Poverty Despite Work in Kentucky

Center on Budget and Policy Priorities

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Kentucky Youth Advocates

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Collaborating Organization

Kentucky Youth Advocates (KYA) is non-profit research organization established in 1975. KYA publishes and distributes information about current and emerging policies affecting children, especially those who are poor or otherwise disadvantaged.

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Executive Summary

Buoyed by years of economic recovery and gradually declining unemployment rates, the standard of living for most people in Kentucky has improved during the past 10 years. But many families have not shared in this growing prosperity. Poverty, especially among the state's youngest residents, remains a significant problem in the state. Kentucky's poverty rate is one-sixth higher than the national average. Almost one in four children lives in poverty. Families with children are three times more likely to be poor than families and individuals without children.

It is common to assume that working means an escape from poverty. However, the evidence tells a different story. Nearly one-sixth of all working families with children are poor. During the past decade, the poverty rate among working families in the state has risen from 12 percent to 16 percent. Understanding the nature and extent of working poverty in Kentucky is especially important now. Efforts to help breadwinners support their families through work and remain off welfare — as well as efforts to reduce child poverty — must include policies to assist low-income working families if they are to be successful. The design of effective programs to reduce this working poverty requires an understanding of its causes and characteristics. A close examination of the poor in Kentucky reveals some important findings.

- **Most poor Kentucky families with children work.**
  Two-thirds of poor families with children in Kentucky had a parent who worked at some point during the year according to Census Bureau data for the mid-1990s. The amount of work was substantial. On average, these families worked 10 full months during the year. Even having a full-time, year-round worker did not guarantee that a family would be lifted

above the poverty line: nearly one-quarter of poor families with children in Kentucky included a full-time, year-round worker.

- **Earnings make up the largest share of income for most poor families with children in Kentucky.**
  Less than 20 percent of poor families with children relied on welfare for the majority of their income. By contrast, earnings from work supplied the majority of income for six in 10 poor families with children. Fully half of families who received public assistance included a worker.

- **Working poor families in Kentucky mirror a broad cross-section of the state's population.**
  Like all families with children in Kentucky, the vast majority of working poor families in the state are white. Almost half of working poor families with children were headed by a married couple. A worker aged 25 or older headed most of these families.

It is common to assume that families are poor because the parents do not work. These statistics demonstrate that this belief is false. Many parents who work do not earn enough to lift their families above the poverty line. They are playing by the rules, but still cannot make ends meet.

Economic trends including the growth in low-wage jobs and some federal and state policies have made it harder for families to bring their incomes above the poverty line through work.

- **Many workers in Kentucky have difficulty finding well-paying jobs and full-time, year-round work.**
  In the mid-1990s, three in 10 working parents had low hourly earnings[1] and four in 10 parents who worked part-year or part-time would have preferred to have full-time work. One explanation for these poor prospects is that job growth has been concentrated — and is likely to continue to be concentrated — in low-paying sectors such as services and retail trade. Kentucky's labor market is particularly unforgiving of those who lack a high school diploma or G.E.D. Working parents with less than a high school education are twice as likely as more educated workers to have low hourly earnings and are six times more likely to be poor.

[1] The Census Bureau definition of workers with low earnings includes full-time, year-round workers whose gross earnings fall below a level roughly equal to — but slightly below — the poverty line for a family of four. Workers with low hourly earnings are those whose hourly wage would produce earnings below the low earnings threshold if the person worked 50 weeks and 40 hours per week.

- **The erosion in the value of the federal minimum wage has made it more difficult for parents to support their families through work.** Since it is not indexed to inflation, the value of the minimum wage has eroded over time. During the 1960s and 1970s, the earnings of a full-time minimum wage worker employed throughout the year typically were enough to lift a family of three out of poverty without considering other sources of income. In 1999, full-time minimum wage earnings equal 80 percent of the poverty line for a family of three. The gap between full-time minimum wage earnings and the poverty line for a family of this size is $2,646.[2]

- **Kentucky places a heavy tax burden on the poor.** By imposing the income tax on families making as little as $5,000 per year, Kentucky makes it harder for low-wage workers to make ends meet. A two-parent family of four with poverty level income in Kentucky paid $550 in income taxes in 1998, the highest burden in the country.

The persistence of poverty among working families deserves the attention of policy makers both because of recent welfare reform efforts and because of the implications of this situation for children. Kentucky's welfare caseload has declined by almost 40 percent since reaching its peak in 1993. Unfortunately, leaving welfare does not necessarily mean leaving poverty. In Kentucky, 59 percent of those exiting welfare for work in 1998 earned less than seven dollars an hour, a wage below the poverty line for a family of four.[3] Moreover, because most poor families with children have one or more parents who work — with a substantial proportion working full-time year-round — Kentucky's high child poverty rate is unlikely to decline significantly without additional efforts to assist low-wage working families. Kentucky can help poor parents find and keep jobs by rewarding their work effort and by relieving some of the costs that families incur as they move from welfare to work.

Implement a refundable state earned income tax credit: The federal earned income tax credit is a tax credit for low- and moderate-income workers, primarily those with children, designed to offset the burden of Social Security payroll taxes,

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[2] This gap between earnings and the poverty line for a family of three disappears if one considers the effects of the federal earned income tax credit. Even after including the value of the EITC, however, the earnings of a full-time minimum wage worker are still insufficient to lift a family of four out of poverty.

[3] Scott Cummings and John P. Nelson, *From Welfare to Work: Second Year Survey of Discontinued K-TAP Recipients*, Center for Policy Research and Evaluation, University of Louisville, 1999. These findings confirm those of national level studies about the earnings of people leaving welfare for work. These studies are summarized in *Welfare Recipients Who Find Jobs: What Do We Know About Their Employment and Earnings?*, Center on Budget and Policy Priorities, 1998.

supplement earnings, and complement efforts to help families make the transition from welfare to work. In 1997 more than four million people were lifted out of poverty by the federal EITC.[4] But many working families remain poor despite this credit. A refundable state earned income tax credit would lift more families out of poverty, relieve the burden of state and local taxes on poor families and supplement the wages of low-income workers.

Raise the state's minimum wage: The value of the federal minimum wage has declined during the past 20 years, making it more difficult for low-wage workers to support their families. A higher minimum wage would help reverse or moderate the decline in wages for workers at the bottom of the pay scale, help more working families escape poverty, and improve the likelihood that parents making the transition from welfare to work can support their families through employment. Because an additional increase in the federal minimum wage is at best uncertain in the near future, only by increasing the state minimum wage can Kentucky boost the wage floor for low-income workers. Eight states and the District of Columbia set their minimum wages above the federal level.

Help working poor adults obtain health insurance: Medical expenses can devastate families lacking health insurance. Working poor parents are generally not covered by any public insurance program and many do not have health insurance coverage through their employers. More than half of working poor parents in Kentucky lacked health insurance in the mid-1990s. Kentucky can take advantage of a little-recognized provision of the 1996 welfare law that allows states to use Medicaid to provide health care coverage to low-income working parents.

Improve outreach efforts to enroll eligible children in Medicaid and the state's child health insurance program: Children in families with incomes below 200 percent of the poverty line will be eligible for public health insurance in Kentucky as of July 1999. However, being eligible for coverage does not always translate into actual coverage. For example, less than 20 percent of the teenagers eligible for Medicaid through the July 1998 expansion were enrolled in the program as of January 1, 1999. The state should develop effective outreach programs to ensure that children eligible for public health insurance receive coverage.

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[4] United State Bureau of the Census, *Poverty in the United States: 1997,* Table C-4. This table shows that the poverty rate in 1997 was 14.3 percent when poverty is measured using the official measure of income — which includes all cash income other than capital gains — plus the impact of federal taxes. When the value of the EITC is then added, the poverty rate drops to 12.7 percent. Under this definition of after-tax cash income, then, the EITC lifted 4.3 million people out of poverty in 1997.

Provide child care assistance to more working poor families: One of the most significant hurdles facing parents attempting to enter or remain in the labor force is finding affordable, reliable child care. To remove the barrier to working caused by high child care costs and to ease the transition from welfare to work, Kentucky should increase its efforts to help families with child care expenses. With child care costs in the state averaging $3,200 per child, even a family earning twice the poverty line for a family of four would have to spend almost one-fifth of its income to place two children in child care.[5] Kentucky currently provides child care assistance to all families with incomes below 150 percent of the poverty line. As soon as income exceeds 150 percent of the poverty line, families no longer qualify for any child care assistance. Funding for Kentucky's child care assistance program should be increased to provide direct assistance to a larger number of families, to gradually phase out assistance instead of abruptly eliminating it after a certain income level, and to ensure that the subsidies it provides are adequate to cover market rates.

[5] Children's Defense Fund, *Kentucky: Child Care Challenges,* May 1998.

I. Poverty Despite Work

Buoyed by years of economic recovery and gradually declining unemployment rates, the standard of living for most people in Kentucky has improved during the past 10 years. But many families have not shared in this growing prosperity. Poverty, especially among the state's youngest residents, remains a significant problem in the state. In the mid-1990s, Kentucky's poverty rate stood at 16 percent, one-sixth higher than the national average. Almost one in four children is poor. Families with children are three times more likely to be poor than families and individuals without children. And these aggregate figures mask stark regional differences in unemployment, poverty, and income.

The high poverty rate among Kentucky's children is cause for concern since strong evidence exists that poverty can hinder the development of children and adversely affect their ability to become productive adults. Important research from the University of Michigan, for example, has found that children under age five who have experienced at least one year of poverty have significantly lower IQ scores than children in families that were never poor. The researchers also found that the longer young children live in poverty, the greater the lag in IQ scores. The relationship between poverty and lower IQ scores remains even when factors such as the mother's education and family structure are taken into account. Other research shows that poor children are more likely to score poorly on indicators of cognitive development, to be short for their age, and to be underweight than children in higher-income families.[6]

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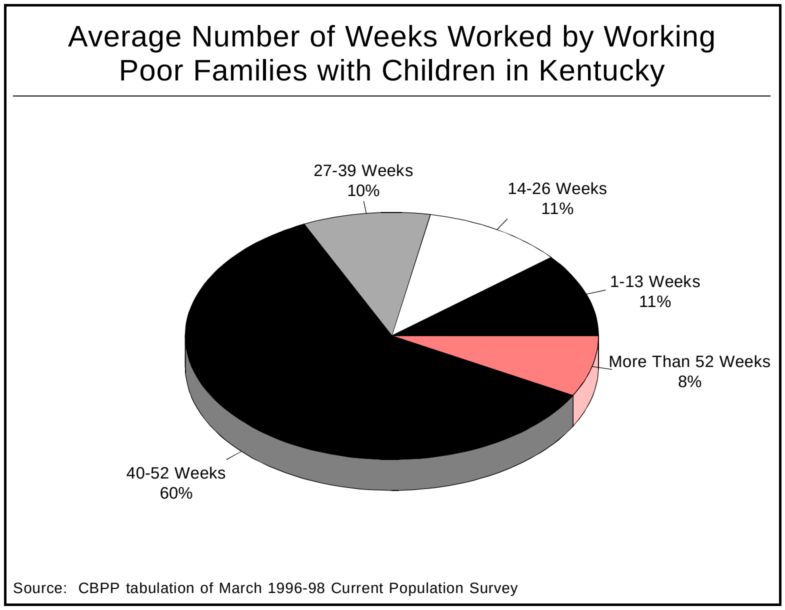
[6] Greg J. Duncan, Jeanne Brooks-Gunn, eds. *The Consequences of Growing Up Poor*. New York: Russell Sage Foundation, 1997.

Figure 1



It is common to assume that working means an escape from poverty. However, the evidence tells a different story. Sixteen percent of working families with children in Kentucky earned too little to escape poverty during the mid-1990s. In 1998 this meant living on less than $13,001 for a family of three or less than $16,655 for a family of four. During the past decade, the poverty rate among working families with children in Kentucky rose from 12 percent to 16 percent, an increase of one-third. Working families now represent the vast majority of poor families in Kentucky. A close examination of the poor in Kentucky reveals some important findings.

- In the mid-1990s, some 118,000 Kentucky families with children in which the parents were able to work had incomes below the federal poverty line. Of these families, two-thirds had one or more working parents.

- Some 254,000 people lived in working poor families in Kentucky in the mid-1990s, including 138,000 children.

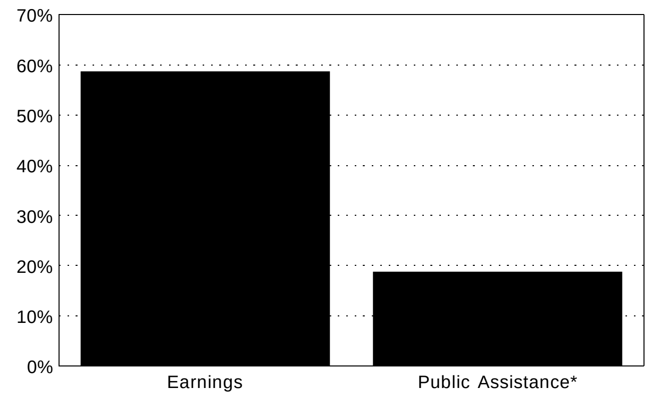
- Working poor families in Kentucky demonstrated a substantial work effort during the mid-1990s. On average, these families worked 10 months out of the year. Even full-time work did not guarantee that a family would escape poverty. One-quarter of families with children living at the poverty level had a worker employed full-time and year-round.[7] Figure 1 presents the distribution of work effort among poor families with children who worked.

[7] For married-couple families, this figure refers to the combined work effort of the head of household and spouse.

The extensive work effort among poor families with children in Kentucky is also reflected in the fact that most poor families rely primarily on earnings from work, while a relatively small fraction rely on welfare. In the mid-1990s, earnings from work supplied the majority of income for 60 percent of poor families with children. Less than one in five poor families with children relied on welfare for the majority of their income.[8] (See Figure 2.) Fully half of families who received cash welfare benefits included a worker.

Figure 2

Percent of Families With Earnings or Public Assistance as a Majority of Income in Kentucky



CBPP tabulation of March 1996-98 Current Population Survey
*Public assistance refers to income from welfare and SSI. The term "welfare" refers to AFDC for data from 1995 and 1996 and to TANF for data from 1997.

Parents also have trouble supporting their families because they have difficulty finding enough work. In the mid-1990s, four in 10 working poor parents in Kentucky who worked part-year or part-time would have preferred to have full-time work.[9]

The data presented above focus on families with incomes below the federal poverty threshold. This measure is used because it is the most commonly accepted measure of low-income status. Nevertheless, the basic formula for determining the poverty threshold has not changed since 1966, and it has been criticized on several grounds in recent years. One oft-cited limitation of the poverty definition is that it does not reflect major changes in consumption patterns among low-income families over the

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[8] These figures do not sum to 100 percent because some poor families receive a majority of their income from a source other than public assistance or earnings, such as Social Security benefits. In addition, other families that receive income from multiple sources may not receive half or more of their income from any one source. In this report, the term "public assistance" refers to Aid to Families with Dependent Children, Temporary Assistance to Needy Families, and Supplemental Security Income.

[9] Center on Budget and Policy Priorities tabulation of March 1996-98 Current Population Survey data.

About the Data Used in This Report

Much of the findings presented in this report come from a special tabulation of data from the U.S. Census Bureau's Current Population Survey. The CPS is a survey conducted every month of roughly 50,000 households nationwide. The data in this report are from the CPS conducted each March, which includes questions on income and employment in the previous calendar year. (In other months, the CPS is limited primarily to questions related to monthly labor force activity.) The Current Population Survey is the source of official data on income, poverty, and unemployment in the United States.

This report presents the averages of March CPS data covering the calendar years 1995 through 1997, the three most recent years for which CPS data are available.[a] Although the CPS is intended to provide both national and state-level data, the number of households surveyed in some states is relatively small.[b] Combining data for three years provides a larger sample for each state and thus provides more reliable findings. It is a method used and endorsed by the Census Bureau. Throughout this report, the data will be described as covering the "mid-1990s."

Several of the figures cited in the text refer to families in which the parents worked a combined total of more than thirteen weeks during the year. On average, these families worked an average of 46 weeks during the year and 41 hours per week during the weeks they worked.

Definition of Poor

This report examines families with incomes below the federal poverty line. The Census Bureau definition of income includes the earned and unearned income of all family residents. Earned income includes wages and salaries, income from farm employment, and income from self-employment. Unearned income includes cash income from public assistance (AFDC, TANF, and SSI), Social Security benefits, investment income, rental income, and retirement income. The Census Bureau's income measure does not include the value of in-kind benefits, such as food stamps, or the effect of taxes — such as payroll taxes or the Earned Income Tax Credit — on family incomes.

The poverty line varies by family size and is adjusted annually for inflation. In this report, each family's income in a given year is compared with the poverty threshold for that year for a family of that size. The estimated poverty threshold for 1999 is $13,358 for a family of three and $17,112 for a family of four. The official poverty thresholds for 1999 for each family size will not be released until the fall of 2000.[c]

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[a] These data are from the March CPS conducted in 1996, 1997, and 1998. As noted, the March CPS includes questions on income and employment in the *previous* calendar year. The March CPS data conducted in 1996 through 1998 thus reflect a family or individual's circumstances in calendar years 1995 through 1997.

[b] This is true even though the CPS "over-samples" in smaller states, meaning that a larger share of the state's households are surveyed than the proportion surveyed in larger states.

[c] The official poverty threshold produced by the Census Bureau differs somewhat from the "poverty guideline" set by the United States Department of Health and Human Services. For instance, in 1997 the poverty threshold for a family of four was $16,400 compared with the poverty guideline of $16,050. The poverty thresholds are used for statistical purposes while the poverty guidelines are used for administrative purposes such as determining eligibility for benefits in federal means-tested programs.

past 30 years, such as the growing use of child care.[10] Many researchers believe the poverty threshold no longer reflects the minimal costs of supporting a family and therefore should be raised. A 1996 study by Kentucky Youth Advocates estimated that the annual income necessary to fully meet the basic living expenses of a single-parent family of three in Louisville in 1997 was between $21,736 and $25,896, while the poverty line for a family of three equaled $12,802.[11] The Kentucky Kids Count Consortium, a partnership of child advocates and university researchers, has suggested that income at double the federal poverty line provides a family a reasonable standard of living.[12]

Because many families struggle to make ends meet even when their income modestly exceeds the federal poverty threshold, it is important also to examine the characteristics of near-poor families — those with incomes between 100 and 200 percent of the poverty line. In 1999, families of three with incomes between $13,358 and $26,716 and families of four with incomes between $17,112 and $34,224 fall in this category.

- More than two in five children in Kentucky live in poor or near-poor families. Twenty-three percent of children live in families with income below the poverty line and another 20 percent of children live in families with income between 100 and 200 percent of the poverty line.

- Ninety percent of families with income between 100 and 200 percent of the poverty line included a worker, and about 70 percent included a full-time, year-round worker during the mid-1990s.

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[10] A second major criticism is that the income measure used by the Census Bureau in its poverty calculations does not include the value of in-kind benefits or the impact of taxes on a family's income. See National Research Council, *Measuring Poverty: A New Approach*, 1995 for recommendations on how the measurement of poverty should be changed.

[11] Kentucky Youth Advocates, "1997 Living Wage Study: Family of Three Living in Louisville / Jefferson County Kentucky," 1996. The lower figure assumes that the parent's employer provided health insurance. The higher figure assumes that the parent had to purchase health insurance coverage independently.

[12] Kentucky Kids Count Consortium, "1993 County Data Book," 1993.

II. The Faces of the Working Poor

Working poor families in Kentucky look surprisingly like the rest of the state's population. Like all families with children in the state, the vast majority of working poor families in the mid-1990s were white. Almost half of working poor families with children were headed by a married couple. A worker aged 25 or older headed most of these families. Figure 3 highlights the demographic characteristics of working poor families with children.[13]

- Almost 85 percent of working poor families with children in Kentucky during the mid-1990s were white, while the remaining 15 percent were either black or Hispanic.[14] Although most working poor families were white, the poverty rate among black and Hispanic families was higher than that of white families.

- Consistent with national trends, 45 percent of working poor families in Kentucky were headed by a married couple in the mid-1990s. Four in 10 of these families were headed by a woman.

- Three-quarters of working poor families were headed by someone in their prime working years: ages 25 to 45.

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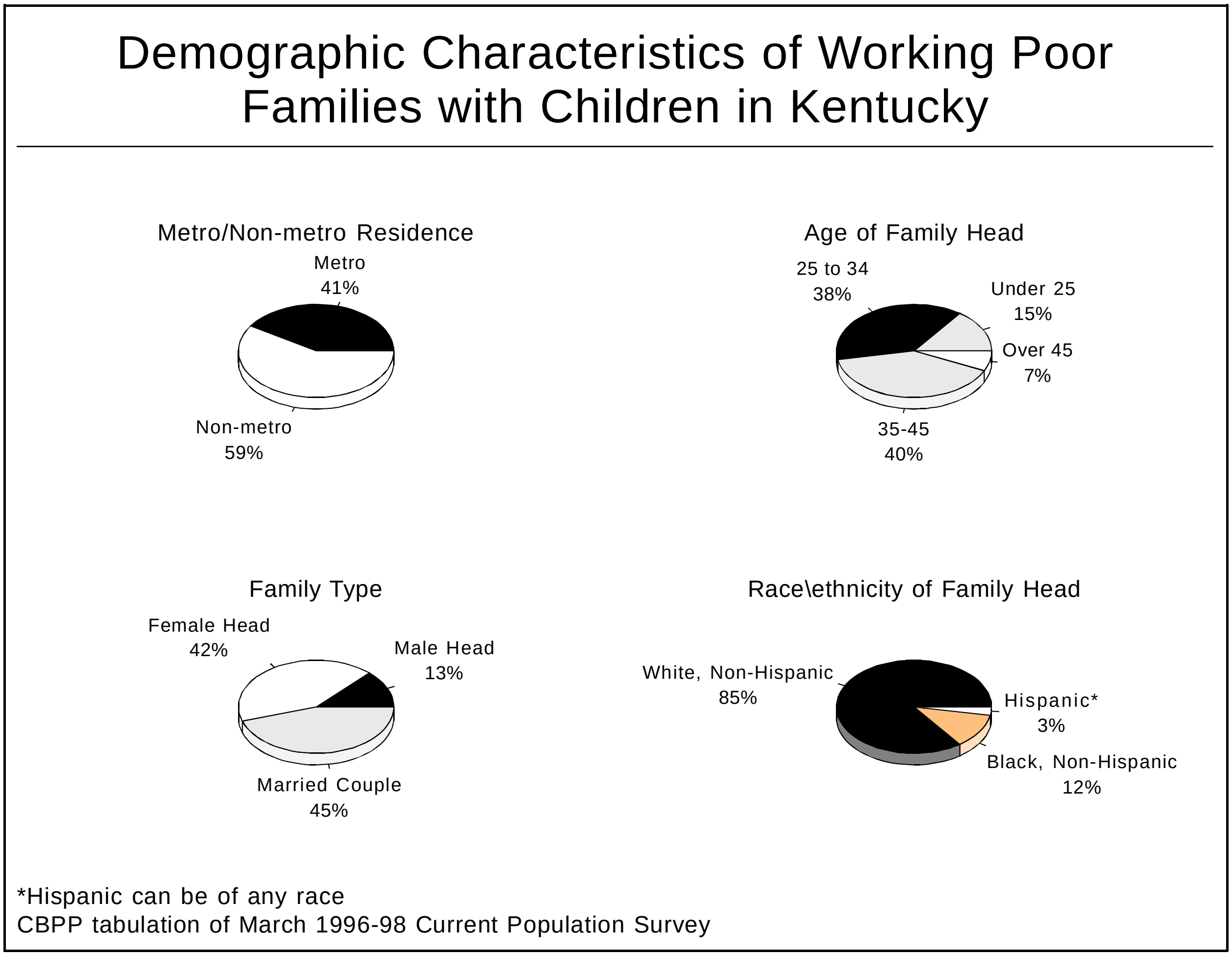
[13] The data in this section refer to families in which the household head and spouse worked a combined total of more than 13 weeks during the year.

[14] Hispanic families can be of any race. White and black families refer here to non-Hispanic white families and non-Hispanic black families.

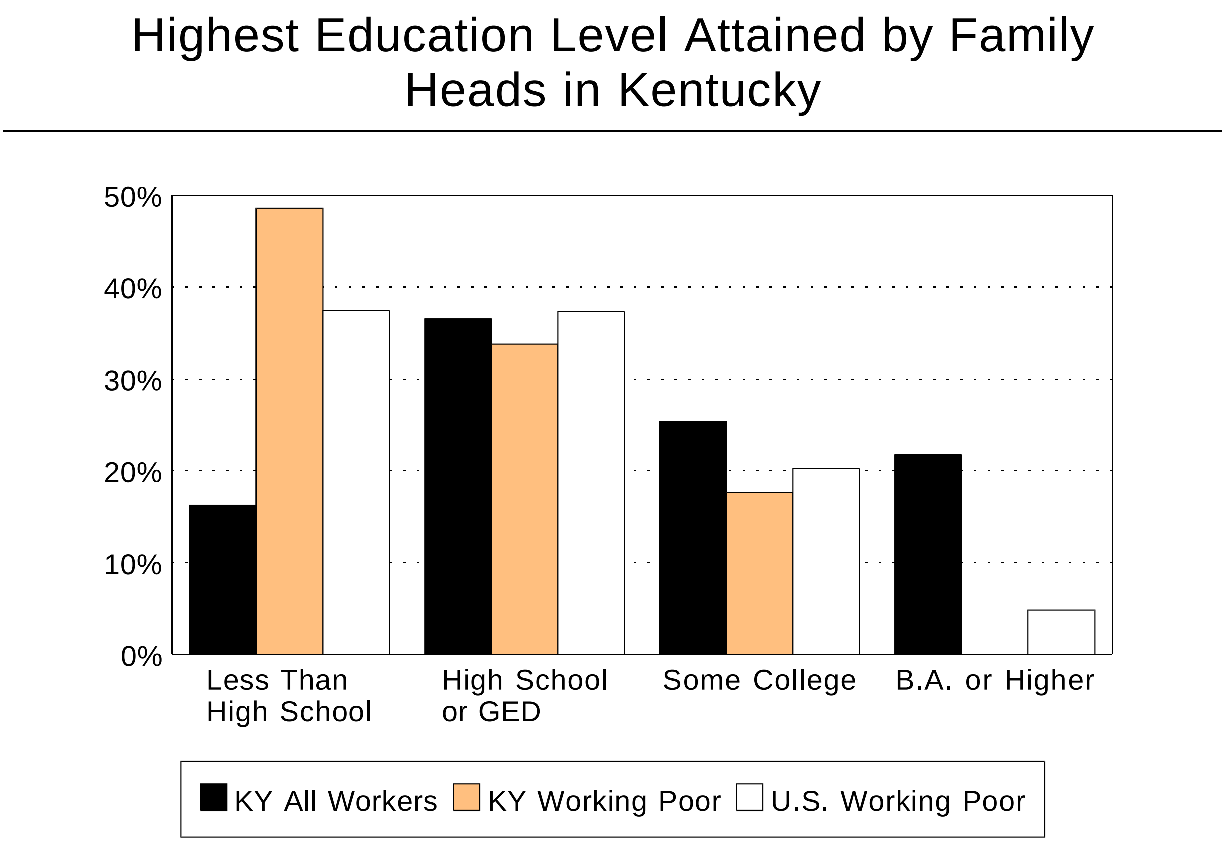
Figure 3



Working poor families in Kentucky differ from the general population in Kentucky as well as from working poor families nationally in one crucial respect: their level of education. Family heads of working poor families are much less likely to have a high school diploma than those with higher incomes. Less than 20 percent of all Kentucky families are headed by someone lacking a high school diploma or GED, but about half of the family heads in working poor families in the state have not completed high school. Nationally, just over one-third of working poor family heads lack a high school diploma. (See Figure 4.) Kentucky's labor market is particularly unforgiving of those who lack a high school diploma or GED. Working parents with less than a high school education are twice as likely as more educated workers to have low hourly earnings and are six times more likely to be poor.

While poverty and difficult economic situations exist for families throughout Kentucky, there are stark regional differences in prosperity. The counties in the "golden

Figure 4

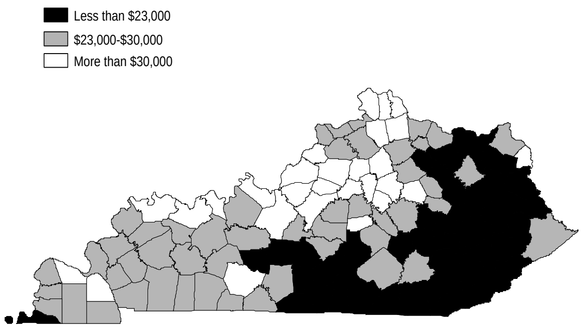


CBPP tabulation of March 1996-1998 Current Population Survey
These results are for families with children in which the parents worked a combined total of more than 13 weeks.

triangle" around Lexington, Louisville, and Northern Kentucky have enjoyed the lowest unemployment and poverty rates and highest incomes in the state. Meanwhile, four counties (Cumberland, Elliott, Fulton, and Magoffin) have suffered unemployment rates of 15 percent or higher, and the area development districts in eastern Kentucky consistently rank at the bottom of the state, with unemployment rates exceeding nine percent, child poverty rates of over 30 percent, and per capita incomes of less than $15,000.

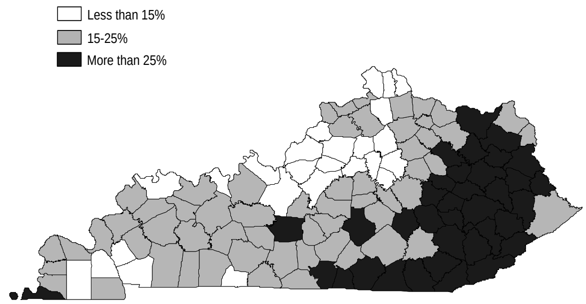
Figure 5

Median Household Income by County, 1995



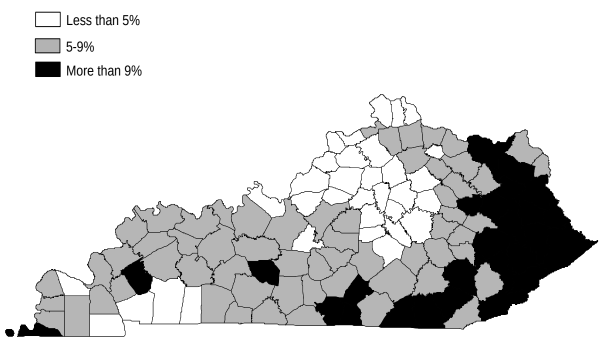
Source: CBPP tabulation of Census Bureau data.

Poverty Rates by County, 1995



Source: CBPP tabulation of Census Bureau data.

Unemployment Rates by County, 1996



Source: Kentucky Department for Employment Services, Labor Market Information.

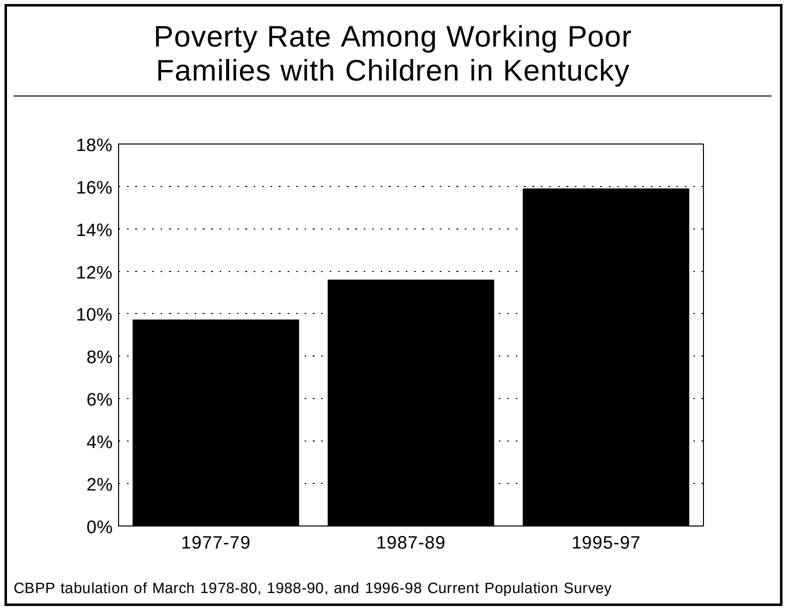
III. Economic Changes and Government Policies Contribute to Poverty Among Working Families

During the mid-1990s in Kentucky, 16 percent of working families with children were poor, a figure nearly two-thirds higher than the poverty rate for working families in the late-1970s, when 10 percent of working families with children lived in poverty. (See Figure 6.) A number of factors contribute to the prevalence of working poverty in Kentucky. First, Kentucky is a relatively low-wage state and job growth during the past two decades has been concentrated in low-wage industries. One-quarter of the heads of working poor families in Kentucky had low-hourly earnings in the mid-1990s, almost twenty percent higher than the national average of 21 percent. Since the late-1970s the percentage of working families with children headed by a low-earner increased by 50 percent. Second, the value of the federal minimum wage has declined significantly during the past 20 years. Third, because of the mix of taxes Kentucky relies on, low-income families pay a higher share of their income in taxes than do more wealthy families.

Growth in Low-Wage Jobs

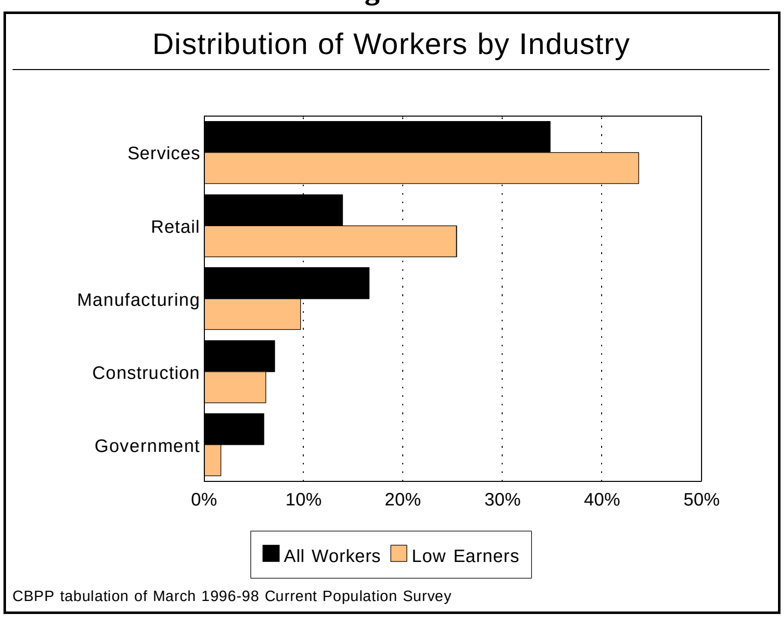
Kentucky employment is currently concentrated in the following industries: services, retail trade, and manufacturing. While farming plays a dominant role in many rural counties, accounting for more than 20 percent of jobs in 24 counties, services jobs are more prevalent in urban counties. Manufacturing job growth has been much stronger in rural areas than in urban areas.[15]

Figure 6



Working parents with low hourly earnings in Kentucky are concentrated in the services and retail trade industries to a much larger extent than workers in general. As defined by the Census Bureau, low earners are those whose hourly wages on a full-time, year-round basis would produce earnings below the four-person poverty line. Figure 7 shows the distribution across industries of both Kentucky workers in general and working parents with low earnings.

Figure 7



Kentucky's job growth has been relatively strong recently. In contrast to a six percent decline in manufacturing jobs nationally since 1969, manufacturing jobs in Kentucky increased by 27 percent during the same period. Even so, manufacturing jobs now make up a smaller share of employment in the state than

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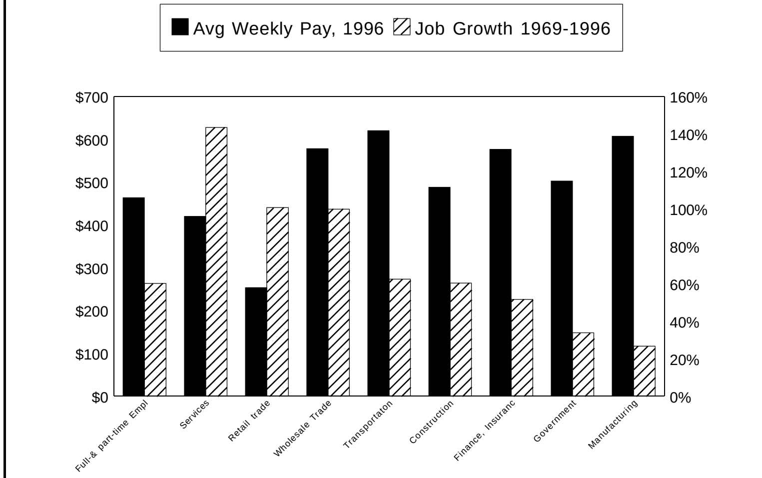
15 Stephan J. Goetz, "Industry Trends: Jobs and Earnings," in eds. Michael T. Childress, Billie M. Sebastian, Peter Schirmer, and Michal Smith-Mello, *Exploring the Frontier of the Future: How Kentucky Will Live, Learn and Work,* The Kentucky Long-Term Policy Research Center, 1996. Also, CBPP tabulation of Bureau of Economic Analysis, Regional Economic Information System data.

they did 25 years ago, as overall job growth has greatly exceeded manufacturing job growth.

As has been the trend nationally, much of the job growth in Kentucky has been concentrated in low-paying sectors such as services and retail trade. (See Figure 8.) These two industries accounted for 63 percent of the new jobs created in Kentucky since 1969. Since these industries generally pay less than other sectors, this trend has resulted in declining incomes for low-skilled workers. Although overall job growth in Kentucky is predicted to exceed the national average in coming years, the detailed forecasts signal further problems for working poor families.

Figure 8

Average Weekly Pay and Job Growth by Industry in Kentucky



Source: CBPP tabulation of Bureau of Economic Analysis, Regional Economic Information system data and Bureau of Labor Statistics data

- Job growth will continue to be concentrated in the low-paying services and retail trade industries and no net employment growth will occur in the better-paying manufacturing sector during the next few years.[16]

- Farm-dependent rural counties will experience significant changes in their economies. While the number of jobs in Kentucky is expected to grow by 17 percent between 1994 and 2005, the number of jobs for farmers and farm workers is expected to *decline* by 18 percent during the same period. Since more than 20 percent of employment in Kentucky is in farms or farm-related jobs, this development could have serious consequences for the state.[17]

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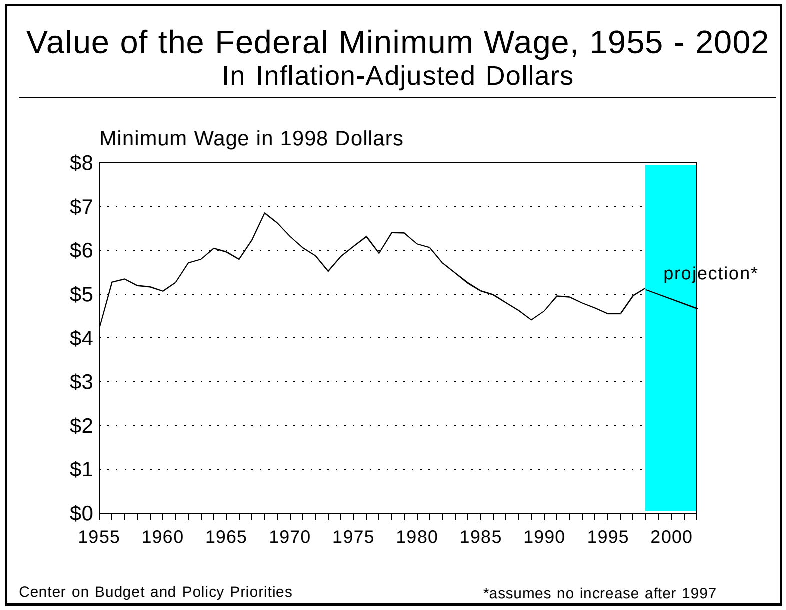
[16] Eric C. Thompson, "Quarterly Forecasts for the Kentucky Economy, 1999-2001," *Kentucky Annual Economic Report: 1999*, Center for Business and Economic Research, University of Kentucky, 1999 and Kentucky Department for Employment Services, Labor Market Information, *Kentucky Occupational Outlook to 2005.*

[17] William S. Snell, "The Volatile and Uncertain Outlook for Tobacco in Kentucky," in eds. Michael T. Childress, Billie M. Sebastian, Peter Schirmer, and Michal Smith-Mello, *Exploring the Frontier of the Future: How Kentucky Will Live, Learn and Work,* The Kentucky Long-Term Policy Research Center, 1996.

Figure 9



- The prospects of less-educated workers are dim as well. The Kentucky Department for Employment Services predicts that occupations available to those without a high school diploma will decline as a share of total employment. Not surprisingly, most of the fastest growing areas of employment for low-educated workers will be low-wage jobs.[18]

Declining Value of the Minimum Wage

In addition to these shifts in the labor market that have made it more difficult for parents to support their families through work, government policies have also hindered rather than helped families' efforts. Most significantly, Congress has allowed the value of the minimum wage to erode over time.

- The inflation-adjusted value of the federal minimum wage in 1999 will be lower than in any year between 1956 and 1985 after adjusting for inflation. (See Figure 9.)

- During the 1960s and 1970s, the earnings of a full-time minimum wage worker employed throughout the year typically were enough to lift a family of three out of poverty without considering other sources of income. In 1999, full-time minimum wage earnings equal just 80 percent of the poverty line for a family of three. The gap between full-time

[18] Kentucky Department for Employment Services, Labor Market Information, *Kentucky Occupational Outlook to 2005.*

minimum wage earnings and the poverty line for a family of this size is $2,646.[19]

Contrary to the popular stereotype, the majority of minimum wage workers nationally are adults, not teenagers. Most minimum wage workers in the United States are in low-income families and provide a significant share of their families' earnings.[20] This means that the decline in the value of the minimum wage has made it harder for low-wage workers to support their families. Research indicates that the fall in the value of the federal minimum wage is a factor behind the substantial decline in earnings for low-wage workers — and the widening gap between low-wage and higher-wage workers — since the late-1970s.[21]

State Tax Burdens on Working Poor Families

Another factor making it difficult for Kentucky's working poor families to make ends meet is the disproportionate state tax burden they bear. Kentucky's tax system is regressive, meaning that taxes absorb a larger proportion of the incomes of lower-income households than of higher-income households. In 1995, the average state and local tax burden on the poorest fifth of married, non-elderly families in Kentucky was 10.5 percent of income. By contrast, the wealthiest one percent of families spent an average of only 8.2 percent of income on taxes.[22] The regressivity of the system stems in large part from the state's substantial reliance on sales taxes, the gasoline tax, and taxes on real property and vehicles, which accounted for 39 percent of state and local own-source revenue in 1996. These taxes fall disproportionately on low-income workers since they must spend a larger fraction of their income on these goods than do more wealthy individuals. This is true even though the state exempts food from the sales tax. Finally, although Kentucky's income tax is mildly progressive, it still exacts a heavy toll on low-wage workers. In 1998, two-parent families of four with incomes as low as $5,000 had income tax liability— one of the lowest tax thresholds in the country.

[19] This gap between earnings and the poverty line for a family of three disappears if one considers the effects of the federal Earned Income Tax Credit. Even after including the value of the EITC, however, the earnings of a full-time minimum wage worker are still insufficient to lift a family of four out of poverty.

[20] Lawrence Mishel, Jared Bernstein, and John Schmitt, *The State of Working America, 1998-99*, Economic Policy Institute, 1999.

[21] See, for example, Nicole Fortin and Thomas Lemieux, "Institutional Change and Rising Wage Inequality: Is There a Linkage?" *Journal of Economic Perspectives*, Spring 1997, pp. 75-96.

[22] *Who Pays?: A Distributional Analysis of the Tax Systems in All 50* States, Citizens for Tax Justice and the Institute on Taxation and Economic Policy, June 1996.

Families of this size with poverty level income paid $550 in Kentucky income taxes in 1998, the highest amount in the nation.[23]

[23] *State Income Tax Burdens on Low-Income Families in 1998: Assessing the Burden and Opportunities for Relief*, Center on Budget and Policy Priorities, 1999.

IV. Policies to Help Working Poor Families

The persistence of poverty among working families deserves the attention of policy makers both because of recent welfare reform efforts and because of the implications of this situation for children. Kentucky's welfare caseload has declined by almost 40 percent since it reached its peak in 1993. Unfortunately, leaving welfare does not automatically mean leaving poverty. In Kentucky, 59 percent of those leaving welfare for work in 1998 earned less than seven dollars an hour, a wage below the poverty line for a family of four.[24] Moreover, because most poor families with children have one or more parents who work — with a substantial proportion working full-time year-round — Kentucky's high child poverty rate is unlikely to decline significantly without additional efforts to assist low-wage working families.

Kentucky can pursue several avenues for addressing the needs of working poor families with children. The particular hardships faced by workers lacking a high school education and the high proportion of working poor parents who have not completed high school suggest that the state should continue to support education reform initiatives designed to boost high school graduation rates. In addition, the state could consider using TANF funds to support basic education and training for welfare recipients to increase their chances of obtaining jobs. Aside from implementing programs to help workers improve their prospects in the labor market, Kentucky can

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[24] Scott Cummings and John P. Nelson, *From Welfare to Work: Second Year Survey of Discontinued K-TAP Recipients*, Center for Policy Research and Evaluation, University of Louisville, 1999. These findings confirm those of national level studies about the earnings of people leaving welfare for work. These studies are summarized in *Welfare Recipients Who Find Jobs: What Do We Know About Their Employment and Earnings?*, Center on Budget and Policy Priorities, 1998.

encourage the labor force participation of poor families by rewarding their work effort and by relieving some of the costs that families incur as they move from welfare to work.

Implement a State Earned Income Tax Credit

Kentucky's overall tax system places a disproportionate burden on low-income families. This excessive tax burden on the poor can most easily be addressed through the income tax system. The design of other major taxes makes targeting relief on the poor much more cumbersome. For example, the sales tax is collected by merchants from consumers without regard to their income level. Although most poor families with children are renters and therefore do not pay property taxes directly, economists generally agree that property taxes are passed through from property owners to renters as part of a rent payment, again without consideration of income level.[25] The income tax, on the other hand, is calculated as a percentage of a taxpayer's total income and thus offers the opportunity to reduce directly the burden of taxes on the poor.

During the past few years, Kentucky has taken some steps to relieve the income tax burden on the working poor. For instance, in 1996 the legislature approved the gradual increase of the standard deduction. The standard deduction reduces the amount of income that is subject to taxation and therefore can remove some low earners from the income tax rolls. In many states the combined value of the standard deduction and personal and dependent exemptions is enough to exclude most working poor families from the income tax. However, in Kentucky, even when the phase-in of the standard deduction increase is complete in 2000, two-parent families of four still will begin paying taxes when their incomes reach only $5,500, less than one-third of the federal poverty line.

Another feature of Kentucky's income tax system which attempts to relieve the tax burden on the poor is the low-income credit for taxpayers earning less than $25,000 annually. Enacted by the 1990 Kentucky General Assembly to partially offset the regressivity of increases in the sales tax, the credit eliminates total income tax liability for those earning less than $5,000 per year. The percentage of tax liability forgiven diminishes as income increases. For example, the credit eliminates half of tax liability for those with incomes between $5,000 and $10,000 and 25 percent of tax liability for those with incomes between $10,000 and $15,000. While this credit provides some relief to poor taxpayers, it does not go far enough. Even after subtracting the credit, a two-

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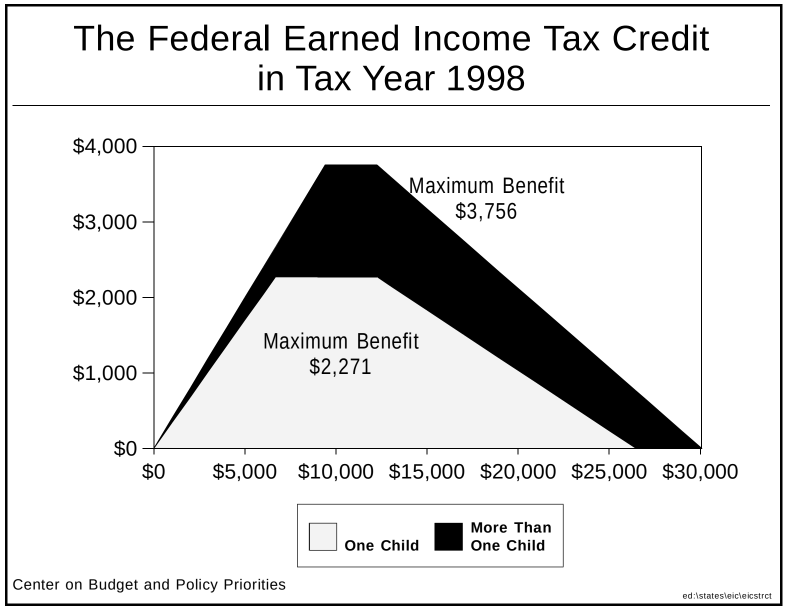
[25] Some states create a property tax relief program called a "circuit breaker". Payments under circuit breaker programs are set at a level to exclude those with income below a certain threshold from the property tax. Kentucky has such an exclusion only for the elderly.

parent family of four with poverty level income owed $550 in state income taxes in 1998, the highest tax burden in the country.

By implementing a state earned income tax credit modeled on the federal EITC, Kentucky would increase its income tax threshold, reduce the income tax burden on poor families, and offset the effects of other, more regressive state taxes.

Figure 10



The federal earned income tax credit is a tax credit for low- and moderate-income workers, primarily those with children, designed to offset the burden of Social Security payroll taxes, supplement earnings, and complement efforts to help families make the transition from welfare to work. It is a refundable credit, meaning that the worker receives the full amount of the credit, even if the credit amount is greater than the worker's income tax liability.

For families with very low earnings, the value of the federal EITC increases as earnings rise. (See Figure 10.) In other words, the EITC encourages work. For example, in 1998 families with two or more children received an EITC equal to 40 cents for each additional dollar earned until earnings reached $9,390, for a maximum benefit of $3,756. Families remained eligible for the maximum EITC benefit until their incomes exceeded $12,260. Then, EITC benefits phased out gradually. In 1998, families with two or more children were eligible for some EITC benefit until income exceeded $30,095 (an amount equal to about 180 percent of the poverty level for a family of four).

The federal credit was claimed by some 300,000 families and individuals in Kentucky in tax year 1997. At least 11 percent of taxpayers in every county in Kentucky claimed the credit in tax year 1996, the most recent year for which county level data are available. The largest number of claims filed were in the urban counties of Jefferson and Fayette, which accounted for 22 percent of all claims in the state. The highest proportion of tax returns claiming the EITC occurred in rural counties. For example, 42 percent of tax returns filed in McCreary County claimed the federal EITC. On average, each Kentucky beneficiary received $1,400 from the credit.

The federal EITC has taken great strides toward meeting its goals of reducing poverty and encouraging work effort. The federal EITC lifts more people out of poverty than any other government program.[26] In 1997 more than four million people — 12 percent of poor people in the country — were lifted out of poverty by the federal EITC.[27] To give a sense of what this means in Kentucky, if the federal EITC were to lift 12 percent of Kentucky's poor population from poverty, 75,000 fewer people would be poor. In addition, research has found that a large share of the increase in employment of single mothers in recent years can be attributed to expansions of the EITC.[28]

Despite the success of the federal EITC in reducing poverty among working families, wages plus the EITC do not guarantee an escape from poverty for all families. Even many families with a full-time, year-round worker remain poor. Supplementing the federal EITC with a state EITC can close or substantially reduce the poverty gap for these families. (See example in box on following page.)

As ten other states have already done, Kentucky could create a state EITC. Setting the Kentucky EITC as a percentage of the federal credit would make the credit relatively easy for the state to administer and for families to claim. Some state EITCS are refundable, like the federal credit, and some are not. While a non-refundable credit can only be used to provide income tax relief and thus cannot lift families out of poverty, a refundable EITC actually puts additional money in the pockets of poor families, boosting the incomes of low-income working families, including those making the transition from welfare to work, and offsetting sales and excise taxes paid by low-income families.

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[26] *Strengths of the Safety Net: How the EITC, Social Security, and Other Government Programs Affect Poverty,* Center on Budget and Policy Priorities, 1998.

[27] United States Bureau of the Census, *Poverty in the United States: 1997,* Table C-4. This table shows that the poverty rate in 1997 was 14.3 percent when poverty is measured using the official measure of income — which includes all cash income other than capital gains — plus the impact of federal taxes. When the value of the EITC is then added, the poverty rate drops to 12.7 percent. Under this definition of after-tax cash income, then, the EITC lifted 4.3 million people out of poverty in 1997.

[28] Nada Eissa and Jeffrey B. Liebman, "Labor Supply Response to the Earned Income Tax Credit," *Quarterly Journal of Economics*, May 1996, 112(2), pp. 605-637 and Bruce D. Meyer and Dan T. Rosenbaum, "Welfare, the Earned Income Tax Credit, and the Labor Supply of Single Mothers," Northwestern University / University of Chicago Joint Center for Policy Research, Working Paper, May 1998 #2.

Deborah and James Williams
Kentucky's Working Poor

Deborah and James Williams (not their real names) live with their two children. James, age 32, works full-time in a furniture factory. Deborah stays at home to care for their two children, both of whom are pre-school age. James earned $14,262 in 1998, and the family qualified for the federal earned income credit, giving them a $3,334 tax refund. Their total income after payroll taxes, the federal EITC, and state taxes, $16,129, fell about $525 below the 1998 poverty line for a family of four — $16,655. A state earned income tax credit set at 20% of the federal EITC would have lifted this family's income above the poverty line.

This family was drawn from responses to the 1998 March Supplement of the Current Population Survey. Their income has been adjusted for inflation to equal 1998 dollars.

	With federal EITC	With federal EITC and 20% State EITC
Earnings less payroll tax	$13,172	$13,172
EITC	+3,334	+3,334
State taxes	-377	+164
Total income	$16,129	$16,670
Poverty line	$16,655	$16,655
Shortfall	$526	($15)

By establishing a state EITC, Kentucky would substantially increase its income tax threshold, the income level at which a family begins to owe taxes. Table 1 presents the income tax threshold in 1998 for a two-parent family of four under current law and what it would have been if Kentucky had a state EITC of various magnitudes. To completely eliminate the income tax burden on these families, Kentucky would need to establish an EITC equal to 25 percent of the federal credit. A more moderate credit of 15 percent of the federal EITC — a level equal to the average of existing state EITCs — would result in a tax threshold of $14,300. While a 15 percent EITC would mean that some poor families would continue to owe income tax, the tax threshold would be almost three times higher than the current level.

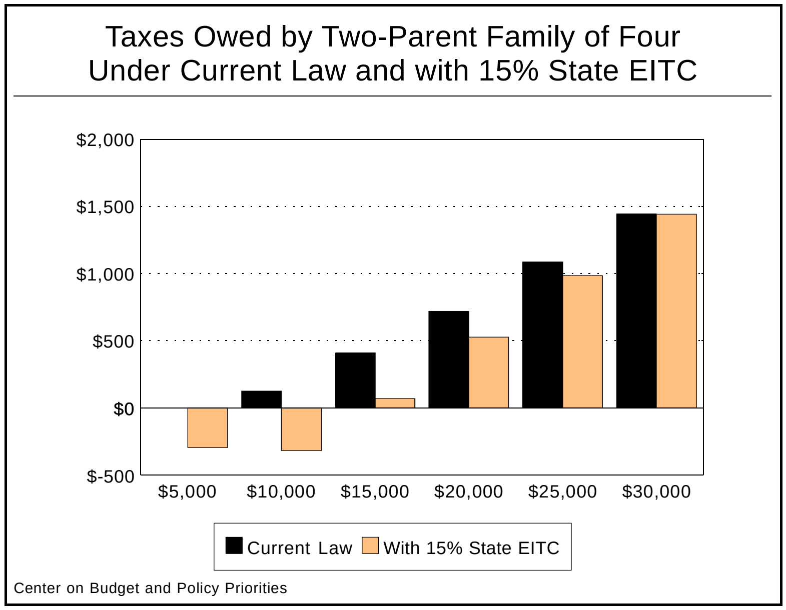
Table 1

Income Tax Thresholds Under Current Law and with State EITCs of Various Sizes

Current Law	$ 5,000
5% EITC	$ 8,800
10% EITC	$12,200
15% EITC	$14,300
20% EITC	$16,000
25% EITC	$17,300

Figure 11 compares the income tax burden under current law for a two-parent family of four to the amount of taxes these families would owe if Kentucky established a refundable EITC equal to 15 percent of the federal credit. Two-parent families of four with income under $14,300 would receive a refund and families below the federal eligibility threshold, which in 1998 was $30,095 for a family with two or more children, would owe less in taxes than they do under the current system.

Figure 11



Raise the State Minimum Wage above the Federal Level

The value of the federal minimum wage has declined during the past 20 years, making it more difficult for low-wage workers to support their families. A higher minimum wage would help reverse or moderate the decline in wages for workers at the bottom of the pay scale, help more working families escape poverty, and improve the likelihood that parents making the transition from welfare to work can support their families through employment. Each 25 cent increase in the minimum wage would boost the income of a full-time minimum wage worker by $480 per year, after payroll taxes.[29]

Because an additional increase in the federal minimum wage is at best uncertain in the near future, only by increasing the state minimum wage can Kentucky boost the wage floor for low-income workers. Currently, Kentucky's state minimum wage

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[29] For someone working 40 hours per week and 52 weeks per year at the minimum wage, a 25 cent increase would yield a *gross* annual wage increase of $0.25 times 2,080, or $520. After payroll taxes of 7.65 percent are deducted, the net gain is $480.

All families receiving food stamps and families in most states that receive welfare benefits would benefit to a smaller extent from an increase in the minimum wage because part of the additional earnings would be offset by benefit reductions.

automatically adjusts to equal the federal standard. Eight states and the District of Columbia set their minimum wages above the federal level.[30]

One of the principal arguments against raising the minimum wage is that it would price many workers out of the job market. In addition, some argue that an increase in the state minimum wage would result in a loss of jobs to neighboring states with lower minimum wages. While these concerns must be considered, the weight of recent findings on the minimum wage challenges this view and suggests that a moderate increase in Kentucky's minimum wage above $5.15 an hour would boost the incomes of low-wage workers without having adverse employment consequences.

One pair of researchers examined the increase in the New Jersey minimum wage to $5.05 an hour in 1992, a level roughly equal to $6.00 an hour in 1999 dollars.[31] The study compared employment growth in fast-food restaurants in the state with employment growth in nearby eastern Pennsylvania, where the minimum wage was not raised. The study found that employment trends actually were more favorable in New Jersey than in Pennsylvania.

The studies do not suggest that any increase in a state's minimum wage — no matter how large — would have negligible employment effects. Instead, they suggest that the labor market functions in a more complicated manner than has been assumed by those who believe any increase in the minimum wage leads to job losses. For example, a higher minimum wage may limit turnover and make it easier for employers to find qualified workers, thereby boosting employment rather than reducing it. The studies also suggest that when the minimum wage is at a low level — as it currently is — moderate increases are likely to have negligible negative impacts on employment.

Help Working Poor Families Obtain Health Insurance

During the mid-1990s in Kentucky, over half of parents and nearly one-third of children in working poor families had no private or government supported health insurance. Increasing the health insurance coverage rate of adults requires a different strategy than the one needed to raise the proportion of children with health insurance.

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[30] These states are Alaska, California, Connecticut, Hawaii, Massachusetts, Oregon, Vermont, and Washington.

[31] David Card and Alan Krueger, "Minimum Wages and Employment: A Case Study of the Fast Food Industry in New Jersey and Pennsylvania," *American Economic Review*, Volume 84, Number 4, September 1994. See also, David Card, "Do Minimum Wages Reduce Employment? A Case Study of California, 1987-89," *Industrial and Labor Relations Review*, October 1992.

While there have been several federal initiatives to extend health insurance to children, until recently very little federal attention had been devoted to expanding health insurance coverage for working parents. Kentucky can expand access to health care for low-income adults by taking advantage of incentives offered by the federal government. To increase the insured rate among children, Kentucky needs to establish an effective outreach system to encourage participation in its existing health insurance programs for children in low-income families.

Expanding Coverage for Parents

Poor parents who work are more likely to be uninsured than poor parents with little or no work during the year: in 1997 among poor adults living in households with children in the United States, 46 percent of those who worked more than 13 weeks were uninsured compared with 25 percent of such adults who worked 13 weeks or less.[32] In the past, the policy of offering adults Medicaid only if they were receiving welfare (with narrow exceptions) meant that low-income working parents were uninsured at much higher rates than their unemployed counterparts. Providing ongoing health care coverage to low-income working parents will make leaving welfare and entering the low-wage job market a more viable option for many parents. Moreover, the opportunity to receive regular health care could promote job retention among low-income working parents by helping them to avoid illnesses that might cause them to miss work.

The federal welfare law enacted in August of 1996 gives states a little-recognized opportunity to use Medicaid to provide health care coverage to these low-income working parents. The opportunity to expand Medicaid to low-income working parents arises primarily from the broad flexibility accorded states to define what counts as income and resources when they determine Medicaid eligibility for families. In the past, states could provide health insurance coverage to working parents only if the states were willing to use their own funds entirely or to pursue a waiver of federal law that would allow them to expand Medicaid to this population. The new option allows states to receive federal Medicaid matching funds to expand coverage for this group without a waiver. For Kentucky, this means that the federal government will finance about 70 percent of the cost of expanding coverage for low-income parents.

Ensuring That Eligible Children Enroll in State Health Programs

Kentucky has already taken great strides toward improving health insurance coverage among children in low-income families. In July 1998, Kentucky expanded its Medicaid eligibility criteria to include all children living in families with income below

[32] Center on Budget and Policy Priorities calculations based on data from the March 1998 Current Population Survey.

100 percent of the federal poverty line. In addition, children under the age of one are Medicaid eligible if family income is below 185 percent of the federal poverty line and children between one and six years of age are eligible if family income is below 133 percent of the federal poverty line. Building on provisions of the Balanced Budget Act of 1997 and enacted by the Kentucky General Assembly in 1998, the Kentucky Children's Health Insurance Program (K-CHIP) will provide health insurance coverage for children living in families with income below 200 percent of the federal poverty line, an estimated 55,000 Kentucky children. Plans call for the K-CHIP program to become available to families in July 1999. Under the program, families will have to make some premium payment (from less than $2 to $20 per month depending upon income) and make minimal co-payments at the time of service for all but preventive care.

K-CHIP significantly increases the pool of children eligible for health insurance coverage. But being *eligible* for coverage does not necessarily translate into *actual* coverage. Of the approximately 24,000 Kentucky teens who became eligible for Medicaid in July 1998, less than 20 percent were enrolled as of January 1, 1999. This experience is consistent with national findings: one-fifth of all poor and near-poor children under age 11 who were income-eligible for Medicaid were neither enrolled in Medicaid nor covered by any other form of health insurance in 1994. It is likely that the proportion of children who are eligible for Medicaid but not enrolled has increased since the enactment of the 1996 federal welfare legislation. Prior to the 1996 legislation, families receiving AFDC were automatically enrolled in the Medicaid program. While the law assures that children and parents who would have qualified for Medicaid based on their eligibility for AFDC will continue to be eligible for Medicaid regardless of whether or not they qualify for TANF benefits, studies have shown that children in families who do not receive cash assistance are much less likely to enroll in the Medicaid program.

A large number of the children are eligible for coverage but are not enrolled because their parents do not know about health insurance programs like Medicaid and Kentucky's child health insurance program, or they believe that because they have a job their children do not qualify. The state must develop effective outreach programs to inform families of the opportunities available to them.

Provide Child Care Assistance to More Working Poor Families

One of the most significant hurdles facing parents attempting to enter or remain in the labor force is finding affordable, reliable, quality child care. To remove the barrier to working caused by high child care costs and to ease the transition from welfare to work, Kentucky should increase its efforts to help families with child care expenses.

Access to quality, affordable child care is important for all families. Child care expenses can absorb a large portion of even a moderate income worker's salary, discouraging participation in the labor force and causing hardship. Without adequate child care subsidies, low-income families frequently will be unable to pay for quality child care and will be forced to choose between unsafe or poor quality care, leaving children unattended, or not working. Parents with access to good child care are more likely to enter and remain in the workforce. National experts recommend low-income families above poverty pay no more than 10 percent of income on child care.[33] With child care costs in the state averaging $3,200 per child, even a family earning $30,000 annually would have to spend one-fifth of its income to place two children in child care.[34]

As currently structured, Kentucky families with incomes below 150 percent of the poverty line are eligible for child care assistance. Through this program, the state provides a subsidy to the child care provider minus a parental co-payment. Currently, families with income under $700 per month are exempt from the co-payment requirement. The co-payments begin at five percent of gross income for families earning at least $700 per month, and increase as income rises. The highest co-payment required of any family is 10 percent. In some areas of the state, the subsidy is considerably below child care charges and families are forced to pay the difference, sometimes up to $30 per week, in addition to their co-payment.

Once a family's income exceeds 150 percent of the poverty line it loses all child care assistance. This "cliff" effect can have a devastating impact on parents as they struggle to support their families through work. A two-parent family of four with both children in child care and annual income of $25,600 would qualify for the child care assistance program and would be responsible for a co-payment of 10 percent of income, or $2,560 per year. If this family's income rose to $25,700 per year, it would no longer qualify for the state-subsidized program and would have to assume the entire cost of child care. At the state average cost of $3,200 per child, this family would spend 25 percent of its income on child care expenses. If this family spent 15 percent of its income on food and 30 percent on housing, adding child care expenses to their monthly expenses would leave very little to cover other costs, particularly once payroll and other taxes are considered.

Kentucky should take a number of steps to improve its child care assistance program. First, it should take steps to ensure that the subsidies it provides are adequate

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33 Children's Defense Fund, *Locked Doors: States Struggling to Meet the Child Care Needs of Low-Income Working Families,* March 1998.

34 Children's Defense Fund, *Kentucky: Child Care Challenges*, May 1998.

to cover market rates. Second, it should expand eligibility for the program to 200 percent of poverty. One-third of the states have already expanded eligibility to this level.[35] Increasing eligibility for the program would ensure that fewer families have to struggle under the burden of high child care expenses. Third, the program's structure should be amended to avoid cliff effects.

[35] Children's Defense Fund, *Locked Doors: States Struggling to Meet the Child Care Needs of Low-Income Working Families,* March 1998.

V. Conclusion

Despite a relatively strong economy, sixteen percent of families in Kentucky that included a worker lived with incomes below the poverty line during the mid-1990s. Given the recent decline in the state's welfare rolls and the dim prospects of finding well-paying jobs with benefits for parents leaving welfare, the poverty rate among working families is likely to increase.

This report has highlighted several policies that Kentucky can establish to reduce poverty among working families with children by rewarding their work effort and reducing the substantial work-related expenses they face when leaving welfare for work. All of these policies — a state earned income tax credit, a higher minimum wage, expanded health insurance coverage, and child care assistance — have been implemented in other states. Their adoption would help parents attempting to make the transition from welfare to work achieve self-sufficiency and would also help families who are only one or two paychecks away from needing to rely on public assistance. Together, these changes would greatly enhance the ability of poor parents in Kentucky to support their families through work.