A DIFFERENT LOOK AT THE WELFARE TRAP: INSTITUTIONAL CAUSES AND REMEDIES

Necati Celik

Abstract: This paper investigates the institutional nexus of *Welfare Support Programs* (WSPs) in the US and households' access to social needs, particularly affordable healthcare and education. A close look at the *Survey of Consumer Finances* (SCF) reveals that households that were turned down when they applied for credit in the past are more likely to receive welfare support in the survey year. Moreover, welfare recipient households report lower status of health and lower years of education regardless of their income and demographic attributes. These results support the hypothesis that WSPs limit households' access to healthcare and education due to the institutional set-up of the two in the US. Constrained-households find themselves in the *welfare trap* because their limited access to better health care and education are reflected in their household income, pushing them further down the ladder and increasing their dependency on WSPs for subsistence. Neither the repeal nor the expansion of WSPs will solve this dilemma unless the US government enacts institutional policies to address the way higher education and health-care is provided and financed in the country. Affordability of health care and higher education should be the main target of these policies to enable households to pull themselves out of the welfare trap by finding and maintaining jobs without regressing back in to welfare support.

Keywords: welfare trap, welfare programs, credit rationing, health, U.S. households

JEL Classification Codes: I380, I10

Welfare Trap is only one of the many contradictions of welfare policies. The term denotes a welfare recipient's reluctance and/or inability to break his/her dependence on public assistance. In a situation like this, welfare support perpetuates the *dependency* of the recipient on public assistance rather than raising them to a level that they don't need assistance anymore. There are two different views on why recipients can get stuck in welfare trap (Fraser & Gordon 1994). The first one takes a behavioral approach and explains that welfare trap is caused by recipients' lack of necessary traits to climb the socio-economic ladder. Lack of these traits might be associated with individual psychology or social environment. According to this view, being in welfare trap is a result of the mistakes recipients make over and over again in their decisions. The other view is a direct reflection of economic orthodoxy and suggests that welfare trap is a result of an economic optimization individuals make when they face the choices of receiving benefits or joining the workforce. Individuals deliberately choose to receive benefits instead of finding employment because the cost of working is too high compared to the minimal pay they get when they cannot work and receive public assistance. In other words, welfare support is a *disincentive* to work. Unlike the other view, individuals are seen as *rational man*, not inadequate individuals.

What follows is a discussion of institutional factors that make it harder for a recipient to break free from welfare trap, which are overlooked in the literature. First, a brief survey of how previous studies looked at participation in welfare programs will be presented. Then, the relation between welfare participation and household credit constraints and also the relation between welfare participation and household health will be investigated.

Who Receives Welfare Support?

The literature on the determinants of welfare participation is not diverse, which allows some degree of consensus among the researchers. All of these studies develop a model based on the premise that households try to maximize utility in their decision to participate in a welfare program (Barr & Hall 1981, Moffitt 1983 and Ashenfelter 1983). In these models, work is naturally *irksome* and welfare receipt is an alternative to it. Therefore, all of these studies conclude that the amount of benefits positively and significantly determine a household's participation in a welfare program (Moffitt 1992). Moreover, despite the mixed results on the significance, household wage appears to share the same negative sign in most of these studies (Table 6 in Moffitt 1992: 20). Of course, there are other non-financial factors that are taken into account in these studies, such as race, gender, education, health and marital status of the household heads, but for the sake of the neoclassical argument these studies attempt to make, these variables are of trivial importance at best.

Although elegant in presentation, there is a practical problem in these models. Not all eligible households participate in welfare programs. This common aspect of welfare participation is due to three causes, which are often discussed in the literature. First, there is the issue of *welfare stigma*. There is ample evidence to support the existence of social stigma associated with welfare assistance (Horan and Austin 1974, Nichols-Casebolt 1986, Jarrett 1996, Ranney & Kushman 1987, Stuber & Kronebusch 2004 and Stuber & Schlesinger 2006). The fact that some eligible households chose not to participate in a welfare program, due to perception of welfare stigma, is partly addressed by Moffitt (1983) in a utility maximizing framework. Yet, there are other reasons that prevent households from participating in a program for which they are eligible, such as simple unawareness, the unobserved costs of filing, or complying with the program. None of these models considered the process of receiving welfare assistance as a multi-step ordeal, in which awareness, eligibility, participation, acceptance and enrollment are different stages (Heckman & Smith 2004). Therefore, the result that the amount of benefit in a welfare program is a positive determinant of participation is a biased one, because the households that don't participate in a program (dependent variable = 0) are likely to be eligible but unaware of the program, hence also unaware of the amount of benefits. On the other hand, participation means awareness of the program, therefore awareness of the amount of benefits. This is a simple issue of adverse selection, which all of these models ignore.

Another issue with these models is that they rarely explain how non-financial factors such as race, gender, health and education, and also some financial factors other than family income, such as assets and credit constraints, affect the participation of a household. The main problem, however, is that receiving welfare is seen as an individual rational choice based on perfect information. In fact, receiving welfare assistance is predominantly a matter of need rather than a choice.

The table below presents data from 2013 SCF. The year selection is to avoid any recession-related bias in the empirical findings that might have existed in the 2010 dataset. Also, 2013 is the most recent dataset on US household finances that is currently available.

Table 1. Characteristics of Welfare Recipients

	welfare=0	welfare=1	Total
inonwelfare	95.678	2.260	84.443
asset	995.790	3.716	876.344
age	52.664	45.090	51.753
race	0.770	0.484	0.736
gender	0.799	0.503	0.763
children	0.783	1.260	0.840
married	0.591	0.210	0.545
cohabit	0.068	0.178	0.082
educ	14.228	12.003	13.961
health	3.081	2.530	3.015
college	0.602	0.165	0.549
insurance	0.908	0.882	0.905
emppart	0.661	0.347	0.623
empfull	0.088	0.136	0.093
crationed	0.165	0.450	0.189
creditlimit	4.212	0.155	3.724

Source: 2013 SCF, Federal Reserve
Note: Please see Table 3 at the end for descriptions of the variables.

On average, welfare recipients (*welfare*=1) have less before-tax non-welfare income (*incnonwelfare*) and less financial assets (*asset*) for obvious reasons. In order to be eligible for welfare assistance, a household should have limited resources and income. To be eligible for TANF cash assistance for instance, household income for a family of three had to be less than $9,353[1] a year on average for 48 contiguous states and the District of Columbia in 2012. This was roughly 49% of the federal poverty guideline for a family of three in that year[2]. Only in Wisconsin, the income requirement, which was $21,948 per year, was actually above the poverty guideline in 2012 (Falk 2014). There are also asset limits for households to be eligible for TANF in many states, except Alabama, Colorado, Louisiana, Maryland, Ohio and Virginia. For the rest of the states, asset limit ranges from $10,000 in DE to $1,000 in Georgia, Indiana, Missouri, New Hampshire, Oklahoma, Pennsylvania, Rhode Island, Texas and

[1] Calculated based on Table A-1 in Falk (2014).
[2] Based on U.S. Department of Health and Human Services (HHS) poverty guidelines in 2012.

Washington. In most states, one vehicle per household is not considered an asset, whereas in some states, only a portion of the vehicle value is excluded. The house that the household is residing in is again not considered in the asset limit.

Participants of welfare programs appear to be younger on average (*age*) and have more children (*children*), which are results consistent with the literature and need little explanation. Similarly, recipients are more likely to be non-white (*race*=0), and also female (*gender*=0). Both of these variables appear to be significant factors increasing the probability of receiving welfare support in the literature. The reasons for this fact are often overlooked. This could be an evidence of non-income related obstacles female and non-white recipients have to face in the welfare participation process (Monnat 2010 & 2010, Keiser *et al.* 2004 and Gooden 2004).

Another consistent finding is that welfare recipients are less likely to be married (*married=1*), but more likely to cohabit (*cohabit=1*) with a partner. Welfare programs have neither a clear definition of marital arrangements of households nor requirements specifically referring to these arrangements. Given the liberty given to states in managing programs such as TANF and SNAP, the way different marital arrangements are considered in a program can vary significantly across the states (Moffitt *et al.,* 2009). Despite this variation, it is still possible to distinguish a standalone affect of marital status on welfare dependency for two main reasons. First, TANF has often been argued to create a disincentive for marriage and an incentive to cohabit with a partner, which is also called "Marriage Penalty" in the literature (Moffitt *et al.* 2009 and Alm *et al.* 1999). If such an effect exists, married couples will be less likely to receive benefit or will receive less benefit than the couples that are not married but living together, or single parent households.

Of course, these descriptive statistics have little explanatory power if any. These variables can be plugged into a multivariate regression to analyze the isolated effects of each one of them. However, in order to do so, a concise model for household decision for welfare participation should be constructed first. As pointed out earlier, this model should take into account the multi-step process for participation in a welfare program. Even after doing so, there exists a greater problem that needs to be solved. Participation in welfare programs has important implications for participants' health and access to credit. And it is the *circular causation* between welfare participation and household health, also between welfare participation and household credit constraints that will be discussed in the following sections.

The Welfare-Credit Nexus

The effects of asset-tested public assistance programs on household saving behavior have grabbed significant attention in the literature (Ziliak 2003). However, the repercussions of welfare program participation on households' access to credit have not been a prevalent topic. A few studies mention program participation as a possible factor that can reduce household access to credit markets (Duca & Rosenthal 1991 & 1993, Duca & Whitesell 1995 and Chakravarty & Scott 1998). These studies use SCF households as their sample and share similar conclusions on the sign and the significance of their coefficients. However, a careful look at the questions asked in the survey would reveal a fundamental mistake in their model selection. The following question is asked to households in SCF: “In the past five years, has a particular lender or creditor turned down any request you (or your husband/wife/partner) made for credit, or not given you as much credit as you applied for?” If a household answered “yes” to this question and either didn’t reapply credit or reapplied with no luck, that household is defined as *credit-rationed.* A household is defined as a welfare recipient if they received some sort of public assistance in the survey year. If a household was credit-rationed in any year preceding the survey year, participating in a welfare program can’t technically be a factor that may have affected their access to credit. But then, how can we find evidence of such a relation in SCF?

Luckily, SCF conducted a panel survey in 2009 amongst the households that were surveyed in 2007. The question in 2009 asked: “In the past two years, has a particular lender or creditor turned down any request you (or your husband/wife/partner) made for credit, or not given you as much credit as you applied for?” The way this question is asked in the panel survey opens the door for some interesting inference. If a household received welfare assistance in 2007 and was also credit-rationed in 2009, there might be a statistical relation between these. Looking at the panel survey reveals that 1,005 of 1,343 welfare recipients in 2007 also received welfare support in 2009. A household that received welfare support in 2007 is around 30% more likely to be credit rationed in 2009. This finding suggests an important conclusion. It appears that welfare recipient households, because of reasons other than their limited income and assets, have more restricted access to credit than the non-recipient households. Although the reasons for this are too crucial to overlook, I will leave this discussion for another study and only ask the following question: “Could lending agencies be discriminating against welfare program participants?”

The Welfare-Health Nexus

Studies in the literature show that participation in welfare programs is socially stigmatized in the society in different ways (Stuber & Kronebusch 2004), at varying degrees for different programs (Ranney & Kushman 1987) and for different groups of participants (Jarrett 1996 and Stuber & Schlesinger 2006). Although stigma is perceived at varying degrees depending on the social situation participant is in, and participants’ cultural history, it exists for every welfare recipient (Rogers-Dillon 1995). The negative effects of the stigmatization on the psychological well being of participants are documented in various studies (Nichols-Casebolt 1986, O’Campo & Rojas-Smith 1998, Jayakody & Stauffer 2000 and Petterson & Friel 2008). These negative effects also tend to perpetuate in the post-participation years, further aggravating recipients’ socio-economic hardship (Danziger *et al.* 2008).

The descriptive statistics from the 2013 survey showed that welfare recipients have lower health status than non-recipients. Even after controlling for other factors in a multivariate estimation, health status appears to be a significant predictor of program participation[3]. However, it is difficult to deduce any causality from this information. The panel survey, on the other hand, can provide some evidence for causality. 338 of 1,005 households who received welfare support in 2007 left welfare in 2009. These households have improved health status (2.54) on average compared to those who stayed on a welfare program (2.49). 610 households that didn't participate in welfare programs in 2007 but enrolled in 2009 saw a slight worsening of their health status on average from 2.68 to 2.69. 17,332 households who didn't receive welfare support in any year had a significantly higher health status than any other group (3.18).

A multivariate regression will provide better support for the isolated impact of welfare program participation on household health. The results from the estimation of a simple regression model are presented below. Leaving any concern about the model selection, fit and reliability aside, the results show one simple thing: participation in welfare programs decreases the household self-reported health status on average when other variables are controlled. Another important result is that being credit-rationed has also a statistically significant negative impact on household health.

Table 2. OLS Estimation Results, Dependent Variable: *Health 09*

income09	0.000***
empfull09	0.237***
emppart09	0.180***
race	0.136***
gender	0.089***
children09	-0.001
age09	-0.004***
smoker09	-0.224***
educ09	0.060***
insurance09	-0.104***
welfare07	-0.083
welfare09	-0.149***
crationed09	-0.091***
Constant	2.316***
Observations	7,149
R-squared	0.168

Source: 2007-09 Panel SCF, Federal Reserve
*Note: *** $p<0.01$, ** $p<0.05$, * $p<0.1$*

Conclusion

Participating in a welfare program and staying in it are often understood as *rational choices* households make in order to maximize utility and minimize pain, which is often associated with work effort. Therefore, it is only second nature to suggest that

[3] The results for this regression are not presented here.

households will choose to stay in a welfare program if they think that it brings them more utility to receive benefits and not work as much, than not receive benefits because they worked more and had higher income. According to this line of logic, welfare trap exists because the welfare system is full of disincentives for households to increase their work effort in order to keep on receiving benefits.

The findings of this study provide support for a different approach to the issue of welfare trap. It appears that households' access to credit and health, besides many other important factors, can significantly affect whether or not they will need and participate in welfare programs. Moreover, households on welfare programs suffer negative health consequences, even after they stop participating in programs, and also their access to credit worsens during their welfare spells. Poor health is no doubt a great obstacle for the poor in their effort to find jobs. In that regard, receiving welfare support is a self-perpetuating situation for many participants. Likewise, with their limited access to credit, welfare recipient households will also have restricted access to crucial resources they can use to improve their health and other socio-economic conditions such as education.

These findings by no means suggest that the welfare system is what causes the poor to stay in welfare. The welfare system in the U.S., despite its chronic problems that need to be addressed, is the only means of survival for many in need. To the contrary, what causes welfare trap is the way basic necessities are provided in the U.S. health care, for instance, has been growing to be a predominantly debt-financed necessity. Although there are programs such as Medicaid to address the health issues of the poor, the limited coverage it provides and the strict eligibility qualifications are still leaving a gap to be paid out-of-pocket. This is the point where having a credit card is the only help many people can get. However, with restricted access to credit, many welfare recipients can't get that help either.

In order to solve the welfare dependency or welfare trap of the poor, health care should be made more affordable, especially for the higher risk groups with limited resources. As long as health care is expensive and requires borrowing to finance, it will perpetuate the problem. Another necessity is education, which is not discussed in this study. The findings of this showed that welfare recipients are more than 40% less likely to have a college degree. Again, there are federal grants for low-income students, but it is not enough to make higher education a possibility for many participants of welfare programs. This is also an intergenerational issue. Studies show that children of welfare recipients receive less education, which is an important factor that creates intergenerational dependency on welfare (Ku, 2001 and Ku & Plotnick, 2003). Better health and better education are two fundamental conditions that improve one's possibility to find a job and keep it. Only one of these conditions is covered in this study in depth because the topic of education requires a separate study. Without improving access of the poor to better health and education, any public policy will remain short of solving the problem of welfare trap.

Table 3. Descriptions of Variables

age	Age of the household head in 2013 (Number of years)
age09	Age of the household head in 2009 (Number of years)
asset	Paper assets of the household in 2013, excluding residential property and vehicles (10,000$)
children	Number of children in the primary economic unit in 2013
children09	Number of children in the primary economic unit in 2009
cohabit	=1 if household head cohabits with a partner in 2013, =0 otherwise
college	=1 if household head has college degree in 2013, =0 otherwise
crationed	=1 if household is turned down for credit or couldn't obtain the desired amount in the five years prior to 2013, =0 otherwise
crationed09	=1 if household is turned down for credit or couldn't obtain the desired amount in the two years prior to 2009, =0 otherwise
creditlimit	The total credit limit on the credit cards the household has in 2013 ($)
educ	Years of education for the household in 2013, averaged for married and cohabiting couples
educ09	Years of education for the household in 2009, averaged for married and cohabiting couples
empfull	=1 if household head is employed full-time in 2013, =0 otherwise
empfull09	=1 if household head is employed full-time in 2009, =0 otherwise
emppart	=1 if household head is employed part-time in 2013, =0 otherwise
emppart09	=1 if household head is employed part-time in 2009 =0 otherwise
gender	Gender of the household head, =1 if male, =0 otherwise
health	Health status index (1-4) for the household in 2013, averaged for married and cohabiting couples
health09	Health status index (1-4) for the household in 2009, averaged for married and cohabiting couples
income09	Before-tax income of the household from all sources in 2009 (10,000$)
inonwelfare	Total income of the household from sources other than welfare assistance in 2013 (10,000$)
insurance	=1 if at least one person is covered by some kind of health insurance in the household in 2013, =0 otherwise
insurance09	=1 if at least one person is covered by some kind of health insurance in the household in 2009, =0 otherwise
married	=1 if household head is living with a spouse in 2013, =0 otherwise
race	Race of the household head, =1 if white, =0 otherwise
smoker09	=1 if either household head or the spouse/partner was a smoker in 2009, =0 otherwise
welfare	=1 if household received welfare assistance such as TANF, SSI or SNAP in 2013, =0 otherwise
welfare07	=1 if household received welfare assistance such as TANF, SSI or SNAP in 2007, =0 otherwise
welfare09	=1 if household received welfare assistance such as TANF, SSI or SNAP in 2009, =0 otherwise

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