Cooperation Needed to Solve Welfare Cliff Problem

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By Erik Randolph, Director of Research, Georgia Center for Opportunity

Introduction

Embedded in America's welfare system are cliffs where recipients can experience loss in benefits greater than what they might gain from increased earnings. Recently demonstrated again for eight southern states with an expanded and updated computational model, this fact calls for a public policy solution.

States—especially the eight southern states in the study—share a common interest in solving the problem. However, the solution is not simple given the complexity of the federal-state welfare system under which states must operate. Therefore, states should consider adopting common principles on the best ways to make the system more rational and also work together to achieve success. This briefing presents those principles and an outline for building a coalition.

Welfare Cliff Problem Pervasive

Funded by a Searle Freedom Trust grant, the Georgia Center for Opportunity (GCO) expanded its welfare cliff model to analyze seven other states in the south. This paper is the second of two briefings on the expanded model. Our first publication[1] demonstrated that the welfare cliff problem is pervasive among the eight states in the study: Alabama, Florida, Georgia, Louisiana, Mississippi, North Carolina, Tennessee, and Texas.

We were not surprised by the results. Although states differ in their approaches, all states are part of the same federal-state system subject to federal laws, regulations, rules, and carved-out exceptions. While the system allows for some consistency across states in addressing the needs of the poor, an unfortunate consequence is that states can also share in its problems. Among the known problems are marriage penalties,[2] shortfalls in program integrity—intended to prevent fraud, waste, and abuse—and, of course, welfare cliffs, which is the focus of our recent study.

1 Erik Randolph, Confirmed. Welfare Cliffs Pervasive in 8 Southeast States, Policy Brief, Georgia Center for Opportunity Policy, May 2020: https://georgiaopportunity.org/wp-content/uploads/2020/05/Confirmed-Welfare-Cliffs-Pervasive-in-8-Southeast-States.pdf

2 Erik Randolph, Deep Red Valleys, Georgia Center for Opportunity, February 2017: https://georgiaopportunity.org/wp-content/uploads/2017/02/Deep-Red-Valleys_WEB.pdf

Federal-State Framework

Dedicated to the study of economics, markets, and liberty, the Library of Economics and Liberty features an online encyclopedia. Its entry on "welfare"—written by a professor of economics at Stanford University and a research fellow at the Hoover Institution—leads with the following paragraph:

> The U.S. welfare system would be an unlikely model for anyone designing a welfare system from scratch. The dozens of programs that make up the "system" have different (sometimes competing) goals, inconsistent rules, and overlapping groups of beneficiaries. Responsibility for administering the various programs is spread throughout the executive branch of the federal government and across many committees of the U.S. Congress. Responsibilities are also shared with state, county, and city governments, which actually deliver the services and contribute to funding.[3]

The authors set the word "system" in quotation marks. The inconsistencies and haphazard manner by which welfare programs evolved happened over nearly ninety years. It was never designed as a system but resulted from various pieces of legislation emerging from different Congressional committees. This is not only true of the federal government but also true for the states. The oversight and administration among the states are spread across various legislative committees and administrative agencies within each state.

The modern welfare system has its roots in the 1930s when the Federal government became more involved, eventually supplanting in part and complicating state and local efforts. Under President Franklin D. Roosevelt, the federal government created the Aid to Families with Dependent Children (AFDC) program (1935) and became involved in public housing (1937). The National School Lunch Program (NSLP—1946) began under President Harry S Truman. Food stamps (1964) were initiated by John F. Kennedy but signed into law by Lyndon B. Johnson. Johnson also created Medicaid (1965), the School Breakfast Program (SBP—1966), and the Women, Infants, and Children (WIC) program (1966).

The Supplemental Security Income (SSI) program (1972) was added under President Richard Nixon's administration. Section 8 Housing (1974) and the Earned Income Tax Credit (EITC—1975) became law under President Gerald Ford. The Low Income Heating and Energy Assistance Program (LIHEAP—1981) was enacted under President Ronald Reagan. President George Herbert Walker Bush signed into law the Child Care Block Grant (CCBG) program (1990). President William Clinton presided over the replacement of the Great Depression era AFDC program with the Temporary Assistance for Needy Families (TANF) program (1996). Clinton also added his signature to the Additional Child Tax Credit (ACTC—1997) and the Children's Health Insurance Program (CHIP—1997). President Barack Obama signed into law the Affordable Care Act (ACA—2010) that created govern-

3 Jeffery M. Jones and Thomas MaCurdy, "Welfare," Online Encyclopedia of the Library of Economics and Liberty, accessed May 14, 2020: https://www.econlib.org/library/Enc/Welfare.html.

ment-run health insurance exchanges (HIX), the premium tax credit (PTC), and would have mandated Medicaid expansion for all adults under 138 percent of the federal poverty level had not the U.S. Supreme Court ruled against it in a 7-to-2 decision.

Most welfare programs are a mixture of federal and state funding and administration. However, among these major programs, a few programs are run exclusively by the federal government.

The TANF and childcare programs are block grants to the states, giving wide latitude on how states may spend the money and run the programs.

Medicaid and CHIP are state programs where states can participate with the federal government to receive matching funds along with controlling rules and regulations. The Affordable Care Act has health insurance exchanges that can be run by the states or the federal government. However, the Premium Tax Credit is run exclusively by the federal government.

All the food programs—the National School Lunch Program, the School Breakfast Program, Women, Infants, and Children's special supplemental nutrition program, and food stamps that was renamed the Supplemental Nutrition Assistance Program (SNAP) in 2008—are funded by the federal government but administered by the states and local school districts.

Public housing and Section 8 housing choice vouchers are funded by the federal government but are mostly run by public housing authorities that are creatures of state law but operate under federal regulation. In some cases, like for most counties in Georgia, a state agency runs Section 8 housing.

Funded exclusively by the federal government, the Earned Income Tax Credit and the Additional Child Tax Credit are cash assistance programs run through the U.S. tax system.

GCO's Principles for Transformation

Despite jurisdictional differences in how governments approach welfare assistance, there are principles that can help make the system more responsive and responsible. Already explored by GCO in its second report on systemic welfare reform, these principles are displayed in the sidebar. [4]

These principles can be viewed as a powerful guideline on how well government welfare programs are faring. A cursory rundown of those principles would demonstrate that the welfare system falls short of what a well-designed system should do. Although beyond the scope of this briefing, it could be shown that not a single principle is being met at an adequate level when the system as a whole is evaluated. For example, contrary to the principle, the administration of all welfare programs is not unified nor coordinated. It is quite the opposite: fragmented across multiple state and federal agencies often with little or no coordination among those programs.

Our focus in this briefing is the eighth principle—the natural financial advantage to earn more money is preserved. In the negative, this means there are welfare cliffs as our recent study demonstrated for eight southern states. [5]

When attempting to solve welfare cliffs, it is important not to attempt a solution in a vacuum. Rather, the solution should be done in a way that is consistent with the other principles.

For example, it would not be good if the cliff solution

PRINCIPLES FOR SYSTEMIC REFORM

- Administration is unified and coordinated
- The system has program integrity safeguards
- Case management exists across all programs
- Individuals and families are treated holistically
- Personal and parental responsibilities are emphasized
- Employment is promoted whenever feasible
- Excess resource tests are implemented and enforced across programs
- The natural financial advantage to earn more money is preserved
- Natural support systems are identified, encouraged, and utiliized
- Benefits provided meet truly essential needs and no more
- For most cases, program participationis time-limited
- The system is linked to economic and educational policies

4 Erik Randolph, System Welfare Reform in Georgia: Part 2: Principles and Framework for Reform, Georgia Center for Opportunity, January 2018: https://georgiaopportunity.org/wp-content/uploads/2018/02/WEB-Part-1-Systemic_Welfare_Reform.pdf.

5 Erik Randolph, Confirmed. Welfare Cliffs Pervasive in 8 Southeast States, Policy Brief, Georgia Center for Opportunity Policy, May 2020: https://georgiaopportunity.org/wp-content/uploads/2020/05/Confirmed-Welfare-Cliffs-Pervasive-in-8-Southeast-States.pdf

worsened marriage penalties, such as the Earned Income Tax Credit that does not have a cliff but a marriage penalty.

Likewise, the solution cannot become prohibitively expensive, such as the case with Section 8 Housing. Because of the expense of the program, funding has always been so grossly inadequate that only a small fraction of eligible families can receive a housing choice voucher.

In response to these challenges, GCO proposed a framework on how a state government can organize its welfare system to meet the principles, including eliminating the welfare cliff.[6] Although the proposal was specific to the state of Georgia, the framework could work for other states, or at least provide a starting point for other states to restructure their systems.

In general, the proposal would streamline the welfare system into a unified eligibility system across all agencies. All welfare programs would be consolidated into five modules: food assistance, cash assistance, shelter assistance, childcare assistance, and medical assistance. The benefit levels would be coordinated by an eligibility rules engine designed to eliminate all welfare cliffs and marriage penalties.

Other states may find alternative frameworks that can also meet the same principles. Differences among the states are a strength of the system, not a weakness. They allow the states to learn from each other's successes and mistakes. They also allow the states to tailor their solutions to circumstances not shared by other states.

Process for Reform

Although states can make headway in reducing the cliffs, the efforts will fall short without cooperation at some point from the federal government. By the way, this is also true for eliminating marriage penalties. In short, cooperation from the federal government is essential.

The cliff model enables evaluation of when the cliffs occur for specific family structures. It also enables policy analysts to focus on specific programs and to discover which programs are the most problematic. Furthermore, it enables analysts to discover the factors underlying the distortions that can assist them in crafting solutions.

There are two basic ways that cliffs can occur. First, whenever there is a hard cutoff in eligibility, there is the potential for a cliff, which we can define as a type one cliff. These cliffs can even occur multiple times within a single program if there are levels of eligibility, such as with the National School Lunch Program that moves children from free school meals to reduced price meals with a hard cutoff or a state's children health insurance program that may have different tiers of income categories.

6 "System Welfare Reform in Georgia: Part 2: Principles and Framework for Reform."

All the major food assistance programs have type one cliffs. Subsidized school meals, as just explained, and WIC supplemental food assistance both always have cliffs for this reason. Food stamps is fickle when it comes to cliffs. It can have cliffs if no one in the household is disabled or elderly. However, the size of the SNAP cliffs varies widely depending on the income disregards that a family qualifies for. For example, if a household without a disabled or elderly member has the maximum excess shelter deduction, there will be a cliff.

Likewise, for the medical assistance programs, there are cliffs. For adults, Medicaid always has cliffs unless the adult can jump over the cliff by securing employment with an employer who provides truly affordable health coverage. When this is not the case, the adult can encounter high costs for purchasing expensive coverage through the government's health insurance exchanges, even with the premium tax credit.

One complication created by medical assistance programs is they do not treat families holistically. Children are treated separately from the family. When the families' incomes are no longer eligible for a child to be on Medicaid, that child can qualify for the state's children health insurance program that itself has cliffs. Making medical assistance even more confusing, eligibility requirements for CHIP often change based on the age of the child, creating situations where children in the same family can have different types of coverage, or one child can have coverage and another child does not.

The worst offender for type one cliffs is subsidized childcare services. No state studied successfully phases out the benefit, and the cliffs can be steep. Rather, state programs—with the complicity of the federal government—typically encourage the higher quality settings that come with higher costs, and consequently higher cliffs.

The second cliff type is the stacking effect demonstrated in an earlier GCO paper.[7] The greater the number of welfare programs an individual qualifies for, and the greater the benefit levels, the greater the likelihood for a cliff. This astounding finding said that this type two cliff can occur even if the underlying programs themselves do not have type one cliffs.

In finding solutions to the cliffs, the states have some ability to mitigate the impacts of some programs by amending state plans, especially for those programs where they have more control, such as TANF and subsidized childcare.

In other cases, states can apply to the federal government for waivers to program rules, enabling states to be more aggressive in addressing cliffs and making programs more effective in helping people emerge from impoverished conditions. For example, the food stamp program allows for demonstration projects including for the purposes of increasing "self-sufficiency of … recipients" and

7 Erik Randolph, Systemic Welfare Reform in Georgia. Part 1: The Case for Reform, Georgia Center for Opportunity, January 2018: https://georgiaopportunity.org/wp-content/uploads/2018/02/WEB-Part-1-Systemic_Welfare_Reform.pdf.

testing "innovative welfare reform strategies." [8]

Medical assistance programs likewise allow for waivers, such as the Section 1115 waiver of the Social Security Act for "experimental, pilot, or demonstration" projects in Medicaid.[9] Additionally, there is the sweeping Section 1332 waiver of the Affordable Care Act[10] that provides relief and flexibility to the states on the federal provisions for qualified health plans, health insurance exchanges, cost sharing subsidies, refundable tax credits, shared responsibilities of employers, and the individual mandate.

In other cases, states have little to no flexibility. For example, the Earned Income Tax Credit, which is comparable in size to food stamps, is an inflexible program operated by the Internal Revenue Service. Although the original intention was to provide cash flow with regular payments to recipients, Congress removed that provision at the beginning of the Obama Administration. Now recipients must wait until they have filed their tax returns and received their tax refunds. Because recipients get the money in one lump sum, federal welfare agents have told us privately that welfare agencies need to develop strategies to advise recipients on how to spend the money wisely. It would be much easier and better for the recipients if the cash flow were reestablished.

Momentum Needed

The federal-state welfare complex presents a reality. The more the federal government cooperates with the states, the more comprehensive and effective can be the solutions. Although there is always resistance to change, there are positive signs that cooperation is possible. Various demonstration projects already exist in federal law. Members of Congress regularly express interest in reforming the system, especially in regard to welfare cliffs and marriage penalties. There is bipartisan interest among blue and red states to fix welfare cliffs and marriage penalties. And the current federal administration, which may soon change, has been open to and active in establishing relationships to finding solutions.

However, despite the interest, the ability of a single state to influence the federal government is challenging. Having a member in congress who is well placed in a leadership position or an administrator in the federal government in key position clearly helps, but it is probably not enough. The best prospect for success is when states band together and form coalitions for change. As the coalition grows, their influence increases, and the possibility for change becomes more probable.

8 7 U.S. Code § 2026.Research, demonstration, and evaluations.

9 42 U.S. Code § 1315. Demonstration Projects.

10 42 U.S. Code §18051 State flexibility to establish basic health programs for low-income individuals not eligible for Medicaid, and 42 U.S. Code §18052. Waiver for State innovation.

How States Can Work Together

More specifically, state-based policy think tanks can help states in putting together a successful coalition to influence positive changes at the federal level that will benefit not just the coalition of states, but all states. By working together, they can better define goals and a common strategy. They can build support among local leaders, advocacy groups, state officials, and other societal leaders. When coalitions expand, they can become movements.

Although not yet demonstrated, it is likely that all states have problems with cliffs. The current model demonstrates that the welfare cliff problem is pervasive in eight southern states. This finding was unsurprising given the federal-state structure. Other states clearly suffer from the same problems and can easily become part of the movement. Expanding the model further would likely provide confirmation of the pervasiveness and accelerate the expansion of the coalition.

While computational models and statistics are essential for making good public policy decisions, many legislators and the general public relate better to human stories. Reading about a real person who encountered a cliff or is experiencing a marriage penalty can give people the burning desire to do something about it. In this regard, state-based policy think tanks can work together on compiling the real life stories that demonstrate the harm welfare cliffs cause.

Numbers are still important. Here, too, state policy groups can collect, share, and standardize program data in a way that better defines outcomes and measures success. They can precisely identify those changes that can be accomplished at the state level without federal approval and share their experiences.

For example, the Georgia Center for Opportunity developed a working paper reference guide[11] outlining state flexibility under federal laws and rules regarding welfare policy. GCO also shared the information with federal officials also interested in reforming the system. However, the information has not been updated in four years, and federal law and regulations are constantly--albeit slowly at times--evolving. In the meantime, some states have discovered creative ways to use their flexibility that were not anticipated in the original working paper, and courts have weighed in on some of those developments. Therefore, collaboration among state-based think tanks would allow for an updated and more complete picture of the federal-state landscape.

Moreover, state welfare agencies regularly cooperate and learn from each other. States typically have data exchanges to enforce program integrity measures, such as catching abusers who might collect food stamps in Alabama, Florida, and Georgia all at once. Additionally, welfare officials in Georgia informed us that they follow how other states operate and try to incorporate the most promising developments into their own system. Collaboration in these areas is mutually beneficial and essential.

States can also cooperate on developing waiver proposals. Waiver requests can be sophisticated and often require fiscal analysis to prove to the federal government that it will not cost the federal government more. When one state successfully receives a reform-minded waiver, it provides a precedent for other states to follow. Federal officials also become familiar with the concepts and can provide better advice for the states that follow.

There are also opportunities for collaboration among states on demonstration projects or running programs. For example, the Affordable Care Act provides collaborative opportunities relative to operating health insurance exchanges. More comprehensive than that, GCO has published studies[12] advocating for risk equalization as a way to achieve universal coverage at more affordable prices while maintaining high quality of care. The studies argue that risk equalization solves the problem of higher costs for persons with preexisting conditions and does not resort to relying on expanding Medicaid, which is known for poor health outcomes. A risk equalization plan would be an excellent policy area where collaborative effort would be beneficial.

As state-based policy think tanks explore changes in federal laws and rules, they come up with approaches that would work not just for their own states but for other states as well. Here there is a prime opportunity for collaboration. These think tanks can develop model legislation for the states and the federal government, such as GCO developed for Georgia.[13] Model legislation gives state and

11 Erik Randolph, Georgia's Welfare System Reference Guide: Program Bases and Flexibility for Reform Assessment, Working Paper, Georgia Center for Opportunity, 2016: https://georgiaopportunity.org/wp-content/uploads/2019/02/Final-Georgia-Welfare-System-Reference-Guide.pdf

12 For example, see Erik Randolph, A Real Solution for Health Insurance and Medical Assistance Reform, Georgia Center for Opportunity, January 2018: https://georgiaopportunity.org/wp-content/uploads/2018/02/WEB-A-Real-Solution-for-Health-Insurance-.pdf

13 "Outline of Legislation for Increasing Work Opportunities by Reducing Cliffs," Georgia Center for Opportunity Submission to the Georgia Rural Development Council and legislative leaders, 2018, https://georgiaopportunity.org/wp-content/uploads/2020/05/Outline-Enabling-Legislation-for-Increasing-Work-Opportunities-final.pdf

federal legislators a good starting point to enact the kind of changes that are necessary. Further assistance can be provided by providing policy summaries, analyses, and testimonies before legislative committees.

Conclusion

The current welfare system, while necessary to help vulnerable individuals and families, can create irrational obstacles, such as welfare cliffs. Because the federal government is heavily intermingled with the states in the funding and regulation of the system, it is necessary for states and the federal government to work together to come to an effective systemic solution.

GCO has identified principles and a framework on how to make the system more rational and better able to deliver on its purpose: to assist people in tough times, while always encouraging independence and self-sufficiency. For GCO's path to be successful, it will require more than one state pressing for reform. By building a coalition and working together, states increase the likelihood of success.

Finally, there will be no losers if we succeed. The real winners will be those who are now stuck in the system. They will be given clearer pathways that can help them escape even intergenerational poverty. The second winner will be society who will benefit from increased productivity and prosperity.

*About the Author

Prior to becoming director of research for GCO, Erik Randolph consulted on public policy issues with organizations in seven states, including Georgia, Maine, Illinois, and Mississippi, plus organizations in Washington, D.C., including the Heritage Foundation and the Secretary's Innovation Group representing about 23 states. Prior to his consulting career, Erik was a special assistant to the Pennsylvania Secretary of Public Welfare, helping to run what was considered to be the largest state agency in the country. He also has served as an analyst to the Committee on Appropriations of the Pennsylvania House of Representatives, an economic development analyst for Pennsylvania's Commerce Department, a research fellow to New York State's Science and Technology Foundation, and a program evaluator for the U.S. Government Accountability Office.