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An Efficiency Argument for the Guaranteed Income

by

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Working Paper No. 212

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Abstract

This paper uses what could be called a multi-school approach to poverty policy, asking the following question: Given the many proposed causes for poverty, and the conflicting theories about how potential solutions would work, what conclusions can we draw about policy? This paper concludes that the Guaranteed Income is the most efficient and comprehensive policy to address poverty.

Key Words

Guaranteed Income
Citizen's Income
Income Redistribution
Welfare Reform
Public Employment
Poverty
Basic Income
Employer of Last Resort
Negative Income Tax
Social Policy
Public Jobs
Minimum Wage
Unemployment

Now, that we have had Welfare reform we need Welfare reform more than ever. In August of 1996, President Clinton signed into law a Welfare reform plan ending sixty years of social Welfare policy. Since the passage of the Social Security Act of 1935, impoverished Americans had a statutory right to governmental assistance. Now, in addition to turning Welfare over to the states, the law removes the guarantee of assistance. The needy can simply be turned away if they appeal to the government for help during hard times. The debate which led to President Clinton's signing of this legislation, as well as the current discussion about how best to implement it, highlights the issue of how best to attack poverty.

We can eliminate poverty in the U.S. Despite all of the talk of an economic slow down, we are wealthier today than we have ever been. The talk of a slow down only refers to a decrease in the *rate* of growth, but our economy continues to grow faster than our population. Yet the poverty rate has been stagnant or increasing for the last 20 years. This is in contrast to comparable nations that have been able to nearly eliminate poverty (e.g., Sweden and

Norway). We could do as well or better if we had a more coherent and comprehensive poverty policy.

In this paper, we will make the case that the Guaranteed Income (in any of its various versions: e.g., negative income tax, basic income, or the social dividend) is the most efficient and comprehensive method to attack poverty. In part 1, we define poverty and our goal for poverty policy. In part 2, we critically examine five theories of the causes of poverty: the physical inability to work, single parenthood, inadequate demand for labor, inadequate human capital, and a poor work ethic. In part three we critically discuss six policy strategies for fighting poverty: promotion of economic growth, Workfare, the minimum wage, separating the "deserving" from the "undeserving" poor, publicly guaranteed employment, and publicly Guaranteed Income. We assess how well each of these programs address the five proposed causes of poverty, making the case that the most efficient and effective of these is the Guaranteed Income.

THE DEFINITION OF POVERTY AND THE GOAL OF POVERTY POLICY

There are two different definitions of poverty: "absolute" and "relative." Poverty, according to the absolute definition, is the lack of resources necessary to meet one's basic needs. According to the relative definition, poverty is the possession of a level of resources which is less than some specific proportion of the level of resources possessed by the average person. According to the absolute definition, "the poverty line" is the amount of income needed for a person or family to purchase their minimum needs for food, shelter, and

clothing.¹ A family with less income than the poverty line is considered to be living in poverty. This is the definition we use. We do so because we think the relative conception is really about another important social issue: this is the issue of inequality. Instead of addressing this issue here, we leave it for a future work. Our first priority should be to meet everyone's basic needs before addressing the question of whether everyone is getting a fair amount of luxuries.

Just exactly how best to calculate the poverty line is the focus of considerable debate (Schiller, 1989; Schwarz and Volgy, 1992, and Mishel and Bernstein, 1994), but that is not the focus of this paper either. For our purposes, we accept the government's standard of the poverty line.

Although the goal one has for policy is closely linked to the particular policy one chooses to achieve that goal, it is important to define both separately. This allows us to evaluate how well different policies achieve the same goal.

We believe that there is a broad consensus among all but the most radical property rights advocates that the ultimate goal of policy should be to reduce poverty as much as possible and eliminate it if we can. Bob Dole exemplified this consensus in the 1996 presidential debates when he said, "this is America, nobody's going to starve." That statement is non-controversial even

¹ Medical care, though important to one's standard of living, we treat as a separate issue. One related problem that we will not be discussing in this paper is someone who is impoverished because of health *expenses* owed by them or a member of their family for a condition that does not prevent them from working. Providing adequate affordable health care to all citizens is an important public policy question, but it is best addressed as a separate issue.

in partisan debates; thus, we evaluate all policies on how effectively and efficiently they reduce poverty. The wide differences of opinion about poverty policy reflect differences about how best to achieve that goal, which in turn depend on people's beliefs about the causes of poverty.

VIEWS ON THE CAUSES OF POVERTY

There are many differing views on the cause or causes of poverty, including the physical inability to work, inadequate demand for labor, inadequate human capital, lack of work ethic, and single parenthood. There is no clear consensus about the relative importance of each of these possible causes. We discuss all of them and then discuss our own view.

A. Physical Inability to Work

Some people are physically incapable of holding a job and, hence, providing for their own subsistence because of old age or disability. Disabilities can be the result of a birth defect or an injury. They can be either physical or mental, including retardation or mental illness. Although this is in some ways the most straight forward and widely accepted cause of poverty, there is considerable gray area as to how disabled one must be to be incapable of working (Dolgoft, Feldstein, and Skolnik, 1993). According to the House Committee on Ways and Means (1992), the official definition of disability is, "Those unable to engage in any substantial gainful activity by reason of

medically determined physical or mental impairment expected to result in death or that has lasted or can be expected to last for a continuous period of at least 12 months.” Problems with this definition include, at what age is a person too old to work? At what I.Q. is a person considered mentally retarded?

B. Single-Parenthood

A single parent, especially of an infant, is faced with the problem of having full time demands on them outside of work. One cause of poverty could be that single parents cannot afford the time away from their children to work (Ellwood, 1988). Diane Pearce (1978) found that female headed families have become a disproportionate share of the impoverished population. William Kelso (1994) tells us that, between 1960 and 1991, the percentage of poor families headed by single women increased from 18.3% to 38.7%. There is disagreement, however, as to whether this should be viewed as a root cause of poverty or not (Mishel and Bernstein, 1994 and Garfinkel and McLanahan, 1986). If single parenthood does cause poverty, the root cause is whatever makes people become single parents. Are they people in unfortunate circumstances or people who have deliberately chosen their position? Some authors (Magnet, 1993, Murray, 1984, and Tanner 1996) argue that Welfare itself causes single parenthood by encouraging women who would not otherwise become single parents to do so. According to Marlene Kim (1997) while most single-parents with children under age six did not work, 46% of those who did work had incomes below the poverty line. We could conclude from this that the

reason that so many single-parents do not work is because if they do they have a high probability of still being in poverty.

C. Inadequate Demand for Labor

According to this view, the demand for labor is presently not high enough to employ, at above poverty wages, all those who are willing and able to supply their labor. Two consequences can follow from this: high unemployment or low wage employment. Keep in mind that, according to this view, low wage employment is caused not by lack of human capital but by inadequate demand. Just as is the case in any other market, when demand is less than supply, there is downward pressure on price, which in this case is the wage (Harvey, 1989; Harrison and Bluestone, 1990; Rose, 1994; and Wilson, 1996).

Unemployment occurs when the demand for labor is less than the supply of labor at the going wage. According to the U.S. Department of Commerce/Bureau of the Census' (1996) definition of unemployment, not everyone who is "not employed" is "unemployed." In order to be unemployed one has to be willing, able, and looking to work at the going wage, but unable to find it. A person can only be unemployed in this sense if there is inadequate demand for her labor at the going wage.

Neoclassical theory rejects the idea that unemployment can exist for very long. According to this view, what appears to be unemployment is really a result of people choosing not to sell their labor at the going wage. When demand for labor is low wages simply fall until an equilibrium is reached in which all workers

who are willing to work can find a job. In other words, if more workers want to work than there are jobs, the wage will simply fall until no one wants those jobs anymore (Munday, 1996). But, even if an equilibrium can be shown to exist there is no reason given to believe that the equilibrium wage will be a living wage.

Both of these situations could leave one sector of the population in poverty. In other words, there is no economic theory that everyone who wants to work can find a job that pays above poverty wages. In history, and in most of the world today, there are more examples of nations with a poverty wage sector than there are nations that employ everyone at living wages. It has been pointed out at least as long ago as Adam Smith (1776), and by many others since, that workers have a disadvantageous position in the labor market because they need a job to survive but the owners of natural resources do not need employees to survive. This could explain the tendency for wages to be low in at least some sectors of the economy. However, this cause of poverty tends to be overlooked, and we caution that any poverty policy should be evaluated by its effect on the market power of laborers.

D. Low Level of Human Capital

Human capital refers to the skills, knowledge, and abilities that make people more productive on the job. If the labor market is competitive, economic theory predicts that the people with more human capital will find more work and better paying jobs. This theory is the basis for one influential view of the cause

of poverty: people with poor skills end up either unemployed or employed in low wage jobs (Atkinson, 1983;Becker, 1993; and Ehrenberg and Smith, 1994).

E. Lack of Work Ethic

Some people may choose to behave in ways that cause their own poverty. For example, Lawrence Mead (1986) contends that an insufficient work ethic causes poverty. Able-bodied persons might choose not to work because they would rather stay home, or they may choose not to work hard and find it hard to hold a job. Individuals who chose not to work are considered “out of the labor force,” because they voluntarily chose not to participate at the going wage.

F. Our View of the Causes of Poverty

As we see it, all of the factors mentioned in the previous sections should be considered. The causes of poverty are many and complex, but the symptom is simple; people are poor if they do not have enough money to buy the basic necessities of life. Because the problem has many possible causes we would be ill advised to ignore any of them. We believe that a significant problem of formulating effective public policy is caused by the fact that many people on all sides of the political spectrum find it appealing to focus on only one or a few causes. The left tends to focus on unemployment while the right tends to believe that people do not value work enough. What tends to be left out of the discussion is that the extent to which people value work depends upon wages and working conditions. People may not value work, not because they lack the

work ethic, not because the alternatives are too appealing, but because the jobs available are not rewarding.

Policies should be evaluated on the basis of their effects on the living standards of the working poor, the living standards of those who do not work and the size of each group. In 1995 (the latest year for which data are available), there were 1.4 million families with at least one year round full-time worker with incomes below the poverty level (U.S. Department of Commerce/Bureau of the Census, 1996). 10 percent of working adults have incomes below the poverty line and another 8% have incomes less than 50% above the poverty line (Kim, 1997). The problem we address in the next section is to design a policy that takes all of the causes of poverty into account. Even though the problem is complex, the solution must be simple enough to be politically manageable. We should focus on treating the symptom, but look carefully on how well any treatment of the symptom addresses the causes.

SOCIAL POLICIES TO ADDRESS POVERTY

In this section, we discuss six possible solutions to poverty: four aspects of the current system and two proposed reforms. We do so by relating these solutions to the different possible causes of poverty, evaluating how well they combat these causes and achieve the goal of cost effectively reducing or eliminating poverty.

A. Policy Aimed at Economic Growth and Full Employment

One often cited approach is to aim government policy at increasing economic growth, indirectly increasing the demand for labor, increasing wages and reducing poverty. However, historically, growth has sometimes reduced but never eliminated poverty. In 1949, despite years of sustained growth and the highest per capita income in the world, almost one third (32%) of Americans lived in poverty (Levy 1987). The greatest reduction in poverty in US history happened in the period 1949 to 1973, falling from a 32% in 1949 to 11.1% in 1973 largely as a result of active government policy (Levy 1987). Since 1973 there has been a disturbing trend in which poverty increased, despite sustained economic growth, creeping back up to 14.5% by 1994 (Gottschalk, 1997).

Clearly, economic growth on its own does not eliminate poverty.

Why growth does not eliminate poverty is a difficult and controversial question that closely relates to the debate about the cause of poverty. Growth cannot cure the disabled. It could provide more opportunities for the unemployed, but not necessarily. William Baumol and Edward Wolff (1996) find that economic growth actually *increases* the average level of unemployment. Constantly changing technology, which stimulates growth, also tends to displace labor, creating demand for new skills, making other skills obsolete. Rebecca Blank (1994) reminds us that the poverty rate declined by little during the relatively long economic expansion which occurred between 1982 and late 1990. Therefore, we believe that economic growth, though strongly desirable, is not a solution to poverty.

A similar belief is that the government can use fiscal and monetary policy to maintain the full employment level of output. We believe that, like economic growth, full employment is desirable but full employment alone is not enough to eliminate poverty. The U.S. government's experiments at maintaining full employment have been mixed and some economists believe that the closest attainable approximation of it is a 5 percent unemployment rate (Munday, 1996). Others contend that it is possible to bring the unemployment rate down as low as 3 or 4 percent as it has been at times in post-war U.S. history. However, in 1966, during the Vietnam War, the unemployment rate was only 3.8 percent but the poverty rate was 14.7 percent (Census Bureau, 1975). In 1953, during the Korean War, the unemployment rate was only 2.9 percent, the lowest rate between the end of the Second World War and the present, yet the poverty rate was 26.2 percent (Murray, 1984). Explanation for this includes: even at "full employment" there are millions not working and there can be millions more working at low wages. Clearly full employment alone will not eliminate poverty.

B. Workfare

Workfare is a policy approach, now being implemented as part of the recent Welfare reform legislation. It serves as a component of The Temporary Assistance for Needy Families program (TANF), formerly AFDC.

TANF recipients are required to work or prepare for work in return for their benefits. Work activities include working in parks, social service agencies and schools. Preparation for work includes enrollment in secondary school,

classroom-based job training programs, and other activities, designed to prepare people to make the transition from Welfare to the job market. TANF recipients who do not take part in these activities stand the risk of losing a portion of their benefits. They are paid less than minimum wage, and far below the poverty line (Center on Social Welfare Policy and Law, 1996a). The Welfare reform law also includes a five year life time limit on Welfare benefits as an added incentive for recipients to move from Welfare to work (Center on Social Welfare Policy and Law, 1996b).

Obviously, Workfare does nothing for people who are physically unable to work. It is usually viewed as part of a more comprehensive strategy along with other policies aimed at those who physically cannot work.

Single parents are the main recipients of Workfare, but it apparently is based on the idea that the demands of raising a child is not a root cause of poverty. Its goal is to get single parents into the workforce, assuming that the reason they do not work is because they lack a work ethic or adequate human capital. This is a departure from the strategy of AFDC, which before 1988 did not require single parents of children under six to work outside the home (Lewis, 1995). Workfare requires that single parents put their children in someone else's care while they work. This increases the cost of the program. Part of the strategy of Workfare seems to be to discourage people from deciding to become single parents, but it does not offer anything very attractive to people who are single parents.

From the perspective of the low level of labor demand theory of poverty, the Workfare approach is unappealing. In fact, it is likely to hurt the working poor, increasing the poverty of those regarded as the most deserving. Neoclassical economic theory predicts that, all else equal, if Workfare succeeds in moving more people into the labor market, it will drive down wages. Keynesian theory predicts that new entrants will not necessarily be able to find work. Neither outcome is very attractive. Since low-wage workers are already paid poverty wages, even if former TANF recipients can find jobs at prevailing wages, they will still have incomes below the poverty line. Public debate has focused on the extent to which Workfare has succeeded in moving recipients from Welfare to work, with very little discussion of its impact on poverty. If TANF succeeds in reducing Welfare rolls by increasing the poverty of the working poor it could hardly be called a success.

From the low level of human capital perspective, the Workfare approach could conceivably be viewed approvingly, but it would take a major revision of the system to be effective from this perspective. This program is ostensibly designed to enhance the skills, work experience, and education of Welfare recipients. However, many of the jobs Workfare recipients are being offered, such as picking up garbage in parks, do not provide people with opportunities to enhance their human capital at all. A similar program, CETA, was canceled in the early eighties for just such rationale. If lack of human capital is the cause of poverty, Workfare would need to be completely overhauled so that the work

done by recipients was truly human capital enhancing. This, however, would greatly increase the expense of the program.

Supporters of the view that poverty is caused by the lack of a work ethic, often advocate Workfare because of its potential to socialize the undeserving poor into recognizing the importance of work. The fact that TANF recipients are denied assistance if they fail to show up for Workfare assignments provides a powerful incentive for them to behave more “responsibly” and go out and get a job. However, even from this perspective there is considerable doubt about the effectiveness of Workfare because it relies largely on negative incentives. Although they are paid less than minimum wage, people on Workfare are expected to work, but are not considered “workers;” they are still treated as “recipients.” It has not yet been established whether they have the right to organize, even though some claim that in many cases, their duties were formerly performed by union workers. Workfare offers its “recipients” work at poverty wages potentially for years. It is hard to see how this will teach people the value of hard work. It may only teach them that if you’re willing to work hard, others will take advantage of you. Perhaps, a program based on positive incentives is more appropriate.

The major problem with Workfare is that it appears grounded on an extreme version of the work ethic: a one sided moral obligation in which the poor are obliged to work for their subsistence, but employers (whether private or government) are not obliged to pay subsistence wages. Neither does it create any incentive for employers to pay living wages. In fact, much of our recent

Welfare reform has primarily benefited low wage employers rather than workers (Lewis, 1995). There are at least two less extreme alternatives. One would be to hold employers to a reciprocal moral obligation; the other is to offer people positive incentives to work rather than an obligation.

The latest round of Welfare reform greatly over-emphasizes the “bad values” explanation of poverty; it ignores even the *possibility* that the poor might already have a good work ethic. Many, perhaps all, would be willing to work if they had enough incentive to do so, but wages are so low that there is little incentive to do so. Our current strategy treats this by making not-working less attractive rather than by making work more attractive. In other words, we make people more willing to work for below poverty wages. This probably will succeed in increasing work, but it will not succeed in helping the poor.

The available evidence suggest that Welfare recipients who have been participants in Workfare programs are not much more likely to leave Welfare for work than those recipients who have not participated in such programs. Those former Workfare participants who do obtain employment usually end up with wages well below the official poverty line (Gueron and Pauly, 1991 and Friedlander and Burtless, 1995).

Supporters of the values argument would probably counter that simply getting people into the workforce will put them on the road to success, while Welfare is a dead end. We have three responses to this argument. First, hard work is no guarantee of long run success in the labor market. From the values perspective, one could say that it is an individual’s responsibility to improve her

skills. However, someone in a desperate situation working two minimum wage jobs to keep her family above the poverty line, would not have much time to enhance her skills. Low wage poverty could in this case be self-perpetuating.

Second, low wage employment has detrimental social consequences. Elliot Currie (1985) found that underemployment is, in fact, more closely associated with crime than unemployment.

Third, if Workfare does provide benefits, they are long delayed. Currently, in no state do Welfare benefits raise income to the poverty line (Center on Social Welfare Policy and Law, 1996a). This could last up to five years and still the recipient may not be able to find a job that pays above the poverty line when leaving the program. Therefore, Workfare risks making participants work through years of poverty only to end up still poor. It holds recipients to a moral obligation to work for subsistence, but does not hold anyone to the obligation to pay subsistence wages.

C. The Minimum Wage

The minimum wage is another strategy to reduce poverty. It has recently been increased to \$5.15 per hour, approximately \$10,000 per year before taxes. However, it would have to be increased much further -- to about \$7.89 per hour -- to bring wages to the poverty line. In 1994 (the latest year for which data are available) the official poverty line for a family of four was \$15,141 per year (U.S. Department of Commerce/Bureau of the Census, 1996).

Clearly, an increased minimum wage is not aimed at those who are physically unable to work. Assisting this group would require a separate program.

It could be somewhat more effective for single parents, although it does nothing directly to make work easier for single parents. It could make it more affordable for single parents to find childcare and increase their willingness to work. However providing daycare without driving living standards back below the poverty line would require either a further increase in the minimum wage or a government funded daycare program.

If the cause of poverty is inadequate demand for labor, the minimum wage approach is an unappealing solution by itself. It does nothing for the unemployed. On the surface, the minimum wage looks like an appealing solution if inadequate demand for labor causes wages to drop below the poverty line. However, even though it increases wages for those who can find jobs, it does not directly expand demand for labor, and, some argue, it might reduce the amount of labor demanded causing an increase in unemployment.

A proponent of the low level of human capital view is not likely to find much to approve of regarding the minimum wage approach, because it does not directly enhance human capital. It would treat the symptom but not the cause of the problem.

A higher minimum wage would have limited appeal for someone who believes poverty is primarily caused by a lack of work ethic on the part of the poor. Lawrence Mead (1992) argues that the poor, even the working poor, can

bring themselves out of poverty, if they take advantages of opportunities that already exist to improve their skills. A minimum wage, does increase the incentive to go to work, but it does not necessarily enough to bring everyone with "bad values" out to work.

Our view of the minimum wage is mixed. It is certainly the case that the government could increase the minimum wage enough to bring those working for it above the poverty line. This would be consistent with the idea of a reciprocal moral obligation for employers. However, there is conflicting evidence whether the minimum wage causes increased unemployment. Brown (1988) found that it does, especially among "minorities" and the unskilled, implying that a higher minimum wage would move some out of poverty and others into it. Card and Krueger's (1995) results suggest that we should question the link between the minimum wage and unemployment. Castillo-Freeman and Freeman (1991) find evidence that small changes in the minimum wage do not cause significant increases in unemployment but large changes do. To increase the minimum wage to \$7.89 per hour would be a 53 percent increase from where it is now and 86 percent from where it was in 1995. There is no certainty whether this would increase unemployment, but it does not help the unemployed. To eliminate poverty the minimum wage would have to be combined with other policies to help the unemployed and those who are unable to work. The Guaranteed Income, which gives low-wage workers market power to command a living wage, and which helps the working poor and the unemployed alike, is a simpler and more comprehensive strategy to achieve the goal of higher wages.

D. Separating the “Deserving” and “Undeserving” poor

The current social insurance system is based largely on the belief that there are not one but many causes of poverty, allowing us to categorize the poor, not by how poor they are, but by how “deserving” they are. People who advocate this policy typically believe that those who cannot work (either because of disability or unemployment) are the “deserving” poor while those who simply do not work, are the “undeserving” poor (Zastro, 1986). The strategy then becomes to categorize the poor by the cause of their poverty, create a different solution for each deserving category, and encourage the undeserving poor to get a job. If it works perfectly all of those who cannot work will be helped, while all those who can work will have no work disincentives. As we discuss below, this definition leaves out some one who does not work because of unacceptable working conditions.

This strategy offers a complex solution to a complex problem, employing each of the strategies discussed in parts A, B, and C as part of an enormous system of incomplete and overlapping programs as summarized in table 1.

Table 1:

<u>Category (cause)</u>	<u>Program</u>
Physically unable to work	Social Security, SSI, Medicare, Worker's Compensation, Medicaid
Single parents	TANF, public housing, Medicaid, Food Stamps
Unemployment	Unemployment Insurance, food stamps, public housing, Medicaid
Low wages	The minimum wage, food stamps, public housing, Medicaid, the earned income tax credit
Inadequate Human capital	Public education, some counseling as a part of TANF and other programs
<u>Lack of work ethic</u>	<u>Employment Counseling</u>

Despite the large number of programs, they are not enough to eliminate poverty or even to bring all workers out of poverty; remember that 10 percent of working adults have incomes below the poverty line (Kim, 1997). Each program has its own eligibility requirements, making it difficult for people in need to know what they might qualify for. Simply having low or no income does not qualify someone for these programs, and many poor people fail to qualify for any assistance at all.

The current method is not cost-effective. According to Frank Levy (1987), in 1984, only one fifth of government transfer payments went to means tested programs specifically aimed at the poor. In 1996, the U.S. spent 744 billion dollars on income assistance (see table 2).

Table 2: Government income assistance spending, 1996

Program	Cost (in billions of dollars)
Social Security	360
Income Security	228
Housing Assistance	27
Food / Nutrition	39
Other Income Security	64
Unemployment Compensation	26
Total	744

Source: U.S. Bureau of the Census (1996)

The categorical approach has been the basis for our social Welfare system since the great depression. Although it has had many successes and has helped to reduce poverty especially among the elderly, we believe it is clear that this approach has proven to be extremely expensive and not completely effective. The rest of this section discusses four reasons why the categorical approach is not efficient or effective: first, the problem with defining “deserving,” second, the cost of categorizing each person, third, the harsh penalty for the undeserving, fourth, the effect of this position on the of workers.

First, how can one accurately define “deserving?” But, even if we accept the distinction between those who cannot and do not work, how can we agree on who is able to work? Most would agree that a person with a severe developmental disability or someone with a profound case of schizophrenia is unable to work, but it is harder to agree about milder disabilities? A blind psychiatrist can still work but not a blind factory worker. Does being blind make a person deserving? Once being a single mother was considered “deserving” now it is not. We cannot expect society to determine a consistent agreeable definition of need.

Second, once a definition of need is determined, it is costly to separate each person into categories of need. The effort involved in categorization is expensive and there are significant costs to making mistakes. Our social Welfare system has numerous overlapping programs all with the same ultimate goal. Each program has its own eligibility requirements making it expensive for the government to determine who is qualified for which program, and it is difficult for needy persons to determine which programs they may be eligible for. Programs vary greatly in the portion of total spending taken up by administrative costs, some being surprisingly high. The administrative cost of Unemployment Insurance is more than 85 percent of its total budget while the administrative costs of social security is less than 1 percent of its total budget (House Ways and Means Committee, 1992).

Third, the cost of making mistakes is just as important. Someone who is actually deserving could be classified as not deserving (a type 1 error), or someone who is not deserving could be classified as deserving (a type 2 error). A type 1 error is someone "falling through the cracks" such as a homeless person with an undiagnosed mental disorder. Type 2 errors include giving benefits to someone who has a high income, such as sending a social security check to a retired billionaire. Type 2 errors also include giving benefits to someone who has a low income but would otherwise be earning a higher private income, such as a person who waits until unemployment runs out before looking for a job.

Separating the deserving from the undeserving involves a very high penalty for laziness. Even if a person is “truly undeserving” should they face imminent starvation? This makes the penalty for laziness more severe than the penalty for most crimes except murder. It seems also to retreat from the goal of eliminating poverty. Saving (1997) characterizes this as “tough love” saying that less redistribution will get more of the poor into the labor force, reducing the number of the poor at the cost of increasing the severity of poverty. Even if this were an acceptable trade off, we doubt that it would work once we seriously consider its effects on the labor market.

Which brings us to the fourth problem with the categorical strategy. It hurts the market position of all laborers. Requiring everyone to work increases the supply (or reduces the market power) of labor making workers desperate to get a job quickly. We have inadequately attempted to solve these problems by other government action such as the minimum wage and labor regulations, but none solve the underlying problem that workers are desperate for jobs, but employers are not desperate for workers. The distinction between deserving and undeserving does not allow a person the freedom to refuse a job because the pay is too low or the working conditions unacceptable. Our effort to impose “tough love” undermines our belief that people who work hard should be rewarded for it. The definition that those who work are “deserving,” implies that no one who works full time full year should live in poverty, yet 10 percent of our workers do—not because they are lazy, but because of their bargaining position.

This problem can lead to a paradox of hard work. The harder workers work, The more labor there is in the market, and the further wages will go down.

The current system over-emphasizes “bad values” as the cause of poverty. Workers may have good values but few opportunities, and “bad values” may be the result, not the cause of poverty. People at the low end of the job market know that the jobs available to them pay very little and offer little hope of advancement. A minimum wage job requires a single parent with two children to work two jobs just to get by; which could take 70 to 80 hours of work a week just to reach the poverty line. This person would not be able to save money to start his own business and would not have time outside of work to learn skills to improve her situation. It would take years to advance out of this situation. It is not surprising that people faced with these options do not develop a strong work ethic. If we want people to value work, we must make work valuable to them in the short run, not as a distant promise coming after years of poverty wages.

We believe that one should not be called “undeserving” for choosing not to work if the only jobs open to them would leave their families in poverty. We, therefore, search for a solution that will give workers greater market power. The Guaranteed Income will increase the market power of workers and so it will help the unemployed and working poor alike.

E. Public Employment

This idea, also known as the public job or the guaranteed job has been proposed in different forms for many years. Hyman Minsky proposed a version in

1986; another version, the WPA, was introduced in the U. S. during the Great Depression. A Comprehensive version would replace all transfer payments to those able to work (including TANF, unemployment insurance, the minimum wage, food stamps, and public housing) with a government guarantee to hire anyone willing and able to work.

Obviously Public Employment is not aimed at those unable to work; it would have to be combined with programs for the elderly and disabled as part of a more comprehensive strategy to eliminate poverty. It would eliminate the problem of separating the unemployed from the unwilling to work, but the problem of separating unable to work, from those able to work discussed in the last section would still be relevant unless it were combined with a Guaranteed Income.

There are a number of ways that Public Employment could eliminate single parenthood as a source of poverty, but not without side effects. The jobs could pay enough to enable workers to obtain private day care, or they could include day care as a fringe benefit, or they could arrange flexible hours and work-sharing arrangements so that groups of workers could take turns caring for each other's children. All of these create the problem of separating parents from children for a significant amount of time, but the alternative would be to classify single parents as "unable to work." This, however, raises the controversy of whether single parents should be held responsible for working and whether we would be providing an incentive for people to become single parents.

Public Employment could eliminate both problems caused by a low demand for labor. It would directly eliminate unemployment, and, if it pays higher than poverty wages, it would eliminate low wages as well, by being an effective minimum wage for the private sector. However, if the wage is significantly below the poverty line Public Employment would be ineffective in fighting poverty. Workfare guarantees a job for single parents, but with inadequate wages. A Public Job with health benefits, daycare, and a living wage would greatly reduce poverty, but a Public Job with wages similar to TANF “benefits” would not reduce poverty and would verge on being exploitative. (The rest of the discussion of Public Employment assumes it pays a living wage.)

Proponents of the low level of human capital view might approve of this approach with qualifications. It could directly eliminate the symptom (low wages), but would less directly address its cause. Public employees might or might not gain valuable work experience and skills necessary for them to increase their earnings if and when they return to the private sector. An extreme proponent of the low human capital view might fear that public jobs would become “make work,” and would not eventually lead to better private sector jobs. However, if such a problem arises, the system could be readjusted to include a job-training program.

People who think that the poor lack sufficient values might also voice qualified approval of this approach. They would see its major weakness being the difficulty to both guarantee a job and give people an incentive to work hard on that job. Could workers be fired for poor performance? If so, the job would not

be a truly guaranteed job, but if not, it wouldn't be much of a job. If a worker does not perform his job adequately, the problem of separating those who cannot perform due to mental disability from those who simply do not perform resurfaces. An employer of last resort may be reluctant to fire employees, but workers who least value hard work would have incentives to try to work as little as possible. One solution to this would be to heavily supervise employees, but this could increase cost, reduce productivity, and develop an antagonism between employees and management. However, like Workfare, Public Employment might socialize the poor into recognizing the value of work. It would do this more effectively than Workfare because it would positively reward work with a higher than poverty income. Thus, participants would directly and immediately see a positive reward for their labor.

Our view is that Public Employment would be a vast improvement over the current state of affairs, or any of the strategies discussed above. Like the Guaranteed Income it would act as an automatic stabilizer on the economy and would eliminate many of the sources of poverty. However, there are four reasons why Public Employment is not as cost effective as the Guaranteed Income.

First, it relies on an extreme version of the work ethic similar to Workfare. We say this because, like Workfare, a public jobs system would require able-bodied persons to work in return for assistance. Those who refused to do so would not be offered assistance. We hasten to add, however, that Public Employment with a living wage would apply the extreme version of the work ethic more fairly than the current system does. This is because it would create a

reciprocal moral obligation rather than a one sided moral obligation. It would require people to work for assistance but would assure that the level of assistance was high enough to allow them to escape poverty.

Second, a major disadvantage of Public Employment is that this would be significantly more expensive than the Guaranteed Income. In addition to the wage costs, the overhead costs would include supervisors, materials, transportation, and planning. The actual cost of the program could turn out to be many times the wages cost. Thus, it is likely to be the most expensive of all programs we discuss in this paper. The Guaranteed Income, because of its simplicity, would be likely to have low administrative costs comparable to Social Security as discussed above.

One could counter that the cost of Public Employment would be compensated by the fact that participants would be producing. However, participants would also be giving up time that they could spend in job training, starting a business, volunteering, getting an education, or doing whatever it is they find valuable. There is no objective way to judge whether participants would make more valuable use of their time with a Guaranteed Job or with Guaranteed Income and thus no way to objectively say that the increased production of the Public Employment approach would be worth its cost.²

² Unless the two are introduced simultaneously and the authority experiments with different wage rates and different Guaranteed Income levels to find out if the wage needed to encourage workers to switch is greater than their productivity.

The marginal tax rate could be reduced by collecting revenue from property, sales, or wealth taxes while collecting less revenue from the income tax.

Those who believe poverty stems from disability or single-parent status might find the Guaranteed Income approach appealing. A Guaranteed Income would assure that everyone unable to work, for any reason, would not become impoverished. Retirees could live off of the minimum income, but would be assured that the more private savings they have accumulated, the better off they would be. Some, however, advocate combining the Guaranteed Income with a retirement program or simply giving a higher maximum supplement to retirees. The Guaranteed Income would eliminate the possibility that someone would fall through the cracks because someone truly unable to work, but who does not qualify for a particular program under the current system, would be guaranteed assistance under the system we propose.

The Guaranteed Income would work very well to prevent poverty if inadequate demand for labor is the cause of poverty, whether it causes low wages or high unemployment. The unemployed would be able to live off of the minimum income until they found another job, while low-wage workers would receive a supplement bringing their income above the poverty line, always making them better off than those who are not working.

The Guaranteed Income would eliminate many of the negative effects of our current policies for low demand for labor. Unlike the minimum wage, it can not have a negative effect on labor demand. And unlike unemployment insurance, it would not encourage workers to stay on until their benefits run out nor leave them desperate to

guarantee that no one's income falls below the poverty line for any reason, but ensuring that the more one makes, the better off one is.

There are two important numbers in a Guaranteed Income scheme: The minimum income and the marginal tax rate. The minimum income (or the maximum supplement) is the amount of money received by a person who makes no private income. The marginal tax rate is the rate at which the supplement is reduced or private income is taxed as private income rises. The Guaranteed Income would replace the entire tax and benefit system with a simple equation. After tax income (D) equals private income (Y) times one minus the marginal tax rate (t) plus the maximum supplement (M):

$$D = Y(1-t) + M$$

The net tax (T) equals private income (Y) times the marginal tax rate (t) minus the maximum supplement (M). If the supplement is greater than private income times the tax rate, net taxes are negative (the family is a net recipient of transfers):

$$T = Yt - M$$

For example, suppose we constructed a system with a \$10,000 guarantee for a family of three and a 50 percent marginal tax rate (meaning that for every dollar a family earns they would lose \$0.50 of their supplement or they would pay \$0.50 tax on their private income). A family with no private income would receive the \$10,000

transfer. If that family earned \$2,000 privately, its benefits would be reduced by \$1000 (50% of \$2,000) amounting to an after tax income of \$11,000 (\$10,000-\$1,000+\$2,000=\$11,000). If this family increased their private earnings to \$10,000, their after tax income would be \$15,000. If this family increased their earnings to 20,000 (the break even point), they would receive no subsidy giving them an after tax income of \$20,000. Notice that this family is always economically better off increasing its private earnings rather than relying solely on the income guarantee.

Table 3: Hypothetical tax and income schedule

<u>Private Income</u>	<u>Net TaxAfter</u>	<u>Tax Income</u>	<u>Average Tax Rate</u>
0	-10,000	10,000	-
5,000	-7,500	12,500	-150%
10,000	-5,000	15,000	-50%
20,000	0	20,000	0
30,000	+5,000	25,000	17%
50,000	+15,000	35,000	30%
100,000	+40,000	60,000	40%

These numbers are purely for illustration. The minimum income level and the marginal tax rate would have to be chosen based on the poverty line and the revenue available. Notice that although the marginal tax rate is fairly high at 50% the average tax rate is much lower for most families. Notice, although the marginal tax rate is proportional, the overall effect of the tax benefit system is quite progressive.

find any job after their benefits run out. A worker on unemployment has to give up her entire supplement to take a job, and risks not being able to get her benefits back if she has to quit her job. Suppose a recipient received \$200 a week in unemployment insurance. If they were offered a \$250 a week job, they would lose all of their unemployment benefits, and start paying income taxes leaving them little better off and possibly worse off than staying on unemployment. A person in the same situation with a Guaranteed Income could take the job and see their after tax income rise from \$200 to \$325 a week without risking that they won't be able to get their benefits back if they have to quit their job. The Guaranteed Income ensures the more one works the more one makes while ensuring that no one fears complete destitution.

People who believe inadequate human capital causes poverty might voice qualified approval of the Guaranteed Income. It does not treat the cause, but it effectively treats the symptom. It does little to directly enhance human capital, simply giving people enough money to meet their subsistence needs. However, they might find something appealing in the approach because it would allow people more time to allocate to attempts to enhance their levels of human capital. If people were assured that their subsistence needs would be met whether they worked or not, they would be in a position to devote more of their time to training and other activities which would increase their levels of human capital. Such a person would have more opportunity to increase her human capital than a minimum wage worker today who would have to work two jobs to keep a family of three above the poverty line and would have nearly no time available to increase her skills. Also, the Guaranteed

Income could be combined with increased job training, placement, and educational funding. This combination would be superior to Workfare because it would offer both a long-term and a short-term solution to poverty caused by inadequate human capital.

The strongest opposition to the Guaranteed Income is likely to come from the perspective that a lack of work ethic causes poverty. Some might make this argument directly, others indirectly.

The strongest objection to the Guaranteed Income would come from people who directly contend that the lack of a work ethic causes poverty. They would say that a policy providing enough money for people's basic needs, would result in a severe work disincentive. We would not be able to get enough people to work to create the things needed to sustain us as a society.

This is an important objection. However, there are three problems with it, which we discuss in turn. First, it relies on a very strong and unrealistic assumption about people's aversion to work. Second, it relies on an extreme and one-sided version of the work ethic. Third, it ignores the incentive effects on businesses. Unlike the present system, the Guaranteed Income would always provide an incentive for people to work and earn more if they could, because no matter what a person earned they would always be better off earning more. The Guaranteed Income is a lump sum transfer (the poor receive it as a grant, others receive it as a tax deduction) and so itself causes no inefficiency; inefficiency could only be caused by collecting taxes to support it. It has a work disincentive only in the sense that one is

not completely destitute if one does not work, but it counters that with a significant reward if someone does work.

As mentioned above, the incentive to work for a person receiving a Guaranteed Income removes some work disincentives that many of our current anti-poverty programs have. TANF, food stamps, unemployment insurance, even public housing are all very difficult to qualify for. However, if something is difficult to obtain, it is risky to give it up. In a Guaranteed Income system a worker takes no risk when he takes a job. This would greatly reduce the “cycle of dependency” problem.

A supporter of the “bad values” view of poverty might respond using the extreme version of the work ethic: able-bodied persons are obligated to work for their subsistence. Those who hold this view tend to be ambivalent about or to oppose poverty policies that provide able-bodied poor people with assistance without requiring them to work for it. We are neither ambivalent about nor opposed to such policies, for two reasons.

First, as we have said it is one sided to hold individuals who do not own property to a moral obligation to work without holding society to a reciprocal moral obligation. There are two ways to solve this inconsistency. Either increase the moral obligation of employers (as the minimum wage and public jobs attempt to do) or decrease the moral obligation on the part of workers. We believe the second is more effective because there is little evidence that people have the bad values it is often assumed they do. On the whole people will work if given incentive to do so, and people are happier and better workers if they *chose* to work rather than if they are *forced* to work. Remember as cited above, that 10 percent of American workers live

in poverty despite working full time; this implies that some Americans have such a strong work ethic that they are willing to work even though there is little incentive to do so. Even before TANF, when AFDC had no time limits, most recipients were off public assistance in less than three years. The times and places where one does see a “cycle of dependency” tend to be where there are few opportunities in the private sector (Handler and Hasenfeld, 1997).

Second, property rights to natural resources *cannot* be created by trade; they are created by society because they are useful. Property rights are not an end in themselves but a means to the end of sustaining our community. People own land and resources and the goods we make from them because governments have made laws defining and protecting ownership. We do this because allowing people to own “the fruits of their labor” provides an incentive for people to labor. Thus, to the extent that our sustenance depends on enough people having an incentive to work and invest, allowing people to own the things they have worked for provides them with an incentive to engage in that activity on which our very existence depends. Property rights and market exchange are useful and justifiable if and only if they serve society. But, they do not serve everyone in society. Some segment of society always seems to be left out. Our understanding of the labor market is what leads us to this conclusion.

Recall that neither Keynesian nor Neoclassical theory necessarily imply that the labor market will provide above poverty wages for everyone who wants to work. Recall that in the absence of a redistribution scheme workers are desperate to work, but employers are not as desperate for workers, causing a tendency for low wages

in the least skilled labor markets. There is no way to hold workers to a moral obligation to work without putting them in this desperate situation. The most effective way to increase the living standards of workers is to remove the desperation by providing a minimum Guaranteed Income. Although the Guaranteed Income provides a supplement for non-workers and workers alike, its main function is to give low-wage workers the market power to command higher wages. If, as people so often fear, a large number of low wage workers attempted to quit their jobs to live off of the minimum income, the market would respond with higher wages to coax them back to work. Even if wages did not rise enough that everyone would chose to work, wages would rise enough so that the hard working would be significantly better off than they are under the current system and significantly better off than those who lived off the minimum income.

Many people make the values argument indirectly. Since the work ethic is so strong in our society, we should advocate poverty policies that are consistent with this ethic. A Guaranteed Income is not consistent with the work ethic because it provides people with "something for nothing." For this reason, even if a Guaranteed Income plan were to be enacted, the income guarantee would not be set high enough to meet subsistence needs. Politicians and the public would not be willing to give non-working people a lot of governmental assistance. A poverty policy that involved the government in the creation of public sector jobs would not run into this problem. Poor persons who took these jobs would be working for their subsistence, and politicians and the public would be willing to reward them with higher income than would be the case under a Guaranteed Income plan. The implication is that

due to our societal adherence to the work ethic, public assistance beneficiaries would end up better off under a public jobs scheme than a Guaranteed Income plan.

We agree that politicians and the public might be willing to give more money under a Public Employment approach than under a Guaranteed Income approach. This does not necessarily mean, however, that recipients would receive more money or would be better off. As we argued above, the Public Employment approach is very expensive. Taxpayers must be willing to give not only more, but enough more to cover the added expense of supervisors, materials, and all the other overhead cost of the Public Employment approach. Public jobs are likely to be so much more expensive and inefficient that it is doubtful whether people would be willing to give enough more to make sure that recipients would actually receive more wages than they would under the Guaranteed Income. Even if they did, they still might not be better off because work is a costly activity. With work often comes travel costs, child care costs, the cost of time lost, and other costs. The money used to purchase these cannot be used to purchase food, shelter, clothing, and other goods/services. If these things are taken into account, wages would have to be *significantly* higher before we could say that recipients would be better off with a guaranteed job than a Guaranteed Income.

CONCLUSION

Currently, states across the nation are in the process of implementing the recently enacted Welfare reform. This law requires those on Welfare to work in return for benefits, and it limits the amount of time recipients are eligible to

receive benefits to five years over their entire lifetimes (Center on Social Welfare Policy and Law, 1996b).

We are doubtful that this approach will do much to curtail poverty. In fact, it might actually exacerbate it. As more people are pushed off the Welfare rolls, they will face increased pressure to compete in the labor market, putting downward pressure on wages. Thus, at best, the result of the recently passed Welfare reform law might simply be to swell the ranks of the working poor.

One who believes that the value of work is that it can provide workers with a better life, would be distressed by this. It is not necessary to have poverty especially among workers in a country this rich. If the goal is to eliminate poverty, the Guaranteed Income is the most efficient and comprehensive means. In the end, the issue is a normative one. Should our society be so committed to the work ethic that we view work, even at poverty wages, as better than public assistance? No, eliminating poverty is so important that everyone deserves the resources required to meet their basic needs. We should reward the work ethic, not enforce the work ethic.

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