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**Policy measures for helping the working
poor: American and British experiences
and lessons to Korea**

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I . Introduction

The financial crisis in 1997 struck a hard blow to the Korean economy. In 1998, the Korean GDP decreased by 5.8% and the unemployment rate soared to a record high rate of around 7%. To the surprise of many, Korea emerged from its economic difficulties in a relatively short period, however. With strenuous efforts of the Korean government and people and thanks to the timely recovery of the world economy and the boom in the information technology(IT) industry, the Korean economy achieved a growth rate of 5% in the following year. By 2001, the unemployment rate fell to 4.0%, which was only slightly higher than the pre-crisis rate, and has since stabilized in the range between 3% and 4%.

The composition of jobs in Korea has recently experienced a major change. The manufacturing industry was the leader in creating jobs in the early stage of industrialization in the 1980s and 1990s. The labor market share of the manufacturing industry rose from 21.6% in 1980 to record-high 27.8% in 1989, but it then fell in the 1990s and reached a low of 19.1% in 2002. The composition of employment within the manufacturing industry has also been changing. The proportion of jobs in the labor-intensive textile and clothing industry has fallen, while that of the capital-intensive information technology and heavy industries has risen. The share of employment in the service industry, on the other hand, rose at an accelerating rate from 43.5% in 1980 to 71.5% in 2002.

One feature of the current Korean labor market is the presence of serious skill mismatches between demand and supply. On the one hand, the fast-growing so-called new technology industries, such as information technology(IT), biotechnology(BT), and nanotechnology(NT), are suffering from a lack of skilled labor. Also, the traditional manufacturing industries with low value added have suffered from a shortage of

resident workers and hence have been forced to hire foreign workers, mainly from South Asia and China. On the other hand, college graduates, whose number has more than doubled since mid 1980s, are having a hard time finding jobs and their search period has been getting longer.

Another aspect of the recent Korean labor market is that decent jobs are not being created at a sufficiently high pace. This is in part due to the changes in the production technology and to the Korean government's post-crisis policies of industry restructuring. Also, the labor market reform, pursued by the government to make the Korean labor market more flexible, has decreased job security of workers and contributed to a substantial increase of temporary workers.^{ㄷ1)} The proportion of temporary workers hovered around 45% in early and mid 1990s, but it has jumped to over 50% since the economic crisis, as more Korean firms took advantage of a more flexible labor market by relying on temporary workers to fill their vacancies. In addition to job insecurity, most temporary workers suffer from low wages. Today, the income levels of a considerable number of workers are quite low, due to low wages and/or long periods of worklessness.

As a result, the number of the working poor, who work but remain poor, has recently been rising. The Korean government estimated in November 2004 that about 1.3 million adults belonged to the working poor, defined as those whose family income is less than 200% of the family-size-adjusted minimum cost of living. Of these, 450 thousand were working, 110 thousand were unemployed, and the remaining 760 thousand were out of the labor force.^{ㄷ2)} They have unstable employment status and hence insecure income.

The resulting income polarization is becoming an important social issue in Korea. The Gini coefficient remained around 0.29 in early and mid 1990s but rose to 0.316 in 1998 and to 0.320 in 1999. The income share of the lowest quintile fell from 8.6% in 1993 to 7.4% in 1998. In contrast, the share of the highest quintile rose from 37.4% in 1993 to 39.8% in 1998, and hence the ratio of income share of the highest quintile to that of the lowest quintile rose from 4.35 in 1993 to 5.38 in 1998. These two shares in the following years have not been much different from the levels recorded in 1998, which implies that despite the recovery from the economic

ㄷ1) Temporary workers are those with the term of employment contract less than one year.

ㄷ2) Presidential Committee for Social Inclusion, 2004.

crisis, the inequality in the income distribution has not been improved. Between 1999 and 2004, the income share of the lowest quintile fluctuated between 7.2%(in 2004) and 7.7%(in 2002), and that of the highest quintile fluctuated between 38.8%(in 2003) and 40.3%(in 2001). The ratio of the highest quintile income share to the lowest remained relatively stable in the range between 5.16(in 2002) and 5.51(in 1999).

The increase in low-income jobs is one of the common features observed in recent labor markets in many countries. For example, in 2002, 20.4% of US jobs paid less than \$8.84 an hour, the wage level which could put a full-time worker out of poverty(US Bureau of Labor Statistics, 2002). Also, households with one or more workers account for up to two-thirds of the "income-poor" in the OECD countries (Forster and Mira d'Ercole, 2005). Needless to say, the most fundamental solution to the problems of the income polarization and the working poor is the creation of jobs that pay well, and hence the macroeconomic policies to accommodate this goal should be given the highest priority. At the same time, today's active labor market policies should take the prevalence of these low-wage jobs into account. That is, these jobs need to be considered as an important option for the unemployed or the underemployed, and hence some serious attention should be paid to such policy measures as in-work benefits that can provide additional financial support to the working poor.

Today, nearly all OECD countries have put employment integration at the very center of their fight against poverty. Active policies to get people back into the job market, first introduced as welfare-to-work for the unemployed, have been extended to other, more excluded, groups. The policies might also include an obligation to participate in labor market programs, and may involve financial penalties to enforce the participation.

Not all the people who get jobs get good jobs, or stay in work for long. Many poor households have low-paid or unstable employment. For these people, the "make work pay" policies are an important option. Low-skilled workers are given support through tax credits or benefits that are only available to them when in employment. These in-work benefits are long-standing pillars of the social protection systems in the UK and the US, where they reach, respectively, 5% and 20% of all households.

The Korean government is planning to introduce an EITC-like program to support low-wage workers. According to the governmental announcement in October 2005, the Korean EITC would be introduced in 2007 and the benefit payment would start in

the following year. The program will pay in-work benefits to low-income families with dependent children, and the amount of benefit will rise as the number of children increases. The income threshold for the eligibility has yet to be decided, but if the most likely level — 140% of the minimum cost of living — is adopted, then the program will cover around 839 thousand low-income families.^{주3)} The government also announced that only wage or salary workers would be eligible at the outset, and the coverage would be expanded in around 2012 to include self-employed workers as well.

In the meantime, the National Basic Living Standard scheme was introduced in 2000 as a means to support unemployed and low-income people struck by the economic crisis. The NBLS scheme replaced the previous Living Protection scheme and expanded its coverage by making all low-income people eligible for the benefit irrespective of whether they can work or not. This means that assistance to low income people has become recognized as a social or governmental responsibility rather than solely a personal responsibility.

Eligibility for the NBLS requires that family income falls short of the threshold set by the government to meet the minimum living standard, with the family size taken into account, and that their wealth does not exceed the program's limit. The family income includes the imputed income from the financial assets of the family's possession. Also required is that the household head has no close family members who are financially able to support the prospective recipient household.^{주4)} The amount of the benefit is the difference between the minimum cost of living, adjusted for family size, and the recipient's income. The benefit is paid in cash.

At the same time, the new scheme emphasizes the responsibility of the recipients to pursue their self-support. To this end, recipients with working ability are required to try to engage in some income-earning activities, and the government is responsible to assist these people to get self-support.

The current NBLS scheme has several weaknesses. First, a large proportion of poor people are not receiving the benefits. The condition of no close family members to rely upon is one of the most important reasons why many poor families become ineligible. In practice, however, a survey(KIHASA & Ministry of Health and Welfare,

주3) In this case, a family of four with the annual earnings less than 19 million Won will be covered.

주4) The close family members include parents, children, their spouses, and siblings.

2003) shows that a majority of these poor people fail to get the expected support from their close family members whose presence made them ineligible for the NBLIS benefits. Some did not want to ask for help, and some were rejected when they did ask.

Second, the low target efficiency is another problem. It is quite difficult to measure the precise amount of the prospective households' income, and hence it is highly probable that households with actual incomes above the poverty line get the benefits and that households get overpayments through the underreporting of their incomes. In fact, over 90% of both the recipients and case workers admit that the reported incomes are not credible.

Third, the amount of benefit is the difference between the minimum cost of living adjusted for the family size and the recipient household's income, which includes the imputed income of the assets of the household. This means that the benefit decreases at the rate of 100% as the household's income rises, which discourages the recipient and his or her household members from finding a job or increasing labor supply. These are the reasons why the recipients' participation in self-support programs administered by the government to help recipients to start working is low.

Fourth, under the current system, two types of employment services are provided to the recipients. For those who are judged as "employable", some assistance with job search and some low level of training are provided. Those who are judged as "non-employable" are encouraged and assisted to start his or her own business. Not only do these services fail to accommodate each client household's individual needs, such as health status, disability etc., but also the classification of clients itself cannot in general be precise or reliable, and hence in many cases recipients are not satisfied with the employment services they get.

Inadequately paid and trained case workers is another problem. It has generally been recognized that the role of the case workers providing employment services to the recipients is of critical importance. The compensation to case workers, however, is far from generous and hence their pride or motivation is not high. This results in poor services to the NBLIS program participants.

As a whole, it is fair to say that the current Korean welfare system leaves much to be desired. This report aims to discuss the measures to help the working poor recently administered in the US and UK in order to find lessons for Korea. Taking

into account the fact that the working poor have a high probability of alternating between working at a low wage and not working, it will cover not only measures for making work pay, i.e., in-work benefits that increase the compensation to work, but also measures to encourage the jobless people to work.

The organization of the report is as follows. Chapter II discusses the issues of defining poverty and anti-poverty programs in general. In Chapter III, the American experiences with the welfare-to-work policy measures are discussed. The EITC, the main in-work benefit in the US, is given special attention. The welfare reform in 1996 by the federal government and the experience with this reform in the state of Wisconsin are also discussed. Chapter IV discusses the British experiences with welfare-to-work policies. Covered are the British in-work benefit schemes and the New Deal programs for two categories of workers, young people and lone parents. Chapter V summarizes the policies for helping the working poor in the US and UK and discusses lessons for Korea based on the experiences of these two countries.

II. Major issues concerning anti-poverty programs

1. Goals and constraints in programs to reduce poverty

Every nation has three objectives in designing and carrying out policies to alleviate the economic hardship of its poorest families. The primary objective is to enable its poorest citizens to achieve at least some minimum standard of living, typically expressed in terms of an income, in money or in-kind, that provides a basic level of food, shelter, medical care, and other needs, including opportunities for success for their children in the next generation. The goal is equity, and its achievement necessarily requires some transfer of resources from the relatively prosperous citizens to the relatively poorest.

The second objective, which follows from the first, is to achieve these transfers of resources efficiently. A direct transfer of resources (or income) from one group of citizens to another causes disincentives to production by the givers, because they will face explicit (or implicit) taxes on their incomes. Correspondingly, the low-income families who receive the transferred resources will tend to have less incentive to produce for their own consumption. If the transfer from "rich" to "poor" is in the form of investments to increase the productive abilities of the poor, such as subsidies to their education and training, an additional efficiency objective is to obtain a return on the investments that exceeds the cost of the investments.

The third objective is to ensure that the type and amount of transfers of resources is consistent with the nation's cultural values and its specific institutions. Some nations rely more on voluntary transfers, perhaps through churches or private charitable organizations. Furthermore, large-scale anti-poverty (or redistribution) programs affect many aspects of the economic and social structure of society, some of which are

unanticipated and unintended. In some instances, policies that promote economic growth may increase inequality, and the choice between growth and equality depends on the nation's political and social values.

Economic growth will be affected — increased or decreased, depending on the types of redistribution programs and their success or failure. Anti-poverty programs are likely to affect the size, composition, and the marital stability of recipient families, the families' choices of where to live, and the educational attainments of the children.

2. Issues in defining poverty

(A) The appropriate demographic unit of analysis

The experience of the U.S. is drawn upon in considering the following choices : (1) the family, defined as two or more persons connected by blood or marriage and living together; (2) the household, which adds single-person units and other non-family combinations of persons living together. (3) A special case is multiple families living in the same dwelling unit. They are counted as separate families if they are not related. (4) Persons in the military and persons who live in long-term hospital-care facilities are not included in the official poverty statistics in the U.S.

(B) Measuring poverty

In the U.S. poverty status depends on both the definition of income(see C. below) and the number and the ages of the family members. Reports of both income received and family size are obtained from a government survey of a random sample of thousands of families each year. The "poverty line" — the minimum income below which the household is considered poor — rises with the number of family members. There is a presumption of economies of scale so that, for example, a 2-person household has a poverty line that is more than half that for a 4-person household. Also, a child under 5 is presumed to require a lower amount of income than an adult or an older child.

The official poverty statistics in the U.S. are defined by an absolute, not a relative, measure of income. The absolute money measure was devised in 1959 and is adjusted each year for inflation, based on the annual change in the Consumer Price Index. A measure of relative poverty, such as the proportion of families with incomes

less than half the median family income, would show less progress in reducing poverty in the U.S., reflecting the increase in income inequality among U.S. families in recent decades.^{주5)}

The severity of family poverty in the nation may be measured by statistics of the proportion of families "below half the poverty line" or "below 1.5 times the poverty line." Such designations are useful in examining a more complete picture of the poverty problem or for administrative purposes to determine a family's eligibility for various income support programs. Another refinement in measuring poverty is the concept of the "poverty gap", defined as the amount of income required to bring all poor families above the poverty line. This statistic measures changes in the incomes of poor families separately from the more frequently used "poverty rate," defined as the proportion of families that are below the official poverty line.

(C) The definition of income and problems with measuring poverty

In the U.S. the accounting period for measuring poverty is the calendar year. Although the poverty lines are adjusted each year for the overall change in inflation or deflation, for reasons of simplicity no adjustments are made to allow for the differences in the cost-of-living for groups with different consumption patterns. For example, food comprises a larger fraction of total expenditures for the poor than for middle or upper income families, and older persons tend to spend more on medical expenditures and less on shelter — the latter because they are more likely to be home owners rather than renters.

Generally, no allowance is made for i) non-monetary sources of income-substitutes, such as free or subsidized rent, subsidies for food purchases(e.g., the Food Stamp program in the U.S.), free or subsidized medical care, and other income in-kind benefits; ii) "imputed income" from various forms of durable goods such as houses and cars; and iii) fringe benefits in the worker's employment earnings and non-pecuniary differences in conditions at work, and usually both fringe benefits and working conditions are less advantageous for low-wage workers.

Money income from assets in the form of rents, interest, dividends, and "realized" capital gains are included in the family's annual income. Cash transfer payments from government or charitable services and cash gifts from family relatives or others are

^{주5)} For an extensive discussion of different ways of measuring income and other various material needs of families concerning poverty, see Citro and Michael (1995).

also included in the measure of annual income, although these sources are often difficult to measure and contain a lot of errors.

Self-employed persons, including farmers, are a special problem, because measuring their incomes is difficult, and their incomes often fluctuate widely from year to year. Negative incomes may be reported by self-employed persons who are not "poor" in terms of their actual consumption and wealth status. In the past the U.S. used a lower poverty line for farm families to take account of their home-produced food, but this was ended because farm families have become only a small percent of all families, and home-grown food is a minor component of their consumption. Many economists (dating back to Milton Friedman) believe that measuring annual consumption is a more valid measure of economic well-being than money income. Consumption is more difficult to measure, however, and in many cases using this measure would require an adjustment for increases in family debt that were incurred to maintain a reported amount of consumption. Also, in a given year, savings for future consumption would not be counted.

Another shortcoming in using money income to measure economic well-being is that neither leisure consumption nor the consumption of goods and services from unpaid house work by family members is included. Home consumption of foods on farms is a version of this issue. An interesting point about leisure consumption is that it may indirectly determine a poor family's eligibility for governmental support if there is a "work requirement" for the income-support program. Also, to receive unemployment insurance, there is usually a "job search" requirement. These cases apply to specific programs. The general point is that income-in-kind in the forms of leisure or home-produced goods and services are not included in measuring income and poverty.

3. Types of programs and strategies to reduce poverty

(A) Income-transfer programs

Transfer programs may consist of private charity or government programs that use tax revenue to transfer cash or income-in-kind from high-income households to low-income households. Government programs have varying eligibility requirements and may be offered for a limited duration, i.e., have "time limits." At the risk of over-simplifying, the income(or benefit) transfer programs can be divided into two

broad categories: those that are "means tested," which generally refers to the benefits being dependent on a low income or low wealth of the recipients, and programs that are not means tested because the benefits are paid to the recipients regardless of their incomes and wealth. In practice, all programs have features that make both the costs and the benefits of the programs at least partially dependent on the recipient's income and wealth.

There are more than a dozen major anti-poverty programs in the U.S. that provide transfer payments of income or income-in-kind to low-income persons and families. We concentrate on two cash transfer programs of historic importance, Aid to Families with Dependent Children(AFDC) and the Earned Income Tax Credit(EITC), because these two programs reflect a major change in anti-poverty policy that has taken place in the U.S. in the last ten years. The U.S. has largely shifted from providing cash transfers with no requirement that the recipient work in the paid labor market, as in the AFDC program, to programs, notably the EITC, that do require the recipient to be employed.

1) From 1935 to 1996, Aid to Families with Dependent Children(AFDC) provided cash transfers to poor families consisting of mothers with children under 18 years of age and no supporting father present. This was the most controversial anti-poverty program in the U.S., and in 1996 it was replaced by a radically different program that will be discussed below. From the 1930s to the mid-1960s, AFDC supported a minuscule fraction of the nation's families. Between 1940 and 1960, for example, only two to three percent of families with children received AFDC benefits(US Congress, 1998, p.402). From the mid-1960s to its demise in 1996 it became increasingly unpopular as its expenditures grew along with the growing numbers and proportions of poor fatherless families with young children. During this later period the cash transfer payments were supplemented by Medicaid, a health insurance program, and other programs providing food and housing benefits, which greatly increased the overall costs of the nation's welfare system.

In addition to the program's cost to taxpayers, AFDC was often blamed for contributing to the large increases in out-of-wedlock births and marital dissolutions, because only women with dependent children and without a husband(or father) present were eligible to receive AFDC benefits. The program also created disincentives to work among the female heads of these families because any earnings of the mothers

in the AFDC program led to a like amount of reduction in their transfer payments, so the program effectively imposed a 100 percent tax on the working mother's earnings. In 1994 and 1995 the expenditures for AFDC reached their peaks of \$29 to \$30 billion(in 2002 dollars), and slightly more than 14 percent of U.S. children received AFDC benefits(US Congress, 2004, pp.7~59 and 7~31).

The unpopularity of AFDC, because of its growing number of participants, increased costs, and its alleged incentives to dysfunctional behavior, led to its replacement by the 1996 welfare reform law, the Personal Responsibility and Work Opportunities Reconciliation Act(PRWORA), which will be discussed in detail in Chapter III. This law also provided a cash-assistance program, called Temporary Assistance for Needy Families(TANF), but this became much less costly than AFDC had been because TANF virtually required that almost all of its clients, mainly mothers in single-parent families, to seek and obtain employment. Once employed, the mother's earnings would usually raise her income above the level for eligibility for the TANF benefits, although not necessarily above the poverty line. This policy of requiring employment fortunately came at time, 1996, when the economy began a period of sustained growth with gains in wages and rising employment levels, and the numbers of families "on welfare" sharply declined. The TANF program also set time limits on the receipt of benefits to no more than 5 years over the course of the mother's lifetime, and this added another incentive for the mothers to find their own means of self-support.

2) The Earned Income-Tax Credit(EITC) is a large and growing income-transfer program in the U.S. that uses the national and state income tax systems to subsidize low-income workers. As a tax credit, the subsidy may consist of a reduction in taxes owed at the end of the year or, more frequently, an end-of-year cash payment that may reimburse previously paid taxes and/or provide an additional government payment according to the wage-subsidy formula(discussed below). It is designed to provide incentives to work. To the extent that the EITC does increase work experience and on-the-job training, it increases these two forms of investments in human capital that will increase the worker's future earnings. In this way the EITC combines features of both an income-transfer program and an investment(in human capital) program. The EITC program is discussed more extensively below in Chapter III. Expenditures for the EITC program were about \$30 billion in 2002.

(B) Human capital programs

The human capital programs discussed here are those that are primarily intended to improve the employment and earnings of low-income persons. Focusing on earnings alone is admittedly narrow, because over the long-run persons with more human capital in the forms of education, training, and health will improve their "life chances" in many ways — better marriages, wiser fertility decisions about the number and timing of children, and better parental skills — in addition to more success in the labor market. All of these skills reduce the risk of poverty.

For young people, education is recognized as a fundamental source of human capital that increases earnings and many desirable non-pecuniary objectives. Schooling from grades kindergarten to high school are freely available in public schools. Colleges or other post-high-school education usually requires tuition payments, although there are public subsidies and, sometimes, free schooling for children from low-income families. For adults of working age, programs that provide training, health services, and, in some instances, migration subsidies are all forms of increasing human capital to raise earnings. Migration is not usually included among types of human capital enhancement, but it is actually a widely used investment to increase earnings. The U.S. population is very mobile.

In principle, human capital programs can be examined by a benefit-cost analysis to determine whether they are justified on "efficiency" grounds. In practice, there are many difficulties in carrying out this analysis, even if the criterion is solely "efficiency." Judging the equity issues by measuring the incidence of who bears the net costs and who receives the net benefits adds to the complexity of evaluating the programs. Despite these difficulties, program evaluation is a major "industry" within economics, using controlled experiments in some cases.

(C) Public employment

Providing jobs in public employment is another source of income for unemployed or under-employed workers. Most jobs involve some on-the-job training (or learning-by-doing), so providing public employment or subsidizing employment will usually increase the worker's human capital in addition to providing a current source of income.

In the U.S. public employment programs historically have been adopted as temporary

sources of employment. During the Great Depression in the 1930s, for example, they were widespread and provided jobs for unemployed workers of varying skills. Since then and up to the time of the 1996 welfare reform, public employment had been used sparingly and temporarily and mainly for adults with limited skills and little or no work experience. Creating public work programs for adults in poverty were generally viewed as inefficient, demeaning to the workers, creating disincentives to work in "regular" labor markets, and failing at creating skills that would have value in "regular" employment — the term, "regular," referring to jobs in both private industry and traditional jobs in the government sector of the economy. Also, the programs did not seem suitable for the steadily increasing number of female adults in the poverty population who were single mothers of dependent children.

(D) Macroeconomic policies

Policies that promote full-employment are effective in reducing poverty in both the short-run and long-run. Expansive macroeconomic policies reduce unemployment in the short run and may have long-run benefits by increasing workers' human capital that come from on-the-job training and job promotions. There is, however, controversy about what types of government macroeconomic interventions are effective.

(E) Demographic policies

Demographic policies that affect the amount and incidence of poverty is a complicated issue, because some anti-poverty programs create incentives for demographic changes that increase poverty, and other programs, or even the same program, have demographic incentives that reduce poverty. Examples of demographic outcomes that increase poverty and that are allegedly caused by various anti-poverty programs are marital break-ups, increased child-bearing, and sending family members — for example, aged grandparents — into separate residences where their low incomes will make them eligible for inclusion in poverty programs. Conversely, examples of demographic policies that may reduce the risk of poverty are programs that promote birth control and stable marriages. It is worth repeating that almost every anti-poverty program carries with it incentives or disincentives that affect family composition and that family composition can be both cause and effect of poverty. Examples are given below in section 4.

(F) Minimum wage

Minimum wage laws have been in effect nation-wide in the U.S. for selected industries since 1935 and now covers almost all workers. The current minimum wage is \$5.15 an hour, which is somewhat less than one-third the median wage among all workers, and if received for full-time work(2,000 hours) during the year would provide only \$10,300, which is considerably less than the poverty line for a two-person family(about \$13,000). Raising the minimum wage has not been considered a major policy tool to reduce poverty in the U.S. for several reasons. Most workers in minimum wage jobs are secondary workers in families, over 60 percent are under 25 years of age, and only a small percent are in poor families. Thus, raising the minimum wage is considered to be a relatively ineffective policy to reduce poverty. There is also the likelihood that raising the minimum wage would decrease employment among these low wage workers, because employers would have incentives to substitute other labor sources and make substitutions in the technology of production. The adoption of the EITC, in contrast, subsidizes rather than "taxes" the employment of low-wage workers, and the EITC is restricted to families with low incomes. For both reasons the EITC is considered "target effective" as an anti-poverty program and has tended to shift attention away from minimum wage policies.

4. The Incentive issues

Two types of incentives are of interest. The first is administrative incentives that stem from the program's explicit rules and administration. If a program requires the presence of dependent children and an absence of a male parent, as the AFDC(Aid to Families with Dependent Children) program once did, then the incentives to bear a child and to be unmarried are present. If the program, a training program for example, requires being unemployed or abstaining from the use of illegal drugs, then those outcomes or behaviors are expected to be affected. Investigation and policing the recipient's behavior may be required, and this has its own complications and costs.

The second type of incentive involves behavioral responses to changes in prices and income, as analyzed by the economic model of consumer choice. These effects are well known to economists, although quantifying their magnitude has been difficult and

controversial. Briefly, benefits from anti-poverty programs raise the income of the recipient, and the "income effect" implies that more "normal" goods will be purchased. With respect to the choice between work and leisure, the conventional view is that leisure is a normal good, and so leisure will be increased. The income effect may also be positive with respect to fertility, although the effect may be very small, and there are some non-economic arguments for a negative effect on fertility from a rise in woman's income.

Price effects on behavior tend to be less controversial.^{주6)} An increase in the transfer payment for another child may provide an incentive for another child, especially if the woman is not working, has other children, and believes that the costs of the additional child are less than the value of the increase in the transfer payment. There are many changes in behavior that can raise(or lower) the transfer payment. For examples: migration from a State that offers a relatively low transfer payment to a State that offers a high transfer payment; the incentive for an unmarried mother receiving welfare payments to stay unmarried because she would become ineligible to receive welfare payments if she became married.

There are many types of incentives to promote or discourage work. As noted above, the AFDC program discouraged work by imposing an implicit 100 percent tax on the earnings of the working mother. Anti-poverty programs may, however, encourage work by subsidies for child care, health insurance conditional on working, transportation to work, and so on. The EITC has become a popular anti-poverty program in the U.S. because it provides transfer payments to low-income workers in a way that generally creates incentives to work. This plan will be examined in the next Chapter, and we will see that the plan has both incentives and disincentives to work, depending on the earnings level of the eligible workers and other factors.

5. Determinants of the poverty problem in the US

Adopting appropriate policies to reduce poverty requires understanding the historical

주6) Strictly speaking, the term "substitution effect" or "compensated price effect," should be used here, because we refer to the relative change in prices among goods and services, holding income constant. A price change in a good or service necessarily changes the real income of a consumer, so both income and substitution effects are operative.

forces that have determined the trends and composition of the poverty population. Since 1959, when modern measures of poverty have been reported by U. S. government statistics, the proportion of poor families — the "poverty rate," to use a convenient term — has declined from 18 percent to 10 percent in 2004.(See Table II-1, "Poverty Status of Families...".)

Table II-1. Poverty Status of US families by Type of Family, Selected Years

(Numbers in thousands. Families as of March of the following year)

Year	All families		Female householder, no husband present	
	Total	percent below poverty level	Total	percent below poverty level
2004	77,019	10.2	14,009	28.4
2003	76,232	10.0	13,791	28.0
1997	70,884	10.3	12,652	31.6
1996	70,241	11.0	12,790	32.6
1993	68,506	12.3	12,411	35.6
1992	68,216	11.9	12,061	35.4
1983	62,015	12.3	9,896	36.0
1982	61,393	12.2	9,469	36.3
1974	55,698	8.8	7,230	32.1
1973	55,053	8.8	7,230	32.1
1969	51,586	9.7	5,591	32.7
1968	50,511	10.0	5,441	32.3
1960	45,435	18.1	4,609	42.4
1959	45,054	18.5	4,493	42.6

(Source: US Census Bureau, 2005, p. 38)

A surprising fact about the 45-year time-series from 1959 to 2004 is that the full decline occurred in just the first 9 years of that period, from 18.5 percent in 1959 to 10.0 percent in 1968. In the following 36 years the poverty rate varied up and down between a low of just under 9 percent achieved in 1973, 1974, and 2000 to a high of slightly over 12 percent in the three years, 1982, 1983, and 1993. In 2004 the poverty percent for all families was 10.2 percent. Clearly, poverty appears to have been a relatively unyielding problem for the last 36 years.

In retrospect, the sharp decline in poverty in the first decade, 1959-1968 and its persistence since then can be largely explained by a combination of three economic and three demographic variables. Two of the economic variables, each positively related to family income and negatively related to poverty, are (1) wages and (2) the labor force participation rate of adult women, particularly married women. A useful measure of average wages is the median annual earnings of full-time, year-round workers for men and women. This measure of annual earnings, divided by 2,000 working hours — based on the standard 40-hour work-week and assuming an average of 50 weeks worked per year — provides an estimate of the average hourly wage (See Table II-2, "Real Median Earnings...").

Table II-2. Real Mean Earnings of Full-time, Year-round Workers by Sex, Selected Years

(People 15 years and older beginning in March 1980, and people 14 years and older as of March of the following year for previous years. Before 1989, earnings are for civilian workers only)

Year	Median earnings (dollars)	
	Males	Females
2004	40,798	31,223
2003	41,761	31,550
1997	39,521	29,309
1996	38,531	28,421
1993	39,143	27,995
1992	39,843	28,203
1983	39,369	25,036
1982	39,498	24,388
1974	39,750	23,355
1973	41,195	23,330
1969	37,335	21,977
1968	35,316	20,538
1961	29,945	17,742
1960	29,013	17,603

(Source: US Census Bureau, 2005, p. 58)

A second key economic variable, related to the first, is the upward trend in employment by married women, which created a second earner in most husband-wife families. A third economic variable is a measure of the dispersion of the distribution of family incomes. Generally, the greater the inequality in family incomes, holding constant the average family income, the larger is the poverty population. Family incomes in the U.S. have become less equal from 1960 to 2004.

Three demographic variables have also been important. The first is the decline in the

fertility rate, which has decreased average family size and, by definition, has lowered the poverty line for the average family. The decline in fertility has also reduced poverty because the decline has been one of the causes of the increase in the employment of women, although it is also true that the increase in the employment of women has been a cause of the decline in fertility.

The second demographic variable is the increased proportion of female-head families; specifically, families in which a mother is a single parent with dependent children (defined as children 18 years of age or younger). This tends to increase the poverty rate, because the mother's responsibilities for the care of her children limit her ability to be employed full-time in a job paying above-poverty earnings. To obtain a family income above the poverty line, she usually needs income support from the father of her children, but in many cases the income support is insufficient or even absent.

The third demographic variable is the increasing proportion of immigrants in the U.S. population (Immigrants are defined as having been born in a foreign country.) By far the largest immigrant group entering the U.S. in the last 40 years has been the Hispanic ethnic group, most from Mexico, but also from other Central American and Caribbean nations. Family incomes of this group of immigrants tend to be low, mainly because the adults have low levels of education and labor market skills. Also contributing to poverty among the Hispanic immigrant families are relatively high fertility rates, large family sizes, and low labor force participation rates of the wives.

Each of the above six variables are examined to indicate their effects on the size of the U.S. poverty population from 1959 to 2004. The variables are interrelated in ways that are not fully understood by social scientists, so quantifying their unique effects can be only suggestive of their general magnitude.

1) As shown in Table II-2, real median earnings of full-time, year-round male workers, the basic wage variable for men, rose by 22 percent in the 8-year period from 1960(the first year this statistic is available) to 1968, increasing at an annual rate of 2.5 percent, and the family poverty rate declined from 18 percent to 10 percent. From 1968 to 2004, a 36-year period, this wage measure for men rose by 15.5 percent, representing an annual rate of increase of only 0.4 percent, and the poverty rate in 2004, 10.2 percent, had hardly changed. Real median earnings of full-time, year-round female workers rose by 17 percent from 1960 to 1968, less than men's increase, but the increase for women from 1968 to 2004 was 52 percent, much greater than the increase for men over the same 36-year period. The female-to-male

ratio of this full-time wage was .607 in 1960 and .765 in 2004. Moreover, in 1960 there were 2.5 men for each woman among full-time, year-round workers, but by 2004 the ratio of men to women among this category of worker had declined to 1.4. These gains in earnings by women workers clearly increase incomes in families where the woman was a "second earner." However, an increasing proportion of these full-time working women were in families without a husband present. The growth in single-parent families with the woman as the sole earner increased poverty, as will be documented in point 5 below.

2) The employment of married women in husband-wife families grew steadily from 1960 to 2004. The labor force participation rate of married women, living with their husbands, rose from 32 percent in 1960 to 62 percent in 2000(US Census Bureau, 1995, p.406 and 2004, p.399). As a result, a majority of married-couple families have had two earners during the last 25 years. Husband-wife families have relatively low poverty rates of around 5 percent, and for husband-wife families with both spouses working the poverty rates are even lower.

3) Inequality of family incomes is the third economic variable and the only one of the three that has been a source of increasing poverty. A simple measure of the dispersion and inequality of the distribution of family incomes is the ratio of the median family income to the mean family income. The three-year average of this ratio from 1967 to 1969(the earliest years reported) was .89. The ratio decreased fairly steadily during the following four decades, and in the three years, 2002 to 2004, the average ratio was .73. The growth of the mean income relative to the median reflects the relative growth of the top part of the right-skewed income distribution(US Census Bureau, 2005, p. 31, Table A-1)

4) From 1960 to 2002, the decline in fertility and the corresponding decline in family size are indicated by the following statistics: (a) for all families the average number of their own children under age 18 living with the family was 1.39 in 1960, reached a high of 1.43 in 1965 and steadily declined to .96 in 2003(US Census Bureau, 2005, p.52). The decline in fertility rates reduced family size and time spent in child-care, which allowed mothers more opportunities for employment in the labor market. Both factors, the reduced size of the family and the increased labor force participation by mothers, lowered the risk of poverty.

5) In 1960 the poverty rate for families with a female head, which usually consisted of families with a single-parent mother and dependent children, was very high, 42

percent, and these families were 10 percent of all families. During the following 44 years the percent of female-head families steadily increased to 18 percent of all families in 2004, mainly because of increases in children born out of wedlock and increases in marital breakups, either by divorce or separation. The poverty rate for female head families declined from 42 to 28 percent, but the increase in the percent of female-head families was large enough to increase the overall poverty rate. If the percent of female-head families in 2004 had remained the same as it was in 1960, and if the poverty rates for female-head families and all other families were at their 2004 levels, the overall poverty rate in 2004 would have been 8.7 percent instead of the actual 10.2 percent. Another important point is that children in low-income, female-head families face a variety of disadvantaged circumstances that increase their risk of being poor in their adulthood. A final important point is that the percent of female-headed families is much higher among the black population, a group that bears the added disadvantage of racial discrimination. The percent of the population that is black, however, is only slightly higher in 2004 than it was in 1960.

6) The third demographic factor that has contributed to the persistence of poverty in the U.S. has been the immigration of Hispanics, mainly from Mexico. The poverty rate for Hispanic families was 20.6 percent in 1972(the first year the Hispanic ethnicity was identified for income statistics), when Hispanics families were 4.3 percent of all families in the U.S.^{주7)} The poverty rate for all U.S. families in 1972 was 9.3 percent. In 2004, the poverty rate for the U.S. families had increased to 10.2 percent, and the poverty rate for Hispanic families had declined slightly to 20.5 percent. By 2004, however, Hispanic families had increased to 12.4 percent of all U.S. families. If Hispanic families had remained at only 4.3 percent of the population in 2004, then with the same poverty rates for Hispanic and Non-Hispanic families in that year, the total U.S. poverty rate would have been 9.7. Therefore, instead of the observed rise in the U.S. poverty rate from 9.3 in 1972 to 10.2 in 2004, the U.S. poverty rate would have shown a much smaller rise from 9.3 to 9.7.

This calculation assumes that the poverty rates in 2004 for the two population groups, non-Hispanic and Hispanic, would not have been different if the relative sizes of the two groups had remained at the 1972 levels, which is a debatable assumption. One could claim that the increased Hispanic immigration lowered incomes among the less-skilled non-Hispanic workers with whom they competed for employment, and

주7) <http://www.census.gov/hhes/www/poverty/histpov/hstpov4/html>

thereby increased the poverty rate of non-Hispanics. Or a counter claim could be made that overall production and incomes in the U.S. were increased by the immigration. Another point is that the Hispanics who immigrated to the U.S. surely raised their incomes, and that this improvement in the economic status of a very poor group increased overall equity.

Two final remarks. First, the foregoing discussion of the major economic and demographic forces affecting poverty rates in the U.S. during the 45-year period between 1959 and 2004 has been restricted to the long-run trends. For this reason the effects of short-run, cyclical changes in the economy, which were discussed in Section 3 under the heading of "Macroeconomic policies," have not been mentioned in this section. The business cycle is, in fact, an important determinant of short-run changes in poverty rates, raising poverty in cyclical downturns when unemployment increases and wages are lowered or stagnant, and lowering poverty in the cyclical boom periods.

Another point is that the above focus on long-run structural changes in the economy has not discussed government programs and policies dealing with the poverty problem or with the distribution of income more broadly. These programs will be discussed later, but two claims about the programs that have been most vigorously debated may be briefly mentioned. The first is that programs that have been specifically intended to subsidize the incomes of the elderly have certainly lowered the poverty rates of this segment of the population. There is little dispute about the benefits received by the elderly from public subsidies to pensions, health care, and disability assistance. Moreover, there is general agreement that these programs are an important reason the elderly are under-represented among the poverty population in 2004 (relative to their numbers in the general population) in contrast to their over-representation among the poverty population in 1959. Second, there is considerable controversy about whether public programs to aid female-head families have increased poverty because of the explicit and implicit incentives these programs create to weaken marriage and marital stability and to discourage work.

III. Welfare-to-work policies in the US

1. The Earned Income Tax Credit (EITC)

(A) The History and Explanation of EITC

The EITC for low-wage workers in low-income families was enacted in 1975 mainly to offset the rising tax burden from increases in the payroll tax they paid for the Social Security programs. The Social Security tax increased steadily from 2 percent in 1937, when the program began, to its current level of 15.3 percent, and the tax was recognized as regressive because annual earnings above high levels — currently, above \$90,000 — are exempt from the tax. The EITC was restricted to low income workers to offset this regressive feature.

In 1987, in order to eliminate income taxes on families with incomes below the poverty line, the EITC was increased to the point where the maximum credit in 1987 equaled the real value of the credit in 1975. Also, in that year, the EITC credit was indexed for inflation. After 1987, the EITC subsidy to work increased several times, and its purposes moved beyond achieving more equity in the tax system to providing a wage subsidy that would encourage non-workers in low-income families to become employed and to encourage under-employed and low-wage workers to increase their employment and earnings. It has become a centerpiece to the anti-poverty program. Operating within the income tax system, it proved to be administratively feasible, and it was viewed by the general public as an acceptable alternative to the existing welfare system that discouraged employment and seemed to perpetuate a never-ending dole.

Administratively, the EITC is a "refundable tax credit," meaning that if the worker's EITC exceeded the amount of income tax the worker owes, then the excess is paid to the worker, usually as an end-of-year lump-sum payment. Workers with low weekly or monthly earnings may receive their expected end-of-year EITC payment in weekly or monthly installments, but over 90 percent of EITC recipients choose to receive the tax credit when their annual income tax records are filed at the end of the year. From 1975 to 1993 the EITC provided federal benefits only to low income families with dependent children, although some States allowed additional EITC benefits to low-income childless families. In 1994 the federal EITC substantially increased the benefit amounts and was expanded to include a much smaller refundable tax credit to low-income childless families.

The nationwide benefit payments of the EITC have risen in inflation-adjusted dollars from \$10 billion in 1990 to \$34 billion in 2003. In 1990, 12.5 million families received an EITC benefit that averaged about \$820(inflation adjusted) per family. By 2003 the transfer program had expanded its coverage to 19.3 million families(about 17 percent of all families) and its benefits to an average of \$1,800 per family.^{주8)}

The eligibility of households to receive EITC benefits involves four major requirements or restrictions. The first is that both the annual earnings from employment and the family's(or household's) annual "adjusted gross income" (explained below) must be less than a specified amount that depends on the number of dependent children in the household. The last column("Phase-out range: end") in Table III-1 shows the maximum income below which an EITC payment is allowable. The steady rise in these maximums reflect increases both in the annual inflation-adjustments and in the real levels of the benefits. Earnings from employment or self-employment are required because the program is intended to assist low-income employed persons.

The requirement that the household's "adjusted gross income" also must be less than the specified maximum is because the EITC is "means-tested" — that is, intended only for low-income households. Thus, the household would not be eligible for EITC if the sum of its employment income and its income from non-employment sources exceeds the phase-out maximums shown in Table III.1, unless the family has certain allowable deductible "adjustments" to its income that brings its total — or "adjusted gross" — income below those maximums.(Certain expenses occurred in obtaining

주8) US Congress, 2004, pp.13~41.

income or certain payments to tax-protected retirement plans are examples of the adjustments.)

The second restriction to be eligible for EITC is the "residence requirement," which applies to families with dependent children and separated parents. In these cases the only parent eligible to receive EITC is the parent who has custody of the child(or children) more than half the year. Thus, a father, to use the most frequent case, who has not met this residence requirement cannot legally receive the EITC even if he is providing a substantial amount of financial support for the child and even if the mother does not receive EITC because, for example, she is not employed or, if employed, her income exceeds the limits for receiving the subsidy.

In the U.S., single-parenthood of dependent children is common because of the frequency of marital break-ups(divorce or separation) and "out-of wedlock" births, and non-compliance with the residence requirement has been the major source of EITC payments to ineligible recipients. Hotz and Scholz(2005) report that in 2003 "between \$8.5 and \$9.9 billion, or 27.0 to 31.7 percent of the total [EITC payments] were paid to taxpayers who are not eligible." They propose methods to reduce this administrative shortcoming of EITC mainly by using information in the U.S. legal system governing child support payments to determine the residences of children and their fathers.

The third eligibility rule is that low-income "childless" households, including one-person households, may receive EITC only if the adult applicant is between 24 and 64. The reason for the minimum age is to exclude persons under age 24 who, although they live in a separate household from their parents, may receive unreported money or non-monetary support from their parents. Young adults between the ages of 18 and 23 who attend a university are one example. The reason for the maximum-age requirement is that low-income persons who are 65 and older have access to Social Security or to Supplemental Security Income(SSI), two programs for the elderly.

The fourth rule to determine eligibility for EITC is that the applicant cannot have received more than a modest amount of annual income(\$2,600 in 2003) from non-labor sources — specifically, from interest, dividends, capital gains, and net rent and royalty income. In addition, the following income losses for the tax year are disregarded and cannot be used to offset positive earnings: "net capital losses, net losses from trusts and estates, and net losses from nonbusiness rents and royalties."

These restrictions serve to exclude persons and households whose wealth status allows them to have a "normal"(or "permanent") income above that of the ordinary "working poor" households. Thus, owners of businesses whose profits for a given year are low, or even negative, would be able to receive EITC only if income from the assets listed above were less than \$2,600 and if their reported income was low enough without including the "net losses" listed above. A practical implication of these provisions is to restrict eligibility for EITC benefits to self-employed workers who normally earn low incomes, such as "street vendors", domestic-help workers, and "handy-man" workers who do yard work and home repairs.

(B) The structure of the EITC subsidy

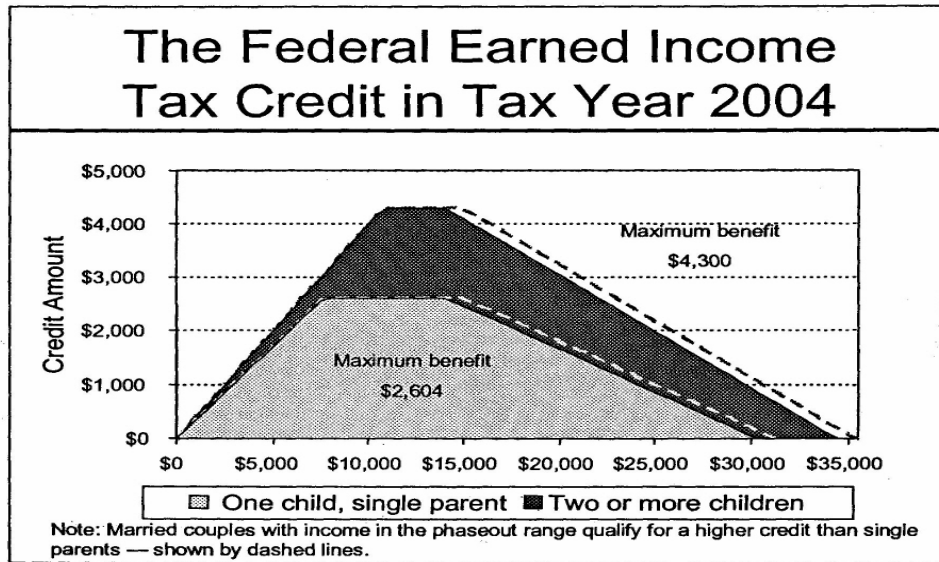
1) To illustrate the benefit structure of the wage subsidy, consider a family with one child. In 2004, the wage subsidy for the earnings of the parent of the child is 34 percent of annual wage earnings up to \$7,659, at which point the subsidy reaches its maximum value of \$2,604(= .34 x \$7,659). This maximum of \$2,604 stays at this level as the worker's earnings rise to \$14,032(at which point the subsidy amounts to 18.6 percent of the worker's annual earnings). At annual earnings amounts between \$14,032 and \$30,322 the EITC subsidy declines at a rate of 15.98 percent, reaching zero at the terminal(or phase-out) earnings level of \$30,322. The rate of subsidy decline is shown as the phase-out rate in Table III-1(Also see Figure III-1: Federal EITC in Tax Year, 2004).

Table III-1. Earned Income Tax Credit Parameters, 1975 ~ 2004

Years	Number of Children	Phase-in Rate(%)	Minimum Income for Maximum Credit(\$)	Maximum Credit(\$)	Phase-out Rate(%)	Phase-out Range(\$)	
						Begin	End
1975 ~ 1978	1+	10.00	4,000	400	10.00	4,000	8,000
1979 ~ 1984	1+	10.00	5,000	500	12.50	6,000	10,000
1985 ~ 1986	1+	14.00	3,929	550	12.22	6,500	11,000
1987	1+	14.00	6,080	851	10.00	6,920	15,432
1988 ~ 1990		(Inflation-indexed increases in maximum credits and in the phase-out ranges)					
1991	1	16.20	7,140	1,192	11.93	11,250	21,250
	2+	17.30	7,140	1,235	12.36	11,250	21,250
1992 ~ 1993		(Inflation-indexed increases in maximum credits and in the phase-out ranges)					
1994	0	7.65	4,000	306	7.65	5,060	9,000
	1	26.30	7,750	2,038	15.98	11,000	23,755
	2+	30.00	8,452	2,528	17.68	11,000	25,296
1995		(Inflation-indexed increases in maximum credits and in the phase-out ranges)					
1996	0	7.65	4,200	323	7.65	5,280	9,500
	1	34.00	6,300	2,152	15.98	11,610	35,078
	2+	40.00	8,890	3,556	21.06	11,610	38,495
1997 ~ 2005		(Inflation-indexed increases in maximum credits and in the phase-out ranges)					
2003	0	7.65	4,990	382	7.65	6,240	11,230
	1	34.00	7,490	2,547	15.98	13,730	29,666
	2+	40.00	10,510	4,204	21.06	13,730	33,692
2004	0	7.65	5,105	391	7.65	6,384	11,488
	1	34.00	7,659	2,604	15.98	14,032	30,322
	2+	40.00	10,752	4,300	21.06	14,032	34,433

(Source: U.S. Congress, 2004, pp.13 ~ 37 and 13 ~ 38)

Figure III-1. EITC Credit By Income



2) If the parent has two or more children, the initial wage subsidy is 40 percent of earnings up to an earnings level of \$10,752, where the subsidy of \$4,300 is at its maximum. The subsidy stays at this maximum until the annual earnings reach \$14,032, and then the subsidy declines at a phase-out rate of 21.06 percent, declining to zero at an annual earnings amount of \$34,433, which is \$4,111 higher than the cutoff point for the one-child family.

The phase-out earnings level of \$34,433 is 64 percent of the median family income (= \$53,800) in 2004. Thus, the program is restricted to assisting families whose incomes are well below the median. However, although the EITC serves to equalize after-tax incomes, about 20 percent of the families receiving its subsidies are above the poverty line.^{주9)} The poverty line for a family of four is around \$20,000, less than \$20,000 for smaller size families, and higher than \$20,000 for larger size families. This assistance to the "near-poor" families and the fact that EITC provides benefits only to working families are two important reasons for the program's popularity.

주9) See the website of the Center on Budget and Policy Priorities <http://www.cbpp.org>

3) The benefit structure of the program for childless households is as follows. If a low-income worker in this household is between 24 and 64 years of age, he or she is eligible to receive a subsidy of 7.65 per cent up to an earnings level of \$5,105. At \$5,105 the tax credit is at its maximum, \$391. The subsidy stays at that amount until the annual earnings reach a level of \$6,384, and then a phase-out reduction rate of 7.65 per cent begins. The \$391 subsidy is reduced to zero at earnings of \$11,488. The poverty line for a childless household is around \$10,000 for a one-person household and \$12,400 for a two-person household, so the EITC subsidy to childless households is much less generous than that for families with children. Thus, the EITC provides an incentive to child-bearing among childless couples, although the subsidy — the difference between the \$2,604 maximum for a one-child family and the \$391 maximum for the childless family — is much less than the annual full costs of the child.

(C) Incentives and disincentives of the EITC

There are many types of behavioral responses to the EITC income transfer program, but we concentrate on how the program affects the labor supply of low-income workers and give some attention to how marriage and fertility might be affected. Mainly we discuss the qualitative expectations of the labor supply responses, based on theory and distinguishing between the short-run and long-run, but there is some quantitative evidence as well. We begin with theoretical considerations of the work incentives for (a) those who are, and those who are not, currently employed, and (b) those in different demographic groups — men and women, married and unmarried, with and without dependent children.

1) Childless households.

The EITC subsidy for low-wage men and women, married or unmarried, who have no dependent children is small, and the subsidy is expected to have only minor effects on their labor supply. It will reduce their tax obligation, and for some provide a small cash bonus. This may be viewed as an improvement, even if slight, in overall equity.

2) Single parents with dependent children

The two principal types of work decisions that the EITC can influence are, first, whether to accept a market job for those who are not currently employed and, second, how much time (and effort) to work in a market job for those who are currently employed. There are several reasons why the work incentive is likely to be larger for those who are not employed.

The EITC provides monetary benefits only for those with jobs, and the decision to accept a job is largely under the control of the job-seeker, allowing for normal, but usually temporary, "frictions" in the labor market or in the job seeker's personal life. To be sure, the job-seeker's choices in the labor market is limited to jobs that correspond to the seeker's general skills and to the range of work schedules available. But, generally speaking, adults who are not physically or mentally handicapped can determine whether or not to work in the paid labor market and whether to work part-time or full-time. For low wage persons who are not employed, the EITC raises the wage they can earn by becoming employed. For low wage persons who are employed, the EITC raises their wages and makes exiting from employment more costly.

In contrast to the choice about taking or leaving employment, the choices about the amount of one's hours of work for those who are already employed are limited for various institutional reasons. Because almost all low-income workers are employees in a firm, rather than being self-employed, their working hours are limited by the firm's schedule of its days and hours of operation. Employees may be able to decrease their scheduled hours of work by absenteeism, but this would jeopardize their employment status and would likely lead to their discharge. The employee may desire to work longer hours than the firm's regularly scheduled hours, but usually such "overtime" hours of work are determined by the employer.

These institutional constraints make the transition to employment more responsive to the EITC's increase in the effective wage than the response of changing one's hours of work. Low wage workers in the firm who wish to increase their hours of work in response to the EITC generally have to leave their current job to search for another job that offers more work hours, a transition with some risk and costs.

For the above reasons, we should expect that the EITC subsidy will have the largest effect on increasing the work time of persons who (a) are not currently working, (b)

who depend on their own earnings as their major source of income, and (c) who have dependent children in their care. Women with dependent children and no husband present and no or minimal outside income support for their family constitute the largest group that matches these characteristics. Thus, it is not surprising that most of the research to measure the effect of the EITC on time at work (on labor supply, to use the economist's term) has been conducted with this demographic group. In a review article of the empirical studies on this issue, Hotz and Scholz (2003) report "employment elasticities with respect to net income (associated with EITC changes) from selected previous studies that range from .69 to 1.16". The mid-point of this range is .92, and an elasticity of this size suggests that a 10 percent increase in net income, stemming from the EITC augmented wage, would lead to a 9.2 percent increase in the ratio of employment-to-population (E/P). The employment-to-population ratio of single mothers is about .70, so the predicted increase would lead to an E/P of about .76.

A recent study by Rothstein (2005) reports that "labor supply increased for single mothers throughout the lower portion of the skill distribution [where the EITC mainly applies] in the mid-1990s, relative to both higher-skilled single mothers and to comparably-skilled single, childless women." He adds: "The largest changes [increases] are seen in two-child families [where the subsidy is largest] and on labor force participation margin, with smaller changes in employment rates - implying a net shift from non-participation into unemployment [i.e., searching for employment] and essentially no change in weekly hours conditional on working" (p. 4). No change by those who are already employed is consistent with the hypotheses (a) that employees have limited control over their hours of work in the short run and (b) that the incentives to work more or less are mixed, depending on where the worker is located with respect to the three earnings phases of the EITC subsidy. In the highest earnings phase, the EITC produces a net reduction in the worker's marginal wage (or, equivalently, a net increase in the worker's marginal tax on his or her wage).

3) Married men and women with dependent children

Married men in families with dependent children are almost all working, or if they are unemployed they are likely to be searching for a job regardless of the presence of EITC. Therefore, EITC is not expected to have much effect on entering the labor market for this group. There are two limitations of the EITC's effect on hours

worked by employed men who are eligible for the program's benefits. The first, already mentioned, is that these men are likely to be working full-time, usually between 35 and 45 hours per week, and they have minimal control over the amount of their work time. A second reason is because men, compared to women, are more likely to have higher wages and to be working full time, and, therefore, they are less likely to be in the low range of earnings where the wage is being subsidized by the EITC and more likely to be in the EITC's "phase-out" range, where their marginal wage is actually decreasing. The declining net wage is not likely to decrease the work hours of men in the phase-out range because their low incomes and responsibility for their dependent children make it unlikely that additional leisure will be considered more valuable than additional market goods and services. Ellwood (2001) reported only a modest increases in the labor supply of men in a family with dependent children.

Another demographic group of interest is married mothers with husband present. The mothers in this group tend to be secondary earners in the family and to have greater responsibility for house work and child care. Thus, compared to their husbands, mothers have more choice and flexibility about working full-time, part-time, or not working in the paid labor market. If their husbands are not working, perhaps unemployed and searching for work, or if their husbands are very low earners, the wives may find the EITC subsidy to employment compelling. Another possibility, however, is that if their husband is employed and committed to his status as the family's main earner, the mother, if also employed, is more likely to be in the phase-out range of EITC where the marginal value of her wage is declining. This would be a disincentive for her to take a job or, if working, an incentive for her to work less in the market. These reasons for expecting small and even negative effects of the EITC on the labor supply of wives, husband present, are supported by the research of Eissa and Hoynes(2004) and Ellwood(2001).

The above discussion has concentrated on relatively short-run responses. In the long run the worker has more control over his hours of work because in the long run he will have opportunities to change his job to satisfy his preferences for an optimal mix of hours and wages. However, perhaps the most important long-run effect from becoming employed and increasing one's working hours is that as low-wage workers work more, their skills are likely to increase from increased on-the-job training or from "learning-by-doing." An increase in workers' skills implies higher wages and greater output for any given amount of time at work.

In summary, the EITC program should be expected to slightly increase the employment and hours worked of low-wage, low-income workers. Even if there is no increase in work time by these workers, the EITC retains its effect on providing a transfer payment that serves the equity goal of alleviating poverty.

4) The effect of EITC on marriage and fertility

There have been no empirical studies of the effects of the EITC on marriage and fertility, and the theoretical analysis does not give a clear answer. Marriage and fertility might be encouraged because the EITC assists low-income married couples with children to achieve a higher income. A one-child family receives a much higher wage subsidy than a childless couple, and a family with two or more children receives a higher wage subsidy than the one-child family.

There are, however, incentives of EITC that may decrease marriages, increase divorce and separations, and decrease fertility. Incentives for increased employment by women may reduce their need for the income support of a husband. It may give married women an improved employment option that could promote divorce and separation. The employment incentives for work by women, single or married, will give them higher earnings and better career options. Because bearing and raising children require large amounts of the mother's time, the fact that the EITC can raise the value of the women's time in market work raises the costs of bearing children.

Marriage and fertility decisions have consequences — benefits and costs — that extend over a long period of time. For this reason, empirical evidence about how EITC, and indeed almost all anti-poverty policies, affect these choices about marriage and fertility will probably take many years of experience with the programs.

2. Welfare reform in the United States: The 1996 Personal Responsibility and Work Opportunity Reconciliation Act (PRWORA)

(A) Background.

The 1996 national welfare reform law, PRWORA, made sweeping changes in the welfare system. The system began in the mid-1930s and had been frequently modified and expanded in the following 60 years. There is no mystery about the reasons for

the recent changes, starting with the widely held view that the old system was a failure; that despite increases in economic prosperity during those 60 years, both the welfare rolls and the costs of the welfare programs had increased substantially, both reaching their highest levels in 1994. Public opinion polls showed general dissatisfaction with the welfare system, and even the recipients of welfare were unhappy with the system. Many of the underlying causes of poverty persisted across generations of the welfare families; causes such as single-parent families with dependent children, out-of-wedlock births and limited income support or parental care from the fathers, and mothers who were chronically jobless. Various programs to provide training and employment, to promote marriage and birth control, and to increase child support from absent fathers, had been tried in fits and starts in the past, and yet the welfare rolls continued to grow.

During the period of 55 years from 1940 to 1995, the labor force participation rate of women, including mothers with young children, steadily increased across all income classes. This change in the composition of the labor force led more and more voters to accept, and eventually to demand, that the "welfare mothers" become employed and self-supporting or at least to become partially employed and partially self-supporting in return for the welfare assistance they were receiving. There was, of course, widespread recognition of many acceptable reasons why "welfare mothers" were not employed. They tended to have limited education and skills, were sometimes burdened with many young children, and sometimes suffered from health problems, including the less accepted problems of substance abuse. Nevertheless, requiring employment among the welfare recipients appeared more justified as other forms of public assistance became available, such as the Earned Income Tax Credit, Food Stamps, subsidized health care insurance, and subsidized child care that could reduce some of the time constraints of working mothers. This shift in public opinion, combined with the growth in the welfare rolls and in the costs of welfare, were major reasons for the passage of a "tougher" welfare reform law, like PRWORA.

A second ascendant idea was that individual States should have greater flexibility to establish their own welfare program in ways suitable to the State's political preferences and economic conditions. Also, there was, and is, much uncertainty and controversy about what types of programs might be successful in promoting more self-support. Allowing States to try different strategies and programs is to give evidence about what works and what fails in welfare policies.

Although the States were granted more independence under PRWORA than they had under the old welfare system, several principles in the new law were essentially required of the State programs. Income transfers to poor families with children, which used to be called AFDC benefits and have been renamed TANF(Temporary Assistance for Needy Families), were no longer to be an entitlement — hence, the term "temporary" in TANF. Although all States would have programs that provided cash payments to their welfare families in residence, the States were encouraged to require reciprocal behavior by the recipients, most importantly a willingness to become employed. Becoming employed, in turn, would take them off welfare because almost any full-time job would raise the family's income above the level of eligibility for welfare benefits. The programs were to make employment the first option and virtually a requirement for welfare participants.

Another mandated requirement of each State was a five-year limit, over the welfare recipient's lifetime, for receiving transfer payments, although PRWORA allowed up to 20 percent of the cases to be exempt from this limit if there were acceptable reasons why employment was not feasible. Somewhat offsetting the leniency of the 20 percent exemption, PRWORA permitted the States to impose shorter time limits, and 30 States did so. Some State limits on receiving benefits were as short as two years. Provisions in PRWORA also gave the States financial incentives to increase the employment of their welfare clients, to promote marriages, and to adopt programs that reduced out-of-wedlock births and teen pregnancy.

Another part of PRWORA was aimed at limiting the rights of non-citizens to obtain welfare benefits. Legal immigrants cannot become citizens immediately, and illegal immigrants are, of course, not eligible for citizenship. The large inflow of immigrants from Central America, especially Mexico, has already been discussed as an important source of the poverty population in the U.S., and there was a growing public resentment, perhaps unjustified, that immigrants added substantially to the growing welfare population.

States were permitted to impose "sanctions" on families that did not cooperate with the programs requiring work or preparation for work. The sanctions were usually in the form of reduced income support payments, even allowing "full family" sanctions that eliminated the entire income support that the State's program allowed. Although the sanctioned families usually were eligible for Food Stamps or Medicaid benefits, the expenditures for both of these programs declined, either because the PRWORA

programs were successful in lifting the incomes of its welfare families above the levels for eligibility or because the new ethos of "work first" may have intimidated the families from seeking assistance from these other welfare sources.

Because States that reduced their welfare rolls were rewarded by an incentive system that was included in the PRWORA law, an interesting policy that almost all States have adopted to reduce their TANF rolls is "diversion." There are several types of the diversion policy. One is for the State agency to give a lump sum payment to a family head to permit her to overcome a temporary financial crisis (for example, debts that prevent the worker from being eligible to take a job) or to meet an immediate need (for example, car repairs needed to take a job). In return, one option was simply that the recipient pay back the loan. Another option for repaying the loan is an understanding by the recipient that she is ineligible for TANF benefits for the length of time that the loan would equal TANF payments. In the time period that the recipient has, she might be expected to undertake job search. Finally, a non-monetary diversion is an agreement that the applicant stays off TANF in exchange for the State agency helping her get assistance from other State agencies (legal help, for example) or Food Stamps. All these cases provide potential "diversions" from TANF. Time will tell whether these apparently short-term policies will have long-run benefits that will, in fact, divert these low-income families from becoming part of the welfare population.

(B) A Summary of the impact of PRWORA on welfare

In 1975 the average monthly enrollment in the AFDC welfare program was 3.4 million families. This number rose steadily to its historic high of 5.0 million in 1994. In 1996, when PRWORA became the new welfare law, the number had declined to 4.5 million, probably as a result of a combination of improvements in the economy in 1995 and 1996 and the beginning of the various experimental methods used by States to decrease participation in AFDC. Three years later, in 1999, the TANF rolls were down to 2.7 million, just over half (54 percent) of the 1994 amount. The decline has continued since then, but at a slower pace. The number of families on the TANF rolls in 2002 is 2.1 million. The percent of all children on the AFDC/TANF rolls declined from a high of 14.3 percent in 1993 to 5.3 percent in 2002 (US Congress, 2004, Table 7-6, pp.7~31).

Merely showing declines in the numbers or percentages of welfare recipients does

not, of course, demonstrate that welfare reform has been successful. If that were the only criterion of success, then we could achieve complete success simply by eliminating all welfare programs. An evaluation of success has to address the question of whether the lives of people, most specifically the low-income population, are better or worse as a result of the reforms, along with a consideration of how much better off are those in the non-poor population. This question, which has no easy answer, will be addressed in the next section, where the welfare reform program in the State of Wisconsin is discussed.

3. The State of Wisconsin's welfare program: Wisconsin Works(W-2)

(A) Background

When the national welfare program, Aid to Families with Dependent Children (AFDC), ended in 1996 and was replaced by PRWORA, the State of Wisconsin had already begun the essential reforms of its State-level AFDC program, which was to become W-2(Wisconsin Works), a program that would satisfy the requirements established in PRWORA. Most importantly, Wisconsin had already ended an "entitlement" to income support for poor families by a State law passed in 1994, and the State had received permission from the Department of Health and Human Services, the Federal government's agency in charge of welfare policies, to conduct various State-wide experimental programs to implement a "work-first" plan for the adults in its AFDC population. The Governor of the State, Tommy Thompson, vowed to "change the culture" of the existing AFDC program in the State to accommodate a strategy of "work, not welfare." The name, W-2 or "Wisconsin Works," played on the two meanings of the word, "works" — "is successful" and "employment in a job."

(B) The emphasis of W-2 on self-support by employment

The W-2 program required market work by the adults, mostly single-parent women in low-income families, who applied for income assistance. The program also was established to help the adults obtain jobs and to provide monetary and non-monetary support for those who cooperated with the work program. Three procedures were adopted to shift the emphasis of the welfare system from income support to

self-support by working.

The main procedure was to enroll the adult applicants for welfare assistance, who were almost all mothers of dependent children, into a "job development" system, the goal of which was to place the applicant in "regular employment" — that is, a job in the private market or a public job in existing government agencies. The job development system, described in more detail in subsection (C) below, included several types of assistance: mainly help in job search, subsidies for child care for the working mother, and subsidies for transportation to the job site. If the welfare mother was unable to obtain a regular job, she would be required to take an alternative temporary job, called Community Service Jobs(CSJ), that paid \$673 per month, which was less than the legal minimum wage.^{주10)} These jobs were intended to prepare the applicant for regular employment, and the women had an incentive to find and accept a regular job because the CSJs paid below-market wages.

The second procedure used in W-2 to establish its mandatory work requirement was to shift the few applicant mothers who were incapable of being employed, usually because of physical or mental impairments, out of W-2 and into the Supplemental Security Income(SSI) program, the welfare program for aged and disabled persons who were not eligible for the more generous Social Security programs. The proportion of the new applicants or of women on the existing welfare rolls who were shifted was not large, but this option was necessary to maintain the "work first" focus of W-2.

The third procedure was to find alternative homes for the children of some of the applicant mothers and allow "child-only" income support from TANF, usually \$215 per month per child, to go to the adult in the alternate home. The alternate home might be a relative's home, such as the child's grandmother, or the home of a "caretaker" family or a "foster-parent" who was unrelated to the child.^{주11)} Without

주10) The CSJ job required 30 hours per week plus up to an additional 10 hours of training. If the required time for the \$673 monthly payment was evaluated for 30 hours per week, the wage would be \$5.18 per hour; if the maximum hour-requirement includes 10 hours of weekly training, then the wage would be \$3.89 per hour.

주11) The National Association of Foster Parents reports the following information: Foster care is the temporary placement of children and youth with families outside of their own home due to child abuse or neglect. Foster parents provide care and nurturing for the duration of the child's stay in foster care. They attend training and work closely with the agency that supervises their home. Medicaid covers the cost of medical, dental and counseling services for children and youth in care. Foster parents also receive a monthly reimbursement that helps cover the cost of food, clothing and

the presence of children in her home, the applicant-mother would have no claim to TANF support. About one-third of the decline in welfare families is attributable to the shift to "child only" cases, although this statistic is difficult to calculate.

(C) The Job Development Program.

Job development is the major component of the W-2 program. Several types of agencies, public and private, were contracted by the State to administer the job development program. Private agencies were both for-profit companies and non-profit organizations. The motivation was to allow competition and innovation among the agencies, which would produce "best practices" and allow market incentives to improve performance. As stated in a report on the W-2 program by the Urban Institute: "W-2 activities attempt to mirror the work world. Cash grants are not based on family size and can be reduced by the minimum hourly wage for every hour a participant does not attend an activity."¹²⁾

The job development system, itself, consisted of four alternative programs, described by the W-2 agency as follows.¹³⁾

1) Unsubsidized Employment: Individuals applying for W-2 are first guided to the best available job opportunity. The W-2 agency supports the participant's efforts to secure employment through job search assistance. Once employed, participants may receive additional W-2 services to help them adjust to their new work environment and build skills that promote career advancement opportunities.

2) Trial Jobs(Subsidized Employment): Individuals who have the basic skills, but lack sufficient work experience to meet employer requirements, may be placed in a Trial Job. Through a Trial Job contract, the employer agrees to provide the participant with on-the-job work experience and training in exchange for a wage subsidy. Trial Jobs are expected to result in permanent employment. The employer must pay the participant a wage comparable to regular employees in similarly classified positions.

3) Community Service Jobs: CSJs are developed for individuals who lack the basic skills and work habits needed in a regular job environment. CSJ positions offer real

other basic needs of the children. Source: <http://www.nfpainc.org>.

¹²⁾ Urban Institute, "Recent Changes in Wisconsin: Welfare and Work, Child Care, and Child Welfare Services." <http://www.urban.org/publications/210223.html>

¹³⁾ <http://www.dwd.state.wi.us/dws/w2/default.htm>

work training opportunities, but with the added supervision and support needed to help the participant succeed. CSJ participants receive a monthly grant of \$673 for up to 30 hours per week in work training activities and up to 10 hours a week in education or training. Individuals who are employed part-time but have personal barriers that prevent them from increasing their work hours, may be placed in a part-time CSJ position with prorated benefits. Under certain circumstances, CSJ participants may be eligible to meet their participation requirements through a combination of 25 hours of work training activities and up to 15 hours of class time in a technical college program.

4) W-2 Transition(W-2 T): W-2 T is reserved for those individuals who, because of severe barriers, are unable to perform independent, self-sustaining work. W-2 T participants receive a monthly grant of \$628 for up to 28 hours per week of participation in work training or other employment activities; and up to 12 hours per week in education and training.

Placements in one of the above four job programs in W-2 are available only to eligible custodial parents, almost all(over 90 percent) women. Three groups of women — non-custodial parents, mothers who are under 18 years of age, and pregnant women — are not required to obtain a job, but may be eligible for an array of case management services, such as dealing with housing problems, debt management, and other assistance services. In addition, a custodial parent of an infant 12 weeks old or younger may be eligible for a \$673 W-2 cash benefit, which is the same amount as the monthly payment for working at a Community Service Job. The fact that mothers with children as young as 13 weeks are required to work is an indication of the emphasis that the W-2 program places on self-support by working. Two of the above four programs, Unsubsidized Jobs and Community Service Jobs, account for almost all of the participants in W-2.

Wisconsin adopted the national PRWORA requirement that eligibility for income support in its W-2 program was limited to five years within the participant's lifetime. W-2 also limited eligibility for participation in its three programs for subsidized employment — CSJ, Trial Jobs, and W-2 Transition Jobs — to a maximum of 24 months. Since the fourth program, unsubsidized employment, would in almost all cases take the client out of welfare, the W-2 welfare system had, in effect, a two-year maximum duration.

Most of the efforts of the administrators of W-2 was devoted to placing their clients in regular market jobs. This included helping individuals receive other available income and job assistance, such as the State and federal Earned Income Tax Credit (EITC), Food Stamps, Medicaid or an alternative state-subsidized health insurance program, subsidized child care during the mother's working hours, assistance for transportation to work or training programs, and Job Access Loans for such work-related expenses as repairs on a car needed for transportation to a job.

For mothers who became employed, the EITC program provides the largest subsidy. For example, assume the Wisconsin worker earns the minimum wage of \$5.15 per hour. This would yield \$10,712 annually, assuming a 40-hour work-week for 52 weeks. For the year of 2004, the additional federal EITC transfer payment would be \$2,604 if there is one qualifying child(defined as a child living with the mother for six or more months) and \$4,285 if there are two or more qualifying children.¹⁴ The Wisconsin state EITC payment would be an additional \$104(4% of the federal EITC) for a household with one child, \$600(14% of the federal EITC) for a household with two children and \$1,843(43% of the federal EITC) for a household with 3 or more children. Thus, Wisconsin mothers earning the minimum wage would receive a total of \$13,420 if they had one child, \$15,597 if they had two children and \$16,840 if they had three or more children. The poverty line in 2004 was \$15,219 for a mother with two children and \$19,223 for a mother with three children.

(D) A Summary of the impact of W-2 on welfare in Wisconsin.

Welfare rolls in Wisconsin, like those in the nation overall, reached their highest levels in 1994, which is the year Wisconsin began experimenting with a "work first" emphasis for the then-existing AFDC program. At the time of this transition to the new program, the economy of the State, like the economy of the entire nation, was emerging from the recession in 1992-3 to a period of low unemployment and rising wages that continued for the next nine years. The number of Wisconsin families participating in AFDC in 1994 was 77,000. Over the next six years the number of Wisconsin's welfare families declined steadily to a low of 17,000 families — a remarkable decline of 78 percent. The number of TANF families in 2002 was 19,000, which is 75 percent less than the number of AFDC families 1994(US Congress,

¹⁴ See Table III-1.

2004, Table 7-7, pp.7~34). The average monthly benefit for AFDC/TANF families over this period declined slightly, from \$463 in 1994 to \$446 in 2002(in constant dollars), which to some extent reflected the change from the earlier larger AFDC payments for larger sized families to the later fixed TANF payment for a family regardless of its size. Also, family support payments for the "child only" cases are not included in the TANF payments that began in 1996, when they were \$433 per month(US Congress, 2004, Table 7-9, pp.7~37).

Like the welfare reform program in the United States, Wisconsin's W-2 program was highly successful in reducing the number of families "on welfare." It is safe to say that both programs are widely claimed to be successful and have the political support of a large majority of voters. However, we do not know much about how the new programs have affected the well-being of the low-income families that have been in the programs, or the well-being of families that would have gone on welfare if the system had not changed in ways that limited their access to the program. Interesting discussions of these questions are found in a book by DeParle(2004), which focused on Wisconsin's W-2 welfare program, and in a review of this book by Jencks(2005). The two scholars acknowledge the largely failed results of the old welfare system, but they also point to the continued struggles of the "welfare moms" in the new welfare programs and the unknown future for their children in the new system.

IV. Welfare-to-work policies in the UK

1. In-work benefits in the UK

Welfare policy toward low-income families in the UK experienced a significant shift toward "in-work" benefits in the late 1980s and 1990s, and the UK now stands, along with the US, at the forefront of the use of in-work benefits.

Although a form of in-work benefit existed in the UK since the late 1970s, the shift in policy began in earnest with the introduction in 1988 of the Family Credit, a minimum-working-hours-based credit for families with children. After a number of reforms during the early 1990s, Family Credit was replaced by the Working Families Tax Credit in 1999, which in turn was replaced in 2003 by the Working Tax Credit as a part of policies to integrate taxes and benefits. Over this period the generosity of these "in-work" benefit schemes also increased, enhancing the emphasis that has been placed in welfare reform in the UK on supplementing low incomes in work for adults with dependent children.

In-work benefit reform in the UK has been motivated as a method of poverty relief that does not create work disincentives. This is achieved by targeting low-income families with an income supplement that is contingent on work. Typically eligibility is based on family income and requires the presence of children, reflecting in part the higher welfare benefits for families with children, partly a desire to help low income working families and partly the costs of childcare. Consequently these benefits are most heavily targeted toward single parents and low-income couples with children.

(A) Family Income Supplement(FIS) and Family Credit(FC)

The UK's long history of in-work benefits began with the Family Income Supplement (FIS) in 1971. This was a non-contributory benefit payable to low-income families with children, provided the head of the family was in full-time paid work(defined as 30 hours per week, or 24 hours if the recipient was a single parent). Entitlement depended on the family's income being below a certain limit. The amount payable was half the difference between the family's income and the relevant limit. The limits in 1983 were £85.50 per week for a one-child family with £9.50 for each subsequent child with a maximum payment of £22 per week. In addition, the entitlement to FIS automatically conferred a number of 'passport' benefits available to those on supplementary benefit — the income assistance program for those not in full-time work, including free school milk and meals, free pharmaceutical prescriptions and dental treatment.¹⁵⁾

FIS was intended to address the fact that low-wage families could be better off out of work than in work(a situation described as the "unemployment trap"). However, there were problems associated with FIS, the main ones being a low take-up and the "poverty trap" — a term which describes a situation where combined tax and benefit rules mean that an increase in earnings can result in little increase or even a reduction in net income.

Although FIS clearly provided some financial incentives to work, the combined effect of the 50% FIS benefit reduction rate together with the impact on housing benefits, taxes and national insurance contributions often resulted in implicit tax rates in excess of 100%. For example, under the FIS system an eligible worker with housing costs would pay a 25% basic tax rate, plus a national insurance contribution of 7%, a 50% benefit reduction rate on FIS and an effective Housing Benefit reduction rate of 23%, all of which sum up to an implicit tax rate of 105%. Partly reflecting this problem of high implicit tax rates, FIS was only taken up by around half of those entitled to it.

In the mid 1980s the social security system was reviewed by the then Secretary of State Norman Fowler. The 1985 Green Paper which resulted originally proposed that the new Family Credit should operate as a tax credit, either offsetting one's tax obligation or being paid through the worker's pay packet, just as the later WFTC was. However, this was vigorously opposed, partly because it would involve a

¹⁵⁾ For details, see Dilnot, Kay and Morris(1984).

transfer of resources from women to men(or "purse to wallet", as this was termed), and partly because of the burdens on employers. In the event, elements of the 1985/6 Social Security Bill were defeated in the House of Lords and the then Government announced that the Family Credit would be paid directly to recipients(DHSS, 1985).

The 1985 Green Paper set out several objectives for the new Family Credit. The main ones were:

- providing extra support for low-income families
- ensuring that they were better off in work(i.e., addressing the unemployment trap)
- ensuring that they could achieve improvements in family income without losing all the benefit because of high marginal tax rates.(i.e., addressing the poverty trap).

Family credit was introduced in 1988, replacing FIS. Family credit served as the main UK in-work benefit until it was replaced by the WFTC in 1999. Family Credit was an extension of FIS and was designed to increase generosity and remove tax rates in excess of 100%. It achieved the latter objective by fully integrating the in-work benefit with the rest of the tax and benefit system, i.e., by determining the amount of benefits on the basis of income after tax and benefits from other programs.¹⁶⁾

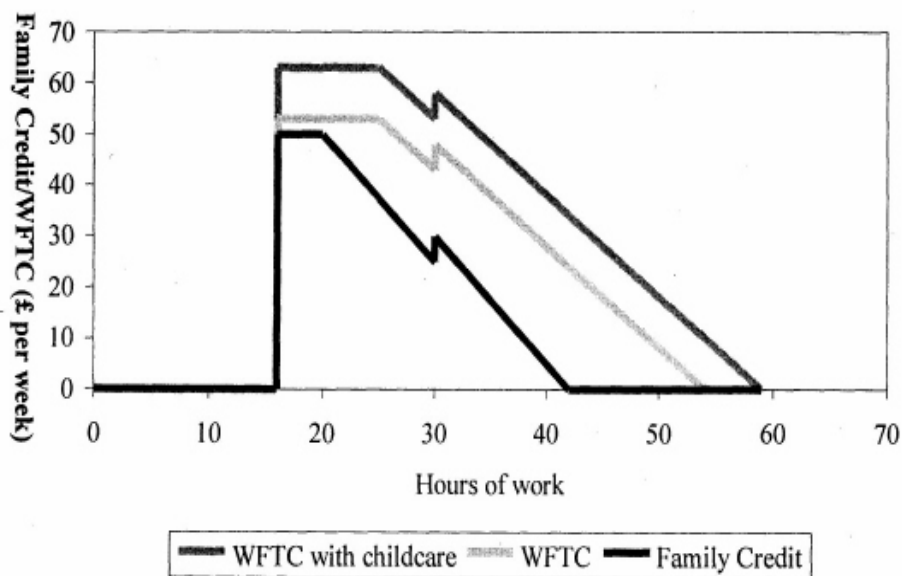
A family with children needs to have at least one adult working 16 hours or more per week to qualify for FC. The minimum weekly hours eligibility criterion was an unusual feature of the Family Credit system, retained from the FIS. At its introduction this was set at 24 hours but then reduced to 16 in April 1992 to encourage part-time work by lone parents with young children. In contrast, as mentioned above, FIS had a minimum hours criteria set at 30 hours for workers in couples and 24 hours for single parents. To partially offset any adverse effects for full time work from these lower hours eligibility levels, a further supplementary credit at 30 hours per week was introduced in April 1995.

Each family is potentially eligible for the specified maximum amount, which increases with the number and age of children in the household, and also for a small addition if they work full-time. This maximum amount is payable if the family's net income

¹⁶⁾ Before the change, supplementary benefit was based on net income, while Housing Benefits and FIS were based on gross income.

(after income tax and National Insurance contributions), normally over a six-week period, is lower than a threshold amount (£79 per week in 1998-99). Net income in excess of this threshold reduces entitlement to FC from the maximum by 70% (i.e., 70p for every £1 of excess income). Family credit is payable on a six-monthly flat rate, regardless of changes in the claimant's circumstances, in order to minimize administrative and compliance costs. It is paid to mothers even when the eligibility is in respect of the father's earnings. Family Credit was not paid and administered by a tax agency through the income tax system, but by the Benefits Agency through the social security system. The basic structures of FC and WFTC (to be discussed later) are shown in Figure IV-1.

Figure IV-1. Family Credit and WFTC



For many families, especially lone parents, the cost of childcare is a major obstacle to work. The Conservative government attempted to address this problem by introducing a childcare disregard in the Family Credit in October 1994. This covered

spending on children under 11(raised to 12 in 1998) with registered childcare providers and certain schools and establishments that are exempt from registration. The FC allowed a childcare cost of up to £60(raised to £100 in 1998 for a family with two or more children) to be disregarded from the family's income when the calculation of the entitlement is made. But the disregard was a failure: it was taken up by only 32,000 families, just 20 per cent of the number originally expected (Department of Social Security, 1997b). Moreover, it was of no help to the poorest families with earnings below the withdrawal threshold(£79 a week). They gained nothing from the disregard, since the disregard could not increase the maximum amount of Family Credit. Only those earning over £139 a week could gain the maximum support.^{주17)}

Unlike the EITC of the US, Family Credit was treated as income in calculating other benefits. This has the effect of dampening down the incentives in the underlying in-work benefit system. The impact of Housing Benefits(Rent Rebate) is particularly notable, since in the UK once family income falls below a specific level, all rental payments are covered through the benefit system.

Take-up of FC after its introduction in 1988 was low but it continued to rise. In 1997, 69 percent of eligible individuals took up 82 percent of the potential expenditures(Department of Social Security, 1997a). Around 45% of these families were headed by a lone parent. Expenditure on Family Credit rose from £626 million in 1991-92 to around £2.35 billion in 1997-98.^{주18)} The average payment at the end of 1996 was £57 per week.

(B) Labor market challenges in 1990s

Before discussing the WFTC introduced in 1999 to replace FC, it is useful to describe the British labor market situations in the 1990s and the unemployment and poverty traps which were present immediately before the introduction of the WFTC.

Although earnings for those in work continued to rise for two decades through mid-1990s, the gap between the high-paid and low-paid workers went up sharply during the same period. Moreover, there was evidence of many people cycling between unemployment and low-paid jobs. For many groups, income mobility was

^{주17)} The WFTC, introduced in 1999, replaced childcare disregard with the child care tax credit.

^{주18)} DHSS, various years.

low. Living on income well below the average for the population as a whole was increasingly a problem for people below pension age, mainly due to lack of work, and also due to low pay. Many of those who suffered most were families with children.

These problems reflected a range of factors including changes on the demand side of the labor market and the incentives faced by people in deciding whether to work. Although the tax and benefit systems were not the only factors influencing incentives, they played a role in a number of ways.

The 1990s also observed increasing polarization between working and non-working families. About 3.5 million households with at least one adult member of working age had no one in work — 18 per cent of all households compared to 9 per cent in 1979. Non-working women were increasingly partnered with workless men, whereas women with working partners, especially in families with young children, experienced rapidly rising employment rates. Five million adults and 2.7 million children lived in workless households, which accounted for a growing proportion of those in poverty. The proportion of children living in families without a full-time employee rose from 16 per cent in 1970 to 33 percent in 1995.

Also, whereas the majority of FC recipients in 1988 conformed to the "traditional" family model with the father working and the mother staying at home, this was no longer the case. Around half of FC recipients were lone parents, and a further 10 per cent were couples where the mother was the main earner.

The unemployment trap occurs where net income after tax and in-work benefits is little or no better than income out of work. Low returns from working reflect partly the low level of wages that some people are able to obtain. But for some, particularly those with large families, the financial gains from working can be small even at moderate earnings. The tax and benefit system plays a key role here.

In the UK, those out of work can claim Jobseeker's Allowance(JSA) or income support(IS), subject to satisfying certain eligibility conditions. Contributory JSA is paid at a flat rate for up to six months to those with sufficient contributions. Income-related JSA can be paid indefinitely depending on the other sources of income of the claimant and his family(i.e., partner/spouse and dependant children). Claimants must be available for, and actively seeking, work. Benefits can be abated if these conditions are not met. For those who leave work voluntarily, benefits can

also be reduced for a certain period.

Income support is income-related and can be claimed by certain categories of people who are not required to be available for work, including lone parents, carers, the sick and disabled, and some people over 50. The unemployment trap in the UK in around 1998, immediately before the introduction of the WFTC, can be described as follows:

<Unemployment trap in the UK in 1998>

The amount of JSA and IS paid is the difference between the sum required to meet the needs of the claimant's family("applicable amounts") and their net income(including Child Benefit and income from savings). These rates are the same for JSA and IS and vary with family circumstances. For example, a couple with two children could receive up to about £120 a week.

Recipients of JSA/IS could also automatically claim:

- full payment of their major housing costs, subject to limits: Housing Benefits (HB) to cover rent or additional IS to cover mortgage interest payments, plus Council Tax Benefit(CTB) to meet council tax;
- other "passport" benefits, such as free school meals and welfare milk and exemption from prescription and other health charges.

When claimants start working, a small amount of earnings is to be disregarded when calculating entitlement to JSA/IS - £5 a week for a single person, £10 a week for a couple and £15 a week for a lone parent. Beyond that, benefit is reduced £ for £ as earnings of the claimant(or his spouse/partner) increase, i.e. they face 100 per cent withdrawal rate.

Once the claimant works for 16 hours a week(or his partner works for 24 hours) all remaining entitlement to JSA/IS is lost irrespective of the family's income. They also lose entitlement to benefit for mortgage interest. Amounts of HB and CTB will also start to be reduced as soon as the family's net income exceeds a threshold.

For those without children there is no replacement benefit for JSA/IS, and they also lose entitlement to most passported benefits. Those with children can switch to claiming Family Credit(FC) if they work for 16 hours a week. The amounts of FC vary with the number and ages of children — the maximum for a two child family is over £70 a week. The rates are set so that generally families will receive more in FC plus earnings from working than they would have received from working less than 16 hours. But the difference can be small, and may not compensate for travel or other costs associated with working, or in the case of owner-occupiers for the loss of benefit to cover mortgage interest. The earnings levels that need to be achieved to be markedly better-off in work depend on various factors. For example, a two-child couple would need to earn over £300 a week to be £30 a week better-off in work if it had work-related costs of £40 a week. On the other hand, a single person with no work-related costs would only need to earn £150 a week to be £30 better-off(HM Treasury, 1998a, pp. 30-31).

The poverty trap arises when people in work cannot improve their net income significantly by increasing their pay, because this is largely offset by income tax and by reduction of in-work benefit. The poverty trap in the UK in around 1998 can be described as follows:

<Poverty trap in the UK in 1998>

For those with sufficient income or hours to take them off JSA/IS, the return from further increases in earnings can be reduced by national insurance contributions (NICs), income tax and the withdrawal of FC, HB, and CTB:

- NICs become payable as soon as each individual's earnings reach £64 a week, after which employees pay a flat rate "entry fee" of £1.28 a week plus 10 per cent of their earnings in excess of £64

- Income tax becomes payable at about £80 a week for a single person (or spouse) and about £100 a week for a lone parent or married person, after which a rate of 20 per cent is paid up to almost £160 a week and 23 per cent beyond that;

- The "maximum" amount of FC is payable to families working 16 hours a week whose income does not exceed the threshold; though there is an additional premium of £10.80 a week for those working 30 hours a week or more. Credit starts being withdrawn once the family's income exceeds £79 a week, beyond which it is reduced at a rate of 70 per cent of the increase in income after income tax and NICs. Payments of up to £60 (£100 for a family with two or more children) a week for registered childcare can be offset against income in calculating the size of entitlement. Family credit is also assessed for a 26-week period, so any increase in earnings within that period does not lead to an immediate loss of benefit;

Rent and council tax can be claimed in full, subject to limits, under HB and CTB by those with incomes up to the JSA/IS rates. Beyond this, payments are reduced at a rate of 65 per cent of the increase in the family's income after income tax, NICs and FC in the case of HB, and at a rate of 20 per cent in the case of CTB. Small amounts of earnings and the additional FC premium for those working over 30 hours a week can be disregarded when calculating entitlement. Payments are in principle reassessed as soon as income or other circumstances change (HM Treasury, 1998a, p. 33).

(C) Introduction of the Working Family Tax Credit

In May 1997, the Chancellor, Gordon Brown, set up a task force under Martin Taylor, the chief executive of Barclays. The terms of reference as set out in the Labour Manifesto were to "examine the interaction of the tax and benefit system so that they can be streamlined and modernized, so as to fulfill our objectives of promoting work incentives, reducing poverty and welfare dependency and strengthening community and family life."(Labour Party, 1997) The task force was, in particular, asked at an early stage to look at the advantages of introducing a tax credit drawing upon the American experience of the Earned Income Tax Credit.

In his report, Taylor said:

I also believe it is important that the design of the tax credit should build on existing features of the UK tax and benefit systems, and should not simply attempt to replicate the very different structures on which the EITC is based. In particular the EITC is designed around the fact that the unit of assessment for income tax in the US is generally the couple and not the individual as in the UK. Building on the existing system should also allow the most rapid and least disruptive introduction for the tax credit. I considered at some length the case for a tax credit assessed on individual income, which would be aligned closely with other parts of the tax system, but concluded that there was a strong case for the credit to be targeted on low-income households rather than low-earning individuals. I believe a credit based on the existing tax system but modeled on Family Credit. I recommend that Family Credit should be replaced with a tax credit. To facilitate its introduction, the tax credit should, in the first instance, be modeled on Family Credit(Taylor, 1998, p.8, p.23, p.24)

The report also made it clear that "a number of design issues would have to be considered". These included:

- payment to the mother or father according to the choice of the couple
- mechanisms to avoid abolishing individual tax assessment
- reducing the burden on employers, possibly by the Inland Revenue calculating entitlement.

In his Pre-Budget Statement to the House in November 1997, Mr. Brown announced that a new tax credit for working families would be one element of the Government's welfare to work strategy. Further details were given in a Treasury paper on reforming tax and benefits published at the time. This stated that the WFTC had a number of advantages in principle:

- As a tax credit rather than a welfare benefit, it would reduce the stigma associated with claiming in-work support;
- It would prove more acceptable than social security benefits to most claimants and taxpayers as a whole;
- Paid through the wage packet, it would reinforce the distinction between the rewards of work and remaining on welfare;
- It could help lower marginal tax and benefit withdrawal rates(HM Treasury, 1998a).

The design of the WFTC had been informed by the period of consultation. The EITC in the United States and the Working Income Supplement(WIS) in Canada had provided important lessons for the design of the WFTC. For example, the government was concerned to avoid the delays in payment, and unresponsiveness to changes in circumstances, inherent in these models and as a result the WFTC was designed to reflect British circumstances, building on the successful elements of FC. In particular, the government claimed:

Women in particular will benefit from the childcare tax credit. The WFTC will be payable through the wage packet. For around half the caseload, the main wage-earner will be the mother. For the other half, where the main earner is the father, there will be no compulsory transfer of resources from women to men. Couples will have the right to elect to whom the credit is paid, the man or the woman.

The WFTC will be assessed and paid over a six month period, on the basis of an initial assessment of household income. In this respect, it will be similar to FC which it replaces. It therefore poses no threat to the principle of independent taxation.¹⁹⁾

¹⁹⁾ An individual-based tax credit was considered but not adopted, since it "would be expensive and could produce some odd results. For example, partners of the rich and individuals with large investment

Another important priority will be to ensure that the WFTC gets to recipients quickly and efficiently: uncertainty about in-work support can be a big disincentive to returning to work. The design of the WFTC will aim to deliver the tax credit to individuals reliably and on time(HM Treasury, 1998b, p.7).

(D) Structure of the WFTC

The working families' tax credit was introduced in October 1999 as a replacement to family credit(FC) and was fully phased in by April 2000. It was available to families with children where any adult member was working 16 hours a week or more. The WFTC was the UK's main in-work benefit until it was replaced by Working Tax Credit in 2003. The structure of WFTC was modeled closely on the FC system, with the exception that WFTC was to be packaged as a refundable tax credit rather than as a welfare benefit. Among a range of stated aims, the government claimed that WFTC 'will improve work incentives, encouraging people without work to move into employment'(HM Treasury Press Release, 17 March 1998).

The amount of credit depended upon weekly earnings, hours worked(full-time or part-time), the number of qualifying children and savings(savings over £3,000 reduce the award; savings over £8,000 remove eligibility completely). Couples were assessed jointly.

There were two regions in the credit schedule. In 2000-01, for a lone parent with two children under 11, for example, the maximum credit was £104.35 a week. Beyond an after-tax income of £91.45 a week, the credit was tapered away at 55 per cent, with an extra credit of £11.25 for families where someone worked more than 30 hours a week. The credit was fully tapered away for a family with two children at a gross income of £385 a week.²⁰⁾

The WFTC was substantially more generous than its predecessor, FC. It increased the level of in-work support relative to the FC system in four ways: by enhancing the credit for younger children; by increasing the threshold; by reducing the benefit reduction rate from 70% to 55%; and by incorporating a newly introduced childcare credit of 70% of actual childcare costs up to a quite generous limit. The maximum

incomes, might be entitled to the credit if they themselves had a low-paid job."(HM Treasury, 1998b)

²⁰⁾ In 2000-01, the national minimum wage was set at £3.70 an hour and poverty line for a household consisting of a single parent and two children was £9,776 a year.

amount of childcare cost was set at £100 per week for those with one child and at £150 per week for those with two or more children. According to the government, these limits were chosen to reflect the average cost of childcare, while also providing a 'shopping incentive' to find good value. The maximum childcare support, therefore, amounted to £70 a week for a family with one child; £105 for a family with two or more children. Moreover, the maximum was available to the lowest paid, unlike with Family Credit.

The childcare credit component was available to all working lone parents and to couples where both partners work more than 16 hours per week. The requirement that both parents work helped to offset the possible negative incentive to work of the second worker in a couple implicit in the family based calculation of the level of the credit in the WFTC. See Table IV-1 for the parameters of the WFTC.

Table IV-1. Working Families' Tax Credit: Rates and Thresholds

		1999 ~ 2000	2000 ~ 2001	2001 ~ 2002	2002 ~ 2003
Basic tax credit	£ per week	52.30	53.15	59.00	62.50
30-hour tax credit	£ per week	11.05	11.25	11.45	11.65
Child tax credit					
Under 11	£ per week	19.85	25.60	26.00	26.45
11-16	£ per week	20.90	25.60	26.00	26.45
16-18	£ per week	25.95	26.35	26.75	27.20
Disabled child tax credit	£ per week	-	22.25	30.00	35.50
Enhanced disability tax credit					
Lone parent or couple	£ per week	-	-	16.00	16.25
Child	£ per week	-	-	41.05	46.75
Childcare tax credit					
Maximum cost allowed					
1 child	£ per week	100.00	100.00	135.00	135.00
2 or more children	£ per week	150.00	150.00	200.00	200.00
Percentage of allowed childcare costs in credit		70%	70%	70%	70%
Savings					
Amount disregard	£	3,000	3,000	3,000	3,000
per week income assumed per additional:	£	250	250	250	250
Upper limit	£	8,000	8,000	8,000	8,000
Reduction of award through income					
Income threshold	£ per week	90.00	91.45	92.90	94.50
Income taper rate		55%	55%	55%	55%
Minimum award	£ per week	0.50	0.50	0.50	0.50

(Source: Inland Revenue, 2003)

An example of calculation of the amount of WFTC payable in 2000-01 is shown in Table IV-2. Considered in this example is a lone parent with one child aged 13 who is disabled. The lone parent had a net income of £175 for work of more than 30 hours a week. He/She paid eligible childcare costs of £85 a week. As shown, the amount of WFTC is £125.80, which amounts to over 70% of his/her net earnings.

Table IV-2. Example of WFTC calculation, 2000 ~ 2001

Income net of tax and National Insurance contributions(1)	175.00
WFTC maximum amount	
Basic tax credit	53.15
Child tax credits (age 13)	25.60
Disabled child tax credit	22.25
30 hour tax credit	11.25
Childcare tax credit (70% of weekly cost of £85)	59.50
Total(2)	171.75
Less 55% of income in excess of threshold of £91.45(3) (£175 - £91.45 = £83.55, and 0.55 x £83.55 = £45.95)	45.95
WFTC payable(4 = 2 - 3)	125.80
Net Income + WFTC(5 = 1 + 4)	300.80
Child benefit(6)	17.55
Total Income(7 = 5 + 6)	318.35

(Source: <http://northernireland.asu.org.uk/NI%20Advisor/wftc230101.html>)

In November 2002, there were 1,376 thousand families receiving WFTC awards, up by 6.4% compared to a year earlier. The number of lone parents were 737.3 thousand(53.6 percent of recipients).

The average WFTC award was £86.78 a week, while the average gross weekly earnings of the main earner in the recipient families was £177. The numbers of couples and lone parents who received the 30-hour credit were 499.8 thousand(78.2 percent of recipient couples) and 301.6 thousand(40.9 percent of recipient lone parents), respectively. For 178 thousand recipient families(13 percent), their award included a childcare tax credit. The average value of the childcare tax credit for those benefiting was £41.25 per week.(Inland Revenue, 2002).

(E) Work incentives

The WFTC was designed to influence the work incentives of those with low potential returns in the labor market. It did this via the increased generosity of in-work means-tested benefits.

Introducing the WFTC, the government claimed:

The WFTC will improve work incentives for families by making work pay. The WFTC's structure reflects the priority the Government attaches to getting those who are out of work into work. The WFTC unambiguously improves the return from work. Moreover, by targeting the greatest increase in support on those earning in the range of £100 to £300 a week, the WFTC will support the sort of jobs those moving from unemployment and inactivity are most likely to take. The accompanying reforms to national insurance paid by employees and employers will reinforce this effect.

The WFTC's structure is also designed to make full-time work more attractive for those already in work, making it easier to move up the earnings ladder. The childcare tax credit, in particular, will help lone parents and two parents families to increase the hours they work. For example, a one-earner couple earning £130 a week (the average entry wage for someone moving from unemployment into work) with two children under 11 will gain £9.25 a week as a result of the change. A similar family on £200 a week(the average entry wage for a full-time job) will gain more than £23 a week(HM Treasury, 1998b, p.13).

It is well known, however, that a change in marginal tax rates has an ambiguous effect on the number of hours worked by those currently in work — the income and substitution effects of the change move in the opposite directions. It should also be noted that such changes have an ambiguous effect on the numbers participating in the labor market. This is because in-work benefits, although nominally paid to one member of a family, are assessed on the basis of household rather than individual income. For second earners in couples, an increase in the generosity of in-work benefits can therefore introduce an incentive to stop participating in the labor market.

Also, as Blundell and Hoynes(2001) argued, the work incentives of in-work benefits get weaker when the replacement rate of out-of-work benefits to in-work benefits is high and when in-work benefits are counted as income in the computation of out-of-work benefit programs. For example, in the UK the WFTC was counted as income in calculating out-of-work benefits, including Housing Benefit, and hence in these cases, the increase in the disposable income of a family could not be as large as the increase in the level of WFTC payment.

Blundell et al(2000) estimated that, assuming full take-up for the FC and other benefits and full take-up of the then newly introduced WFTC, replacement of WFTC for FC led the participation rate for single mothers to increase by 2.2 percentage points(from 39.8% to 42.0%), and the participation rate for married women with employed partners to decrease by 0.57 percentage points(from 67.6% to 67.0%).

Brewer and Gregg(2003) used a simple difference in difference methodology to report that, after taking into account of the strong employment recovery during mid 1990s in the UK, which slowed after 1999 and stopped entirely in 2001, and also adjusting for differences in age of the children of the lone parents, the annual changes in employment rates among live-alone lone parents for the periods of 1996-99 and 1999-2001 were 0.16 and 1.20 percentage points, respectively. This finding led them to conclude that "it tentatively appears that lone parents have had an exceptional increase in employment rates over this period, which could reflect a behavioral response to the financial incentives and other aspects of welfare reform since 1999. (p.103)"

More recently, Brewer et al(2005) estimated that the greater generosity of the WFTC has increased labor market participation of lone mothers by about 5.11 percentage points(2.36 percentage points to part-time work, and 2.75 percentage points to full-time work), slightly reduced labor supply of mothers in couples by 0.57

percentage points, and increased the labor supply of fathers in couples by 0.75 percentage points.

(F) Comparison of WFTC with EITC

A direct financial comparison between the WFTC and the EITC suggests that the UK system is substantially more generous. But this comparison can be misleading, because there are differences in what counts as income when in-work benefits are assessed in the US and the UK, and in whether in-work benefits are counted as income for other means-tested transfers. Both EITC and WFTC generally disregard other transfer payments (i.e. WFTC disregards, among others, attendance allowance, child benefit, education maintenance allowance, housing benefit, council tax benefit, maternity allowance and statutory maternity pay; EITC disregards food stamp and TANF payments). But the credits treat tax payments differently. EITC is based on gross income but WFTC is assessed on income after tax and National Insurance payments. Basing a means-tested award on net income ensures that marginal withdrawal rates never exceed 100%, but equally it means that the impact of tax cuts on tax credit recipients is dulled. It turns out that marginal withdrawal rates for EITC recipients are relatively low despite it being assessed on gross income, but this is because the rates of income tax and payroll tax, and the EITC phase-out rate are low in the US compared with in the UK.

Looking at the other direction of interactions, since 1991, EITC awards have not counted as income in other parts of the US tax and welfare system. States are prohibited from counting EITC awards in determining food stamps, Supplementary Security Income and Medicaid assessments. EITC awards did not count as income when assessing AFDC awards but, since 1997, states have been permitted to count EITC payments as income when assessing TANF payments. By contrast, WFTC awards do count as income in assessing housing benefits and council tax benefits awards. Hence, it is important to consider the entire budget when comparing the generosity of in-work benefits system or when calculating marginal and average withdrawal rates.

The structure and administrative details of the WFTC are also quite different from the EITC. First, whereas EITC is closely linked with the US income tax system and is therefore usually paid annually in arrears, with the credit assessed on the past year's income.²¹ WFTC does not work in the same way as the income tax system

in the UK. WFTC is a weekly award, assessed every 26 weeks on a snapshot of average weekly income. The assessment period is between seven weeks and four months, depending on the frequency of wage payments. The award is then paid as a fixed rate during the next 26 weeks, regardless of any changes in income or employment status, although some changes in family circumstances can trigger a reassessment of the award. Unlike means-tested benefits or income tax, there is no concept of being underpaid or overpaid during this 26-week period.

Brewer(2001) argues that there are three implications of these features. (i) The long gap between the assessment of in-work benefits will mean that marginal withdrawal rates calculated by a tax and benefit model will not apply to recipients in the very short run. (ii) There should be different behavioral and economic effects between receiving an in-work benefit annually and receiving it fortnightly or monthly where families are myopic or credit-constrained. (iii) In the UK, the difference between assessment and non-assessment periods introduces some short-run incentives to alter labor supply and manipulate earnings between periods.

Second, while the EITC applicants claim the credit when they file an annual tax return and they receive the award as a payable rebate of their annual income tax bill, WFTC payments are paid either fortnightly(for non-earning recipients in a couple) or with wage payments. This may reflect the greater importance of WFTC payments as a proportion of total income. In fact, WFTC can represent over 40 percent of total income for some low-income parents. WFTC, with frequent payments, provides a fixed income stream over 26 weeks and hence predictability of income payments, which is a key to manage on a low income. The desire to get money to claimants quickly - rather than waiting for the end of the tax year - is primarily motivated by two concerns. First, most taxpayers in the UK have their income tax correctly withheld by employers, and only the rich, the self-employed, and those with complex tax affairs file a tax return. Second, people entering work on low wages would be worse off in work without the WFTC, because of the relatively high level of out-of-work benefits compared to the US.

주21) The EITC allows an estimated tax credit to be distributed in the employee's weekly or monthly wage or salary payment, but only around 10% of EITC recipients have chosen this method of benefit payment.

(G) New tax credits

The new credits, child tax credit and working tax credit, were introduced in April 2003, replacing the WFTC. The eligibility for the working tax credit was extended to adults without children (with restrictions to full-time employment and a minimum age of 25).

They are, like the WFTC, administered and delivered by the Inland Revenue. This represents an important step towards tax and benefit integration, one of the Labour government's goals of the tax and benefit reforms. It recognizes the fact that the Inland Revenue already collect income information on three quarters of the integrated child credit caseload, over 3.5 million families.

The aim is that, with the reform, families who are also claiming Income Support and Jobseeker's Allowance will need to provide income and family details only once, through ONE, the new agency for people of working age, with the relevant information being transferred electronically to the Inland Revenue.

The child tax credit is designed to simplify the system of financial support for parents, and provides support that is means-tested against family income. The child tax credit effectively merges together several parts of the existing tax and benefit system that support families with children.

Separately, the working tax credit is designed to make work more financially attractive. It means that people (around 1 million single people and couples) with or without children in work and on a low income may receive extra help from the State. That is, the working tax credit supports adults with or without children in low-paid work, as well as providing subsidies for certain childcare expenditure for some working parents.

In introducing the working tax credit to replace the Working Family Tax Credit, extending the tax credit to those without children was a discretionary policy decision, and the stated aim was to reduce poverty and improve work incentives amongst those without children. This objective, however, has been criticized for the following reasons:

- Those without children who might be entitled to the working tax credit do not tend to be in poverty by the standard definitions (i.e. in households with an income below 60% of the national median)

- There is no evidence that individuals without children are deterred from working by inadequate financial incentives. This contrasts strongly with the research findings for those with children, which supported the introduction of the WFTC for families with children.

This suggests that the working tax credit may be aimed more at raising the income of those on low incomes in a way that does not create any disincentives to work.

The parameters of the Working Tax Credit for 2003-04 are shown in Table IV-3.

Table IV-3. Working Tax Credit: Rates and Thresholds, 2003 ~2004

	£ a year	Weekly equivalents, £
Basic Element	1,525.00	29.20
Couples and lone parent element	1,500.00	28.80
30 hour element	620.00	11.90
Disabled worker element	2,040.00	39.15
Enhanced disabled adult element	865.00	16.60
Childcare element		
- maximum eligible cost for 1 child	7,040.00	135.00
- maximum eligible cost for 2 or more children	10,430.00	200.00
- percent of eligible cost covered	70	
Income threshold	5,060.00	97.00
Withdrawal rate (per cent)	37	

(Source: Inland Revenue, 2003)

In 2003 ~2004, the working tax credit consisted of the following:

- Single people without children were entitled to a credit of £1,525 per year (approximately £29.20 a week).^{ㄹ22)}
- Couples with or without children and lone parents were entitled to a credit of

^{ㄹ22)} Brewer(2003) estimated that average entitlements to working tax credit for those without children would be less than £20 a week, with around 650,000 families entitled.

£3,025 per year(approximately £58.20 a week).

- There was a bonus of £620 per year(approximately £11.90 a week) for those working 30 or more hours a week.
- Families with children where all adults were working, caring or disabled could receive help with approved childcare costs. This operated in the same way as the child tax credit under the WFTC, paying 70% of approved childcare costs below a generous maximum(£135 a week for those with one child under 16, £200 for others).
- There were extra amounts for some adults with disabilities and for people over 50 returning to work.
- Families with children had to work 16 or more hours a week to be entitled, and those without children must work 30 or more hours a week(and therefore were always entitled to the bonus for working full-time).

Families with annual incomes below £5,060 were entitled to the full amount. Incomes above this level reduced entitlement at the rate of 37%, i.e., 37p in the pound. Entitlement was exhausted at an annual income of around £10,857 for a single person without children working full-time, £13,236 for a lone parent or a couple with children working part-time, and £14,911 for a lone parent or a couple with or without children working full-time.^{주23)} It was hence theoretically possible for a family with children spending the maximum allowed on childcare(£10,430 a year) to be entitled to the working tax credit at an annual income as high as £34,590.

Until 2003, the tax credits depended on income in the corresponding tax year. From 2004 onwards, most families apply for or renew an award in the summer, at which point an award is made based on the annual income in the previous tax year.

After the end of the tax year, though, the Inland Revenue recalculates awards based on people's actual income in the tax year. Families whose income has fallen and

^{주23)} The reduction in the working tax credit for a single person without children who earned £10,857 in 2003-04 is £2,145(= (£10,857-£5,060)x0.37). This amount is equivalent to his or her maximum working tax credit, which is the sum of the basic element(£1,525) and 30 hour element(£620). Similarly, for a lone parent or a couple with children working part-time who earned £13,236 and did not claim for the childcare element, the related calculation is (£13,236 - £5,060) x 0.37 = £3,025 = £1,525(basic element) + £1,500(couples and lone parent element).

therefore has become entitled to more tax credit receive the balance due to them. Families whose income has risen and that have been paid too much tax credit may have to pay some of the extra back, although the first £2,500 of income changes is disregarded when performing this calculation. These corrections are made either by adjusting future awards or by one-off payments.

This feature means that the tax credits are not based solely on a single year's income, as is the Earned Income Tax Credit in the US. There is a danger that this will cause uncertainty amongst families, as people cannot be sure that they will not have to pay back credit they are currently receiving. It also means that the amount of tax credit being received by families in a given month may bear little relationship to their circumstances in that month.²⁴⁾

The new tax credits confirm the Labour government's belief in targeted support assessed against joint family income. A practical disadvantage of means-tested benefits and income-related tax credits is that people have to apply for them, but not everyone does, either because they do not know they are eligible or because they decide not to apply, although those who do not claim benefits or tax credits tend to be entitled to small amounts. By contrast, income tax cuts affect income-tax-payers automatically, and most universal benefits are claimed by virtually all who are entitled. In fact, the WFTC take-up rate has been estimated at 62~65%, lower than that for family credit(72% in Summer 1999) and much lower than the estimated take-up rates for income support and housing benefits(over 95% in 1999~2000).

Finally, although precise figures are not known, the Labour government spent more money advertising the WTC and CTC to increase their awareness than it did on advertising the WFTC.

²⁴⁾ The government estimated that in 2004-05 and later years, 1 million families would be entitled to extra tax credit and a further 750,000 families would face the possibility of having to pay back credit to the Revenue because they experience a rise in income over £2,500(HM Treasury, 2002).

2. New Deal for Young People^{주25)}

(A) Introduction

New Deal is a major element of the Labour Government's Welfare to Work strategy. It comprises a family of welfare-to-work programs, each designed for a certain target group and gives unemployed people a chance to develop their potential, gain skills and experience, and find work. The New Deal for Young People and New Deal 25+ are for those aged 18 to 24 and 25 to 49, respectively. New Deal 50plus aims to help people aged 50 and over who are looking for or considering a return to work. In addition, the New Deal for Lone Parents and the New Deal for Partners offer assistance to lone parents in receipt of Income Support and to partners of Jobseeker's Allowance(JSA) claimants(and partners of certain other benefit recipients), respectively, to find work. The Government also hopes that it can provide employers with an opportunity to utilize the energies and talents of an important labour market resource. In this and in the following sections, two of the New Deal programs, the New Deal for Young People and the New Deal for Lone Parents, are discussed.

The New Deal for Young People was established as a national program in April 1998 and is targeted at 18- to 24-year-olds who generally have been unemployed for six or more months. In Britain, almost all young unemployed people over age 17 are entitled to a cash benefit, called Jobseeker's Allowance, even if they have never worked. Most will receive this benefit following a means test, but some will have acquired the right to the benefit on the basis of insurance contributions made while working. The New Deal for Young People encompasses recipients not just of means-tested, cash benefits but also of contributory, social insurance benefits. New Labour has therefore moved beyond traditional welfare and addressed groups that in many other countries would at least potentially be recipients of unemployment insurance payments.^{주26)}

Jobseeker's Allowance paid on the basis of social insurance contributions can be paid

^{주25)} This section draws on Stafford(2003).

^{주26)} The welfare-to-work model has also been applied in the UK to people claiming benefits on the grounds of incapacity for work who have traditionally been considered exempt from the expectation that they should obtain paid work.

for up to the first 26 weeks of a spell of unemployment, after which the individual is eligible for a means-tested Jobseeker's Allowance. Claimants of contribution-based Jobseeker's Allowance with a partner or children often claim means-tested Jobseeker's Allowance from the beginning of their spell of unemployment because their household circumstances often meet the requirements of the means test.

(B) Background

The New Deals form part of the New Labour government's modernization of the welfare state. The broad policy intent is to tackle poverty (especially childhood poverty) and social exclusion by helping people find paid work and assisting them to stay and progress in employment, to improve labor market efficiency, and to make the UK economy more internationally competitive (HM Treasury, 2000). There is also a desire to change the nature of the contract between the individual and the state, whereby the right of individuals to get support from the government when looking for work is balanced by the responsibility to seek training and work if they are able to do so (Blunkett, 2000).

As such, the New Deals, including NDYP, are products of a common policy paradigm comprising the following elements:

- a belief that paid work is the surest route out of poverty and social exclusion and the best means of securing independence (HM Treasury, 2000);
- an expectation that increasing the supply of labour will increase the pool of (skilled) labour available to employers which, in turn, will increase production and productivity (Blunkett 2000; HM Treasury, 2000);
- a presumption that movements into work can be assisted by:
 - i) delivering a proactive benefit system founded on a flexible, integrated, personalized (or caseworker) service backed by investment in information and communication technology; and
 - ii) providing enabling services and support that tackle people's barriers to work and improve their employability;
- a stress on the rights and responsibilities of individuals as well as those of the state (Blair, 1977; Blunkett 2000); and
- a commitment to government working in partnership with the voluntary and private

sectors to deliver benefit and employment services.

New Labour was elected in 1997 with a well-publicized manifesto commitment to move 250,000 young people from benefit into work. The New Deal for Young People is the mechanism by which this objective is mainly to be achieved; hence, as well as being a central element in the government's labor market policy, it has a high political and policy profile(HC, 2000).

The commitment to tackling unemployment among young people resulted from a number of interrelated economic, social, and ideological factors. Most important was concern about the adverse consequence of youth unemployment. The strong presumption was that unemployment among young people leads to benefit dependency, social exclusion, dysfunctional and anti-social behavior, low self-esteem, and even the emergency of an underclass. Paid work, on the other hand, was perceived as providing a route to independence and 'mainstream' society.

Such beliefs were formed against a backdrop of substantial change in the UK youth labor market(Hasluck, 1999). Youth unemployment rose following the 'oil crisis' of the 1970s and recessions in the 1980s, peaking in 1993 at 21.3% for males and 13.6% for females aged between 18 and 24(ONS, 2000). Since then, the trend has been downwards —unemployment had fallen to 13.5% and 10.3% for young men and young women, respectively, by the time the NDYP was introduced. Nevertheless, the risk of experiencing unemployment before the age of 25 has increased with successive cohorts of young men. Also, higher proportions of young people, men in particular, enter the labour market after a prolonged spell of unemployment.

In fact, policy makers fear that unemployed young people, who disproportionately lack qualifications and confront a labor market that places a growing premium on accreditation, are spending increasing lengths of time "on benefit" and thereby becoming more susceptible to the negative consequences of unemployment. This growing problem engendered political support for the NDYP, which was the first New Deal to be established nationwide(in April 1998). Nevertheless, its introduction still proved to be somewhat controversial because of its compulsory nature.

(C) Contents of the New Deal for Young People

The most obvious difference among various New Deals is, as stated before, the target

group. The NDYP targets a group traditionally required to seek employment; unemployed people aged 18 to 24 who are eligible to receive Jobseeker's Allowance. Young people are in general disadvantaged in the labor market due to lack of work experiences. Fifty five per cent have mainly been unemployed since leaving school and another 17% have mainly held casual or short-term jobs. While better educated than unemployed people in general, 21% have no qualifications and 12% admit to problems to literacy(Stafford, 2003).

The NDYP has a formal and linear structure. Under NDYP, the activity sequence begins with a four-month Gateway. The Gateway aims to get young people into work through providing intensive help with job search, and participants are assigned to a personal adviser, a caseworker who provides advice and support concerning job search, training opportunities, childcare services, and in-work taxes and benefits.^{주27)} Following the initial Gateway stage, clients are presented with a menu of set Options, which are generally perceived by staff as a hierarchy, with jobs and training or education being preferable to placements in the voluntary sector or on the environment task force. The latter two in particular can be used as a 'threat' when confronted by 'uncooperative' clients(Stafford et al., 2000). Formally, clients leave Jobseeker's Allowance at the Options stage, and participants returning to unemployment within 13 weeks of the Options stage enter the Follow Through stage, which is similar to the Gateway. Although some may re-enter the program, the intention is that this should not need to happen.

Each of the options generally lasts for up to six months and provides vocational training of at least a day a week, which leads to accreditation. Participation is mandatory; the sanction for refusal to participate is a time-limited withdrawal of Jobseeker's Allowance. Sanctions can be imposed for a variety of reasons and for different lengths of time. Young people face two sanction regimes depending upon their stage in the New Deal process. While in the Gateway they are subject to the same sanction regime as all Jobseeker's Allowance claimants. For example, if they fail to look for work or are a full-time student, their claim to benefit is terminated; if they refuse an offer of an unsubsidized job without good cause, their benefit can be suspended for up to 26 weeks; if they refuse to take up one of the Options(or

주27) The New Deal Personal Advisers have mainly been drawn from existing staff of either the Benefit Agency(the government agency responsible for paying benefits) or the Employment Service(the agency responsible for job placement and labour market programmes). Since 2002 these have been merged into a single body, called Jobcentre Plus.

any other government program of course), benefit is stopped for two weeks, or four weeks if previously sanctioned. At the Options stage, the sanctions regime changes. Failure to attend an Option, leaving early, or being dismissed without good cause can lead to an initial two-week benefit suspension that rises to four weeks, then to 26 weeks for subsequent breaches. The Personal Adviser does not impose benefit sanctions, rather the case is referred to an Adjudication Officer for a decision on whether a penalty should be imposed.

The NDYP aims to remove barriers to immediate employment, so that participants can move as quickly as possible into employment, and to enhance longer-term employability through provision of advice/support and training. It is clear, however, that the NDYP is not a model 'work first' program whereby clients are encouraged to take the first available job. Nor is it pure 'human capital development' initiatives, with the emphasis on improving the skills and knowledge of clients through training and education so as to increase employability and career prospects(Stafford, 2003).

In practice, the balance between work first and human capital development strategies appears to have changed over time, with the need for clients to obtain paid work increasingly being stressed. Because the early implementation of the New Deal for Young People was seen as too passive, an Intensive Gateway was piloted in 12 areas in August 1999 and rolled out nationally in June 2000(HM Treasury, 2000). This provides more help from personal advisers with job search and assistance in developing soft skills, including punctuality and team working. In addition, the last month of the four-month Gateway stage was made more intensive in July 1999. Participants are now told that remaining on benefit without activity is not an option, and they are prepared for the next stage of the program(Options).

The NDYP is of a compulsory nature. Participants in the NDYP must be available for work and demonstrate that they are actively seeking it. As recipients of Jobseeker's Allowance, they have to sign and follow an agreement that is repeatedly updated, specifying the activities they need to undertake in order to find work. Failure to follow the agreement provides prima facie evidence that the young person is not actively seeking work and grounds for the temporary removal of benefit. Around one in eight young people at the Options stage are sanctioned, with the proportion sanctioned varying by type of Option. During the last quarter of 2000, for example, the proportion sanctioned ranged from 28% for those on the Environmental Task Force to 6% for those in subsidized employment(TEN, 2001).²⁸

As for the delivery of services, the NDYP, like other New Deals, included a mix of delivery by public sector agencies (typically Employment Service), for-profit and not-for-profit sector organizations, or a mixture of both acting in consortia. Partnership arrangements had usually evolved and were increasingly characterized by core or strategic partners together with a group of operational partners or service providers (Hasluck, 2000).

For-profit and not-for-profit organizations were incorporated in the program with a view to introducing innovation in service delivery. Personal advisers were encouraged to exercise discretion in determining the help and assistance provided. On the one hand, clients can see this as positive when it addresses their expressed needs and improves their employability. On the other hand, any discretionary system can lead to a spatial inequity in the delivery of services, as clients with the same needs may be treated differently, with a risk that the quality of service provided becomes a lottery with prizes dependent upon where the client lives. The challenge, of course, is to provide a consistently high quality service while allowing staff the freedom to be innovative (Stafford, 2003).

Early evidence suggested that the performance of private sector-led schemes was relatively poor and that performance was generally higher in offices with small caseloads and those covering rural areas and small towns and lower in offices with a large number of clients or located in large urban areas (Hasluck, 2000). In contrast, subsequent analysis of the performance of local units found no significant difference in the performance of private sector providers compared with the public sector (NAO, 2002).

By giving young people 'no fifth option' — that is, of remaining on benefit and avoiding work experience and training — the government sought to ensure that those who would benefit from the scheme but who would not otherwise participate receive some help and assistance. Moreover, the judgment has been that public opinion will support the use of sanctions for young people, provided that the interests of any dependent children they may have are protected.

The government also recognized that past youth schemes had a poor reputation because the training and work experience provided could be of a very poor quality. It was, therefore, determined that young people on the program would receive high

주28) This also illustrates the hierarchy of Options.

quality service provisions. The compulsory nature of the NDYP is, therefore, legitimized by the provision of decent options (such as training, work experience, and subsidized employment) — thus ensuring that clients are not being required to participate in a process that might be ineffectual, stigmatizing, or demeaning.

Employers are key customers for New Deal programs. When the NDYP was first implemented, government expended considerable effort in marketing and signing up employers to demonstrate that placements would be available during the Options stage. A major national advertising campaign aimed at employers accompanied the introduction of the NDYP. Also, financial support is available to employers and non-for-profit organizations that offer placements to young people under the terms of the NDYP.

Employers have generally supported the NDYP (Hasluck, 2000), although their initial awareness and enthusiasm has waned over time and some have even become critical of it. Large employers do not always want to replace their existing training programs with those that meet the vocational qualification requirements of the NDYP, while small voluntary groups can find the program difficult to administer. A common criticism of the NDYP is that young people referred to employers were not always 'job ready'. The government has responded by piloting in inner city areas the use of private and voluntary sector intermediaries to improve the match between employers' needs and participants' basic skill levels.

(D) Outcomes

The NDYP has been subject to extensive research and evaluation, mainly funded by the government. For the NDYP, as a welfare-to-work policy, estimates are required of its specific effects on movements into employment over and above those that would have occurred in its absence — that is, estimates of its net impact (or additionality).

Of particular interest are movements into sustainable employment. Also, since compulsion is used in the NDYP, the effectiveness of sanctions in leading to behavioral changes and to sustained employment outcomes should also be assessed.

The NDYP was more generously resourced than any other New Deal programs, although the eligible population was probably the smallest. It had the budget of £2,620 million, 77% of the total New Deal budgets.

The NDYP caseload rose rapidly during the early months of the program, as the

large number of claimants who had already been unemployed for six months or more joined the program. Numbers peaked at 149,500 in July 1999 and thereafter fell slowly to 98,400 in November 2000, and to 72,790 in March 2005(DfEE, 2001: DWP, 2005).

The key outcome for government is a move into sustained unsubsidized employment. The government counts employment to be sustained if former participants do not return to Jobseeker's Allowance or another Option within 13 weeks, and by November 2000 the Labour government felt able to declare that they had achieved their pre-election pledge of getting 250,000 young people back to work.

By March 2005, the total number of starters and leavers of the NDYP reached 1,292,890 and 1,220,100, respectively, leaving 72,790 as current participants as of the end of March 2005. The proportion of female participants was around 29%. Of the current participants, those in the stage of the Gateway, Options, and Follow-Through were 48,070(66.0%), 13,470(18.5%), and 11,260(15.5%), respectively. Of those in the stage of Options, the Employment option accounted for 12.0%(1,610 cases)(DWP, 2005).

Of the leavers, 460,550(37.7%) were reported to be placed into unsubsidized employment. The remainders were transferred to a training program or became recipients of other benefits. About two thirds of the participants left the program during the Gateway stage. The immediate destinations of the leavers were different across the stages during which they left the NDYP. The proportions of those who moved into unsubsidized employments was over 40% among those leaving the program at the stage of either Gateway or Options, but among those leaving at the stage of Follow-Through, the proportion was only 27%, suggesting their relatively low employability.

These official figures do not provide a measure of the net impact of the program, however, because they do not take account of the number of young people that would have found employment had there been no NDYP. Evaluations that have attempted such estimates use one of two analytical approaches. The first consists of comparing actual numbers against the predicted numbers obtained by using econometric techniques. The second approach to get the net impact of programs also relies on an econometric technique, called the difference-in-difference approach, which involves comparing differences in outflows between 18-to-24-year-olds and older age groups within the same areas and/or across different areas before and after the NDYP

was introduced. The first line of research covering the first two years of the program to March 2000 estimates that youth employment(subsidized and unsubsidized) has increased by approximately 15,000(Riley and Young, 2001a and 2001b). A difference-in-difference analysis using longitudinal data reveals that the NDYP significantly increased outflows to employment by 17,250, mainly because of the subsidy paid to employers(van Reenen, 2001).

In addition, there is a consensus in the literature that employment placements resulting from the NDYP did not displace non-participants from jobs(that is, substitution effects were not present)(Riley and Young, 2001b; van Reenen, 2001).

More importantly, concern has been expressed by commentators about the relatively high proportion of young people(23% up to November 2000: DfEE 2001) who fail to find sustainable employment through the NDYP. Policies may be needed to prevent clients alternating between New Deal programs and brief periods of paid work.

Findings on the effects of sanctions are mixed. Research on the 26-week sanction indicates that clients increased their level of job search activity as a result(quoted in Britton, 2002). Indeed, some entered employment, but mainly casual short-term jobs. Moreover, a national survey of participants showed that, controlling for other factors that can influence job entry, those sanctioned were as likely as other clients to enter work(Bonjour et al, 2001). However, sanctioned clients were more likely to still be on New Deal when re-interviewed for the survey; and the sanctioning had not encouraged them to leave for non-employment outcomes.

Another positive outcome of the NDYP is its cost-effectiveness. That is, while the additionality is not great, it is allegedly self-funding(Anderton et al, 1999) and benefits exceed costs(van Reenen, 2001).

(E) Looking ahead

The longer term effects of the New Deals are unknown. The government, however, would seem to have learned much about the implementation and operation of welfare-to-work schemes, with the value of case and partnership working now firmly established. Although the programs and test initiatives continue to be refined, New Deals are now part of the landscape of welfare-to-work in the UK, and have already been influential in changing how benefit and employment services are delivered to workless people.

3. New Deal for Lone Parents^{주29)}

(A) Introduction

Lone parents receiving social assistance are still not required to be available for employment if they have a child less than 16 years old, the minimum school-leaving age. Since 1970s, the number of lone-parent families has more than tripled, their employment rate has fallen, their receipt of benefits has risen, and their poverty rate has increased dramatically.

The current Labour government has initiated a significant policy shift, one that begins to reconceptualize lone parents as workers as well as parents and that, for the first time, sets an employment target for policy.

Interestingly, it is the US, rather than any European country, that has been most influential in British policy debates about lone parenthood. In the 1980s and early 1990s, the 'underclass' view of lone parents prevailed in both countries, and the growth in lone parenthood was interpreted as a sign of declining moral standards. This is very much in contrast to the debates in many European countries, where there has been much less moral concern over changing family patterns(Lewis, 1997).

The standard British definition of lone parenthood is a person living without a cohabiting partner and with one or more dependent children, defined as children aged under 16 or under 19 if still in full-time education. This definition excludes cohabiting couples but includes lone parents living with their parents(or other adults) in the same household. In 2000, there were about 1.75 million lone-parent families with about 2.9 million dependent children(Haskey, 2002). This is almost one in four children in the country.

By the mid-1990s, 48% of lone parents(excluding widows and widowers) were separated from marriage, and 28% from cohabitation. The remainder were single, never-married women(Marsh, 2001). The vast majority — over nine in ten — of lone parents are women. They are less likely to have any educational qualifications, with 28% of lone mothers having no qualification compared with 17% of married mothers(Holtermann et al, 1999). About 11% of lone mothers come disproportionately

^{주29)} This section draws on Millar(2003).

from ethnic minorities, compared with about 7% of married mothers(ONS, 1999).

The gap between lone and married mothers' employment rates has widened steadily over these years. In the mid-1970s, 47% of lone mothers were employed compared with 52% of married mothers. By the mid-1990s, the proportion of lone mothers employed had fallen to 42% while the corresponding figure for married mothers had risen to 66%. These falling employment rates have meant that lone mothers have become increasingly reliant upon social security benefits, notably Income Support(a national means-tested benefit providing a basic minimum benefit for those with no or very little income from other sources). The proportion of lone parents receiving Income Support rose from about 43% in the mid-1970s to about 65% by the mid 1990s. In 1996, just before the Labour government took office, slightly over one million lone-parent families were receiving Income Support(DSS, 1999b)

Lower employment rates have meant more poverty among lone parents, since benefit levels are below poverty thresholds. In 1979 about 19% of lone parents had income of less than half the contemporary mean(after meeting housing costs and taking account of family size), and this rose to about 60% by 1994/95(DSS, 2000). In fact, living in a lone-parent family has become one of the main factors associated with child poverty. Of the 4 million children living in poor households(defined as above) in 1994/95, about 1.5 million were in lone-parent families. Lone parents also tend to stay poor for longer periods than any other working-age households, and often only escape poverty if they repartner(Jenkins, 2000).

(B) Politics of lone parents in the UK

While lone parents occupy a significant and distinctive place in British political and policy discourses, the politics of lone parenthood are, in important ways, very different in Britain than in the US. This applies both to current Labour and past Conservative policy.

First, the key policy issue in Britain has, until very recently, been(male) unemployment rather than(female) lone parenthood. Throughout the 1980s and into the 1990s, high rates of unemployment, especially long-term unemployment in the areas of declining manufacturing industry, had a very strong political resonance. In the late 1990s, the New Labour government began focusing on 'worklessness', rather than just unemployment.³⁰ While this brought in groups not previously targeted in labour market policy, including lone parents as well as disabled people, the main policy

focus was and remains male unemployment, especially among young people(Land, 1999). Thus young people, not lone parents, were the major target of attention in welfare-to-work policies for Prime Minister Blair's government, although it is true that lone parents are very important in British welfare policy.

Second, there is no consensus in Britain that lone mothers should be expected to take employment, and there is only limited support for policies that would require, or compel, paid work. While the proportion of mothers in employment has increased steadily over the past decades, as noted above, most mothers work part time, and the view that paid work should take second place to motherhood remains strong, reinforced by politicians and the media and apparent in the attitudes of women themselves. Orloff(2002) argues that, in the US, increased employment among women was one of the key factors that made the 1996 welfare reform acceptable across a wide range of opinion. This contrasts with the UK, where there is much stronger support — again across a range of political opinion — for the view that lone mothers should not necessarily be expected to engage with paid work. As a result, there was only limited support within government for policies that would require lone mothers to seek employment, although there were some moves to improve financial incentives to work.

Failure to agree on an employment-based strategy led policy attention to focus on child support requirements for separated fathers rather than work requirements for lone mothers. The child support reforms in the UK in the early 1990s were driven both by ideology(separated parents have an obligation to contribute towards the costs of their children, and the state has a duty to enforce this) and economic considerations(pursuing the separated parents for child support should lead to reduced benefit expenditure on lone parents).

With the introduction of the 1991 Child Support Act, lone parents receiving benefits were required to cooperate with a newly established agency in charge of determining child support liabilities and collecting and distributing payments. But any child support paid by former partners was deducted directly from Income Support, leaving the lone-parent family no better off. These measures were deeply unpopular and controversial, both in respect of the policy itself and its implementation. Furthermore,

주30) "Worklessness" is similar to "not in the labor force", a concept used in the U.S. The latter term is defined as not employed and not looking for employment — that is, either having "dropped" out of the labor force or never having entered the labor force.

there was no consensus around the principle that all separated biological fathers owed an unconditional obligation of support to their children. In addition, the men affected turned out to be a very effective pressure group who resisted the policy by both individual non-compliance and collective lobbying. In response, changes were made to the scheme almost every year between 1993 and 1997, when the Conservatives lost the election.

This very public failure of the child support legislation led policy attention back to the employment issue. By the 1990s, the Conservatives were starting to introduce measures to increase the work incentives, both for unemployed families and for lone parents. The most significant of these was the 1992 reduction in the weekly hours of work needed to qualify for the in-work, means-tested Family Credit from 24 to 16. Possibly as a result of this change, the number of lone parents receiving Family Credit rose by about one third between 1992 and 1994. Thus by the mid-1990s, British policy towards lone parents and employment was steadily moving away from the neutral model favored by the Finer Committee. Even so, it was still far from being an employment-based model.

Finally, 'welfare' does not have the same negative connotations in Britain as it does in the US. The 1980s were probably the decade in which popular support for the welfare state was at its lowest level in Britain, but even then there was much opposition to cuts in benefits and other welfare provisions. Moreover, based on social attitudes survey data, support for redistributive policies has strengthened in recent years (Hills and Lokes, 1999; Jarvis et al., 2000).

In the US welfare reform has focused upon lone parents, has been based on a broad consensus that the goal should be paid work for all lone parents, and has included a strong emphasis on "family values" — an emphasis that has grown since the 2000 election. None of this is the case in the UK, where lone parents are one of several groups of policy interest, where attitudes towards employment for mothers are more ambivalent, and where family values rhetoric has not been translated directly into welfare policy. Moreover, given bedrock popular support for welfare, reform in the direction of compulsion to work outside the home risks electoral unpopularity.

(C) New Deal for Lone Parents: Implementation and outcomes

The New Deal for Lone Parents is the first of the Labour policies affecting lone-parent families, and this program is essentially an advice- and information-providing service, with voluntary participation. The objectives of the program are "for lone parents to be offered advice by the Employment Service to develop a package of job search, training and after-school care to help them off benefits and into work"(DWP 2002). Those who take part in the New Deal are allocated to a New Deal Personal Adviser. The New Deal Advisers can also offer in-work support and mentoring for those lone parents who find jobs. The programme was introduced in three phases, the first, in July 1997, being a prototype in eight areas of the country. The second, from April 1998, extended the scheme nationally to lone parents making new or repeat claims for Income Support. The third, from October 1998, brought in existing Income Support recipients to the national scheme.

A number of changes have been made in the way the New Deal for Lone Parents programme operates since it was originally introduced. These have included a progressive widening of the target group, initially from lone parents with children aged over five years and three months, then to those with children over three years, and finally to all lone parents. In addition, although participation in the New Deal remains voluntary, lone parents in receipt of Income Support are now required to attend a 'personal adviser' interview as part of their benefit claim. At this interview they are given information about the New Deal programme and invited to join. These compulsory personal adviser interviews were introduced in April 2001 for all lone parents making a new or repeat claim for Income Support, and were phased in nationally over two years from April 2002 for existing recipients.

Other employment-based policies include replacement of Family Credit in 1999 with the more generous Working Families' Tax Credit and the introduction of state support for childcare provisions and costs. The National Child Care Strategy, which began in May 1998 with a start-up budget of £470 million, aims to "ensure good quality, affordable childcare for children aged up to 14, and up to 16 for those with special needs, in every neighbourhood"(DfEE, 1998). These provisions represent a significant policy break with the past, with the acceptance of a role for government in the provision of childcare and in helping working parents to care for their children replacing the assumption that childcare was essentially a private matter(Randall, 2001).

In order to understand the impact of Labour's New Deal for Lone Parents and its attendant programmes, we need to consider three main issues(Millar, 2003).

The first is participation and take-up. Since the New Deal for Lone Parents is a voluntary program in which all participants have elected to take part, it is important to know how many people have elected to participate and what proportion of the eligible population this represents (that is, the take-up rate). This gives an indication of the success of the scheme at reaching the target population. In the evaluation of the prototype program, it was estimated that about 24% of those in the target group were participating(Hales et al., 2000)

The introduction of compulsory personal adviser interviews was intended to improve participation. The national statistics show that the vast majority(80% to 90%) of lone parent who attended an initial interview did go on to take part in the program. The qualitative data from the evaluation also suggest that the vast majority of participants responded very positively to the program, even if they had been reluctant or concerned beforehand. Early results from these pilots were encouraging, and seemed to suggest that compulsory interviews increased participation in the New Deal program and also led to increased employment outcomes, although later evidence did not confirm these results in respect of employment(Evans et al., 2002).

It is worth noting that there have been some changes in the characteristics of participants over time. There are now more older lone parents, the average age of their children is slightly older, and there is a higher proportion with longer spells in receipt of Income Support. These changes in the characteristics of lone parents receiving Income Support over the past several years suggest that participants are increasingly including the 'harder to help' lone parents, those who lack recent work experience(Evans et al, 2002).

The second issue is outcomes — what effect the program has on the factors it was designed to change. Since the main objective of the New Deal for Lone Parents is to help them enter work, the number entering work as a consequence of program participation is the main outcome measure of interest.

The number of lone parents who have participated in the national New Deal program during the period of October 1998 through January 2002, and their destinations after program participation, are shown in Table IV-4. About two thirds(66%) of the participants had left the program by the end of January 2002. About one third(36%)

of the participants had entered employment, representing just over half(54%) of all who had left the program. About a quarter of the participants(38% of all exits) had returned to Income Support.

Table IV-4. New Deal for Lone Parents: exits and destinations, October 1998 to January 2002

	Number	% of participants	% of leavers
Participants	318,990	100	
Left New Deal	211,350	66	100
- into employment	115,060	36	54
- Withdrawal, still on Income Support	80,870	25	38
- Unknown destination	8,970	3	4
- No longer eligible	4,480	1	2
- Other Benefits	1,970	1	1

(Source: New Deal Evaluation Database, Statistical First Release, March 2002)

However, these national statistics shown in Table IV-4 give no indication of the impact of the New Deal in comparison with what would have happened if there had been no program. There is some evidence available from both the evaluation of the prototype and from the evaluation of the national program. As mentioned above, the prototype was designed to be an implementation trial and to provide a basis for impact assessment for national implementation. Its quasi-experimental design (a) introduced the program in eight prototype areas, chosen to represent areas with low, medium, and high unemployment, and (b) included six comparison areas matched to the prototype sites in unemployment, industrial mix, and geographical location. The prototype ran for about eight months before the national scheme was implemented.

The main outcome results from the prototype are reported by Hasluck et al.(2000) and also summarized by Hales et al.(2000). The most marked difference between the participant and control groups, as defined in the natural experiment, occurred six months into the project when the odds of long-term recipients leaving benefit were 12% higher for participants. This differential, however, declined with time and averaged about 5% over 18 months.

Survey data revealed that not all participants left Income Support for employment

(Hales et al., 2000). The same data also indicated that, at least over the period October 1998 to January 1999, there was no significant difference between prototype and comparison areas in the proportion of lone parents who secured jobs on leaving Income Support (17% and 18% respectively), nor in the types of jobs secured, the hours worked, or the pay received. However, those lone parents who found jobs were more likely to report that they were better-off financially in work if they had participated in the program than if they had not (66% compared to 46%), perhaps suggesting that participants were able to make better job matches and/or more often accessed in-work benefit support. In their synthesis of the evaluation as a whole, Hales et al. conclude that the program had a "small but appreciable effect" (Hales et al., 2000, p.9) at a modest net cost. However, there are important limits in the extent to which one can extrapolate from the prototype findings to the national program. The prototype was small, staffed by people who were highly committed to the program, and was generally well resourced, although there were few complementary services in place at the time.

The national program was evaluated over a period of seven months from late 2000 to 2001 by means of a matched comparison quasi-experimental design. This involved a postal survey of about 7,000 lone parents from whom matched pairs of participants and non-participants were identified. The impact of the program was estimated by comparing the outcomes of these two groups. After six months, about 43% of participants had entered full-time or part-time work compared with about 19% of matched non-participants. This suggests an additional effect of participation of about 24% (Lessof et al., 2003). Thus, it appears that employment outcomes in the national program may be better than those achieved in the prototype.

The third issue is process: how well various parts of the program work on the ground. This includes understanding which parts of the program are most effective at increasing employment and which are not, comparing the effectiveness of different models of delivery, and identifying any gaps and problems in the program's organization.

The New Deal for Lone Parents is, as noted above, essentially an advice and information service, with some opportunities for referrals to training. The National Database shows that most participants are 'receiving advice and guidance'. This accounted for 66% of participants at January 2002, with a further 29% receiving 'in-work support' from a New Deal Personal Adviser, and 5% in education or training

(DWP, 2002).

Those who took part in the prototype usually said they had found the process helpful. Most participants had just one interview, usually lasting an hour or less which was generally considered to be 'about right'. Only one fifth of participants said they would have liked more contact. The main topics discussed in interviews were job search, benefits, and childcare. Very few participants were referred to other service or offered access to education or training. Most felt the discussion to be helpful, but some were disappointed that there was such limited follow-up help available. About half of those who found work said they had been encouraged and helped by the advice on job seeking; about 34% said the program had directly aided them in finding work.

Lone parents' assessment of the program was closely linked to their perceptions of their Personal Advisers, which fell into two quite different categories. The majority (eight in ten participants) were very positive about the manner and approach of Advisers (they were seen as friendly, helpful, supportive) and were also positive in their overall responses, even if they had not received much concrete help. But about one fifth found their Advisers patronizing, unclear, and unhelpful. Most participants felt that they would have liked more information, especially about jobs and childcare.

The evaluations of the national program tend to confirm this picture from the prototype (Lewis et al., 2000; GHK, 2001; Lessof et al., 2001, 2003). These studies also found that lone parents had a variety of motivations for taking part in the program including curiosity, a wish for further information or guidance, a motivation to work and a search for specific help, and a belief that participation was compulsory (Lewis et al, 2000). Help with job search and the limited type and level of training on offer were seen as the weakest elements.

Information about the financial aspects of working was highly valued and most participants were very positive about the New Deal Personal Advisers, as participants in the prototype had been (GHK, 2001). There was some evidence from the qualitative studies that participants were highly motivated and the large postal survey (which included 42,000 lone parents) found that participants tended to be more work-ready than non-participants (Lessof et al., 2001). However, the matched pairs analysis found an additional impact of the program and also confirmed the positive response to the program, especially from the Personal Adviser, found in the prototype (Lessof et al., 2003).

(D) Looking ahead

Two of the new elements warrant special attention: the introduction of compulsory personal adviser interviews as part of the process of claiming benefits and the measures to encourage part-time work (Millar, 2003).

The element of compulsion is mild when compared to the US. It does not compel lone parents to join the New Deal, which will remain voluntary. Nor does it change the rules regarding availability to work: lone parents will continue to be eligible for benefits without any work requirements as long as they have a youngest child under 16. But it is the first time that such requirements have been placed upon lone parents in the modern British welfare state. The additional support for part-time employment is intended to make it possible for lone parents to construct an 'income package' from part-time wages, benefits, and child support.

The Labour government's approach to the lone parents programs supports their employment but also recognizes that lone parents cannot always be available for work. Lone parents will be required to attend interviews where they will be given regular information about employment and training options, but they will not be compelled to act upon these. There are also financial measures intended to make work pay and in-kind measures designed to make work possible. Childcare is the most important in-kind support, and here there is reliance upon a mixture of public, private, and voluntary provision.

A substantial gap still exists between the 54% currently in employment and the 70% employment target set in Britain. However, the employment target does not necessarily imply that 70% of lone parents should be in full-time work and, as discussed above, the policy is increasingly focused upon measures that would allow lone parents to combine 'work and welfare'. This shift — away from tax and social security systems that sharply distinguishes between workers and non-workers towards more integrated systems that recognize more varied patterns of employment, both contemporaneously and over time, and that are based on providing wage supplements rather than wage replacements — may be one of the most significant developments in UK history. Such an approach may be better adapted to current labor market and family patterns, although it runs the risk of institutionalizing a large low-paid sector of employment, particularly for women.

V. Conclusion

Perhaps the most important component of the British welfare reform is the recognition of the centrality of work and the place of obligations in welfare reform. Proactive, work-based policies were first pursued by Conservative governments under Margaret Thatcher and, after some soul-searching, developed as a unifying element within the current Labour government's reform strategy. Work-based obligations have always been a feature of Britain's welfare provision, although they were less evident in the 1970s when a social rights agenda was given greater prominence. The Conservative government led by John Major experimented with a workfare program in the mid-1990s, but it is the current Labour government, drawing on American communitarianism and the new paternalism, that has placed an emphasis on the duties and responsibilities of welfare recipients at the heart of reform.

Prime Minister Tony Blair's characterization — work for those who can, security for those who cannot — usefully underscores the work orientation of social assistance, which provides both security and incentive, either financial or through obligation, to work toward self-sufficiency, while at the same time reaffirming the responsibility of government to preserve the social safety net given the central importance of employment.

Also important is the longstanding goal of 'making work pay' — that is, assuring that persons moving from welfare to work secure higher incomes than those received when dependent on benefit. The antecedents of the current system of tax credits, first introduced in 1999 under the name of the Working Family Tax Credit and shaped by observations of the US Earned Income Tax Credit (EITC), were instigated by a Conservative government as early as in 1972. They were implemented as cash benefits instead of tax credits after attempts to introduce a tax credit in Britain

floundered. In the meantime, a national minimum wage was not introduced until 1999.

In acknowledging the need to reconcile what were once viewed as competing claims — rights versus responsibilities, promotion of enterprise versus eradication of poverty, and so on — the current Labour government, led by Tony Blair, has built upon, rather than reversed, changes introduced by successive Conservative governments. In so doing, it has distanced itself from earlier Labour governments and developed welfare institutions of considerable relevance to other countries.

The Labour government's central ambition has been to use the leverage of government to eradicate child poverty within a generation. As a result, in the UK, unlike in the US, where the welfare reform debates have recently been confined to questions of what can be done to get welfare mothers into work, or how former welfare recipients can attain self-sufficiency, questions were centered on what policies are there that foster self-sufficiency across the entire low-income population and how can they be made mutually supporting.

Also, in recognition of the fact that policies needed to achieve the specified goal involve most central departments, new agencies have been created at the heart of the central government — located in the Treasury, the Cabinet Office and the Prime Minister's Office, with its mission to coordinate policy development across the traditional divisions of government.

Another aspect of Labour's strategic vision worth mentioning is that, in seeking to eradicate childhood poverty and to promote equal opportunity, the British government has embarked on a long-term policy designed to raise the skill base of the labor force and to remove rigidities that have slowed economic change. The New Deal family of welfare-to-work programs accords with this global vision, imparting work experience and accredited training, so as to enhance the skills and advancement of the current generation of workers while providing, through their parenting, good role models and opportunities for the next.

In conceptualizing and presenting welfare provisions as a positive agent of economic change rather than as a constraint on economic performance, the Labour government is also aware that this can enhance public support and thereby free additional resources to invest in programs.

In sum, Britain's strategy is long-term and embracing. Social assistance and

welfare-to-work measures are not viewed so much as independent programs but as part of a panoply of policy instruments designed to eradicate child poverty and promote individual opportunity to the benefit of the economy and society as a whole.

The broader vision of UK-style welfare means that Britain has sought to employ US-style welfare-to-work models in a wide range of settings. The reasons for this lie in both distant history and the immediate past. Historically, British provisions are a legacy of mass unemployment rather than a response to the problem of fatherless families. In the contemporary context, child poverty and social inequality have been driven by the growth in workless families at a time when the social norm is for both parents to be in paid work.

The NDYP has marked similarities to Wisconsin's W-2. As in the US, long-term unemployment among young people, especially young men, is associated in politicians' minds with crime, disorder, and thoughtless fatherhood. Also, there is statistical evidence in Britain that early experience of unemployment is causally related to poor employment records later in life (Brewer and Gregg, 2001). Add to these concerns the economic objective of upgrading the skill base of the British economy, and it is evident why the NDYP was highlighted in Labour's 1997 election manifesto.

In Britain, as in the US, young unemployed people are typically very poorly educated and lack the soft skills that work experience supplies. Turnover is also high as many young people inhabit the unstable fringe of the labor market. Unlike in the US, young people over the age of 18 in the UK who can demonstrate that they are both available for, and actively seeking, work have always been able to claim means-tested assistance even if their insurance record has been insufficient to allow them to receive unemployment benefit (i.e., contributory Jobseeker's Allowance). Since 1998 benefit beyond six months has been conditional on enrolment in NDYP with its mix of job-search, work experience and universal accredited training. Since 1999 the same obligations have applied to the partners of unemployed young people. Sanctions are mild compared to those that apply under TANF — up to four weeks loss of benefit for each instance of non-attendance in the participant's New Deal option but with a cumulative maximum of 26 weeks, compared to eventual total loss of benefit for non-compliance in most state TANF programs.

With the NDYP, the Labour government claims to have fulfilled its manifesto commitment to return 250,000 young people to work, and has thus been encouraged to extend the intensive welfare-to-work model represented by the NDYP to other

groups of unemployed people, replacing less intensive versions implemented earlier. British experience suggests that the case for experimenting with a benefit aimed at workless young men, conditioned on work activity, could be persuasive for a policy focus that is aimed at poverty prevention rather than poverty relief.

US welfare policies to edge single mothers from dependence on welfare into sustained economic independence have their counterparts in Britain: welfare-to-work schemes, tax credits, regulated child support, and a national childcare strategy. With limited skills and work experience, often burdened by guilt, self-doubt, and scars of physical and emotional abuse, lone parents have to juggle the demands of parenthood with those of the breadwinner. Policy systems reflect a common response to this lack of security in employment, finance, and relationships confronted by lone parents, attempting to raise skills and income with varying success.

However, there are some important differences in policies between the UK and the US. While the TANF reforms in the US require work obligations on virtually all welfare mothers and require States to place time limits on financial support, neither condition applies in Britain. In fact, measures introduced in Britain during the last decade, including changes in child support policy and the Working Tax Credit (Working Families' Tax Credit, prior to 2003) and New Deal for Lone Parents, have actually enhanced the ability of lone parents to choose whether to work or not. Certainly 20 years ago lone parents in Britain were expected to give priority to caring for children rather than to paid employment, and until very recently they were denied access to job-search and training facilities available to other benefit recipients. Labour's welfare-to-work initiatives, building on a small pilot instigated by the last Conservative government, mean that lone parents are now more able to draw on government resources to equip themselves for paid employment, should they wish to do so.

At present, public support in Britain would not condone policy that enforced lone parents with young children to take paid work. It seems that priority is given to the immediate care needs of children rather than to ensuring the role model of an employed parent or enforcing the conditionality of the receipt of the benefits.

Given that work obligations are not enforced in Britain, it provides evidence of what can be achieved by a mixture of voluntary welfare-to-work programs, childcare facilities, and financial incentives. Britain's national childcare strategy, introduced in May 1998 with the goal of providing childcare places for all those wishing to use

them, is by no means yet in place. The dramatic six-percentage-point increase in the employment increase among lone parents that was observed between 1997 and 2000 was therefore achieved without this basic support. Millar(2003) suggests that financial incentives and voluntary employment and advice schemes are of equal importance in explaining employment growth among lone parents set against a backdrop of buoyant labor demand. Two thirds of lone parents who returned to work through the New Deal felt themselves to be better off financially. Relative poverty among lone parents fell from 38% in 1996/97 to 32% in 2001/01, and the poverty rate for all children dropped from 26% to 21%(CPAG, 2002; these data use as the poverty standard 60% of median income before housing costs). Moreover, the proportion of lone parents rapidly returning to benefit — about 8% within in eight months — has been low in comparison with American experience. This may be a selection effect: on average lone parents moving from welfare to work under Britain's voluntary system may be more motivated to continue. But it may also reflect the ready access of such parents to in-work supports and the seamless health care coverage Britain provides.

One concern, however, is that lone mothers taking up paid work in the UK and the US, and in many other countries as well, are typically entering the bottom of the labor market and assuming the economic risks such entry entails. While work-first policies succeed in reducing welfare rolls and increasing employment, they are much less effective in ensuring either substantial or sustained increases in income. Miller (2003) and Stafford(2003) both report worrying numbers of lone parents and formerly unemployed claimants in Britain returning rapidly to benefit. The story is repeated among former welfare recipients in the US, where research indicates that wage growth is typically very slow, with people's earnings not exceeding the poverty line even many years after leaving welfare(Primus et al., 1999; Pavetti and Arcs, 2001; Wavelet and Anderson, 2002). If policy is to achieve more than transforming the claimant poor to the working poor, strategies are needed to stimulate career development. Hotz and his colleagues(2002) have called this the next frontier in anti-poverty employment policy.

The precipitous decline of the welfare caseload in the US has generated great concern about the status of families who have either left welfare or, if poor, are not receiving assistance. So-called 'leavers' studies have been conducted in the US both by states and by independent researchers. Most report that a significant proportion — around 20% — of those exiting assistance do not sustain employment. Multiple problems, ranging from lack of skills and credentials to drug addiction, contribute to

such experience. Families with barriers to self-support have always been part of the assistance caseload, but until recently they were generally passed over when targets for employment policy were selected. Struggling families are a problem that never dies. Strategies are needed to help these hard-to-serve population.

The New Deals in Britain are now largely delivered through 'one-stop' centers based on American models and, as in the US, advisers/case workers working face-to-face with clients play central roles. As Walker and Wiseman(2003) argue, identifying the influence of program organization and management on outcomes at the local level is essential for understanding sources of differences in performance capabilities. Study of process could be as important as study of outcomes.

One of the lessons that can be learned from the British experience is that the British government has developed a political strategy for gaining public support for sustaining the safety net by recognizing need, linking benefit to work, and casting reform as one of multiple means toward attaining larger national goals of modernization and improved productivity. To be politically useful, visions for welfare reform must link change to what a better assistance system might do for the country as a whole.

We finish this report with some recommendations to Korea, in particular with reference to the National Basic Living Standard scheme and the planned EITC-like program, based on the American and British experiences.

One of the problems with the NBLS scheme is that a considerable proportion of people who are ruled ineligible for the benefits due to the presence of nonpoor close family members do not in fact get the expected support from them. One way of encouraging the grown-up children or siblings to support their poor parents or siblings is to increase the amount of allowance of the income tax for the expenditure spent for the support of poor parents or siblings. It could be done, for example, by introducing a weight of 1.5 or 2, say, for the amount spent for the support of poor parents or siblings in computing the amount of income tax allowance, with the provision that a written statement of those supported should be presented to the tax agency.

On the other hand, the underreporting of income and the resulting benefit payment to nonpoor people has always been another major problem. Serious efforts to get the real amount of income, of both employed and self-employed, need to be made. Also,

the planned EITC-like program will be of some help to encourage people with low income to report their true amount of income if it can pay some generous amount of credit to the low-income people.

The lack of work incentive of the NBLs scheme also needs an urgent attention. Except for a limited number of categories of recipients such as the disabled, students, and participants in the organizations for self-support for whom 30% of earned income is disregarded in computing the household income, the current 100% marginal tax rate for the income earned by the recipients discourages them from getting a job or working more hours. It would be desirable for the amount of NBLs benefits to decrease only by a fraction of the recipients' earnings. The taper rate of 55% of the WFTC in the UK would be an example. Also, the planned in-work benefit program to be introduced in 2007 will help cure the employment and poverty traps. In addition, the current system under which the recipients households loses eligibility for the NBLs benefits as well as other supplementary benefits such as housing benefits, medical benefits, and education benefits once their income rises above the designated income threshold also leads to a weak work incentive. Solutions to this problem include allowing the recipients to maintain their eligibility for these supplementary benefits within some limited range of income above the threshold income as in the US, or to disregard a certain amount of income in deciding eligibility for these supplementary benefits, as was done for the WFTC in the UK.

The employment services intended for the self-support of the recipients leave much to be desired. The classification of the recipients into two types of categories based on their ability to work is somewhat arbitrary and discretionary and hence may prevent the clients from getting the right employment services they need. Also, the services provided are generally of poor quality, and case workers are in many cases neither well qualified nor highly motivated. Further, the recipients are very often quite disadvantaged in terms not only of education, labor market experiences, and skills but also of self-confidence and motivation. The employment services and training programs need to be diversified and client-tailored, and for this to happen, the case workers, among other things, should become more able and motivated through training and better compensation. Also, the number of case workers needs to be increased significantly, and the service delivery system needs to be upgraded. The British experiences with the Jobcentre Plus are worthy of serious studying. In particular, it is worth remembering that in the UK lone parents' assessment of the New Deal program was closely linked to their perceptions of their Personal Advisers.

Given that the recipients are disadvantaged in terms of working ability, subsidized jobs and community service jobs can be quite important. They can provide the recipients with good working experiences, and hence efforts should be made to develop and design some good community service jobs, taking into account the specific characteristics of each locality and the recipients. In doing this, lessons could be found in the New Deal programs in the UK and the W-2 program in Wisconsin. For example, in the W-2 program, people who lack the basic skills and work habit needed in regular job environment are assigned to the community service jobs, which offer real work training opportunities with the needed supervision and support. Also, if necessary, they are allowed to spend a portion of their required working hours participating in the training programs.

We now turn to the Korean EITC-like program under consideration.

One of the issues is the scope of coverage. According to the government plan, the in-work benefit program is to cover only the wage or salary workers at the time of introduction and then to be expanded to cover the self-employed after several years. The reason of excluding the self-employed is of course the difficulties faced by the tax agency with getting the precise amount of income of the self-employed. This decision, however, will mean that many poor self-employed with low and unstable earnings, who would need the in-work benefit no less than the wage and salary workers, would not get the governmental support until the coverage expansion occurs. One remedy would be to allow the self-employed to voluntarily participate in the scheme on the conditions that they report their precise amount of income and that punitive penalties for failing to report the true income are imposed and informed to the potential participants in advance. In addition, the amount of wealth also needs to be considered in determining eligibility. This can be done by setting the upper limit of amount of wealth for eligibility as is the case with the US EITC.

Looking at the income threshold, in the US in 1997, the poverty line for a family consisting of a single parent and two children was \$12,802. This family could receive the maximum EITC of \$3,656(28.6% of the poverty line) at the earned income between \$9,140 and \$11,930, and with the phase-out rate of 21.06%, the credit was completely phased out at the earned income of \$29,290(229% of the poverty line). In the UK in 2000-01, the poverty line for a family consisting of a single parent and two children under 11 was £188 a week or £9,776 a year. This family could receive the weekly maximum working family tax credit of £104.35(55.5% of the poverty

line) at the weekly net income below £91.45. With the taper rate of 55%, the credit was fully tapered away at a weekly gross income of £385(205% of the poverty line).

One major difference between the British and American in-work benefit programs is that the WFTC(or WTC) does not have the phase-in range of income over which the tax credit rises. This is because the WFTC requires at least 16 hours of weekly working hours to be eligible while the EITC is eligible for all workers with any positive number of working hours. It might be worth considering requiring workers to work a certain number of hours or more to be eligible for the tax credit, like in the UK. This restriction will lead workers to remain in the labor market more steadily, which in turn results in a more stable and higher income.

Another related issue is whether to require the presence of children to be eligible for the benefit. In the US and UK, the in-work benefits were originally available only to a family with children and it was not until quite recently that the programs were expanded to cover poor families without dependent children. Moreover, the amount of benefits awarded to the childless families is significantly smaller than that awarded to families with children. This was because households with dependent children are more prone to poverty, and because child poverty has long lasting effect on the affected children's future accomplishment. It seems reasonable, therefore, to confine the eligibility only to families with dependent children, at least at the time of introduction. Also, it would be desirable to include a childcare subsidy in the program as in the UK and as in various State welfare-to-work programs in the U.S.

Another question is related to the magnitude of in-work benefit. The key parameters determining the actual amount of the benefit to be paid include among other things the maximum payable amount and the phase-out or taper rate. It might be meaningful to compare the maximum tax credit amount with full-time labor income that can be earned at the minimum wage in the US and in the UK. In the US in 1997 a full-time(2,000 hours a year) minimum-wage worker and a single-parent with two children could earn \$10,300 in wages and was eligible for a \$3,656 EITC. The poverty line for this family was \$12,802.³¹⁾ Looking at the British experience, in the budget year of 2000-01, a full-time minimum wage worker and a lone parent with two children under 11 could earn £7,400 in wages and could get the maximum working family tax credit of £115.6 a week or £6,011.2 a year. The poverty line for this family including the housing cost was £188 a week or £9,776 a year.³²⁾ The

³¹⁾ Hotz, V. J. and Scholz, J, 2003. p.159.

ratios of the maximum in-work credit to the full-time earnings at the minimum wage of these families therefore were 0.355 and 0.812 in the US and UK, respectively. The ratios of the sum of the earnings and tax credit to the poverty line in the UK and US were 1.09 and 1.37, respectively. The tax credit taper rates are 15.98% and 21.06% for a family with one qualifying child and a family with two or more qualifying children in the US, and 55% in the UK irrespective of the number of children.

A related issue is that there is some opposition to the introduction of the EITC-like program on the ground that it would prevent or delay the increase of the minimum wage. Burkhauser et al(1996), who compared the effect of minimum wage and the EITC on the income of poor people in the US, reported that increases in the EITC between 1989 and 1992 delivered a much larger proportion of a given dollar of benefits to the poor than did increases in the minimum wage in 1989 from \$3.35 to \$4.25. Their simulation results also showed that the then scheduled increase in the EITC through 1996 would also do far more for the working poor than raising the minimum wage. This suggests that the aforesaid opposition may not be justified since in-work benefits may well make a larger contribution to raising financial situations of the working poor than raising the minimum wage, although the actual effects should certainly depend on the magnitude of the current level of and the change in both the in-work benefits and the minimum wage.

Although the Korean income tax system is individual based rather than family based, it should not be a major obstacle to introducing an in-work benefits in the form of the family-based tax credit, as the British experience shows.

Lastly, it would be desirable for the sake of the work incentive that, the earned income tax credit is not included in the income in calculating the NBL benefits and the NBL benefits not counted as income in computing the earned income tax credit, which is generally the case with the EITC and the WFTC.

주32) DWP, 2002, p.13.

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