Economic
Policy
Institute

Briefing Paper

1660 L Street, NW • Suite 1200 • Washington, D.C. 20036 • 202/775-8810

WIDE CAST FOR SAFETY NET

OVER TIME, MIDDLE CLASS AS WELL AS POOR RELY ON ENTITLEMENT HELP

by Howard Chernick[1]

Reductions in federal entitlement programs are a major component of both the House and Senate plans to balance the federal budget by the year 2002. While there are numerous reports that document the importance of entitlement benefits to low-income families, most studies focus on short-term benefit patterns.[2] In contrast, this study examines the impact of transfer programs on individuals both in one year, 1988, and over the 13-year period 1976-88. If entitlement income is primarily an income support for the permanently poor, then both the annual and intermediate-term receipt of such income will be restricted to those who are at the bottom of the income distribution. On the other hand, if such programs serve primarily as a safety net for those who become temporarily vulnerable to changes in economic circumstances, then longer-term income histories will show substantial benefits to those who are not persistently poor. Through an examination of the short- and intermediate-term data, this study finds:

- Overall, 23.5% of the population-nearly one-quarter-received cash entitlements during at least one year between 1976 and 1988;
- In 1988, 39.1% of people in the lowest income decile (i.e., the bottom 10%) and 14.5% in the second decile received cash transfers or Medicaid;
- During at least one year between 1976 and 1988, 59.4% of people in the lowest income decile, 47.9% of people in the second decile, 39.8% of people in the third decile, and 22.9% of people in the fifth decile received cash transfers;
- In 1988, transfer recipients in the lowest decile received 46.1% of income from cash transfers; the proposed cuts would reduce their cash income by 10.9% ($884 in 1995 dollars) or by 33.8% ($2,741) if the value of Medicaid is included;

- Over a 13-year period among people in the lowest decile, cash transfers were 27.3% of income; over the intermediate term, the proposed cuts would reduce annual income by 6.5% ($747 in 1995 dollars) or by 14.1% ($1,621) if the value of Medicaid is included;
- Among those with 13-year average incomes below the poverty level, entitlements provide 60-100% of income; proposed cuts would result in a 15-20% loss in income:
- If the proposed cuts in Medicare had been in effect in 1988, Medicare beneficiaries in the lowest decile would have experienced a reduction in benefits equal to 10.8% of income; the corresponding cut in 1999 would be 16.7% of income.

The study includes all the major entitlements programs (with the exception of Social Security), namely, the cash programs Aid to Families With Dependent Children (AFDC), General Assistance (GA), Supplemental Security Income (SSI), and Food Stamps (which is equivalent to cash), and the medical assistance programs Medicaid and Medicare.

In 1993 federal outlays on these programs totaled $281 billion, or 18.6% of the federal budget. The financing of Medicaid and AFDC is shared with the states; the federal government pays about 55% of total program costs. The total federal plus state outlay on the programs was about $343 billion. The Congressional Budget Office (CBO 1994) projects that Medicare and Medicaid will grow 8% per year in real terms between 1993 and 1999, while the other programs will grow 2.4% per year. Most of the growth in the nonmedical entitlement programs is projected to occur in the SSI program.

METHODOLOGY

The data source for the estimates in this study is the Panel Study of Income Dynamics (PSID). The study simulates the distributional impact of program cuts ranging from 18.6% for Food Stamps to 33% for AFDC and Medicaid. These magnitudes are the estimated program reductions relative to the baseline for fiscal year 2002, as passed by the House of Representatives. For AFDC and Medicaid, it is assumed that cuts would be accompanied by a switch to block grants, and the estimates incorporate a calculation of the likely state fiscal response to eliminating the matching provisions for these programs (see the appendix for more details). Based on these assumptions, the cut in total spending on these programs in 2002 would be $207 billion. If the full cuts had been implemented in 1993, the dollar cost would have been almost $100 billion.

Except for Medicare, the entitlement programs analyzed here are all means tested. Hence, it is expected that, in any one year, most of the benefits would be received by low-income families and individuals. Based primarily on the Current Population Survey, CBO (1994) estimated that fewer than 1% of families with incomes above $30,000 (in 1990 dollars) received benefits under AFDC, Food Stamps, or SSI. For Medicaid the comparable figure was 3%.

Research based on longitudinal data has stressed the dynamic aspects of poverty and participation in means-tested programs. For example, AFDC participation is characterized by a considerable amount of cycling onto and off of the roils, although there is a relatively small group with long continuous spells of welfare recipiency. A third group will have only a single, relatively brief spell of welfare recipiency over a long period.' Since AFDC recipients are almost always eligible for both Food Stamps and Medicaid, this dynamic behavior implies similar patterns of receipt of both of these transfer programs. These patterns suggest that the intermediate-term role of transfer payments may differ somewhat from the short-term role.

In contrast to AFDC, there has been relatively little research on the long-run dynamics of SSI participation. The SSI program has been growing rapidly, with program costs rising 20% annually in the last four years, primarily due to an increase in the number of disabled. Given that the recipients of SSI are elderly, blind, or disabled, the presumption would be one of relatively long spells of recipiency, as opposed to the episodic nature of AFDC participation. However, SSI recipients are required to apply for other programs first, and many of the disabled are also eligible for disability insurance (DI). The General Accounting Office reports that, of adult recipients who also qualify for DI benefits, 75% stop receiving SSI within one year (GAO 1995). For all of the programs considered in this paper, results are presented here for two periods: annual receipt in 1988 and average benefits over the 13-year period 1976-88.

WHO PARTICIPATES IN TRANSFER PROGRAMS

Program participation is examined both in a single year and over a 13-year period. Participation over the longer period is defined as the proportion of respondents who *ever received* entitlement benefits during an observation period. This proportion will indicate the extent to which transfers go primarily to the persistently poor, as opposed to the extent to which they serve as a temporary safety net for people whose longer-run economic circumstances are more favorable.

Table 1 presents participation in 1988. **Table 2** shows the proportion of each intermediate-term income decile that received transfers in at least one year from 1976 to 1988. The annual income distribution both among participants and overall is more dispersed in the annual data than in the 13-year income distribution. Average income in the lowest decile of 1988 annual income ($8,594) is only 73% of average income in the lowest decile of 13-year income ($11,708), while average income in the highest decile is 38% higher. This greater dispersion results in part from the greater relative importance in the annual measure of a purely transitory component of income, as compared to the greater relative importance of the permanent component of income in the intermediate measure. Because annual income is given for 1988, the last year of the measurement period, the difference also reflects the trend in income over the period, particularly the decline in the earnings and income of those in the bottom of the income distribution.

Comparing recipiency rates in a single year with recipiency rates over the longer period highlights the dynamic nature of entitlement eligibility. In a single year, 39.1% of those in the lowest decile received cash transfers; this proportion rises to 59.4% over a longer period. Also, while on an

TABLE 1
Participation in Entitlement Programs, 1988, by Family Income Group

Family income Decile	Average Family Income (1995$)	Percent Receiving					
		Food Stamps	AFDC or GA	SSI	Any Cash Entitlement	Medicare	Medicaid
1 (lowest)	$8,594	33.2%	13.7%	13.4%	39.1%	51.1%	22.8%
2	16,770	11.2	5.8	3.4	14.5	38.2	7.3
3	24,769	4.1	2.5	0.9	4.4	31.2	2.0
4	32,266	3.2	1.0	0.4	4.0	21.2	1.3
5	39,850	1.2	0.3	0.3	1.3	18.0	0.5
6	48,206	0.4	0.1	0.3	0.7	11.5	0.3
7	58,455	0.1	--	0.2	0.3	5.9	0.3
8	70,778	--	_	0.1	0.1	3.7	0.1
9	89,628		_	0.1	0.2	7.1	0.1
10	173,082	--	--	--	--	3.6	--
Average	$56,727	5.1%	2.2	1.8	6.1	18.8	3.3

Note: Income in any year is the income of the family of which the person is a member and includes money income plus Food Stamps.

TABLE 2
Participation in Entitlement Programs, 1976-88, by Family Income Group

Intermediate Family Income Decile	Average Family Income (1995$)	Percent Receiving[1]					
		Food Stamps	AFDC or GA	SSI	Any Cash Entitlement	Medicare	Medicaid
1 (lowest)	$11,708	52.5%	29.8%	27.8%	59.4%	60.9%	41.3%
2	20,166	42.6	27.5	10.3	47.9	38.8	27.8
3	27,477	35.5	18.9	5.5	39.8	26.4	16.7
4	34,297	25.6	11.7	4.3	29.2	20.0	10.0
5	40,714	18.9	9.4	2.0	22.9	14.7	6.3
6	47,291	13.8	7.9	1.3	16.9	13.0	5.7
7	54,167	9.1	3.2	0.8	10.1	10.8	2.6
8	63,546	5.8	1.2	0.5	6.3	12.1	1.5
9	76,736	2.6	1.2	0.4	3.3	8.3	0.9
10	125,804	1.1	0.6	1.0	2.5	9.0	1.3
Average	$50,582	20.4	10.9	5.2	23.5	21.0	11.1

Note: Income in any year is the income of the family of which the person is a member and includes money income plus food stamps. Intermediate family income deciles are constructed based on each person's inflation-adjusted family income averaged over the 13-year period.

[1] Percentage of all people in the decile who received entitlement benefits in at least one out of the 13 years.

annual basis transfer receipt drops off sharply for those above the first decile of income, the dropoff is more gradual over a 13-year period.

As shown in Table 2, a significant share of families in the lower half of the intermediate income distribution received at least some cash transfers over the 13-year period. Over half of those in the lowest decile and 47.9% in the second decile were recipients, as were almost a quarter (22.9%) of those in the fifth decile. The major program extending up into the middle class is Food Stamps: while less than 10% of the combined sample in the fourth and fifth deciles of intermediate income ever get AFDC, SSI, or Medicaid, more than 20% get Food Stamps. Over the 13-year period, 23.5% of people-nearly one-quarter of the population-received transfers. The results suggest that even among those whose intermediate-run economic position puts them solidly in the middle class, a substantial proportion are vulnerable to temporary economic dislocations that make them eligible for means-tested transfers. These results suggest that cuts in these programs could have a potentially serious effect on the middle class as well as on families with low incomes.

Table 2 also highlights the importance of medical care entitlements. Almost two-thirds (60.9%) of those in the lowest decile of the intermediate income distribution were eligible for Medicare at some point between 1976 and 1988, and 41.3% received benefits in at least one year under Medicaid. Since almost all Medicare eligibles are over 65, the high rate of receipt among the lowest income groups reflects the concentration of the elderly at the bottom of the income distribution. The importance of Medicare entitlements continues well up the intermediate income distribution, while Medicaid eligibility drops off more rapidly.

The difference between Medicare and the means-tested programs stands out when we compare annual to intermediate-run participation rates. Because Medicare eligibility is based on age and not income, there is little difference between annual and longer-term rates of Medicare recipiency. By contrast, a much higher proportion of those in the lower half of the intermediate-run income distribution gets some entitlement benefits than is the case for a particular year.

THE IMPORTANCE OF TRANSFER INCOME

Tables 3, 4, and 5 show the importance of cash entitlement income and medical benefits among those who participate in the programs. While most AFDC and SSI recipients are also eligible for Food Stamps and Medicaid, the overlap among all the programs is far from perfect. For example, the intermediate-run share of the population getting Food Stamps is twice as high as the intermediate-run share getting AFDC or General Assistance (see Table 2). To deal with this issue, the sample of participants is defined as those who have ever received any cash entitlement or Medicaid in the observation period. (Computation of transfer ratios, the portion of income received as transfers, is discussed in the appendix.) It should be noted that the income measure is primarily a money-income concept. Hence, in-kind income from medical care entitlements is not included in the denominator of the transfer

TABLE 3
Entitlements as a Share of Family income Among Recipients of Any Entitlement,’ 1988, by Family Income Group

Family Income Decile	Entitlement Recipients as a Share of All People in Decile (%)	Average Family Income of Recipients (1995$)	Food Stamps	AFDC or GA	SSI	All Cash Entitlements	Medicaid
1 (lowest)	39.1%	$ 8,110	20.2%	42.3%	41.2%	46.1%	69.3%
2	14.5	16,520	12.5	27.6	38.2	28.9	32.8
3	4.4	24,572	9.8	20.0	21.1	23.6	25.0
4	4.0	31,884	6.3	10.0	--	9.2	15.4
5	1.3	40,234	--	–	_	3.9	–
6	0.7	47,1 a7		–	_	7.3	–
7	0.3	57,139	--	–	_	2.0	--
a	0.1	73,285		–	_	1.7	--
9	0.2	96,369		–	_	2.8	–
10	–	–	--				
Average	6.1	14,662	15.7	31 .a	38.9	36.2	54.5

Note: Income in any year is the income of the family of which the person is a member and includes money income plus Food Stamps. Shares are calculated as the average transfer ratio for each program for all persons in the decile in families receiving any cash transfer, divided by the ratio of program recipients to the total number of persons in the decile.

[1] Calculated for a subsample that includes only families receiving cash entitlements (Food Stamps, AFDC-General Assistance, or SSI) or Medicaid in 1988.

TABLE 4
Entitlements as a Share of 13-Year Average Family Income Among Recipients of Any Entitlement,’ 1976-88, by Family Income Group

Family income Decile	Entitlement Recipients as a Share of All People in Decile (%)	Average Family Income of Recipients (1995$)	Food Stamps	AFDC and GA	SSI	All Cash Entitlements	Medicaid
1 (lowest)	59.4%	$11,495	7.6%	20.0%	17.6%	27.3%	23.0%
2	47.9	20,164	3.8	9.8	6.8	13.7	7.2
3	39.8	27,480	1.7	4.2	1.8	6.0	3.6
4	29.2	33,985	1.5	2.4	0.4	4.3	3.0
5	22.9	40,672	0.9	1.6	0.2	2.7	1.6
6	16.9	46,773	0.8	1.9	0.3	3.0	1 .a
7	10.1	53,959	0.4	0.3	0.2	0.8	–
a	6.3	62,627	0.3	0.6	1.2	2.1	
9	3.3	77,312	0.2	0.5	0.4	1.1	
10	2.5	95,541	0.1	--	0.3	0.5	
Average	23.5	29,343	3.5	5.1	2.7	11.3	10.8

Note: Income in any year is the income of the family of which the person is a member and includes money income plus Food Stamps. Intermediate family income deciles are constructed based on each person’s inflation-adjusted family income averaged over the 13-year period. Shares are calculated as the average of the yearly transfer ratios for a person‘s family over the period 1976-88, divided by the ratio of program recipients to the total number of persons in the decile.

[1] Calculated for a subsample that includes only families receiving cash entitlements (Food Stamps, AFDC-General Assistance, or SSI) or Medicaid in at least one year between 1976 and 1988.

TABLE 5
Medicare Participation and Medicare Benefits as a Share of Income Among Recipients, 1988 and 1976-88, by Family Income Group

Family Income Decile	1988 Percent Receiving	1988 Income Share[1]	1976-88 Percent Receiving	1976-88 Income Share[1]
1 (lowest)	51.1%	47.9%	60.9%	18.2%
2	38.2	21.5	38.8	9.3
3	31.2	14.1	26.4	6.4
4	21.2	10.8	20.0	5.0
5	la.0	a.9	14.7	3.4
6	11.5	7.0	13.0	3.1
7	5.9	5.1	10.8	1.9
a	3.7	5.4	12.1	1.7
9	7.1	4.2	a.3	1.2
10	3.6		9.0	1.1
Average	18.8	20.7	21.0	8.6

[1] Calculated as the average transfer ratio for Medicare for all persons in the decile, divided by the ratio of program recipients to the total number of persons in the decile. Income numbers in the denominator of the transfer ratios do not include imputed Medicare benefits.

ratio. Medicare transfer ratios are presented in Table 5.

Given the strict limits on earnings and assets under the means-tested transfer programs, such transfers should make up a high proportion of total income in any given year.[4] Since transfer income is relatively meager, we would also expect that these sources of income would not be high enough to lift many recipients out of the bottom of the income distribution.

Among those who ever receive transfers, the importance of transfer income over the entire period depends on both the proportion of years of transfer receipt and the level of alternative income. The participation results above are suggestive of a substantial amount of temporary receipt of transfers. We also know from prior studies that, while a substantial proportion of those who are poor in any given year are in the midst of extended spells of poverty, the proportion of persistently poor families is fairly low (Duncan and Rodgers 1991). Therefore, we would expect high cash-transfer ratios among those persistently at the bottom of the income distribution, with a substantial dropoff in importance as we move up the intermediate-run income distribution.

Among recipients in the lowest decile of the 1988 income distribution, cash transfers equaled 46.1% of income (Table 3). Adding in Medicaid, the transfer ratio rises to over 100% for many recipients. These high ratios emphasize the level of dependency on transfers among recipients in any given year. Among recipients in the second and third deciles of 1988 income, respectively, 28.9% and

23.6% of income came from cash transfers.

Among recipients in the lowest decile of the intermediate-term income distribution, 27.3% of income came from cash entitlements (Table 4). Adding in Medicaid, the figure is close to 50%.[5] While lower than on an annual basis, these figures show the importance of entitlement income to those with persistently low incomes. Even on a 13-year basis, entitlements are still important sources of income for recipients who are in the second (20.9% of income) and third deciles (9.6% of income).

Several factors stand out when Tables 3 and 4 are compared. First, transfer ratios are substantially higher on an annual basis than on a longer-term basis. This means that for most recipients, benefits are temporary rather than permanent, and that other sources of income become more important over the longer period. Second, transfer ratios drop off more rapidly in the intermediate income distribution than in the annual income distribution. For example, the transfer ratio for all cash entitlements in the third decile of the intermediate distribution is less than half the value of the ratio in the second decile. By contrast, in the single-year distribution, the ratio in the third decile is only slightly smaller than the ratio in the second. These differences are consistent with the use of entitlements as a safety net.

Table 5 shows participation and benefits under the Medicare program. The results are shown for both a single year and for the 13-year period. Participation rates are similar, which follows from the fact that Medicare eligibility is continuous once one reaches age 65. Intermediate transfer ratios for Medicare are less than half the annual ratios, reflecting the fact that for those who turned 65 after 1976, in some of the years they were not eligible for the program.

A second reason that the 1988 transfer ratio is higher than the average transfer ratio is that Medicare benefits have been rising steadily over time. Using actual growth rates up to 1993 and projected growth rates until 1999 (CBO 1994), the real value of Medicare benefits per beneficiary will grow by 73% between 1988 and 1999. Assuming a uniform 1% rate of growth in the real income of Medicare recipients, this implies that by 1999 average Medicare benefits as a fraction of 1999 income would be 55% higher than in 1988. Overall, this would imply an average transfer ratio of 32% and a transfer ratio for the poorest elderly of 74%. For those elderly whose real income is fixed or even declining, the transfer ratios would be even higher.

THE EFFECT OF REDUCTIONS IN ENTITLEMENT PROGRAMS

The budget resolution that passed the House of Representatives would enact the following cuts in entitlements: Medicare, 22.5%; AFDC-General Assistance and Medicaid, 33%; Food Stamps, 18.6%; and SSI, 19.7%. Based on a weighted average of cuts in the cash programs, all cash entitlements are estimated to fall 23.7%. (The appendix describes the assumptions underlying these estimates of the cuts.)

In estimating the impact of these changes, it is assumed that all program cuts are passed forward to the beneficiaries of the programs. This implies that administrative savings from converting AFDC and Medicaid to block grants or otherwise increasing state discretion would be relatively small.

(Evidence from GAO studies of block grants in the 1980s suggests administrative savings of no more than 2-3% of program costs.)

The assumption that cuts in medical entitlements would be passed on to beneficiaries implies that none of these cuts will be shifted backward onto providers. While this is probably an overstatement, it seems unlikely that providers would bear a major portion of the cuts while holding access and the quality and quantity of services constant. Reimbursement rates for physicians and hospitals under Medicaid are currently relatively low, as are administrative costs. Innovations such as the Diagnostic Related Groups prospective reimbursement system under Medicare have driven reimbursements for hospitals below the cost of services delivered. The past decade's cost-containment efforts have eliminated much of the wasted spending in these programs.

Table 6 shows how the proposed reductions in cash entitlements and Medicaid would have affected different income groups in 1988 (the "single year" examined in this study). The sample is restricted to beneficiaries. Combining cash entitlements and Medicaid, families in the lowest income decile would face a cut in transfers equal to 33.8% of income, or $2,741, on average. The largest impact would come from the cuts in AFDC-GA and Medicaid, because recipients in these programs

TABLE 6
Decrease in Entitlements as a Share of 1988 Annual Income of Recipients,[1] Under the 1995 House of Representatives Budget Proposal,[2] by Family Income Group

Family Income Decile	Food Stamps	AFDC or GA	SSI	All Cash Entitlements	Medicaid
1 (lowest)	3.8%	14.0%	8.1%	10.9%	22.9%
2	2.3	9.1	7.5	6.8	10.8
3	1.8	6.6	4.2	5.6	8.3
4	1.2	3.3	--	2.2	5.0
5	–	–	–	0.9	–
6	–	–	–	1.7	--
7	–	–	–	0.5	–
8	–	–	–	0.4	--
9	–	–	–	0.7	–
10	–	–	–	–	–
Average	2.9	10.5	7.7	8.6	18.0

Note: Income in any year is the income of the family of which the person is a member and includes money income plus Food Stamps.

[1] Calculated for a subsample that includes only families receiving cash entitlements (Food Stamps, AFDC-General Assistance, or SSI) or Medicaid in 1988.

[2] Assumes the following cuts, compared to the baseline estimate for FY 2002: Medicare 22.5%; AFDC-GA and Medicaid 33%; Food Stamps 18.6%; SSI 19.7%; all cash entitlements 23.7%. See text for explanation of projected cuts.

have few other sources of income and because average expenditures are large. In the second and third deciles the combined cuts total 17.6% and 13.9% of income.

The intermediate-term impact of the proposed cuts **(Table 7)** is lower than the annual impact because relatively few beneficiaries participate in the programs in all years. Nonetheless, those in the lowest decile of 13-year income would still experience average cuts in income of 6.5% under the cash programs and 7.6% under Medicaid, for a combined cut equal to 14.1% of income, or $1,621 per year. In the lowest decile alone, 9.6 million people would be affected by the cuts. In the second decile, the cut in cash entitlements and Medicaid would be about 5% of income, affecting at least 8.6 million people. Thus, unless these changes were offset by substantial increases in market income, the proposed cuts would lead to a significant drop in the share of total income received by those at the bottom of the income distribution.

Another way of looking at the distributional impact of cuts is to classify the population by income relative to the poverty line, that is, to adjust income for a measure of family need. Among the persistently poor-those whose 13-year average incomes are below the poverty line-entitlements

TABLE 7
Decrease in Entitlements as a Share of 13-Year Income of Recipients,[1] 1976-88, Under the 1995 House of Representatives Budget Proposal,[2] by Family Income Group

Intermediate Family Income Decile	Food Stamps	AFDC or GA	SSI	All Cash Entitlements	Medicaid
1 (lowest)	1.4%	6.6%	3.5%	6.5%	7.6%
2	0.7	3.2	1.3	3.2	2.4
3	_	1.4	0.4	1.4	1.2
4	_	0.8	--	1.0	1.0
5	_	0.5	--	0.6	0.5
6	_	0.6	--	0.7	0.6
7	—	—	_	0.2	—
a	—	—	_	0.5	—
9	—	—	_	0.3	--
10	—	—	_	0.1	--
Average	0.7	1.7	0.5	2.7	3.6

Note: Income in any year is the income of the family of which the person is a member and includes money income plus Food Stamps. Intermediate family income deciles are constructed based on each person's inflation-adjusted family income averaged over the 13-year period. The transfer ratio for any person is the average of the yearly transfer ratios for a person's family over the period 1976-88. Shares are calculated as the average of the yearly transfer ratios for a person's family over the period 1976-88, divided by the ratio of program recipients to the total number of persons in the decile.

[1] Calculated for a subsample that includes only families receiving cash entitlements (Food Stamps, AFDC-General Assistance, or SSI) or Medicaid in at least one year between 1976 and 1988.

[2] Assumes the following cuts, compared to the baseline estimate for FY 2002: AFDC-GA and Medicaid 33%; Food Stamps 18.6%; SSI 19.7%; all cash entitlements 23.7%. See text for explanation of projected cuts.

provide anywhere from 60% to 100% of intermediate-run income. Over time the poorest of the poor would face cuts of 15% to 25% of their intermediate-run income.

For a number of reasons, these estimates are likely to understate the impact for low-income families of cuts in entitlements. First, because the Panel Study of Income Dynamics provides a representative sample of the U.S. population in 1968, it does not account for additional immigration after that year. Hence, the Hispanic population, among whom poverty rates and transfer recipiency are relatively high, is underrepresented in the sample. Second, the exclusion of the lowest 1% of families (to reduce the influence of very high transfer ratios due to negative reported income) eliminates at least some persistently poor families with very high transfer ratios. Third, Medicaid cuts in future years are understated because Medicaid spending has been rising faster than incomes. Finally, the sample in this analysis includes all those who participated in the programs in at least one year from 1976 to 1988. If we eliminated the very short term recipients by restricting the sample to those who receive benefits in at least two years, the increase in entitlement share, and the corresponding impact of cuts, would increase substantially.

Table 8 shows the distributional impact of projected cuts in Medicare. Because Medicare has been growing rapidly in terms of average benefits per recipient, and because Medicare recipiency is

TABLE 8
Decrease in Medicare Benefits as a Share of Annual Income of Recipients Under the 1995 House of Representatives Budget Proposal[1]

Family Income Decile	Reduction in Benefits From 1988 Levels	Reduction in Benefits From Projected 1999 Levels[2]
1 (lowest)	10.8%	16.7%
2	4.8	7.4
3	3.2	5.0
4	2.4	3.7
5	2.0	3.1
6	1.6	2.5
7	1.1	1.7
8	1.2	1.9
9	0.9	1.4
10	–	–
Average	4.7	7.3

[1] Assumes a 22.5% cut in Medicare, compared to the baseline estimate for FY 2002.
[2] Assumed to be uniformly 55% larger than the cuts from 1988 levels. This is based on actual Medicare growth rates up to 1993 and projected growth rates until 1999 (CBO 1994), implying that the real value of Medicare benefits per beneficiary will grow by 73% between 1988 and 1999. Calculation assumes a uniform 1% rate of annual growth in the real income of Medicare recipients.

continuous from age 65 until death, the 13-year average effect from 1976 to 1988 does not accurately depict the real impact of the cuts. Therefore, in addition to showing the annual reduction in income that would have occurred if the proposed 22.5% cut in Medicare had been imposed in 1988, we also show the hypothetical impact of a similar cut in 1999, using projected growth rates in Medicare and an assumed increase in average income of 1% per year.

The results show that, among the 6.7 million Medicare-eligible people in the lowest decile of the 1988 income distribution, the cuts would represent 10.8% of income in 1988 and 16.7% of income in 1999. The 1988 cut represents a loss of $928 per recipient.

CONCLUSION

By studying a large sample of families over a 13-year period, we find that participants in AFDC-GA, Food Stamps, SSI, and Medicaid who are in the lowest income decile would be subject to permanent reductions in program benefits equal to 14.1% of income. On an annual basis, the comparable cuts total 33.8% of income. In the second decile of the 13-year income distribution, the cut in cash entitlements and Medicaid would be 5.6% of income. The impact of Medicare cuts on those at the low end of the distribution is even greater. About 51.1% of persons in the bottom quintile of the annual income distribution are eligible for Medicare, and program cuts, if passed through to beneficiaries, would equal 10.8% of income in 1988 and 16.7% in 1999.

The results also indicate that substantial fractions of people, not only among the poor but also in the middle class, become eligible for entitlement benefits at some point. Participation rates in cash transfer programs in at least one year of a 13-year period ranged from 59.4% of people in the lowest intermediate-income decile to 22.9% in the fifth decile. This means that if cuts in entitlements were imposed uniformly on all recipients, whether short or intermediate term, a substantial fraction of the population would encounter at first hand the weakened safety net during periods of economic vulnerability.

November 1995

Acknowledgments. *The author would like to thank John Pepper for excellent research assistance and Max Sawicky and Edith Rasell for comments.*

APPENDIX

Sample selection

The study uses a sample from the Panel Study of Income Dynamics (PSID) to compute intermediate-run transfer ratios. The PSID is a large longitudinal survey that has followed the members of over 5,000 families since 1968. The high quality of the income data. including the dollar value of benefits received under all of the major cash entitlement programs? makes the PSID the best available data set for examining long-term benefits.

While annual studies of transfer incidence typically use the family as the basic unit of analysis, for longer-term incidence the basic unit of analysis should be the individual, since individuals may change families over time. In this study, in any year, income is the total income of the family of which the person is a member. Thus, children are included in the income unit and fully represented in the sample. It is assumed that income and expenditures are pooled equally among all members of the family unit. Therefore, at any point the resources available to any individual equal the total resources, including entitlements, of the family unit in which the individual resides. The measure of intermediate-run income used to construct income deciles is the average income of the family (or families) in which an individual lives over the 13-year period covered by our sample. If the individual stays in the same family unit over the sample period, then family and individual income are the same. If the individual passes through different family units, then intermediate-run income is the average of family income in each year.

The sampling frame consists of all families who were in the PSID in 1982. The sample is a 13-year panel constructed by following both the family head and the spouse in the 1982 families backward to 1976 and forward to 1988. It originally consisted of 10,407 individuals, but it fell to 8,265 by 1988, reflecting some sample attrition as well as nonreporting of income in a particular year. The overall proportion receiving transfers in 1988, shown in the last row of Table 1, is substantially smaller than the proportions reported using the Current Population Survey.[6] However, our interest is in the comparison between the annual and intermediate-run rates of recipiency. The analysis is conducted in terms of family income and family transfer recipiency. Many studies using the PSID select samples where the head of the household does not change over the sample period. While this simplifies analysis, it also makes the sample unrepresentative, particularly among low-income individuals. Since changes in family composition are major determinants of changes in income, it is important that inclusion or exclusion from the sample not be conditional on such changes (Bane and Ellwood 1986). Making the individual the unit of analysis avoids these selection problems.[7]

There are a number of cases of reported transfer ratios well in excess of 1. Many of these may represent underreporting of income or temporary negative incomes from business losses. To avoid the excessive impact of these ratios on the computed averages, the lowest 1% of the intermediate income distribution is excluded from the sample.

Imputation of Medicare and Medicaid benefits

While the PSID provides data on the dollar amount of benefits received under the cash programs, it indicates only eligibility for Medicaid and Medicare. To put a value on these benefits, this study imputes an annual dollar value that is equal to the average expenditure per eligible recipient under the program. This is equivalent to assigning the insurance value of the program. that is, what it would cost the individual to purchase an equivalent insurance policy. For Medicaid, separate expenditure amounts have been assigned for AFDC and SSI recipients, with the latter being substantially higher. The Medicaid assignment for AFDC recipients is a function of family size and number of children; income is defined as cash income plus Food Stamps. In computing the medical care transfer ratios, the income measure has not been adjusted to include the medical transfers. While this approach obviously overstates the transfer ratio for medical programs, there is no widely accepted procedure for valuing such transfers.[8]

Calculation of transfer ratios

For the intermediate period, the analysis in the text computes the transfer ratio as the average of the annual transfer ratios. This approach weights each year equally. Implicitly. it assumes that it is difficult for low-income people to share income over time by saving or borrowing. Evidence from the PSID suggests the importance of liquidity constraints for many low-income households (Zeldes 1989).

The alternative way of computing the transfer ratio is to divide average transfers by average income. The formula is:

$$Ratio_i = \frac{\frac{1}{13}\sum_{t=1}^{13} Transf_{it}}{\frac{1}{13}\sum_{t=1}^{13} Income_{it}}$$

In this expression, $Transf_{it}$ is the amount of the transfer received by i’s family in year t, and $Income_{it}$ is i’s family income in year t. This second way of computing the transfer ratio is equivalent to a weighted average of each year’s ratio, where the weight is annual family income relative to the total 13-year income.

The weighted transfer ratio assumes that individuals can smooth consumption over time. If a person experiences, say, three very poor years, with transfers equaling a high fraction of total income, and 10 good years, with transfers making up a smaller share of larger incomes, the good years are more heavily weighted in the calculation of the average transfer ratio. The rationale is that some of the income in the good years can be shared (through dissaving) with the low-income years. In this case the weighted average transfer ratio would be lower than the unweighted average.

Empirically, the difference between the two measures will depend on the extent to which family income varies over the period. In the extreme case, if family income in each year were identical to average family income, the two measures would be identical. However, if the pattern is one of substantial fluctuation in income, annual transfer ratios would be much higher in the low-income years than in the high-income years, and the unweighted average could be significantly higher than the weighted average. For the lowest decile of intermediate income. the unweighted average transfer share for all cash transfers is 27.3%, compared to 24.9% using the income-weighted ratio. In the second decile, the ratios are 13.7% and 10.6%: in the third they are 6.0% and 3.8%. These relatively small differences suggest that income mobility over the intermediate period analyzed in this report is not very great."

State responses

To simulate the cuts in AFDC and Medicaid, the analysis accounts not only for the projected federal cut but also for the likely state response to a switch to block grants. Every dollar of assistance in the form of a block grant is assumed to stimulate only one-third as much spending on the aided programs as a dollar of matching aid. The estimate is taken from previous studies of AFDC matching rate effects (see Chernick 1982). Studies by Inman (198.5) and Gramlich (1985) suggest that if anything the one-third estimate for block grant dollars is conservative. Gramlich stresses the role of interstate migration in dampening down welfare benefits. while Inman emphasizes that, without strong categorical restrictions, federal welfare money leaks out into other parts of the state budget.

ENDNOTES

1. Department of Economics, Hunter College, and Graduate Center, City University of New York.

2. Studies based on the Current Population Survey look at annual benefits, while monthly participation and benefits over periods ranging from one to 28 months have been analyzed using the Survey of Income and Program Participation. Annual benefit levels by income class for the various transfer programs are discussed in CBO 1994. Monthly dynamics are analyzed in Shea 1995.

3. See Bane and Ellwood 1994, chapter 2.

4. Annual data show the extreme importance of transfer income for AFDC recipients. In 1988, for example, less than 9% of AFDC families reported any earned income. See Committee on Ways and Means, U.S. House of Representatives, 199 1.

5. Recall that because the sample of recipients is not perfectly overlapping among the programs, one cannot simply add up the transfer ratios for cash entitlements and Medicaid.

6. The Congressional Budget Office reports AFDC and Food Stamp recipiency rates in 199 1 that are about double the PSID rates. See CBO 1994, Table 7.

7. The same approach is used here to analyze intermediate-run tax burdens. See Chernick and Reschovsky 1994.

8. For an extensive discussion of the difficult issues involved in valuing in-kind medical transfers, see Citro and Michael 1995.

9. See Chemick and Reschovsky 1994 for a discussion of income mobility in this same sample.

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