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Measuring Poverty in America

Douglas J. Besharov*

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Chairman McDermott, members of the subcommittee, thank you for inviting me to testify on this important topic.

"We declared war on poverty, and poverty won," famously quipped Ronald Reagan. That was certainly the impression most Americans got from the media images of the flood-stranded poor in New Orleans. And that is surely the message from the continuing high rate of poverty reported by the federal government's official poverty measure. But poverty, or at least material deprivation, has declined sharply over the past forty years and that, in turn, should give us confidence that more progress is possible.

Each year, the Census Bureau reports on the nation's poverty rate, based on the number of people with incomes below the official poverty line, adjusted annually for inflation. In 2005, the poverty line, which varies by family size, was $15,577 for a family of three, and $19,971 for

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*Douglas J. Besharov is the Joseph J. and Violet Jacobs Scholar at the American Enterprise Institute for Public Policy Research and a professor at the University of Maryland School of Public Policy. He was the first director of the U.S. National Center on Child Abuse and Neglect, and is the author of *Recognizing Child Abuse: A Guide for the Concerned*, published by the Free Press.

a family of four.[1] By this measure, in 2005, about 12.6 percent of the population, or about 37 million people, were reported as poor,[2] including 17.6 percent of children and 10.1 percent of the elderly.[3] That's essentially the same as the 1968 rate of 12.8 percent[4]—which is a big reason why people think so little progress has been made against poverty.[5] (Little noted, however, is that the poverty rates for the elderly declined considerably, from 25 percent in 1968.)[6]

Many on the left as well as the right believe that there has been "much greater progress in poverty reduction over the last two decades than the official poverty measure would indicate,"[7] in the words of the Democrats on the Congressional Joint Economic Committee:

> The results presented in this paper suggest much greater progress in poverty reduction over the last two decades than the official poverty measure would indicate. Antipoverty programs such as the Earned Income Tax Credit, combined with changing family formation patterns, including declining teen birth rates and increases in cohabitation, resulted in significant decreases in poverty among all demographic groups. The level of poverty reduction was particularly dramatic during the decade of the 1990s.[8]

What's going on?

Technical Flaws in the Official Poverty Measure

The poverty measure, however, has been widely criticized by analysts from the left and the right for under- or overstating poverty. Let me focus on its technical flaws because they are

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[1]U.S. Census Bureau, "Income, Poverty, and Health Insurance Coverage in the United States: 2005," *Current Population Reports*, Series P60-231 (Washington, DC: U.S. Government Printing Office, August 2006), http://www.census.gov/prod/2006pubs/p60-231.pdf (accessed July 31, 2007), p. 45.

[2]Ibid., 13.

[3]Ibid.

[4]Ibid., 46.

[5]The major differences in the trends among particular demographic groups, such as the elderly (down) and children (up), are usually lost in discussions of the general poverty trend. We describe them below.

[6]U.S. Census Bureau, "Income, Poverty, and Health Insurance Coverage in the United States: 2005," *Current Population Reports*, Series P60-231 (Washington, DC: U.S. Government Printing Office, August 2006), http://www.census.gov/prod/2006pubs/p60-231.pdf (accessed July 31, 2007), p. 52.

[7]Joint Economic Committee Democrats, "Reductions in Poverty Significantly Greater in the 1990s than Official Estimates Suggest," *Economic Policy Brief*, (Washington, DC: Joint Economic Committee, August 2004), http://www.welfareacademy.org/pubs/poverty/Poverty10.pdf (accessed May 9, 2006).

[8]Ibid.

palpable and relatively objective—although correcting them raises what I consider to be unresolvable conceptual, technical, ideological, and financial challenges.

The official poverty measure does a poor job accounting for *inflation.* Each year since 1969, the poverty thresholds have been adjusted for inflation, so that they more accurately reflect the costs of the goods and services in the original 1963 thresholds. The measure used, called the "deflator," is the Consumer Price Index (CPI).

However, it is widely accepted that the CPI overstated the rate of inflation in the late 1970s and early 1980s because it measured housing costs improperly. The Census Bureau *income series* has been adjusted to correct for this inaccuracy by using the CPI-U-X1 for the period 1967 to 1977 and the CPI-U-RS for 1978 to the present.[9] But the corrected CPIs have not have been used to adjust the poverty measure or other formulas that affect the distribution of means-tested benefits largely because of the political disruption that could result.

In addition, the Bureau of Labor Statistics (BLS) developed the chained CPI, an inflation adjustment that takes into account consumer behavior, which further adjusts overstated rates of inflation in the CPI, CPI-U-X1, and CPI-U-RS.

Using the CPI-U-RS to adjust the poverty thresholds for the period from 1978 to the present lowers the poverty rate by about 1.5 percentage points; using the CPI-U-X1 for the period from 1967 to 1977 lowers the poverty rate by about 0.8 percentage points; and using the chained CPI reduces it another 0.4 percentage points. (All adjustments are summarized in table 2.)

The main objection to making these corrections is not based on a defense of past CPI adjustments but, instead, stems from the outcome: a lowering of a poverty line that many feel is already too low and, in any event, that should be raised to reflect higher levels of general affluence.

The official poverty measure does a poor job *counting market income.* The starting point for any analysis of poverty is, of course, the income that individuals and families receive from the market.

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[9] Kenneth J. Stewart and Stephen B. Reed, "Consumer Price Index research series using current methods, 1978–98," *Monthly Labor Review*, June 1999, http://www.bls.gov/opub/mlr/1999/06/art4full.pdf (accessed May 10, 2006). The CPI-U-RS and the CPI-U-X1 are consumer price index series produced by the Bureau of Labor Statistics. The CPI-U-RS is the CPI research series using current methods, and incorporates most of the improvements made to CPI measurement since 1978. The CPI-U-X1 is an experimental consumer price index that uses the rental equivalence approach for estimating housing costs between 1967 and 1982. The CPI-U-RS, which begins in 1978, also incorporates the rental equivalence approach for housing, among other improvements. By combining the CPI-U-X1 for 1967 to 1977 and the CPI-U-RS from 1978 onward, it is possible to correct for the overstatement of inflation from 1967 to the present.

Unfortunately, Census Bureau data substantially understate the cash income of Americans. Government estimates are that, in 2001, about $804 billion of personal income went unreported, including about $747 billion of various forms of market income such as wages and salaries ($158 billion), self-employment income ($302 billion), interest and dividends ($132 billion), Social Security ($49 billion), and other retirement payments ($106 billion).[10] Also unreported was about $53 billion of government cash transfer payments from just three government programs (income maintenance/$24 billion, workers' compensation/$20 billion and unemployment compensation/$10 billion).[11] Other income also is surely unreported.

Conservative estimates that adjust for the underreporting of various forms of market income (but not including means-tested government benefits) would lower the poverty rate by about 1.6 percentage points. (It is not clear whether this undercounting of income has worsened over time, so applying this figure to obtain a poverty rate trend has to be done with care.)

The official poverty measure, moreover, is based on the Census Bureau's definitions of cash income which do not include employer contributions to pensions and health insurance. Although there are no estimates for the effect of employer contributions to pensions on measured poverty, counting employer contributions to health insurance would lower measured poverty by about 0.7 percentage points.[12]

Ironically, while excluding these forms of private income, the official poverty measure does count *cash* welfare payments. (That proviso is important because, as discussed below, *noncash* benefits are not counted, although they are often much larger.) In 2004, the average

[10] John Ruser, Adrienne Pilot, and Charles Nelson, "Alternative Measures of Household Income: BEA Personal Income, CPS Money Income, and Beyond," paper prepared for presentation to the Federal Economic Statistics Advisory Committee (FESAC), December 14, 2004, http://www.bea.gov/bea/about/fesac/AlternativemeasuresHHincomeFESAC121404.pdf (accessed May 22, 2006). See also Daniel H. Weinberg, "Alternative Measures of Income Poverty and the Anti-poverty Effects of Taxes and Transfers," paper prepared for the University of Maryland/American Enterprise Institute seminar on "Reconsidering the Federal Poverty Measure," May 10, 2005, http://www.welfareacademy.org/pubs/poverty/Weinberg_Alt_Measures.pdf (accessed May 10, 2006), pp. 12–13.

[11] Another $4 billion of unreported income is attributed to small amounts of "other" income, income amounts collected in the CPS but not accounted for in the administrative data, and a residual amount.

[12] U.S. Census Bureau, "Table 5: Percent of People in Poverty, by Definition of Income and Selected Characteristics: 2002 (Revised)," http://www.census.gov/hhes/www/poverty/poverty02/r&dtable5.html (accessed July 31, 2007).

TANF benefit per year for a family was about $3,030.[13] Removing cash welfare payments from income raises the poverty rate by about 0.8 percentage points.

The official poverty measure ignores *major forms of wealth.* The official poverty measure counts as income interest on money in the bank, for example, but not the wealth embedded in homes and the stock market. This ignores the roughly $9 trillion[14] in home equity (that is, the home's current value minus the amount of money owed on the mortgage). If the equivalent amount of money were in the bank, it would be earning interest that could be used to pay household expenses, and so forth.

Imputing what economists call the "service flow" from home ownership would lower poverty by about 1.0 percentage points. This would mostly impact the elderly, and would lower their poverty rate by about 3 percentage points, from about 10.1 percent under the current measure to about 7.1 percent.

Of course, many people (especially the elderly) feel that they have no choice but to live in their highly appreciated homes, and that moving to another home would place them in a less desirable and perhaps equally expensive situation. But whether or not one counts home equity in a formal poverty measure, it should modify our view of the material needs of a third of the elderly who are now labeled poor.

The official poverty measure does not *subtract taxes.* The current poverty measure does not take taxes into account, largely because they did not affect the poor very much in the 1960s. Back then, a household at the median family income with four dependents paid less than 5 percent of its income in federal income taxes[15] and Social Security payroll taxes were only 7.25

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[13]U.S. Department of Health and Human Services, Administration for Children and Families, Office of Financial Services, "Table A – Combined Federal Funds Spent in FY," http://www.acf.hhs.gov/programs/ofs/data/2004/tableA_spending_2004.html (accessed July 31, 2007); and U.S. Department of Health and Human Services, Administration for Children and Families, Office of Family Assistance, "TANF: Total Number of Families, Fiscal and Calendar Year 2004," http://www.acf.hhs.gov//programs/ofa/caseload/2004/2004_family_tan.htm (accessed July 31, 2007).

[14]Joint Center for Housing Studies of Harvard University, "The Changing Structure of the Home Remodeling Industry: Improving America's Housing 2005," http://www.jchs.harvard.edu/publications/remodeling/remodeling2005.pdf (accessed May 24, 2006), p. 8.

[15]Eugene C. Steuerle, "The Tax Treatment of Households of Different Size," in *Taxing the Family*, ed. Rudolph G. Penner (Washington, DC: The American Enterprise Institute, 1983), p. 76.

percent (with the employee's direct share being only 3.63 percent).[16] (Even sales taxes were low compared to today.)[17]

Now, however, taxes represent a major burden on low-income families and individuals, with, for example, Social Security/Medicare payroll taxes at about 12.4 percent.[18] Counting taxes would raise measured poverty by about 1.4 percentage points: federal income taxes (about -0.2 percentage points), state income taxes (about 0.0 percentage points), Social Security/Medicare payroll taxes (about 1.0 percentage points), and property taxes (about 0.6 percentage points).[19] State and local sales taxes are not included in this discussion because their impact is tracked through the CPI.

The official poverty measure does not account for changes in *family/household structure.* The poverty rate is most often presented for either individuals or families (more accurately, close relatives living together). In the 1960s, that made sense. Now, however, many couples live together without getting married ("cohabitation") and large numbers of unrelated people live together to share household expenses ("coresidency").

This is probably a throwback to the time when nonfamily household members were usually boarders, and their contribution (in rent) was captured in the income to the householder. Now, however, cohabitation among couples (with or without children) is widespread, as are multi-adult shared households (common among young singles and also many immigrants).

Using the Census Bureau's definition of family, the income of grandparents living with a single mother is counted, but not her boyfriend's income (on average about $22,700). Counting the boyfriend's income would lower poverty by about 0.5 percentage points.

[16]Tax Policy Center, Urban Institute and Brookings Institution, "Historical Social Security Tax Rates," http://www.taxpolicycenter.org/taxfacts/payroll/rate_historical.cfm (accessed May 10, 2006).

[17]In 1979, for example, the average state sales tax was about 4 percent; today, it is about 5.4 percent. See Kevin A. Hassett and Anne Moore, "How Do Tax Policies Affect Low Income Workers?" (NPC Working Paper #05-16, National Poverty Center, University of Michigan, September 2005), http://www.npc.umich.edu/publications/workingpaper05/paper16/ (accessed May 18, 2006), p. 18.

[18]Tax Policy Center, Urban Institute and Brookings Institution, "Historical Social Security Tax Rates," http://www.taxpolicycenter.org/taxfacts/payroll/rate_historical.cfm (accessed May 10, 2006). See also Amy O'Hara, "New Methods for Simulating CPS Taxes" (Washington, DC: U.S. Census Bureau, 2004), http://www.census.gov/hhes/www/income/oharataxmodel.pdf (accessed June 1, 2006), p. 3.

[19]U.S. Census Bureau, "Table 5: Percent of People in Poverty, by Definition of Income and Selected Characteristics: 2002 (Revised)," http://www.census.gov/hhes/www/poverty/poverty02/r&dtable5.html (accessed July 31, 2007).

The main argument against counting the income of nonfamily members is that it is not clear how much of the income goes toward supporting the household. The same is true, of course, for family members, but to nowhere near the same degree.

The official poverty measure does not account for *changing consumption patterns.* When the poverty measure was developed, food expenditures represented about one-third of after-tax income for the typical family, so the food-plan amount was multiplied by three to establish the poverty line. Since then, food expenditures have fallen to about one-seventh of total expenditures (and are apparently still declining).[20]

Furthermore, spending patterns in general have changed because the costs of various items have changed at different rates. For example, the poverty measure already implicitly includes medical out-of-pocket ("MOOP") expenditures, such as health insurance premiums, copayments to medical providers, and over-the-counter medications. But these expenditures have risen sharply since the 1960s, and some have suggested subtracting them from income, or adding them to the poverty thresholds, or some combination of the two. Depending upon the approach chosen, this would raise poverty by between 0.2 and 1.2 percentage points. (However, other analysts would argue against doing so on the ground that MOOP expenditures are an implicit element in the current measure.)[21]

The official poverty measure does not account for *increases in national affluence.* Many observers would like to see a relative measure that rises with general affluence. In fact, many would like to see the U.S. adopt the informal approach used in some western European countries that defines poverty as the bottom 40 percent of median family income.

To the extent that poverty should be a function of society's wealth/affluence, they have a point: In the 1960s, the poverty line was 45 percent of median family income for a family of four, now it is only 29 percent. Here are the figures over time:

- In 1960, the poverty threshold for a family of four ($3,022) was 48 percent of the median income for a family of four ($6,295).

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[20]University of Wisconsin, Institute for Research on Poverty, "Improving the measurement of American poverty," *Focus* 19 (2) (Spring 1998): 2, http://www.ssc.wisc.edu/irp/focus/foc192.pdf (accessed March 28, 2004).

[21]Richard Bavier, "Do the current poverty thresholds include any amount for health care?" (Poverty Measurement Working Papers, U.S. Census Bureau, undated) http://www.census.gov/hhes/www/povmeas/papers/moopnow.html (accessed July 31, 2007). Bavier mentions at least three reasons why the poverty thresholds implicitly include an element for medical expenditures: "First, and most important, Mollie Orshansky's seminal articles on the creation of the poverty thresholds give no indication that health care was excluded. . . . The presence of medical needs in the official thresholds is confirmed by the 1969 decision to index the thresholds to the CPI for all items, rather than to continue to index with price changes in a low cost market basket of food. . . . Finally, expert opinion has consistently inferred from the multiplier approach used to set the original thresholds that something for medical care was included."

- In 1965, the poverty threshold for a family of four ($3,223) was 41 percent of the median income for a family of four ($7,800).

- In 1970, the poverty threshold for a family of four ($3,968) was 36 percent of the median income for a family of four ($11,167).

- In 2004, the poverty threshold for a family of four ($19,307) was 29 percent of the median income for a family of four ($66,111).[22]

For 2005, the Census Bureau added a separate adjustment that increased the poverty thresholds by 15 percent, based on the observed increase in real median income for four-person families between 1978 and 2005 using the CPI-U.[23] The result was an increase in poverty of about 2.7 percentage points.

The official poverty measure does not account for *geographic differences in the cost of living.* The current approach treats the entire United States as one economic entity, even though there are often major differences in the cost of living among the states and urban, suburban, and rural areas.[24]

How large an impact would adjusting for geographic differences make? Adjustment of the poverty thresholds for geographical differences in the cost of living has very little effect on the overall poverty rate, but significantly affects the poverty rate in some individual states. The official poverty thresholds are the same for every state in the Union, regardless of the cost of living. Charles Nelson of the Census Bureau has developed a procedure to make adjustments for geographical differences in the cost of living using data on fair market rents (FMRs) from the Department of Housing and Urban Development (HUD).[25] Although this procedure does not capture all of the components involved in the cost of living in a state, the cost of housing is

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[22]For poverty thresholds, see U. S. Census Bureau, “Table 1. Weighted Average Poverty Thresholds for Families of Specified Size: 1959 to 2005” (Washington, DC: U.S. Census Bureau, 2006), http://www.census.gov/hhes/www/poverty/histpov/hstpov1.html (accessed May 31, 2006); and for median income, see U.S. Census Bureau, “Table F-8. Size of Family, All Races, by Median and Mean Income: 1947 to 2005” (Washington, DC: U.S. Census Bureau, 2006), http://www.census.gov/hhes/www/income/histinc/f08ar.html (accessed May31, 2006).

[23]U.S. Census Bureau, “The Effect of Taxes and Transfers on Income and Poverty in the United States: 2005,” *Current Population Reports*, Series P60-232, http://www.census.gov/prod/2007pubs/p60-232.pdf (accessed July 31, 2007), p. 13.

[24]The poverty guidelines, however, provide higher thresholds for Alaska and Hawaii.

[25]Charles Nelson, “Geographic Adjustments in Poverty Thresholds,” paper prepared for the National Academy of Sciences Workshop on Experimental Poverty Measures, June 15–16, 2004, http://www7.nationalacademies.org/cnstat/Geographic_Adjustments.pdf (accessed July 30, 2007).

certainly a major—if not *the* major—component. For 2004, applying Nelson's geographical adjustments to the poverty thresholds would lower the overall poverty rate from 12.7 to 12.6 percent, an insignificant change. However, the poverty rate would be increased in relatively high-cost states such as California (from 13.2 to 17.8 percent) and New York (from 15.0 to 16.9 percent), and in the District of Columbia (from 17.0 to 25.2 percent). In contrast, the poverty rate would be decreased significantly in relatively low-cost states such as Mississippi (from 18.7 to 13.4 percent), Kentucky (from 17.8 to 12.4 percent), and West Virginia (from 14.2 to 10.3 percent).

Data problems and the realization that intra-area differences are larger than inter-area differences have discouraged analysts from pursuing this kind of differentiation. But the large potential impact on individuals and families of doing so reveals the often arbitrary and politicized nature of the current debate over poverty rates.

The official poverty measure does a poor job measuring *poverty alleviation efforts (ignoring, for example, the EITC and noncash benefits).* This is perhaps the measure's most damning flaw—because it ignores the important impact of many means-tested benefits on reducing material poverty. A study by the Center on Budget and Policy Priorities, for example, found that the Earned Income Tax Credit (EITC) has a significant effect in reducing poverty:

> Recent research also documents another powerful effect of the EITC: reducing poverty. Census data show that in 2003, the EITC lifted 4.4 million people out of poverty, including 2.4 million children. Without the EITC, the poverty rate among children would have been nearly one-fourth higher. [[26]] Census data show that the EITC lifts more children out of poverty than any other single program or category of programs.[27]

But while the current measure counts cash welfare payments, because they are cash, it does not count the EITC, because the EITC is formally part of the tax code and the official poverty measure is based on "pretax" income. The Earned Income Tax Credit (EITC), instituted in 1975, is a refundable tax credit for low-income, working individuals. In 2006, the maximum amount of the EITC that a family could receive was $4,536 (if the family had two or more

[26]Analysis of Current Population Survey data by the Center on Budget and Policy Priorities. In 2003, the EITC reduced the number of children in families with below-poverty disposable income from 12.6 million to 10.2 million and the number of Americans (all ages) in families with below-poverty disposable income from 35.3 million to 30.9 million, a decline of 4.4 million. This analysis uses a measure of poverty that counts food, housing, and energy assistance benefits as income and subtracts income and payroll taxes.

[27]Robert Greenstein, "The Earned Income Tax Credit: Boosting Income, Aiding the Working Poor" (Washington, DC: Center on Budget and Priorities, August 17, 2005), http://www.cbpp.org/7-19-05eic.htm (accessed May 19, 2006).

children) and $2,747 (if the family had one child).[28] A working family or individual with no child present was eligible for the EITC if earned income was less than $12,000 to $14,000 (depending on marital status), but the amount received was much smaller than for families with children (as much as $412).[29]

Counting the EITC would lower measured poverty by about 1.2 percentage points. But because the EITC goes mainly to families with children (lowering the poverty rate for children under the current measure from about 18.3 percent to about 15 percent), counting it would have almost no impact on other groups.[30]

The current measure also ignores the value of noncash welfare benefits such as food stamps, housing assistance, and free- or reduced-price school lunches—probably because they were quite limited in scope and size in the mid-1960s. But they have grown considerably since then. In 2006, food stamps provided the equivalent of as much as $5,716 for a four person

[28]U.S. Department of the Treasury, Internal Revenue Service, *Earned Income Credit (EIC): For Use in Preparing 2006 Returns*, http://www.irs.gov/pub/irs-pdf/p596.pdf (accessed July 31, 2007).

[29]Ibid.

[30]Counting the EITC would have no effect on the poverty rate for unrelated individuals (which remains at 20.4 percent) and a barely measurable effect for the elderly (from 10.4 percent to 10.3 percent). See U.S. Census Bureau, "Table 5: Percent of People in Poverty, by Definition of Income and Selected Characteristics: 2002 (Revised)," http://www.census.gov/hhes/www/poverty/poverty02/r&dtable5.html (accessed July 31, 2007).

family[31] (on average, about $2,600 per household or $1,100 per recipient),[32] and housing subsidies as much as $15,300[33] (on average, about $5,388 per household).[34]

Treating the benefits from these three means-tested, noncash programs as the equivalent of income (although their valuation can be problematic) would lower poverty by about 1.2 percentage points.

There are other noncash, means-tested benefits not in this calculation, including school breakfasts, WIC, and child care subsidies (as mentioned above). But the biggest exclusions are Medicaid for the poor, roughly $2,000 per person[35] (about $7,290 for a four-person family),[36]

[31]U.S. Department of Agriculture, Center for Nutrition Policy and Promotion, "Cost of Food at Home: U.S. Average at Four Cost Levels," http://www.cnpp.usda.gov/Publications/FoodPlans/CostofFoodMay06.pdf (accessed July 31, 2007).

[32]U.S. Department of Agriculture, Food and Nutrition Service, "Food Stamp Program: Average Monthly Benefit Per Person" (Washington, DC: FNS, 2007), http://www.fns.usda.gov/pd/18fsavgben.htm (accessed July 31, 2007). Author's calculations to annualize the amounts.

[33]Sharon Stern, "Housing Subsidies in a Measure of Poverty," paper prepared for the National Academy of Sciences Workshop on Experimental Poverty Measures, June 15–16, 2004, http://www7.nationalacademies.org/cnstat/Housing_Subsidies.pdf (accessed August 1, 2005), p. 11. The maximum monthly housing subsidy on the 1999 American Housing Survey data file is $1,275, or about $15,300 per year. This amount is largely in agreement with maximum amounts for housing subsidies reported at the state level. See Alan S. Oser, "Perspectives: State Housing Aid; In the Albany Crucible, New Subsidies for Shelter," *The New York Times*, December 1, 1985, http://query.nytimes.com/gst/fullpage.html?res=9B00EEDC1F38F932A35751C1A963948260&sec=&pagewanted=print (accessed June 7, 2006), stating: "The grants in the affordable-housing program can go as high as $15,000 a unit or 40 percent of the cost of a project, whichever is less."

[34]Vee Burke, "Cash and Noncash Benefits for Persons with Limited Income: Eligibility Rules, Recipient and Expenditure Data, FY2000–FY2002" (Washington, DC: Congressional Research Service, November 25, 2003), http://www.opencrs.com/rpts/RL32233_20031125.pdf (accessed June 6, 2006), p. 120.

[35]U.S. Congressional Budget Office, "Fact Sheet for CBO's March 2004 Baseline: Medicaid and the State Children's Health Insurance Program" (Washington, DC: CBO, 2004), http://www.cbo.gov/budget/factsheets/2004b/medicaid.pdf (accessed May 18, 2006).

[36]U.S. Department of Health and Human Services, "Table 95: Medicaid Payments per Person Served (Beneficiary), by Eligibility Group: Fiscal Years 1975-2002" (Washington, DC: HHS, 2004), http://www.cms.hhs.gov/MedicareMedicaidStatSupp/LT/itemdetail.asp?filterType=none&filterByDID=-99&sortByDID=1&sortOrder=ascending&itemID=CMS060377 (accessed June 7, 2006). The calculation of average Medicaid payments for a four-person family assumes the presence of two adults and two children, but no aged or disabled persons.

and Medicare for the aged and disabled, almost $5,500 per person.[37] Depending on how they are valued, including them would reduce measured poverty by about 0.5 percentage points to about 3.0 percentage points.[38] Ironically, the impact of this medical coverage on the poverty rate is so large that few analysts suggest counting it.

Implications

Taken together, the adjustments described above—except for raising the poverty thresholds to estimate a relative poverty measure—are in accord with the documented improvement in the standard of living of low-income families. As analysts as politically diverse as Christopher Jencks of Harvard University and Nicholas Eberstadt, my colleague at the American Enterprise Institute, have pointed out, the well-being of the poor, whether it be measured in health or material possessions, is palpably better than in the early 1970s—even though there is little sign of that improvement in the official poverty rate. After examining a wide range of data that included housing conditions, food spending, health indicators (including doctor visits), and access to telephones and motor vehicles, in addition to the data on poverty, Christopher Jencks, Susan Mayer, and Joseph Swingle concluded:

> Almost all our measures suggest that low-income children's living conditions improved fairly steadily between 1969 and 1999. The data on food expenditures are an exception, but their accuracy is suspect. . . . Our best poverty estimates suggest, for example, that the level of child poverty was roughly the same at the end of the 1980s as at the end of the 1960s. Yet our measures of living conditions almost all improved during this period.[39]

And Nicholas Eberstadt, drawing on statistical data from a wide range of government sources, found equally significant improvements over the past several decades for low-income people in

[37]Committee on Ways and Means, U.S. House of Representatives, *2004 Green Book: Background Material and Data on the Programs within the Jurisdiction of the Committee on Ways and Means*, WMCP: 108-6 (Washington, DC: U.S. Government Printing Office, March 2004), tables 2-1 and 2-2.

[38]For estimates of the fungible value of medical care, see U.S. Census Bureau, "Table 5: Percent of People in Poverty, by Definition of Income and Selected Characteristics: 2002 (Revised)," http://www.census.gov/hhes/www/poverty/poverty02/r&dtable5.html (accessed May 18, 2006); and for estimates of the market value of medical care, see U.S. Census Bureau, "Alternative Methods for Valuing Selected In-Kind Transfer Benefits and Measuring Their Effect on Poverty," *Technical Paper 50* (Washington, DC: U.S. Government Printing Office, 1982), p. 82.

[39]Christopher Jencks, Susan E. Mayer, and Joseph Swingle, "Can We Fix the Federal Poverty Measure So It Provides Reliable Information about Changes in Children's Living Conditions?" paper prepared for the University of Maryland/American Enterprise Institute seminar on "Reconsidering the Federal Poverty Measure," September 7, 2004, http://www.welfareacademy.org/pubs/poverty/povmeas_canwefix.pdf (accessed May 9, 2006).

their health status and access to medical care, ownership of vehicles and major consumer durables, and in the general condition of their housing.[40]

Poverty has not disappeared. Even taking the most aggressive approach to these new statistics, about 5 percent of Americans, or about 15 million people, are living below the poverty line, with millions more living just above it. And, as the post-Katrina images have reminded us, there are still large pockets of deep poverty and social deprivation.

But these new statistics do mean that over the past thirty-eight years, substantial progress has been made against poverty. Millions of people are living palpably better lives because of higher earnings or because of government assistance.

Both conservatives and liberals should welcome this news. Conservatives will prefer the earnings side of the story, of course, and will argue that economic expansion and responsible personal behavior are the best antipoverty programs. And liberals will like the government assistance story, and will argue that cutting benefits would increase poverty; in fact, they will probably argue that increasing benefits would further reduce "post-transfer" poverty.

The broader point, however, should not be lost. A combination of higher earnings and government assistance has reduced material deprivation over the past forty years. Certainly not as much as any of us would like, but this very good news should encourage those on both sides of the ideological divide who have been disheartened by the seeming intractability of poverty.

Obstacles to Reform

As shown above, the official poverty measure provides an imperfect picture of economic resources available to low-income Americans. If the flaws are so clear, why has it proven so difficult to reform the measure? I think that there are four main reasons:

- Correcting the technical flaws in the official poverty measure is *scientifically difficult and raises many legitimate conceptual disagreements*. Much of the Census Bureau data upon which a new measure would be based are obsolete and inaccurate, and even the infusion of substantial additional funds might not help. Moreover, there are broad disagreements about how to handle a myriad of issues, such as MOOP and transportation and child care expenses.

[40]Nicholas Eberstadt, "Indicators of Deprivation and Well-Being in Modern America: A Look Beyond the Poverty Rate," presentation at an American Enterprise Institute seminar on "Reconsidering the Federal Poverty Measure," May 16, 2005, http://www.welfareacademy.org/pubs/poverty/eberstadt.ppt#318,2,Outline of Presentation (accessed May 18, 2006).

- Correcting the technical flaws in the official poverty measure *would tend to lower poverty rates, and many think the current measure understates true poverty.* I think the others on this panel have expressed this issue as well as I can.

- Correcting the technical flaws in the official poverty measure—or raising poverty thresholds—*would wreack havoc with the eligibility rules of many means-tested programs (and many formulas for federal aid to the states).*

- Finally, the current measure does *a credible job making year-to-year comparisons in poverty rates—and the political system has adjusted to it by setting eligibility for many programs at multiples of the current thresholds.*

Multiple Definitions

Hence, I despair of achieving wide agreement about a reformed poverty measure and, in fact, have grown to believe that it would be much better to develop additional measures that broaden and enrich our understanding of contemporary poverty and the needs of the poor.

That's what is so important about recent Census Bureau efforts to develop additional definitions of income and therefore poverty: money income, market income, post-social insurance income, and disposable income.[41] The Census Bureau notes that, "These measures are presented to illustrate various dimensions of economic well-being and the impact of taxes and transfers."[42] A description of each of the definitions from the Census Bureau report is shown below:[43]

- **Money Income** includes all cash income received by individuals who are 15 years or older. It consists of income as reported, before deductions for taxes and other expenses. It does not include realized capital gains or lump-sum payments that may be disbursed from insurance companies, workers' compensation, or pension plans.

- **Market Income** includes money income as described above and deducts government cash transfers. Government cash transfers are social security; supplemental security income (SSI); public assistance (including Temporary Assistance for Needy Families [TANF]); unemployment compensation; workers' compensation; veterans' payments;

[41]U.S. Census Bureau, "The Effect of Taxes and Transfers on Income and Poverty in the United States: 2005," *Current Population Reports*, Series P60-232, http://www.census.gov/prod/2007pubs/p60-232.pdf (accessed July 30, 2007).

[42]Ibid., 1.

[43]Ibid., 2.

and survivor, pension, and disability benefits from certain sources.[44] This definition also includes imputed net realized capital gains and imputed rental income (also called return on home equity) and subtracts imputed work expenses excluding child care.[45]

- **Post-Social Insurance Income** includes money income, imputed net realized capital gains, and imputed rental income; subtracts imputed work expenses as in market income; and also deducts government means-tested cash transfers. These include SSI, public assistance, and government paid means-tested veterans' payments. Post-social insurance income differs from market income by adding non-means-tested government transfers, most notably social security.[46]

- **Disposable Income** includes money income, imputed net realized capital gains, and imputed rental income; and subtracts imputed work expenses. It also deducts federal payroll taxes, federal and state income taxes, and property taxes for owner-occupied homes.[47] The value of noncash transfers is added, including food stamps, public or subsidized housing, and free or reduced-price school lunches.[48]

(See table 1.)

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[44]Government paid survivor, pension, and disability benefits include those paid by workers' compensation, U.S. Railroad Retirement, Black Lung Benefits, and State Temporary Sickness.

[45]Capital gains and losses are imputed using a statistical match to the 2001 Statistics of Income public use file from the Internal Revenue Service as part of the CPS ASEC tax model. For modeled tax filers, the imputed amounts are added to money income and are included as taxable income. Imputed rental income reflects the income homeowners would receive if they rented out their home; this value is added to money income to put homeowners and renters on a more equal footing. The return on home equity imputed for the CPS ASEC is an approximation of this income flow computed by applying a rate of return to imputed home equity. The American Housing Survey (AHS) provides the home and land values and mortgage debt used to compute home equity. The current year's return on municipal bonds is used as the rate of return. The 2006 ASEC uses 2003 National AHS data. Previous years used home equity based on 1995 National AHS data. This modeling improvement was repeated for the 2005 ASEC to make valid year-to-year comparisons in Table A-1. Work expenses are imputed from the Survey of Income and Program Participation (SIPP) 2001 Panel. The Census Bureau is considering changes to its child-care expenses imputation procedures and is deferring their inclusion in the report until either the current method can be validated or an improved method can be found.

[46]Non-means-tested government transfers include unemployment compensation, workers' compensation, social security, and the survivor, pension, and disability benefits (described in footnote 18 in the Census Bureau report).

[47]Property taxes are imputed from the 2003 National AHS.

[48]The reported value of food stamps is used; the value of housing subsidies is modeled using the 1985 National AHS; and the value of school lunches is modeled using parameters from the Food and Nutrition Service of the U.S. Department of Agriculture.

A recent Census Bureau report shows the effect of these four different definitions on the poverty rate in 2005, as well as the effect of using poverty thresholds that are 15 percent higher than the official thresholds (discussed above).[49] Based on money income, which is the official definition, the poverty rate was 12.6 percent. The poverty rate was higher using market income (18.9 percent), about the same using post-social insurance income (12.7 percent), and lower using disposable income (10.3 percent). The Census Bureau also estimated the poverty rate using poverty thresholds that are 15 percent higher than the official thresholds, which are based on the roughly 15 percent increase in real median family income for four-person families from 1978 to 2005 using the CPI-U. The resulting poverty rates using these higher thresholds are as follows: money income (15.3 percent), market income (21.2 percent), post-social insurance income (15.1 percent), and disposable income (13.2 percent).[50]

I strongly support such efforts (although I disagree with some of the particulars) and I think your subcommittee is considering legislation along the same lines.

Thank you.

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[49]U.S. Census Bureau, "The Effect of Taxes and Transfers on Income and Poverty in the United States: 2005," *Current Population Reports*, Series P60-232, http://www.census.gov/prod/2007pubs/p60-232.pdf (accessed July 30, 2007).

[50]Ibid., 13.

Table 1. Census Bureau Definitions of Income.

Income Sources	**Money Income**	**Market Income**	**Post-Social Insurance Income**	**Disposable Income**
Market Cash Income				
Wages and salaries	✓	✓	✓	✓
Self-employment income	✓	✓	✓	✓
Property income[a]	✓	✓	✓	✓
Retirement pensions and annuities	✓	✓[b]	✓	✓
Survivor pensions and annuities	✓	✓[b]	✓	✓
Disability pensions and annuities	✓	✓[b]	✓	✓
Net realized capital gains		✓	✓	✓
Market Noncash Income				
Employer contributions for health insurance				
Employer contributions for pensions				
Net imputed rent for owner-occupied housing		✓	✓	✓
Contributions from Outside the Household				
Child Support	✓	✓	✓	✓
Alimony	✓	✓	✓	✓
Contributions from persons outside the household	✓	✓	✓	✓
Educational Assistance				
Educational assistance from government sources only	✓		✓	✓
Grants, scholarships, etc. from school only	✓	✓	✓	✓
Other Cash Income	✓	✓	✓	✓
Expenditures Deducted from Income				
Deduct MOOP				
Deduct work-related child care				
Deduct work-related transportation and other (excluding child care)		✓	✓	✓
Taxes				
Deduct federal income taxes				✓
Deduct state income taxes				✓

Table 1. Census Bureau Definitions of Income.

Income Sources	**Money Income**	**Market Income**	**Post-Social Insurance Income**	**Disposable Income**
Deduct federal payroll taxes				✓
Deduct property taxes				✓
Nonmeans-tested Government Cash Benefits				
Social security and railroad retirement	✓		✓	✓
Unemployment compensation	✓		✓	✓
Workers' compensation	✓		✓	✓
Veterans' payments (other than pensions)	✓		✓	✓
Means-tested Government Cash Benefits				
TANF/AFDC/ADC	✓			✓
Other cash public assistance	✓			✓
Supplemental security income	✓			✓
Veterans' means-tested pension	✓			✓
Earned income tax credit				✓
Means-tested Government Noncash Income				
Food stamps				✓
Public or subsidized housing				✓
Free or reduced price school lunches				✓
Free or reduced price school breakfasts				
WIC				
LI-HEAP				
Medical Benefits				
Medicare				
Medicaid				

Notes:
[a]Includes interest, dividends, rent, estates, trusts, royalties, etc.
[b]Excludes government retirement, survivor, and disability pensions and annuities.

Table 2

Possible Corrections to the Federal Poverty Measure

Official 2004 poverty rate = 12.7%

Adjusted 2004 poverty rate = 5.4%

	Impact of (√)	Estimated individual impact	Estimated cumulative impact
Poverty based on market income			
Subtract means-tested cash transfers	☑	0.8%	13.5%
(subtract TANF, SSI, and general assistance, but not Social Security)			
Correct inflation adjustment			
(1978 to 2004) retrospective application of CPI-U-RS	☑	-1.5%	12.0%
(1967 to 1977) retrospective application of CPI-U-XI	☑	-0.8%	11.2%
Chained CPI	☑	-0.4%	10.8%
Revise equivalence scales			
For families	☑	-0.1%	10.7%
For unrelated coresidents	☑	-0.5%	10.2%
For cohabitors income	☑	-0.5%	9.7%
Count capital gains (and losses)	☑	0.0%	9.7%
(capital losses limited to $3,000 per year)			
Count non-income producing assets			
Imputed return on home equity	☑	-1.0%	8.7%
Imputed return on other assets?	☑		8.7%
Subtract work-related expenses			
Child care	☑	0.6%	9.3%
Other work-related expenses	☑	0.9%	10.2%
Subtract medical out-of-pocket (MOOP) expenses	☑	1.2%	11.4%
(impact ranges from 0.2 to 0.8 percentage points)			
Correct for unreported income	☑	-1.6%	9.8%
(wages, salaries, Social Security, etc.)			

	Impact of (√)	Estimated individual impact	Estimated cumulative impact
The government's impact on poverty			
(The impact of taxes and means-tested benefits on poverty rates)			
Subtract federal and state income taxes, and Social Security payroll taxes			
Federal income taxes	☑	-0.2%	9.6%
State income taxes	☑	0.0%	9.6%
Social Security payroll taxes	☑	1.0%	10.6%
Property taxes	☑	0.6%	11.2%
Add EITC	☑	-1.2%	10.0%
Add means-tested cash transfers	☑	-0.8%	9.2%
(add TANF, SSI, and general assistance, but not Social Security)			
Add selected means-tested non-cash benefits	☑	-1.2%	8.0%
(add food stamps, public housing subsidies, and school lunches, and LI-HEAP)			
Add Medicare, Medicaid, and SCHIP benefits	☑	-1.1%	6.9%
(impact ranges from -0.5 to -3.0 percentage points)			
Improve imputation of welfare, food stamps, and SSI benefits	☑	-0.8%	6.1%
Adjustment for interaction effects	☑	-0.7%	5.4%
Increase the poverty thresholds by 15 percent	☑	2.7%	8.1%
(based on a 15 percent increase in real median income for four-person families between 1978 and 2005)			