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## TANF CHANGES PENDING IN CONGRESS WOULD IMPOSE SIGNIFICANT COSTS ON CALIFORNIA

**T**he conference agreement on the budget reconciliation bill (S. 1932), pending before the House of Representatives, includes the most significant changes to federal welfare policy since Congress enacted welfare reform in 1996. This measure would increase Temporary Assistance for Needy Families (TANF) work requirements and reduce state flexibility, while providing little new federal funding. The California Budget Project (CBP) estimates that approximately 52,000 additional CalWORKs families would have to meet federal work requirements starting in October 2006 due to these changes. In addition, the CBP estimates that meeting the proposed requirements could require the state to spend more than \$400 million each year for employment services and child care. California also could face substantial federal penalties if it fails to meet the proposed requirements. Penalties could exceed \$160 million in the first year that the state fails to meet the requirements, escalating to more than \$350 million if the state fails to comply for four consecutive years.

### Background

The conference agreement on the budget reconciliation bill (S. 1932), pending before the House of Representatives, includes the most significant changes to federal welfare policy since Congress enacted welfare reform in 1996. The bill would reauthorize the TANF block grant through federal fiscal year (FFY) 2010 and would impose costly new work requirements on states, while freezing the block grant and providing only a minimal increase in federal funding for child care.

The proposed work requirements would reduce the flexibility of California and its 58 counties to develop programs that meet the needs of families in the California Work Opportunity and Responsibility to Kids (CalWORKs) Program.<sup>1</sup> For example, the new requirements would discourage California from allowing CalWORKs recipients to receive vocational educational training for longer than 12 months, since federal law does not allow additional vocational training to count toward the work requirements. These proposed work requirements would greatly increase the state's costs and put California at risk of incurring

substantial federal penalties if, as is likely, the state is unable to meet the new requirements.

In late December, the Senate made minor changes – unrelated to the TANF provisions – to the House-passed conference agreement. These changes require the House to vote again on the full conference agreement. The House is expected to vote on the amended version after reconvening on January 31. This *Budget Brief* outlines key TANF-related changes in the conference agreement and assesses how those proposals could affect California should they become law.

### Conference Agreement Increases TANF Work Requirements and Reduces State Flexibility, But Provides Little Additional Funding

The conference agreement includes several provisions that would have a major impact on the CalWORKs Program.<sup>2</sup>

Specifically, the conference agreement:

- **Requires states to substantially increase the percentage of families meeting federal work requirements starting in October 2006.** Current law requires 50 percent of all families with an adult receiving TANF assistance and 90 percent of two-parent families to meet federal work requirements.<sup>3</sup> However, current law also provides a “caseload reduction credit” that allows states to reduce these rates. The credit is based on the percentage point decline in a state’s TANF caseload since FFY 1995. For example, since California’s caseload has dropped by more than 40 percentage points, the state’s “all-families” requirement was reduced from 50 percent to 6.7 percent in FFY 2002.<sup>4</sup> Most states, including California, would not meet current federal work participation rates absent the caseload reduction credit.<sup>5</sup> In FFY 2002, 27.3 percent of CalWORKs families included in the state’s all-families rate met TANF work requirements – below the 50 percent work participation standard, but above the reduced standard of 6.7 percent. In addition, 41.1 percent of two-parent CalWORKs families met TANF work requirements in FFY 2002.

The conference agreement would change the base year for the caseload reduction credit from FFY 1995 to FFY 2005. This change would substantially increase the work participation rates that states are required to meet. States whose caseloads have not declined or have increased since FFY 2005 would have to meet the maximum work participation rates starting in FFY 2007, which begins October 1, 2006. The CalWORKs caseload has leveled off in recent years and the Schwarzenegger Administration estimates the caseload will increase slightly in 2006-07. Therefore, California is not likely to qualify for a caseload reduction credit and would have to meet the maximum participation rates – including the virtually unreachable 90 percent threshold for two-parent families – or face substantial federal penalties.<sup>6</sup>

In addition, this change could discourage California from allowing CalWORKs recipients to participate in activities that may help move individuals toward self-sufficiency, but which do not meet federal work requirements. For example, federal law only allows vocational educational training to count toward TANF work requirements for up to 12 months. California would be less likely to allow CalWORKs recipients to participate in training for a longer period, since doing so could jeopardize the state’s ability to meet the increased work participation requirements.

- **Restricts states’ flexibility to set policies for programs funded solely with state “maintenance of effort” (MOE) dollars.** Currently, federal work participation requirements do not apply to families receiving assistance funded entirely

with state MOE dollars – funds a state must spend to receive its TANF block grant allotment.<sup>7</sup> States use separate, state-funded programs to establish flexible work requirements for certain families with significant barriers to employment. In addition, many states, including California, moved two-parent families into state-only programs to avoid federal penalties for failing to meet the very high two-parent work participation rate. The conference agreement would eliminate this flexibility by requiring all families served through separate state programs to be included in calculating the work participation rates. This change would increase the likelihood that California would face federal penalties for failing to meet the two-parent work participation rate.

- **Freezes the TANF block grant.** Despite requiring states to meet higher work participation rates, the conference agreement would freeze California’s annual TANF block grant at \$3.7 billion per year. The block grant has remained constant since 1996 when Congress enacted welfare reform and has lost more than one-quarter (25.5 percent) of its purchasing power since FFY 1996. California would receive no additional federal funding to support job training and other employment services to help additional CalWORKs families meet the increased TANF work requirements.
- **Provides minimal additional funding to help states meet child care needs.** The conference agreement provides just \$1.0 billion in additional child care funds through FFY 2010. California would receive an estimated additional \$25.7 million per year in federal child care funds, but this increase is insufficient to keep pace with inflation, let alone meet the cost of additional child care needed due to the increased TANF work requirements.

## Approximately 52,000 Additional CalWORKs Families Would Have to Meet Federal Work Requirements in FFY 2007 for California to Avoid Federal Penalties

California has consistently fallen short of the 50 percent all-families rate and the 90 percent two-parent rate that would take effect in October 2006 under the conference agreement. Using California’s FFY 2002 participation rates and FFY 2005 caseload as a baseline, the CBP estimates that approximately 52,000 additional CalWORKs families, including nearly 18,000 two-parent families, would have to meet TANF work requirements in FFY 2007 for California to meet the higher work participation standards and thereby avoid federal penalties (Table 1).<sup>8</sup>

**Table 1: Approximately 52,000 Additional CalWORKs Families Would Have to Meet Federal Work Requirements in FFY 2007 Under Proposed TANF Changes Pending in Congress**

Share of CalWORKs Families Who Met TANF Work Requirements in FFY 2002	27.3%
Share of All CalWORKs Families Who Would Have to Meet TANF Work Requirements Starting October 2006	50.0%
Share of CalWORKs Two-Parent Families Who Would Have to Meet TANF Work Requirements Starting October 2006	90.0%
Number of CalWORKs Families Estimated to Meet TANF Work Requirements in FFY 2007 (Assuming FFY 2002 Work Participation Rates)	74,000, including 15,000 two-parent families
Estimated Additional CalWORKs Families Needed to Meet Federal Work Requirements in FFY 2007 in Order to Meet the 50% Work Participation Rate	52,300, including 17,800 two-parent families

Notes: Caseload estimates are adjusted for the number of families who are exempt from federal work requirements, including two-parent families with a disabled adult and single parents with a child under age 1. In addition, these estimates assume California would not receive a caseload reduction credit to reduce the all-families and two-parent work participation rates in FFY 2007.

Source: CBP analysis of California Department of Social Services and federal Department of Health and Human Services data

## Meeting the Proposed TANF Work Requirements Would Cost California More Than \$400 Million Per Year

California would likely need to substantially increase spending on employment services and child care for the tens of thousands of additional families who would need to meet federal work requirements. The Congressional Budget Office (CBO) estimates that the cost to all states of meeting the new requirements would total approximately \$8.4 billion over five years.<sup>9</sup> Using the CBO estimates as a baseline, the CBP estimates that the proposed TANF changes could require more than \$400 million in additional CalWORKs spending in FFY 2007, rising to more than \$500 million in FFY 2010.<sup>10</sup> Governor Schwarzenegger's Proposed 2006-07 Budget does not reflect these potential net costs. In fact, the Governor proposes to reduce state funding for the CalWORKs Program – including funding for employment services and child care services that would require additional state funds should the TANF provisions become law.

California could adopt a number of strategies to fund these new CalWORKs costs, including increasing state and county MOE funding above the current level of \$2.7 billion per year. Alternatively, the state could shift funds currently used to provide subsidized child care for non-CalWORKs, low-income families to CalWORKs to meet the increased need for child care for families receiving cash assistance. The state could also reduce the amount of TANF funds that it uses to supplant General Fund dollars in Child Welfare Services, Foster Care, and other programs and use those TANF funds for the CalWORKs Program.<sup>11</sup>

## California Could Face Substantial Federal Penalties If It Does Not Meet the Proposed Work Participation Rates

Federal law imposes fiscal penalties on states that fail to meet the required federal work participation rates for families receiving TANF assistance. The base penalty for failure to meet the all-families rate is 5 percent of the state's TANF block grant, an amount that increases by 2 percentage points for each consecutive year that the state fails to meet the minimum work participation rate, up to a maximum of 21 percent of a state's block grant.<sup>12</sup> The penalty for failure to meet only the two-parent work participation rate is smaller because the base penalty is adjusted according to the size of the state's two-parent caseload. States that are subject to a penalty must spend additional state funds to replace reduced TANF block grant funds.<sup>13</sup>

California could face substantial federal penalties if it is unable to meet the higher work requirements. The CBP estimates penalties could exceed \$160 million for failing to comply with work requirements in FFY 2007, escalating to more than \$350 million if the state is unable to comply for four consecutive years.<sup>14</sup>

In addition to incurring federal penalties, California would be required to increase its MOE spending by approximately \$180 million per year if the state fails to meet its federal work participation requirements. However, the impact of this requirement would depend on the extent to which California increases state spending on CalWORKs in an effort to meet the increased federal work requirements.

Scott Graves prepared this Budget Brief. The California Budget Project (CBP) was founded in 1994 to provide Californians with a source of timely, objective, and accessible expertise on state fiscal and economic policy issues. The CBP engages in independent fiscal and policy analysis and public education with the goal of improving public policies affecting the economic and social well-being of low- and middle-income Californians. General operating support for the CBP is provided by foundation grants, individual donations, and subscriptions. Please visit the CBP's website at [www.cbp.org](http://www.cbp.org).

## ENDNOTES

- <sup>1</sup> CalWORKs was created in 1997 in response to federal welfare reform and was implemented by counties beginning in 1998. See California Budget Project, *CalWORKs: California's Welfare-to-Work Program* (February 2004) for an overview.
- <sup>2</sup> In addition to the TANF-related provisions described below, the conference agreement makes several additional TANF-related changes, including requiring the federal Department of Health and Human Services to issue regulations defining TANF work activities and establishing new administrative procedures for states. The bill also would create a new penalty for states that fail to comply with the new administrative procedures.
- <sup>3</sup> Federal law specifies both the number of hours that TANF recipients must work and the activities that count toward meeting federal work participation rates. Many families are exempt from federal work requirements, including families in which no adult receives TANF assistance.
- <sup>4</sup> Two-parent CalWORKs families were moved to a separate, state-funded program in FFY 2000 and therefore are not subject to federal work requirements.
- <sup>5</sup> See US Department of Health and Human Services, *Temporary Assistance for Needy Families (TANF): Sixth Annual Report to Congress* (November 2004), Table 3:1.a.
- <sup>6</sup> Independent analysts, including MDRC, which has extensively studied the implementation of welfare reform, believe these rates will be virtually unattainable. See, for example, Gordon Berlin, *Testimony on the Reauthorization of the Temporary Assistance for Needy Families Program* (MDRC: March 2002), downloaded from <http://www.mdrc.org/publications/358/testimony.html#implications> on January 18, 2006.
- <sup>7</sup> California's annual MOE requirement of \$2.7 billion is funded with both state and county dollars.
- <sup>8</sup> The Congressional Research Service (CRS) estimates that that approximately 60,700 CalWORKs families would have to meet TANF work requirements in FFY 2007 for California to meet the higher federal work participation standards. See CRS, *TANF Work Participation Standards: Revising the Caseload Reduction Credit* (December 19, 2005).
- <sup>9</sup> The CBO estimate excludes the additional \$1.0 billion in federal child care funding over five years included in the conference agreement.
- <sup>10</sup> This reflects California's share of the additional families expected to meet the work requirements as estimated by the Congressional Research Service (26 percent), multiplied by the total annual cost for each fiscal year as estimated by the CBO, less additional child care funding of approximately \$25 million. In addition, the CBO estimates that states would spend \$800 million prior to the effective date of the new requirements in order to prepare for the implementation date. The Legislative Analyst's Office (LAO) estimates that, based on current state law, the proposed TANF changes would result in net added costs and reduced federal funds of \$1.5 billion over five years (the LAO estimate assumes that California would not increase General Fund spending to meet the new requirements and would be assessed federal penalties, which in turn would trigger a required General Fund backfill of the penalties and a required 5 percent increase in the state's MOE spending level). Legislative Analyst's Office, *Fiscal Effect on California: Pending Federal Deficit Reduction Act of 2005* (January 20, 2006).
- <sup>11</sup> This option would require the state to "backfill" redirected TANF funds with state General Fund dollars to prevent funding reductions in these programs.
- <sup>12</sup> The penalty is based on a state's adjusted TANF block grant, which reflects certain reductions, including transfers of TANF funds to the Social Services Block Grant and the Child Care and Development Block Grant.
- <sup>13</sup> Under current law, the maximum penalty can be automatically reduced based on the degree to which a state is out of compliance. In addition, a state may avoid a penalty by demonstrating reasonable cause for its failure or by entering into a corrective compliance plan with the federal government.
- <sup>14</sup> According to the Legislative Analyst's Office, a penalty is typically assessed two years after a state fails to comply with federal work requirements. Legislative Analyst's Office, *Fiscal Effect on California: Pending Federal Deficit Reduction Act of 2005* (January 20, 2006), pp. 10-11.