

Financial Incentives Can Be Key to Moving Families Off Welfare and Raising Income, Research Reveals *by Ellen C. Berrey*

At least 30 states are now using financial incentives in their welfare programs. Financial incentives change the economic structure of income support policies to “make work pay.” They reward recipients who look for a job, work, or work longer hours. With the passage of the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (PRWORA), states have the opportunity to design Temporary Aid for Needy Families (TANF) programs to replace AFDC that include a variety of financial incentives. Among the most prominent of these are earnings disregards, which in New Jersey, for example, enable a working TANF recipient to keep 100 percent of her income during her first full month of employment. Increased asset limits allow TANF families in North Carolina to own a car worth \$5,000 and retain \$3,000 in assets. Earnings supplements and benefits like the Earned Income Tax Credit (EITC) also can make work in the low-wage labor market considerably more advantageous than public assistance. Other financial incentives include bonuses or benefit increases for enrolling, participating, or completing a program; Individual Development Accounts; and utility, food, rent, child care, or shelter allowances often paid directly to the recipient.

While earlier research raised concerns that financial incentives could reduce recipients’ work effort, more recent findings indicate that incentives are helping some families improve their income, obtain jobs, and escape poverty without increasing welfare receipt. This article describes findings from three large-scale evaluations of programs with significant financial incentives in Canada, New York, and Minnesota (see chart on p. 3). To encourage

specific behaviors, each of these programs supplements income and/or lowers the rate at which cash benefits are decreased as recipients’ earnings increase. The two U.S. programs were created through state waivers available prior to the passage of PRWORA. All three evaluations include controlled experiments with random assignment of welfare recipients into treatment and control groups in order to assess the programs’ impacts.

The lessons outlined here are not conclusive; final findings are available only for the New York project. Caution should also be exercised in comparing results from programs with different economic situations, incentives, and research samples. Nevertheless, the three projects provide valuable lessons about how various financial incentives can be used.

Generous Earnings Supplement Appears to Work

Canada’s Self-Sufficiency Project (SSP) is a voluntary program for single parents. After receiving welfare benefits for one year, individuals who work at least 30 hours/week can leave welfare and receive an earnings supplement for as many as three years. This supplement is equal to half the difference between one’s earnings and a target or “break-even” earnings level set at about U.S. \$27,750 in British Columbia and about U.S. \$22,500 in New Brunswick. The supplement effectively doubles income for jobs paying between U.S. \$3.75–\$6.00 per hour.

Interim findings show that Canada’s SSP program is producing positive impacts—improving employment and

Note from the Director—Barbara B. Blum

The growing disparity between levels of income for working poor families as compared to the incomes of our wealthiest families is one of the starkest issues facing our nation. The experiments described in this issue of *the forum* provide provocative clues about strategies to alleviate the magnitude of this income gap, which, at the same time can also reduce the level of poverty experienced by so many working families

in the U.S. In addition, the research highlights challenges that must be confronted in conceptualizing an affordable approach to making work pay enough to provide adequate support to families.

The findings, however preliminary, are promising and should help guide our thinking about future income security policies which can further reduce the numbers of children living in poverty.

Common Characteristics of Effective Programs with Financial Incentives

- Fully implemented policies
- Voluntary program enrollment but restricted eligibility
- Mandatory full-time (30 hrs/wk) work requirements
- Positioning “outside” the welfare system (e.g. state-funded, separate office location, different staff training, de-stigmatized program)
- Simultaneous changes in welfare office culture
- Explicit efforts to explain and promote incentives
- Well-constructed rules concerning the incentives
- Careful integration of the incentives with other components of the program

earnings while decreasing welfare payment and receipt. Over the first 18 months, 34 percent of the program group went to work full-time; 75 percent of these working individuals retained their jobs for at least six months. In the fifth quarter, program participants had incomes that were, on average, 23 percent higher (about U.S. \$173/month more) than control group members and household earnings that were about 58 percent greater (about U.S. \$103/month more). Welfare payments were 15 percent lower (about U.S. \$87/month less). During this same period, participants’ employment rates increased by 13 percent, and they worked 20 more hours each month—66 percent more hours than control group members. After 15 months, the program’s net cost was approximately U.S. \$1,500 per participant.

Policymakers and practitioners have expressed concern that financial incentives, particularly a supplement as generous as SSP’s, may induce individuals to remain on welfare when they would not have otherwise in order to qualify for the incentive (also called “entry effects”). In SSP, very few Canadian welfare recipients—even those considered most knowledgeable about the earnings supplement—prolonged their stay on welfare in order to qualify for the incentive. Researchers cite the one-year eligibility restriction as a primary reason for the small overall entry effects. According to most program participants, their dislike of welfare, the difficulty of finding a job (and, thus, the imperative to take a job when offered), and the need to balance the demands of childrearing and work all precluded them from staying on welfare just to become SSP eligible.

Success Seems to Hinge on Supportive Case Management

The New York Child Assistance Program (CAP) has an innovative grant structure that creates an incentive for custodial parents to establish court orders for child support from the non-custodial parent while enabling

families to achieve incomes above the poverty level. Prior to entering this voluntary program, recipients must secure support orders for each child in the family. Also, recipients’ earnings must reach the threshold where the CAP grant exceeds the welfare grant, which is typically about \$350/month. This feature is intended to encourage recipients to begin working or to increase their earnings. Once families qualify for CAP, their base grant is about one third lower than the welfare grant level; however, a lower benefit reduction rate (10 cents for each dollar earned when monthly earnings are under the 1990 poverty level and 67 cents for each dollar when monthly earnings are above that level) raises families’ incomes above the poverty level before they lose program eligibility.

Final findings show that CAP had many positive impacts. Over five years, CAP produced 20 percent greater household earnings (\$2,613 more per family, on average, than the control group) and 4 percent smaller welfare payments (\$1,613 less). After five years, program participants had 6 percent higher employment rates than control group members; within the treatment group, those who participated in CAP had 38 percent higher employment rates. Overall, the program saved the state government about \$2,366 per family, with approximately \$50 million in total saving for the three counties where it is functioning. Researchers attribute these impacts to the combination of the high entry threshold, low benefit reduction rate, individualized case management, and the program’s “non-welfare” image. The delivery of the CAP message through innovative packaging and marketing also seemed to play a significant role.

Different experiences in each CAP county highlight the importance of program implementation and how components of the program interact. For example, Monroe County, which had the greatest success for most outcomes, had an especially well-implemented program. Case managers in Monroe focused intensively on identifying job opportunities and assisting individuals to become employed, work more hours, and find better jobs. In contrast, the program in Suffolk County had low enrollment rates and less substantial impacts, which researchers partially attribute to weak program implementation, less active recruitment of welfare recipients by case managers, and the lack of a separate identity and office space for the program.

Mandatory Work Requirement Can Make a Difference

Minnesota’s Family Investment Program (MFIP) is a mandatory program with differing rules for welfare applicants and long-term recipients (individuals who have received benefits for 24 out of 36 months). Both applicants and recipients in the program are eligible for the financial incentives. When the work requirements are met, the base grant is increased by 20 percent and 38 percent of gross

Database Research Projects with Findings on Financial Incentives*

CANADA SELF-SUFFICIENCY PROJECT (SSP)

Evaluator	Social Research and Demonstration Corporation (SRDC)
Research duration	November 1992 – March 2001 (Interim findings available)
Sites studied	British Columbia and New Brunswick, Canada
Primary financial incentives	Earnings supplement
Forthcoming publications	<i>Final Report on 54-month Impacts and Cost/Benefit Findings (June 2000); Report on 36-Month Impacts (September 1999); Report on SSP Plus (November 1998); When Financial Incentives Encourage Work: Complete 18-month Findings (September 1998)</i>
Publications	<i>Do Work Incentives Have Unintended Consequences? Measuring the “Entry Effects” in the Self-Sufficiency Project (March 1998); When Work Pays Better Than Welfare: A Summary of the Self-Sufficiency Project’s Implementation, Focus Group, and Initial 18-Month Impact Reports (March 1996)</i>

MINNESOTA’S FAMILY INVESTMENT PROGRAM (MFIP)

Evaluator	Manpower Demonstration Research Corporation (MDRC)
Research duration	January 1993 – December 1999 (Interim findings available)
Sites studied	8 Minnesota counties
Primary financial incentives	Larger base grant, earnings disregard
Forthcoming publications	<i>Final Report (Fall 1999); Child Outcomes Report (Fall 1999)</i>
Publications	<i>Making Welfare Work and Work Pay: Implementation and 18-Month Impacts of MFIP (October 1997)</i>

NEW YORK CHILD ASSISTANCE PROGRAM (NY CAP)

Evaluator	Abt Associates, Inc.
Research duration	April 1989 – December 1996 (Final findings available)
Sites studied	3 New York counties
Primary financial incentives	Child support incentives, lower benefit reduction rate
Forthcoming publications	<i>Final Report (Fall 1999); Child Outcomes Report (Fall 1999)</i>
Publications	<i>Five-Year Impacts, Costs, and Benefits (December 1996); Selected Analyses of Families’ Experiences with CAP (December 1996)</i>

* The evaluation of Milwaukee’s New Hope Project is not described here, but is in the Research Forum database. Financial incentives in this project include monthly earnings supplements and state and federal EITCs incentives. Interim impact findings should be available from MDRC next year.

earned income is disregarded in determining welfare payments. Most long-term welfare recipients are also mandated to participate in either full-time employment (30 hours/week) or training. The MFIP evaluation studied new applicants and long-term recipients as separate treatment groups, and thus can describe differential impacts for each set of program rules.

Interim findings from MFIP indicate that financial incentives, when combined with mandatory employment services, can produce substantial improvements in employment, earnings, and poverty rates. After 18 months, the program’s primary impact on new applicants was to increase welfare payments among those who were working, which assisted some families in escaping poverty. By the end of the follow-up period, there was no significant effect on employment for these individuals. However, long-term recipients living in urban areas experienced considerable increases in their employment rates (40 percent greater than the control group) and total

family incomes (13 percent greater), while welfare payments increased modestly (8 percent). A substantial number of these families—16 percent—had incomes sufficient to move them above the poverty line.

Findings to date also suggest that the employment and training mandate improves responses to the financial incentives considerably. With the mandate, program staff found more opportunities to describe to recipients the gains available through the financial incentives. Staff felt more capable of persuading program participants that work would pay, as well.

Time Limits May Adversely Effect Incentives

The combination of financial incentives and time limits must be carefully constructed to avoid unintended but serious consequences for working welfare recipients. When a program uses federally-funded earnings disregards or supplements and time spent working also counts against TANF time limits, employed recipients may

prematurely use up valuable months. While most state programs with financial incentives have not addressed this issue, Illinois' program is an exception. Its earnings disregard is funded with state money and designed to avoid this time limit effect.

None of the three programs described in this article included time limits at the time of the evaluation. New York is continuing CAP voluntarily by county, without adding time limits. However, Minnesota has recently passed legislation to operate a modified, statewide version of MFIP in which recipients have a five-year time limit on federally-funded cash welfare. Evaluation findings in states such as Connecticut, Florida, and North Dakota will likely highlight the implications of programs combining incentives and time limits.

Questions about each project remain unanswered. In Canada, for example, what happens to welfare recipients' income and poverty rates when these recipients reach the three-year limit on receiving supplements? Do participants who qualify for MFIP's financial incentives use up time against the TANF time limit sooner? In NY CAP, the requirement for child support orders increased the number of orders but restricted participation and, thus, limited gains in earnings and reductions in welfare payments. Was this requirement necessary?

It is much too early to make conclusive statements about the full impacts of two of the three programs described here. Nonetheless, findings to date point to important ways that financial incentives can reduce poverty and improve incomes. Research results such as these offer valuable, reliable information which should inform both federal and local decisions about welfare programs, most notably the re-authorization of PRWORA in 2002.

RESEARCH FORUM ON CHILDREN, FAMILIES, AND THE NEW FEDERALISM

The Research Forum, an initiative of the National Center for Children in Poverty, hosted at the Joseph L. Mailman School of Public Health of Columbia University, encourages collaborative research and informed policy on welfare reform and vulnerable populations. The Forum's ultimate goal is to identify and promote strategies that protect and enhance the well-being of poor children and their families.

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CORRECTION: On p. 2 of the May issue of *the forum*, the Minority Female Single Parent Demonstration was incorrectly attributed to MDRC. The correct evaluator for this project is Mathematica Policy Research, Inc.

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