WELFARE AND POVERTY

NCPA POLICY REPORT #107

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EXECUTIVE SUMMARY

The welfare system of the United States is creating poverty, not destroying it. The War on Poverty not only is not being won, but the weapons designed to defeat poverty are being used to insure its proliferation.

Whether we look at children, at the elderly, at women head of households, at whites, at blacks, or at Hispanics--the statistics all tell the same story. Poverty, as it is measured by the government, is rising and it is rising at an alarming rate.

- Over the last decade there has been a steady, almost unbroken upward trend in the number of people living below the poverty level.

- There are more people living in poverty today than in 1965, when the War on Poverty was just getting started.

Poverty in America is on the rise for only one reason: We subsidize it. In particular, we are subsidizing divorce, unwed teenage pregnancies, the abandonment of the elderly by their children, and the wholesale dissolution of the family. Not only are we subsidizing these activities, but in some cases we are subsidizing them lavishly.

The welfare system is designed from top to bottom to insure that it has maximum appeal to people living in near-poverty without at the same time reducing the poverty count. The system achieves this both in the way it defines poverty and in the way it disburses benefits.

Official measurements of poverty count only cash income. In-kind benefits such as food, housing, education and medical care are ignored. The welfare bureaucracy has capitalized on this fact by instigating a virtual explosion of in-kind benefits, while being almost stingy in giving out cash.

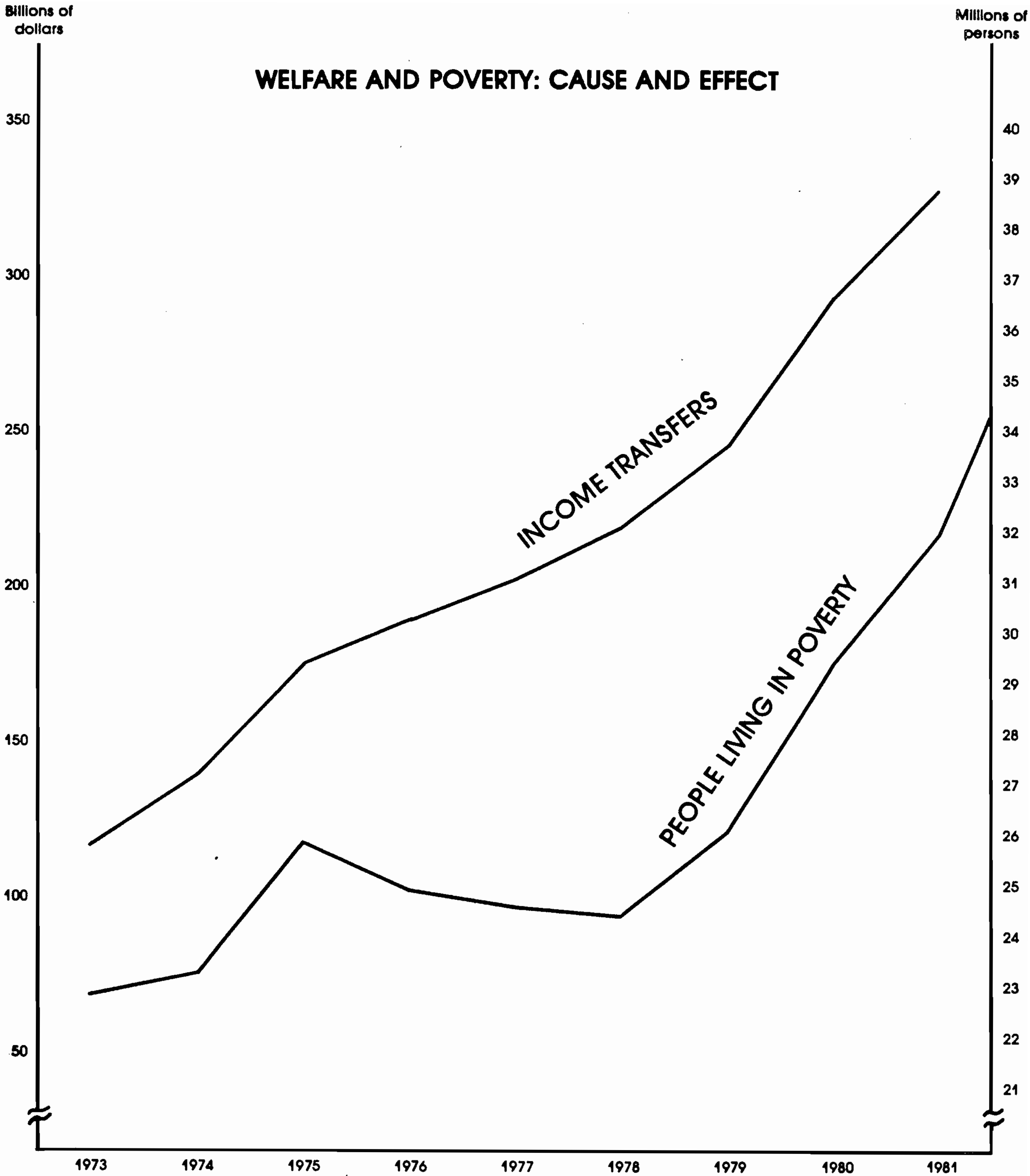
- Since 1965, spending on means-tested in-kind benefits has increased more than 5,238 percent, while spending on cash benefits has barely changed in real terms.

- Only nine percent of all income transfers and less than seven percent of all social welfare spending is given in cash to poor people, because they are poor.

The welfare system demands one thing from its clientelle: a low money income. In return it offers passage through an entitlements gateway to more than 49 major benefit programs, including Medicaid, the most complete and comprehensive health insurance policy anywhere in the world.

Once they are in the system, individuals face virtually no penalty for any act, save the act of earning an income. On the average, for each dollar earned, the poor lose 62 cents in the form of taxes and reduced welfare benefits. The effective marginal "tax" rates they face are higher than those for any other income group.

The welfare system is reaching crisis proportions and is in urgent need of reform.



SOURCE: National Center for Policy Analysis

WELFARE AND POVERTY

In 1982 more than $403 billion was spent on social welfare programs at the federal, state and local level in the United States.[1] This amounts to $2,117 for every man, woman and child in the country who is not poor, or $8,468 for a family of four.

Since the advent of the War on Poverty, the poverty industry has been a growth industry. Today it employs more than five million public and private workers and provides benefits to between 50 and 60 million people. The social welfare budget has grown by more than 400 percent over the last decade--about 43 percent faster than the rate of inflation. At the federal level, social welfare spending now consumes almost 50 percent of the federal budget and is twice the size of defense spending.

In order to appreciate the magnitude of the amount of money being spent to eliminate poverty, consider the following:

- Had the $403 billion in social welfare spending simply been given to people living below the poverty level, it would have amounted to $11,730 per poor person, or $46,920 for a family of four.

- $403 billion is enough money to support almost 60 percent of the U.S. families at the poverty threshold, disregarding all other sources of income.

Despite these facts, in the Fall of 1983 the U.S. Bureau of Census made an amazing announcement. According to the Census Bureau, there were 34.4 million Americans living in poverty in 1982. This is more than the number of people who were living in poverty in 1965 when the War on Poverty was just getting started.[2]

Is it possible that we could spend so much money "eliminating" poverty and not put a dent in the poverty level population? Not only is it possible, but there is probably no limit to the extent of such failures. Were a benevolent deity to bestow upon Congress an extra $400 billion to spend on social welfare programs, there can be little doubt that Congress could exhaust the entire amount without eliminating poverty. Indeed, if we doubled the poverty budget, it is possible, even likely, that the number of persons classified as poor would rise, not fall.

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1 This is the estimate of Johnathon Hobbs. It includes all major income transfer programs as well as such programs as child nutrition and youth job training. See "Welfare Need and Welfare Spending," (Washington, D.C.: Heritage Foundation, October 13, 1982).

2 The most recent Census Bureau estimates are to be found in Bureau of Census, "Money Income and Poverty Status of Families and Persons in the United States: 1982," Current Population Reports.

In order to see why this is true, it is necessary to understand three facts about the U.S. welfare system. First, the official poverty statistics have only a scant relationship to the actual incidence of human need in our society; they are a totally inaccurate account of the real incidence of poverty. Second, although the official designations of poverty bear little relationship to reality, the designations are highly valuable to individuals. Individuals who become certified as in some sense "poor" pass through the gateway of entitlements to one or more of 49 major programs, including Medicaid, the most complete and comprehensive health insurance policy in the world. Third, individuals by the millions are responding to this incentive and succeeding at becoming classified as poor.

PAYING PEOPLE TO BE POOR

Poverty in the U.S. is on the increase, and it is increasing for only one reason: We are paying people to be poor. Since the time of Adam Smith, economists have known that if you want to encourage an activity you subsidize it; if you want to discourage an activity you tax it. In the United States we subsidize poverty and we tax non-poverty. Not only do we subsidize poverty, but in some cases we subsidize it lavishly.

To say that we subsidize poverty is only a first order approximation. To be more specific, government welfare programs in the U.S. are subsidizing divorce, unwed teenage pregnancies, the abandonment of the elderly by their children, and the wholesale dissolution of the family.

A hotly debated issue in the 1960s was whether efforts to reduce poverty would encourage people to be poor. At that time the answer on balance seemed to be no; the number of people living in poverty was dropping. Today, however, that trend has been reversed:

- Over the last decade there has been a steady, almost unbroken upward trend in the number of people living below the poverty level.
- By 1982, the number of people living in poverty was 50 percent higher than in 1973.

This is not the result of an increase in the population. Over the same period of time, there has been a steady, almost unbroken upward trend in the percentage of people living in poverty.

Whether we look at children, the elderly, women head-of-households, or persons living apart from their families; at whites, blacks, or Hispanics--the statistics all tell the same story. Poverty as it is officially measured is rising at an alarming rate. From 1973 to 1982:

- The number of blacks living in poverty rose by 31 percent.
- The number of whites living in poverty rose 55 percent.
- The number of Hispanics living in poverty rose 82 percent.

Persons Living Apart From Their Families. The dissolution of the family is best illustrated by the Census Bureau statistics on "unrelated individuals," persons living apart from a spouse or other family members. In an earlier era, if such individuals were in financial trouble many would have lived with relatives. Not so in the modern welfare state. Since 1959, the number of unrelated individuals living below the poverty level has increased by 31 percent.

A popular conception of the poverty population is that of large families with many children. In fact, almost one-third of poverty families consists of unrelated individuals. (Families with incomes in the lowest fifth of the income distribution contain only 13.8 percent of the population. By contrast, families in the highest fifth of the income distribution contain twice that many people.)

Female-Parent-Only Families. Most people are aware that the welfare state makes divorce financially attractive. However, it is not generally appreciated that more than one-third of all female-parent-only families are now living in poverty. Moreover, the number is growing.

- Since 1959, the number of these families has increased by 79 percent.
- Among blacks, the number living in poverty has almost tripled since 1959.
- Among Hispanics, the number living in poverty has more than doubled over the last decade.

Unwed Teenage Pregnancy. The increase in the number of mothers living without a husband present is due only in part to the fact that the welfare state subsidizes divorce. The increase is also due to the fact that the welfare state subsidizes teenage pregnancies.

- In the 1940s, less than 10 percent of all black babies were born out of wedlock. Today, over half of all black babies are born out of wedlock.

Children. Since 1959 the number of children living in poverty in a family with no father present has increased 62 percent.

- Today almost half of all black children are living in a family with no father present. More than 70 percent of these children are living in poverty.
- Twenty-five percent of all Hispanic children are now living in a family with no father present. About 72 percent of these children are living in poverty.

The Elderly. During the 1970s no other group in America received more government largesse than the elderly. Social Security and Medicare benefits grew at a rate that far surpassed the rate of inflation, and today more than 25 percent of the federal budget is spent on the elderly. Despite this fact, there were more elderly persons living in poverty in 1982 than there were in 1972.

The trend toward poverty status is especially pronounced among elderly women living without a man in the household. In 1982 there were more of these women living in poverty than there were in 1959. Among elderly black women, the number living in poverty in 1982 was almost double the number in 1959.

Can the trend toward an increasing number of Americans officially classified as poor continue much further? According to George Gilder, we have barely scratched the surface:

> AFDC (Aid to Families with Dependent Children) offers a guaranteed income to any child-raising couple that is willing to break up, or to any teenage girl over sixteen who is willing to bear an illegitimate child. In 1979 there were some 20 million families that could substantially improve their economic lot by leaving work and splitting up. Yet they did not. Three-fifths of eligible two-parent families even resist all the noxious advertising campaigns to apply for food stamps, which they can have merely by the asking. Millions of qualified couples continue to jilt the welfare state. Only in the ghetto, among the most visible, concentrated, and identifiable poor, have the insidious seductions of the War on Poverty and its well-paid agents fully prevailed over home and family.[3]

THE BENEFITS OF BEING POOR

To be officially poor in 1982, a family of four had to have an income of less than $9,862. At first glance it would appear that such an income would support only a very meager standard of living. The official statistics, however, count only money income. They conveniently ignore the value of housing, food, medical care, and a great many other items that most other people pay for out of their own budget.

In the U.S. welfare system the key to being classified as poor is to have a low cash income, or at least to have a low reported cash income. Other kinds of income, however abundant, are ignored. In the 1970s, a Congressional committee found that among families receiving Aid to Families with Dependent Children (AFDC) benefits, 99 percent were covered by Medicaid, 60 percent got food stamps, and 14 percent lived in public housing.[4].

To see how lucrative these and other benefits can be, consider the case of a welfare mother reported in the Boston Globe in 1975:

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[3] George Gilder, Wealth and Poverty (New York: Basic Books, 1981), p. 123.

[4] See Martin Anderson, Welfare (Stanford: Hoover Institution Press, 1978), p. 32.

> The mother is well-organized. She buys food stamps twice a month, refuses to live in a housing project, is a member of a community women's group at Catholic charities, and is studying for her high school diploma. Her bimonthly cash grant is $466; she gets a flat grant every three months of $142; and her monthly savings from food stamps amount to $86. Her cash income may be given at $599 monthly, or $7,188 a year. If she and her family spent the average amount paid personally for health care in this country (and the mother gets some psychiatric care), this would amount at full cost to an additional $1,750 in health care expenses. Since there are no financial restrictions for the family on the use of health care, and the mother is intelligent and knowledgeable, one may assume that full use of this opportunity is taken. The three older children go free of charge to an alternative school which costs paying pupils $2,000 a year, and another child goes to a day care center whose cost for a paying child would be $1,000 a year. Cash income and free health and education services to this family thus amount to $16,028. The older children work summers, and I will not cost that out. The family pays no taxes, and need put nothing aside for savings, as the welfare department is committed to meeting its needs. A working head of family would have to earn at least $20,000 to match this standard of living.[5]

In 1975 about three-fourths of the families in the United States had incomes below $20,000.

Charles Hobbs has estimated that in 1976 the average welfare family of four received $15,000 in government subsidies. In 1979 the amount was close to $18,000. These figures compare with the U.S. median family income of $14,500 in 1976 and $16,500 in 1979. They are about double the amount of full-time earnings at the minimum wage.[6]

As George Gilder has noted, "The fundamental fact in the lives of the poor in most parts of America today is that the wages of common labor are far below the benefits of AFDC, Medicaid, food stamps, public housing, public defenders, leisure time and all the other goods and services of the welfare state."[7]

Viewed in strictly material terms, in the United States today there are enormous benefits that flow from being classified as poor. Poverty pays, and in some cases, it pays very well.

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5 Reprinted in Anderson, Welfare, p. 36.

6 Charles D. Hobbs, The Welfare Industry (Washington, D.C.: Heritage Foundation, 1978), pp. 83-84.

7 Gilder, Wealth and Poverty, p. 122.

THE REAL INCIDENCE OF POVERTY

As we noted earlier, Census Bureau statistics on the number of Americans living in poverty count only cash income. They ignore the value of food, housing, medical care and other goods and services which are known as in-kind benefits. Yet, this method of counting seriously distorts the true picture. In 1976, families in the lowest fifth of the income distribution received on the average 43 cents in the form of in-kind income for every dollar they received in the form of cash. Among families in the second fifth of the income distribution, for every dollar received in cash, another 28 cents was received in in-kind income.[8]

There is some question as to how much value should be attached to goods and services received in-kind. This is a question to which we shall return. For the moment it is sufficient to note that food, shelter and medical care surely have some value, and that to ignore them altogether, as the Census Bureau does, is indefensible.

It is not surprising that the official statistics exaggerate the extent of poverty. After all, the vast welfare bureaucracy has a vested interest in maintaining and expanding poverty. The result is a major distortion of the truth. While Census Bureau statistics point to an ever-increasing number of people living in poverty, virtually all scholarly studies on the incidence of real poverty point in the opposite direction.

Here are the conclusions of just a few studies:

- Edgar Browning, University of Virginia, 1975: "In a meaningful sense poverty had become virtually non-existent in America by 1973."[9]
- Morton Paglin, Portland State University, 1977: Only three percent of Americans were poor in 1975.[10]
- Sar Levitan, George Washington University, 1977: "If poverty is defined as a lack of basic needs, it's almost been eliminated."[11]

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[8] Congressional Budget Office, "Poverty Status of Families Under Alternative Definitions of Income," Background Paper No. 17, January 13, 1977, Table A-4. Reprinted in Edgar K. Browning and Jacqueline M. Browning, Public Finance and the Price System (New York: Macmillan Publishing Co., 1979), Table 7-8, p. 204.

[9] Edgar K. Browning, Redistribution in the Welfare System (Washington, D.C.: American Enterprise Institute for Public Policy Research, 1975), p. 2.

[10] Quoted in Anderson, Welfare, p. 24.

[11] Reported in Anderson, Welfare p. 25.

- Martin Anderson, Hoover Institution, 1978: "The war on poverty has been won, except for perhaps a few mopping-up operations. The combination of strong economic growth and a dramatic increase in government spending on welfare and income transfer programs during the last decade has virtually wiped out poverty in the United States."[12]

Most scholarly studies show that the inclusion of in-kind benefits reduces the poverty rate by one-half to two-thirds of the level reported by the Census Bureau. These figures could be further modified to take into account the large amount of unreported income among low-income families. Some estimates of the underground economy place it between 10 and 25 percent of GNP. And one study concluded that individuals with reported incomes under $1,000 were spending $224 for every $100 of reported income.[13] Add to this consideration the fact that among low-income individuals there were would-be writers, artists and actors--people whose earning ability is actually quite high.

What the welfare state does, then, is not so much induce people to be poor, but encourage them to have low reported cash incomes. In return it offers a wealth of non-cash benefits. To see how, and why, this is done, let's take a closer look at the difference between cash and in-kind benefits.

CASH VS. IN-KIND BENEFITS

There are two important differences between cash and in-kind benefits. First, with in-kind transfers the money eventually ends up in the pockets of people who are not poor. Money spent on Medicaid, for example, goes to doctors, hospitals and nursing homes. Money spent on food stamps goes to farmers, mostly wealthy farmers. Money spent on housing goes to landlords and contractors. The poor, in other words, are a mere way-station or conduit through which money is channeled from taxpayers to a non-poor receiving group.

The second important difference is that there is no assurance that when transfers are made in-kind, those same goods and services would have been purchased by poor persons had they been given the cash instead. In other words, the goods and services received may be a lot less valuable to the recipients than the price paid for them. If an elderly person had $10,000 in cash, for example, would he spend it to stay in a nursing home? Would poor families spend their own money to visit "Medicaid mills"? In-kind transfers are ideal if the objective is to divert income to the medical, farming, and housing industries. But in general they are lousy vehicles for raising the standard of living of low-income families.

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12 Anderson, Welfare, p. 37.

13 Reported in Banfield, The Unheavenly City: The Nature and Future of Our Urban Crisis (Boston: Little, Brown and Company, 1970), p. 116.

Why then does so much welfare spending take the form of in-kind transfers to the poor? One reason may be that most Americans want to force a lifestyle on the poor that they otherwise would not choose willingly. When benefits are given in the form of food, housing, medical care, and education, for example, we are able to exert more control over how poor families allocate their total budget. Recipients are almost always forbidden to sell their in-kind benefits to others. Food stamps, subsidized housing, and the right to free medical care cannot legally be exchanged for cash in the marketplace. In-kind transfers, then, may simply represent a paternalistic desire to tell poor people how to spend the money we give them.

On the other hand, there are other, more subtle reasons for preferring in-kind transfers -- reasons which are consistent with the self-interest of the welfare bureaucracy. In-kind transfers achieve two goals which are of great value to the poverty industry. First, since money spent on in-kind benefits goes to non-poor people, it elicits the loyal political support of powerful special interest groups for poverty programs. Chief among these groups is the welfare bureaucracy itself. Second, since in-kind benefits are valuable, they are a seductive lure by which the number of poor people can be greatly expanded, given the way we officially measure poverty.

In fact, the welfare system is designed from top to bottom to insure that it has maximum appeal to people living in near-poverty, without at the same time reducing the poverty count. To see this point more clearly, let's take a look at where the welfare dollars actually go.

WHERE THE WELFARE DOLLARS GO

In 1981 almost $300 billion was taken out of the pockets of some Americans and given to other Americans in the form of income transfers. These transfers now amount to 10 percent of our gross national product, and transfers in the form of cash now go to 42 percent of all U.S. households.[14]

Almost all of the programs listed in Table I in the Appendix are welfare programs, or programs which enjoy widespread support because they are thought to assist low-income families. Yet only 24 percent of these transfers go to poor families <u>because they are poor</u>. In other words, only 24 percent of these funds are <u>means-tested</u> benefits. The vast bulk of transfer income goes to families that are solidly middle class. Take Social Security, for example. A number of Social Security recipients have low-incomes. But, partly because of Social Security, the per capita after-tax income of the elderly now exceeds the per capita after-tax income of those under 65 years of age. In addition, the elderly, on the average, are wealthier than those under 65 years of age.

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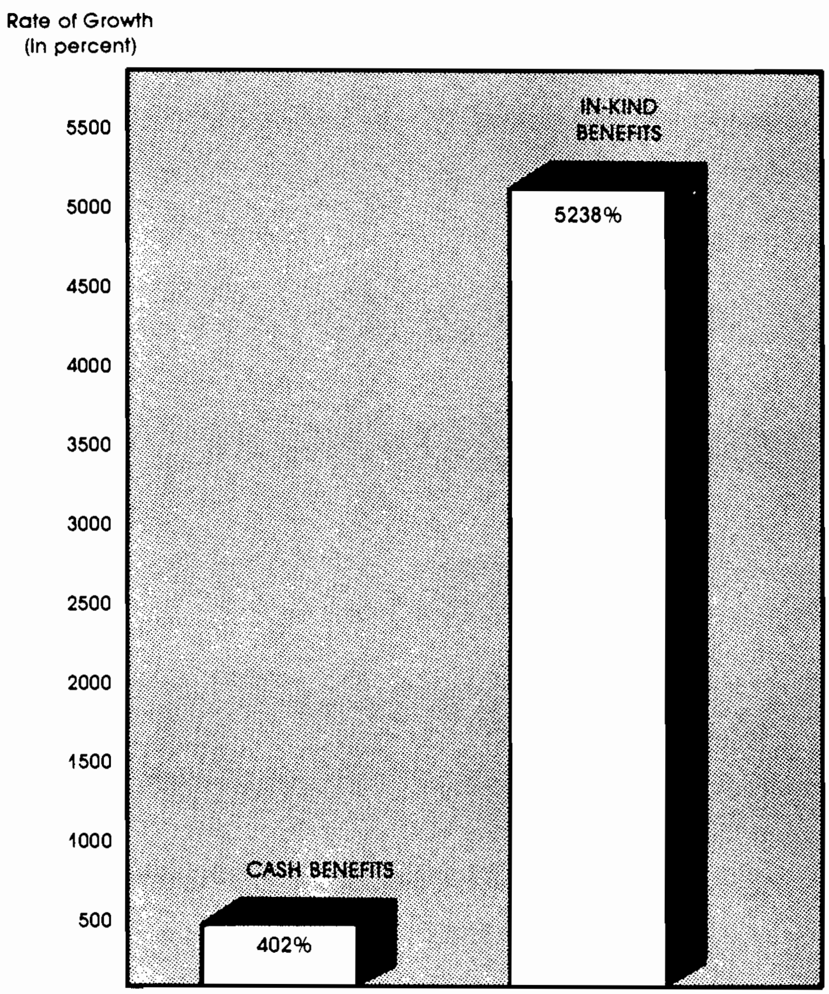
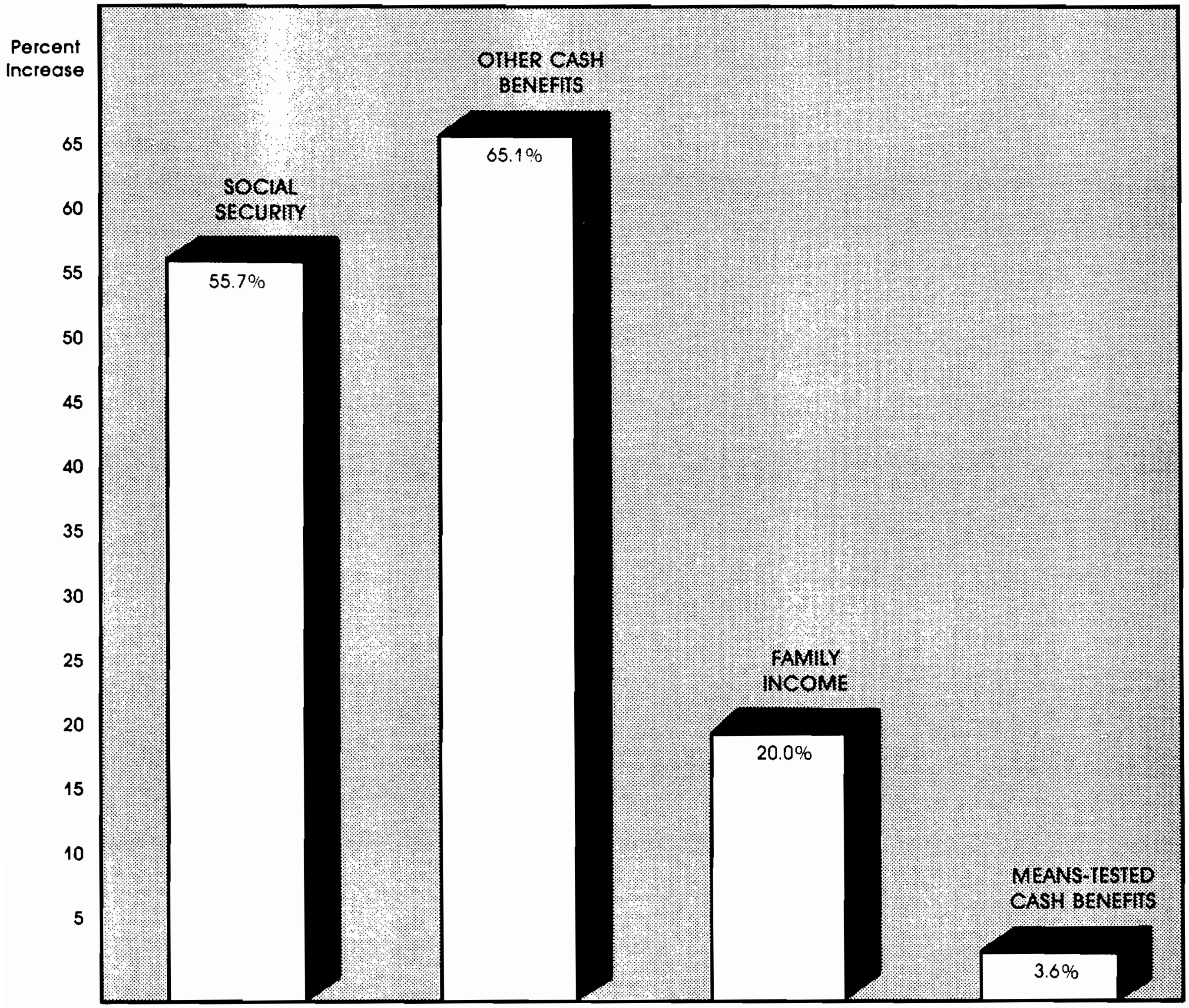
14 Sheldon Danziger, Robert Haveman, and Robert Plotnik, "How Income Transfer Programs Affect Work, Savings and the Income Distribution; A Critical Review," <u>Journal of Economic Literature</u>, Vol. 19, September 1981, p. 977.

THE GROWTH OF MEANS-TESTED BENEFITS
1965-1981



SOURCE: National Center for Policy Analysis

REAL RATES OF GROWTH IN CASH-BENEFITS 1965-1978



SOURCE: Table I

Of those benefits which are means-tested, the great bulk--almost two-thirds--are in-kind benefits, not cash benefits. Moreover, virtually all of the recent growth in means-tested benefits has been in the form of in-kind transfers.

- Over the last two decades, means-tested cash transfers have increased only four-fold, while in-kind transfers have increased by more than 50-fold.
- In real terms the amount of cash given to the poor, because they are poor, has barely changed since 1965.

While Social Security benefits have experienced a real growth rate of almost 55.7 percent since 1965, and other non-means-tested cash benefits have grown by over 65 percent, means-tested cash benefits have increased at less than one-fifth the rate of increase in household income.[15]

In his classic book Welfare, Martin Anderson wrote:

> The growth of social welfare programs--AFDC, SSI, food stamps, child nutrition, day care, public housing, Medicaid and Medicare, tuition aid, and Social Security--has been so comprehensive and diffuse that there is virtually no person in the United States needing help who is not eligible for some form of government aid.[16]

The rich variety of benefit programs is not in doubt. But there may be one thing which the poor individual cannot get from the welfare bureaucracy--cash. Indeed, among families who are truly needy and not adept at manipulating the welfare system to get in-kind benefits, it appears that public assistance has been relatively stingy.

It is sobering to realize that almost all of transfer income in the U.S. goes to special interest groups for whom poverty status is not a condition for aid, or to some group that is providing a good or service in-kind which may or may not be highly valued by people who consume it.

- In 1981, only nine percent of all income transfers and less than seven percent of all social welfare spending was given in the form of cash to poor people, because they were poor.

UNDESIRABLE SIDE EFFECTS OF THE WELFARE SYSTEM

Even if real poverty has been eliminated, or at least held to a bare minimum, we are paying a very high price for the way we achieve this goal. The American welfare bureaucracy is slowly changing our economic system, and threatens to change our culture.

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[15] Danziger, et al, "Income Transfer Programs," Table II, p. 978.

[16] Reported in Anderson, Welfare, p. 37.

Penalizing Productive Work. It is now recognized by most students of the subject that welfare undermines personal incentives to become self-sufficient. Once a hotly debated issue, the fact that the welfare system reduces productive work is now accepted as a fact of life.

During the late 1960s and early 1970s there were six major guaranteed income experiments conducted by the federal government. The results of these experiments varied from case to case, but a rough summary of the results is as follows: Male head-of-households reduced their work effort by five percent. Female head-of-households reduced their work effort by eight percent. Wives reduced work efforts by 22 percent; dependents by 46 percent. Moreover, there are reasons to believe that these results significantly understate the negative effects of welfare on the willingness to work.[17]

A survey article in a recent issue of the Journal of Economic Literature summarized the results of the latest econometric estimates of reduced work incentives under all major income transfer programs:[18]

- On the average, the studies suggest that income transfers reduce aggregate production in the economy by an amount equal to 3.5 percent of total household income.

- This was about $62 billion in 1981 -- an amount equal to more than one-fifth of the total income transfers that year.

Part of the reason for reduced work incentives is that it is practically impossible to construct a welfare system that does not penalize the welfare recipient who earns more in the marketplace. After all, few of us would want to subsidize welfare recipients regardless of their private sector earnings.

The American welfare system, however, erects such penalties in the worst possible way. When a low-income family receiving welfare benefits earns an additional dollar of income, it is penalized in two ways. The family not only faces income and payroll taxes, it also is penalized by a reduction in welfare benefits:[19]

- For each additional dollar of earned income, low-income families lose 27 cents in taxes and 35 cents in reduced welfare benefits.

- The combined effect of these two penalties is an effective marginal tax rate of 62 percent, a higher tax rate than that forced on any other income group.

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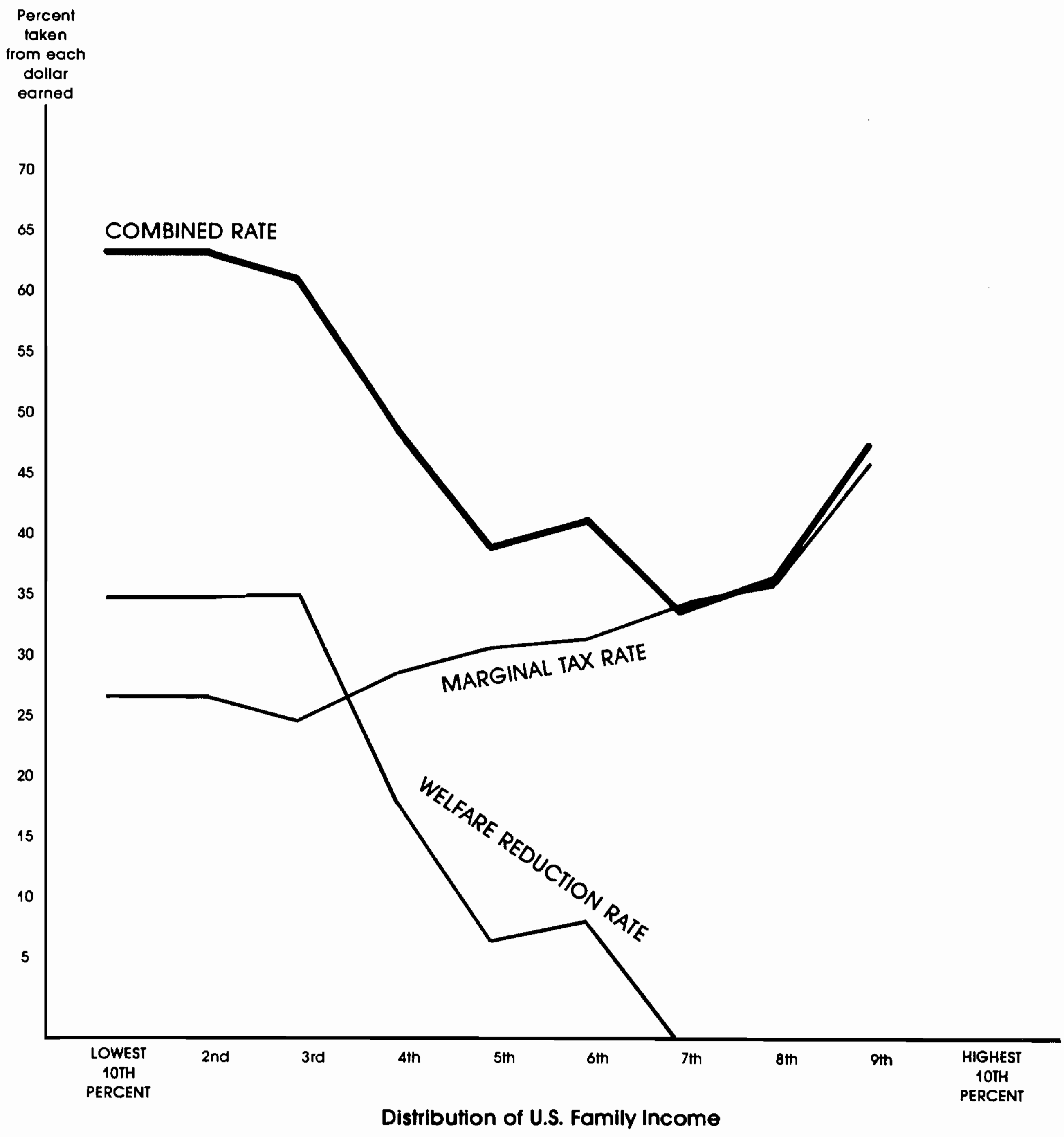
[17] Reported in Anderson, Welfare, Chapter 5.

[18] Danziger, et. al., "Income Transfer Programs," p. 999.

[19] Edgar K. Browning and William R. Johnson The Distribution of the Tax Burden (Washington, D.C.: American Enterprise Institute for Public Policy Research, 1979), Table 17, p. 70.

PENALTIES ON EARNED INCOME



Source: Table II

The marginal tax rate of 62 percent is only the average for low-income families. For certain families at certain income levels, the tax rate can be much higher. Henry Aaron of the Brookings Institution has explained why: "On earnings from $576 to $8,390 per year, the family eligible solely for AFDC and Medicaid faces a tax rate of 67 percent. Eligibility for food stamp and housing assistance raises the tax rate as high as 80 percent, and brings it to 73 percent over the income range from $4,000 to $8,300." When earnings reach $8,390, the family is removed from the welfare rolls, and as a result of the last dollar earned, loses $1,000 in Medicaid benefits and a $288 food stamp bonus. At $8,389, in other words, the family faces a marginal tax rate of 1,288 percent![20]

<u>Discouraging Savings.</u> The United States has one of the lowest rates of personal savings among developed countries, and many believe that our welfare system contributes to the low savings rate. For example, when people know that they can rely on transfer income, particularly Social Security retirement income, they have less incentive to engage in personal saving for retirement and adverse contingencies. There is considerable debate over the magnitude of this effect, but some recent estimates suggest that income transfer programs may reduce the personal savings rate by as much as 20 percent.[21]

<u>Encouraging the Breakup of Families.</u> It is generally well known that the welfare system has encouraged the breakup of poor families. As Gilder put it, from a financial viewpoint an indexed welfare benefit for a mother is "more preferable in every way to the taxable, inflatable, losable, drinkable, druggable, and interruptible earnings of a man."[22]

What is less well known is that a guaranteed income from welfare apparently encourages divorce even when there are no financial incentives to break up.

- The results of a guaranteed income experiment conducted in Seattle and Denver show the incidence of divorce among whites increased 430 percent during the first six months of the experiment.

- Over a two-year period, the incidence of divorce, relative to a control group, increased 244 percent for whites, 169 percent for blacks and 194 percent for Hispanics. Apparently financial need is a strong force holding marriages together.[23]

Gilder has proposed a persuasive theory of why this is true:

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20 Henry J. Aaron, <u>Why is Welfare So Hard to Reform?</u> (Washington, D.C.: The Brookings Institution, 1973), pp. 33-34.

21 Danziger, et al, "Income Transfer Programs," p. 1006.

22 Gilder, <u>Wealth and Poverty</u>, p. 18

23 Anderson, <u>Welfare</u>, p. 149.

> The combination of welfare and other social services enhance the mother's role and obviate the man's. As a result, men tend to leave their children, whether before or after marriage. Crises that would be resolved in a normal family may break up a ghetto family. Perhaps not the first time or the fifth, but sooner or later the pressures of the subsidy state dissolve the roles of fatherhood, the disciplines of work, and the rules of marriage.[24]

Encouraging Dependence. One of the remarkable facts about U.S. family income is that 20 percent of all the families in the country depend upon government welfare for 96 percent of their income.[25] Much has been made of the fact that only 20 percent of those on the dole accept it as a more or less permanent way of life. This figure, however, is apparently much higher than it used to be. One study found that permanent dependency, which characterized only five percent of the welfare recipients 20 years ago, now has reached 30 percent in Los Angeles. The study predicts that it will rise to 40 percent over the next ten years.[26]

THE DISTRIBUTION OF INCOME

A natural question to ask about the welfare system is, to what extent has it reduced inequality of income in our society? After surveying the results of a number of econometric studies, one team of authors concluded that the cumulative effect of all income transfer programs has been a reduction in poverty of 74 percent and a substantial reduction in inequality of income distribution as well.[27]

Before we accept this conclusion, however, consider the statistics on family money income in Table III. What the table clearly indicates is that there has been little change in the U.S. distribution of money income since 1947. Indeed, were it not for the fact that 1982 was a recession year, one might conclude that there is less equality of income in the U.S. today than at any time since World War II.

Econometric models are designed to estimate the effects of marginal changes on individual behavior. They are not designed to measure large institutional changes in the economy, or in the culture. Clearly we have had large institutional changes. In 1935, for example, about 50 percent of all welfare was private charity. Today, private charity accounts for about one percent. The broad picture presented in Table III suggests that if we had never created the welfare state, the distribution of family income today would not be much different. We have paid a high price for the institutional changes which the welfare society has wrought. But it is not clear what we have gained in return.

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24 Gilder, Wealth and Poverty, p. 122.

25 Browning and Browning, Public Finance, Table 7-8, p. 204.

26 Reported in Gilder, p. 124 and n. 12., p. 278.

27 Danziger, et al., "How Income Transfer Programs Affect Work, Savings and the Income Distribution," p. 1014.

TOWARD WELFARE REFORM

Welfare reform is urgently needed. But to achieve reform there first must be widespread agreement on the general principles which shape and govern the welfare system. The following are some principles that seem imminently reasonable.

PRINCIPLE ONE: **Most people can and should take responsibility for supporting themselves and their families.** In the absence of physical or mental impairment, individuals should perceive that society expects them to support themselves and their families, and this perception should be reinforced by the operation of the welfare system.

PRINCIPLE TWO: **Short-term help should be available to many; long-term help should be reserved for a few.** A humane welfare system is one which readily provides temporary and emergency help to those in need. A responsible welfare system is one which provides permanent aid to only the very few who cannot support themselves.

PRINCIPLE THREE: **The welfare system should not encourage the breakup of the family.** Family members should not find it in their economic self-interest to dissolve the family unit. One of the reasons why families exist in every culture is that there are economic advantages to specialization and division of labor within the family. The welfare system should not undermine these advantages.

PRINCIPLE FOUR: **The goals of the welfare system should be achieved at minimum cost.** As with every other social goal, it is in our self-interest to find the most cost-effective ways of operating the welfare systm based on these principles.

While these goals may seem acceptable on the surface, if they are to be adopted and pursued vigorously they will necessitate radical reform of the U.S. welfare system. Here are just a few of the reforms implied by these principles:

REFORM ONE: **Welfare should be separated from social insurance.** This is implied by Principle Four. Under the current system, the working poor are paying taxes under the Social Security and Medicare programs to fund the retirement pensions and medical care of retired millionaires. Yet these programs enjoy widespread support because they are thought to benefit many needy individuals. By separating social insurance from welfare, we can greatly lower the cost of achieving legitimate welfare objectives.

REFORM TWO: **All welfare benefits should be means-tested.** This is implied by Principles One and Two. There is no legitimate reason for welfare benefits except to provide for needs that otherwise will go unmet. In order to insure that the objectives of a rational welfare system are achieved, there must be evidence that genuine needs exist.

REFORM THREE: It should be easy to enter the welfare system, but difficult to remain there. This is implied by Principle Two. As George Gilder has pointed out, this kind of change would move us in the opposite direction of many recent reforms, especially those in New York and California.[28]

REFORM FOUR: Welfare should be dispensed at the state and local level rather than at the federal level, and preferably by private, voluntary organizations. This reform is dictated by Principles One, Two and Three. It is beyond the capability of the national welfare bureaucracy to distinguish between real need and the lack thereof, or between short-term and long-term needs. Moreover, it is in the self-interest of the bureaucracy at every level of government to expand both the number of welfare recipients and their duration on the dole. By contrast, private charitable organizations in this country have traditionally focused on short-term emergency relief.

What could be expected as a result of such reforms? From an economic standpoint alone, the potential savings are enormous. Jonathon Hobbs has estimated, conservatively, that simply by handing money to poor families we could bring every family in America up to the non-poverty threshold for a cost of about $100 billion--one-fourth of current social welfare spending.[29]

This estimate ignores the vast amount of unreported income, and it does not consider the goal of dispensing welfare benefits in a way that does not encourage the dissolution of the family. These two considerations would probably cut the $100 billion figure in half.

In other words, there is every reason to believe that we could solve the problem of real poverty in America for as little as one to two percent of our gross national product.

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28 Gilder, Wealth and Poverty, p. 126.

29 Jonathon Hobbs, "Welfare Need and Welfare Spending," Table 1, p. 3.

TABLE I

Spending On Major Income Transfer Programs
(in billions of dollars)

Program	1965	1981*
Social Insurance		
Cash Benefits:		
Social Security (OASDI)	$16.5	$137.0
Unemployment Insurance	2.5	18.7
Workers' Compensation	1.8	14.8
Veterans' Disability Compensation	2.2	7.5
Railroad Retirement	1.1	5.2
Black Lung	--	0.9
In-Kind Benefits:		
Medicare	--	38.4
Public Assistance		
Cash Benefits:		
Aid to Families with Dependent Children (AFDC)	1.7	12.8
Pensions to Needy Veterns	1.9	4.1
Supplemental Security Income (SSI)	2.7	8.5
General Assistance	0.4	1.5
In-Kind Benefits:		
Medicaid	0.5	27.6
Food Stamps	0.04	9.7
Housing Assistance	.3	6.6
Total Spending	$31.5	$293.2
Total Spending as Percent of GNP	4.6%	10.0%

* Estimate

Source: Sheldon Danziger, Robert Haveman, and Robert Plotnik, "How Income Transfer Programs Affect Work, Savings, and the Income Distribution; A Critical Review," Journal of Economic Literature, Vol. 19, September 1981, Table I, p. 977.

TABLE II

Marginal Tax Rates, 1976

Family Income Group	Income Transfer System	Tax System	Effective Combined Rate
Lowest two tenths	35.3%	27.4%	62.9%
Third tenth	35.5	25.4	61.0
Fourth tenth	19.2	29.2	48.4
Fifth tenth	7.7	31.3	39.0
Sixth tenth	9.4	31.9	41.3
Seventh tenth	-0.3	34.4	34.1
Eighth tenth	0.2	36.4	36.6
Ninth tenth	-1.5	47.4	46.0
Highest tenth	--	--	--

Source: Edgar K. Browning and William R. Johnson The Distribution of the Tax Burden (Washington, D.C.: American Enterprise Institute for Public Policy Research, 1979), Table 17, p. 70.

TABLE III

The Distribution of Family Income in the U.S., Selected Years

Year	Lowest Fifth	Second Fifth	Third Fifth	Fourth Fifth	Highest Fifth
1947	5.1%	11.8%	16.7%	23.2%	43.3%
1952	4.9	12.2	17.1	23.5	42.2
1962	5.0	12.1	17.6	24.0	41.3
1972	5.4	11.9	17.5	23.9	41.4
1982	4.7	11.2	17.1	24.3	42.7

Source: Edgar K. Browning and Jacquelene M. Browning Public Finance and the Price System (Macmillan Publishing Co., 1979), Table 7-4, p. 197 and U.S. Bureau of the Census, "Money Income and Poverty Status of Families and Persons in the United States: 1982," Current Population Reports, Table 4, p. 11.