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*Need for meeting
Dec. 6 - 2 pm*

THE WHITE HOUSE

WASHINGTON

December 5, 1974

MEMORANDUM TO: BOB HARTMANN

FROM: KEN COLE

SUBJECT: Secretary Weinberger's Memorandum
on an Alternative Approach to
Welfare Replacement

Attached is a memorandum Secretary Weinberger prepared at the President's request on an alternative welfare reform option.

I thought you would like the opportunity to review the memorandum before our meeting with the Secretary tomorrow, December 6, at 2 p.m.





THE SECRETARY OF HEALTH, EDUCATION, AND WELFARE
WASHINGTON, D. C. 20201

DEC 4 1974

MEMORANDUM FOR THE PRESIDENT

SUBJECT: An Alternative Approach to Welfare Replacement

INTRODUCTION AND SUMMARY

At the November 13 briefing on the Income Supplement Program (ISP) you requested an analysis of what we might accomplish within the context of the present welfare programs if the ISP were not proposed to the Congress.

Incremental change to the existing system has a history. Twice--in 1962 and 1967--we made substantial revisions in the Aid to Families with Dependent Children (AFDC) program; in 1969 Food Stamps was transformed from a small demonstration project into a nationwide program; and in 1972 the Congress "federalized" public assistance to the aged, blind, and disabled in the form of the Supplemental Security Income (SSI) program. In addition to these measures in income assistance, new programs were directed at the poverty population in the fields of education and child development, manpower training, public employment, urban development and housing, community action, legal services and so on.

Results from this decade of "tireless tinkering" are best described as mixed. Poverty surely declined, but more by reason of economic expansion, broad demographic changes and growth in the income assistance programs than by reason of the explicitly "anti-poverty" endeavors as such. It was the growth in the income assistance programs (especially AFDC) that disquieted many, for it did not come from any conscious national policy. Rather that growth was and is even now a haphazard compounding of uncoordinated, separate decisions made at the Federal, state and local levels by the courts, several different Federal agencies, the Congress, and state executives and legislatures. No one can say with any certainty where the "system" is going and what it is doing to the recipient population, nor can we see any broad accomplishments from these many programs. We just go on expanding each piece.

The Family Assistance Program (with its companion SSI program) was the first real attempt to formulate a conscious national policy on income

support to the poor. In the aftermath of that proposal's failure in 1972, we engaged in an extensive interagency analysis of what the principal program options are for a national income support policy. This eventually led to a wholly new plan, to the Welfare Replacement Proposal, presented to you on November 13. One of the products of interagency analysis was a lengthy Welfare Reform Options Paper, completed in the autumn of 1973, which covered much of the territory you requested us to study. A copy of that Options Paper is attached, a brief description of its contents is at Tab A of this memorandum.

I think it is proper to say that there is no one alternative to the approach embodied in the Income Supplement Program. Rather, should we decide to stay with the existing programs, we face a wide range of possibilities, which have to be measured in accordance with several, often competing objectives:

- o Adequacy Although hard to define, adequacy is nonetheless a desirable characteristic of a system in which both those who work and those who cannot work have access to some level of income which is adequate for subsistence.
- o Equity People in similar circumstances should be treated similarly. Those who earn more should end up having more total income for their own use; and those who have greater needs (e.g., more children) should receive relatively more.
- o Work Incentives Those who can work should find it financially rewarding to do so and should be required, if they have no caretaker responsibilities, to be working or actively seeking work as a condition of receiving assistance. In addition, recipients should not receive so much income assistance without working that they lose all incentive to get work or go on working.
- o Objectivity Discretionary authority in the hands of program administrators should be kept to the necessary minimum.
- o Administrative Efficiency The system should be as simple and straightforward as possible; administrative costs, the burden on participants, and fraud and error should be minimized; system objectives should be fulfilled at minimum cost.

o Coherency
and Control

The system as a whole should be coherent, and consistent, and be understandable in its operation and effect, have the intended effect, and be subject to policy and fiscal control.

For the purposes of this memorandum we have extracted and updated selected material from the 1973 Options Paper and arranged its presentation under somewhat different headings. We have tried to give you a sense of how the various possibilities weigh in terms of the objectives described above, what the probable impacts on cost and caseload would be, and how we expect each option to be received by Congress and the states. While I encourage you to read this material to gain an understanding of the technical, administrative, political and policy complexities involved, the following will give you a quick overview of what follows except for the concluding section.

- o Changes in Existing Programs. In this section we outline those measures which might be undertaken to rationalize each of the three major welfare programs -- AFDC, Food Stamps and SSI -- short of major structural changes in them. In the case of AFDC, this would involve considerable national standardization. (An alternative approach for AFDC is also discussed.)

If we assume favorable Congressional and State reaction, enactment of the changes discussed under this heading would enhance the equity, administrative efficiency, objectivity and the predictability of the current programs. Two measures would increase costs and caseload in the interests of work incentives and equity, but most measures would eliminate those program defects that have led to caseload growth among relatively high income recipients, leading most probably to net savings. Firm figures are impossible to give because of State variations in AFDC payment levels and practices. Similarly, the net effect on work incentives is mixed but the balance is probably favorable. Very substantial inequities between the states and our treatment of single parent versus intact families would remain. Assistance in many areas would still be very inadequate and little overall improvement in the fiscal and policy control of the overall welfare system will result.

- o Major Modifications and Additions. Here are outlined those often suggested measures that would either fundamentally transform the AFDC program or would add major new programs, such as an Earnings Supplement or a Housing Allowance, to the existing three.

The modifications in AFDC -- a national minimum and a nation-wide mandate of the Unemployed Fathers (UF) option -- presuppose a national standardization of the program and would go the last step in transforming AFDC into a fully national program on the Food Stamps model. States would still administer the program and have the option of setting higher levels than the minimum. These steps would reduce present interstate inequities, impose a national criterion of adequacy in AFDC, and be achievable with relatively minor impact on cost and caseload. The administrative inefficiencies and policy defects that are inherent in the categorical nature of AFDC would remain untouched, arguably made worse, by these modifications.

An Earnings Supplement and/or a Housing Allowance are the most often suggested proposals to redress the imbalance in our low coverage of low-income families where both parents are present and the father is more or less fully employed at low wages. A comprehensive Housing Allowance would additionally cover AFDC and SSI recipients. Unquestionably these and other proposals for new programs would improve the adequacy and interstate equity of the overall income support system, most especially with respect to the "working poor." However, such proposals also demand the creation of new structures to administer them or substantial personnel additions to present transfer bureaucracies, and would aggravate work disincentives because of compounded benefit reduction rates. It is also my judgment that they would lead to very high net budget costs because of a probable unwillingness in Congress to reduce AFDC and SSI grant levels despite the introduction of a Housing Allowance, and would exacerbate the political problems that have made it difficult to subject the present system to coherent policy and fiscal control.

- o Program Integration. In this final section we discuss five sets of measures that could be undertaken to reduce the excessive amount of overlap and duplication in the existing programs. These measures would become even more necessary

should new programs, such as a Housing Allowance, be added. All would improve administrative efficiency, equity and possibly work incentives. However, the most ambitious and potentially useful undertaking -- full scale administrative integration -- would equal the Income Supplement Program (ISP) in controversy and far surpass it in complexity.

The political perception should not be underestimated. What would be important, but not highly visible features of the ISP initiative (for example, frequent reporting and an annual accountable period) and thus not likely to invoke much controversy, would become major steps if we tried to implement them in existing programs, and would be strongly opposed.

Finally, we should keep in mind that Mrs. Griffiths' long-awaited welfare reform proposal is being privately circulated on the Hill and will soon be made public. We will, of course, have to react, and to the extent that we reject a major effort such as the ISP, we will have to show why we oppose her comprehensive proposal from the perspective of a more limited "tinkering" strategy.

CHANGES IN EXISTING PROGRAMS

There are a number of changes that could be made in the existing AFDC, Food Stamps and SSI programs that would both improve their operations and make more predictable their results. These changes would not, by themselves, materially advance either adequacy or equity in the overall income assistance system, nor would they make a comprehensive, logical system out of the three separate programs. For the former of these goals to be significantly addressed, major structural revisions on the order of those reviewed in the next section would be needed. Of course, along with seeking some of the program design changes discussed in this section, we could seek at the same time to integrate the operations and rationalize the overall effects of the programs. This possibility is also explored in a later section of this memorandum. However, no strategy of incremental reform can result in a fully integrated system.

Revise Programs, Especially AFDC, Along ISP Characteristics

Inherent in the design of the Income Supplement Program (ISP) are a number of features which if imposed on the existing programs would rationalize their operations, make their effects more understandable, and more fully subject them to conscious policy choices at the national and state levels. In order of probable impact in terms of costs, case-load and therefore political controversy, they are:

- Standardize Eligibility Criteria and Benefit Computation Rules. Such measures include instituting flat grants that vary only by family size and a standard work-related expenses deduction. These and similar changes could be enacted in AFDC and Food Stamps; many are already in effect in SSI.
- Improve Work Incentives in AFDC. In order to be initially eligible, a family's income must be well below that level at which an already participating family's grant is phased down to zero. This creates an incentive for a working mother to reduce her earnings so as to become eligible. This disincentive could be eliminated by establishing both initial and continuing eligibility on the same income criterion. In the AFDC-UF (Unemployed Fathers) program, work effort beyond 100 hours a month results in a total loss of benefits. This problem could be alleviated by, for example, moving to an income test for partial unemployment similar to that used in Unemployment Insurance.
- Administrative or Procedural Changes. We should amend all programs to require recipients to report frequently relevant information and we should base benefit calculations on a retrospective time period.

- Accountable Period. Our public assistance programs do not now measure a potential recipient's income on an annual basis. This allows payments to some recipients during months when their income is temporarily low even though their total yearly income would make them ineligible.

In addition to these changes largely common to all three programs, we need to limit the administration by our Social Security Administration of State supplements to SSI. The provision for Federal administration of State supplements is correct in concept, but unfortunately the Congress chose not only to "grandfather" in all recipients under the superseded State aid to the aged, blind and disabled programs, but also to allow Federal administration of that highly mixed caseload. This has imposed an intolerable and costly administrative burden.

Even though these measures appear technical, their introduction would have significant impact. Families similarly situated in terms of income and size, both within a given state and among the several states, would be treated more equally, and administration of AFDC and Food Stamps would become more objective and efficient. In fact many States are, under the pressure of our Federal Quality Control program which was started in 1973, beginning to adopt changes of this sort in order to reduce their error rates. However, because the categorical nature of AFDC would remain (in many states only families with an absent father are eligible), these various changes would necessarily leave in effect all the present inequities in our treatment of single-parent and intact families. In addition, these changes do nothing about the adequacy of AFDC levels in low-payment jurisdictions. In the absence of basic benefit levels being raised (or some sort of grandfathering provision being instituted) some of these changes would lead to substantial reductions in aid to families who now benefit from itemizable income disregards and infrequent reporting of their status. The overall effect on work incentives would be mixed, for the various changes we have mentioned would eliminate the relatively generous disregards for work related expenses, but would make the overall work incentive structure more rational.

The politics involved with these minor changes or "tinkering" would be quite controversial. For example, we would move AFDC from a grant-in-aid program with substantial discretion at the state and local levels to the very edge of becoming a national program administered by the states, on the model of the Food Stamps program. Even though these measures would tighten control, reduce error and actual fraud, and in a broad sense enhance objectivity and efficiency in program operations, state and local officials would no doubt sense their prerogatives being violated. However, the states would retain control of the single most important variable in AFDC, the payment level.

In addition, since absent major changes such as those discussed later, many current recipients would be made worse off, many of the measures are certain to provoke Congressional opposition. Interest groups, especially the day-care lobby, who attach symbolic importance to certain items of family income or expenditures now disregarded by present law, would strongly oppose the standardization changes.

Frequent reporting and retrospective determination, a good minor reform by itself, would demand data processing capabilities beyond those currently in place, and it is questionable whether either the Congress or the states would perceive the initial investment costs worth the substantial long term savings.

There is also a body of interest group and Congressional opinion that argues, despite fairly conclusive evidence to the contrary, that the welfare poor cannot cope with the demands of frequent reporting. Unfortunately, the introduction of an annual accountable period, which would have a very sizable favorable impact on internal program equity and cost and caseload control, presupposes such administrative changes.

In regard to our suggestion earlier that we propose tightening the conditions under which the Federal government, through the Social Security Administration, administers state supplements to SSI, I have to warn that Congress has been favorable to that issue in the past, given that the indigent aged are involved. We should, however, pursue this proposal regardless of whether we also go forward with the Income Supplement Program.

In summary, if we assume favorable Congressional and state reaction, enactment of the changes discussed here would enhance the equity, administrative efficiency, objectivity and most especially the predictability of the current programs. While some measures would increase caseload and costs, most would eliminate those program design defects that have led to caseload growth among relatively high income recipients. Due to state by state variations in AFDC it is impossible to give a firm figure on the net effect, but our work on the ISP proposal indicates that more would be saved by the tightening measures than would be spent by the two measures that would expand eligibility. (We would, of course, be running the risk that Congress would accept the cost and eligibility expanding features while rejecting the tightening proposals.) Substantial inequities between the states and our treatment of single parent versus intact families would remain, and assistance in many areas would still be very inadequate.

Finally, I am quite skeptical about favorable reaction by Congress, the states and the bureaucracy. We would be dealing with several different sets of committees, each wed to its own vision of the poor and their needs. What is accepted as commonplace in other contexts -- for example, measuring income on an annual basis -- becomes "oppressive" in the minds of many when applied to low-income population. As mentioned before, the states are used to their own discretion in the AFDC program and, despite the savings in state as well as Federal money that these changes would occasion, generally oppose any moves toward national standards in that program.

An Alternative Approach to AFDC

There are a variety of measures which some states, to the extent permitted by current law, have employed to contain caseloads in AFDC. Typically, these proposals reinforce the categorical nature of AFDC based on the notion, implicit in the program's beginning, that it is a program for single parent families with an unemployable female head. It has been argued that Federal law should be amended not only to permit but mandate such changes. Examples of this alternative approach are:

- establish a gross income eligibility limitation as a percent of the State's welfare needs standard;
- redetermine eligibility without earnings exemption for recipients who have received earned income for four consecutive months; and
- categorical exclusion of strikers from AFDC and AFDC-UF.

These and similar measures would, if enacted, hold down costs and caseload in the short run. But I would not propose most of them as part of a package for long term incremental reform, for they are opposed to such other policy objectives as providing work incentives, improving equity and introducing more efficiency and objectivity in program administration.

Further they avoid the central design problems of the present programs that could be remedied by changes discussed earlier. For example, some states are not very efficient in focusing income support on the most needy because they permit itemizing of work related expenses, and because assistance is not reduced by reason of other income between the state's actual payment level and its standard of need. Trying to contain the consequences of these defects by means of yet more complicated rules that encourage a dependency attitude on the part of AFDC recipients moves in the wrong direction. Earnings from work and income assistance should not be regarded as mutually exclusive.

MAJOR ADDITIONS

The measures discussed in the preceding section would improve somewhat the administrative efficiency, internal equity and objectivity of the three major welfare programs, result in somewhat better control of costs and limit caseloads. They would not, however, promote other goals. For example, the interstate inequities in the level of AFDC benefits would remain, as would the categorical nature of that program with its exclusion from cash assistance and comparable benefits of the so-called working poor. In addition, many would continue to view the system as providing inadequate benefits. Changes in the existing set of programs or major additions that would help lessen these deficiencies are discussed in this section. They are: (1) a national minimum benefit for AFDC; (2) a mandating of the AFDC-Unemployed Father program option to all states; (3) an Earnings Supplement or "work bonus" program; and/or (4) a housing allowance.

National Minimum Benefit for AFDC. In some states, AFDC payments fall far short of providing access to basic consumption needs. Each state sets its own payment standards and Federal assistance to states is based on amounts the states are able and willing to allocate to the AFDC program. The limited ability of states with low per capita incomes is recognized in the matching formula which provides a proportionately greater share of Federal funds to low-income states, but this has not provided incentive for a number of low-income states to increase their payments significantly. The maximum payment in 15 states is less than one-half of the poverty level. As a result, Federal resources help to support families above twice the poverty level in some states while in other states many families receive only the most minimal assistance.

A national minimum benefit in AFDC would improve benefit adequacy and, if primarily Federally-financed, would better target Federal support on those most in need. Substantial restructuring of Federal-state relationships would, however, be required. Decisions would have to be made on the minimum level of benefits to be mandated, changes in Federal-state sharing of costs, and possible changes in Federal-state division of administrative authority. The increased cost (above present expenditures) of an AFDC minimum, set roughly at proposed ISP levels, is estimated at \$700 million, most of which would probably have to be financed by the Federal government.

A national minimum benefit in AFDC would have a number of beneficial aspects. It would reduce significantly interstate variations in payment levels and increase the target efficiency of Federal funds in securing more adequate incomes for the poorest AFDC families. On the other hand, such a change would result in no substantial re-

structuring of the welfare system. The problems stemming from the multiplicity of overlapping categorical cash and in-kind programs would persist. Intact families would still be excluded; and because benefit levels would be higher, incentives for family instability might actually increase in those states now below the national minimum.

We could not move to a national minimum in AFDC without simultaneously enacting virtually all the standardization changes discussed in the previous section. The combination of two actions would mean that AFDC would become a fully national program, though state administered. This is now the case with the Food Stamp program. This would properly be regarded as a major change in Federal-state relations and would likely invoke the same criticisms about increased power at the Federal level that we assume the ISP proposal would generate.

Some of the critical issues involved in such a move are the choice of a method to finance the national minimum, and therefore, the relative roles of the Federal and state governments, incentives for efficient administration and "hold harmless" provisions for both states and recipients.

Mandatory AFDC-UF Program. The recession of the early 1960's brought attention to the needs of intact families when the father was unemployed for an extended period of time. In 1961, the Social Security Act was amended to include unemployment of a parent (amended again in 1967 to specify unemployment of a father) as an eligibility condition for receipt of AFDC. The use of this eligibility condition is optional with the states. Currently, 24 states and the District of Columbia administer AFDC-UF programs. Most of the remaining states have never participated in this program.

In order for a family to receive AFDC-UF benefits, the father must have been previously employed for a specified minimum period of time, must not be receiving unemployment insurance benefits, and must have been unemployed for at least 30 days. Unemployment is defined by regulation as employment of less than 100 hours in a month.

One of our minor proposals could be a requirement that all states include the families of unemployed fathers in the AFDC program. This would help alleviate the problems of extended unemployment of some additional male heads of families with children. However, since the categorical requirements of the program are so narrow and most of the larger states have already adopted it, such a change will have minimal impact. We estimate it would result in an additional 50,000 families receiving assistance at a cost to the Federal government of \$90-\$130 million (depending upon whether it is done in conjunction with a AFDC national minimum or not).

Earnings Supplement. Another response to the inequity of excluding most intact families from cash assistance would be to develop a program that covers specifically a portion of that population. Added impetus to this idea has also been given by the growing recognition of the burden of the payroll tax on the low-income population. This was the origin of the "work bonus," supported by Senator Long. This program was passed by the Senate in 1972 and died along with the Family Assistance Plan, in Conference. A similar program has again passed the Senate and has been pending in conference for almost a year.* It would add a benefit of 10 cents to each dollar earned by those family heads with incomes below \$4000 per year. Thus, the maximum benefit under the program would be \$400, with an average benefit likely to be about \$250 per year. As income rose above \$4000, benefits would be reduced by 25 cents on the dollar until eligibility ceased at an income of \$5600. A presumed advantage of such a program is that over a range (earnings below \$4000) earnings would increase by more than the full amount of any wage increase.

It is estimated that in 1976 such a program would transfer about \$500 million to more than 10 million persons in some three million families all of whom are currently covered by the Food Stamp program and many by AFDC. About 65 percent of the transfers would go to families below the poverty line. Earnings supplement plans that have higher transfer levels have also been proposed. For example, a plan that added 50 cents to each worker's wage for each dollar earned (and later reduced benefits by 33 cents on the dollar) would cover the same 10 million persons and cost about \$1 billion.

Housing Allowance. Another way to increase significantly the adequacy and equity of our welfare system while simultaneously fulfilling certain goals of housing policy would be to enact a housing allowance. Such a program would seek to insure that (some or all) low-income households could afford safe and sanitary housing by "filling the gap" between a minimal housing cost standard and the price the consumer could afford to pay. More specifically, the housing allowance would be the difference between the "fair market rent" for decent housing and, say, 25 percent of family income.

For an urban four person family this could translate into a plan offering a basic benefit of \$1800 per year in today's dollars which would then be reduced by 25 cents per dollar of other income. This relatively low benefit reduction rate (25 percent) -- a consequence

* It is part of a very large controversial bill that makes many AFDC and other changes.

of the desire to insure that families do not spend more than a quarter of their income on housing -- implies that benefit eligibility would cease at an annual income of \$7200.

Present plans within the Department of Housing and Urban Development would implement a housing allowance (if proposed and enacted) over a multi-year period. This would be another "in-kind" program rather than an unrestricted cash payment. Initially eligibility would be restricted to the aged, low-income population and later extended to the low-income working population. Ultimately eligibility would be extended to the entire low-income population including AFDC recipients. While a housing allowance could be restricted to, for example, the aged population, this would raise severe questions of equity.

HUD estimates that in 1976 a non-categorical housing allowance would cost about \$9 billion with 40 million persons in nearly 12 million households eligible. This of course would be in addition to AFDC, SSI and Food Stamps.

Thus the coverage of a housing allowance for the entire low-income population would be slightly greater than ISP, with net benefit costs well over twice as great.

In fact the combined benefit structures of the two comprehensive programs -- a housing allowance and Food Stamps -- would be roughly the same as the proposed ISP; however, these would be in addition to, rather than in lieu of the present AFDC and SSI programs.

Consequences of Program Additions and AFDC Modifications

The consequences of the various proposals discussed under this heading would involve major changes in the existing support system.

The modifications in AFDC, a national minimum and a national mandate of the UF (Unemployed Fathers), would take us that last step toward transforming AFDC into a fully national program with states administering it and determining upper, but not lower, limits on benefit levels. On the other hand, those steps to reduce present inter-state inequities and impose a national criterion of adequacy in AFDC could be achieved with relatively minor impact in costs and caseloads.

However, no amount of change in AFDC will redress the imbalance in our present treatment of the so-called "working poor," families where both parents are present and the father (and often the mother also) are more or less fully employed, although at low wages. It is to that portion of the low-income population that the Earnings Supplement and Housing Allowance proposals would provide the greatest

net benefits although the latter would be comprehensive in its coverage and, therefore, would also assist substantially present cash assistance recipients. Unquestionably these and most other proposals for new programs would improve adequacy and equity in the overall income support system, but we would I fear, end up only aggravating some of the worse features of the present system. (The technical and political difficulties of integrating several different means-tested programs are discussed in the next section.) For example:

- o Each new welfare program could demand the creation of a new administrative apparatus to administer it: a new unit in IRS to run the earnings supplement, and either a new component in the Social Security Administration or HUD or substantial personnel additions there and in the state and local welfare bureaucracies to administer a Housing Allowance.
- o Absent some very unlikely changes in our present cash assistance programs we would be adding these new programs -- much as we now do Food Stamps -- on top of AFDC and SSI. We could theoretically reorder matters to reduce AFDC and SSI to residual, subordinate cash programs. But I am skeptical that the Congress and the states would, for example, reduce AFDC assistance to recognize that housing needs were being met by a Housing Allowance any more than such an adjustment occurred when the Food Stamp program was introduced. This layering on of new programs without reduction in or elimination of existing ones would not only lead to very significant net costs, but also would further aggravate the problems of work disincentives and lack of coherency and control already associated with the present welfare system.

My own political assessment is that any gap filling strategy, especially one that includes an expansion of in-kind programs, merely leads to more uncontrolled and rapid growth in overall transfers. We could easily end up in the situation that now exists in some European countries where moderate income people pay substantial taxes and receive some of it back in the form of government subsidies that control their consumption.

PROGRAM INTEGRATION: PROBLEMS AND PROSPECTS

Departmental and Joint Economic Committee studies emphasize that the problems of the current welfare system cannot be resolved if programs are viewed in isolation. Many of the problems associated with the "welfare mess" have been caused by the continuous creation of categorical programs without much regard for the way in which these programs fit together. Because the largest transfer programs have been planned and administered independent of one another, there have been unintended consequences. The negative impact of high cumulative benefit reduction rates on work incentives, and the inequities of categorization are now widely recognized and discussed. While tinkering with the current system can do little to remedy these ills, the administrative inefficiencies of the current system are problems that are more amenable to marginal improvement. Though here the prospects for major improvements are also less than overwhelming, national program integration becomes even more important as the addition of major new programs is considered.

In the existing welfare system each program has its own eligibility criteria, income exclusions and disregards, assets limits and accountable periods; and, almost without exception, each program has its own administrative structure for carrying out the necessary functions of eligibility and income certification, computation of benefits, and distribution of payments. Even allowing for desirable differences, it is clear that there is an excessive amount of overlap and duplication in such an uncoordinated collection of programs.

Below are outlined five alternative improvements that could be made within the context of the existing system. We attempt to assess the relative effectiveness and political prospects of each alternative. They range from marginal improvement to major reconstruction, from the difficult to the improbable.

1. Transfer the Food Stamp Program to HEW. This often suggested transfer would pave the way for more recognition that Food Stamps are more an income transfer than an agricultural support program. Food Stamp benefits could presumably be delivered, through the SSI program, for the aged, blind and disabled population, while other recipients continued to collect Food Stamp benefits through the local welfare agency. Some changes could be made to bring income definitions (exclusions, disregards, deductions) into conformity with the SSI program and the AFDC program, but differences in filing eligibility units would remain because SSI is an individual-oriented program, AFDC is family-oriented, and the Food Stamp Program is household-oriented.

These changes would be of some value, but would occasion no dramatic increase in efficiency. I have therefore questioned the net advantage of adding yet another program to the panoply which HEW already administers or oversees, absent more fundamental reforms.

2. Standardize Program Definitions Among Various Transfer Programs.

This would involve conforming, or at least coordinating, eligibility rules, income exclusions and deductions, assets limits and work tests with various programs. Eligibility unit rules are less subject to standardization because they reflect the categorization of benefits that underlies the current welfare system. Simplifying program definitions, while seemingly sensible and non-controversial, has encountered strong opposition in the past, sometimes because there is disagreement about appropriate definitions, but more often because some recipients would be disadvantaged by the changes. In the latter cases, changes can be effected only by setting a high average for recipients, a costly process. Coordinating programs is also difficult when changes must be approved by more than one Department and, more importantly, more than one Congressional committee. Furthermore, conforming AFDC to other welfare program definitions would require a major increase in Federal regulations of a grant-in-aid program.

In the current system, coordination of program definitions could foster efficiency in those programs administered by the same agency (such as AFDC, Medicaid and Food Stamps), but would not be as useful for other programs (such as public housing). In almost every program standardization of income exclusions, disregards and deductions would be a marked departure from current practices and, as such, would encounter substantial resistance.

3. Institute a Dependents' Allowance in SSI. The SSI program covers only those who are aged, blind and disabled. If SSI adults have dependent children, these latter must be covered under AFDC. Rather than having two different cash assistance programs, one Federally administered, and the other state administered, dealing with the same families, it would be more sensible for both administrators and the families if SSI were broadened to cover dependent children of adult recipients. A major drawback to this is that it would increase the costs of assistance to those children to the Federal government since the basic SSI program is 100 percent Federally financed.

4. Integrate the Administration of all Major Means-Tested Income Transfer Programs. This approach would be a reform on the scale of the ISP proposal. It would require a complete restructuring of all current programs. All programs would use the same basic set of definitions, the same field operation and standardized procedures to determine eligibility, calculating benefits and making payments -- in essence, the whole system would be run as one unit. Such a proposal would be an ambitious undertaking, in some respects more ambitious than ISP. It would require major changes in all existing programs and heretofore unimagined cooperation of more than a dozen Congressional committees and several Federal agencies and their counterparts at the state and local levels. But it is the only alternative, within the context of the current system, that even comes close to realizing the administrative efficiency of the ISP.
5. Cash Out Food Stamps for AFDC Recipients and SSI Recipients. Elimination of in-kind forms of transfers in forms of cash would greatly simplify the present welfare system. Food Stamps, in theory, could be cashed out for current recipients of cash assistance. Of course, this has been tried once for SSI recipients. Under the terms of H.R. 1, SSI recipients were to be categorically ineligible for Food Stamp benefits. However, in many states former recipients of Old Age Assistance and Food Stamps, who were supposed to receive equal cash benefits under SSI, were actually disadvantaged. This experience suggests that it will be difficult to cash out only part of the Food Stamp program; if we do not go for all of it, we are likely to get none of it.

CONCLUSION

As you weigh the options of either adopting the Income Supplement Program (ISP) or attempting to improve our income support system through some of the above modifications (and possibly additions) to the present assistance programs, you might wish to consider that:

- o Though we often fail to realize it, we already have a national "guaranteed" annual income through a combination of Food Stamps, the public assistance programs of SSI and AFDC, residual general assistance programs of state and local government, and miscellaneous Federal measures including some of the veteran programs, the minimum benefit in Social Security, emergency extensions of Unemployment Insurance, and special programs for Indians and Cuban Refugees. The social realities that occasion low income -- old age, disability, unemployment, family breakups, and low skill jobs with correspondingly low wages -- often do not easily lend themselves to direct intervention or short term solution by government. While we must continue our efforts to deal with the problems of unemployment and underemployment of the low-income population, there do not appear to be any near term solutions. An income support strategy is thus an inevitable and critical component of our social policy. The relevant questions are then: How will the income support function be performed? To what extent do we wish to continue segmenting the low-income population into particular categories for income support? At which level of government should primary financial and administrative responsibility for supplementing the incomes of the poor rest? And what is the best program or mix of programs that will further best the objectives outlined at the beginning of this memorandum?
- o Should we decide to forego an ISP initiative at this time, we will nonetheless have to reconsider the same issues again over the next two years in different guise. For example:
 - You will soon have to consider HUD's Housing Allowance proposals, which, though improving adequacy and equity in the overall transfer system, would do so at great cost and to the detriment of the other goals of an effective income support system.

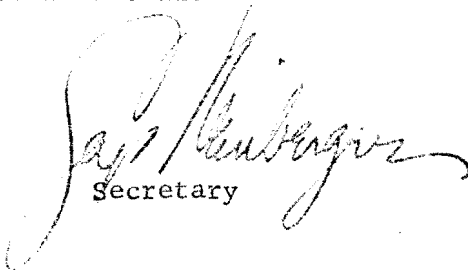
-- Congress will itself be proposing various gap filling measures such as Senator Long's Work Bonus, a Fuel Stamp program, and some quite substantial public employment programs.

In the absence of a well-defined income support strategy, we are much more vulnerable to the addition of new categorical or in-kind programs that have wide support because each addresses a single important problem. But no one pays attention to the totality of all public assistance programs -- the end result being an even more complex and uncontrollable set of interacting programs.

- o In the much needed debate about the public sector's command of our national resources, we will remain limited in our ability to explicitly set priorities for the governmental sector until we reorder and rationalize our income transfer programs, we cannot hope to begin that task until we strike a balance among the competing objectives for the means-tested income support programs. For example, control of our major social insurance program, Social Security, will not be possible in the absence of a coherent and comprehensive minimum income support system.
- o All these considerations argue for a long range perspective. What you choose today could determine the future disposition of the Federal government's resources. Based on its past performance, the Congress, as soon as it perceives any excess of future revenues over expenditures, will dispose of much of those resources by adding to our income transfer programs in ways that are popular, but do not necessarily focus the dollars on those with the greatest need. In short, most of the alternatives would cost as much as ISP, or Congressional additions to the existing system would use up our equivalent or greater amount of the Federal revenues by Fiscal Year 1978. The President, in his unique position to focus national debate, can prevent this past pattern from repeating itself, but only by presenting a comprehensive strategy that commands Congressional deliberation.

Clearly, I believe that the Income Supplement Program approach addresses these concerns better than any alternative. However, it is also the case that we could attempt to design a strategy that builds upon the existing programs. In order for that latter strategy to address the basic policy and fiscal trade-offs in our larger income transfer system,

we would have to propose some fundamental and controversial changes in the existing programs, especially AFDC, and at least consider some substantial additions. Thus, either way -- should you choose the ISP "replacement" approach or should you direct the development of an interdepartmental "reform" package that adds up to a coherent whole -- there would be a controversial and heavily debated program before the Congress for an extended period of time. But if we do not propose a major reform the present pattern of piecemeal and uncontrolled growth will reassert itself.



Secretary

Attachments

TAB A

TABLE OF CONTENTS

THE OPTIONS PAPER

Page

I. INTRODUCTION

1

This section notes the importance of continuing the effort to reform the welfare system and cites several sources of new evidence that help to clarify some of the unresolved policy issues. There follows a summary of the "Overview Paper on Welfare Reform," which describes the current welfare system and its shortcomings, examines the trade-offs among various goals, and lays a general foundation for the discussion of alternative approaches to welfare reform.

II. POLICIES OF GENERAL APPLICATION

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This section describes two general policies that can complement any major welfare reform strategy. Several labor market policies aimed at improving job opportunities are discussed. These include equal employment opportunity enforcement, job subsidies to employers, public employment and manpower training programs. Several initiatives to improve program management are outlined. They include AFDC program standardization, program integration, administrative changes and management capability improvements. Many of these initiatives are now HEW policy.

III. MAJOR STRUCTURAL REFORM

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This section begins with a general discussion of relating assistance to work effort. It then presents five specific options for substantial change or reconstruction of the current welfare system. These are: an AFDC national minimum benefit; an earnings supplement; an in-kind strategy based on the Food Stamp program; a new national health insurance program, and some sort of housing allowance program; and two alternative comprehensive cash assistance strategies, a variation on FAP and a Friedman-type negative income tax.

IV. CONCLUSION

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This section briefly summarizes the strategies discussed in the previous sections. Cost and coverage estimates are restated for each option. Relative comparisons are made among options and absolute comparisons are made against the standard goals of a transfer system.

TAB A: SUMMARY AND CONCLUSIONS (of the OVERVIEW ...)

This paper is the executive summary and conclusion section from the "OVERVIEW PAPER ON WELFARE REFORM." It describes the current welfare system and its shortcomings, examines the trade-offs among various goals, and lays a general foundation for the discussion of alternative approaches to welfare reform. (This material has been summarized in previous memos.)

TAB B: PROGRAM INTERRELATION AND SYSTEM INTEGRATION

This paper briefly notes the problems and inefficiencies that result from several overlapping and uncoordinated transfer programs. It discusses standardization within and among programs as it facilitates functional integration, and it notes the importance of rational integration in a multi-program system. This paper concludes with a section on the problems of integration under alternative reform strategies.

TAB C: FOOD STAMPS AND HOUSING ALLOWANCES

This paper describes the existing Food Stamp program and the emerging proposal for a Housing Allowance. Eligibility criteria, benefit structures, costs and coverage are discussed. The impact of a housing allowance proposal on welfare reform is noted.

TAB D: EQUAL EMPLOYMENT OPPORTUNITY

This paper includes a description of current anti-discrimination efforts, proposals for increased effectiveness and the impact of EEO on the low-income population.

TAB E: JOB SUBSIDIES IN THE PRIVATE SECTOR

This paper discusses various ways to subsidize private employment as a means of increasing job opportunities. It describes the target population and likely effectiveness.

TAB F: PUBLIC EMPLOYMENT

This paper outlines the problems addressed by public employment proposals, various alternative program structures, and the costs and likely impact of such programs.

TAB G: EARNINGS SUPPLEMENTATION PLANS

This paper discusses alternative structures for earnings-related assistance programs, interrelations with other programs, administrative issues and costs of various plans.

TAB H: THE CASE FOR THE NEGATIVE INCOME TAX,
 by Milton Friedman

Taken from THE REPUBLICAN PAPERS, a collection of conservative alternatives edited by (then) Congressman Melvin Laird, this paper is Friedman's own argument in favor of replacing the current welfare system with a simple and objective transfer program that is interlocked with the personal income tax system.