Benefit Cliffs and Disincentives to Work in West Virginia

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CARDINAL INSTITUTE
FOR WEST VIRGINIA POLICY

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Author Biography

Jessi Troyan is the Director of Policy & Research for the Cardinal Institute for West Virginia Policy and was raised in Pinch, WV. She graduated from West Virginia University in 2011 with a Bachelor's degree in economics and a minor in Spanish. She received both her Master's & PhD in economics from George Mason University.

She is a guest host of the Forgotten America podcast, and her writing can be found in the *National Review* and the *Charleston Gazette-Mail*.

Brief History of Social Safety Nets in the United States

The earliest origins of social welfare policies in the United States are rooted in communities. Friends and neighbors would assist one another in times of need. Should needs throughout the community surpass what friends and neighbors could provide, local villages and towns rose to the occasion to offer that relief. Overwhelmingly, these programs were relatively small-scale and locally-led efforts. Where programs were more widespread and supported by the federal government, they were primarily related to supporting veterans and their families.[i]

The onset of the Great Depression and corresponding economic strife put these locally-driven social welfare policies on the precipice of catastrophe. Throughout the country, the levels of need were so dire that states and local communities lacked the resources to handle the magnitude of need. Under the presidential administration of Franklin D. Roosevelt, the federal government became a major player in social welfare programs through legislation passed in the New Deal.

Among the most important of these New Deal programs, and surely the most enduring, is the Social Security Act. As passed in 1935, the legislation marked the beginning of the federal government taking on the responsibility of ensuring a level of economic security for elderly, disabled, dependent children, and temporarily unemployed populations.

The size and scope of economic security and poverty alleviation efforts continued to grow throughout successive administrations. The National School Lunch Program (NSLP) began in the Truman administration. The Supplemental Nutrition Assistance Program (SNAP) began as a pilot program during the Kennedy administration and was made permanent during the subsequent Johnson administration in 1964.

In particular, President Lyndon B. Johnson's declaration of a war on poverty and the implementation of the Great Society programs: Medicare, Medicaid, the School Breakfast Program (SBP), and the Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) further expanded and cemented the role of government in the social safety net we know today.

Further efforts throughout the 20th and 21st centuries have, again, broadened the vast apparatus of government assistance. The Supplemental Security Income (SSI) program, a means-tested program providing cash payments to disabled children, disabled adults, and individuals aged 65 and older, was introduced during the Nixon administration. The Ford administration added the federal Earned Income Tax Credit (EITC) and Section 8 Housing programs to the safety net apparatus. The Low Income Home Energy Assistance Program (LIHEAP) was a product of the Reagan administration. The Child Care and Development Block Grant program was implemented under George H.W. Bush. The Clinton Administration further expanded the safety net through the Additional Child Tax Credit and Children's Health Insurance Program (CHIP). It also replaced the Depression-era Aid to Families with Dependent Children program with the Temporary Assistance for Needy Families (TANF) program.

The most recent programmatic expansions to the safety net include the Patient Protection and Affordable Care Act (ACA) under the Obama administration and the corresponding Health Insurance Exchange Premium tax credit.

Incentive Structures

As the size and scope of social safety net programs have grown, there is no question that low-income individuals and families enjoy a better standard of material well-being. When evaluated in terms of engagement with President Johnson's declaration of a War on Poverty, these efforts have been almost wholly successful.[ii] While the social safety net means that abject poverty is mostly unknown in the United States, questions remain about the effectiveness of these programs from the perspective of helping these individuals and families reach a greater level of self-sufficiency through work. Due to perverse incentives, the safety net has the capacity to trap individuals who would otherwise become self-sufficient.

The disjointed nature of programs throughout the social safety net has led to unintended consequences and disincentives for individuals to realize true economic self-sufficiency and stability for themselves and their families. Primarily, this works by distorting the relationship between work and income. Absent any sort of assistance program, an individual earns more by working harder or smarter. The introduction of assistance programs leads to a state of the world where income is not directly related to work.

One such example is known as a “benefits cliff.” In this scenario, a small rise in income results in a loss of assistance that surpasses the increase in earnings. Often, this discrepancy is vast, leading to the use of the “cliff” metaphor, rather than something like a step-down. In the face of such a scenario, it is a rational decision on the part of the individual to pass on additional hours worked, pay raises, or promotions to preserve the current material standard of living.

West Virginia Landscape

To set the stage for examining these benefit cliffs, we need an appreciation of the underlying demographics in West Virginia. The state’s population is 1,775,156. Among that population, 17.9% are in poverty, or nearly 318,000. The median household income is $50,884. Per capita income, in 2021, was $28,761.[iii] The labor force participation rate in September 2023 was 55.1%.[iv]

Wages in West Virginia, according to the May 2022 State Occupational and Wage Estimates from the Bureau of Labor Statistics, across all occupations are:

	Hourly	**Annual**
Mean	**$23.64**	**$49,170**
10th Percentile	**$10.55**	**$21,940**
25th Percentile	**$13.30**	**$24,670**
50th Percentile	**$18.16**	**$37,770**
75th Percentile	**$28.09**	**$58,420**
90th Percentile	**$40.32**	**$83,870**

Modeling Benefit Cliffs

To demonstrate the impact of assistance programs on the material well-being of individuals and families, I use the Benefits Cliffs v2 model developed by the Georgia Center for Opportunity. The model factors in over 16 local, state, and federal benefits programs. Likewise, it accounts for earnings after non-refundable taxes.

In the modeling, these programs are condensed into eight assistance categories. These include and are denoted in the model as Refundable Tax Credits, Cash Assistance, Food Assistance, the Health Insurance Exchange (HIX) Premium Tax Credit, Medical Assistance, Child Care Subsidy Final, Section 8 Housing Entry, and Section 8 Housing Extended. The Section 8 Housing program is separated into "entry" and "extended" to show the difference between when a family would be income eligible, but often not able to even get on the waiting list for this assistance, and the extent to which they would receive assistance once they were selected to receive a housing voucher and are in the program.

For refundable tax credits, the sub-categories include the federal and state EITC and child tax credits. For purposes of this discussion, West Virginia lacks a state EITC. Therefore, only the federal EITC and federal child tax credits are applicable to any scenario considered in the Mountain State. These are determined at the federal level, and there is no influence state-level policy has on these programs.

In terms of cash assistance, the subcategories include TANF and the Low Income Home Energy Assistance Program (LIHEAP). The amount of cash grants from the TANF program is determined by the states, whereas LIHEAP is a federal program that is administered by the states.

Food assistance is modeled through three programs: SNAP, WIC, and the school breakfast and lunch programs. All three of these are federal programs administered by the states.

The HIX Premium tax credit is a federal refundable tax credit dedicated to offsetting the purchase of health insurance on the individual Health Insurance Exchange.

Medical assistance consists of Medicaid and the Child Health Insurance Program (CHIP). Both are joint state-federal programs that provide healthcare coverage. Medicaid focuses on the elderly, disabled individuals, and low-income populations. CHIP provides the same benefits to children who are unable to receive Medicaid.

The child-care subsidies can be either partially or fully funded by federal grants and are focused on providing that assistance to low-income families.

Section 8 housing assistance provides vouchers for rental assistance in specified properties. The vouchers are provided by the federal government but administered by public housing agencies or the states. The entry vouchers provide housing assistance for people up to the income level of eligibility, and the extended vouchers provide assistance for individuals who may surpass the income eligibility limits but nonetheless are benefitting from past eligibility and selection to participate in the program. Among all the programs, Section 8 housing is perhaps the least likely for an eligible individual to receive as demand for housing assistance generally far outstrips the supply – both in terms of funding and housing availability.

Snapshot of the Typical Recipient of Assistance

All Assistance Programs

Here, I consider the scenario of a single mother, 30 years old, of two children in West Virginia. Statistically speaking, this is the likely representative of an individual who is receiving government assistance.[v] She earns at the 10th percentile in wages ($10.55 hourly, $21,940 annually) while working full time, 40 hours per week (2080 hours per year), and receiving no employer-sponsored health insurance. One child is 5 years old and attending school; the other is 2 years old. Both children live with and are taken care of by the mother. Neither child is disabled. As a full-time worker, the mother relies on a formal child-care setting. Within the model specifications, I chose a 'Tier 2' rate category. Figure 1 shows the full scope of assistance she is eligible to receive and illustrates where she and her family encounter benefit cliffs.

The scenario-year chosen in the model is 2023 to minimize the impact of COVID-19 era policies that extended the assistance available to those experiencing economic hardship. This decision minimizes the likelihood that cliffs and other disincentives for work are exaggerated, particularly through child-care subsidies.

While the model offers county-by-county analysis, for simplification, I consider only the 'Statewide Average' scenario.

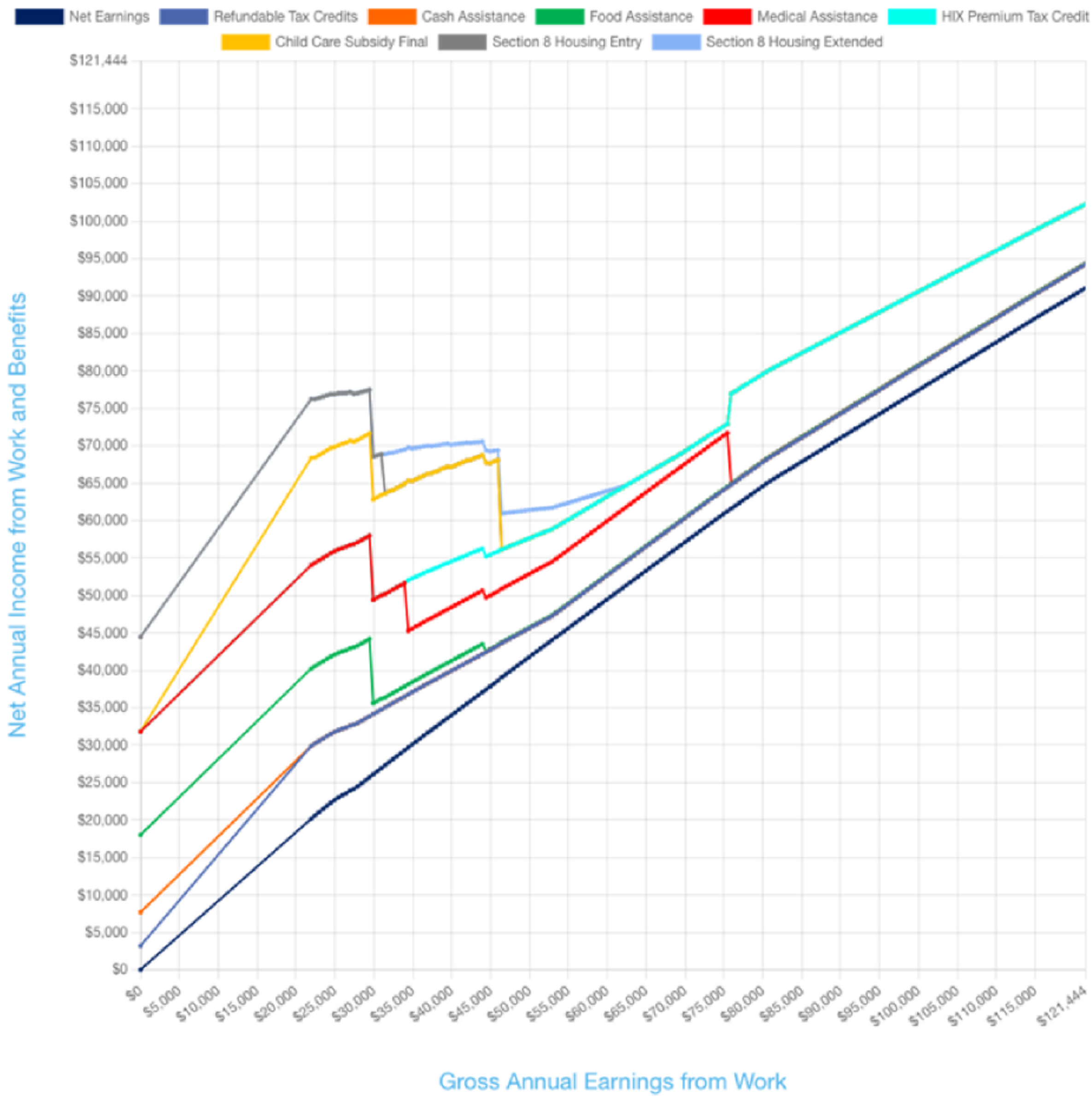

Figure 1: Benefit Cliffs Scenario, All Modeled Assistance Programs

In this scenario, we can quickly observe that even in the absence of any work and earnings, this mother can receive nearly $45,000 in assistance for herself and her children through social safety net programs.[1] As she transitions from no work to working full-time, we can see that her and her family's material well-being increases with increased earnings until just before she hits $30,000 in gross earnings.[2] Beyond that point, the graph illustrates a sharp drop in material well-being. In fact, the drop is so large that she does not re-attain that same level of material well-being until her gross annual earnings surpass $75,000.[3]

[1] Exact total is $44,454.
[2] The cliff occurs between $29,444 and $29,944 in gross earnings, or hourly wages between $14.16 and $14.40 for a 40-hour work week.
[3] The break-even point is between $76,944 and $77,444 in gross earnings, or between hourly wages of $36.99 and $37.23.

The three particular categories where cliffs occur are food assistance, medical assistance, and child-care subsidies. In the case of medical assistance, the cliff is offset by the introduction of the HIX Premium Tax Credits around the $35,000 level of gross annual earnings.[4] However, that is only applicable if the mother opts into purchasing healthcare coverage on the individual exchange.

This fall in material well-being does not occur all at once. Nonetheless, the combination of the various assistance programs along with the assortment of cutoffs among those programs results in a scenario where the single mother in question encounters other cliffs as she continues to advance and earn more income.

The first cliff she encounters is with food assistance (the green line) as she approaches $30,000 in gross earnings. As she approaches $45,000 in gross earnings, she encounters another, smaller, food assistance cliff.[5] Shortly after surpassing that same $45,000 in gross earnings, she encounters the child-care subsidy (yellow line) cliff.[6]

To simplify and disentangle the analysis, the following three sections will examine each of these assistance categories individually. First food, then medical, then child care. In all the following scenarios, the refundable child tax credits and federal EITC are included. The consideration of HIX Premium Tax Credits is omitted in this stage of examination.

A fourth section will follow that examines the entirety of health care assistance by incorporating the medical assistance programs as well as the HIX Premium tax credits to demonstrate the interplay between the two forms of assistance.

Food Assistance

To better illuminate the details illustrated in the previous section, Figure 2 simplifies the scope of assistance and considers only the refundable tax credits and food assistance (SNAP, WIC, and School Breakfast and Lunch Programs) this mother is eligible for.

Thanks to the isolation of the food assistance programs, we can more easily identify the number of cliffs, respective magnitudes, and track the “break-even” earnings to return to that prior material standard of well-being.

[4] Eligibility for HIX Premium Tax Credits occurs between $33,944 and $34,444 in gross earnings, or between hourly wages of $16.32 and $16.56.

[5] The second food assistance cliff occurs between $43,944 and $44,444 in gross earnings, or hourly wages of $21.13 and $21.37.

[6] Child-care subsidy cliff occurs between $45,944 and $46,555 in gross income, or hourly wages of $22.09 to $22.33.

In the graph, we can clearly see the major and minor food assistance cliffs that occur. The major cliff occurs as the mother moves between $29,444 and $29,944 in gross annual earnings, or between earning $14.16 and $14.40 per hour. As her earnings rise within this range, she goes from receiving $10,325 in food assistance per year to only $1,445.

Put differently, with a mere $500 in additional annual earnings or a $0.24 hourly raise, she loses $8,880 worth of food assistance per year. To cover that loss, she would need an additional $4.27 per hour in post-tax earnings to break even at this major food assistance cliff.
However, that is not the only cliff. She encounters a second, minor, cliff as she goes from $43,944 to $44,444 in gross annual earnings, or between $21.13 and $21.27 per hour. In this minor cliff, she goes from receiving $1,445 in annual food assistance to only $114. To cover this loss would require an additional $0.59 per hour in post-tax earnings.

Considered as a whole, this mother faces a clear disincentive for professional advancement. As her earnings take her to the precipice of the first cliff, her family does not again reach the same level of material well-being until her gross annual earnings reach between $46,944 and $47,444 or her hourly wage is between $22.57 and $22.81.

Based on food assistance alone, this mother is faced with a choice as she nears $30,000 in annual earnings. She can opt to professionally stagnate to preserve the assistance her family receives, or she can forge onward under a lower level of material well-being for herself and her family until her earnings increase by over 50%.

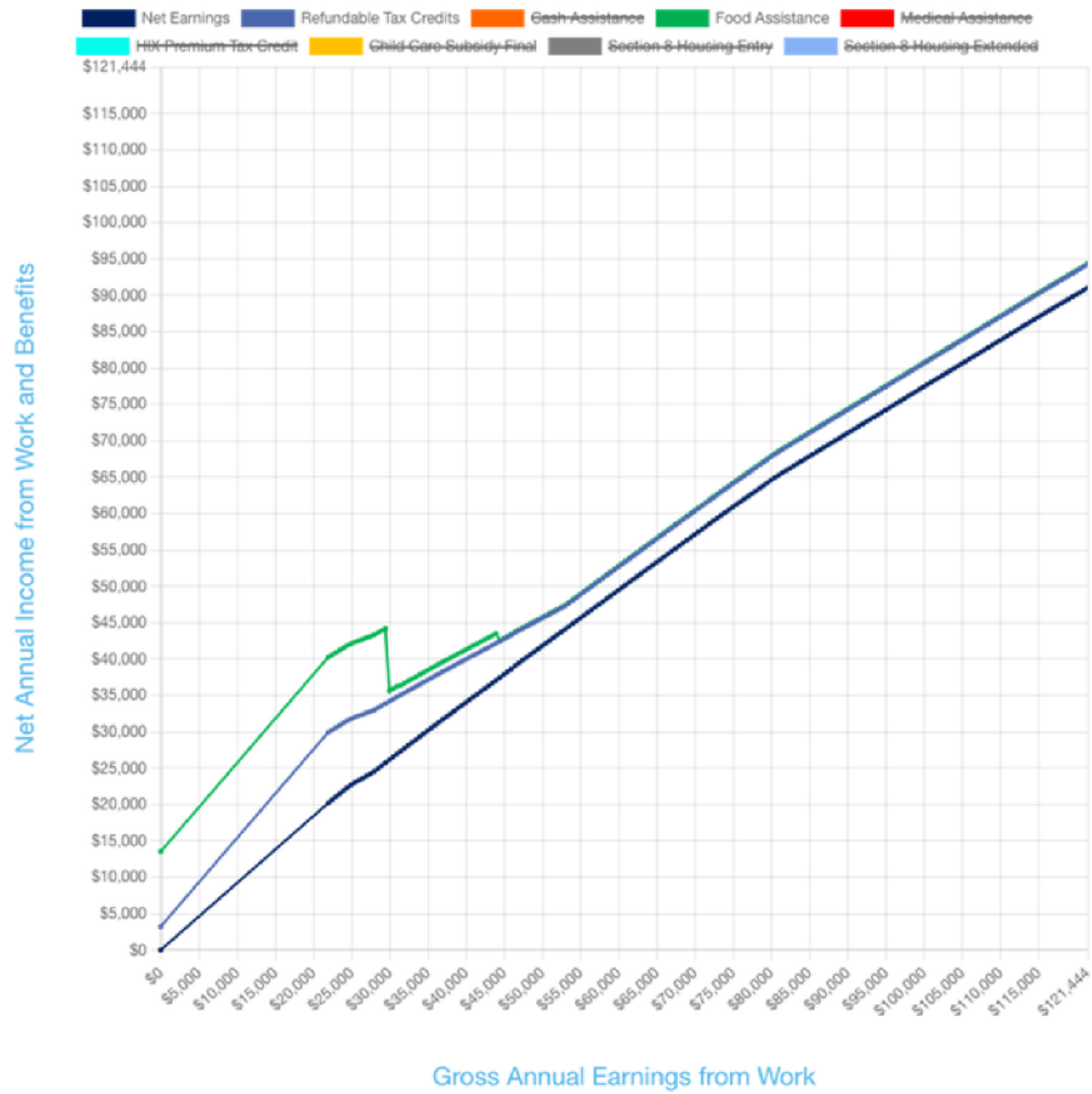

Figure 2: Food Assistance and Refundable Tax Credits

Medical Assistance

Like in the previous section, Figure 3 depicts a clearer demonstration of where the cliffs occur with medical assistance (Medicaid and CHIP). In this case, though, both cliffs are of significant magnitude.

The first cliff occurs as her gross earnings rise from $33,944 to $34,444 annually, or $16.32 to $16.56 hourly. Here, she goes from receiving $13,807 to $7,151 in annual medical assistance. This means an additional $500 in gross annual earnings results in a $6,656 loss of annual medical assistance. To cover that loss, she would need another $3.20 in post-tax earnings to preserve that standard of material well-being. In annual gross earnings, she does not break even until she is making between $45,444 and $45,944, or about 33% more.

However, this is not the only cliff she experiences with the medical assistance programs considered in the model. A second cliff occurs as she reaches between $75,444 and $75,944 in gross annual earnings, or between $36.27 and $36.51 hourly. As she crosses this threshold, she goes from receiving $7,151 to $0 in medical assistance. Here, she would need to make an additional $3.44 in hourly post-tax wages to break even and does not reach the same level of material well-being until her gross annual income is between $85,444 and $85,944, or between $41.08 and $41.32 hourly.

Again, she faces disincentives for professional advancement and faces a difficult scenario where she can either choose to stagnate or forge on despite the material difficulties her family may face.

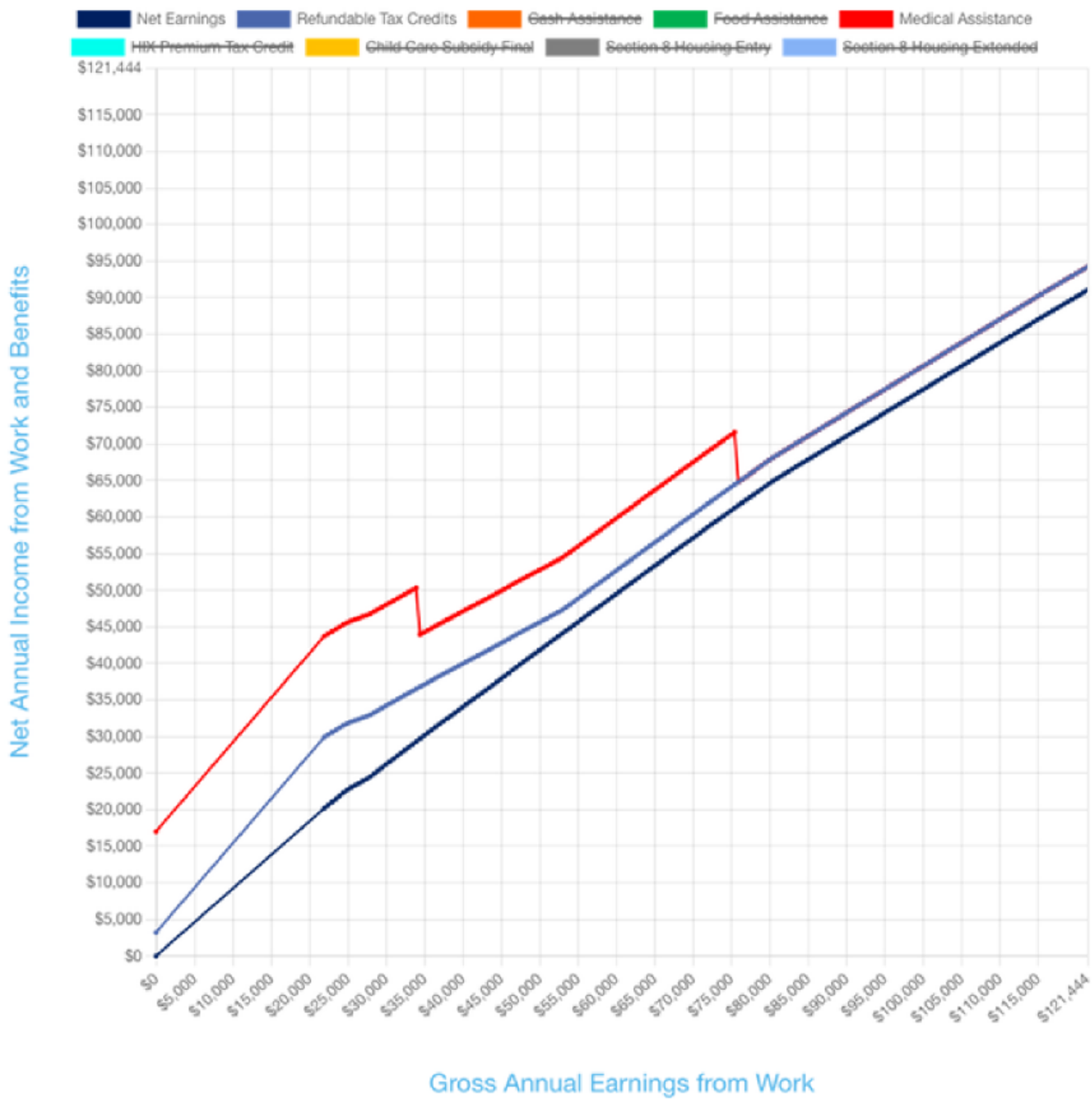

Figure 3: Medical Assistance and Refundable Tax Credits

Child-Care Assistance

Figure 4 depicts assistance through the child-care subsidy. The graph demonstrates that the level of child-care assistance through the subsidy is mostly constant throughout the eligibility range but drops to zero as soon as the income limit is surpassed.

This cliff occurs as the mother's gross annual income moves from $45,944 to $46,444, or $22.09 to $22.33 in hourly wages. As she crosses that threshold, her child-care assistance goes from $12,227 to $0. In order to cover the loss from the child-care subsidy cliff, she would need to earn another $5.88 per hour in post-tax wages. She does not again reach the same standard of material well-being until her gross annual earnings are between $63,444 and $63,944.

Once again, this mother is faced with a difficult set of options and a strong disincentive to engage in more work as her income approaches $46,000. She can opt for stagnation at that level to preserve over $1,000 per month in child-care assistance or continue advancing in her career at the cost of material well-being for her family.

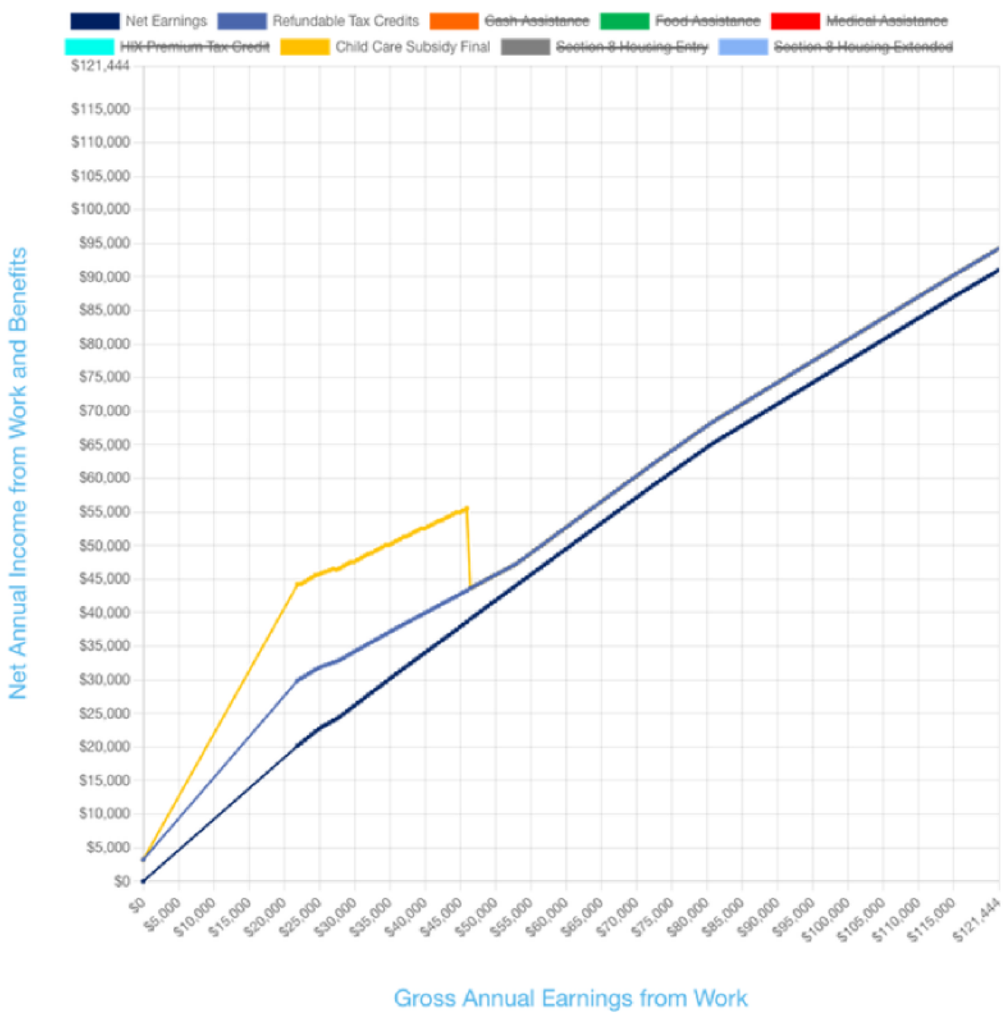

Figure 4: Child-Care Assistance Only

Medical Assistance and HIX Premium Tax Credits

As a quick demonstration of the claim made in the ‘All Assistance Programs’ section above, Figure 5 depicts the lack of cliff in health coverage when Medicaid, CHIP, and HIX Premium subsidies are all considered and used. Where earlier discussion noted the first medical assistance cliff around $34,000, we can see that the mother in question becomes eligible for HIX Premium tax credits at the same income level.

In using both medical assistance programs and the HIX Premium tax credits, she avoids any scenario where a small raise will result in a loss of assistance that exceeds her additional earnings.

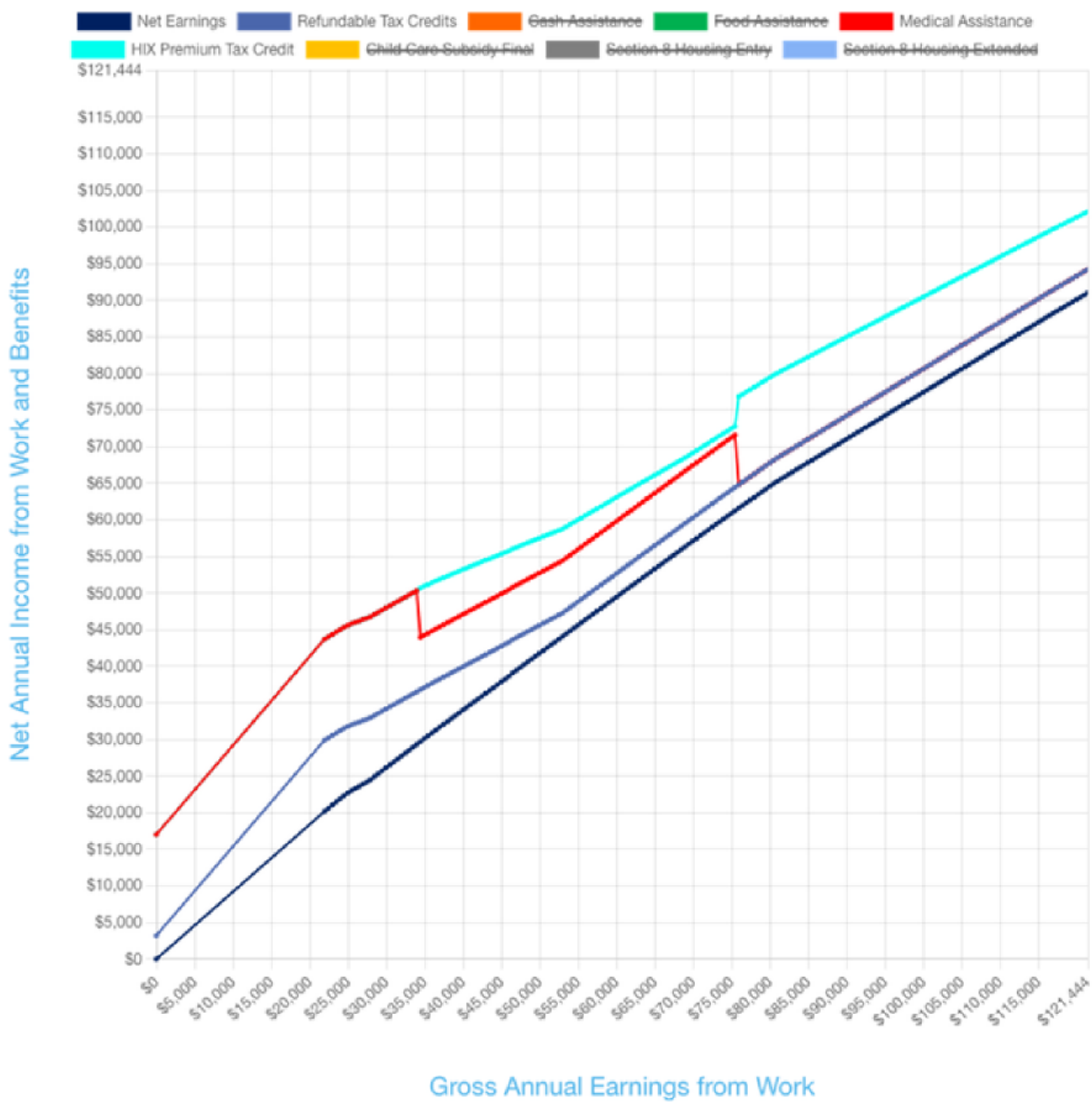

Figure 5: Medical assistance and HIX Premium tax credits

Conclusion

By itself, this example in the modeling invites us to ask deep questions about the logic and incentives that have been built into the social safety net. One might be tempted to ask if such logic or consideration of incentives exists at all in the sprawling apparatus. The evidence presented in this report suggests that it does not.

Recalling the scenario where the hypothetical single mother of two children is receiving the entire bundle of assistance programs possible, the first cliff example remains the starkest. As she approaches $30,000 in gross annual earnings, her net income from both wage income and assistance programs surpasses $75,000. Once she encounters the first benefit cliff, she does not reach that same level of material well-being again until her gross annual earnings approach $77,000 because of the other cliffs she encounters as her earnings rise.

Faced with that sharp of a contrast and that vast of a gap, we must be honest with ourselves, disincentives to work exist in West Virginia. The scope and interactions of the myriad disjointed assistance programs for our fellow Mountaineers facing economic hardship send a message. For the statistically representative individual receiving assistance, that message is essentially, “It’s not worth your time and energy to earn more than $30,000.”

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