children claimed for the EITC on tax forms in order to use this information to ensure that both parents income is taken into account when determining the EITC amount. The proposal appears to be motivated by a concern that the EITC provides a disincentive for parents to be married.

In fact, the EITC provides very strong incentives for some taxpayers to marry and others to separate. Consider, for example, a single man with two children and a single woman with two children. Both have incomes of \$11,000. By 1996, each will be eligible for an EITC of \$3,370. If they marry, their joint income will be \$22,000 and they will be eligible for a credit of \$1,054. By marrying, their combined EITC falls by almost \$5,700, or more than 25 percent of their combined earned income. Similarly, a two-earner couple with four children and with both the husband and wife making \$11,000 would increase their combined after-tax incomes by more than \$5,700 by separating

and maintaining separate households.⁶ Thus, it is clear that the EITC creates very large financial incentives for some taxpayers not to marry and for others to separate.

At the same time, the credit increases the incentive for some households to marry. Consider, for example a single man earning \$11,000 and a mother with two children with no earned income. If this pair marries, they will be eligible for an EITC of \$3,370. In general, positive incentives to marry are provided to low- or zero-earning taxpayers with children; and positive incentives for separation (or negative incentives for marriage) are provided to couples with children when each has modest earned income. My suspicion is that more taxpayers have an incentive to marry than to separate because of the EITC, but I know of no empirical evidence on the topic, nor any evidence that suggests people manipulate their legal living arrangements to respond to these incentives.

As the IRS scrutinizes social security numbers, it is important to ensure that separated parents do not both claim the same child in order to receive the EITC. The IRS presumably already has the information needed to enforce this. Beyond that, it does not make sense to me to reduce the EITC a taxpayer could receive because a separated spouse's income or assets, as long as those resources are not available (in the form of a child support order) to the child.

Change the tax treatment of some payments for the purpose of the EITC

The third proposal asks whether the tax law should treat some monetary and non-monetary payments from other sources as nontaxable income to be added to income in determining the EITC. Revising the earned income definition would be intended to encourage work and ensure that total federal benefits provided to individuals are restrained and directed toward those who provide the support of children.

A current serious problem with the EITC is that several unverifiable sources of income are currently included in the EITC income base. These include housing allowances or the rental value of a parsonage for the clergy, excludable employer-provided dependent care benefits, nontaxable military quarters and subsistence benefits, voluntary salary reduction amounts (e.g., deductions to 401(k) plans), and anything else of value (money, goods, or services) received from someone for services performed even if it is not taxable (IRS Publication 596). With perfect compliance the inclusion of these items in the EITC income base may enhance the targeting of the credit, but reporting these income items is essentially voluntary. Given the difficulty of enforcing these provisions, I would support a proposal to restrict EITC eligibility and benefits to verifiable items.

Receipt of the EITC does not affect one's eligibility for, or level of benefits available from AFDC, food stamps, or other federal means-tested programs for the poor. Changing this aspect of the EITC would be ill-advised, given the already extremely high tax rates many low-income households face. If the EITC resulted in additional benefit reductions, tax rates on many low-income households could easily exceed 100 percent, which would undoubtedly severely inhibit labor force participation.

⁶Separating would also reduce their (small) federal tax liability. If the family owns their home, it is not even clear that they could not continue to live in the same house. One partner would receive the house in the separation agreement. The homeowner could then "rent" a portion of the home to the separated spouse and children.

Incorporate an asset test on the EITC

The fourth proposal would deny the EITC to taxpayers with assets (based on dividend, interest, and tax-exempt bond income) above some threshold. This proposal would be relatively straightforward to administer, and consequently could, in an effective manner, enhance the targeting of the EITC. I would not oppose such a proposal, though two things should be kept in mind when debating it. First, it will be relatively easy to manipulate portfolios so as to avoid the asset income thresholds without altering the value of the portfolio. Hence, the asset test will in all likelihood exclude fewer families than expected. Second, it may be counterproductive to implement a very restrictive asset test. While asset tests of any kind enhance targeting in a static sense, they also can make it nearly impossible for recipients to legally accumulate the assets necessary to take a wide range of choices leading to independence – helping a child attend college, acquiring additional training, or moving away from a dangerous neighborhood.⁷ While asset tests might help target benefits to the poorest members of society, they also make it extremely difficult for program recipients to acquire skills that may help them or their children avoid poverty in the future. As with high implicit tax rates on labor earnings, asset tests distort the economic decisions of low-income households and hence reduce the efficiency of antipoverty policy.

Conclusions

Over the past 20 years the EITC has been a favored policy tool for assisting low-income families with children. Between 1975 and 1990 the EITC remained roughly constant in real terms. By 1996 the real value of the EITC will nearly triple from its 1990 level. No other major program directed toward low-income families has grown at a comparable rate in recent years.

The effectiveness of the EITC will depend, in part, on its effect on labor market behavior. Most workers that will receive the credit have incomes that place them in the flat or phaseout range of the credit, where the credit provides an unambiguous incentive for people to work fewer hours. Using recent estimates from the empirical literature on taxes and labor supply, we find that the change in incentives caused by the 1993 expansion of the credit are expected to lead to a reduction in hours of work by those already in the labor market. Our central estimate predicts an overall reduction of roughly 54 million hours a year for families in our sample.

One of the attractions of the EITC is that it provides an unambiguously positive incentive to people not working to get a job. We find, both in descriptive tabulations and empirical models, that the after-tax wage has an economically and statistically positive effect on labor market participation and negative effect on transfer program participation. Thus, when fully phased in, the 1993 EITC expansion will increase labor force participation. Our preferred estimates suggest the magnitude of the

⁷For example, a family receiving food stamps cannot have financial assets exceeding \$2,000 (\$3,000 if the family unit has a member older than 59), and cannot own assets and a car whose combined market value exceeds \$6,500. A family receiving AFDC cannot have more than \$1,000 of financial assets. In a well publicized case, Cecelia Mercado was ordered by the Connecticut Supreme Court to repay \$9,342.75 in AFDC payments because her daughter, without her knowledge, had taken a part-time job and, in a year and a half, had saved almost \$5,000 toward attending college. To become recertified to receive AFDC, the daughter and her brother (who had saved nearly \$1,000) had to spend their saving until the household's assets fell below the \$1,000 asset limit (William Raspberry, Atlanta Journal and Constitution, 8/21/92, p. A10).

participation effect will be large enough to offset the decrease in hours worked by workers.

While economists are predisposed to concentrate on the labor market responses to the EITC, the credit gets mixed reviews on two additional, important, policy dimensions. The participation rate – the fraction of eligible taxpayers that actually receive the credit – is quite high. The credit is reaching its intended beneficiaries. At the same time, many that are not eligible for the credit receive it. With the recent expansion of the EITC, the amount of overpayment could reach \$10 billion annually, an amount that, if it persists, will surely cause the credit to be scaled back, if not repealed altogether. I am hopeful that recent IRS attention to this problem will reduce the error rate and the credit will remain in place. My support for the credit results from the fact that (i) a high fraction of eligible taxpayers receive the credit, (ii) its labor market effects are probably, in aggregate, beneficial, and without a doubt, they are less pernicious than alternative ways of assisting the working poor, (iii) the credit is well-targeted toward poor and near-poor families, and (iv) families receiving the EITC are working, that is, they are "doing the right thing." Given the performance of labor markets for low-skill workers over the last 20 years in the U.S., it sound social policy to try to supplement the earnings of working poor families.



Focus

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An evolving child support system

by Daniel R. Meyer, Irwin Garfinkel, Judi Bartfeld, and Pat Brown

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The Wisconsin Child Support Assurance System

Concern about the well-being of single-parent families, particularly those headed by women, has intensified in the last two decades. Two of the chief factors fueling

this concern are the growth in this type of family and the increase in child poverty. The proportion of children living with only one parent has risen dramatically, from 9 percent in 1960 to almost 27 percent in 1992.¹ Further, 45.7 percent of mother-only families were poor in 1992, making them the most impoverished major demographic group.² In addition, there is growing evidence that children in single-parent families are worse off than children in two-parent families in a number of ways unrelated to income.³

The rising numbers and deteriorating circumstances of children in single-parent families have contributed to intense interest in determining the effects of the child support system on this vulnerable population. In the mid-1970s, officials in the U.S. Department of Health, Education, and Welfare asked the Institute for Research on Poverty to study the child support system. The system then in place included case-by-case determinations of the amount of support to be paid, and there was little standardization of collection procedures. IRP researchers identified a variety of deficiencies in the system. Few custodial parents had child support awards. When there was an award, the dollar amount was low and was not updated over time. Cases in very similar circum-

stances frequently received very different treatment. The poor, who seldom received child support settlements, obtained economic support from the Aid to Families with Dependent Children (AFDC) program: in effect the taxpayers bore the support obligations of absent fathers.⁴

Exposure of these problems led to a number of proposals for reform both in Wisconsin and at the national level. Irwin Garfinkel and Marygold Melli proposed a comprehensive reform, calling it a "Child Support Assurance System" (CSAS).⁵ It was based on the philosophy that all parents—custodial and noncustodial—are obligated to share their income with their children. The government's primary role is to enforce the responsibility of parents to provide for their own children, rather than provide an alternative means of support. A secondary role for the government under this proposal is to supplement child support when the amount paid by the noncustodial parent is lower than an established minimum. This public funding was envisioned as an extension of the American social security system. Like Survivors Insurance, child support assurance was designed to replace a portion of the earnings of an absent parent. As proposed, the CSAS had three main components:

1. A numerical formula for establishing child support obligations (the percentage-of-income standard). The specific proposal was that the award should be based on the gross income of the noncustodial parent and the number of children, as follows: 17 percent of income for one child, and 25 percent, 29 percent, 31 percent, and 34 percent, respectively, for two, three, four, and five or more children. Child support awards were to be explicitly expressed as a percentage of income so that they would automatically adjust to changes in the income of the noncustodial parent.
2. Routine withholding of the child support obligation from wages and other sources of income of the noncustodial parent. Withholding from the income of the noncustodial parent was already possible in some states if the noncustodial parent was delinquent in meeting the child support obligation; this reform went further, instituting withholding automatically from the time the award was first issued.
3. An assured (guaranteed) child support benefit for each family with a child support award. The government would guarantee to each custodial family having a child support award, a minimum amount of support each month; if the noncustodial parent did not pay the minimum amount, the remainder would be paid from public funds.⁶

All three proposals were favorably received in the state of Wisconsin and were recommended by the Wisconsin Welfare Reform Advisory Commission in 1979. However, the components of CSAS met different fates.

The percentage-of-income standard was published through a 1983 Wisconsin law and was available as a guideline for judges to refer to in setting child support awards. In July 1987, the standard became presumptive: that is, it was required unless the court made a finding on the record that it would be unfair to the child or one of the parents. Both laws allowed, but did not require, that awards be expressed as percentages. Many judges used the percentage standard to determine the amount of award, but then expressed the award as a fixed-dollar amount.

The 1983 law also established a ten-county demonstration to test routine withholding. By 1987, all counties were required to use routine withholding in all cases.

Although Wisconsin received a waiver from the federal government to test an assured benefit, the assured benefit was never tested in the state.⁷

Several researchers at IRP have been involved in evaluating the implementation of these reforms and estimating their effects. In this article we review the results from this research, first presenting information on the data gathered to evaluate the reforms, then presenting results in four areas: (a) the prevalence and effects of setting initial awards according to the percentage-of-income standard; (b) the prevalence and effects of expressing child support orders as a percentage of income rather than as a fixed amount; (c) the extent to which child support orders are revised; and (d) the use and effects of routine withholding. We close with a discussion of the national implications of this research.

The Wisconsin child support data

Court record data were gathered by IRP staff from the court records of over 14,000 families eligible for child support who came to family court in twenty-one counties in Wisconsin over the years 1980-91. (For a list of publications based on these data, see box, p. 10). The court record includes demographic information on the father, the mother, and the children, and detailed information about the court decision (legal custody, physical placement, the amount of the child support award, etc.). It also usually includes information about the incomes of the father and mother at the time of the court hearing. Each case was followed for up to four years. Each time a case returned to court during this follow-up period for an action that could affect child support, information was collected about the court petition and the resulting action. Because all child support payments in Wisconsin are supposed to go through the clerk of courts, the court record contains information on payments throughout the follow-up period.⁸ The IRP merged these data with data from two other sources: the tax records of the Wisconsin Department of Revenue and the administrative records of the AFDC program.

Studies of the percentage-of-income standard

Use of the standard

The percentage-of-income standard applies in its simplest form only to sole-custody cases.⁹

Figure 1 shows the distribution for sole-custody cases of award amounts compared to the standard over the twelve-year period 1980–91. The effects of the reform are striking. Very few awards were within 1 percent of the standard before the standard was published (1980–83). In 1984, the first year after the standard was published, twice as many awards as the year before were close to the standard. The percentage of cases with awards consistent with the standard continued to increase from 1984 through 1987. Since 1988, the first full year in which the standard was presumptive, about half of all cases have orders for the requisite amount.¹⁰

Table 1 presents information on the sole-custody cases decided between 1988 and 1991, after the standard be-

came presumptive. The first row shows that most of the orders in paternity cases that deviated from the standard were too low, and 24 percent had no order at all. There was significant variation among the counties: the three counties that used the standard in paternity cases the least used it about one-third of the time; the three counties that used it the most used it in 88 percent of their cases. The standard was used more often in divorce cases than in paternity cases. It was applied much more often when the payer was the father than when it was the mother, perhaps because it is used less when the non-custodial parent has a low income. Use of the standard is greatest in the middle-income range for divorce cases, whereas low-income and high-income cases are more likely to have nonstandard orders. (Extensive missing income information precludes a comparable statistic for paternity cases.) Finally, great county variation occurs in the use of the standard in divorce cases as well as in paternity cases.

Several researchers examined whether judges who deviated from the standard included their reason in the case

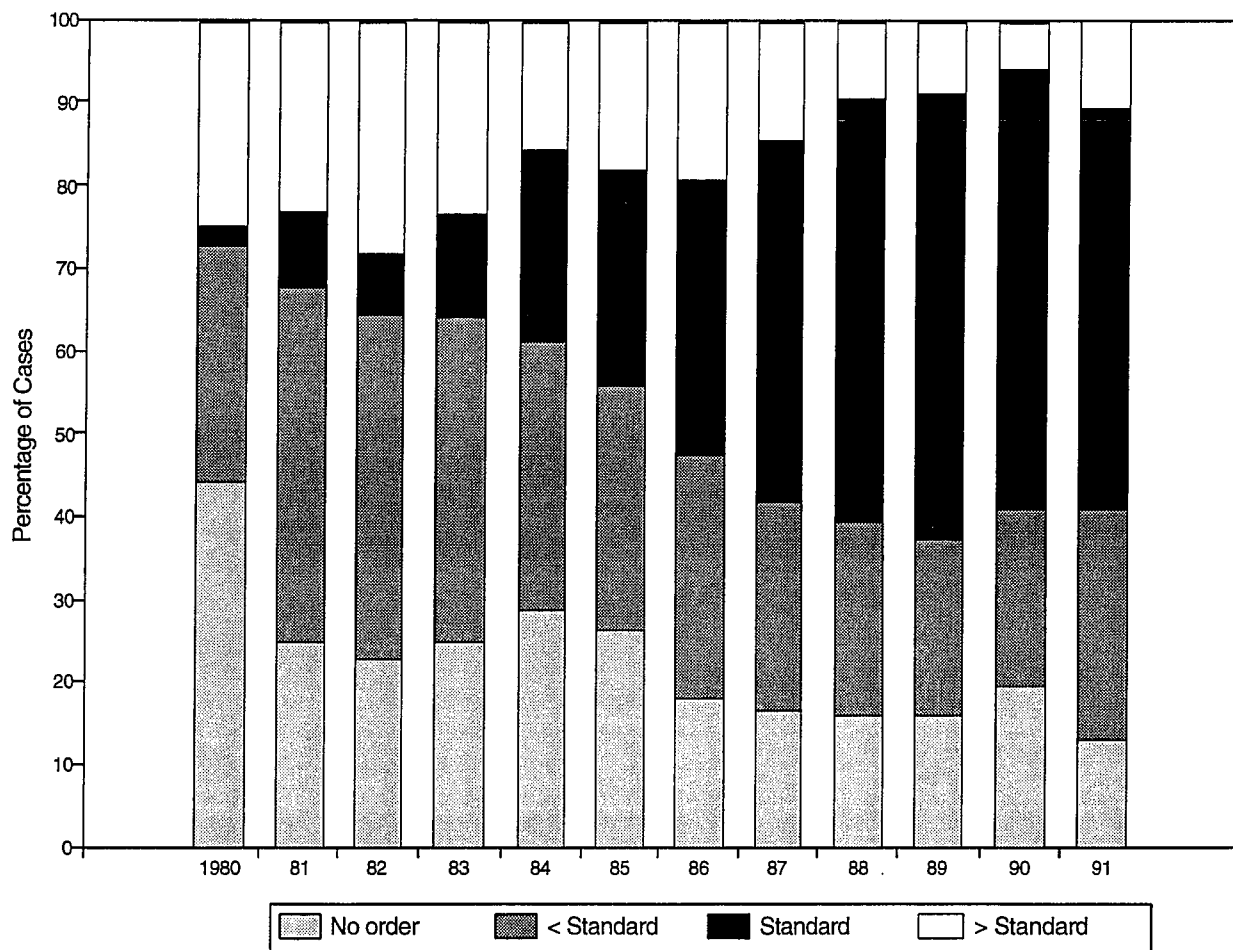


Figure 1. Relationship of Awards to the Standard. Sole-custody cases only.

Table 1
Use of the Standard Percentage Guidelines in Sole-Custody Cases in Wisconsin, 1988-1991

	Below the Standard			Above the Standard
	No Order	Low Order	Standard	
Paternity cases				
All cases (N=612)	23.9%	28.1%	41.5%	6.5%
Use of the guideline by county				
Lowest usage, 3 counties (N=37)	10.4	34.7	35.5	19.4
Highest usage, 3 counties (N=67)	7.2	4.4	88.4	5.9
Divorce cases				
All cases (N=1,986)	15.1	16.4	58.5	10.0
Payer				
Father (N=1,739)	6.5	16.5	65.7	11.3
Mother (N=247)	55.5	14.9	28.7	.9
Income of payer ^a				
\$1-10,000 (N=257)	31.9	9.7	48.0	10.4
\$10-15,000 (N=287)	11.6	21.3	54.7	12.4
\$15-20,000 (N=320)	12.2	21.4	52.9	13.5
\$20-30,000 (N=460)	2.9	16.0	72.6	8.5
\$30-40,000 (N=221)	2.9	22.6	64.4	10.1
> \$40,000 (N=133)	6.7	24.2	61.2	7.9
Use of the guideline by county				
Lowest usage, 3 counties (N=232)	12.7	22.6	50.6	14.1
Highest usage, 3 counties (N=174)	4.9	10.6	80.4	4.1

Notes: Weighted data. "Standard" is defined as the Wisconsin standard plus or minus 1% of income. In divorce cases, the support order was taken from the final judgment of divorce. In paternity cases, the support order was taken from the paternity adjudication action or subsequent support action within six months of paternity establishment.

^aNot shown in this panel are the 92 cases when the payer has no income. Of these cases, 21.5 percent are above the standard (a fixed-dollar order of any amount or a percentage-expressed order that uses a percentage higher than the standard would require). The rest use the standard (percentage-expressed orders that use the percentage specified by the standard) (24.1 percent); or have low orders (percentage-expressed orders that use a percentage lower than that specified by the standard) (2.1 percent); or have no awards (52.3 percent). Also not shown on this panel are 216 cases with missing income.

record. They found only a few written reasons, and these mostly had to do with a judge's finding that the income of the noncustodial parent was so low that applying the standard would be burdensome.¹¹

Effects of the standard on the percentage of noncustodial income that is owed

Prior to the use of numerical formulae, awards varied dramatically as a percentage of a noncustodial parent's income.¹² One effect of the standard has been to decrease this variability in award amounts (see Figures 2 and 3). The figures depict the distribution of awards as a percentage of father's income for all divorce cases with one and two children, respectively, in which the mother has sole custody. The solid line shows the percentage required by the standard. The other lines show the median award and the 25th and 75th percentile. Figure 2 shows that in cases with one child decided in 1981, one-quarter had awards that were less than 9.9 percent of the father's income (the 25th percentile line), half had awards below 13.0 percent of his income (the median), and one-quarter had awards above 20.1 percent of his income. The figures reveal that in the early part of the 1980s, before the standard was published, median child

support awards were substantially below the standard (13-15 percent of noncustodial income for one child and 16-21 percent for two children). There was considerable variation among awards: one-fourth of the awards were quite low and one-fourth were at or above the standard. When the standard was published in 1983, the median award began to increase until it reached the proportion required by the standard. Further, the spread in awards began to lessen, until, by 1987, both the median award and the award at the 75th percentile were identical for families with one child. For families with two children, the award at the 25th percentile, the median, and the 75th percentile all matched the guideline by 1989.

Effects of the standard on compliance

Other studies provide information on the relationship between the standard and compliance (the amount paid divided by the amount owed). One study found that fathers of one child with moderate and high incomes who had standard orders (15 to 20 percent) had the same compliance rate as those with orders below the standard (less than 15 percent). For poor fathers, low-percentage awards were associated with higher compliance rates. Fathers of all income groups with orders above the

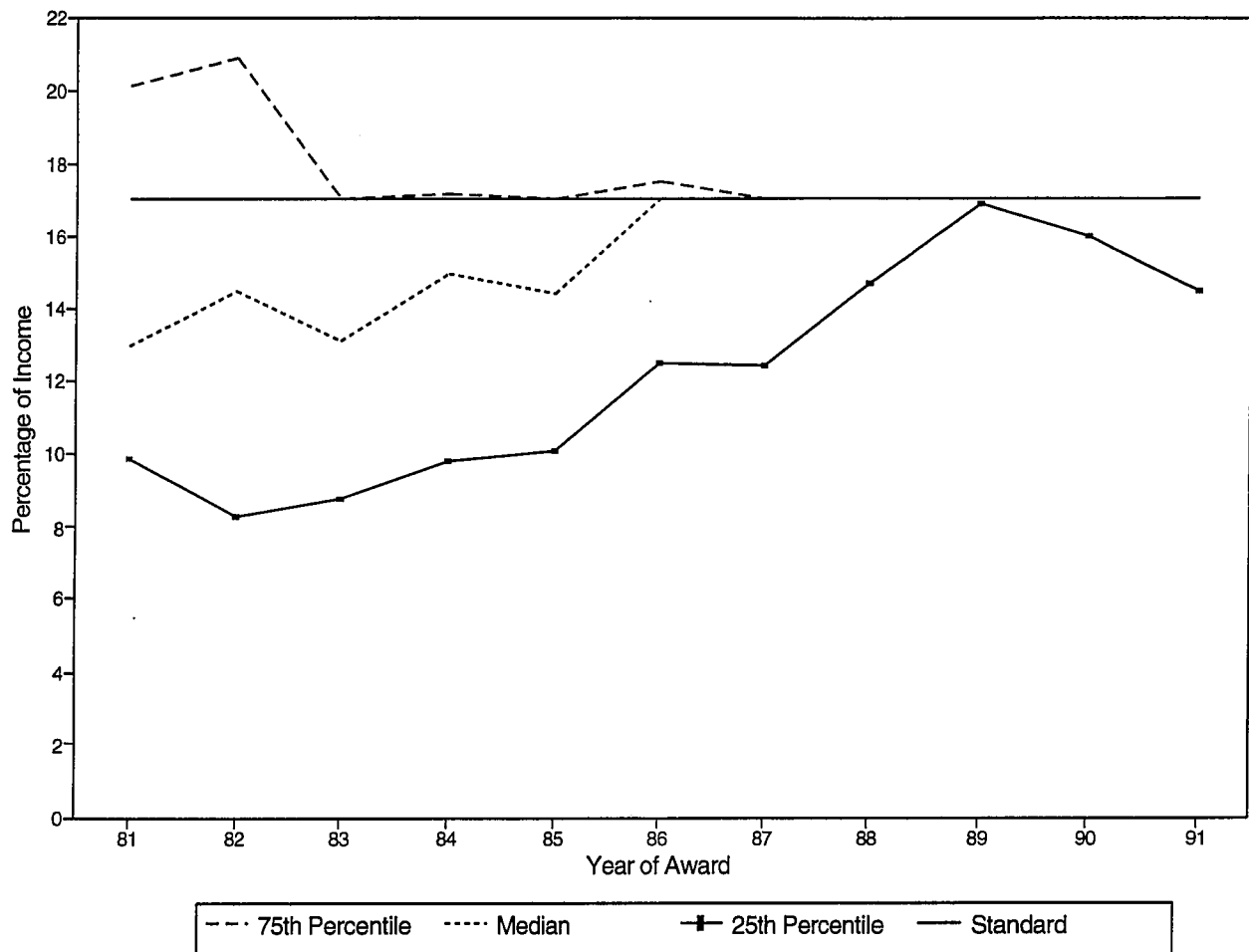


Figure 2. Child Support Awards as a Percentage of Payer's Income. For one child. Mother has physical custody, 1981-1991.

standard had lower compliance rates.¹³ Another study analyzed the determinants of compliance in divorce cases.¹⁴ It found that compliance in these cases begins to drop after orders exceed 25 percent of income. Although these two studies were not explicitly examining the effects of the standard, they do suggest that orders set according to the standard generally have compliance rates as high as orders below the standard, whereas orders in excess of the standard have lower compliance.

Studies of percentage-expressed orders

As mentioned, the original CSAS proposal called for awards to be expressed as a percentage of noncustodial income in order to automatically keep pace with changes in noncustodial income. What actually happened, however, was that the standard was often used to determine the award, which was then expressed as a fixed amount rather than as a percentage; thus the award did not automatically change with changes in the income of the noncustodial parent.

Use of percentage-expressed orders

Judges in Wisconsin now mainly use one of three order types: fixed-dollar awards, percentage-expressed awards, and "hybrid" awards, which combine fixed and percentage orders into a two-part award of the form "\$XX/month, or YY percent of income, whichever is higher." Until the child support standard was introduced in the mid-1980s, virtually all support orders in Wisconsin were fixed-dollar orders.¹⁵ By the late 1980s, however, this type was used in only 44 percent of paternity cases and 37 percent of divorce cases, with substantial variation across counties.¹⁶ Percentage-expressed orders were first introduced in the mid-1980s. Their use increased from about 1 percent at that time¹⁷ to 39 percent of paternity cases and 36 percent of divorce cases in the late 1980s.¹⁸ They are more commonly used when the payer is unemployed or has an extremely low income.¹⁹ Hybrid orders were used in 8 percent of cases in 1990,²⁰ most often in cases in which the payer had an extremely low income.²¹ Their pattern of use suggests that the courts use hybrid orders for varying reasons—sometimes to prevent the obligation from dropping too low

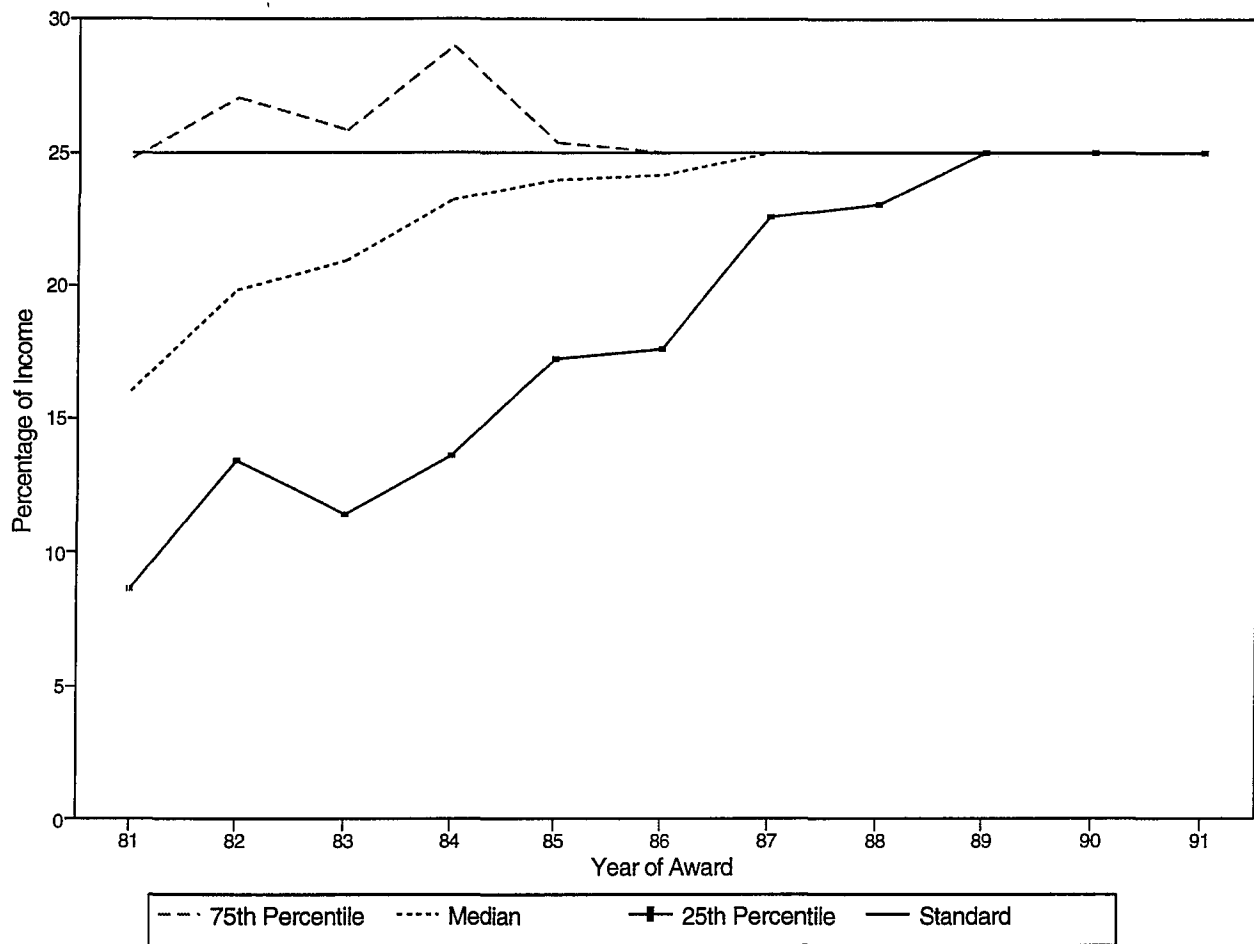


Figure 3. Child Support Awards as a Percentage of Payer's Income. For two children. Mother has physical custody, 1981-1991.

should income fall, at other times to set an award higher than warranted based on income at the time of the award.²² Finally, 9 percent of the most recent cases coming to court have other kinds of two-part orders, in which the order in effect at any given time varies depending on some criterion, such as the type of income of the noncustodial parent or variations in custody arrangements.

Effect of percentage-expressed orders on awards

The available research shows that award amounts under percentage-expressed orders increase faster than those under fixed orders. (Fixed-dollar orders require a court action to change their value.) One study found that after one year, 29 percent of percentage-expressed orders had increased by at least \$75 per month, compared to only 2 percent of fixed orders.²³ After three years the comparable figures were 53 percent and 5 percent. Twenty-two percent of fixed orders *would have* increased by at least \$75 per month after one year had they been expressed as a percentage (and thus indexed to income), and 42 percent would have done so after three years. Over a three-

year period, fixed orders would have been on average \$63 higher per month had they been indexed to income. Even if these orders were updated every three years, as is now mandated by the Family Support Act of 1988, these interim gains would not be captured. And, as discussed below, fixed orders are often not updated.²⁴

Effects of percentage-expressed orders on compliance and payments

There are at least two ways in which the order type could affect compliance rates. Monitoring compliance is more difficult with percentage-expressed orders, since the exact amount due is based on the noncustodial parent's income and is thus not always available to child support staff. This could presumably result in lower compliance. However, percentage-expressed orders may be perceived by noncustodial parents as fairer than other order types, which could have a positive impact on compliance.

Researchers have not thoroughly examined whether order type has an impact on compliance rates. In one

study, percentage-expressed orders were found to have lower compliance rates than fixed orders, but no attempt was made to determine whether this difference was due to the type of order rather than underlying differences among the parents involved.²⁵ Because percentage-expressed orders have been used disproportionately in cases in which the payer is unemployed or has a very low income, differential compliance could be due, at least in part, to case differences.

Despite the lower compliance rates of cases with percentage-expressed orders, research shows that the net effect of such orders on payments is positive. (As mentioned earlier, the compliance rate is the amount paid divided by the amount due. Because the amount due tends to increase under percentage-expressed orders, the amount paid could still increase even if the compliance rate was decreasing.) An examination of payments in percentage-expressed cases in the Order Revision Project, described below, shows substantial increases in payments over time.²⁶ A more comprehensive analysis showed that percentage-expressed orders are associated with the collection of substantially higher child support payments than are fixed orders, after controlling for the amount of the initial award as well as for differences between cases which receive the two award types. Three years after the orders were issued, payments for percentage-expressed orders increased by an estimated \$66 per month relative to fixed orders.²⁷ Collections increased *because* of large increases over time in the amount of noncustodial income (and therefore in awards) and *despite* the lower rates of compliance. Further gains may therefore be possible by improving the access of the courts to information on the noncustodial parent's income.

Studies of the extent to which orders are revised

Orders that are expressed as fixed-dollar amounts become outdated whenever the noncustodial parent's income changes, unless the parties return to court. Recent research shows that orders are not updated, despite substantial increases in noncustodial income.²⁸ The policy response to this, in the Family Support Act of 1988, is to mandate that all cases within the child support system be reviewed every three years and modified as appropriate. In conjunction with this mandate, several Wisconsin counties began the process of reviewing all old orders, and the Wisconsin DHSS requested that IRP evaluate the effects of these efforts (the Order Revision Project). Child support workers filled out a short form on every case they reviewed; these were collected and analyzed by IRP.

Four counties began order-revision operations in early 1990; nine additional counties began during late 1992.²⁹

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In the thirteen counties, 11,451 cases were reviewed as potential candidates for revision. Of these, about 8000 (70 percent) were selected for a revision attempt. The most frequent reason for dropping a case at this point was that it had been recently set or recently revised. Of the remaining cases that were dropped, the most frequent reason was that the case should have been closed (the child turned 18, was adopted, or died, the parents had reconciled, the noncustodial parent had died, or the case belonged to another jurisdiction).

Of the cases selected for revision, over 6600 (83 percent) have been disposed of, and the remaining 18 percent are still in process. Successful revisions accounted for one-fourth of the cases disposed of, unsuccessful petitions for revisions accounted for a small number (less than 1 percent), and the remainder (74 percent of the total) were dropped at this point. The reasons for dropping cases once the revision process was initiated fall into a clear pattern. If the custodial parent was not receiving AFDC, she or he had to give permission to the

child support agency to proceed with a revision: this lack of permission was the primary reason non-AFDC cases were dropped. If the custodial parent was receiving AFDC, custodial-parent permission was not required. For these cases, the dominant issue was the economic situation of the noncustodial parent (68 percent of the AFDC cases that were dropped at this point were dropped because of factors related to unemployment or low income).

The average increase in child support orders for all revised orders was over \$110 per month, an increase of 70 percent. This large increase confirms that a pool of orders exists for which the present support obligation seriously underrepresents the noncustodial parent's ability to pay. The dollar increases in AFDC cases were similar to those in non-AFDC cases, about \$100/month. Even though these orders showed large increases, in most cases they were still below what the standard required. In 63 percent of the revisions, the new orders were below the standard, 33 percent were close to the standard, and 4 percent were above. When orders deviated from the standard, it was usually because the court let stand an agreement between the parents over the award amount, or because the court found that the standard would place an undue financial hardship on the noncustodial parent. So even though orders that were revised increased substantially, if the standard had been used, they would have increased by an even larger amount.

Collections over the six months following the revision were an average of \$88 per month more than they were in the six months preceding the revision. On average, 80 percent of the increased order amounts were paid. In addition, an average of an additional \$7 per month was collected toward arrearages in the cases that were revised. Increases in both current support and arrearages were somewhat smaller for AFDC cases than for non-AFDC cases. An examination of payments over the first twelve months following the revision showed an increase for the first four months, followed by a gradual decline by the end of the year. However, even by the twelfth month, collections were substantially higher than they had been prior to the revision.

The key findings of the project were the substantial increases in child support orders and child support collections, which indicate how out of date many of the orders had become. Also noteworthy was the reluctance of custodial parents to reopen cases already settled, even though they were aware that revision would most likely increase the amount they received from the noncustodial parents of their children.

Comparing two methods for keeping orders current

Requiring that child support orders be reviewed periodically is one method to keep them current; expressing orders as a percentage of income is another. Although

no research has directly compared the two methods, the studies that have been done offer some insights into the relative advantages and disadvantages of each approach.

Percentage-expressed orders are more successful at keeping pace with changes in noncustodial income over time, because the link to income is explicit. While fixed orders that are routinely updated would also keep awards current, they are inferior in two ways. First, as noted above, there is a strong tendency of cases to "drop out" during the administrative process and not be routinely revised. Second, even the awards that are revised every three years do not reflect interim changes in the noncustodial parent's income. Payments have been found to increase for both fixed-dollar orders that are updated and orders that are expressed as a percentage.

Another relevant comparison between the two methods is their relative cost. Costs are incurred by cases with fixed orders when these orders are updated on a case-by-case basis, whereas costs are incurred by percentage-expressed cases when child support staff reconcile payments to the noncustodial parent's income. Note that if fixed-dollar orders are not updated, no additional costs are incurred, but orders are not current. In contrast, percentage-expressed orders that are not reconciled also incur no additional administrative costs, but the orders reflect current income of the noncustodial parent. A formal comparison of these costs is not possible with the data that we have.

Studies of routine withholding of child support

The final major child support reform tested in Wisconsin was the use of routine withholding of child support from the incomes of noncustodial parents. This reform, and its impact on payments, has been the focus of extensive analysis.

Use of routine withholding

Table 2 shows the use of routine withholding during two periods: 1984-88 and 1988-90. In the most recent period, routine withholding was used in 76 percent of paternity cases and 77 percent of divorce cases, which is somewhat lower than in the earlier period (84 percent and 82 percent, respectively). Use increased between 1984 and 1986, and has fallen somewhat since then. The chief determinant of the use of withholding is the source of income of the noncustodial parent. In both paternity and divorce cases, withholding is far more likely to be used when the primary income source is an employer than when it is self-employment or Unemployment Compensation, or when there is no income source. Thus in 1988-90, routine withholding was used in 89 percent of paternity cases and 87 percent of divorce cases in which an employer was the primary income source,

Table 2
Use of Immediate Withholding in Wisconsin

	1984-88				1988-90			
	Paternity		Divorce		Paternity		Divorce	
	N	Yes	N	Yes	N	Yes	N	Yes
Total	938	84%	2,600	82%	342	76%	877	77%
Father's income source								
Employer	628	92	1,972	88	321	89	923	87
Self-employed	28	39	176	44	21	29	105	28
Unemployment Comp.	12	100	51	80	4	75	17	76
Other	12	83	45	56	7	43	20	45
None	52	64	60	45	8	75	8	50
Missing	206	71	296	75	176	47	191	54
Father's income								
Missing	333	79	512	81	371	68	444	71
None	72	65	68	51	12	83	13	69
Quartile 1 (\$1-11,247) (\$1-12,253)	317	90	322	76	96	76	145	70
Quartile 2 (\$11,248-18,745) (\$12,254-18,775)	129	93	509	85	36	86	204	81
Quartile 3 (\$18,746-27,232) (\$18,776-27,838)	56	89	582	86	12	92	278	87
Quartile 4 (\$27,233+) (\$27,839+)	31	84	607	82	10	90	230	76

Notes: The sample includes paternity and divorce cases in which support was ordered and the father is the payer. Note that the income quartiles are slightly different for the two sets of periods.

compared to 29 percent and 28 percent when the source was self-employment, and 47 percent and 54 percent when no source was identified in the record.

Use of routine withholding also varied according to the father's income level (standardized to 1988 dollars and categorized in quartiles).³⁰ The high proportion of cases with missing income information precludes drawing any conclusions about paternity cases. For divorces in both time periods, use of withholding increased through the third income quartile, and then declined.

Researchers documented a substantial amount of county variation in the use of routine withholding for both paternity and divorce cases. One county used routine withholding in 45 percent of its paternity cases in 1988-90, whereas another county used it in all paternity cases in our data. In divorce cases, the percentage of cases with routine withholding ranged from 50 percent to 100 percent. This large cross-county variance suggests that even though the use of withholding is fairly high, there is room for substantial improvement in some counties.³¹

Effect of routine withholding on compliance with child support orders

In the initial implementation plan, the impact of routine withholding was intended to be measured by the differ-

ence in collections between ten counties that would implement withholding ("pilot" counties) and ten similar counties that would not ("control" counties). However, the pilot counties did not routinely withhold child support payments in every case. As a further complication, judges in some control counties began to use withholding in selected cases. Thus a different evaluation plan was called for.

In the initial research on the effects of withholding, three different indicators of routine withholding were used for each case: whether the county was supposed to be using routine withholding or not; the county withholding rate for the year; and whether the individual case had a withholding order.³² These three indicators were then used to estimate the impact of withholding on three outcome measures: the ratio of dollars paid to dollars owed, the ratio of months in which a payment was made to months in which a payment was owed, and the length of time until a child support payment was missed completely. Results suggested that routine withholding did have a positive effect on child support collections, although the estimated impacts varied substantially according to the indicator of withholding used. The effect of routine withholding on the ratio of dollars paid to dollars owed varied from an 11 percent improvement to a 28 percent improvement, and the effect on the ratio of months paid to months owed varied from a 14

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percent improvement to a 30 percent improvement. The pay-to-owe ratios reflect the full case history available in the data, which ranged from less than one year to three years. There was also some evidence that the impact of withholding increased as counties gained implementation experience.

Another study analyzed the effect of withholding on the payment amounts, rather than the compliance rates, of noncustodial parents involved in paternity cases.³³ Cases with routine withholding had significantly higher payments than cases without withholding or those in which withholding was a response to delinquency. Routine withholding increased payments by about \$25 per month over cases in which withholding was a response to delinquency.

Changes in the impact of routine withholding over time was the focus of another study. There are several reasons why this impact could change. If one effect of routine withholding is to keep some noncustodial parents from becoming delinquent, then withholding would be expected to increase compliance over time. On the other hand, if withholding orders do not adequately track noncustodial parents when they change jobs (a problem noted in a multistate study of routine withholding),³⁴ the value of an initial withholding order would be lost. The study found that, consistent with earlier research, routine withholding had a positive impact on compliance. The impact, however, decreased over time. If routine withholding were used in the cases in which it was not, the compliance rate among these cases would have been 20 percent higher in the first year, 11 percent higher in the second, and 9 percent higher in the third. These results suggest that greater attention be paid to ensuring that withholding orders are able to keep pace with job changes so that their effectiveness does not fade over time.

Wisconsin results

In summary, research on child support in Wisconsin has produced the following findings:

- The percentage-of-income standard is used in about 50 percent of the relevant cases. (The simple formula is not appropriate for cases of split custody, shared custody, or serial families.) Before the standard was published, few awards conformed to the percentages specified in the standard. Since publication of the standard, a clear trend has been evident of awards conforming to the standard.
- Variance in the level of child support awards, given a noncustodial parent's income, has been dramatically lowered.
- Although awards set according to the standard generally reflect a higher percentage of noncustodial income than they did prior to the publication of the standard, this does not seem to lead to lower compliance, in most cases.
- Awards that are explicitly expressed as a percentage of income increase more rapidly over time than fixed-dollar awards, and they are associated with higher child support payments.
- Some old child support awards do not reflect the current economic circumstances of the noncustodial parents and can be increased dramatically. However, the percentage of old cases that were revised in the Order Revision Project was lower than some observers expected (25 percent), in part because most non-AFDC custodial parents did not give permission to proceed with a revision and in part because of the poor economic circumstances of some noncustodial parents. The rate of revision in Wisconsin is similar to that found in other states.³⁵

- When old child support awards were revised, collections in these cases increased dramatically.
- Routine withholding significantly increases compliance with child support awards. The effect declines over time, however, suggesting that greater attention be paid to ensuring that withholding orders keep pace with job changes.

National implications of the research

Wisconsin's experience with child support reform offers a valuable case study of the potential contributions of the social sciences to public policy research. Researchers at the IRP played key roles in identifying problems inherent in the existing child support system, developing a proposal for comprehensive reform, designing an evaluation, and deriving estimates of the impacts of reform. Further, the experience has fueled extensive debate and ultimately reform at the national level. Two of the three basic features of the CSAS—presumptive

support guidelines based on income, and routine withholding of support from noncustodial income—were mandated by the 1988 Family Support Act. The third component, a guaranteed minimum child support benefit, has been proposed in Congress and is currently under consideration.

What kinds of impacts might we expect from recent nationwide reforms in the child support system? Wisconsin's experience illustrates the potential for dramatic changes in behavior—both institutional and individual—in a relatively short time frame. Despite less than perfect adherence to child support guidelines, support orders in Wisconsin experienced remarkable convergence toward the standard in less than a decade. Likewise, the implementation rate of immediate income withholding has been consistently high, especially among cases in which withholding is most feasible. Changes at the individual level have also been impressive: compliance with support orders among new cases has increased substantially over the past decade, particularly for divorce cases (see Figure 4).

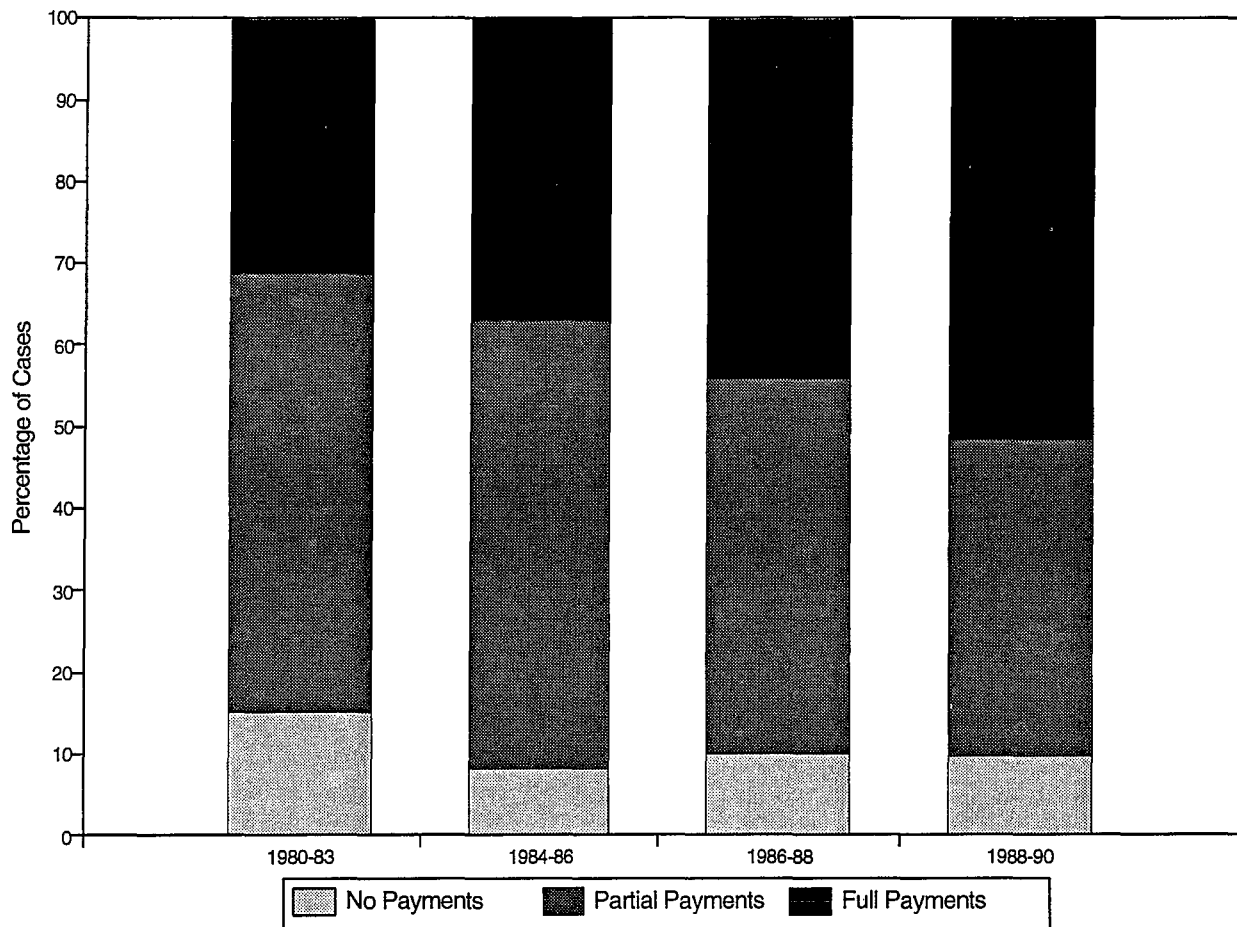


Figure 4. Trends in Compliance with Awards, Divorce Cases.

On the other hand, some findings from the Wisconsin research warrant caution. In particular, the Wisconsin experience suggests that simply enacting new laws may not be sufficient, and that the ultimate success of reform will depend on the details of implementation. While the overall figures on the use of the standard and on the use of routine withholding seem fairly high, substantial county variation remains. This suggests that implementation is still incomplete.

Wisconsin's experience with reviewing and updating support orders also points to the importance of implementation procedures. The relatively low rates of order revision in Wisconsin and elsewhere suggest that a more routinized method of updating, such as explicitly indexing awards to income by issuing percentage-expressed orders, may be necessary in order for awards to remain up-to-date.

Although compliance has increased, substantial amounts remain uncollected: among recent paternity cases, only 30 percent receive the full award, and only about half of recent divorce cases receive the full award. Experience in Wisconsin suggests that states should focus not only on ordering income withholding, but also on developing better procedures for administering and tracking withholding orders over time.

Another caution about the potential impacts of national reform pertains to the low incomes of some noncustodial parents. Compliance rates remain substantially lower for low-income noncustodial parents than for those with higher incomes, a difference that is not explained by differential use of income withholding. The importance of income as a determinant of compliance offers a valuable reminder that, if noncustodial parents are to share their income with their children, they must have income to share.

Finally, the economic status of children in single-parent families is so vulnerable that we believe providing support to these families is required. A publicly guaranteed child support benefit could increase the well-being of these children by increasing their economic security. Whereas the components of CSAS that were intended to increase private responsibility have been enacted, we believe it is now time for us to accept some public responsibility as well and guarantee a minimum amount of child support. ■

¹U.S. Bureau of the Census, Current Population Reports, Series P20-468, *Marital Status and Living Arrangements: March 1992* (Washington, D.C.: U.S. GPO, 1993, p. xi).

²U.S. Bureau of the Census, Current Population Reports, Series P60-185, *Poverty in the United States: 1992* (Washington, D.C.: U.S. GPO, 1993, p. 6).

³For example, see Sara S. McLanahan and Gary D. Sandefur, *Growing Up with a Single Parent: What Hurts and What Helps* (Cambridge: Harvard University Press, 1994), p. 6.

⁴See, for example, Irwin Garfinkel and Marygold Melli, eds., "Child Support: Weaknesses of the Old and Features of a Proposed New System," IRP Special Report no. 32A, University of Wisconsin-Madison, 1982.

⁵Ibid.

⁶To cover the costs of child care and other work-related expenses, a wage subsidy was added to the benefit package in the proposed Wisconsin demonstration of the assured benefit. See Irwin Garfinkel, Philip K. Robins, Pat Wong, and Daniel R. Meyer, "The Wisconsin Child Support Assurance System: Estimated Effects on Poverty, Labor Supply, Caseloads, and Costs," *Journal of Human Resources*, 25 (1990), 1-31.

⁷Tom Corbett ("The Wisconsin Child Support Assurance System: From Plausible Proposals to Improbable Prospects," in *Child Support Assurance*, ed. Irwin Garfinkel, Sara S. McLanahan, and Philip K. Robins [Washington, D.C.: Urban Institute Press, 1992]) discusses the various factors that caused this reform to be terminated. The only research conducted on it was based on potential effects predicted by microeconomic simulation models (see, for example, Garfinkel, Robins, Wong, and Meyer, "Wisconsin Child Support Assurance System"; and Meyer, Garfinkel, Donald Oellerich, and Robins, "Who Should Be Eligible for an Assured Child Support Benefit?" in *Child Support Assurance*, ed. Garfinkel, McLanahan, and Robins).

⁸Further details on the data collection methods can be found in Pat Brown and J. Laird Marshall, "Sampling Report, Wisconsin Child Support Demonstration Project," IRP, University of Wisconsin-Madison, June 1992.

⁹The calculations are more complex and the percentages differ when one parent has physical custody of one child and the other parent has physical custody of another (split custody), when parents share physical custody of the same child (shared custody), or when the noncustodial parent is subject to two different child support orders (serial families). Since 1980-81, use of these other arrangements has increased. Whereas 93 percent of the divorce cases decided in 1981 were sole-custody cases, only 77 percent of the divorce cases decided in 1991 were, with 12 percent shared custody, 7 percent serial families, and 4 percent split custody. Similarly, whereas 99 percent of the paternity cases were sole-custody cases in 1980, the percentage had declined to 89 percent by 1991, the remainder being serial-family cases.

¹⁰The figures in this section come from a recent thorough analysis of the use of the standard and are thus somewhat different from those reported in other preliminary IRP reports (which include Marygold Melli and Judi Bartfeld, "Use of the Percentage-of-Income Standard to Set Child Support: Experience in Twenty Counties, September 1987-December 1989," report submitted to the Wisconsin Department of Health and Social Services, June 1991; Melli and Leslie McCall, "The Use of the Percentage of Income Standard to Set Child Support in Wisconsin: An Update," report submitted to the Wisconsin Department of Health and Social Services, June 1993; Daniel R. Meyer and Bartfeld, "Cases Eligible for Child Support in Wisconsin, 1980-1990," report submitted to the Wisconsin Department of Health and Social Services, June 1993).

¹¹See Melli and Bartfeld, "Use of the Percentage-of-Income Standard to Set Child Support"; Melli and McCall, "Use of the Percentage of Income Standard to Set Child Support in Wisconsin."

¹²Kenneth R. White and R. Thomas Stone, "A Study of Alimony and Child Support Rulings with Some Recommendations," *Family Law Quarterly*, 10 (1976), 75-91; Lucy M. Yee, "What Really Happens in Child Support Cases: An Empirical Study of the Establishment and Enforcement of Child Support Awards in the Denver District Court," *Denver Law Journal*, 57, no. 1 (1979), 21-70.

¹³Judi Bartfeld and Daniel R. Meyer, "Are There Really Dead-Beat Dads? The Relationship between Enforcement, Ability to Pay, and Compliance in Nonmarital Child Support Cases," *Social Service Review*, forthcoming, 1994.

¹⁴Daniel R. Meyer and Judi Bartfeld, "The Relationship between Compliance with Child Support Orders, Enforcement Tools, and Ability to Pay in Divorce Cases," manuscript, 1994.

¹⁵Meyer and Bartfeld, "Cases Eligible for Child Support in Wisconsin, 1980-1990."

¹⁶Daniel R. Meyer, Judi Bartfeld, and Kathleen Kost, "Fixed, Percentage-Expressed, and Hybrid Child Support Orders in Wisconsin," report submitted to the Wisconsin Department of Health and Social Services, 1993, Table 1.

¹⁷Meyer and Bartfeld, "Cases Eligible for Child Support in Wisconsin, 1980-1990," Tables 1-3.

¹⁸Meyer, Bartfeld, and Kost, "Fixed, Percentage-Expressed, and Hybrid Child Support Orders in Wisconsin," Table 1.

¹⁹Judi Bartfeld and Irwin Garfinkel, "Utilization and Effects on Payments of Percentage-Expressed Child Support Orders," IRP Special Report no. 55, University of Wisconsin-Madison, 1992, p. 13.

²⁰The number of hybrid orders is slightly different from that reported by Meyer, Bartfeld, and Kost, in "Fixed, Percentage-Expressed, and Hybrid Child Support Orders in Wisconsin," because the earlier figures were based on preliminary data.

²¹Meyer, Bartfeld, and Kost, "Fixed, Percentage-Expressed, and Hybrid Child Support Orders in Wisconsin," Table 1.

²²Ibid.

²³Bartfeld and Garfinkel, "Utilization and Effects on Payments of Percentage-Expressed Child Support Orders," p. 19.

²⁴See Caliber Associates, "Evaluation of Child Support Review and Modification Demonstration Projects in Four States, Cross Site Final Report," report to the U.S. Department of Health and Human Services, 1992; Daniel R. Meyer, Thomas Corbett, and Kathleen Kost, "The Wisconsin Child Support Order Revision Project: Final Report," manuscript, 1994.

²⁵Bartfeld and Garfinkel, "Utilization and Effects on Payments of Percentage-Expressed Child Support Orders."

²⁶For 116 cases with four years of payment data, the average payment in the first calendar year after the percentage-expressed order was \$370. This increased dramatically, to \$503 in the second year, \$640 in the third year, and \$1531 in the fourth (see Daniel R. Meyer and Judi Bartfeld, "An Assessment of the Advantages and Disadvantages of Fixed, Percentage-Expressed, and Hybrid Child Support Orders," final report submitted to the Wisconsin Department of Health and Social Services, January 1994).

²⁷Bartfeld and Garfinkel, "Utilization and Effects on Payments of Percentage-Expressed Child Support Orders," revised 1994, manuscript.

²⁸Daniel R. Meyer, "Supporting Children Born Outside of Marriage: Do Child Support Awards Keep Pace with Changes in Fathers' Incomes?" IRP Discussion Paper no. 1026-93, 1993.

²⁹Two preliminary evaluation reports were given to the Wisconsin Department of Health and Social Services: Tom Corbett, Pat Brown, and Kathleen Kost, "An Evaluation of the Order Revision Pilot Project," report to the Wisconsin Department of Health and Social Services, 1991; Corbett and Kost, "The Wisconsin Child Support Order Revision Project: A Preliminary Evaluation," report to the Wisconsin Department of Health and Social Services, 1993. The final evaluation is now being completed (Meyer, Corbett, and Kost, "The Wisconsin Child Support Order Revision Project: Final Report").

³⁰One difference between the two analyses is that the 1988-90 period data rely only on income information available in the court record, whereas the earlier analysis supplemented the court record data with tax records.

³¹Daniel Meyer and Judi Bartfeld examined predictors of whether a case was given withholding and found that variables denoting the counties remained significant predictors even after case characteristics were held constant (Meyer and Bartfeld, "How Routine Is 'Routine' Withholding? Evidence from Wisconsin," report to the Wisconsin Department of Health and Social Services, June 1992).

³²Irwin Garfinkel and Marieka M. Klawitter, "The Effect of Routine Income Withholding of Child Support Collections," *Journal of Policy Analysis and Management*, 9 (1990), 155-177.

³³Sandra K. Danziger and Ann Nichols-Casebolt, "Child Support in Paternity Cases," *Social Service Review*, 64 (1990), 458-474.

³⁴Anne R. Gordon, "Income Withholding, Medical Support and Services to Non-AFDC Cases after the Child Support Enforcement Amendments of 1984," Vol. I, report submitted to the U.S. Office of Child Support Enforcement under Contract 282-87-1009, Mathematica Policy Research, Inc., Princeton, N.J., 1991.

³⁵Caliber Associates, "Evaluation of Child Support Review and Modification Demonstration Projects in Four States."

The Child-Support Revolution

By IRWIN GARFINKEL*

Because more than half of this generation of American children will spend part of their childhood living apart from one of their parents, the quality of our child-support system is of vital importance to the nation's future (Garfinkel, 1992).¹ The American child-support system is in the midst of a profound transformation. This article describes the traditional child-support system and the newly emerging child-support assurance system.

I. The Traditional System

Child support is a transfer of income to a child living apart from a parent. Private support is paid for by the nonresident parent; public child support is paid for by the government.

Prior to 1974, private child support was nearly exclusively a state and local matter. Family law was traditionally a province of the states. State laws established the duty of nonresident parents to pay child support but left all the details up to local courts. Judges had the authority to decide whether any child support should be paid, and if so, how much. They also had full authority over what action would be taken if nonresident parents failed to pay, jail being the most severe punishment. In short, the system was characterized by local judicial discretion.

In a few jurisdictions, judges used a child-support obligation schedule, which is similar to a tax table. For example, in the 1970's most counties in Michigan, used only two facts to determine child support: the absent parent's income and the number of children who require support. The entire

state of Delaware used a much more complicated formula designed by Judge Melson. But such schedules were the exception rather than the rule.

In a few states, all child-support payments had to be made to a governmental agency which had the authority to initiate legal action when child-support obligations were not met. The Michigan Friend of the Court, founded in 1917, is the oldest such agency. Still, these governmental agencies usually did not use their authority unless specifically requested to do so by the custodial parent. In most cases, the burden of collecting overdue support fell to the custodial parent.

The ultimate sanction for those who did not pay was jail. In Michigan, for example, as of the 1970's thousands of absent fathers were jailed each year for failing to comply with child-support orders. Although imprisonment was used throughout the country, there are no data to indicate the numbers imprisoned.

Public assistance dates back to Colonial days. The British settlers brought with them the old Poor Law, which required local governments to provide and fund public assistance to their needy residents. Mothers' pensions, enacted by 40 states between 1910 and 1920, shifted fiscal responsibility to the state level and with the enactment of the Aid to Dependent Children (ADC) program in the 1935 Social Security Act, the federal government assumed about half of the cost. When ADC was enacted, most of the children who benefited were orphans. Now, the overwhelming majority of the children's mothers are divorced, separated, or have not been married. Widows constitute less than 2 percent of the AFDC caseload.

Throughout most of our history, the aid provided to poor children of divorce, separation, and out-of-wedlock birth and their mothers was meager. In the decade following President Lyndon Johnson's declaration

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¹Unless otherwise noted, all of the data describing the old and new child-support systems can be found in this book.

of a War on Poverty in 1964, welfare benefits were increased substantially. The Congress added Medicaid and food stamps to the welfare benefit package and allowed mothers on welfare to keep a small portion of earnings and continue to receive welfare. Supreme Court decisions expanded eligibility by declaring unconstitutional state residency requirements and man-in-the-house rules. States raised AFDC levels. Between 1976 and 1991, however, AFDC plus food stamps benefits declined by 23 percent. In 1992, the median state AFDC plus food stamps benefit (for a family of three) equaled only 72 percent of the poverty level—only 3.5 percent higher than AFDC alone prior to declaration of the War on Poverty (Committee on Ways and Means, 1992).

Finally, it is worth noting that public child-support transfers to poor children via AFDC, food stamps, Medicaid, and public housing are three times as large as private transfers to children from all income classes.

II. Weaknesses of the Traditional System

The traditional private child-support system condoned and thereby fostered parental irresponsibility, was rife with inequity, and contributed to the poverty and welfare dependence of single mothers and their children. Only six of ten mothers potentially eligible for child support had an award. Of those legally entitled to support, only half received the full amount, and one-quarter received nothing. Awards were too low and too infrequently updated to keep pace with either inflation or increases in the nonresident parent's income.

Although many people believed that nonresident fathers did not pay child support because they were too poor, research indicates that poverty is a small part of the problem. Based on estimates of the incomes of nonresident fathers and the share of income that should be devoted to child support according to the two most widely used child-support guidelines, in 1983 nonresident fathers should have been paying between \$25 billion and \$32 billion in child support, when in fact they owed only \$9 billion and paid only \$7 billion.

The traditional system treated equals unequally and imposed higher burdens in percentage terms on poor than nonpoor nonresident fathers. The majority of nonresident fathers paid no child support during the course of the year and suffered no consequences. At the same time, thousands of nonresident parents were jailed for failure to pay support.

Finally, if the private child-support system were perfectly efficient (i.e., with all nonresident fathers obligated to pay support in accordance with modern child-support guidelines and with all paying the full amount), the poverty gap of children potentially eligible for support and welfare costs would both drop by one-quarter.

The public part of the child-support system is also severely flawed. Welfare does nothing to prevent poverty, provides meager, below-poverty-level benefits, sharply reduces benefits when mothers earn more, and takes away medical-care coverage when a mother leaves welfare. For unskilled single mothers who cannot earn much more than welfare and cannot afford to forgo health insurance, the current welfare system is akin to a poverty trap. Because they have little education and experience and would have child-care expenses if they worked, most women on AFDC could not earn enough to lift their families from poverty even if they worked full time. If they also received child support from the children's absent father, some, but not all, of these families would attain an income above the poverty level. The only way to alleviate this kind of poverty without creating dependence is to supplement rather than replace the earnings of these custodial parents.

As AFDC cases began to reflect the demographic trends of divorce, separation, and out-of-wedlock births, Congressional interest in child-support payments grew. In 1950, Congress enacted the first federal child-support legislation and added two other minor pieces of legislation in 1965 and 1967. The first major piece of legislation was enacted in 1974, when Congress added Part D to Title IV of the Social Security Act, thereby establishing the Child Support Enforcement (or IV-D) program. The legislation created

the Federal Office of Child Support Enforcement, required all states to establish comparable state offices, and authorized federal funding for three-quarters of the state's expenditures on child-support enforcement. Federal funds were made available for all welfare cases and for nonwelfare cases for up to one year. After a series of one-year extensions, in 1980, federal support was extended permanently to all children eligible for support, irrespective of income or AFDC status.

III. The Newly Emerging Child-Support Assurance System

The creation of the new child-support enforcement program stimulated research and proposals for reform. The most comprehensive proposal and the model for most recent legislation was the proposal for a new child-support assurance system (CSAS). CSAS would replace the local judicial discretion of the traditional private system with the bureaucratic regularity of the federal social-security system and, like survivors' insurance, simultaneously prevent poverty and reduce dependence on welfare by providing aid to beneficiaries in all income classes.

CSAS is based on a partnership of responsibility between parents and government. Parents are responsible for sharing income with their children. Government is responsible for enforcing private support and for insuring a steady flow of income to all children with an absent parent.

The essential mechanics are easy to understand. Child-support awards are set by a legislated formula (based on a percentage of the nonresident parent's income), and payments are deducted from the absent parent's earnings, just like social-security deductions. The government guarantees a minimum level of child support to all children legally entitled to private child support—an assured benefit. The assured benefit is financed from welfare savings and from a very small addition to the social-security payroll tax.

Like survivors' insurance, CSAS aids children of all income classes who suffer an income loss due to the absence of a parent.

Survivors' insurance compensates for the loss of income arising from widowhood. CSAS compensates for the loss arising from divorce, separation, and nonmarriage. Withholding a flat percentage of the nonresident parent's income makes the bulk of the financing of CSAS similar to a proportional payroll tax, which is used to finance all social insurance programs in the United States. In the CSAS case, however, the "tax" applies only to those who are legally liable for child support. The assured-benefit component of CSAS makes the benefit structure of the system like all other social insurance programs in that it provides greater benefits to low-income families than are justified on the basis of the family's contributions or taxes.

The benefits and costs of CSAS will depend upon the level of the assured benefit, whether the assured benefit is taxable, and how much it increases private support payments. Micro-simulation analysis indicates that, with a medium-run improvement in payments achievable perhaps in 15–20 years, a \$2,000 assured benefit for the first child would reduce the poverty gap of children potentially eligible for child support and the proportion dependent on welfare by about one-fifth at no extra cost to the government.²

How can a government program not limited to poor families be so cheap? There are two reasons. First, the collection parts of the system lead to savings in welfare costs. These savings would be placed in a trust fund to offset the cost of an assured benefit.

Second, despite the fact that it insures children of all income classes, the assured benefit per se is not very costly. For the

²The medium-run improvement entails an increase in award rates (the proportion of cases with child-support awards) and collection rates (the proportion owed that is collected) halfway between the current level and perfection and an increase in awards to the level of the Wisconsin child-support guidelines: 17 percent of gross income for one child, 25 percent, 29 percent, 31 percent, and 34 percent for two, three, four, and five or more children, respectively. The assured benefit would be increased for the second and third child by \$1,000 per child and for the fourth, fifth, and sixth child by \$500 per child.

most part, men and women tend to mate with people from the same sorts of backgrounds. This assortative mating guarantees that only a small proportion of government expenditure for the assured benefit will go to a child living with a wealthy parent, because in the overwhelming majority of such cases, the nonresident parent will be equally wealthy, and there will be no public subsidy. In rare cases, of course there will be a poor nonresident parent of a child residing with a wealthy parent. Counting the public portion of the assured benefit for income tax purposes substantially reduces this already small leakage.

Even if child-support collections fail to increase at all, the extra costs of a national assured benefit would be only \$2 billion. This small cost can be paid for by a social-security payroll tax of only 0.07 percentage points. This is a small amount, which is likely to diminish over time as private child-support payments increase.

In 1984 and 1988, the Congress enacted major legislation which enticed or required the states to take large strides toward the collection-side features of CSAS and permitted two states to take minor steps toward an assured benefit. The Child Support Enforcement Amendments of 1984 required states to adopt numeric child-support guidelines which courts *could use* to determine child-support obligations. The 1988 Family Support Act made the guidelines the *presumptive* child-support award. Judges may depart from the guidelines only if they construct a written justification which can be reviewed by a higher court. Furthermore, the Family Support Act required that, by 1993, states review child-support awards of Title IV-D cases (those being handled by the Office of Child Support Enforcement) at least every three years and directed the Department of Health and Human Services to study the impact of requiring periodic review of all child-support cases.

The 1984 legislation also required states to withhold child-support obligations from wages and other income of nonresident parents who became *one month delinquent* in their payments of child support. The 1988 legislation required withholding of the

child-support obligation *from the outset* for all IV-D cases as of 1990 and for all child-support cases as of 1994.

While the 1984 legislation encouraged states to substitute administrative for judicial processes for establishing paternity, the 1988 Family Support Act *required* states to either establish paternity in at least half of the out-of-wedlock cases on AFDC or increase the proportion of such cases in which they establish paternity by three percentage points each year; to obtain the social-security numbers of both parents in conjunction with the issuance of birth certificates; and to require all parties in a contested paternity case to take a genetic test upon the request of any party, with the federal government paying 90 percent of the cost of the test.

Finally, federal legislation took two extremely cautious steps in the direction of an assured child-support benefit by granting the state of Wisconsin (in 1984) and the state of New York (in 1988) waivers that would allow them to use federal AFDC funds to pilot an assured child-support benefit.

Although the paternity, guidelines, and withholding provisions of FSA-88 are large strides toward a CSAS on the collection side, as of the early 1990's the United States has only begun the transition from the traditional to the new child-support assurance system. Despite the fact that the federal government has offered to pay 90 percent of the costs to states for automating their child-support record-keeping systems for over a decade, most states have yet to automate. Most states lack the administrative capacity to receive, monitor, and disburse all child-support payments and are therefore unlikely to be able to implement universal income withholding by 1994. While child-support guidelines have been enacted in all states, the degree to which they are being utilized, especially in nonwelfare cases, is unclear. Indeed, there is debate in many states about whether Congress really meant the guidelines and withholding provisions to apply to all cases (Robert Williams, 1992). Demonstrations of periodic updating suggest that until a way is found to routinize updating (e.g., by establishing child-support orders as a percentage of income) in prac-

tice, the vast majority of cases will not be updated. All states are a long way from universal establishment of paternity. Crossing state lines still remains a very effective way to avoid a child-support obligation.

Moreover, neither the federal government nor any state has adopted an assured child-support benefit. Tommy Thompson, Wisconsin's Governor since 1987, blocked the Wisconsin demonstration. New York State is currently conducting such a demonstration, but only mothers who qualify for welfare are eligible to receive the assured benefit. By targeting benefits on poor single mothers, New York moves away from the principle of universality that sustains our Social Security System.

Strong bipartisan support exists for further reforming the child-support system. Most important, President Bill Clinton has stated his intention both to strengthen the private child-support system and to end welfare as we know it. Heretofore, leadership on child support has emanated from the Congress.

As the provisions of the 1988 Family Support Act are implemented and new legislation is enacted, the traditional American child-support system will continue its evolution toward a new child-support assurance

system. Local judicial discretion will increasingly be replaced by the bureaucratic regularity characteristic of our social-security and income tax systems. At the very least, it seems likely that the federal government will provide funding for a number of states to pilot a non-income-tested assured child-support benefit.

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