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LOW-INCOME FAMILIES

Comparison of Incomes of
AFDC and Working Poor
Families

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Mr. Chairman and Members of the Committee:

I am pleased to be here today to discuss our comparison of the incomes and poverty status of Aid to Families with Dependent Children (AFDC) female-headed families and working poor families.

In recent years a rapid growth in welfare caseloads, concerns about program costs and beneficiaries' long-term welfare dependence, and dissatisfaction with current programs have again focused attention on the nation's welfare system. The debate centers on AFDC, which provides cash benefits to economically needy families with children. AFDC caseloads rose dramatically beginning in 1989; in 1993 nearly 5 million families were receiving over \$22.3 billion worth of AFDC benefits. AFDC families also may be receiving other types of government assistance, including Medicaid and food stamps. AFDC families received an estimated \$49.6 billion worth of benefits from these three programs in 1993.

Our testimony today will focus on four major points: (1) the range of benefits that AFDC and working poor families receive, (2) AFDC families' incomes and poverty status, (3) how AFDC families' incomes compare with those of working poor families not on AFDC, and (4) how work-related supports may help AFDC families transition from welfare to work.

In summary, we found that the incomes of AFDC families who also received benefits, such as food stamps and Medicaid, were quite similar to the incomes of families with earnings close to the minimum wage. In addition, we found that the incomes of most families in both groups fell below the poverty line.

The information we are presenting today is based on data from a national household survey, the Census Bureau's March 1994 Current Population Survey (CPS). The CPS provides information not only on families' earned incomes and cash assistance but also has cash equivalents for the following benefits provided to eligible low-income people: Medicaid, food stamps, housing assistance,¹ and school lunches. We included these four benefits in our analyses. For ease of comparison, we focused our analyses on female-headed families with two children, the most common family type receiving AFDC.

LOW-INCOME FAMILIES' BENEFITS VARY WIDELY

The AFDC program is jointly funded by the federal government and the states. Federal funds pay from 50 to 80 percent of AFDC benefit costs and 50 percent of administrative costs. The states define benefit need, set their own benefit levels, establish (within federal limitations) income and resource limits, and

¹The Census Bureau calculates cash equivalents for both public housing and Section 8 rental assistance.

administer the program. As a result, AFDC monthly benefits vary among states--from Mississippi, where a family of three received \$120 as of January 1994, to Alaska, where the monthly benefit totaled \$923. Moreover, AFDC benefits generally increase with family size.

To be eligible for AFDC benefits, recipients must generally have monthly family incomes that are well below the poverty line.² For example, the poverty threshold for a family of three is \$1,027 in monthly income; many states have income eligibility cutoffs that are less than half that amount.

AFDC families may also be eligible for noncash benefits, such as housing assistance and food stamps. The value of such noncash assistance generally does not count in determining AFDC eligibility. However, the Food Stamp Program does consider AFDC payments to be countable income, and reduces the food stamp benefit by .30¢ for each \$1 of countable cash income.

AFDC Families More Likely to Receive Certain Noncash Benefits

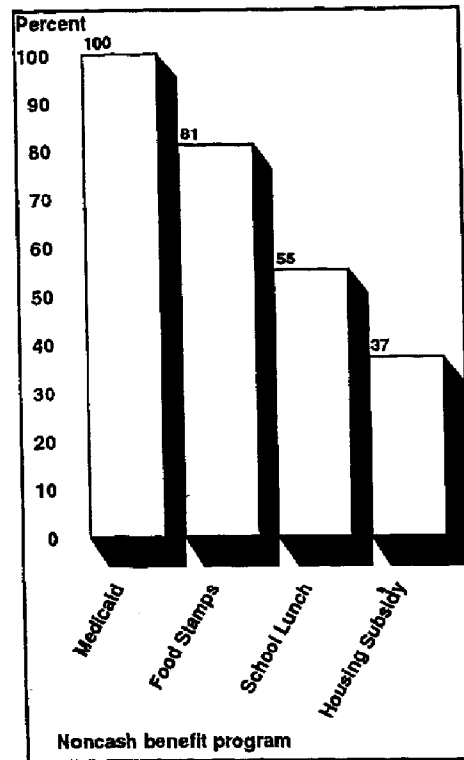
Most AFDC families receive noncash assistance from at least one program. However, the extent to which they participate in these programs may vary. For example, AFDC families are automatically eligible for Medicaid. As with AFDC, states design and administer their Medicaid programs within federal guidelines. As a result, the types and scope of benefits offered, and the amounts paid for services, vary considerably from state to state. The Food Stamp Program, on the other hand, is fully federally funded and has uniform program rules in the contiguous 48 states;³ a three-person family with comparable income generally receives the same level of assistance nationwide. Most AFDC families qualify for and receive food stamps.

AFDC, Medicaid, and food stamps are entitlements--everyone who qualifies and applies for assistance receives it. In contrast, funding for housing assistance, another low-income benefit, is limited. Moreover, housing assistance is not equally available in all parts of the country or even within some states. As figure 1 shows, only about 37 percent of AFDC families reported receiving housing assistance in 1993.

²Under the official definition of poverty, a family is considered to be living in poverty if its annual cash income is below the threshold believed necessary for that family to purchase a minimum standard of living. Under this definition, cash income includes pretax earnings and government cash transfers, such as AFDC benefits, but excludes the value of noncash benefits.

³Food stamp benefits are higher in Alaska and Hawaii.

Figure 1: AFDC Families Participating in Noncash Benefit Programs (1993)



All families are shown as participating in Medicaid because of their automatic eligibility, although not all may receive medical care in a given month.

AFDC families included are female-headed with two children.

Source: March CPS, 1994.

Some AFDC Families Have Earned Income

AFDC program rules allow recipients to work and earn income; however, AFDC benefits are gradually reduced and ultimately eliminated as recipients' earnings increase. While most AFDC families report no earnings, some AFDC family heads do work while receiving welfare. About 6 percent of women worked while receiving AFDC, according to 1992 AFDC administrative data. These data may understate workforce participation, because studies have suggested that AFDC recipients may underreport occasional or irregular work while receiving AFDC benefits because reporting earnings may lower or cause them to lose AFDC benefits. Using a different measure, CPS data showed a higher proportion of women working--38 percent in 1993. However, CPS data measure women who received AFDC at any

time during 1993 and who also worked sometime during that year.⁴ This measure, thus, includes women who may have worked part of the year and received AFDC only when they were not working.

Working Poor Families May Receive Some Public Assistance

The working poor families in our analysis⁵ were not receiving AFDC benefits. However, such families may be eligible for and receiving other types of assistance. For example, a three-person family could have a gross monthly income over \$1,200 and be eligible for a small food stamp benefit.⁶ The same family could have a monthly income as high as \$3,000 and still receive housing assistance. Of the working poor families we studied, about 22 percent received food stamps, and about 12 percent received housing assistance.⁷

Low-income families with earnings, including AFDC families, are also eligible for the Earned Income Tax Credit (EITC). This refundable tax credit was recently expanded to make the credit more generous for low-income workers. When the expanded provisions are fully implemented in 1996, a parent with two children who earns \$8,900 annually--an income just slightly above the minimum wage--would receive the maximum credit of \$3,560. This credit would be reduced beginning with an income of \$11,620 and fully phased out at a \$28,524 income.

MOST AFDC FAMILIES' INCOMES AND BENEFITS ARE BELOW THE POVERTY LINE

Developing dollar estimates of AFDC families' incomes that include noncash benefits requires obtaining cash equivalents for these benefits. However, cash equivalents are more readily available and more widely accepted for some forms of noncash assistance than others. Attaching a dollar value to Medicaid benefits is especially complex and controversial.

⁴CPS data measure whether women receiving AFDC for all or some part of a given year worked at any point during that year.

⁵For this analysis, we defined working poor as non-AFDC female-headed families of three, in which the family head worked full time for a full year and earned up to 1-1/4 times the minimum wage or \$921 per month.

⁶An eligible family of three could receive as little as \$2 and as much as about \$80 per month.

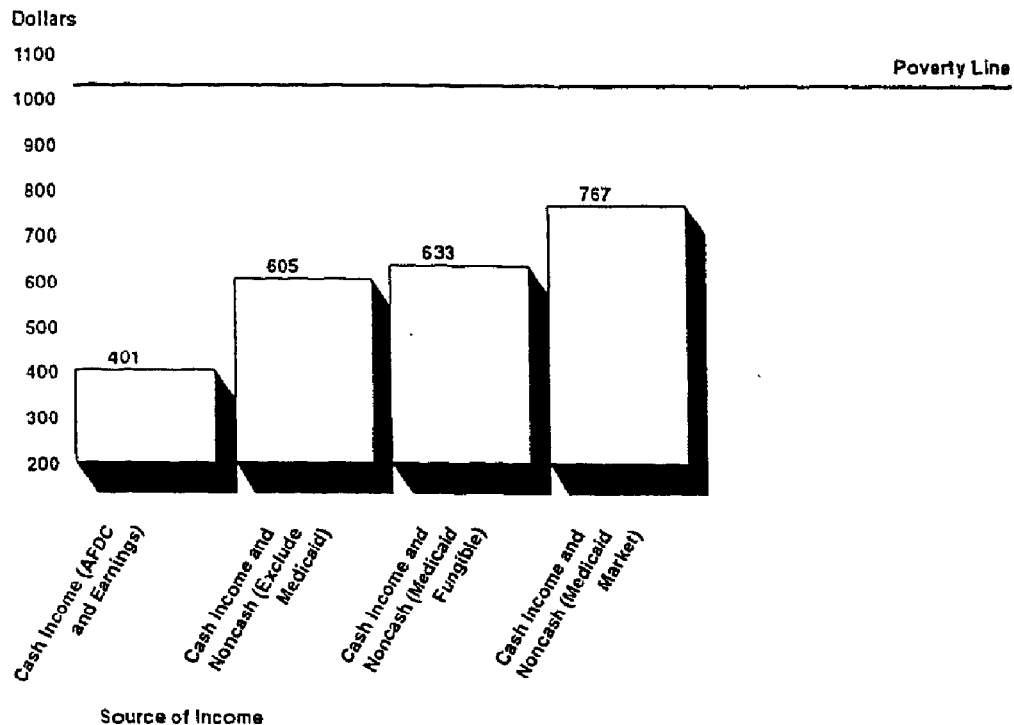
⁷Sampling errors at the 95-percent confidence level are about plus or minus 12 percentage points for food stamps and about plus or minus 9 percentage points for housing assistance.

AFDC Families' Median Income, Excluding Medicaid,
Is Well Below Poverty Line

To separately demonstrate the effects of cash and noncash assistance on family incomes, we developed median income and relative poverty measures both excluding and including noncash assistance. Accounting only for cash assistance and earnings,⁸ AFDC families' median monthly income in 1993 was only \$401--well below the poverty threshold of \$1,027 for a family of three. Using this measure, nearly two-thirds of the AFDC families were below 50 percent of the poverty line. Including noncash benefits (except Medicaid) raised their median monthly income 50 percent, to \$605. However, most families' incomes remained well below the poverty line.

⁸Earnings include salary and wages, self-employment earnings, and farm income. We added the EITC in our earnings measure and subtracted Social Security payroll taxes. The Census Bureau computes EITC amounts for low-income families; the CPS does not contain information on the numbers of families actually receiving this credit.

Figure 2: AFDC Families Median Monthly Incomes Relative to the Poverty Line (1993)



The EITC minus Social Security taxes is included in earnings.

Noncash benefits include food stamps, school lunches, and housing subsidies.

AFDC families included are female-headed with two children.

Source: March CPS, 1994.

Including Medicaid Benefits in Family Income Is Controversial

Including a value for Medicaid benefits in family income is controversial because no commonly accepted valuation method exists. Moreover, many experts argue that counting the value of medical care as if it were income can be misleading.⁹ For these reasons,

⁹Some researchers argue that, unlike food and housing needs, the health needs of families in comparable circumstances vary enormously depending on the health status of household members.

we have presented median income estimates excluding Medicaid. However, to show the possible effects of Medicaid benefits on family income, we are also presenting estimates that include Medicaid.

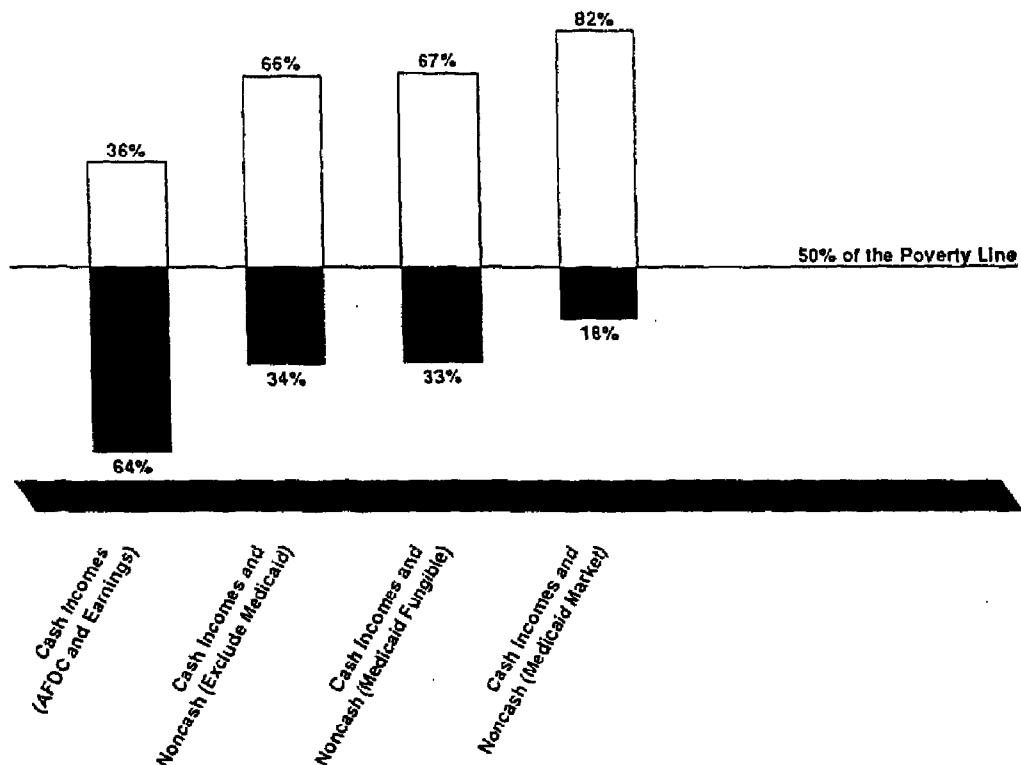
We used two different valuation approaches for Medicaid-- fungible¹⁰ and market value;¹¹ the Census Bureau has adopted the fungible value approach. Adding Medicaid benefits increased AFDC families' median incomes to \$633 (fungible) or \$767 (market). While \$767 is nearly double the median income we estimated for earnings and cash assistance alone, this income is still well below the poverty line.

Moreover, because medical care prices are so high, some families who are eligible for Medicaid could theoretically receive resources above the poverty line in medical benefits alone.

¹⁰The fungible value approach counts Medicaid benefits as income only to the extent that they free up resources that could have been spent on medical care. For example, if family income is not sufficient to cover the family's basic food and housing requirements, the fungible value methodology treats Medicaid as having no income value.

¹¹The market value is calculated by dividing actual expenditures by the number of people enrolled in a given risk class.

Figure 3: AFDC Families With Incomes Below 50 Percent of Poverty Line (1993)



AFDC families included are female-headed with two children.

Source: March CPS, 1994.

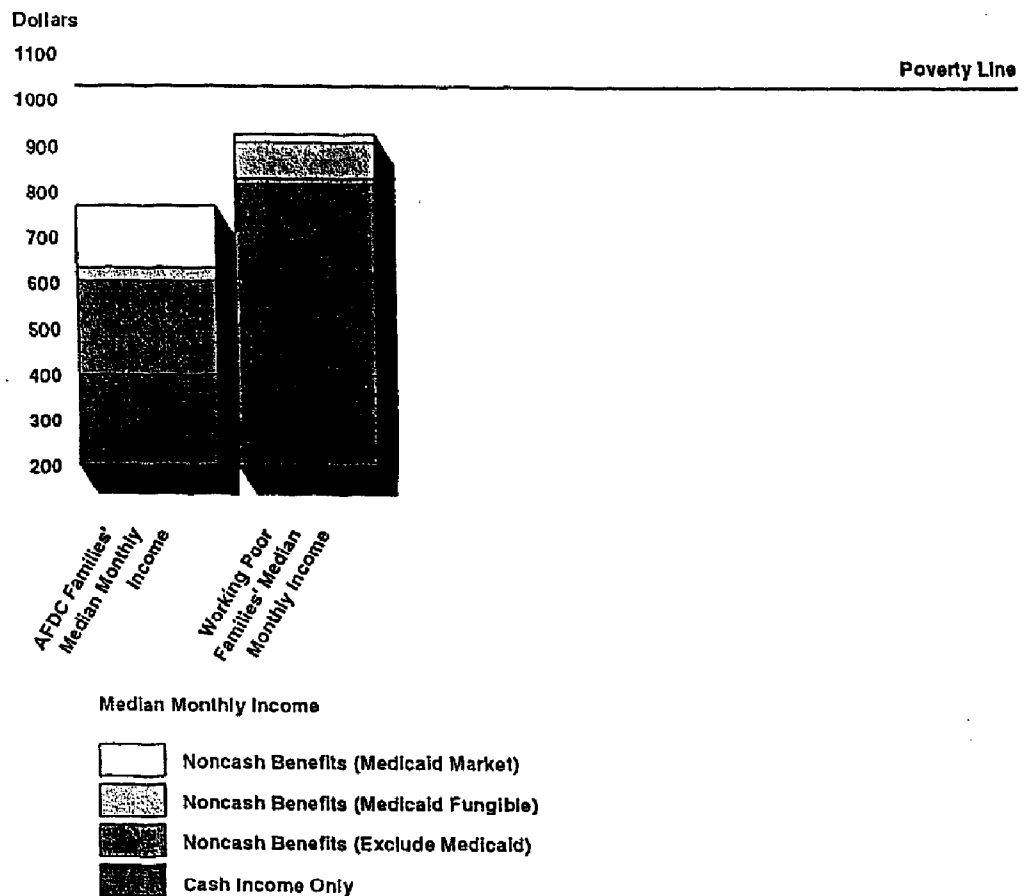
WORKING POOR FAMILIES FARE LITTLE BETTER THAN AFDC FAMILIES

To determine whether working poor families not receiving AFDC had higher incomes than AFDC families, we analyzed the income and noncash benefits a working poor family receives. Although working poor families with full time, full year earnings up to 1-1/4 times the minimum wage--\$921 a month--did have higher median incomes than AFDC families, many were still below the poverty line. Moreover, our analysis did not include work-related expenses, such as child care, which could be significant for these families. Accounting for these expenses could possibly increase the number of working poor families that could be financially worse off than some AFDC families.

As we noted earlier, some working poor families also received noncash public assistance such as food stamps. We estimated their

median incomes both excluding and including these benefits, as we did for AFDC families. Using earned income only, working poor families' median monthly income was \$819--about \$50 higher than the highest estimate of AFDC families' income. When noncash benefits, including health benefits, were added, these families' median monthly income rose to \$926 per month. As figure 4 shows, working poor families' median monthly income was nearly \$160 higher than that of AFDC families when noncash assistance was included. Even with these benefits added, over 70 percent of working poor families had incomes below the poverty line.

Figure 4: Comparison of AFDC and Working Poor Families' Median Monthly Income (1993)



Cash income includes the EITC minus Social Security taxes.

For working poor families, the employer contribution to health insurance was included along with the Medicaid values.

AFDC families included are female-headed with two children.

Source: March CPS, 1994.

Work-Related Expenses May Be Significant

While working poor families had a median monthly income higher than AFDC families', working poor families may incur significant work-related expenses. These expenses may adversely impact their ability to stay employed. In taking paid employment, workers often incur additional expenses, such as the costs of tools or uniforms, travel to their workplaces, or paid child care. For example, child care costs can be a significant portion of low-income working families' budgets. Working poor families with child care costs spent on average \$260 a month for child care in 1991, according to a Census Bureau survey.

WORK-RELATED SUPPORTS MAY HELP TRANSITION FROM WELFARE TO WORK

The two types of families we examined, AFDC families and working poor non-AFDC families, are frequently the same families observed at different points in time. Many low-income families go on and off the welfare rolls because of events that affect their ability to work at a particular time--for example, changes in availability of a job, child care arrangements, health of children, and access to affordable transportation. Nearly 64 percent of welfare recipients leave AFDC within 2 years; however, between two-thirds and three-fourths of those who leave AFDC return within a 5-year period, according to a recent study.¹²

When AFDC recipients move into the workforce, they generally work at low paying jobs and incur the types of job-related expenses mentioned earlier. Some discussions of changes in the welfare system have incorporated ideas about how to reduce the number of working poor who return to welfare, in addition to concentrating on ways to get jobs for welfare recipients. Our recent child care study¹³ found that one work-related support--child care subsidies--can help women on welfare move into the workforce and stay there. For example, providing a full subsidy to mothers who pay for child care could increase the number of poor mothers who work from 29 to 44 percent.

A second work-related support--the EITC--may also help women stay in the workforce. A low-wage worker can substantially supplement her family income with the EITC. When fully implemented in 1996, the EITC would provide a woman with two children who works full time at the minimum wage--\$737 per month--an income above the

¹²LaDonna A. Pavetti, "The Dynamics of Welfare and Work: Exploring the Process by Which Women Work Their Way Off Welfare." (Harvard University, May 1993).

¹³Child Care: Child Care Subsidies Increase Likelihood That Low-Income Mothers Will Work (GAO/HEHS-95-20, Dec. 30, 1994).

poverty line. The EITC would add nearly \$300 to her gross monthly income, for a monthly total of \$1,033.

These work-related supports could become more important under welfare reform. Most proposed reforms call for moving hundreds of thousands of parents from welfare to work. Work-related supports, such as the child care subsidy and EITC, could serve as important factors in helping these former welfare recipients remain in the workforce and preventing non-AFDC working poor families from becoming welfare dependent.

CONCLUSIONS

The median monthly income of AFDC three-person families--a female head with two children--was below the poverty line, even when noncash benefits were added in. Working poor non-AFDC families' median income was higher--\$926 as compared with \$767 for AFDC families--but still below the poverty line. Moreover, low-wage workers may incur significant job-related costs, such as child care, which could increase the number of them financially worse off than some AFDC families. Two public supports available to low-income workers--child care subsidies and the EITC--can be important factors in helping women join and stay in the workforce. These supports may become more important under welfare reform, as policymakers seek changes to move more welfare recipients from welfare to work.

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Mr. Chairman, that concludes my prepared statement. At this time, I will be happy to answer any questions you or other members of the Committee may have.

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RELATED GAO PRODUCTS

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Welfare to Work: Current AFDC Program Not Sufficiently Focused on Employment (GAO/HEHS-95-28, Dec. 19, 1994).

Child Care: Promoting Quality in Family Child Care (GAO/HEHS-95-36, Dec. 7, 1994).

Child Care: Current System Could Undermine Goals of Welfare Reform (GAO/T-HEHS-94-238, Sept. 20, 1994).

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Welfare: Income and Relative Poverty Status of AFDC Families (GAO/HRD-88-9, Nov., 1987).

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Public Assistance Benefits Vary Widely From State To State, But Generally Exceed The Poverty Line (GAO/HRD-81-6, Nov. 14, 1980).

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