Policy Brief April 2011

The Cliff Effect: Easing the Transition to Economic Self-Sufficiency

What is Self-Sufficiency?

The Self-Sufficiency Standard measures how much income is needed for a family of a certain composition in a specific geographic location to adequately meet their basic needs without public or private assistance. The Self-Sufficiency Standard is a more accurate measure of income adequacy compared to the Federal Poverty Guidelines (FPG). According to the FPG, families are characterized as "poor" if their income is below the FPG and "not poor" if their incomes are above them. The most significant shortcoming of the FPG is that for most families, in most places, they are simply not high enough. The Self-Sufficiency Standard varies by both family type and by geographic location because the amount of money families need to be economically self-sufficient depends on family size, composition, children's ages, and the state and county of residence.

For example, the FPG for a family of three in 2009 is $18,310 annually, the equivalent of earning or $8.80 an hour for full-time employment. According to the 2009 Self-Sufficiency Standard, a family of three – consisting of one adult, one preschooler, and one schoolage child in Marion County– is $42,117 annually – the equivalent of earning $19.94 an hour and approximately 230 percent of the FPG.[1]

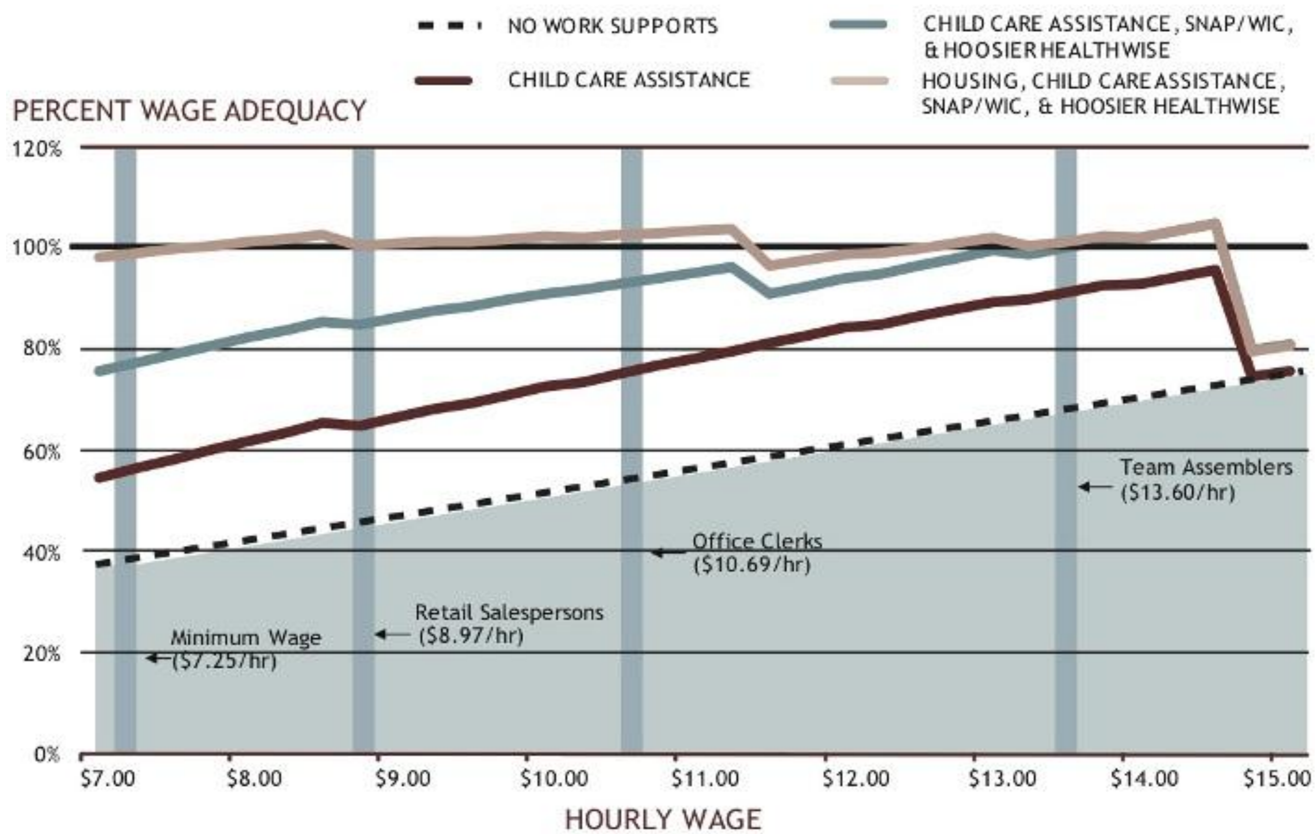
What is the Cliff Effect?

Most often the single barrier to self-sufficiency for low-income individuals is the "cliff effect." Eligibility for work support programs such as Supplemental Nutrition Assistance Program (SNAP), Temporary Assistance for Needy Families (TANF), Hoosier Healthwise, Women, Infants and Children (WIC) Nutrition Program, and Child Care Development Fund (CCDF), which assist low-income families to close the gap between their earnings and basic living expense, is typically based on income. Generally eligibility for these programs is below 200% of the Federal Poverty Guidelines (FPG), which is $37,060 for a family of three in 2011.

Program/Measure	Percent of Federal Poverty Guidelines (FPG)	Monetary Amount for Family of Three in 2011
100% of FPG	-	$18,530
SNAP	130%	$24,089
CCDF	170%	$31,501
WIC	185%	$34,281
200% of FPG	-	$37,060
Hoosier Healthwise	250%	$46,325

A benefit cliff occurs when just a small increase in income leads to the complete termination of a benefit. The result is that parents can work and earn more, while their families end up worse off than they were before. Because they will suddenly lose their eligibility for work support programs and those benefits could be worth <u>*more than*</u> the raise or increase in earnings from a new job. This phenomenon is called the cliff effect and can be found in many of the programs that serve as economic "bridges" for tens of thousands of families each month in Indiana.

In the chart below, the 2009 Self-Sufficiency Standard wage for the family of three in Marion County and work supports are measured against various wages to gauge their impact on wage adequacy. When a $13.60 an hour team assembler job is combined with no work supports (except for eligible tax credits), a family with one adult, one preschooler and one school age child in Marion County reaches approximately 67 percent of the Self-Sufficiency Standard. When child care assistance is added, this jumps to - 85 percent. When a housing subsidy, child care, SNAP/WIC, and Hoosier Healthwise are added, the family achieves 100 percent wage adequacy. However, if the adult were to get a $1.50 per hour raise, they would lose their eligibility for all programs and their wage adequacy would plummet to - 75 percent. This is an example of the cliff effect. It would make more financial sense to turn down a raise in this situation.



*Median wage source: U.S. Department of Labor, Bureau of Labor Statistics. May 2008 state occupational employment and wage estimates: Indiana. Retrieved July 14, 2009 from http://www.bls.gov/oes/current/oes_in.htm

How Can Indiana Ease the Cliff Effect?

There are several ways for Indiana to ease the cliff effect so that seeking higher earnings makes sense for low-income families. A comprehensive and thorough examination of all work support programs – with the intent of developing a strong plan to address the cliff effect – is recommended.

1. **Establish a gradual phase-out for all work supports.** Individuals are being cut off entirely or suffer dramatic decreases in work support subsidies before they are actually able to pay for their families' basic needs with their income. As a result, they are often left with less money at the end of the month than when they earned a lower wage. All work supports should gradually phase out (rather than drop off suddenly) as wages rise to provide an incentive to workers to accept promotions or wage increases. In order to cover all families in need, there must be a corresponding increase in overall appropriations for these programs.

2. **Change the way income eligibility is determined to approximate average earnings over a longer period of time and continue to simplify application and re-certification processes.** For individuals who have fluctuating earnings (e.g., due to irregular hours or seasonal employment), re-certification periods that occur frequently do not realistically capture one's overall income and may lead to inadequate assistance. Earnings should be considered over a longer period of time (e.g., average income earned over three months or six months instead of one month). Also, the application process should be made easier by moving to online applications and standardizing recertification periods to one year, as the SNAP has recently done.

3. **Eliminate asset tests in Indiana's Temporary Assistance for Needy Families (TANF) and Supplemental Nutrition Assistance Program (SNAP) programs so that families can access needed support in times of financial crises.** Many public benefit programs limit eligibility to those with few or no assets. If a family has assets exceeding the state's asset limit, the family must first eliminate or "spend down" its savings in order to be eligible to receive public assistance. Asset limits, no matter how high, signal to low-income families that asset building should be avoided. However, the opposite is true. Personal savings and asset building are necessary for families to move off of work support programs towards economic self-sufficiency.

   In addition, vehicles, which are vital for many to find and maintain employment, should be exempted. States should also exempt Earned Income Tax Credit (EITC) refunds for at least a year to offer protection from emergencies and unexpected expenses.

4. **Create a State Child Care Tax Credit that is refundable.** Child and dependent care expenses can demand a significant amount of money from the budget of a working family. With few increases in state or federal funding, direct child care assistance is not available to every working family that needs help paying for child and dependent care. In Indiana, the waitlist for child care vouchers exceeded 10,000 in 2009.

The federal Child and Dependent Care Tax Credit and similar state tax credits and deductions can help eligible families offset their child care expenses. These tax provisions can lower the income taxes that families must pay and, in some cases, give cash refunds to families whose incomes are too low to owe taxes. Twenty-eight states (including the District of Columbia) have child and dependent care tax provisions. Thirteen of those states offer refundable credits.

5. **Increase the state's Earned Income Tax Credit.** Indiana is one of 24 states that have their own state EITC to supplement the federal credit. State EITCs range from 3.5 percent to 33 percent. Indiana's state EITC is currently set at 9 percent of the federal credit. An additional increase would help to offset the regressive nature of Indiana's tax system while assisting more low-income working families in closing the gap between poverty and economic self-sufficiency.

Policy Brief Made Possible Through Generous Funding From:

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[1] To calculate Indiana's online Self-Sufficiency Standard calculator can be found at: www.indianaselfsufficiencystandard.org/.