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CHAPTER 5

LIVING IN THE NEW ECONOMY

THE CLINTON ADMINISTRATION FIRST came to office on a platform of "Putting People First." And indeed that pledge has been met. While the phrase "the New Economy" typically brings to mind technological innovation and globalization, arguably one of the most important outcomes has been the improvement in the well being of the American people. By virtually any measure, Americans are better off today than they were 8 years ago. As we highlight in this chapter, many of these improvements have benefited minority and female-headed households, as well as residents of central cities and rural areas – populations that have been among the hardest to reach in the past. Yet despite dramatic gains, challenges remain. Through a combination of public policy and continued economic growth, our country can build upon its recent successes and address the remaining problems.

Good News from the American Economy

The record setting gains in the stock market and growth in the net worth of wealthy individuals have received much attention in the popular press. What is most noteworthy about this economic expansion, however, is its length and the breadth of its reach. The last few years in particular have brought tremendous gains to all segments of our society.

Employment gains have been astounding. Between January 1993 and October 2000, 22.4 million new jobs were created.[1] In 1999 the unemployment rate reached 4.2 percent, the lowest

level since 1969 and wages are increasing. After declining steadily from 1986 to 1994, real hourly wages for private sector workers increased by 7.2 percent from 1994 to 1999.[2] These gains in employment and wages are echoed in growth in income and decreases in poverty. Median household income reached a new high of $40,800 in 1999, an increase of 2.7 percent in real terms since 1998, and a total increase of 13.3 percent from 1993. In 1999 the poverty rate fell to 11.8 percent, the lowest level since 1979, and 3.3 percentage points below the 1993 rate of 15.1 percent.

Unlike previous expansions these gains were shared across the income distribution. Between 1998 and 1999 real income grew by 4.4 percent at the 20th percentile compared to 3.5 percent at the 80th percentile. From 1993 to 1999 the respective growth rates were 15.0 and 14.2 percent.[3] In addition, the most disadvantaged subgroups tended to experience the largest improvements in financial well being. Unemployment for African Americans fell from 13 percent in 1993 to 7.0 percent in 1999, reaching the lowest level ever recorded, [4] At 5.6 percent, the unemployment rate for Hispanics is also the lowest on record.[5] Earnings have also increased, particularly for African Americans. Between 1998 and 1999 median earnings for full time year-round African American male workers increased by $2,379 or 8.6 percent a dramatic rise in a single year. With this sharp increase, the ratio of black-male earnings to white-male earnings rose to 0.81, the highest level ever recorded.[6]

<insert chart of unemployment rates by race here>

On a household level, median income for African American households increased 7.7 percent between 1998 and 1999, up 23.9 percent since 1993 to reach a record high of $27,910. Household income for Hispanics also reached a record high, rising to $30,735, an increase of 6.1 percent between 1998 and 1999, and 16.5 percent since 1993. [7]

Along with these record-high increases in income over the past year have come record declines in poverty. With the largest one-year decline ever, the poverty rate for African Americans reached an all-time low of 23.6 percent. Hispanics also experienced a record drop in poverty between 1998 and 1999, and the poverty rate for this group, at 22.8 percent, is now at its lowest level since 1979. [8]

<insert chart of poverty rates by race here>

Female-headed households are another group on which past economic growth has had limited impact. However, during this Administration, the strong economy and a social welfare policy that has emphasized work have brought substantial benefits to this group. In March 1993 just 56.8 percent of women maintaining families (no spouse present) were employed, compared to 63.4 percent in March of 1998 and 65.2 percent in March of 1999.[9] This increase in employment corresponded to an increase in income. Between 1993 and 1999 median income for female-headed households increased by 22.4 percent with a 4.9 percent increase between 1998 and 1999 alone.[10] The poverty rate for female-headed households fell over this time frame, from 38.7 in 1993 to 33.1 in 1998, and 30.4 in 1999. The group most likely affected by welfare reform is low-income single mothers and their children. According to a recently released survey,

between 1997 and 1999 the number of working low-income (below 200 percent of the poverty line) single mothers increased from 59.7 to 65.2 percent, and their children benefited.[11] Between 1998 and 1999 the poverty rate for children fell by 2 percentage points to 16.9 percent, the lowest level since 1979 and the largest percentage point decline since 1966. Poverty among black children declined by an even larger amount in absolute terms, falling by 3.6 percentage points to 33.1 percent. Since 1993, the poverty rate for children has fallen by 5.8 percentage points.

Our oldest Americans have also benefited. The poverty rate among the elderly fell below 10 percent for the first time ever. With the elimination of the Social Security earnings test for those age 65 and over, elderly Americans will likely participate in the labor force in greater numbers, and further improvements in their financial status may result. For years poverty in central cities has seemed intractable, yet here too the situation is improving; residents of central cities experienced an above-average increase in median income and the largest declines in poverty of any geographic category. [12]

The gains experienced by Americans over the past 8 years have not been limited to financial measures, but include a long list of improvements in the quality of life. Low interest rates and a strong economy have helped more Americans than ever before become homeowners. In the third quarter of 2000, 67.7 percent of American families owned a home, up from 64.2 percent in the same quarter of 1993 and surpassing the end-of-Administration goal set in 1995.[1314] Improvements in job opportunities, in combination with Administration initiatives to hire additional police officers, strengthen gun laws, and increase local resources to improve

public safety, have all contributed to a dramatic reduction in crime, with the overall crime rate falling to its lowest levels in 26 years.[15]

Our public schools today are also showing improvements on several fronts. Since 1992, reading and math scores on the National Assessment of Educational Progress (NAEP) have increased for fourth, eighth, and twelfth graders, including those students in the highest poverty schools.[16] More young people are graduating from high school than ever before, and more are attending college.[17] Average Scholastic Aptitude Test (SAT) math scores have reached their highest level in 30 years, and average verbal SAT scores have held steady while the number of non-native English speakers taking the exam has increased.[18] There have also been notable academic achievements by minorities. Among those who complete high school, the proportion of African American and Hispanic students who continue their education at a 4-year college is at a record high.[19]

Strides have also been made with respect to health. The birth rate among teenagers declined 17 percent between 1993 and 1999,[20] and smoking among teenagers declined for the first time in nearly a decade.[21] The fraction of high school students who said they had smoked a cigarette in the preceding 30 days fell from 36.4 percent in 1997 to 34.8 percent in 1999. Infant mortality is down from 8.4 per thousand in 1993, to 7.2 per thousand in 1998. Deaths from heart disease, cancer, strokes, and HIV are all down, and life expectancy has improved. A child born in 1998 can expect to live nearly 76.7 years, up from 74.9 years just 10 years earlier.[22]

While these statistics present a glowing picture of the New Economy and the well being of the nation as a whole, more work remains. Despite the tremendous recent gains, incomes of minorities remain significantly below those of whites, and their poverty rates are significantly higher. Infant mortality and life expectancy also differ substantially by race and ethnicity, as does access to a quality education. Certain areas of the country continue to experience unemployment rates above 10 percent and above average levels of poverty. As the country moves into the new millennium, we must confront these issues.

Helping Families Help Themselves

As noted in earlier chapters, the New Economy has been characterized by new technologies, new methods of communication, and new avenues of trade. However, it has also brought with it new ways of providing for the least well-off Americans, methods which appear to have been quite successful. Low-income families are receiving assistance in becoming or remaining independent of public support through a network of programs designed to help families move from welfare to work and to assist other low-income working families. By placing its emphasis on helping working families, the Administration has changed the tenor of American social welfare policy.

Welfare Reform

One of the most impressive achievements of the past 8 years has been the reduction in the number of individuals receiving welfare, along with an increase in employment among current

and former welfare recipients. The Administration began working toward welfare reform beginning in 1993, and approved a record number of waivers that allowed states to implement changes in their welfare programs on an experimental basis. As of August 1996, 43 states had implemented waiver programs that emphasized work and parental responsibility, and caseloads had begun to fall.[23]

These state-level changes were followed by the bipartisan Personal Responsibility and Work Opportunity Reconciliation Act (PRWORA) signed by President Clinton in 1996. This Act significantly changed the welfare system on a national level. It replaced the Aid to Families with Dependent Children (AFDC) program with a program of Temporary Assistance for Needy Families (TANF), established time limits on welfare receipt, and placed an emphasis on helping families leave welfare and entering the labor market.[24] Families are aided in this transition through policies that provide assistance with child care, expanded eligibility for health insurance, and tax credits to subsidize the earnings of low-income workers.

TANF differs from AFDC in several fundamental ways. Under the former AFDC program, states set eligibility and benefit levels and received matching funds from the Federal government to help with the cost of the program. In contrast, TANF provides states with block grants that are used to finance cash benefits, job preparation, and other worker support programs. Under TANF states have much more flexibility in spending than they did under the former AFDC program, and they have used this flexibility to meet the particular demands of their constituencies. States are also eligible for performance bonuses for moving individuals into jobs, increasing participation in the Food Stamp, Medicaid, and Children's Health Insurance

programs, providing child care, and increasing family formation and stability. States can also receive bonus awards for reducing out-of-wedlock births.

The new system differs further from AFDC in that it imposes time limits and work requirements on welfare recipients: Federal funds cannot be used to pay benefits to recipients who have received assistance for a lifetime total of 60 months (although states can exempt a portion of recipients from this requirement). Alternatively, states may set even shorter time limits or may use state-only funds to continue support beyond 5 years. In 1999, 38 states used the 60-month time limit, and the remainder implemented other policies (7 states have shorter time limits, 3 currently have no time limit, and others intend to use longer periods).[25] With respect to work requirements, TANF recipients must work in some capacity after receiving benefits for 2 years. Again, states have flexibility in implementing the rule, and particularly in strengthening requirements. In 1999, 28 states had welfare policies that imposed immediate work requirements in lieu of the 2-year requirement.[26]

Finally, a third dimension in which TANF and AFDC differ significantly is the ability of states to design the parameters of the program to best suit the needs of their poor families. While states always had the freedom to set benefit levels, TANF allows them to establish their own methods of calculating the income of potentially eligible families, and to set income and asset limits for eligibility. The majority of states have used this freedom to reward work by decreasing the implicit tax on earnings. The AFDC program often reduced benefits dollar for dollar for any earnings above $90 per month if the individual had been enrolled in AFDC and working for one or more years. This 100 percent "tax" created a strong disincentive to work, as many AFDC

participants received no increase in income for additional hours of work. Under TANF many states impose a more gradual benefit reduction rate to encourage greater workforce participation. States are also using the flexibility and resources provided under the welfare reform law and regulations to invest in a wide range of supports to help welfare recipients and other low-income working families enter the work force and succeed on the job.

Since August of 1996 caseloads have fallen dramatically; the average monthly caseload has declined by 6 million individuals, a reduction of 49 percent.[27]

<insert chart of AFDC/TANF Recipients here>

Including the reductions that took place during the period of state waivers, the welfare caseloads fell by 7.8 million individuals or 56 percent since 1993. Declines in some states have been even more dramatic. In Wisconsin, for example, the number of welfare recipients fell by 70 percent between 1996 and 1999, and by 82 percent since 1993.

The 1996 reforms have undeniably been successful in reducing the number of individuals receiving welfare. However, reductions in caseloads are not the only measure by which to judge the accomplishments of the policy. An important outcome is the well being of individuals once they leave welfare rolls. Much of what we know about outcomes for welfare leavers comes from studies undertaken in individual states. To date, over 30 states have conducted studies monitoring the outcomes of those who have left welfare. In addition, some of the data from state

waiver experiments undertaken prior to PRWORA have implications for current TANF programs.[28]

Because the available data can differ significantly across states and does not represent nation-wide averages, this Report supplements the state-level information with new results from the 1996 panel of the Survey of Income and Program Participation (SIPP),[29] providing some of the first evidence of the effect of welfare reform for a nationally representative sample. The majority of these results are based on a sample of individuals who left welfare and are observed for at least 12 months following their exits. Individuals in SIPP are first interviewed between December 1995 and March 1996, and are then re-interviewed every 4 months. Survey data currently exists for respondents through November 1998 to February 1999, depending on the month of the initial interview. We are therefore examining the experience of some of the early leavers after welfare reform, and are unlikely to observe the direct effects of the 2-year TANF time limit that exists for many TANF cases and will certainly not observe the effects of the 5-year lifetime limit. In addition, we do not yet know the long-term impact on these families who may, over time, experience substantial wage gains as they accumulate labor market experience.

When considering the outcomes of the 7.8 million individuals who left welfare, one of the most important issues is the incidence of recidivism – the number of individuals cycling on and off the rolls. Both data from SIPP and a synthesis of state studies show that only approximately 25 percent of the leavers return to welfare during the first 12 months after leaving. The majority of those who do return do so quickly; in SIPP 18 percent of those who exit return within the first 6 months of leaving, while only 7 percent return during the second 6-month

window. One would imagine that the probability of returning would continue to fall with the length of time off welfare. Indeed, evidence for welfare leavers in Maryland shows such a pattern: excluding those who exited for just one month (as is done in the SIPP analysis and most studies of recidivism), 25 percent had returned to welfare within 12 months of exit. This fraction increased by only 10 percent in the next 12 months, and by just 2 percent in the third 12-month period.[30]

A key component to successful exits from welfare is the ability to obtain a job and remain employed. The Administration provided $3 billion in fiscal years 1998 and 1999 in Welfare-to-Work grants[31] to help states and local communities move long-term welfare recipients and certain non-custodial parents into jobs, as well as implementing the Workforce Investment Act to provide job assistance to low-income workers.[32]

Workforce Investment Act

The Workforce Investment Act of 1998 (WIA) was the result of a bipartisan effort on the part of Congress and the Administration. The law creates One-Stop Career Center systems to knit together multiple programs at the local level and requires that basic job and career information and assistance be available to all Americans. The law also provides for intensive assessment, counseling, job search assistance, and training for low-income individuals and dislocated workers on a priority basis.

The law created three reforms to maximize customer choice for individuals in need of training: individual training accounts, systems for identifying eligible training providers and their programs, and state and local Consumer Reports Systems containing extensive information on programs and their performance. These reforms were designed so that customers under WIA had the opportunity and purchasing power to select the training programs of their choice, rather than being channeled into a handful of programs under contract with local workforce systems. The reforms were designed to provide high levels of reliable information empowering WIA customers and the general public to make informed choices.

Efforts to help individuals secure jobs have tended to use one of two strategies. The "work first" approach aims to get people employed as quickly as possible, assuming that work itself will teach the skills needed to remain in the labor force, after which, they eventually move to a better job. In this approach the focus is on maintaining some attachment to the labor force rather than on initial wages. The alternative approach uses more extensive education and training prior to entering the labor market. In this case, labor market entry is delayed, but it is hoped that the initial job will be of higher quality. The work first approach is by far the most commonly employed, and initial evidence indicated that it is more successful – employment and earnings are higher in areas that employed this strategy. However, a new study comparing outcomes across counties in California over a 9-year period finds that over the long-term, results for the two methods appear to be similar.[33] A study that compared the outcomes of 11 different welfare to work programs over a 2-year period found that the most successful program was one

that offered a combined approach, emphasizing work while providing assistance with completing a GED for those for whom this goal appeared to be in reach. [34]

Increases in employment for former welfare recipients were also substantial. Administrative data from studies of several different states demonstrate that between 62 and 75 percent of those leaving welfare were employed at some point in the following year, and approximately 40 percent were employed in all four quarters.[35] Similar results are observable on a national level. Data from SIPP show that of those observed for 12 months after leaving welfare, 66 percent were employed at some point, and 43 percent had earnings in all four quarters of the year. However, even many of those working all four quarters are employed less than full-time. Only 32 percent of welfare leavers worked 50 weeks or more during the year, and just 40 percent of this group (12.8 percent of all leavers) worked 35 or more hours in every week. Thus, while significant increases in labor force participation have been made, considerable room for further gains remains.

Importantly, the rates of employment increased even among those who remained on welfare. In 1999, 33 percent of welfare recipients were working, compared to just 7 percent in 1992.[36] The development of an attachment to the labor market for those currently on welfare bodes well for the probability of successful future exits.[37]

For both workers who have left the welfare rolls, and those receiving welfare benefits in addition to their earnings, the importance of the booming economy should not be understated: based on theories of human capital accumulation and the tenants behind work-first programs,

time spent working increases one's productivity, job skills, and wage rates. Thus, the longer the economic expansion continues and unemployment rates remain at historic lows, the more work experience former and current welfare recipients will accumulate, and the better prepared they will be to weather an economic downturn.

While employment in and of itself is important, so too are earnings. It is unlikely that exits from welfare will be successful if individuals are no better off than they were prior to exit. Evidence from state studies indicates that, at least initially, few leavers are significantly better off. Median quarterly earnings for those leavers who found employment varied from $2,000 to $3,000 across states, or approximately $700 to $1000 per month. In Wisconsin the majority of leavers had lower incomes (earnings plus AFDC benefits) after exiting welfare than while receiving benefits. Incomes are relatively low for those recently leaving welfare. For the sample of SIPP leavers, median monthly household income plus food stamps for the year following exit was $1,605, compared to $1,509 in the 2 months preceding exit. For 44 percent of leavers, the total household income plus food stamps in the post-exit year was more than $50 higher than in the months before leaving, while for 49 percent it was at least $50 lower.

It is important to recognize that the Earned Income Tax Credit (EITC), discussed in detail below is not included in these calculations. Although benefits from the EITC are not recorded in the SIPP data, the EITC provides a substantial subsidy to the earnings of low-income workers, and including the effects of the EITC would likely improve observed incomes and poverty rates considerably. Although not focusing on the population of welfare leavers, the Census Bureau

estimates that in 1999 the fraction of households with after tax incomes below $10,000 a year falls from 9.9 to 9.3 when the EITC is added into income.[38]

The idea behind work first programs is that an initial job would lead to earnings growth over time. Because many former welfare recipients find employment in low-wage industries such as restaurant/fast food prospects for earnings growth may not seem extremely bright.[39] However, comparing outcomes over just the first 12 months after exit, 39 percent of SIPP leavers had monthly earnings in the second 6 months that were $50 or more higher than in the first 6 months while 28 percent had a $50 or greater reduction in earnings over the two 6 month periods. Thus, a relatively large fraction of former welfare recipients did find jobs that provide earnings growth through increases in hours or wages or both.

Making Work Pay

A network of government support programs available to working families facilitates the transition from welfare to work. In the past, families leaving welfare often lost not only their cash assistance and incurred explicit payroll taxes, but also faced the loss of other benefits, such as food stamps and Medicaid, and incurred additional expenses associated with work, such as the cost of child care and transportation. One study found that the implicit marginal tax rate—the net amount lost due to taxes, lost benefits, and expenses from a one dollar increase in income--for AFDC recipients could easily be well over 50 percent.[40] In other words, earning one dollar more in the labor market would increase disposable income by less than 50 cents.

The Administration's welfare reform proposals have attempted to reduce these implicit taxes by expanding health insurance coverage to include many working families not previously eligible for public programs, increasing subsidies for child care, and increasing the rewards from work through minimum wage policies and increases in the Earned Income Tax Credit (EITC).[41] The Administration has also worked to help unmarried parents collect the child support payments they are due. These programs help both working families who were not receiving welfare and ease the difficulty of leaving welfare for others. By reaching out to both groups the Administration has worked to ensure that no working families are left behind.

***EITC*:** Operating through the income tax system, the EITC provides a wage subsidy to low income workers with the amount of the subsidy depending on earned income and whether the family has zero, one, or two or more children. By increasing the wage rate, the EITC increases the incentives for individuals to participate in the labor force. In 2000, for families with two or more children, wages are subsidized by 40 cents for every dollar of earned income until earned income reaches $9,720 for a maximum credit of $3,888. This tax credit is refundable so that even families who pay little or no income tax can benefit fully from the tax provision. Rather than eliminating the credit when earnings surpass this level, the credit remains at $3,888 until earnings reach $12,690 and then gradually falls, phasing out completely at earned income of $31,152.[42] This gradual reduction reduces the disincentive to work past the level at which the credit peaks relative to a program that discontinues all benefits immediately when income increases beyond a given level.

<insert chart of the EITC over time here>

The EITC has been expanded greatly since 1990 with increases in both benefits and in the scope of coverage. The 1993 expansions increased benefits for approximately 15 million families, in large part by increasing benefits to families with two or more children.[43] The expansion also allowed workers without children to claim a tax credit.[44] As a result of both the 1990 and 1993 expansions, credits paid through the EITC provision increased from $15.5 billion (in 1999 dollars) in 1993 to nearly $32 billion in 1999,[45] and the number of families receiving assistance from the program increased by one-third, from 15 million to nearly 20 million.[46] The EITC is now larger in dollar terms than the combined amounts distributed through the AFDC and food stamp programs.[47]

This wage subsidy has been effective in attracting more workers to the labor market.[48] One study in particular estimated that the EITC alone was responsible for 34 percent of the increase in annual employment of unmarried mothers over the period 1992 to 1996.[49]

<insert EITC/Labor force participation rate chart here>

By increasing wages for low-wage workers the EITC also plays an important role in reducing the implicit marginal tax rate faced by those exiting welfare.

In addition to increasing the probability of employment, the EITC has done much to improve the well-being of those who take advantage of the program. While the discussion above pointed out the difficulty former welfare recipients have in securing jobs that pay above poverty

level wages, when the EITC is taken into account, the earnings of many of these new workers increase substantially. In 1999, the EITC lifted 4.1 million individuals, including 2.3 million children, out of poverty. The provision has also been effective in targeting benefits to the most needy. Estimates are that over 60 percent of EITC benefits accrue to families who have pre-EITC incomes below the poverty line.[50]

Minimum wage: Operating in tandem with the EITC is the minimum wage. While the EITC provides an effective wage subsidy, the minimum wage laws ensure that the subsidy is based on an acceptable wage. The real value of the minimum wage declined substantially in the early 1990s, falling to just 68 percent of its 1968 value in 1995.[51] Subsequent Administration-backed efforts led to increases in the minimum wage in 1996 and 1997. Even with these most recent increases, the minimum wage is equal to only 68 percent of its 1968 level after controlling for inflation.

However when the minimum wage is combined with a possible 40 percent EITC subsidy, the true minimum wage for workers with earnings below $9,540 is $7.21, a figure nearly as high in real terms as the peak minimum wage rates in the 1960s. Yet despite the generosity of the EITC program, an individual working full-time at minimum wage would have a yearly income of just $14,116 including the EITC, well below the poverty line of $16,895 for a family of two adults and two children.

<insert minimum wage with EITC chart here>

Child care. For many parents, one of the most difficult barriers to employment is finding affordable quality child care. For low-income families and new entrants to the labor market, the costs associated with child care may make working impossible. Recognizing the cost of child care as a barrier to work, the Administration has fought to make child care more affordable for low-income families, and to provide assistance to a greater number of families. In doing so, it more than doubled the funding for child care assistance and combined the various child care programs already in existence to create the Child Care and Development Fund (CCDF). The CCDF provides states with block grants to subsidize approved child care arrangements. In 2001 states will have access to more **than $4.5 billion [includes proposed $1 billion increase]** to make child care more affordable and to improve the quality of that care.[52] The program provides assistance to many. Estimates suggest that over 2 million children will benefit from the program in 2001. Unfortunately, despite the substantial investment, many states have waiting lists for benefits, and many of those families who qualify for the subsidies do not receive benefits. According to one study, only 30 percent of families who left welfare and are now working are also receiving assistance with child care.

Food stamp program: The Food Stamp Program supplements family incomes to ensure that low-income families receive adequate nutrition. Benefits are available to families with incomes up to 130 percent of the poverty line. The vast majority of benefits, nearly 90 percent in dollar terms in 1999, go either to families with children or to elderly individuals.[53] In 1999, 32 percent of benefits went to working families. Over the past few years, enrollment in the food stamp program has fallen dramatically, from a high of 27.5 million participants in 1994 to 18.2 million in 1999. This decline is notable even among families with children. While asset limits in

the food stamp program result in some poor families being ineligible for benefits, in 1999 only 51 percent of children in families with incomes below the poverty line received food stamps. Even among the very poorest---children in families with incomes below 50 percent of the poverty line---only 58 percent received food stamps, a decrease of 47 percent since 1993.[54] Some of the decline in participation is attributable to changes in the law that denied benefits to immigrants and put restrictions on benefits received by able-bodied workers. However, the observed decline in participation is greater than these specific changes would suggest.

While the strong economy and greater labor force participation would be expected to reduce the number of families needing food stamps, there is a concern that some eligible families may not be receiving the benefits they need. One possibility for the decline results from the increased labor market activity of those on welfare and those who have recently exited. States require that food stamp recipients who have labor earnings have their incomes re-certified at regular intervals, three months is a common interval. Traveling to the welfare office every few months over the course of a year to document earnings, could well be a substantial deterrent to participation. Indeed, a recent study attributed large portion of non-participation to the "costs" involved in the regular re-certifications.[55]

In response to recent trends the Administration has implemented a series of changes in the food stamp regulations. These changes substantially reduce the need for re-certifications for those leaving welfare or newly employed and otherwise simplify the application process. States are also offered the opportunity to receive bonus awards for levels of food stamp participation among low-income working households and for percentage increases in participation. Twenty

million dollars has been allocated for these awards. Finally, the Administration has also provided funding for educational and outreach campaigns aimed at enhancing nutritional security.[56]

Child Support Programs. An important component of the Administration's policies to help working families is to ensure that unmarried parents receive the support they are entitled to under the law from non-custodial parents. Between 1992 and 1999 dollar value of child support collections increased in real terms by over two-thirds, from $9.5 billion to nearly $16 billion dollars, and the number of child support cases with collections increased from 2.8 million in 1992 to 6.1 million in 1999. Currently in many states, TANF benefits are reduced dollar-for-dollar with child support collections. This reduction reduces the incentive for noncustodial parents to provide for their children. The President has proposed legislative changes that ....., giving parents more reason to cooperate with the system. Some states, such as Wisconsin, are already experimenting with similar policies, and the results have shown that collections do increase when parents receiving welfare benefits are permitted to keep a greater share of child support payments than in the past. This change improves the incentives for non-custodial parents to make support payments and may therefore increase the amount of payments actually made.

Receipt of child support payments is further aided by policies that reach out to low-income non-custodial parents. The Administration requested $125 million for "Fathers Work" grants that, along with responsible fatherhood initiatives funded through the Department of

Labor, help these non-custodial parents work, pay child support, and reconnect with their children.

Child support is an important source of income for poor children. In 1997 child support lifted an estimated half million children out of poverty.[57] This support is particularly important for those leaving welfare. Women who leave welfare and do not receive child support have over a 30 percent chance of returning to welfare after 6 months, while those who do receive child support have only a 9 percent chance. [58]

Health Insurance Expansions. Historically AFDC recipients exiting welfare lost their Medicaid coverage when they left welfare. However, in the 1980s a series of Medicaid expansions and the implementation of Transitional Medicaid Coverage (TMC) began to provide health insurance benefits for former welfare recipients and low-income families, easing the transition to work. Prior to PRWORA, children under age 6 with family incomes below 133 percent of the poverty line, and children between age 6 and 19 with family incomes below 100 percent of the poverty line, were covered by Medicaid under Federal mandate. Many states opted for even greater coverage, with higher income thresholds and coverage for children of all ages. Adults could also obtain Medicaid up to 12 months through the TMC program or through state medically needy programs. In 1996 PRWORA further expanded Medicaid coverage to unmarried and some two-parent families for families leaving welfare, and in 1997 the State Children's Health Insurance Program (SCHIP) was created to target all children in low-income families. Because of the importance of these programs, they are the focus of a larger section later in the chapter.

Reaching out to Underserved Communities

Providing opportunity and independence for American families may require more than a strong national economy and responsible welfare policy. In some areas poverty is so entrenched and the local economy so weak that additional efforts may be called for. Some of the most intractable poverty is found in our Nation's central cities and rural areas. In 1967, when statistics for these regions were first recorded, the poverty rate for central cities was 15.0 percent, compared to a nationwide rate of 14.2 percent. In contrast, poverty in rural areas in 1967 was over 20 percent. By this measure, central cities were nearly as well off as the rest of the country, while rural areas suffered from disproportionately high rates of poverty. From 1967 until the early 1990s, there was a substantial shift in the incidence of poverty, with a worsening of conditions in the central cities and a slight improvement in non-metropolitan areas. By 1993 the percent of central city residents living in poverty had reached 21.5 percent, its highest level ever, while the poverty rate in non-metropolitan areas declined somewhat to 17.2 percent. Both rates were well above the national poverty rate of 15.1 percent in that year. Since 1993, the situation for both types of areas has improved dramatically, as we detail below. In 1999, the poverty in central cities fell to 16.4 percent, and that in rural areas has declined to 14.3 percent, yet these rates are still above the national average. Because both central cities and rural areas are home to large numbers of Americans--30 percent of the United States' population lived in central cities, and 20 percent lived in rural areas[59]-- the above average poverty are a cause for great concern.

The strong national economy and current policies to make work pay, discourage out-of-wedlock child-bearing, and improve schools in poor neighborhoods would be expected to provide some relief to these distressed regions. However, the persistently high poverty rates of central cities and rural areas may also require additional strategies. In attempting to reach out to these distressed areas, the Administration has enacted a series of programs that directly target communities. We discuss these here, turning our attention first to the problems and progress in central cities and then to rural areas.

Central Cities: In some respects central cities are more attractive places to live for many low-income workers than outlying suburbs; public transportation is readily accessible, and city governments often provide more generous support services than other areas.[60] However, one factor that appears to distinguish the situation in central cities from that in other areas is limited job opportunities. Recent research has shown that most job creation is taking place in suburbs rather than in inner cities. One study by the U.S. Department of Housing and Urban Development (HUD) found that not only was job growth slower in the cities than in the suburbs between 1992 and 1997, but also that the job mix in cities is shifting towards high-tech jobs unsuitable to low-skilled workers.[61]

The difficulty central city residents face in finding employment is further heightened by problems with transportation and discrimination. Low-income workers, and welfare recipients in particular, are unlikely to own cars, and therefore must rely on public transportation to commute to jobs. However, a recent study found that nearly half of low-skilled jobs in the suburbs were not accessible by public transportation.[62] Minority workers in central cities are further hindered

in finding jobs by discrimination in the housing and employment markets. A recent study found that minorities have difficulty in renting or purchasing housing in the suburbs and are less likely to be hired by white owned firms that predominate in the suburbs.[63] The cost of housing in the suburbs may also make it difficult to move to homes near suburban jobs.

From a policy perspective there are several approaches to addressing this mismatch between where low-skilled workers live and where they work. First, rebuild the economies of central cities. Second, overcome the transportation hurdles of commutes to the suburbs. Third, help low-income families obtain housing near available jobs. And finally, improve the skills of workers through education and training programs to increase access to a wider range of jobs. The Administration has pursued policies along each of these dimensions.

The Empowerment Zones (EZs) and Enterprise Communities (ECs) are one part of the Administration's strategy for rebuilding central city economies. **Add sentence on magnitude** These programs aim to assist distressed communities by encouraging investments from private businesses through the use of tax credits, wage subsidies, and improved access to credit markets. To help solve commuting problems the Administration's Transportation Equity Act for the 21st Century established a new Job Access and Reverse Commute Program designed specifically to connect low-income persons to employment and support services. Similarly, the Bridges to Work (BtW) program provides placement, transportation, and retention services in a select group of cites. The Administration has also made it easier for low-income families to own a car by allowing states the flexibility to raise the limit on the value of a car that an individual may own and still qualify for welfare benefits[64] and increased the federal limits on car ownership for food

stamp eligibility.[65] Finally, to help workers live closer to jobs in the suburbs, HUD's Section 8 program subsidizes families' rents so that private sector rental units near jobs are affordable. The Administration has created two special programs specifically designed to maximize the impact of the Section 8 program on improving employment outcomes for low-income families. The Administration's Moving to Opportunity (MTO) program provides intensive counseling with Section 8 assistance to help families move from high poverty public housing projects to private housing in low poverty areas. The Welfare-to-Work Voucher (WtWV) program provides housing subsidy and services to TANF-eligible families to help them obtain or retain employment.[66] Limited preliminary evidence from MTO programs in Baltimore and Boston suggest that the program is successful in improving educational outcomes for children.[67] Finally, the Administration has invested heavily in education as described in the following section.

Rural communities: Like central cities, many of America's rural communities face high rates of poverty and unemployment.[68] However, because rural communities tend to have smaller, less diversified economies than central cities, they can be severely affected by the closing of only one or two industrial plants.[69] Furthermore, many rural communities suffer from geographic isolation from major markets, which makes it harder for residents to find jobs and for businesses to reach their customers.[70] Also, with little public transportation available, transportation problems are likely to be more acute in rural than urban areas. Although recent advances in telecommunications promise to reduce some of this disadvantage, rural communities lag behind urban communities in access to this technology.[71] In addition, rural governments often lack the economies of scale needed to make investments in many public services economical.[72]

A variety of programs exist to help rural communities. Assistance with basic infrastructure needs, such as electricity, telecommunications, and water and waste facilities, is provided through technical assistance, grants, and loans through the Rural Utilities Service (RUS). The Rural Housing Service (RHS) assists rural communities with community facilities and housing. Its programs target new or improved housing for moderate and low-income families and also assist communities in improving or developing facilities, such as fire stations, libraries, and hospitals. Assistance to rural businesses and cooperatives is provided through the Rural Business-Cooperative Service (RBS), which cultivates partnerships between the private sector and community-based organizations.[73] It also provides technical assistance and helps to fund projects that generate employment. Furthermore, many of the Administration's EZ/ECs are

located in rural communities. In addition, the Telecommunications Act of 1996 is addressing the digital divide problem by providing funds to assist in the provision of modern communication infrastructure for schools and medical facilities in low-income communities, both in rural and urban areas.[74]

Results: These programs, coupled with the strong national economy and policies of making work pay (described earlier) have led to substantial improvements in quality of life for those living in these areas. The unemployment rate in central cities has fallen from 8.2 percent in 1993 to 5.3 percent in 1999, while unemployment in rural areas has fallen from 5.9 to 3.7 percent.[75] These increases in employment have brought with them reductions in poverty and increases in median incomes. The poverty rate in central cities declined from 21.5 percent in 1993 to 16.4 percent in 1999, with the largest drop, a decline of 2.1 percentage points, coming in the past year. In fact, 80 percent of the total reduction in poverty from 1998 to 1999 came from the reduction in central cities.[76] Poverty in rural areas has also fallen substantially, from 17.2 percent in 1993 to 14.3 percent in 1999.

<insert metro/nonmetro poverty chart here>

Median household income in central cities has increased, rising 5 percent in real terms from 1998 to 1999, compared to a 2.1 percent increase for median incomes in metropolitan areas as a whole.[77] For African Americans the gains were particularly striking. After adjusting for inflation, median income for African American households in central cities increased by 13.9 percent between 1998 and 1999. Along with these economic gains has come a decline in the

number of individuals on welfare. Caseloads in the largest central cities have declined by 40.6 percent from 1994 to 1999.[78] Median household income in rural areas increased less dramatically than that in cities, rising just 0.9 percent in real terms between 1998 and 1999.

Despite these obvious improvements, there is more to do. Poverty rates and unemployment are higher in central cities and rural areas than elsewhere, and rural areas, while experiencing lower poverty rates than central cities, have shown smaller gains over time. In 1999 the national poverty rate was 11.8 percent, compared to 16.4 percent in central cities and 14.3 in rural areas. While it is too soon to judge the effectiveness of community based policies such as EZs/ECs, by reaching out to these communities through a variety of programs, the Administration has shown a willingness to seek creative solutions to our most pressing problems.

Education in the New Economy

Investments in human capital play an important role in the new economy. The most direct ways in which individuals invest in human capital are through education and training. Last year's Economic Report focused on the demand for educated workers, on post secondary education, and on training. This year we examine America's public elementary and secondary schools, institutions crucial to the development of our future workforce. We note recent changes in how we educate our children and ways in which we may best improve the quality of schooling we offer.

Many factors go into producing a quality education. Parents, families, and communities certainly must rank among the most important contributors to the education of children, but the discussion here focuses on those components of the education system more directly under the control of federal, state and local governments. We highlight in particular the effects of class size, teacher quality, and the school infrastructure and equipment. By improving the quality of these inputs to the education process we can hope to improve the final outcome.

A Role for Federal Education Policy

The federal government has long sought to improve access to education for the nation's poorest children and to help states ensure that their public schools are of high quality. Federal funds are primarily targeted to helping local communities afford needed reforms, expand new programs,[79] and access new technology,[80] and are targeted to schools and school districts serving poorer students.[81] Because it is directed to these important areas, the federal investment in schooling can have a larger impact than the magnitude of the funds would suggest.

In the United States, primary responsibility for elementary and secondary education rests with states and local school districts. Excluding school-based nutrition programs, the federal government provides just over 6 percent of the funding for K-12 education. [82] Federal spending in the poorest schools does reduce inequalities across school districts, but it does not fully compensate for the overall pattern of funding disparities derived from differences in the local property tax bases and state funding levels. Federal expenditures per student were more than four times as large in the poorest 25 percent of school districts as in the wealthiest quartile, yet

despite this sizable difference, overall expenditures per student continue to be greater among the wealthiest school districts. [83]

<insert school district revenue by income chart here>

The largest single federal program for kindergarten through 12th grade (K-12) education is Title I,[84] which allocates additional funds to schools based on the rate of child poverty in the local area.[85] The targeting of Title I funding to schools serving poorer children increased significantly with the passage of the 1994 Improving America's Schools Act, which reauthorized the 1965 Elementary and Secondary Education Act. In the 1997-98 academic year, 96 percent of schools in the highest-poverty quartile received federal Title I funds, up from 79 percent in 1993-94.[86] This quarter of schools served 49 percent of the nation's poor children in 1997-98, and received 43 percent of all federal funds for K-12 education.[87] These redistributional aspects of Title I funding are typically larger than any comparable efforts on the state level and thereby serve as a critical resource for improving equity. [88]

Reducing class size

For decades, there has been a debate over whether broad-based education spending programs, such as those aimed at reducing class size, are effective in improving student achievement. However, there is now beginning to be a consensus formed among experts that class size reductions are beneficial, especially for disadvantaged students and students in early grades.

Much of the most compelling evidence concerning the potential effectiveness of reductions in class size comes from a class size reduction experiment in Tennessee. To determine the extent to which smaller class sizes would improve academic outcomes, the state authorized and financed an experiment in which students and teachers were randomly assigned to classes with standard (22-25) or smaller (13-17) numbers of students[89]. The results showed significant improvements for children in smaller classes: Students enrolled in smaller classes from kindergarten through grade 3 did better on standardized tests of reading and math administered in middle school than students enrolled in normal-sized classes. These students also scored higher on their SAT and ACT exams in high school, and were more likely to take such college entrance exams than students enrolled in larger classes in grades kindergarten through grade 3. The results were especially strong for minority students—being in a small class in elementary school narrowed, by 54 percent, the difference between the probability a white child takes a college entrance exam in high school and the probability a black child takes the exam.[90]

The quality of this experiment persuaded many scholars that reductions in class size can improve outcomes for children. Teachers in smaller classes spend more time on individual instruction and review and less time on student discipline and routine administrative tasks.[91] Teachers of small classes may also get to know their students better, interact with them more frequently and individually, and provide more frequent and in-depth feedback than teachers of large classes.[92] Similar results are now emerging from class-size reduction programs in other states, such as the SAGE program in Wisconsin and the Class Size Reduction Program in California, reinforcing the conclusions of the STAR program.

While students appear to do better in smaller classes, reducing class sizes is expensive. Fully funding reductions in class sizes in grades 1-3 nationwide to 18 students per class would cost an estimated $5 billion per year.[93] Despite the expense, the expected gains in students' future earnings appear large enough to offset this investment.[94] However, the financing of these reductions in class size is hampered by the current distribution of students and resources. A disproportionate share of the spending for class size reductions is needed by schools serving poor students, because these schools generally have larger classes than more wealthy schools. Also, because the majority of funding inequality from school district to school district occurs between states, not within states, there is little room for states to reallocation of funds to assist poor schools. Differences in funding may therefore most readily be addressed through Federal programs.[95] In 1998, the Administration proposed a seven-year Class Size Reduction Initiative to reduce class sizes in grades 1-3 to a national average of 18 students per class. (The program was later expanded to include kindergarten classes.) In the first two years of the program it has enabled school districts to hire 29,000 new teachers, reducing class sizes for 1.7 million children.

The importance of teachers

While reducing class size has been shown to have measurable affects on student performance, the affects of teacher quality may play an even more important role in improving student outcomes. Most parents, children, and professional educators agree that teacher quality is a significant factor in student achievement. Results of a recent study show that teacher differences have a significant impact on student achievement in math and reading.[96] Even within schools, differences in the quality of teachers across grades led to significant differences in student performance. Because this study did not examine differences in teacher quality across

schools or within grades, the true effects of teacher quality can only be larger than those estimated in the study.

What is notable about this and other analyses of teacher quality is that measurable characteristics, in particular holding a Masters degree, is not indicative of the ability of the teacher to enhance student performance. Furthermore, beyond the first two years of teaching, the number of years of experience has little effect on student achievement. To ensure that our students have access to high quality teachers and to reward the very best, we need to be able to understand what signals quality. Despite the difficulty of measuring these differences in quality, evidence suggests that good teachers make a difference. **[waiting for at least one additional academic study on quality]**

Many schools are finding it difficult to attract and retain high quality teachers. Some of this difficulty likely stems from the existing pay scales in public schools. Currently the average starting salary of teachers is **[we are looking for something like "teacher salaries are xx percent lower than the average of all professions requiring a college degree" any suggestions?].** And this difference is increasing over time as the starting salaries in most occupations are increasing at a much sharper rate than starting salaries than the teaching profession.[97] Other factors that affect the quality of the job such as crowded classrooms, inadequate facilities and insufficient time for planning and professional development are also important components of compensation as more generally measured.

The challenge of attracting and retaining qualified teacher will become particularly difficult in the years ahead. Between July 2000 and July 2008, the population aged 5-17 will increase by more than a million,[98] significantly increasing the demand for teachers. Over this same time, about three-quarters of a million teachers are expected to retire, [99] while others will likely leave the field to pursue different occupations. Based on these statistics it is estimated that the United States will need approximately 2 million new teachers over the next 8 years.[100] The demands for teachers will be heightened by mandates to reduce class sizes. Decreasing the number of students per class to 18 will require the staffing of an estimated 100,000 additional classrooms.[101]

These increases in the demand for teachers will make it increasingly difficult to maintain consistently high levels of teacher quality in all classrooms. Already there is some indication of magnitude of the challenge. In 1996 California began a massive class-size reduction program in the early grades, spending $1.5 billion per year with the goal of reducing class sizes statewide from an average of 28 students per class to a maximum of 20. The state has largely been successful in achieving its goal; by the 1998-99 school year, over 92 percent of California's students in the targeted grades of K-3 were in classes of 20 or fewer students.[102] However, in these grades the percentage of teachers who were fully credentialed fell from 98 percent in the 1995-96 school year to 87 percent in the 1998-99 school year. Perhaps of greatest concern, this fall in the proportion of credentialed teachers was largest in schools with the highest proportions of low-income children.[103] While uncredentialed teachers are not uniformly less talented teachers than those with certification, the trend is discouraging. The ultimate benefits of nationwide

reductions in class size will depend on our ability to attract and retain greater numbers of highly qualified teachers, and to providing training to those just entering the profession.

This Administration has supported investments in teachers. Its Class Size Reduction Initiative requres that teachers hired with federal funds be fully certified and offers additional funds for professional development and teacher certifications. The Teacher Quality Enhancement Grant program has helped to prepare about 3,000 new teachers for high-need school districts and has improved the training of about 17,000 other new teachers. Federal funding for the continued professional development of experienced teachers has increased from $335 million for Eisenhower Professional Development grants in 1993 to $1,000,000 for Teaching to High Standards grants in the President's 2001 Budget Request.[104]

Box 5-x. Performance Based Pay for Teachers

Some proposals for improving school performance involve rewarding teachers with performance based awards, a change from most systems which base pay on education, experience, and responsibilities. Performance-based pay systems might improve the quality of instruction by providing teachers with additional motivation to achieve specified goals. In addition, by establishing the criteria for performance-based awards, unclear goals will be clarified, providing better guidance for teachers. Further, tying teacher compensation to performance may help attract talented people to the teaching profession, if they know that their hard work and skills will be rewarded.

Performance based pay systems must be carefully designed. Because student achievement depends on many factors that teachers cannot control, such as family circumstances and previous education, fair performance-based incentive systems should reward teachers for gains in student achievement, rather than for absolute levels of student achievement. Furthermore, because student learning involves cooperative effort, incentives must be designed to create cooperative and not competitive environments among teachers. For example, such team-spiritedness might be enhanced by basing the awards on school-wide achievement rather than the achievement of individual classes. Performance standards should not be narrowly based on a few easily measurable indicators of educational achievement, but rather should focus on gains in important skills and should be coordinated with other important goals of the school.[105]

School-based performance awards were introduced in Charlotte-Mecklenburg and Kentucky in 1991, and in Maryland in 1996. Studies have found that the success of these programs varies with the care with which they were implemented. Well-designed programs were successful in focusing attention on goals, channeling organizational resources to meeting those goals and motivating teachers, even though the best of these programs did increase the pressure felt by teachers.

The Need for New Schools

In addition to the students and teachers in classrooms, the physical condition of classrooms and educational materials are also important to a quality education. Communities across the country are struggling to address the problems of aging schools. In 1998, the average public school was 40 years old and schools in largely poor or minority districts were even older.[106] Many older buildings require extensive upgrades of their electrical systems in order to

install computers, upgrades made even more expensive for some schools by the presence of asbestos in their walls.[107] Older buildings may also require extensive renovations to be accessible to disabled students.

Increasing enrollments and reductions in class sizes will increase the number of classrooms needed per school, putting further pressure on aging educational facilities. The Department of Education estimates that $127 billion is needed to bring America's schools into good overall condition.[108] Already, 39 percent of public schools in the U.S. contain temporary additions, one-fifth of which are in less than adequate condition. Schools with higher fractions of poor and minority students[109]—the very schools whose students would benefit most from reduced class sizes—are more likely than other public schools to have temporary buildings and thus will have difficulty housing additional classes. To help address these problems, current Administration spending proposals would leverage $25 billion in school modernization bonds and $6.5 billion in loans and grants for urgent school renovation to help communities build and modernize 6,000 schools and make emergency repairs to another 25,000 over the next five years.[110]

New Educational Technology and Internet Access

As workplaces require more computer literacy from their workers, schools must prepare their students to enter the labor force with familiarity with these technologies. Internet access can also be a tremendous resource in classrooms, giving students new incentives for learning and

communicating, and connecting them to the resources of libraries, museums, and educational materials from around the world.[111] Tremendous increases in access to technology within American classrooms have taken place over the past 8 years, and federal programs, especially the E-rate program, have played a large role.

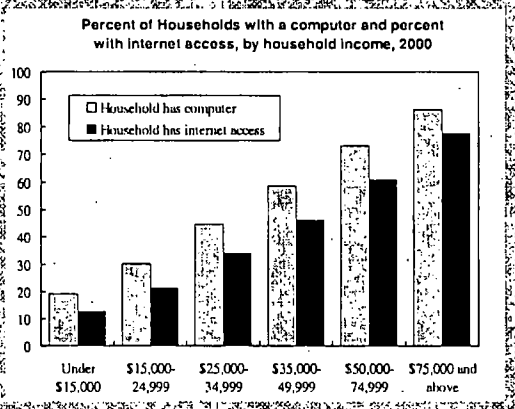
Between 1994 and 1999, tremendous strides were made in connecting public schools to the Internet. The number of public schools with a connection to the Internet nearly tripled between 1994 and 1999—by 1999, 95 percent of all public schools had a connection to the Internet. Increases in Internet connectivity were even more dramatic for classroom connections: increasing from 3 percent of public school classrooms in 1994 to 63 percent in 1999.[112]

<insert internet access chart here>

The federal government has helped local school districts make the transition to the digital age. Over the last three years, the federal government has allocated $6.3 billion through its E-rate program to connect school and library computers to each other and to the Internet.[113] These funds have been targeted to poor students: Schools with 75 percent or more of their students receiving free school lunches receive approximately ten times as much funding per student from the program as schools with the smallest percentage of poor students. Most of the funds have gone to establishing within-building connections between computers.[114]

Schools are Reducing the Digital Divide

Since 1993 computer use in America has grown at an enormous rate, revolutionizing the way Americans communicate, work and do business. Computer knowledge and access are increasingly important for success in today's society. Currently more than one-half of all US households have computers, and more than two-fifths have Internet access at home. However, Internet access is not spread evenly among Americans. Its use varies greatly with income and education--people in households earning more than $75,000 per year are almost 4 times as likely to use the Internet as people in households earning less than $15,000 per year.



Adults with college degrees are nearly 6 times as likely to use the Internet as adults who have not completed high school. There are also large differences by race. African Americans and Hispanics are substantially less likely than white and Asian Americans to use the Internet. While some of this difference is due to differences in income and education, a recent study finds that approximately one-half of the racial difference in access is not explained by these factors. As the level of technological literacy required by employers rises, there is an increased risk that individuals from disadvantaged groups who already face obstacles in the workplace will fall even further behind.

However, there is encouraging news. African American, Hispanic, and lower-income Americans are connecting to the Internet at faster rates than whites, Asians, or wealthier Americans. Notable

changes are occurring among school aged children, suggesting that the widespread availability of computers in the classroom is playing a role. Across all income and demographic groups, children aged 9-17 are more likely to use the Internet than are older Americans. And over the last few years Internet usage has grown faster among African American and Hispanic children than among white children, and faster among children in households earning less than $35,000 per year than among children from higher income households. Between 1998 and 2000, the gap in Internet usage between African American and white children decreased by 9 percent, although the gap in Internet usage between Hispanic and white children grew by 9 percent. The gap between Internet usage among children from households earning less than $35,000 per year and children from more wealthy households was unchanged.[115]

Other federal programs have also helped schools purchase new educational technology. In 1997-98, the most recent year for which such data is available, the federal government spent $688 million on increased access to technology in schools, in addition to the E-rate program funds. These funds were used primarily for the purchase of computers and for professional development in using new technology. During the 1997-98 school year, federal funds paid for one-fourth of new computers in schools. Federal funds were especially important in the acquisition of technology in high poverty schools, accounting for nearly 60 percent of funds for new computers in high-poverty elementary schools.[116]

<insert new computer funding chart here>

For computers to improve the quality of instruction, teachers must know how to use the technology and how to integrate its use into classroom instruction. Only one-half of the public school teachers with computers or Internet access in their schools report using these resources for classroom instruction.[117] Teachers who have received more professional development in using computers and the Internet, younger teachers, and teachers in schools with fewer poor students were most likely to report using computers and the Internet. However, a recent study found that only one-third of teachers with access to computers and the Internet said that they felt well or very well prepared to use computers and the Internet, and only one-fifth felt very well prepared to integrate educational technology into the classroom.[118] [119] Clearly, more investment in teacher preparation is needed. The federal government has helped with its Preparing Tomorrow's Teachers to Use Technology grant program, which supports 1,350 partnerships among colleges, educational agencies, high tech companies, and non-profit organizations. These partnerships are training 400,000 new teachers to be better able to integrate technology into the classroom. An additional $150 million has been requested for this program in the Administration's 2001 budget.[120]

Standards and Accountability

Large investments in education are taking place in hiring new teachers, in educational technology, in connecting schools nationwide to the Internet, and in professional development for teachers. Yet the changes in American public schools which have happened over the past decade go far beyond increasing the levels of these investments.

One of the most significant state-level strategies today is standards-driven accountability. It is hoped that establishing clear performance outcomes and systematically testing student progress will help teachers and students focus their efforts where they are most needed. Spurred in part by the 1994 Improving America's Schools Act and Goals 2000 Acts, state after state has implemented standards for what all students need to learn in school. Forty-nine states now have adopted statewide standards for what students should be studying in English, mathematics, science, and history and the social studies and thirty of these states implemented these standards since 1994.[121]

The establishment of these standards has been followed by an increase in standards-based assessment. Forty-eight states have adopted state tests to assess student performance relative to these standards in reading and math and 17 also assess student performance relative to science and social studies standards. Thirty-six states currently publish some form of report card for each school, measuring school performance against a number of indicators, including assessment tests.[122]

By implementing challenging, well-constructed tests, schools can raise the expectations for students, teachers, and parents and provide information about the relative performance of their local schools.[123] For many years, opinion surveys have shown that Americans believe our nation's schools are doing poorly but that their own schools are doing far better than the average.[124] Experts fear that without objective measures, such as standards-based tests, parents, teachers, and other local decision makers may not realize how children are doing relative to their classmates or children in other schools.[125] Broad-based tests of these sorts are relatively new in

the United States, but cross-country comparisons have demonstrated a positive correlation between student achievement and the existence of standards and external assessments. These results provide some indication that the imposition of standards may benefit our children.[126]

The federal government has played an important role in spurring the standards movement by granting more than $1 billion to help state and local education agencies in every state implement school reforms through the 1994 Goals 2000 Act and earlier supporting the development of voluntary national standards which formed the basis for many state standards.[127] In addition, the 1994 Improving America's Schools Act tied state standards implementation to continued receipt of Title I funds for poor schools. This legislation required that the standards used in schools receiving Title I funds be the same standards used in schools not receiving Title I if such standards existed. This meant that states had to implement uniform standards for all schools, rich or poor, or risk losing millions of dollars in Title I funds.

The federal government has also increased its assessment of American students' progress, better enabling us to evaluate these state-level reforms. [128] In recent years, the Department of Education has expanded the National Assessment of Educational Progress (NAEP) to track student performance in each state. From the NAEP, we now have a valuable set of baseline indicators against which we will be able to measure student progress. Amendments to the Individuals with Disabilities Education Act of 1997 further required that children with disabilities be included in state and district-level assessment programs, allowing us to measure the performance of these children as well.[129]

Increasing Public School Choice

A persistent thread in the last decade of educational change has been a call for parental choice. Critics have argued that with near-monopolies on public education in a particular locality, public schools have little incentive to respond to calls for changes. In addition, larger school districts may find it difficult to foster innovations in curriculum and school design on the district scale. Allowing more variation at the school level, with parents choosing between different school models, would both allow educators to perfect good innovations and give parents the option to choose schools which best seem to fit their children's individual needs.

Many states have responded to these critiques by allowing parents, teachers, or other interested parties to establish independent public schools chartered by state or local education agencies. These charters give schools autonomy over their operations, and exempt them from certain state and local regulations (although not from standards-based assessment) in exchange for strict accountability and results. Beginning with Minnesota in 1991, the number of states allowing such charter schools swelled to 36 states and the District of Columbia by the end of 1999. By the beginning of the 2000-2001 school year, there were 2,069 charter schools in operation nationwide and the number of such schools was growing by about 30 percent per year.

Although charter schools represent only 2 percent of all US public schools,[130] their rapid growth has made them the recipients of a great deal of attention, especially in areas where a significant percentage of students now attend these schools. Charter schools tend to be about one-third the size of nearby public schools. Most enroll students of similar racial and ethnic backgrounds as the students in their surrounding districts, although school districts with charter

schools tend to have larger minority student populations than the national average. Most reported that they became charter schools to "realize an alternative vision of schooling".[131]

Charter schools have great potential as laboratories of educational innovation, allowing individual schools to experiment with a variety of different educational methods and student populations, while maintaining public accountability. It is hoped that successful charter school innovations will eventually spread back to the broader public education community.

Helping Students Make the Transition from Secondary School to College

Other federal programs are helping primary and secondary school students make the transition from secondary school to further education. The Gaining Early Awareness and Readiness for Undergraduate Programs (GEAR-UP) partners nearly half a million students in high-poverty middle schools with local colleges and universities. These programs provide entire classes of students and their families with academic enrichment programs; information about college options, financial aid, and necessary preparations for college; and in some cases college scholarships. TRIO programs, such as Upward Bound, help 730,000 low-income, first-generation college, and disabled students prepare for and succeed in college. After 6 years of seed money from the federal government, all states have instituted local school-to-work programs to benefit secondary school students as they prepare for their working lives.[132]

Over the past 8 years, federal assistance to help Americans invest in college educations has also increased. Direct Pell grants have increased from a maximum of $2,300 per student per year to $3,300, while the Hope and Lifetime learning tax credits also reduced the cost of

education for American families. Fees and interest rates on student loans have been reduced, while the restructuring of the federal student loan program has saved billions in taxpayer dollars.[133]

Innovation and Access in Health Care

Another major aspect of any individual's well being is his/her health status. The quality of medical care available in the United States is the best in the world.[134] This excellent ability to treat medical conditions has been enhanced by recent medical innovations. In addition to the primary benefit of a better and longer life, improved health can also reduce the number of sick days for employees and thereby improve productivity ***(need reference for fact-check)***, which in turn contributes to economic growth.

While new treatments can provide better care, they are often very expensive, and thus contribute to high medical spending. This has prompted the health care system to evolve processes designed to encourage utilization of the most cost-effective treatments. Further, the higher cost of health care treatment makes health insurance coverage very important, yet at the same makes it more expensive and unaffordable for some families. In this section, we will illustrate the value of some medical innovations of recent years. We will also discuss the challenges the health care system faces in determining how to apply technology appropriately, and how the health care delivery system has tried to address that challenge. Finally, we will review the effectiveness of the health insurance system and issues that any proposal to change the health insurance system must address.

Innovation

Dramatic innovations in the medical care—often driven by computerization or biotechnological innovations—have led to improvements such as treatments for previously untreatable conditions, less invasive procedures and more accurate diagnostic techniques. For example, the development of minimally invasive laparoscopic surgery was made possible by advanced digital technology[135]. Using new robotic and computer-generated positioning of instruments and advances in high-resolution three-dimensional video cameras, surgeons can now perform a wide range of operations with few tiny incisions. During the 1990s, Magnetic Resonance Imaging (MRI), which provides very high resolution anatomical and pathological images to enable more accurate diagnosis, was widely diffused in the United States and radically improved. When doing brain surgery, new highly computerized open MRI can provide continuous pictures to guide the surgeon. A treatment of Alzheimer's disease, which afflicts more than four million Americans[136], was not available until the introduction of new drugs in 1993 that enhance cognitive function and delay disease progression.[137] These improvements are not isolated cases. The number of new drugs approved mirror this trend—from 1995 to 1998, an average of 37.5 new drugs per year were approved, up from 25.2 per year from 1989 to 1994, and 22.8 per year from 1985 to 1989 (New Molecular Entities).[138]

Costs and Value of Innovative Treatments

By requiring fewer medical inputs to produce the same or better health outcomes, medical innovations can be cost-saving. For example, techniques developed and widely diffused between 1972 and 1990 have made cataract surgery a ten-minute outpatient procedure, eliminating one week of post-operative hospitalization.[139] As a result, the treatment cost per cataract extraction has declined.[140] Some pharmaceuticals can be cost-saving innovations. Drug therapies for peptic ulcers[141] and depression,[142] for example, can sometimes substitute for more expensive abdominal surgery and psychotherapy and are therefore making the treatments for these conditions cheaper. Nonetheless, cost-saving innovations can contribute to higher total expenditures because more procedures are performed due to lower unit price, reduced risks, and/or better outcomes of treating these conditions[143].

As innovations produce better care, they can also increase costs, by requiring more intense and expensive inputs to produce better outcomes, such as MRI and the treatments for heart attacks. In addition, the innovations that provide treatments for previously untreatable conditions, such as premature births, one cause of growing expenditures. From 1975 to 1995, intensive cardiac interventions such as catherization, coronary bypass, and angioplasty were developed and diffused, with usage 4 to 15 times higher for heart attack patients.[144] This was reflected in an average annual real increase of 4 percent in the cost per heart attack treated. Although costs increased, life expectancy after heart attacks rose by 8 months between 1984 and 1991,[145] and innovations in the acute management were estimated to account for about 55 percent of the declining mortality. [146,147] ***[consider automatic implantable cardiac defibrillate, which is a computerized chip for irregular heart-beat problem]***

Whether the rapid innovations are worth the increased costs depends on the value of the resulting health improvements. Research indicates that better medical interventions have provided significant health improvements. In addition to the contribution of technology to heart attack treatments, other estimates looking at congestive heart diseases also found medical technology played a large role in decreased mortality (43 to xx %). Between 24 and 41 percent of elderly people's decline in functional disability has been attributed to innovations in medical care. These innovations have contributed to overall advances in health: between 1990 and 1998, life expectancy at birth rose approximately 1.3 years, and life expectancy at age 65 rose 0.6 year. The rate of chronic disability declined 1.3% annually between 1982 and 1994.[148,149 150] Another study sought to estimate the overall value of innovations relative to their costs between 1970 and 1990. It concluded that the lifetime value of higher quality and longer life outweighed the higher health expenditures. In sum, medical innovations are cost-effective on average, and new technology has made the production of health more efficient.[151]

The health care system has provided stronger incentives for innovations that produce *better* health outcomes rather than less expensive treatments. One reason for this is that people prefer the best possible treatment, and thus, patients and physicians rarely choose technology that produces 1970s results at lower cost to the latest technology that produces better results at higher cost. Second, malpractice lawsuits may enforce the latest technology as the standard of care. The legal criteria to establish a medical negligence is the conventional standard of care, and thus most physicians would not use outdated technology.[152] Finally, the pace of basic scientific discovery and information technology developments can spillover into medical treatments, creating an increasing rate of medical innovation independent of health care system. Therefore,

without cost constraints, cost-increasing innovations for better health will dominate cost-saving innovations.

Studies suggest that medical innovations have been the main force in rising health care expenditures in the last two decades, accounting for more than 50 percent of the long term growth.[153, 154] Rising health expenditures can create access barriers indirectly for everyone, by driving up health insurance prices. However, because innovations are beneficial, a system that simply focuses on 'containing cost' would eliminate beneficial interventions. Thus, medical innovations present two challenges: determining the situations where innovations are likely to improve outcomes that can justify the additional cost, and structuring a system that utilizes medical technology in a efficient manner to improve health outcomes as much as possible.

Delivery system innovation

The new economy involves not only technological but also organizational innovations, and managed care has evolved as a cost-saving organizational innovation that attempts to address rising health expenditures. Because health insurers pay for most health care, the incentives embedded in the health insurance system strongly influence the efficiency of the entire health care system. Before the 1990s, the predominate health insurance arrangement was fee-for-service (FFS), where patients face low co-payments and providers are reimbursed on a cost-based method after each medical encounter. This system provides great flexibility to those who determine the course of treatment for a medical condition, which is desirable given the complexity of medical needs and variability of appropriate responses. However, because the

system reimburses on the basis of utilization, it also provides few direct incentives to use the most cost-effective health care technologies and practices. Specifically, physicians have incentives to over-prescribe services and procedures, and patients have incentives to oversubscribe to those services. To address these problems, the incentive structure in the health insurance system was changed so that providers would choose the services efficiently.

Managed care employs two mechanisms - financial and non-financial - to alter providers' incentives: first, it uses capitation, which aims to pay providers a fixed payment for a pool of patients. Under this fixed payment, providers have the greatest incentive to reduce treatment costs, as they retain all savings above the costs. The second set of tools managed care plans use is non-financial utilization management, such as treatment guidelines, gate-keeping, and monitoring physicians' performance to reduce low-valued services. In addition, managed care can influence the expected profitability of new technology by reducing reimbursement and restricting utilization. Hospitals and physicians would in turn slow down the rate of acquiring and using new and expensive technologies because of lower expected profitability. By balancing patients' desire for better health and the cost-reduction incentives of providers, managed care can encourage more cost-effective utilization of technology, and promote innovations that improve health and reduce costs.[155]

However, while addressing incentive problems in traditional health insurance practices, managed care creates different problems. These include incentives for structuring insurance plans to select healthy patients and the under-provision of services[156]. Fully prospective payment provides a strong incentive to select healthy patients whose health care costs will be low, rather

than actually improving efficiency. Furthermore, providers have an incentive to restrict even cost effective services because they receive no additional revenue from providing these services. Because patients frequently lack information about the effectiveness of alternative treatments, and are thus unable to press for better treatment, this problem can be severe. Therefore, the optimal incentive likely lies between FFS and capitation, and involves partial cost-sharing by providers and patients via copayment and coinsurance. Unfortunately the ideal incentive design is still unknown. As managed care plans evolve to allow patients more choices, the ability to influence utilization is undermined. Consolidation among physicians and hospitals in the 1990s created organizations that pay providers by salary or by FFS, so that fewer physicians and hospitals actually operate on a fixed payment basis. Consequently, current managed care plans are quite different from the original plans, because both sets of tools managed care uses to influence cost-effectiveness have been significantly relaxed.

Empirical evidence suggests that managed care was one of the factors that slowed the growth in total health expenditures in the last decades[157]. These reductions were achieved by reducing utilization of more expensive procedures, and by paying lower physician and hospital fees.[158] However, further reductions in utilization may not be feasible, and managed care's ability to restrict fees in the future is not certain because fees cannot not fall below costs[159, 160]. Thus, there is uncertainty whether the observed effect on expenditures will continue.

< insert chart on expenditure growth and managed care here >

If technological progress remains the key force driving expenditures, managed care's effect on the rate of health expenditure growth will depend on its ability to influence the types of innovation. If managed care can increase cost-saving innovations, then the rate of growth may be slowed. However, if patients continue to value health highly and are willing to pay for any innovations, managed care may be unwilling or unable to impose cost-saving innovations. The evidence of managed care's impact on the types and rate of technology adoption is mixed. Some researchers found that increased managed care enrollment not only restricts the adoption of cost-increasing technologies, but also reduces utilization of the new technologies[161] [162]. One study found evidence of more cost-effective adoption and utilization of Neonatal Intensive Care Units in areas with a high concentration of managed care, while a different study found no effect. Thus, managed care's longer-term impact on health expenditures is uncertain.

e-Health (Online Medical Information)

Information asymmetry has been a long-recognized problem in medical care. Patients often do not know as much as their physicians and therefore cannot participate actively in medical decision making. Instead, patients rely heavily on their physician's advice. Similarly, patients have little information about the quality of health care providers. Because quality of care is hard to measure and information is costly, patients often make choices about health plans and providers with insufficient data. The Internet can play an important role on bridging the information gap thereby significantly altering the relationship between patients and providers.

What's available

There are currently more than 2 million Internet web sites providing medical-related information to both physicians and their patients.[163] This information covers a wide array of topics including the diagnosis and treatment of specific diseases, information about prevention, public health, and health behaviors, and alternative therapies. The Internet is also being used as a forum for discussion and support groups.

Information on the quality of providers' is also growing. Within second individuals can now access information about a physician's training, experience, and litigation history. Data on the performance of hospitals and health plans with respect to the treatment of specific diseases and patient satisfaction can also be had.

Numerous organizations sponsor medically related web sites including the government (AHQR), medical professional organizations (AMA, AHA), most health plans, employer health coalitions, and other non-for-profit organizations. However, a majority of the owners are commercial, for-profit businesses.[164]

Utilization pattern

The Internet is providing medical information to a large fraction of Americans. About 60 million[165] (or 22 million[166]) Americans *(% of population age xx-xx?)* searched for health information on line in 1998 and the number is expected to increase in 2000. An analysis of inquiries made to one university hospital web site found that most of requests (40%) could have been answered by a librarian *(to clarify when get the full article)*; 28% could have been answered

by a physician via email; and 27% were cases in which a visit to a physician would be necessary to deal adequately with the issue. In only a few cases (5 out of 209?) did patients attempted to self-diagnose.[167]

Potential impact

An important aspect of the use of online medical information services is whether it complement a physician's input or substitutes for advice from a physician. The ready availability of medical information may help improve the efficiency of office visits if patients know what questions to ask and what concerns to raise before the visit. It can also eliminate unnecessary visits that can be answered without a costly office visit. As shown earlier, many of a patient's concerns can be addressed online or email answers by physicians or trained professionals.

There are also many potential risks with these web sites. While the Internet can provide information, it is not clear that the information can be well understood by users. One study showed the average medical information on selected web sites was written at a 10th grade level, which is not comprehensible to the majority of patients.[168] To the extent that patients use these information to self-diagnose and self-treat, this information could be harmful. Furthermore, the quality of information varies greatly, and many search engines are not very effective. There are also potential commercial interests that influence the content of web sites. It is questionable whether patients have the ability to distinguish quality information from commercially motivated advertisements. Finally, patients from different socio-economic background may not have equal access to information, and privacy protection is still a serious problem. Although online

information can potentially redirect a better patient-physician relation, its development must proceed with caution.

Improving Health Insurance Coverage

As noted, the health care system in the United States is capable of providing the highest quality health care in the world. However, that health care can also be very expensive, particularly treatments for non-routine health care. Even routine health care costs are beyond the means of some people. Thus, health insurance is an important means of ensuring people can get health care. However, about 43[169] million Americans were without coverage in 1999. In this section we will discuss the current state of the health insurance system, and some approaches that have been considered for extending health insurance to more people.

The Health Insurance System

The American health insurance system relies primarily on employer-sponsored health insurance--about 63[170] percent of all Americans (74[171] percent of all insured people) are covered by an employer-sponsored program. One reason for this dominance of employer-sponsored group insurance is that the Federal tax code favors employer-sponsored insurance. Insurance premiums paid by firms on behalf of employees are not included in the employees' taxable income, and in certain arrangements such as flexible spending accounts employees can make contributions to their health care expenses with pre-tax dollars.

There are several valuable aspects of the employer-sponsored insurance system. One benefit is that it encourages substantive risk pooling among a firm's employees, enhancing insurance affordability and availability for all risk categories. In addition, firms can hire benefits administrators who can evaluate different health insurance policies and act on behalf of the employees to ensure quality plans are offered. Finally, insurance companies are able to provide lower premiums to large employers, in part because of the lower administrative cost resulting from economies of scale.

Because low-income people have a lower marginal tax rate and are less likely to have insurance, the tax-preferred treatment of employer-sponsored health insurance provides them a smaller benefit (See chart). In addition, those who do not obtain health insurance through their employer must pay for insurance with after-tax dollars. This includes not only the unemployed, but also those people who work for employers that do not offer health insurance, groups that are more likely to need a subsidy to be able to purchase health insurance.

<insert chart on tax benefit by income here>

People without employer-sponsored health insurance and who do not qualify for publicly funded programs must enter the individual insurance market if they want coverage. This market can present problems that limit affordable access. Some insurers may chose not to cover people with pre-existing health problems, or sell policies that omit coverage for those conditions. Insurers may also charge different premiums based on an individual's perceived risk; for example, people with diabetes may have to pay significantly higher premiums because they are

more likely to experience health problems. In some cases, these premiums can be unaffordable. In addition, individual policies have higher administrative costs.

Publicly provided health insurance programs—Medicare, Medicaid, and the State Children's Health Insurance Program (SCHIP)—provide an important source of coverage for many people. Created in 1965, Medicare and Medicaid provide health insurance for elderly, people with disability, and low-income Americans. Over 36[172] million individuals received medical insurance through Medicare in 1999.[173] Medicaid offers federal assistance to States that provide medical care to low-income Americans. Medicaid served over 28[174] million people in 1999. Historically, eligibility for Medicaid was primarily linked to eligibility for welfare assistance, that is, for very low-income single-parent families. Medicaid coverage was gradually extended through a series of expansions in the late 1980's and early- and mid-1990's, and formally de-linked from cash assistance eligibility by the 1996 Personal Responsibility and Work Opportunity Reconciliation Act to cover more low-income households, including both single and 2-parent families.[175] In 1997, the federal government created SCHIP to target the growing number of uninsured children in families that have too much income to be eligible for Medicaid but too little to afford private insurance. Through SCHIP states can provide health insurance to eligible children through Medicaid, a separate state non-Medicaid program, or a combination of both.

<insert chart on health insurance coverage by income here>

A significant number—42.6 million people, or 15.5% of the population—remain uninsured. (See chart) The status and source of insurance coverage varies with income and other demographic characteristics. Because of the near-universal coverage of elderly by Medicare, only 1.3% of the elderly were uninsured in 1999. About 17% of the non-elderly were uninsured. Non-elderly people in lower-income households are more likely to be without insurance: of people in households below the poverty line, 36% were uninsured in 1999. Medicaid was the source of insurance for almost two-thirds of the non-elderly those who had coverage, while 27% were covered by an employer's plan. In contrast, only 9% of non-elderly people in households with income greater than 300 percent of poverty were uninsured, and 92% of the covered had insurance through an employer.[176]

Part-time employees are much less likely to be insured—31 percent of people in households with only part-time workers are uninsured.[177] This is due in part to firms' restricting eligibility to exclude many part-time and temporary workers from health insurance coverage.[178] Twenty-six percent of small business adult employees are uninsured (including those covered under another person's policy), compared to 12% of large firm employees.[179] This reflects the fact that small businesses are less likely to offer health benefits,[180] perhaps in part because small firms have a higher share of part-time workers.[181] There are significant differences in health insurance coverage across different racial and ethnic groups. Approximately 11 percent of non-Hispanic whites, 21 percent of blacks, 33 percent of Hispanics, and 21 percent of Asians and Pacific Islanders were uninsured in 1999.[182] **[NEC: rural vs urban]**

Options and Issues in Health Insurance Reform

Three approaches to subsidizing health insurance to extend coverage are often considered. One of these is providing an "above-the-line" deduction of premiums for insurance purchased in the non-group market, which enables people to deduct the full amount of their premiums from their taxable income, thereby reducing taxes. A second approach is to directly reduce taxes by providing tax credits, which directly reduce tax payments, for health insurance premiums. A third approach is to extend government-provided insurance to more people, like SCHIP, which funds state insurance programs for children in low-income households. All of these proposals seeking to expand health insurance coverage must address the possibilities of crowding out current health insurance and exacerbating adverse selection while effectively reaching the uninsured.

Tax incentives as well as direct programs for expanding health care coverage can crowd out existing health insurance by leading people to drop their current coverage in favor of a newly subsidized alternative. A new subsidy may also prompt an employer to stop offering coverage and thus encourage its employees to use the new publicly-financed insurance or tax subsidy. When crowding out occurs, government expenditures go not just to the newly insured; some fraction of the money goes to people who had coverage and are now switching to a newly subsidized plan. If crowding out is severe, the cost to the government of each net newly insured person increases. Moreover, some employees may lose coverage and be unable to find replacement coverage, reducing the net increase in coverage, or possibly leading to a net decrease.

The mid-range of studies of the Medicaid child eligibility expansions of the late 1980s and first half of the 1990s found that about 10 to 20 percent of the increase in Medicaid coverage was due to a reduction in private insurance coverage. Because Medicaid covers mostly low-income people who are less likely to have private insurance, crowding out is expected to be modest. In general, if a tax subsidy or expanded government program were available to people with high income to reach more uninsured, more crowding out might occur since the eligible population is more likely to include people with coverage. Thus designing a health insurance subsidy that is effectively targeted to people who are less likely to be insured will limit crow-out.

Tax credits and tax deduction plans that subsidize non-group health insurance may produce adverse selection in the employer-sponsored insurance market. Adverse selection occurs when relatively healthy, low-risk individuals believe the cost of insurance is greater than the benefit, and therefore leave the risk pool. As these healthier people with lower health care costs leave the original pool, the average cost per person remaining in the pool will increase. When the medical costs of the remaining participants rise, resulting in higher premiums, still more people will leave that risk pool. The result is a spiral of rising premiums for those remaining and declining enrollment. People who still desire to purchase health care insurance may experience prohibitively high premiums.

Studies of insurance choices by employees offered multiple health insurance plans have shown that adverse selection occurs in the group market. One study of government employees found that premiums for plans with more generous benefits increased much faster than premiums for plans with less generous benefits. The study attributed the variability in premiums to the

poorer health status of the people selecting the plans with generous benefits; healthy people opted out of the expensive plan. A second study, where employees were offered a choice of several plans, found that healthy employees were less likely to choose the more generous benefit plan, and that the premium for the most generous plan became so expensive that the employer dropped it.

Employment-sponsored group health insurance provides a good base for risk-pooling because workers are attracted to firms for reasons other than health insurance, and therefore a wide range of health risks exists within a firm. The existing tax subsidy encourages healthy workers to remain in the group pool, because of the less favorable tax treatment for non-group purchased insurance. However, if a tax credit or above-the-line deduction for non-group insurance is available, non-group insurance may be more attractive, thus leading to adverse selection in the group insurance risk pool. Adverse selection can also affect the non-group pool. Proposals to reduce the rating variability in the individual market must also be careful to employ pooling mechanisms so as not to drive out the healthy individuals.

Finally, design details of a new tax policy or a new direct subsidy programs will elicit different participation rates. In addition, a tax credit or deduction that is available only after premiums are paid may not help individuals who do not have the funds to pay up front costs. A partial subsidy might not increase insurance coverage among low-income people, because even modest out-of-pocket expenses can discourage their participation. This may especially affect families without health problems, who may choose to forgo health insurance to pay for items such as food and housing. Tax deductions, because they provide only limited benefits to those

with low income and because most uninsured individuals are low-income, are not likely to lead to a significant expansion of health insurance coverage. Further, a complex application process designed to determine eligibility for government-provided health insurance may have the unintended side effect of inhibiting participation by otherwise qualified individuals.

Meeting the Challenge of Covering More People

The Administration has taken steps to extend coverage to more people. As a result, the number of uninsured has declined for the first time in 14 [?] years. Particularly noteworthy successes have been the expanded eligibility for Medicaid and the creation of the SCHIP. In addition, the Health Insurance Portability and Accountability Act of 1996 limits exclusions for pre-existing conditions in employer health insurance plans and for people converting from employer's plans to individual insurance. The Administration proposed a FamilyCare program to extend publicly provided insurance to the parents of children covered by SCHIP, covering more low and moderate income families.

Although much has been done to ensure access to health care for millions of individuals, a number of challenges lie ahead. Prescription drugs have become a significant health care expenditure for many, particularly for the elderly. Helping individuals afford needed prescription medications is a priority. We must also prepare for a growing elderly population and forecasted increase in long-term care needs. And finally, we must continue to work towards providing access to the health care system for the millions of Americans who remain uninsured.

Building Livable Communities

As the New Economy presents greater options and opportunities for Americans, it also poses critical challenges for securing the livability of our existing and developing communities. Throughout much of the 20th century the population shifted from central cities to suburbs, with this trend accelerating in the last decade.[183] From 1990 to 1999 the suburban population grew by nearly 19 percent, compared to population growth of only 6 percent for central cities. This rate of increase is striking, relative to rates of growth during the 1980s: 15 percent in the cities and only 13 percent in the suburbs.

However, the New Economy has witnessed a change in the pattern of job location as well. While central cities are impacted by growth, regardless of where in their vicinities it occurs, they are no longer the source of the majority of job growth. Rather, new jobs and new industries are also springing up on the fringes of cities, in "technology parks" or "research corridors." Between 1979 and 1999 cities' share of metropolitan office space significantly diminished. In 1979, 74 percent of office space existed in central cities, and only 26 percent was found in suburbs. By 1999 the central city share of office space dropped to 58 percent, while the suburban share expanded to 42 percent.

Though many still seek the high quality of life available in America's cities, others are opting for outlying communities. These suburbs have the potential to offer the best of both worlds to American families: the amenities and quality of life many prefer, and the availability of jobs formerly associated only with central cities.[184] However, there are also drawbacks to this

trend, and communities must invest now in developing plans to channel this growth to ensure that rapid growth does not spoil the attractive aspects of entire regions.[185] With new growth comes the need to grow in a manner consistent with social well-being and environmental quality.

Economic Forces Driving Suburbanization

Economists have noted the positive relationship between the density of economic activity and productivity.[186] In the past many economic gains were attributed to access to natural resources and means of transportation. In contrast, today's agglomeration economies are often based on the clustering[187] of firms in the same industry which gain from sharing ideas, consumers, and specialized pools of skilled workers. Familiar examples include the financial industry cluster in Manhattan, the oil and gas cluster in Houston, and the high-tech cluster in Silicon Valley. Often freer from traditional resource-related ties to specific locations, New Economy firms are able to choose from a wider array of potential business sites, and may locate in a community for its proximity to other firms, its cultural amenities, its livability, etc.[188]

With current development occurring on the outskirts of cities, rather than in central cities themselves, development is now consuming land at a rate twice that of population growth. An average of 2.3 million acres of land is being consumed annually, with a significant share of this in fringe suburbs or smaller cities – residential development on lots of one acre or more. Such discontinuous growth is commonly known as "sprawl." It is important to recognize that rapid growth does not have to be unplanned growth; rather, smart growth principles can accompany and inform successful economic development.

Given the outward expansion of these new suburbs, it is not surprising that rural areas just beyond the edge of urban settlement have seen rapid growth. In metropolitan counties that were primarily rural in 1990, population rose by 20 percent from 1990-99 – a much higher rate than that in any other type of county. Such areas are becoming low-density urban areas as farmland is converted to other uses.

Several economic explanations exist for this form of suburbanization. First, for many of young, growing firms, urban areas exhibit diseconomies that offset benefits associated with the central city. The building stock in many central cities is old, and it may be costly to upgrade existing facilities to current technological standards. Although efforts are underway to deal with these problems, such as the President's Partnership to Advance Technology in Housing (PATH) which works with the building industry to develop provisions that make building codes more receptive to rehabilitation, rents in revitalized or redeveloped urban areas may still be too expensive for new firms to afford to locate there. Similarly, the unintended consequences of environmental cleanup laws may discourage reusing urban properties due to fear of cleanup liability.[189] Despite the more than $2.3 billion in leveraged economic development occurring at brownfields through the national Brownfields Initiative,[190] there are still hundreds of thousands of properties for which reuse is hampered by real or perceived environmental contamination.

For these reasons it may be more cost-effective to "start from scratch" in outlying areas. For example, firms in new "edge cities" may be more attractive to workers seeking to live near

work, and avoid the congestion and pollution of a central city. Also, by locating near similar organizations, firms can generate new externalities and benefit from shared resources. In the most well-known examples, firms in Silicon Valley, California; Cambridge, Massachusetts; and the Research Triangle of North Carolina benefit from access to pools of specialized high-tech labor.

Sprawl, defined as dispersed development beyond metro centers, often stretches along established highways and throughout rural areas. Identified by low-density residential and commercial settlements, sprawl often requires reliance on automobiles for transportation, including long-distance commutes. Jurisdiction over transportation routes and systems, as well as over housing and economic development decisions, is often fragmented among different local and state governments, resulting in little coordinated influence on land-use decisions. Carefully aligning decision making with the government entities to which tax revenues accrue can help. Facing such problems may require regional commissions concerned with the spillover effects that community decisions have on neighboring municipalities. Often, sprawling communities are divided by great fiscal disparities and distinctly zoned land uses.[191] Planners interested in regional growth may be better able to work with communities to accommodate new development collaboratively, ensuring proper population density throughout a region. HUD maintains that if economic growth took into account the underutilized resources of central cities and the externalities of sprawl, central cities would capture a larger share of growth. One example of their efforts is the HOPE VI initiative that seeks to eradicate and replace severely distressed public housing, and to revitalize surrounding communities.

Challenges of new growth.

In terms of jobs and tax revenues, the rapid economic growth of technology centers provides benefits to suburban communities and central cities alike. However, this growth can also bring significant costs to entire regions.[192] Many suburban communities are becoming increasingly congested and are in danger of losing the very attributes that make them attractive places to live and work. Increasing population strains public resources like schools and parks. Affordable housing is moving farther away from jobs, increasing average commuting distances throughout metropolitan areas. However, commuting is only one factor in increasing congestion. Four out of five household trips are now for non-commuting purposes, and distances between home, shopping, schools, recreation, etc. are increasing[193]. The resulting traffic problems, worsened by limited public transportation, often make driving difficult and time-consuming and increase the demand for new road construction; however, transit-oriented development can help.

Unplanned growth affects environmental quality,[194] as evidenced by water quality, air quality, and land use patterns.[195] Increases in paved surfaces, including roads, buildings, and parking lots, can contribute to deterioration of water quality and to an overall loss of greenspace. This loss of greenspace leads to less effective natural drainage, poorer water quality, and a dramatic increase in the potential for flooding in some areas. For example, residents along California's Russian River experienced four major floods in 3 consecutive years. Hydrologists attribute such events in part to urbanization's effects on stream flow: downstream runoff into streams and rivers increases as impervious surfaces from development increase.[196] Impervious surfaces are defined as any impenetrable material that prevents infiltration of water into the soil.

Increased traffic not only affects commuting and quality of life, but also ambient air quality, as emissions can lead to elevated levels of ozone and particulate matter. While national air quality trends have improved over the last 10 years, as of September 1999, 121 metropolitan areas still did not meet the national standards for air pollutants. This pollution affects the health of residents, especially those in sensitive segments of the population. For example, incidence of pediatric asthma, aggravated by particulate matter, sulfur dioxide, and ozone, has increased 55 percent between 1982 and 1996.

Economic Dimensions and Solutions

One of the difficulties with ensuring appropriate development is that the costs and benefits of development are typically borne by different entities; decisions benefiting private individuals may have adverse public effects, but private decision makers are unlikely to weigh these social costs. For example, individuals may prefer homes on large private lots, distant from both city centers and major highways. However, these homes require new roads, more driving, and the installation of public utilities. If a large number of individuals chose to live in such homes, the negative externalities that the decision generates – increased traffic, air pollution, impervious surfaces, and increased local property taxes – can outweigh the benefits individuals receive. The results of such decisions are evident in many areas of the country, and are particularly vivid in Atlanta, Georgia.

Atlanta, Georgia: Challenges to Smart Growth

Ranked by some as the nation's most sprawl-threatened large city, Atlanta continues to expand at a phenomenal pace. From 1980 to 1998 the Atlanta area's population grew almost 68 percent, with almost all of this growth occurring beyond the city limits. According to some studies, the Atlanta metropolitan area loses 500 acres of greenspace, forest, and farmland each week. This means that greenspace is disappearing to development faster than in any metropolitan area in history, and the city is suffering its consequences: water quality of the Chattahoochee River and Lake Allatoona is deteriorating, and air quality is in violation of clean air standards. Traffic congestion costs from lost time and wasted fuel are estimated at an overwhelming $1.5 billion a year. With an average work commute by car of 37 minutes (which is estimated to stretch to 45 minutes in 20 years, given continued growth), Atlanta residents may enjoy New Economy benefits, but are clearly suffering the resulting costs of sprawl. Motorists in Atlanta lead the nation in miles driven per person per day, totaling over 100 million miles logged daily by its drivers; the region's growth has exacerbated isolation of minority and low-income communities; and there are tremendous geographical imbalances in both job availability and housing affordability.

The Atlanta Regional Commission (ARC) is attempting to limit and coordinate this expansive growth. To help this coalition of regional governments, the Georgia Regional Transportation Authority (GRTA) was created by the state government in 1999, with broad powers to manage transportation and air quality projects and land use in air pollution non-attainment areas, and particularly Atlanta. Atlanta metro governments are opposing a perimeter highway proposal for the reason that it threatens urban investment and encourages further sprawl. The ARC, supported by the state government, is trying hard to provide and encourage alternatives to single-

motorist car transportation. The ARC and GRTA are also seeking to encourage development that incorporates elements of smart growth by revitalizing older community and emerging activity centers to promote greater livability, introducing modal choices, and advocating increased mixtures of land uses and housing types.[197] However, the momentum of sprawl continues, and Atlanta faces a serious challenge to channel future growth toward building sustainable, attractive communities.[198]

The true economic cost of building a new home should include the costs of the associated externalities created by developers and homeowners, but quantifying these social and environmental burdens is more difficult than identifying the private costs of development. There are, however, positive steps that can be taken in this direction. For instance, studies have found that the additional tax revenue received from new development does not cover the installation of roads and water utilities, and the provision of public services to new residents. If new development were required to bear the full cost of services, including infrastructure, the resulting pattern of development would be less like urban sprawl. Many governments have begun to assess impact fees on new construction so that the financial burdens of infrastructure and public service provision are included in development decisions.

Communities are beginning to use other kinds of economic incentives[199] to achieve outcomes more consistent with smart growth. For example, some communities, such as South Bend, Washington, have imposed fees on impervious surface area to encourage development with less detrimental effects on water quality and flooding potential. Other communities are using road pricing to improve traffic patterns. San Diego charges solo drivers in the express

lanes of I-15 higher prices during congested times than during off-peak hours. The use of electronic transponder technology to identify motorists and collect tolls makes this system possible without the significant slowdowns caused by toll collection plazas. Other communities use transferable development rights to provide incentives for maintaining land in agriculture and other uses that maintain open space and provide ecological benefits.

The Clinton-Gore Administration's 30-point Livable Communities Initiative[200] encourages "smart growth." It sets forth several principles to align Federal policy efforts with smart growth priorities, and to encourage greater planning and coordination over larger regions to resolve existing negative externalities. The Livable Communities Initiative seeks to sustain prosperity, expand economic opportunity, enhance the quality of life, and build a stronger sense of community. It provides funds for regional smart growth efforts, including Better America Bonds for state, local, and tribal governments. The initiative aims to reuse brownfields and preserve green spaces, ease traffic congestion, restore senses of community, promote collaboration among neighboring municipalities through regional governance, and enhance economic competitiveness. In addition, such smart growth efforts attempt to counter various socially undesirable effects of sprawl: racial segregation, concentrated poverty, decreased personal interaction, and a less active civil society. Initiatives on the state and local levels are beginning to have real impacts on communities. Examples of such progress are found in the State of Maryland[201] and the City of Chattanooga, Tennessee.[202]

Examples of Smart Growth

Many governments are making significant efforts to encourage smart growth. For example, Maryland has established the following goals in its smart growth program: to preserve its most valuable remaining natural resources; to support existing communities and neighborhoods by targeting state resources to development in areas where the infrastructure is already in place; and to save taxpayer dollars by avoiding the unnecessary cost of building the infrastructure required to support sprawl. It also ensures that the State will regularly evaluate the program's effectiveness. By winning Federal grant money, reprioritizing within the state budget, and designing financial incentives for businesses, local governments, and homeowners, the State has been able to leverage the funds necessary to emerge as a leader in the smart growth community, while preserving local decision-making authority.

Similarly, the smart growth success of Chattanooga, Tennessee, affirms the conviction that Americans can enjoy both economic prosperity and a high quality of life. Chattanooga's economy had historically been based on iron foundries, textile mills, and chemical plants, which were not providing the growth and employment the city required. However, through thoughtful economic development efforts, Chattanooga has become a model for other cities seeking environmentally sound urban renewal. Through extensive grants from private foundations, along with Federal and local public funds, Chattanooga has built successful public-private partnerships throughout their visionary redevelopment process. The city now prides itself as a "laboratory" for sustainable development projects involving rezoning, reclamation, revitalization, and

redevelopment. Illustrating how older cities can thrive in the New Economy, Chattanooga boasts a 22-mile "Riverwalk" with picnic areas, the world's largest freshwater aquarium, a sculpture garden, waterfront housing developments, an electric-bus public transit system, footbridges, and an arts district.

Many of the areas of new and rapid growth are characterized by the combination of an educated workforce that places emphasis on the quality of life and favorable economic conditions. Therefore, they have both the constituency to demand change and the resources necessary to implement it. There is evidence that business and community leaders are already recognizing the costs and impacts of sprawl and acting to mitigate its negative effects. In areas such as the Washington, D.C. Beltway, Boston, San Francisco, and Seattle, leaders are acting to improve land use and transportation decisions and to enhance environmental quality. The success of these endeavors will depend on the ability of these communities to make hard choices and find creative solutions to the challenges of urban sprawl.

Conclusion

These historic improvements in the well-being of Americans have come in large part because of Administation policies that have led to unprecedented growth. This continued growth has provided sufficient opportunities to those who are often the last to benefit from growth. Our most disadvantaged Americans have also benefited from particular policies that have helped ease the transition from welfare to work, improved educational opportunities, and increased access to

health care. By improving outcomes for those who are in danger of being left behind the nation as a whole benefits. Helping those on welfare secure employment, increases our labor force helps our economy expand further. Throughout this Administration we have successfully maintained high levels of economic growth along with low levels of inflation. We have kept interest rates low, helping Americans purchase homes of their own. We have created jobs, bringing milions into the work force. We have also invested in the education of our young people, helping to ensure that future generations will have the skills necessary to succeed in the new economy and to help our country become even more productive. And we have provided health care to millions more Americans. The Administration has also worked to ensure that our communities have the amenities families desire, safe streets, lower pollution, reliable transportation, and access to green spaces.

While these gains have been substantial, there are also many challenges that remain, challenges that can be helped by continued policies that combine economic growth with policies that reach out to help those who still need our assistance. We have made enormous strides in helping the least well-off Americans but there are still substantial disparities in income, education quality, access to health and the quality of life. These differences must be addressed. Furthermore, we must consider how to help those who need additional assistance even in this time of strong economic growth, our elderly, our disabled, and our children. Americans are certainly better off than we were 8 years ago, but there is still more we can do to ensure an even brighter future for all Americans.

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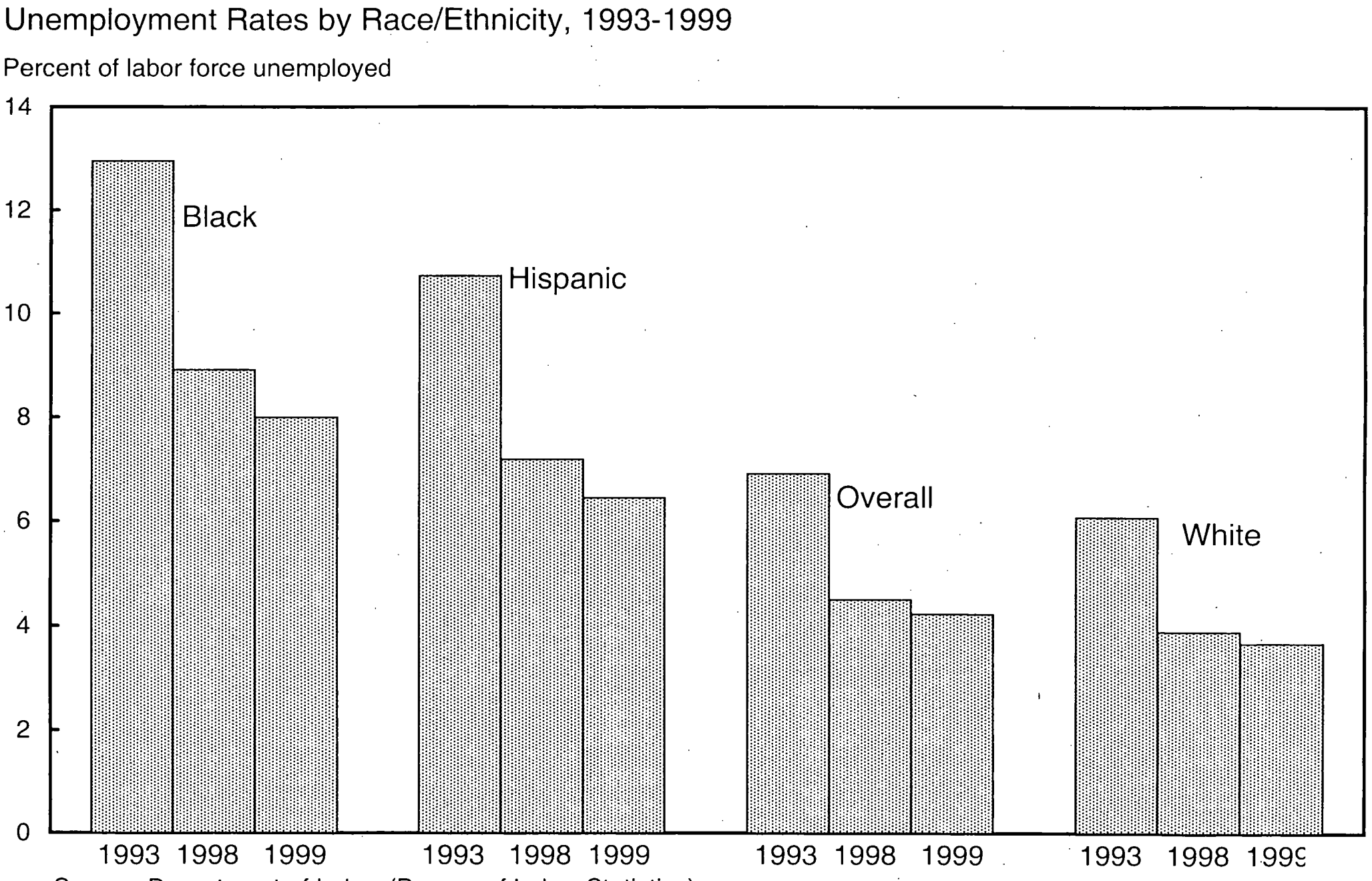
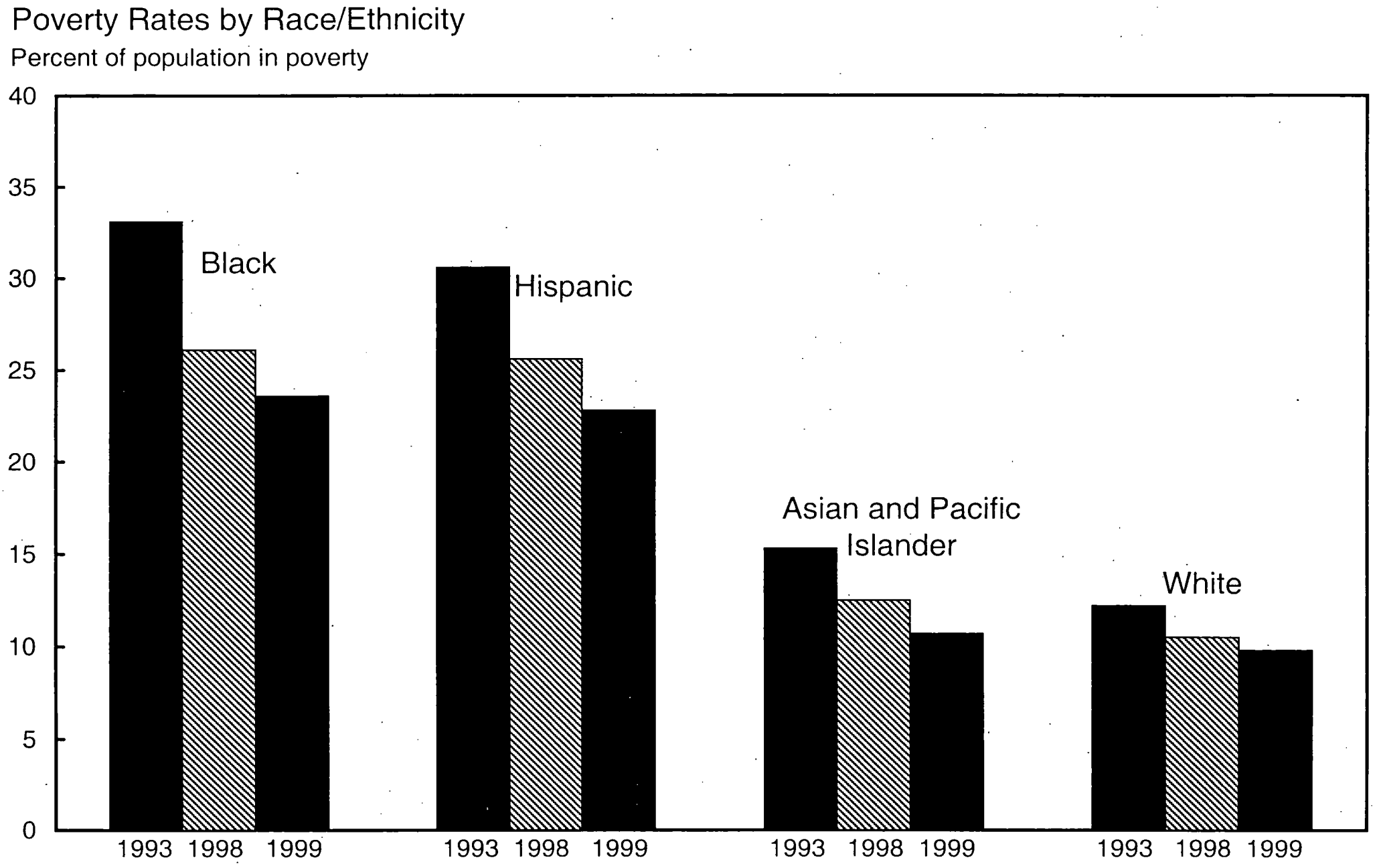
Chart 5-1 **Jobs are Plentiful Now. The Black and Hispanic Annual Unemployment Rates are at Record Lows.**



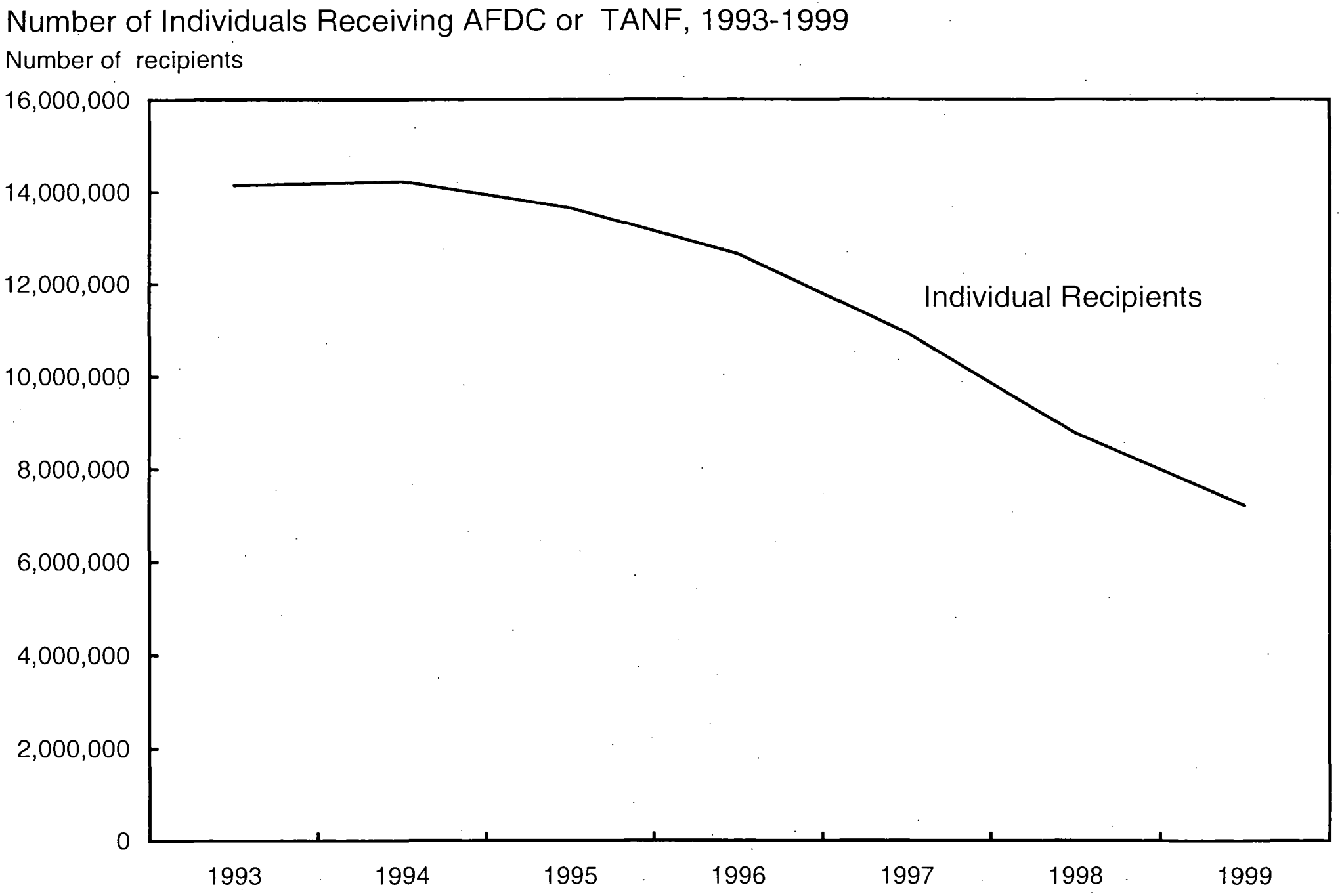
Source: Department of Labor (Bureau of Labor Statistics).

Chart 5-2 **All Races/Ethnic Groups Have Lower Poverty Rates. Reductions Most Dramatic for Blacks and Hispanics.**



Source: Department of Commerce (Census Bureau).

Chart 5-3 **The Number of AFDC/TANF Recipients has Fallen Dramatically.**

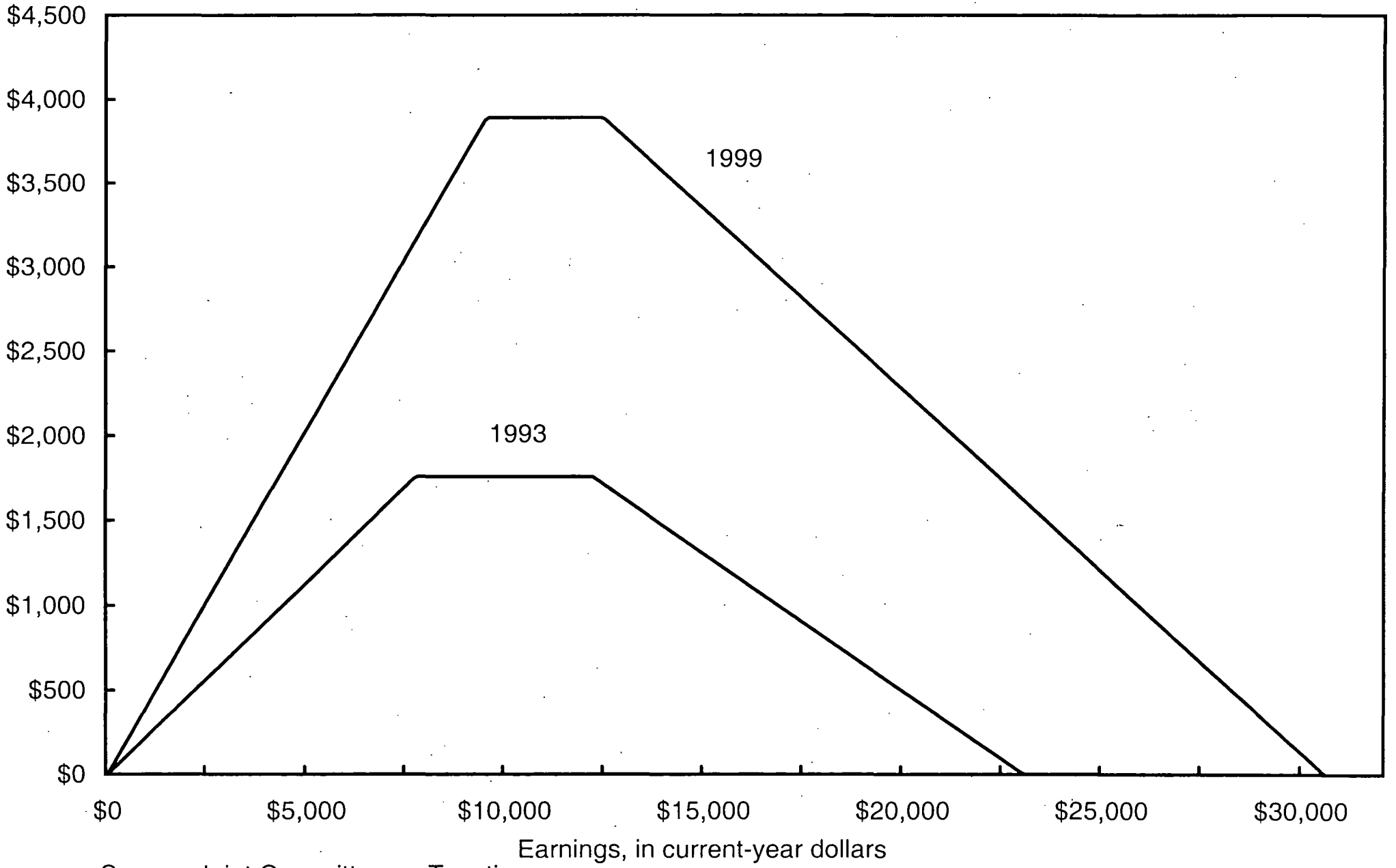


Source: Department of Health and Human Services.

Chart 5-4 **The EITC has Expanded Greatly During the Clinton Administration.**

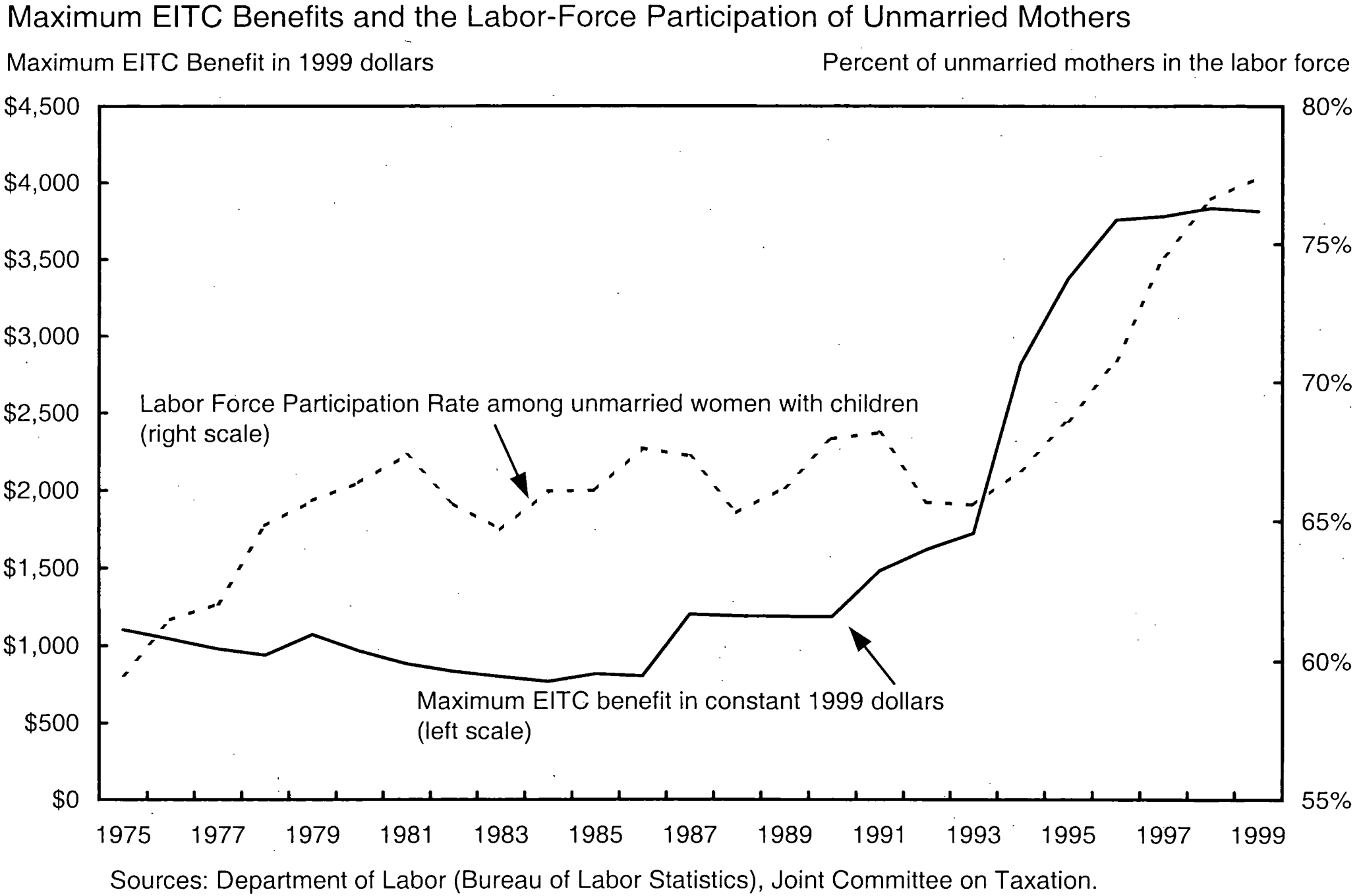
Maximum EITC Benefit in Constant Dollars by Current-year Earnings, 1993 and 1999

Benefit level for a family with two eligible children, in constant dollars



Source: Joint Committee on Taxation.

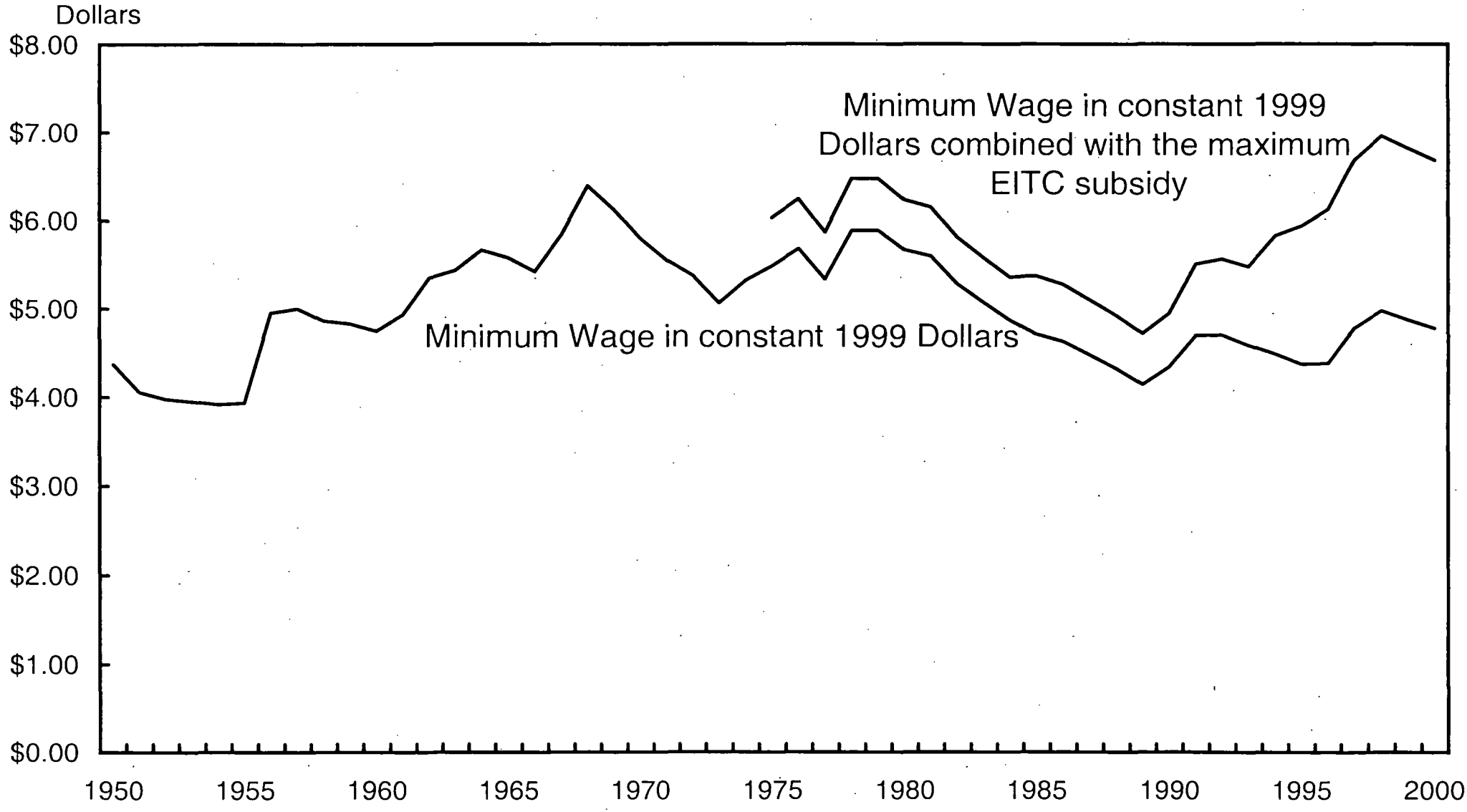
Chart 5-5 **Leap in the Labor Force Participation of Unmarried Mothers Closely Followed Increases in Maximum EITC Benefits.**



Sources: Department of Labor (Bureau of Labor Statistics), Joint Committee on Taxation.

Chart 5-6 **When Combined with Maximum EITC Subsidy Rate, the Real Minimum Wage is as High as Ever.**

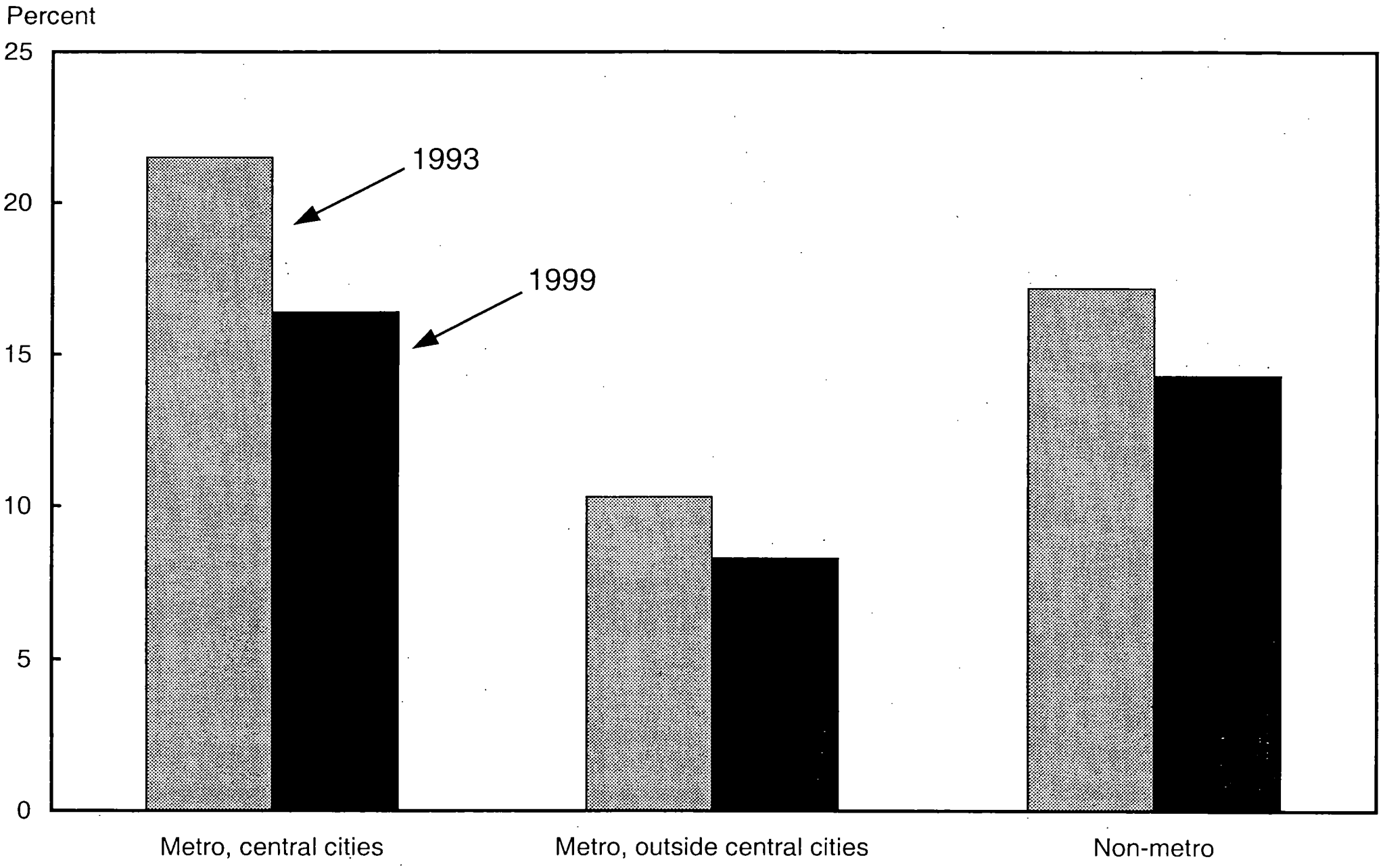
The Real Minimum Wage Over Time Combined with EITC Subsidy Rates for People with Two or More Children



Source: Joint Committee on Taxation.

Chart 5-7 **Dramatic Declines in Poverty Rates in All Areas—Particularly in Central Cities.**

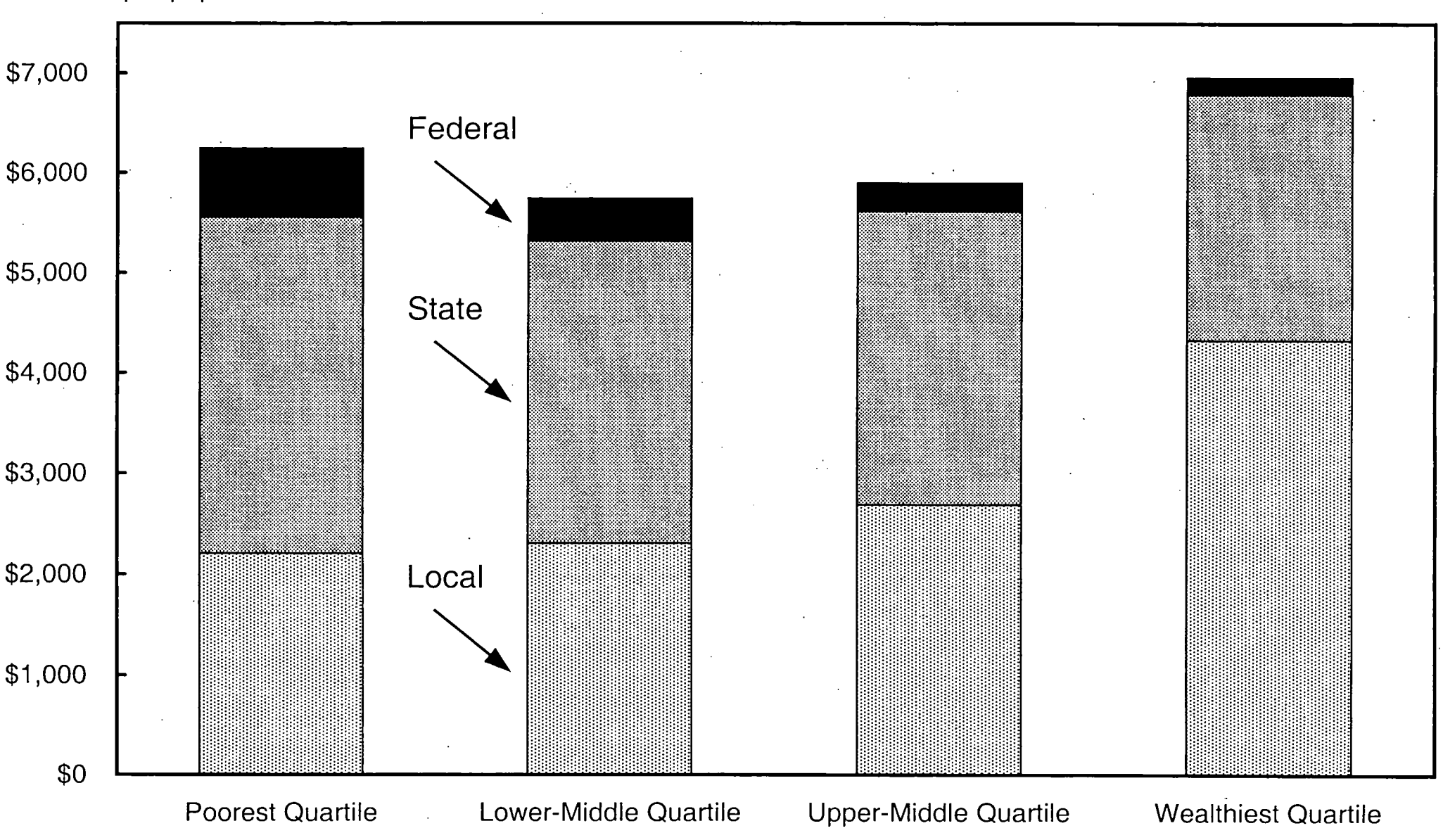
Poverty Rates by Area Type, 1993 and 1999



Source: Commerce Department (Census Bureau).

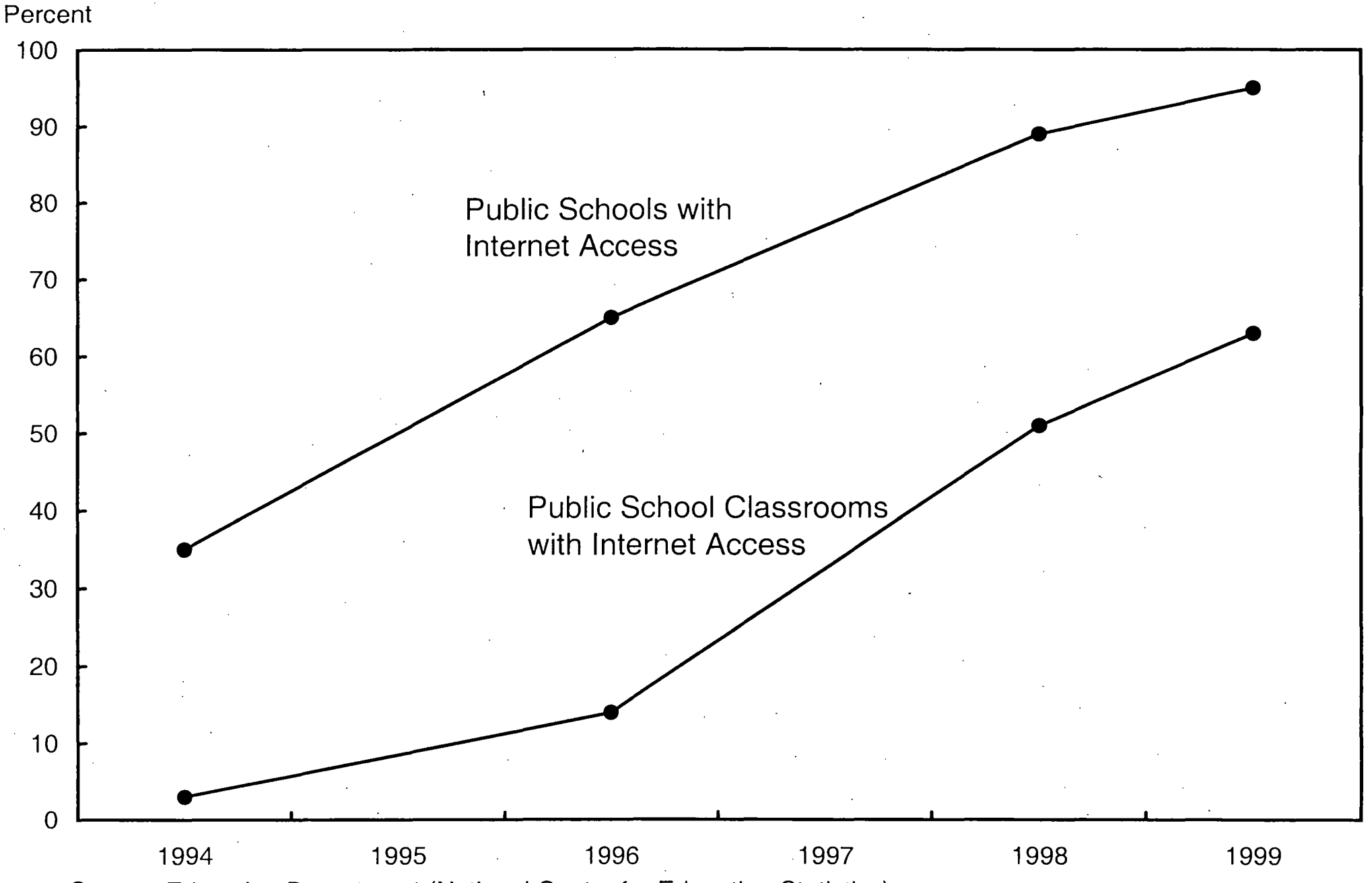
Chart 5-8 **Poorer School Districts Rely More on the Federal Governments than do Wealthier School Districts.**

Per-pupil School District Revenue by Source and District Poverty Quartile, 1994-1995



Source: Education Department.

Chart 5-9 **Access to the Internet in Schools has Grown Dramatically.**

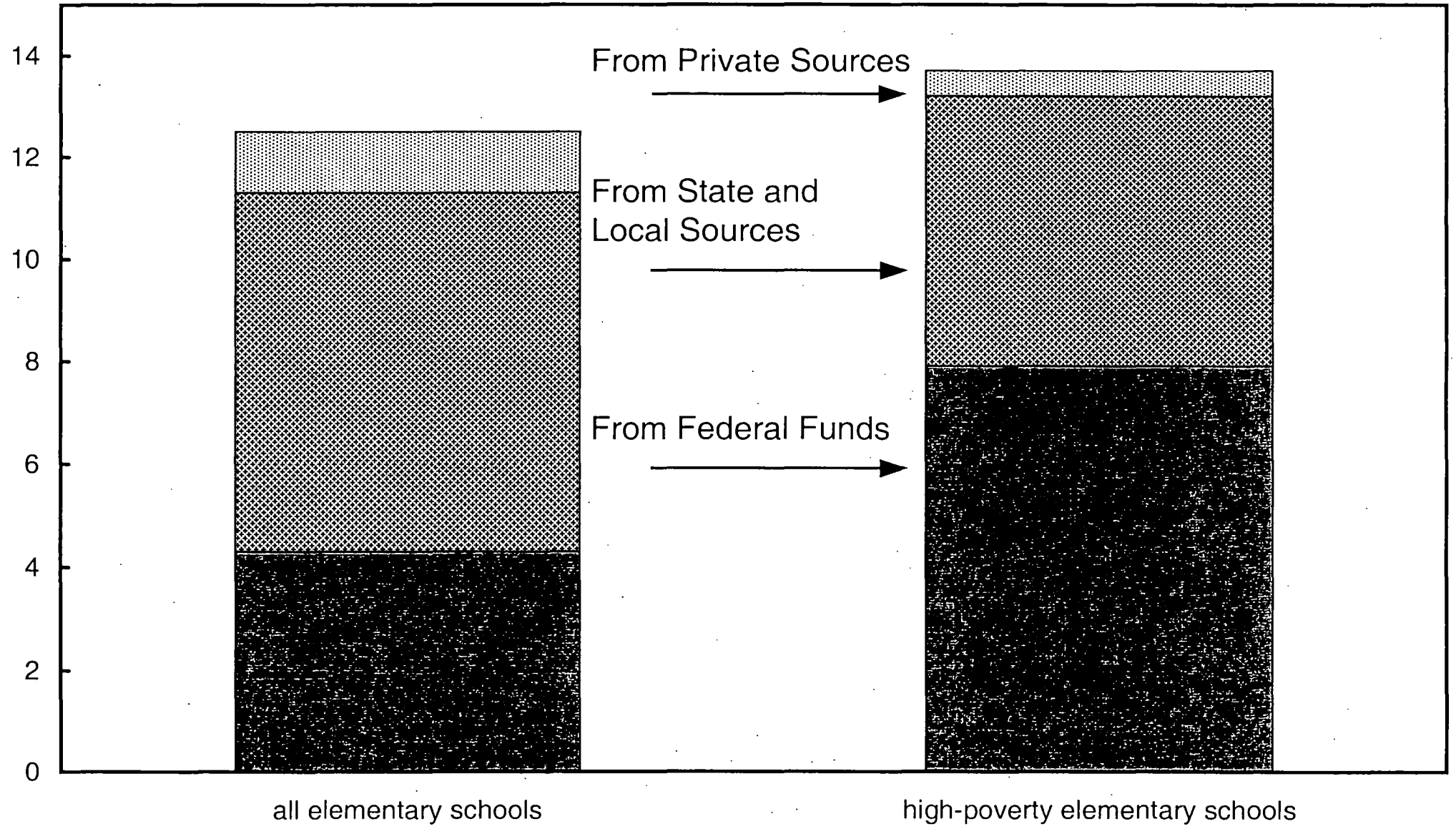


Source: Education Department (National Center for Education Statistics).

Chart 5-10 **High-poverty Elementary Schools Receive Fewer Computers from Private and Local Sources, More from Federal Funds.**

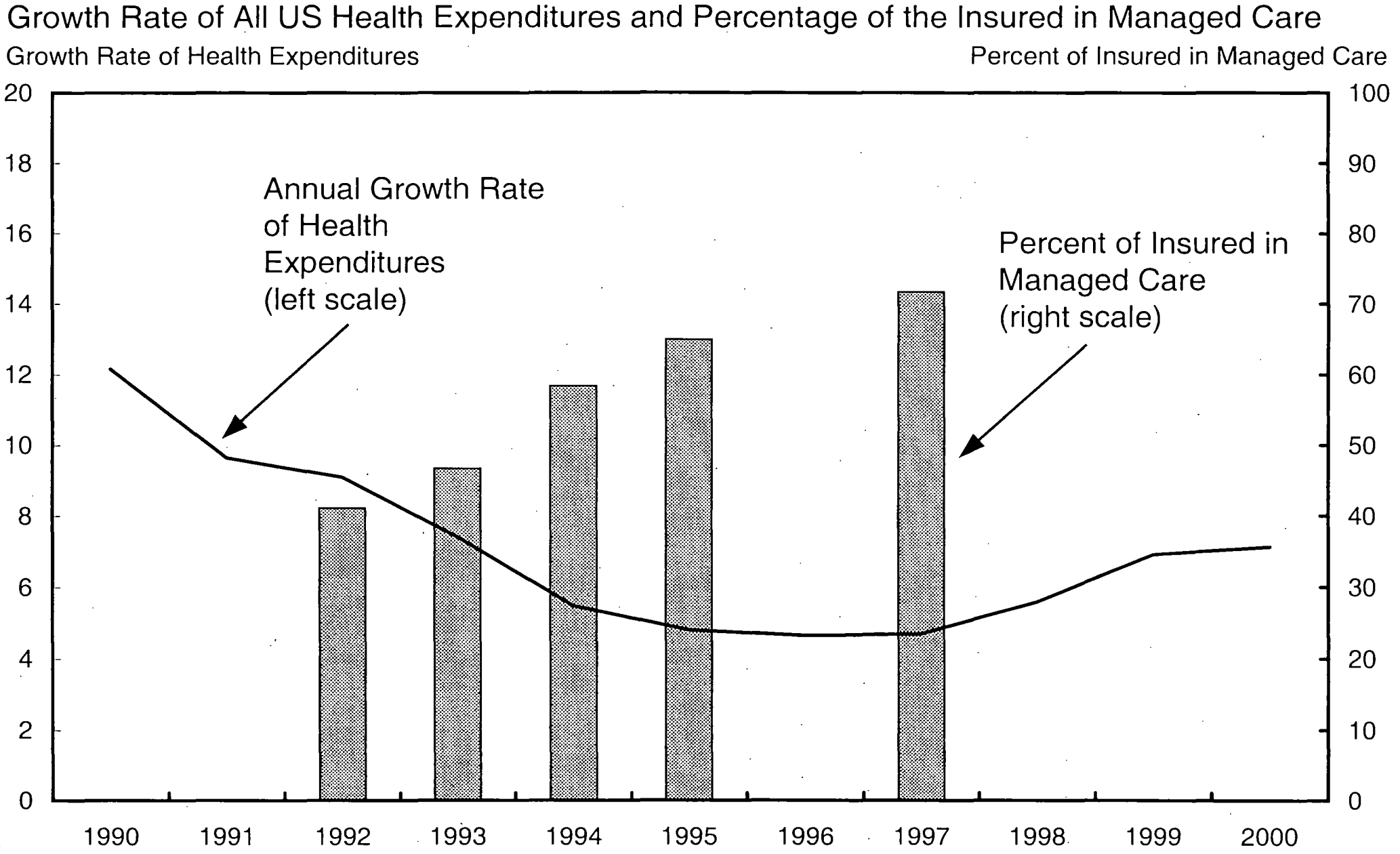
Number of New Computers Received by Elementary Schools in 1997-98

Number of computers per school of 500 students



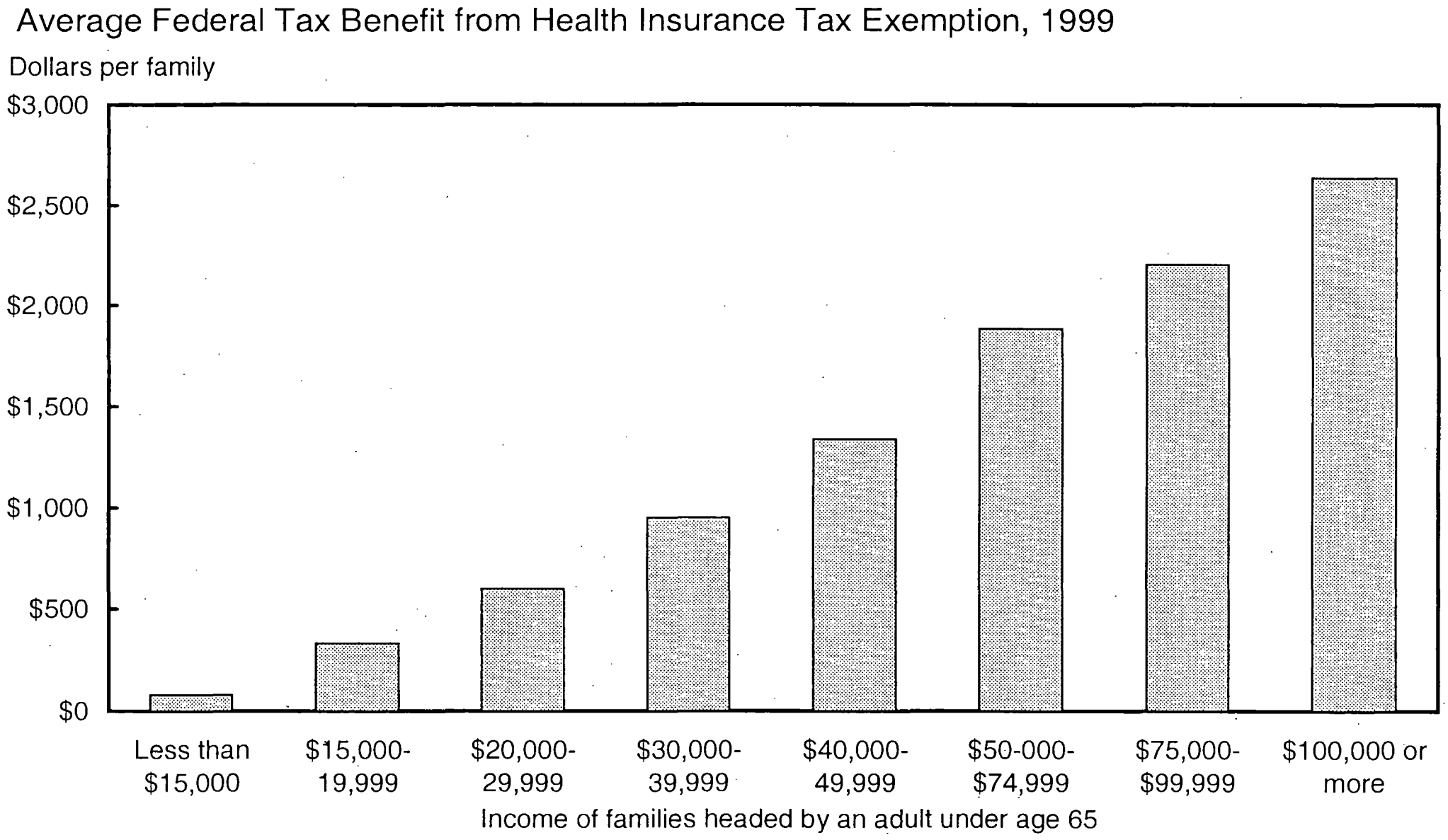
Source: Education Department.

Chart 5-11 **Growth in Health Expenditures was Smaller During Years of Mananged Care Expansions.**



Sources: Department of Health and Human Services (Health Care Financing Administration) and Employee Benefits Research Institute.

Chart 5-12 **Value of Federal Tax Exemption for Health Insurance Rises With Income:**

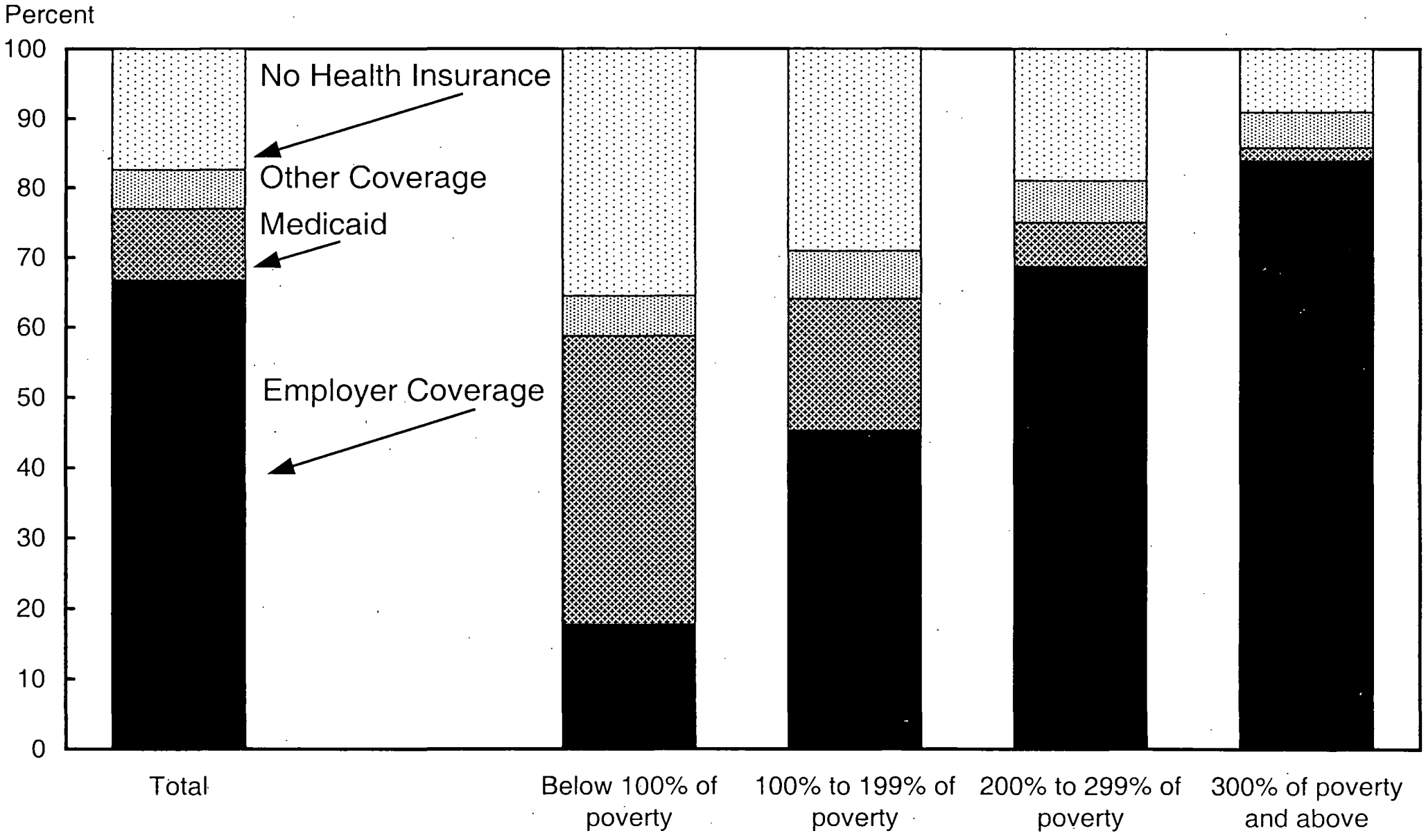


Note: Calculations incorporate likelihood of receiving employer-provided health benefits and the value of the tax benefit of employer-provided health insurance.

Source: John Sheils, Paul Hogan and Randall Haught, "Health Insurance and Taxes: The Impact of Proposed Changes in Current Federal Policy," October 1999, The Lewin Group, Inc.

Chart 5-13 **The Well-off Receive Health Insurance through Employers. Those with Lower Incomes Recieve Health Insurance from the Government, or not at all.**

Health Insurance Coverage of the Non-elderly by Coverage Type and Family Income, 1999



Source: Commerce Department (Census Bureau).