CBO MEMORANDUM

THE ADMINISTRATION'S WELFARE REFORM PROPOSALS: A PRELIMINARY COST ESTIMATE

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CONGRESSIONAL BUDGET OFFICE

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INTRODUCTION AND SUMMARY

The Clinton Administration's welfare reform proposal, the Work and Responsibility Act of 1994, was introduced on June 21, 1994, as H.R. 4605 in the House and S. 2224 in the Senate. It was one of more than two dozen proposals introduced in the 103rd Congress to change the Aid to Families with Dependent Children (AFDC) program and its related training and work programs. Several committees held hearings on the bill during the summer of 1994, but the Congress adjourned before taking action on it. Discussion of welfare reform was prominent during the fall political campaigns, and the issue is likely to be a priority of the 104th Congress.

This memorandum presents the Congressional Budget Office's (CBO's) preliminary analysis of the Administration's proposal and the issues surrounding welfare reform. The methodology underlying this estimate will serve as the groundwork for future analyses of other proposals for welfare reform. It incorporates economic and technical assumptions from CBO's February 1994 baseline, so the estimates will change when the baseline is updated in early 1995 to incorporate new information about the economy and the AFDC population.

Provisions in titles I through VIII of the Work and Responsibility Act would expand training and work programs for recipients of Aid to Families

with Dependent Children, impose a two-year limit on AFDC benefits for certain young mothers, liberalize the treatment of earnings and resources in calculating benefits for AFDC families, increase child support enforcement efforts, and extend child care subsidies to families whose incomes are near the poverty level. Title IX is designed to finance the spending in the first eight titles through a number of spending cuts and revenue measures, including capping expenditures in the AFDC-Emergency Assistance program and reducing welfare payments to legal aliens.

CBO estimates that if the first eight titles of the bill had been enacted by October 1, 1994, they would have increased mandatory federal outlays by $0.2 billion in fiscal year 1995 and $11.8 billion through 1999. The combination of spending cuts and revenue increases in title IX would have amounted to $0.2 billion in 1995 and $6.9 billion over the five-year period. Overall, CBO estimates that the enactment of H.R. 4605 would have generated a net federal cost of $4.8 billion during the 1995-1999 period (see Appendix Table 1). The bill would also authorize an additional $0.1 billion in spending between 1995 and 1999, subject to annual appropriations. CBO estimates that titles I to VIII of H.R. 4605 would have increased state and local government spending by $2.6 billion over the 1995-1999 period (see Appendix Table 2).

Much uncertainty surrounds these estimated fiscal effects. H.R. 4605 gives states considerable flexibility in determining when and how to carry out mandated provisions and leaves the adoption of other key provisions entirely up to the states. CBO assumed that all states would spend sufficient resources to meet the bill's required participation rates for training and work programs. For other provisions, CBO projected states' behavior by examining their interest in pilot programs operated under federal waivers and discussing the provisions with numerous state and local officials. For some provisions, CBO may need to revise its assumptions about state behavior because of changes in the political leadership of many states after the 1994 elections.

Unless specified otherwise in the legislation, CBO assumed that the states would carry out major reforms, including the time limit on benefits, beginning on October 1, 1995. Although some states would not be ready to initiate these programs within one year, other states, which have experimented with similar reforms through federal waivers, could accelerate their application. CBO assumed that the effect would be as if all states carried out the programs on October 1, 1995. Given the delay, CBO's estimates represent the costs and savings over the initial four years of the reform.

CBO's estimate of $11.8 billion for the welfare reform proposals in titles I to VIII is higher than the $9.3 billion estimate released by the

Department of Health and Human Services (HHS) in June 1994. CBO's estimates of child care and child support enforcement costs, welfare savings, and some other expenses differ from those of HHS.

FEDERAL GOVERNMENT COSTS AND SAVINGS

Titles I and II: JOBS and WORK

Titles I and II would expand federal spending for training and work-experience programs for AFDC recipients, resulting in increases in net outlays of $340 million in 1996 and $2.5 billion through 1999. These figures include the costs of expanding the existing Job Opportunities and Basic Skills (JOBS) training program and of creating a new work-experience program called WORK. The net outlay totals also incorporate estimated savings that would accrue in AFDC and other programs as recipients, through training and work experience, acquire job skills and reduce their reliance on welfare. This $2.5 billion estimate does not include associated child care costs, which are shown under title III.

H.R. 4605 would make three changes in the way states train AFDC recipients. First, the bill would concentrate on moving recipients through the

JOBS program within two years. Second, for recipients who exceed their time limits, states would provide jobs; typically, entry-level positions in public or nonprofit agencies, where participants would perform clerical, park service, or maintenance work. Third, the bill would initially require states to focus their efforts on younger recipients, specifically those born after 1971, but would not limit states to that group. Single parents with very young children, disabled individuals, and part-time workers, as well as families that live in remote areas, would be exempt from training and the time limit.

The bill funds additional training slots by raising the existing federal spending cap for the JOBS program. The cap would increase in 1996 from $1 billion to $1.75 billion and in 1999 to $1.9 billion. Although the bill would raise the cap to $1.75 billion in 1996, $0.3 billion of this amount would be appropriated to the Secretary of Health and Human Services for use in 1996 and subsequent years. The Secretary would use this $0.3 billion to match spending in states that had exceeded their individual spending caps.

In addition, the bill would create the WORK program, a new capped entitlement that would provide jobs for people who exceed their two-year limits. Federal spending would be capped at $0.2 billion in 1998 and $0.7 billion in 1999. The funding of wages for WORK participants would be matched at the state's regular AFDC rate (a national average of 55 percent)

and would not be capped. The federal share of total spending in JOBS would be increased from about 61 percent to an estimated average of 67 percent in 1996, rising to 71 percent by 1999. In addition to raising federal caps and matching rates, amendments to current law would raise participation rates, tighten exemption categories, and require states to enroll more AFDC recipients in training or work activities.

CBO uses data on AFDC recipients collected by the Census Bureau through the Survey of Income and Program Participation to model the movement of individuals through the JOBS and WORK programs and various exemption categories. CBO estimates that in 1999, 1.83 million AFDC families will be headed by an adult born after 1971 (these represent families that would be phased into the new time-limited program). Families not included in the time-limited program by 1999 would include 2.74 million headed by adults born in 1971 or before and 0.8 million cases without an adult recipient. Of the phased-in families, about 670,000, or 37 percent, would be exempt from the time limit and participation in the JOBS program in an average month. The remaining 1.16 million families would be deemed "mandatory," which means that, if asked, they would have to participate in either the JOBS or WORK program or face a reduction in or suspension of their AFDC payments.

Most participants in the JOBS and WORK programs would come from this population of mandatory workers. But states would also have to serve volunteers interested in enrolling in training or education programs, depending upon the availability of state resources. Incorporating the standards of participation outlined in the bill, CBO estimates that the average number of monthly JOBS participants would increase from current projections of about 600,000 to approximately 760,000 in 1999. Participation in the WORK program would begin in 1998; that is, two years after states establish their time-limited programs. The average monthly participation in WORK would start at an estimated 100,000 in 1998, increase to 240,000 in 1999, and continue to rise in subsequent years, as more families enter the time-limited program.

Estimates of costs for titles I and II depend on average costs for JOBS and WORK programs, as well as the number of participants in each program. CBO derives average participant costs using administrative data from the JOBS program and evaluations from demonstration projects of similar programs operated in the 1980s. By 1999, the average combined federal and state cost of keeping a JOBS training slot filled with participants for one year is estimated to be $3,000. A comparable slot in the WORK program would cost nearly $4,000 annually ($2,600 in operational costs and $1,400 in wages). The cost of providing transportation services is included in the $3,000 estimate

for JOBS but not in the $2,600 estimate for WORK because participants in the WORK program would be expected to cover their own transportation expenses. States would spend more on a typical WORK position because--unlike JOBS activities--it would involve costs for wages and Federal Insurance Contribution Act (FICA) payments. In addition to wage and FICA expenses, these averages represent the costs of creating the education, training, or work positions; monitoring attendance; imposing penalties; and providing support services other than child care.

In 1999, average monthly JOBS participation (760,000) multiplied by average costs ($3,000) yields total federal and state spending of $2.3 billion. Other provisions in titles I and II would raise the JOBS total to $2.4 billion in 1999, and the federal share would be $1.7 billion (that is, 71 percent). Subtracting the $1 billion in expected federal JOBS expenditures under current law yields an estimated increase in JOBS program outlays of $0.7 billion in 1999.

The WORK expenditures, subject to the new amount of the cap in federal spending, can be derived similarly. Average monthly participation (240,000) multiplied by the operational costs subject to the cap ($2,600) produces total 1999 spending of $0.6 billion, with the federal share totaling $0.4 billion. Welfare agencies would also incur about $0.3 billion in costs for

providing WORK-related wages. The federal government would match such payments at the regular AFDC rate (that is, an average of 55 percent), which yields a federal estimate of slightly less than $0.2 billion.

CBO's estimate of average costs indicates that it should be possible to attain the projected monthly average of 1 million participants without exceeding caps on federal spending, which would be set for each state. In fact, as is the case with the current JOBS program, CBO's estimates assume that some states would meet the requirements for participation without drawing down their entire share of the capped entitlement.

Empirical analyses consistently show that training and work programs for AFDC recipients help some leave welfare faster than they would have without the programs, generating savings in AFDC, Food Stamps, and Medicaid. As families move from welfare to work, however, they become eligible for the earned income tax credit (EITC), which would increase federal costs. Incorporating the findings by the Manpower Demonstration Research Corporation from several welfare-to-work programs operated in the 1980s and early 1990s, CBO estimates that $1 invested in training activities would produce AFDC savings of about 70 cents during the following five years.[1]

1. The 70 cent return was used only for estimated increases in traditional JOBS program spending. For WORK program expenditures, CBO used a lower estimate because the experience with such programs is limited.

These findings also suggest that Food Stamp and Medicaid outlays would be reduced, but such savings would be partially offset by higher EITC costs.

CBO estimates that H.R. 4605's investment in training and work experience would generate savings of more than $0.6 billion between 1996 and 1999, reducing federal costs of titles I and II from about $3.2 billion to a net of $2.5 billion. Most of these savings would be attributable to reductions in AFDC caseloads. An estimated 70,000 fewer families would receive cash assistance in 1999. This figure represents a net caseload reduction by 1999 and accounts for people who would leave AFDC and return shortly thereafter. Additional savings would be generated when families find part-time work (and remain on AFDC) or are penalized for not participating.

These reductions in caseloads (1.3 percent) may seem relatively minor when compared with the 5.5 million families that are expected to receive AFDC in 1999. But because the reform would affect only a fraction of the AFDC caseload in 1999, it may be more appropriate to compare the figure with the average 1 million families a month that are expected to participate in JOBS or WORK--a comparison that yields a 7 percent reduction.

Title III: Child Care

CBO estimates that title III would increase federal outlays by $5.5 billion between 1996 and 1999, including $3.8 billion in child care costs associated with the expansion of the JOBS and WORK programs, $1.3 billion in increased funding for the "At-Risk" Child Care Block Grant, and $0.3 billion resulting from various policy changes in child care. Under H.R. 4605, costs for child care related to JOBS and WORK programs would increase more rapidly than the direct costs for training and work supervision. In 1999, child care costs associated with titles I and II are expected to total nearly $1.5 billion, compared with $1.1 billion in direct costs of the JOBS and WORK programs.

Several factors explain the expected $1.5 billion increase in child care costs in 1999. First, more AFDC recipients would be enrolled in the JOBS or WORK programs under the bill. By 1999, about 1 million AFDC recipients would be enrolled in either JOBS or WORK programs in an average month (760,000 in JOBS; 240,000 in WORK), compared with 600,000 people under current law.

Second, the average participant in the JOBS and WORK programs would be more likely to have young children than current JOBS participants.

Parents would be exempt from mandatory participation if they were caring for a child under a year old. Current law exempts caretakers of children under 3. Moreover, the program primarily would serve women born after 1971, who, because of their age, would tend to have young children. Young children are more likely to be placed in paid child care arrangements than school-age children and are more costly in those situations.

Third, the $1.5 billion figure for child care costs under titles I and II includes the effects of the JOBS and WORK program expansions on child care administrative costs; the Child Nutrition program, which subsidizes meals for low-income children in child care; and Transitional Child Care, which subsidizes child care for families leaving the AFDC program because their earnings increased. Finally, the federal match rate for child care expenditures would be brought up to the match rates for the JOBS and WORK programs, increasing from an average of 58 percent under current law to an estimated average of 71 percent in 1999 under the proposed Work and Responsibility Act.

Given CBO's assumptions, about 1.7 million children 12 years old or younger would be eligible for child care subsidies in an average month in 1999 because their parents participate in the JOBS or WORK program. Slightly under 40 percent of these children would be placed in subsidized child care

arrangements, with subsidy utilization rates ranging from more than 50 percent for preschool children in single-parent families to less than 10 percent for school-age children in two-parent families. Costs for those in care are expected to average $310 a month ($3,710 annually). Average costs would range from more than $360 for children under 2 ($4,340 annually), to $310 for children 2 to 5 years old ($3,710 annually), to $220 for children who are 6 years old and older ($2,590 annually). The federal government would pay an average of 71 percent of those costs. These utilization rates and costs are based on analyses of data from the Survey on Income and Program Participation, the National Day Care Survey, and a multistate database of records of JOBS participants in 1992.

Title III would also significantly increase the "At-Risk" Child Care Block Grant, which subsidizes child care for poor working parents who are thought to be "at risk" of being on AFDC if they had no child care assistance. Currently a capped entitlement with a $0.3 billion federal cap and federal matching rates that average 57 percent among states, the program would expand substantially under section 306 of H.R. 4605. The federal cap would double to $0.6 billion in 1997 and quadruple to $1.2 billion by fiscal year 2003. Federal matching rates would increase to the same rates used for JOBS, WORK, and associated child care programs, averaging 67 percent in 1996 and increasing to 71 percent in 1999 and 72 percent in 2000 and

subsequent years. On the basis of a telephone survey of 20 states, CBO assumes that three-fourths of the states would spend all of their allotted funds. The remaining one-fourth would be unable to do so because of difficulties in raising state matching funds. These assumptions, combined with previous outlay patterns, result in outlay estimates of $160 million in 1996, $260 million in 1997, $350 million in 1998, and $570 million in 1999, or $1.3 billion between 1996 and 1999.

Amendments in sections 301-305 and section 307 of the Work and Responsibility Act would make several changes in child care policies that would increase federal outlays by a total of $0.3 billion between 1996 and 1999. The changes include continuing child care during temporary interruptions in a parent's training, requiring children to be immunized, and providing funding for licensing activities. The bill also would require states to increase child care assistance for employed AFDC recipients. Under current law, expenses for child care can be deducted from countable income when calculating a family's AFDC benefit. The amount of income that can be disregarded, however, is capped at $175 per child (or $200 if the child is under 2 years old). The bill would require states to provide a supplemental payment if costs exceed the income that can be disregarded or to give the family the option to use JOBS child care subsidies, which are typically higher

than the disregarded amounts. The costs of these amendments are limited by the fact that such policies are already in place in many states.

Title IV: Provisions with Multiprogram Applicability

Title IV would provide federal funds to create a registry containing key information on every AFDC and WORK participant in the country. In addition, the title would provide a four-year total of $0.1 billion to evaluate the performance of the new time-limited program. Title IV would increase federal outlays by a total of $0.7 billion between 1995 and 1999.

The registry would help states keep track of AFDC recipients' accumulated time on the program even though they may move across state or county lines. The bill would provide $0.8 billion in federal funding over the next five years to assist states in developing the registry. Once placed in effect, the registry would reduce fraud in the AFDC and Food Stamp programs (particularly among recipients who are receiving benefits in more than one jurisdiction simultaneously), thereby reducing federal spending in those programs by nearly $0.3 billion through 1999.