

2 X
EITC

Bruce
Kathu } Fy1

U.S. DEPARTMENT OF LABOR
SECRETARY OF LABOR
WASHINGTON, D.C.

Copy: CHR

July 20, 1993

JUL 21 RECEIVED

MEMORANDUM TO THE PRESIDENT

VIA: Robert Rubin
FROM: Robert B. Reich *BM*
SUBJECT: Reconciliation, the EITC, and the Minimum Wage:
How much progress towards the make work pay goal?
cc: Lloyd Bentsen, Leon Panetta, Donna Shalala,
Laura Tyson, Carol Rasco

An assessment of the EITC proposals in the reconciliation bills and the objective of "making work pay" leads to two recommendations. First, we should work to ensure that the House EITC reforms -- which reflect the Administration's proposal -- are retained. The Administration/House reforms make it easier to achieve the goal of lifting families with full-time workers out of poverty and provide overdue tax relief to poor childless workers.

Second, such an assessment underscores how the minimum wage and the EITC are complementary policies, and that it is time to begin to investigate what minimum wage reforms may be appropriate. To achieve the goal of making work pay, the minimum wage should be raised and then indexed. Even the substantial Administration/House EITC expansion cannot achieve the goal alone. And just as certain features of the EITC make up for shortcomings with the minimum wage, certain features of the minimum wage address shortcomings with the EITC. For example, in contrast to the EITC which is nearly always received through one lump sum payment at tax time, the effects of a change in the minimum wage are felt with every paycheck.

This assessment has led me to step up Labor Department efforts to review the minimum wage. I will report back to you in 90 days with my initial recommendations, via the NEC and/or the Domestic Policy Council.

House vs. Senate EITC

In designing the parameters of your EITC expansion, the combined value of full-time minimum wage earnings, plus EITC benefits, plus food stamps, and minus payroll taxes, was compared to the poverty line. The proposed EITC increase for families

with two or more children was set at a level that would lift a family of four with a full-time minimum wage worker out of poverty.

The Administration's EITC proposal, incorporated in the House bill, would attain this objective virtually precisely. But two of the assumptions made in the calculation should be highlighted. First, to reach the objective, the calculation assumed that the value of the minimum wage would equal \$4.50 an hour in 1994 dollars.¹ Second, the assumption of the receipt of food stamps -- valued at more than \$3,000 for a family of four with minimum wage earnings -- is often unwarranted. Substantially less than half of working poor families receive food stamps.

All this suggests there is virtually no room to maneuver in terms of cutting back our proposed expansions in the EITC. Nevertheless, the Senate reduced the proposed increases in a variety of ways. For example, the Senate provisions make it somewhat less likely that families with full-time workers will be lifted out of poverty. A family of four with two children would receive a maximum EITC benefit that would be \$56 lower than under the House bill. Such a family with a full-time minimum wage worker would therefore fall \$56 further below the poverty line.

The Senate's elimination of the new, small EITC for childless workers also is very troubling. Poor childless workers would no longer receive an offset for the new energy taxes they may have to pay. In addition, more than any other group of taxpayers, poor childless workers have been hit hardest by tax increases since 1980. Several of these increases contained regressive tax provisions that included an EITC offset for working poor families with children, but did not include an offset for poor workers without children. As a result, the overall federal tax burden of the poorest fifth of households without children has risen a dramatic 38 percent since 1980. Single workers also are the one group that still pays federal income taxes even when they are in poverty. The new EITC for childless workers would help address these problems.

The Role of the Minimum Wage

The minimum wage and the goal. Even if the Administration/House EITC reforms are fully adopted, indexing the minimum wage at \$4.50 an hour is a minimum prerequisite to reaching the goal of lifting families of four with full-time

¹A minimum wage level of \$4.50 an hour in 1994 is consistent with indexing the wage floor at its 1992 level of \$4.25 an hour.

workers out of poverty. If the minimum wage is not indexed, or if it is indexed at a lower level, the goal will not be achieved.

- If the minimum wage remains unchanged at a given, nominal level year after year, it will take a continuously expanding EITC just to maintain minimum wage families at the same real income level. Otherwise, the fall in the purchasing power of the minimum wage will drop families further into poverty.
- A small difference in hourly wage levels can have substantial effects on total income. If the minimum wage is indexed at \$4.25 an hour instead of at \$4.50, the effect on the annual earnings of a full-time worker (employed 2,080 hours a year) would be a reduction of \$520.² For a minimum-wage worker employed half-time, the reduction would be \$260.
- Since the large majority of the working poor are employed for part of the year or for less than 40 hours a week, since most of the working poor do not receive food stamps, and since many of the working poor live in families of five or more, most of the working poor will remain in poverty even under the Administration/House EITC expansion and a \$4.50-an-hour minimum wage. A larger minimum wage increase could narrow the poverty gap for these working poor households.

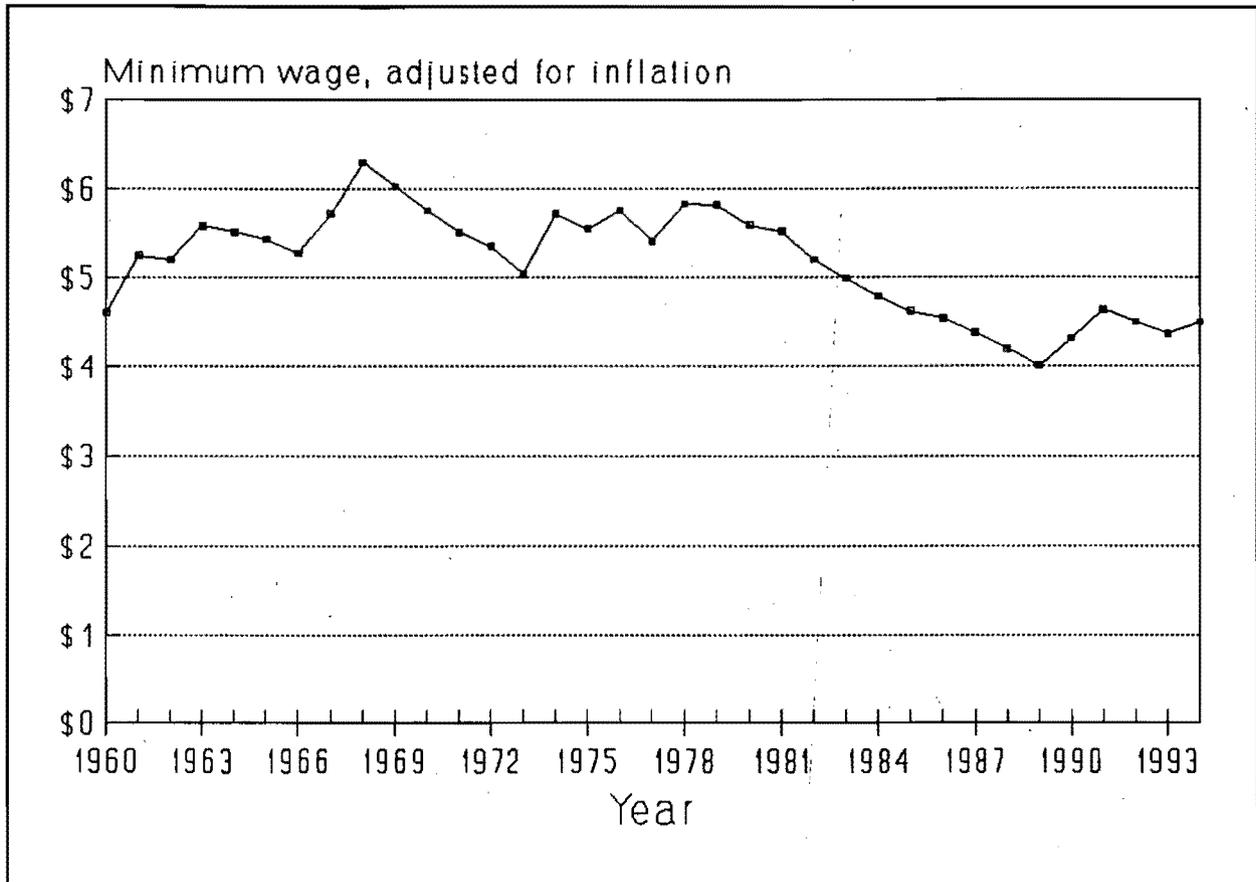
Historic Comparisons. From 1981 to 1990, the minimum wage remained at \$3.35 an hour, despite the jump in the cost of living. President Bush agreed to raise the wage floor to \$4.25 an hour, after vetoing a bill mandating a higher level. But this increase made up less than half of the ground that had been lost to inflation.

Consequently, increasing the minimum wage by just 25 cents to \$4.50 an hour, and then indexing it, would yield a minimum wage well below its traditional value.

- A minimum wage of \$4.50 an hour in 1994 would be more than \$1 -- or about 19 percent -- below its average value in the 1970s, after adjusting for inflation. (See Figure 1.)

²The net effect on income would be less because the family would owe less in payroll taxes. If the family receives food stamp benefits, which are higher for families with lower incomes, the net effect would also be diminished somewhat.

Figure 1. Historic value of the minimum wage, assuming a minimum wage of \$4.50 an hour in 1994. (Values in 1994 dollars.)



- In fact, setting the minimum wage at \$4.50 an hour in 1994 would establish a lower real level than what was agreed to by President Bush. He supported a level of \$4.25 an hour as of April 1, 1991; in 1994 dollars, that would equal an estimated \$4.67 an hour.

For full-time minimum wage earners living in families with two or more children, the net income of a full-time worker receiving \$4.50 an hour and the Administration/House EITC would be significantly higher than the net income of a full-time minimum wage worker during the Bush years. The larger EITC would more than offset the somewhat lower value of the minimum wage.

Taking a longer view, under the Administration/House EITC and a \$4.50 an hour minimum wage, the combined value of minimum wage earnings and the EITC, minus payroll taxes, would be about the same for families with two children as the average combined

value in the 1970s.³ In other words, for these families, the establishment and expansion of the EITC over time will have essentially offset the fall in the value of the minimum wage over time.

Since, however, workers with less than two children qualify for a smaller EITC than workers with two or more children, minimum wage earners with less than two children would have less net income than in the 1970s. The increase in their EITC will not have offset the fall in the minimum wage.

Delivery issues. On the one hand, it can be argued that the substitution of a higher minimum wage with a higher EITC would be a positive accomplishment. To be sure, the EITC poses no threat to employment opportunities and can be better targeted to families in need.

On the other hand, there are several reasons why the minimum wage and the EITC are best viewed as policies that complement -- rather than substitute for -- each other. One is the timing of payments:

- More than 99 percent of EITC recipients receive their benefits in one lump sum payment when they file their taxes. A partial redress to this delivery problem may be included in the reconciliation bill, and stronger remedies are being examined in the context of welfare reform, but it is likely to prove very difficult to change this proportion substantially.
- By contrast, the minimum wage is delivered in a more timely manner for struggling families; the effects of the minimum wage are felt with each paycheck.

A second factor to consider is public perception. Your pledge to make work pay has been well-received, but despite the EITC's many merits, I believe a larger lump sum payment delivered through the tax code will not demonstrate our commitment to supporting those who play by the rules as much as a minimum wage increase would.

Finally, there is the issue of striking the right balance between a private and public sector approach. The costs of making work pay are too large to be borne entirely by either the public or private sectors. Relying on both a stronger EITC and a stronger minimum wage involves the appropriate sharing of the

³Because changes in the value of food stamps are difficult to compare over time, these calculations did not consider food stamp benefits.

burden between the two sectors.

Next Steps

The complementary effects of the EITC and the minimum wage on the working poor are important. For this reason, it is important to consider the value of the minimum wage in the context of developing our welfare reform proposal.

At the same time, however, a full assessment of where to set the minimum wage should consider a wide range of factors beyond its income effects on the working poor. After all, most minimum wage workers are not poor. And the potential effects of a minimum wage increase on employment should of course be weighed, particularly in combination with the effects of the health reform proposal.

Unless you prefer a different schedule or approach, the Labor Department intends to fully assess all these factors over the next 90 days. I will then forward my initial recommendations to you, via Carol Rasco and Bob Rubin.

OFFICE OF DOMESTIC POLICY

THE WHITE HOUSE

JAN 1 9 11

FROM THE OFFICE OF: **CAROL H. RASCO**
ASSISTANT TO THE PRESIDENT
FOR DOMESTIC POLICY

TO: Sylvia

DRAFT RESPONSE FOR CHR. BY: _____

PLEASE REPLY (COPY TO CHR): _____

PLEASE ADVISE BY: _____

LET'S DISCUSS: _____

FOR YOUR INFORMATION: _____

REPLY USING FORM CODE: _____

FILE: _____

RETURN ORIGINAL TO CHR: _____

SCHEDULE: _____

REMARKS: I think this ^{is} for NEC
to handle.

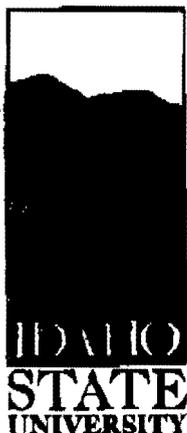
FAX # (202) - 456 - 2878

TO: CAROL ROSCOE,
WHITE HOUSE

FROM: PAUL ANIR.

Idaho State University
College of Engineering
(208) 236- 2772
FAX (208) 236-4538

3 Pages, including cover sheet.



Carol Roscoe
Assistant to the President
Domestic Policy
West Wing, 2nd Floor
White House

01/19/94

Dear Ms. Roscoe:

I write this letter requesting assistance in starting an International Internship/Training program with a view to "crack" open markets around the world.

Idaho State University is attempting to start a pilot internship program that will link students with businesses in Asia. For starters we will focus on Taiwanese businesses and are working with their Coordination Council to that end. The internships will be of one year duration and the goal would be to get a better understanding of Asian business practices and "non-tariff barriers".

We think that an innovative approach such as this could possibly be funded from current programs in either commerce, labor or education departments. Unfortunately despite our efforts we have had no meaningful response. We believe that the Secretary of Labor's retraining/re-employment proposal can be adapted to include innovative approaches like the one described above. If not, we sincerely hope that your staff will be able to assist us in locating grant programs that we could apply for.

Enclosed is a copy of the letter from the Department of Labor in response to our request for assistance.

Sincerely Yours


Paul Anir
Assistant to the Dean
College of Engineering
Idaho State University
Pocatello, ID-83209

Phone:
(208) 236-2902
FAX:
(208) 236-4538



U.S. Department of Labor

Employment and Training Administration
200 Constitution Avenue, N.W.
Washington, D.C. 20210



JAN 10 1994

Mr. Paul Anir
Assistant to the Dean
College of Engineering
Idaho State University
P.O. Box 8060
Pocatello, Idaho 83209

Dear Mr. Anir:

Thank you for your recent letter to Secretary Reich in which you shared information about your pilot internship program and requested funds to partially support it. Your letter was forwarded to my office for consideration.

We are not able to directly offer financial assistance for your proposal nor are we able to identify a specific office in another Federal agency that could assist you. However, your proposal is a novel one and may be of interest to a private foundation. We are aware of a number of foundations that have been specifically set up to further relations between the United States and other countries.

Good luck in your search.

Sincerely,

JACK RAPPORT
Deputy Administrator
Office of Work-Based Learning