UNIVERSITY OF MARYLAND

MEMORANDUM

March 14, 2005

To: Seminar Members, "Reconsidering the Federal Poverty Measure"

From: Douglas Besharov and Gordon Green

Subject: Summary of Session #5: The Poverty Thresholds: What Additional Forms of Income Can Be Counted Using the Current Thresholds? And, Under What Conditions Should the Thresholds Be Changed?

The fifth seminar on "Reconsidering the Federal Poverty Measure" was held at the American Enterprise Institute on January 11, 2005. The seminar focused on a presentation titled "Measuring Poverty: Income Thresholds and Resource Measures—An Outline for a Conversation," by Timothy Smeeding, Maxwell Professor of Public Policy at Syracuse University and director of the Luxembourg Income Study (LIS). Comments on Smeeding's presentation were provided by Patricia Ruggles, who is now chief economist and policy director for the Democratic Staff of the House Budget Committee. Her presentation was titled "Measuring Poverty: What Should be Counted Where?" A presentation on "Health Needs in the Poverty Thresholds" was given by Richard Bavier, a policy analyst at the Office of Management and Budget (OMB). Douglas Besharov introduced each of the speakers, whose presentations were followed by a question-and-answer session, and a general discussion session at the end.

Timothy Smeeding's First Presentation

Smeeding provided a short history of the development of the poverty thresholds over the past fifty years. During the 1950s, CEA economist Robert Lampman included information in the *Economic Report of the President* that showed the percentage of the population with less than $3,000 in annual income. In 1963, Mollie Orshansky at the Social Security Administration (SSA) improved the methodology used by Lampman and the Council of Economic Advisors (CEA) by including family size adjustments, and came up with the same percentage poor as did the CEA. She derived a poverty threshold that was $3,128, about half the median family income at the time. Shortly thereafter, the federal government adopted the Orshansky measure as the official poverty measure. Since that time, numerous analysts have reviewed the poverty measure and recommended changes. However, while times have changed significantly over the past fifty years, the official poverty thresholds and income measures have remained the same.

Smeeding examined the types of benefits that should be included in the definition of income used to determine poverty status without changing the current poverty thresholds. He concluded that direct taxes should be subtracted from income, and near cash income transfers that reflect goods in the current poverty threshold should be included (such as Food Stamps and public housing subsidies). Smeeding expressed conceptual support for including the Earned Income Tax Credit (EITC) in income for the purpose of measuring poverty, since it often amounts to $3,000–$4,000 per year and allows people to make large purchases. However, he expressed concern about various expenses associated with going to work, such as child care, and said that these should be accounted for when adding the EITC to income. Smeeding also questioned whether the EITC should be counted in the year in which it is earned or the year in which it is received. (Since the Census Bureau simulates the receipt and amount of the EITC, it is counted in the year that it is earned, which is the reference period for income.)

Smeeding discussed whether medical benefits and the imputed return on equity in owned homes should be included in income for the purpose of measuring poverty. In his Ph.D. dissertation, Smeeding was able to determine what people were actually spending on medical care, using data from the 1960–61 Consumer Expenditure Survey (CE). However, since the Medicaid and Medicare programs were enacted in 1965, the cost of medical care has increased dramatically. Smeeding concluded that the market value of medical subsidies is very large, but they are not fungible and should not be included in income for the purpose of measuring poverty. Concerning housing, Smeeding noted that Orshansky looked at actual expenses in the poverty measure, not flow values, so flow values are not imputed for any assets. He expressed concern about treating housing differently than other assets by imputing the return to equity for owner-occupied housing.

Turning to the poverty thresholds, Smeeding said that they should be modified to reflect changes in real living standards over the past fifty years, and the next fifty years as well. He argued in favor of recalibrating and updating the current poverty thresholds to reflect a relative measure rather than an absolute measure. Smeeding stated that there is no absolute poverty line, because it varies by where a person lives. He noted that the United Nations (UN) and the OECD use a relative poverty measure of half the median income in a country, but acknowledged that this may not tell the entire story when income is increasing rapidly. As an example, Gross Domestic Product (GDP) in Ireland increased very rapidly in recent years, which caused relative poverty to increase, while in reality, well-being had improved and absolute poverty had fallen. However, Smeeding argued that an accurate picture can be obtained by comparing current poverty estimates with those in previous years and applying appropriate price adjustments. He said that relative well-being in a society is an important concept to measure.

Smeeding said that there are several things to consider when changing the poverty thresholds and income measures. First, work-related costs need to be accounted for as well as benefits. Second, intra-household transfers and economies of scale are important, which relates to the question of whether households or families and unrelated individuals should be used as the measurement unit for determining poverty status. Third, the current equivalence scales used in the poverty thresholds need to be fixed, since they do not exhibit a defensible progression. Fourth, the poverty thresholds should be set using a more current market basket. Smeeding argued that the market basket should be reconsidered every decade and adjusted during the interim using the Consumer Price Index (CPI).

In conclusion, Smeeding encouraged participants at the workshop to consider two relative poverty measures. The two measures being half the median resources in the current year, and half the median resources ten to twenty years ago, priced to the current year. Smeeding noted that he is not wedded to any particular approach for measuring poverty, and is open to alternatives.

Group Discussion

Besharov opened the floor for questions and answers, and the discussion turned to housing. Besharov asked Smeeding if he was ambivalent about counting public housing benefits. Smeeding said that he is not ambivalent about counting public housing subsidies, which is the difference between what a unit rents for and what the tenant pays, but is ambivalent about counting the imputed return to owner-occupied housing. Dan Weinberg noted that Smeeding did not discuss geographical adjustment to the poverty thresholds, which is tied to the cost of housing. Smeeding acknowledged that geographical adjustments are very complex, and Weinberg suggested that one could price housing at the national level to avoid geographical differences. Smeeding noted that the quality of housing for the poor seems to be increasing, but so is the hardship of paying for housing.

Charles Murray turned the discussion to the EITC, and asked Smeeding why it should not be counted in income since it is cash. Smeeding said that there are large costs associated with going to work, such as transportation and child care, and that these costs need to be accounted for if the EITC is to be included in income. Murray asked if a “rough and ready” solution—such as deducting a set amount for work related expenses—would suffice, and Smeeding acknowledged that it may be possible to account for the fixed costs of going to work in an acceptable manner. It was suggested that perhaps the EITC could be reduced by a set amount, such as 10 percent. Becky Blank noted that the problem with this approach is how to handle the work expenses of people who do not get the EITC.

Robert Rector returned the discussion to housing issues. He noted that in some localities the value of Section 8 housing subsidies is over $10,000. Rector agreed that probably no one is getting the full $10,000 in utility from these subsidies, but the huge amount of money that Congress is spending on the program needs to be accounted for. Smeeding agreed that something needs to be done to count public housing. He noted that when he estimated the cash equivalent value of housing subsidies it was in the range of 80–85 percent, as opposed to Food Stamps which were nearly as good as cash. Smeeding also compared medical care with other noncash benefits and noted that the average uninsured person can get free medical care if needed, but medical care needs to be set off to the side when measuring poverty because of various complexities. He said that the costs and benefits of medical care subsidies are very large, but they do not compare very well with other subsidies because their cash equivalent value is very low and people have different medical needs.

Besharov returned the discussion to the imputed return on owner-occupied housing, and the methodology used to compute it. Weinberg noted that the Census Bureau applies the interest rate on high-grade municipal bonds to the equity in a home to calculate the imputed return. Smeeding said that this is one way of doing the calculation, but there are others as well. Kathleen Cooper expressed concern about the ability to distribute the estimates across geographical areas. Smeeding suggested that it may be possible to provide an estimate if geographical differences in the cost of housing can be obtained. He noted that consumption by the elderly is up considerably, mainly because of the value of their housing. People may be taking out home equity loans at relatively low interest rates and spending the money obtained from the loan, which is very different than what has happened in the past. Smeeding reiterated his concern about selecting just one asset (housing) to estimate the imputed return, and not others.

Patricia Ruggles's Presentation

Patricia Ruggles stated that her views about the poverty measure were not significantly different than Smeeding's, and that there are four major questions to consider. First, there is the question about resources versus the poverty thresholds: what assumptions underlie the current poverty measure? Second, should any changes be made to the resource measure without rethinking the poverty thresholds? Third, how should a decision be made on where to count specific needs and resources? And fourth, what other changes to the poverty measure are still needed?

Ruggles noted that, historically, the poverty measure has involved a comparison of cash resources against cash needs. On the resource side, several distortions have occurred over time. There has been a growth in the level of taxes paid by the poor (especially Social Security payroll taxes), a growth in the level of noncash benefits, and a growth in certain pre-consumption expenses. On the poverty threshold side, Ruggles noted that new technologies have been introduced—such as medical advances and new drugs—and standards of living have improved. She argued that if the poverty thresholds based on consumption patterns during the 1960s continue to be used, it implies that the poor should not have access to the same goods and services as everyone else. Ruggles said that it is impossible to have an absolute poverty measure over the long run, because it would not allow for changes in the standard of living and the introduction of new goods. She concluded that over time, income measures and the poverty thresholds have become inconsistent with reality, and this needs to be corrected.

Ruggles turned her attention to the issue of whether income measures should be changed if the poverty thresholds are not, and said that sometimes a partial solution is better than none, if underlying assumptions are not violated. Her view is that statistics that do not reflect reality should be changed. For example, a more accurate measure of cash resources could be introduced even while the thresholds are still under construction. However, she argued that items should not be included in resources that are inconsistent with the current poverty thresholds.

In terms of possible short-term adjustments, Ruggles said that income measures should be refined to reflect more accurately the actual net income available for consumption. She said that resource measures should adjust for taxes and the EITC, remove work expenses such as child care, and add noncash benefits that are largely fungible such as Food Stamps, perhaps with a small discount. Ruggles expressed more concern about including public housing subsidies than Smeeding, because the amount spent and the fungible value are often quite different. She felt that a better methodology is needed to estimate the fungible value of housing subsidies, and the estimated value of the subsidy should never be more than what the unit would rent for (the market value). She also argued that the equivalence scales implicit in the current poverty thresholds should be corrected because they include several eccentricities.

Ruggles said that, broadly speaking, all forms of cash and non-cash income should be included in resources and needs should be included in the poverty thresholds. However, many items can be accounted for either by subtracting them from income or adding them to needs—for example, taxes and medical care. Her rule of thumb is that if an item is fairly similar across all families of a given size and type, it should be included in needs; if there are huge variations within family size categories, the item should probably be included in resources. Ruggles pointed to medical care as an example, because there are huge differences in what people need and spend.

Ruggles believes that the poverty thresholds were not well-constructed to begin with, and need to be updated. For instance, the multiplier, which is based on the relationship of food needs to income, would now probably be in the range of seven or eight, as opposed to the multiplier of three that was derived when the thresholds were first developed. She argued that the poverty thresholds need to be rethought, and again pointed to medical care as an example. Medical care is difficult to measure in either needs or resources, but is becoming increasingly important as costs rise. She said that in the long run, changes in the goods and services that people consider necessary should be accounted for. As an example, Ruggles said that the poverty measure needs to be updated to reflect a new market basket, as is done with the CPI. As with the CPI, the old series can be run for a period of time, and when there are major changes, the effect can be shown retrospectively.

Ruggles said that relative poverty thresholds can be useful for cross-country comparisons and to consider how the poor are doing relative to others. However, relative thresholds are probably not the right approach for political purposes. She speculated that Congress is more interested in a measure that is tied to specific needs. Ruggles said that analysts need to work on the details of how to update the poverty thresholds. For example, she said that she would entertain the idea of counting household income rather than family income to determine poverty status.

In conclusion, Ruggles said that there are some changes to the poverty measure that can, and probably should, be made now, using the existing poverty thresholds. Specifically, income should be adjusted to include Food Stamps and the EITC and exclude taxes and work-related expenses such as child care. She said that a better valuation methodology is needed before housing subsidies are counted. Concerning the poverty thresholds themselves, Ruggles said that the equivalence scales implicit in the thresholds should be corrected. Moreover, efforts are still needed on the longer term goal of revising the poverty thresholds to take account of the technological and social changes that have occurred over the past forty years. Finally, Ruggles said that there is a need to develop an acceptable methodology for dealing with such change in the future.

Group Discussion

During the question-and-answer session that followed, Kathleen Cooper asked whether the CPI-U-RS should be used to adjust the poverty thresholds for price changes. Ruggles said that the first task is to think about what should be included in the market basket, and then how to update it. Smeeding noted that it is important to use a measure that adjusts for quality changes. Ruggles said that the goals should not be too demanding, to avoid a situation in which "the best becomes the enemy of the good." Smeeding noted that the CPI is also very important for making adjustments to Social Security payments. Cooper asked how much is known about the differences between the market basket that is suitable for the poor as opposed to all urban consumers. Ruggles replied that the consumption patterns are different, but they are also different than what the poor used to consume. David Johnson noted that there are a variety of issues to consider when updating for price changes, and that some people may be paying different prices than others.

Additional discussion continued about how the CPI is used to adjust the poverty thresholds over time. Robert Reischauer noted that the CPI measures the rate of change over time, and while the CPI may be capturing some of the changes, he was worried about its ability to capture sharp declines in relative prices. He noted that if improvements in medical care are accounted for, then the relative price of this component has declined over time. Ruggles said that the CPI does adjust for quality changes over time, and this needs to be thought of in the context of how the poverty thresholds are adjusted. Reischauer said that the difference between absolute and relative poverty has probably not been as big an issue in the past as it will be in the future, as the gap between the two concepts becomes more stark. Blank said that the poverty thresholds can only be adjusted with a CPI-type index. She thought that more goods should be included in the market basket, which would increase the ability to measure price changes over time. Blank said that a one-to-one movement of the thresholds with economic growth is not required, but perhaps instead some percentage of the amount. Smeeding noted that past research has examined changes in the poverty thresholds based on responses from the Gallup poll.

Robert Rector said that the original mistake analytically was to use the term poverty to describe the measure that the Census Bureau produces. He said that a larger problem now is that the concept is being applied to higher and higher standards. Rector noted that his paper at the Heritage Foundation on resources that the poor actually possess is one of its most popular papers. During the era when the measure was created, the word "poverty" was chosen so that the Administration could wage its "War on Poverty." But to most people, the word "poverty" connotes dire need, hunger, malnutrition, homelessness, and a lack of basic resources. Thus, Rector said that there is a huge disparity between what people think the word poverty means and the statistical concept that the government uses to measure it. He said that if the poverty threshold is raised to a higher level, its relationship to reality will become more tenuous and the concept may no longer be accepted. Rector said that the American public is not interested in a war on inequality, and relative poverty concepts are essentially inequality measures. He thought that there would be little public support for a measure in which the only way to reduce poverty is through income equalization.

Ruggles noted that she does not favor a relative poverty measure, but an absolute measure that changes if the market basket changes. Rector responded that this would be a hybrid of a relative and an absolute measure. Murray agreed that there needs to be some adjustment to the poverty measure over time, but questioned whether the original measure should be reconsidered to determine if roughly three times the cost of food is the appropriate measure. He agreed with Rector that a poverty measure should reflect dire need. He also asserted that, as technicians, we can make some tweaks to the original poverty measure without making it a relative measure. Murray added that if the poverty measure changes dramatically, it will be rejected out of hand.

Additional discussion followed about how the poverty measure should change over time. Ed Montgomery said that if a pure absolute measure of poverty was desired, it would start with the poor houses in England when an attempt was first made to estimate poverty. He said that the poverty measure should not be locked into what people consumed in the early 1960s, but that the market basket should change with public expectations because things have changed since the measure was first developed in the United States. Smeeding added that the main consideration was to have a poverty line that reflects policies directed towards helping poor people. Policy makers need to know if their policies have achieved the desired objectives, just as the Congress wants to know the effect that the EITC is having on people. Wade Horn noted that the concern historically was about poverty, not the poverty line, and expressed concern about adjusting the measure for rising expectations. For example, it is desirable to have computers in the home, but resources need to be conserved so they can be targeted most effectively. Horn expressed the concern that if the poverty measure goes overboard in adjusting for rising expectations, the public will not accept it.

The discussion turned to the distinction between presumed and actual child care expenses. Ruggles suggested that a value could be imputed for child care. Horn asked how free child care would be accounted for, and Ruggles responded that only paid child care would be counted. Besharov noted that if a mother paid the grandmother to provide child care, the money would be deducted from the mother's income and could cause her to move into poverty and become eligible to receive benefits. If the grandmother is providing free child care, then no money is deducted from the mother's income unless she is also paying someone else. Ruggles said that while programs have their own rules, and there are many inconsistencies between programs, under most the mother's eligibility would not be affected if she paid her mother for child care. Besharov noted that such an approach could impose a series of nuances on programs. Smeeding added that married-couple families may have more options for providing care to their children than single parents, but child care is a large area with big benefits and costs that requires more research.

A series of ideas were presented on how to actually count child care. Ruggles suggested the general principle that only things that go through the market should be counted, and the approach should not be changed for child care. Michael O'Grady suggested that, to move the discussion forward, the market value of child care could be estimated in terms of how much child care would be worth if people had to pay for it out of their own pockets. Ruggles said that a distinction needs to be made between when a person receives something tangible, such as Food Stamps, and when the entire transaction is nonmarket. O'Grady added that there should still be a market equivalent, but Ruggles said only if there is a counterfactual large enough to estimate it. O'Grady expressed concern that a distinction needs to be made between women who receive free child care and those who do not. Ruggles replied that a poverty measure should reflect whether people have enough money to scrape by, and while free care may help them, the measure needs to adhere to market situations.

O'Grady noted that actuaries can estimate what Medicaid and Medicare are worth, and if one person has health care while another does not, their circumstances are certainly different. Ruggles said that there is also the issue of whether the health care low-income people receive meets their needs, not just what it costs. Reischauer added that if all government workers were young, medical costs would fall. Medicaid is particularly difficult to value, because people can get it when they need it. O'Grady added that while the approaches for valuing medical care are not perfect, it is possible to go a long way toward estimating the value. Bringing the discussion back to child care, Weinberg said that to develop a good estimate of the net cost of child care for the purpose of a poverty measure, a different approach to survey measurement than what is now available might be needed.

Timothy Smeeding's Second Presentation

In the second part of his presentation, Smeeding examined how other countries approach the measurement of poverty. He noted that the idea of measuring poverty dates back to Rowntree in England in 1901. There is an Anglo-Saxon tradition of measuring poverty, which is also practiced in Canada and Australia, and these are the only individual countries that measure poverty. The European Union uses 60 percent of the median family income, adjusted for family size. The Organization for Economic Cooperation and Development (OECD) and the Luxembourg Income Study (LIS) use less than 50 percent of the median family income as a measure, while the poverty line in the United States is closer to 40 percent of the median family income. Smeeding mentioned that the LIS contains a wide variety of data for developed countries, and may move in the future to obtain more data for developing countries as well. Much of the data for developing countries comes from the World Bank, which uses an entirely different standard of $1.00–$2.00 per person a day.

Smeeding presented a chart that showed changes in the absolute poverty rate for children in the United Kingdom and the United States between 1989 and 2003. Between 1995 and 1999, the poverty rate for children went down in both countries. However, after 2000, the poverty rate for children declined in the United Kingdom, but not in the United States.

Group Discussion

The group discussion focused on how other countries measure poverty. Besharov wondered how other countries measure poverty, since few have actual poverty lines. Smeeding described how other countries take a relative poverty concept, usually set as a percent of incomes. Rector inquired whether other countries refer to their estimates as "poverty." Smeeding explained that countries did not previously describe their estimates as poverty, merely 60 percent of the median income, but much of the current terminology is being driven by the European Union. Smeeding noted that the United Kingdom had spent a substantial amount of money on children, and wanted to know if these efforts were making a difference. Besharov asked how much money per child it took to obtain the reduction in poverty in the United Kingdom. Smeeding replied that he did not know, but would find out. O'Grady noted that much of American thought is based on equality of opportunity, not equality of outcome. In contrast, the British are more interested in reducing inequality. O'Grady said that the poverty measure in the United States is a reflection of our political culture.

There was also discussion about what might have caused the difference in child poverty trends between the United States and United Kingdom presented by Smeeding. Reischauer speculated that most of the decline in child poverty rates from 1995–1999 was due to an improving economy in both countries. Smeeding agreed. Louis Kincannon noted that unemployment rates typically are much higher in European countries than in the United States, and their populations tend to be more stable as well. Don Winstead said that it is important to find out how much of the decline in child poverty rates in England was due to the economy and how much was due to policy, in order to guide future actions. O'Grady speculated that it would be very interesting to see what the trends look like five or ten years from now, as the populations of more European countries become diverse. He wondered whether they would be able to maintain their philosophy of equality of outcome. Horn noted that there is a backlash against immigration occurring throughout the European Union. The new emphasis is that every mother and father should be in the labor force in order to support welfare payments. In addition, the focus of the World Bank is on eliminating poverty around the world, so if needs are ratcheted up in the United States, it will be more difficult to help in meeting needs elsewhere. Rector said that some analysts equate hunger in the United States with hunger in other countries, but this is often an unreasonable approach because the latter is so much worse.

Discussion on Equivalence Scales

Ruggles noted that the current poverty thresholds developed by Mollie Orshansky incorporate food needs for different sizes of families, based on caloric needs. When the poverty line was made official in 1969, the relationship across different family types and sizes was frozen. She said that the current equivalence scale based on family types and sizes in 1969 bears little resemblance to reality today. The needs for married-couple and female-headed families were collapsed into one category in the thresholds, but this has only complicated the situation. Needs go up and down between different family sizes in a pattern that is often not realistic. Ruggles said that whatever is done to fix the equivalence scales in the poverty thresholds will be preferable to the way they are now constructed. She favors the three-parameter equivalence scale developed by David Betson of Notre Dame.

Besharov asked what would be the impact of changing the equivalence scales on different demographic groups. Ruggles noted that a change in the equivalence scale would raise the poverty rate for the elderly and lower the poverty rate for people in large families. The poverty thresholds now have a discount for the elderly, so one can move out of poverty by aging even if there is no change in income. Besharov asked if OMB had a position on a change in the equivalence scale, and Katherine Wallman said that OMB took no official position on this issue. Smeeding noted that virtually everyone who attended the National Academy of Sciences (NAS) poverty workshop in June 2004 thought that the current equivalence scales are wrong. Besharov asked if it is reasonable to go to Congress and say that a change is needed that will raise poverty rates for the elderly. Robert Greenstein asked what the net effect of changing the equivalence scale would be on the elderly, and Johnson replied that it would be small.

Reischauer suggested that since the poverty thresholds are arbitrary, changes should be made to the thresholds that do not have a large effect of the number of poor people. Blank stated that such changes could have a large effect on the distribution of the poor, and Besharov added that the changes could be particularly large in states such as California and Florida. He also stated that the internal distribution of the poor could be just as important politically as the overall poverty rate. O’Grady noted that the traditional Congressional response was to figure out what the estimate should be and then phase it in; there is precedent for compromise.

Richard Bavier’s Presentation

Bavier’s presentation dealt with the issue of valuing medical benefits and whether including medical out-of-pocket (MOOP) expenditures in the poverty thresholds would lead to more poverty misclassification than would including other needs. Bavier said that his views did not reflect the official position of the OMB. His conclusions were as follows: (1) A long debate over how to value public medical transfers (Medicare and Medicaid) in the measure of poverty seems to have reached the conclusion that we should just give up; (2) Although the National Research Council (NRC) asserted that retaining something for MOOP spending in the poverty thresholds would introduce too much error, this does not appear to be the case; and (3) If medical-out-of-pocket spending is retained in the poverty thresholds, equivalence scales should reflect variation in medical needs among different family types, which is very different from variation in food, clothing, and housing needs.

Bavier provided some background on the treatment of medical benefits in the measurement of poverty. In addition to other items, some amount for medical care is included implicitly in Orshansky's multiplier used to derive the poverty thresholds. A 1976 Federal Poverty Task Force report to Congress and initial Census Bureau experimental poverty reports used Smeeding's work, and noted that medical transfers credited as income to ill people would make them appear better off economically than healthy people. During the Census Bureau's 1985 Conference on the Measurement of Noncash Benefits, the balance of expert opinion seemed to be that the valuation of public and private health insurance to individuals was so difficult that it would be better not even to attempt it. In her 1990 book, *Drawing the Line*, Ruggles concluded that income counted in the measurement of poverty should include near-cash transfers such as Food Stamps, but not non-fungible benefits such as Medicare and Medicaid. This also was the conclusion reached by the NRC in its 1995 report, *Measuring Poverty, A New Approach*. In the 1995 NRC report, the variation in medical need itself was highlighted as a threshold issue separate from the resource issue of valuing medical transfers. For the first time, the NRC report raised variation in medical needs as a threshold issue, as opposed to an income issue. The report argued that because of the large variation in medical spending within family types, medical needs should not be included in their new poverty thresholds at all, and MOOP expenditures should be subtracted from a family's income that is compared against the new thresholds.

Using the Consumer Expenditure Survey (CE) and looking at shelter because it is the largest component in most families' budgets, Bavier set out to compare misclassification from including health needs to misclassification from including shelter needs. In his analysis, he assumed that families are no more likely to make discretionary purchases on shelter that leave insufficient resources for non-shelter needs than they are to make discretionary expenditures on MOOP that leave insufficient resources for non-medical needs. Based on this assumption, if a consumer unit changed poverty classification when MOOP or shelter costs were subtracted from both thresholds and expenditures, it was counted as a misclassification.

By comparing poverty rates when *family-type* amounts were included in the *thresholds* to rates when *family-specific* amounts were subtracted from *income*, Bavier found that including shelter needs in the poverty thresholds led to more *total* poverty misclassification (although less *net* poverty misclassification) than including MOOP. Subtracting MOOP from income leads to a comparatively older and whiter poverty population, while subtracting shelter from income increases the proportion of the poor who live by themselves. From this analysis, Bavier concluded that there does not seem to be strong empirical evidence for the NRC's position that MOOP needs vary by too much to include in the poverty thresholds. He also noted that if health spending is financed by dissaving or borrowing, then household spending on medical care does not reduce current income available for food, shelter, and clothing, as the NRC's method assumes. This suggests that poverty thresholds might reasonably include something for medical needs. Bavier also noted that including MOOP in new poverty thresholds also has implications for equivalence scales, since separate equivalence scales are usually used for MOOP and everything else (as the Census Bureau did in its experimental poverty report).

Group Discussion

The group subsequently discussed the implications of Bavier's findings. Ruggles challenged the assumption that people plan for their medical expenditures, and said that additional thought needs to be given to how debt interacts with poverty measurement. Rector asked Bavier to expand on his finding of a 6.7 percent poverty misclassification from MOOP for the aged, as shown in the table he presented at the seminar. Bavier replied that 37 percent of these cases had a head of household who was 75 years old or over. Ruggles noted that when people have large medical expenditures, they probably spend down their assets, which would also reduce their income. Rector asked that since this analysis was based on the CE, how does it relate to the fact that many low-income people in this survey spend more than their income? Bavier replied that it should have very little effect, and that is why he looked at expenditures rather than income.

There was additional discussion among the group about the difficulty of valuing medical transfers. Robert Greenstein noted that there are fundamental differences between medical care and housing. While people can do without housing insurance, it is more difficult for them to do without medical insurance. Greenstein expressed concern about calculating Medicaid premiums, because people who sign up for Medicaid are probably sicker than average. Low-income people may not sign up for Medicaid until they are sick. Greenstein said that if total Medicaid expenditures are divided by the number of people who are in the program, this probably does not equate to an accurate subsidy that could be added to income for the purpose of measuring poverty.

Greenstein also made some additional comments on the valuation of housing subsidies, which he said were prompted by Bavier's comments on medical care. He argued that not enough effort has been put into the valuation of housing subsidies across areas, which is important because of geographical differences in rent. Looking only at the amount that the government spends on housing creates distortions in the estimates. He concluded that medical benefits should not be included, and more work is needed before housing subsidies could be counted. Bavier suggested that the approach used for MOOP might be adequate for dealing with housing as well.

Concluding Remarks

O'Grady emphasized that while valuing medical care is a difficult proposition, the importance of medical subsidies should not be overlooked. He argued that a person who has Medicaid is substantially better off than a person who does not. Women and children on the program are not that expensive; most of the expense comes from the elderly and people who are in long term care. He said that the proper way to look at medical care was as a measure of need. If people did not have the benefit, what value would the market assign to it?

Cooper said that she heard much agreement on what needs to be done to improve the poverty measure. Cooper agreed with Reischauer that there are some technical fixes that need to be made to the poverty measure, but it is important to show some history so the changed measure that can be compared with the existing measure. Echoing Ruggles, she said it was important that the “best not become the enemy of the good” in the effort to fix the poverty measure. She expressed optimism that some significant changes in the poverty measure can be made, but said that they might have to be phased in. Cooper also said that she does not see why a changed poverty measure should necessarily yield the same numerical result as the existing measure. She commended all of the participants at the seminar for a very successful meeting.

Besharov agreed with the statements made by O’Grady and Cooper. He said that there also seems to be agreement that certain types of means-tested benefits can be included in income without changing the existing poverty thresholds, such as Food Stamps, the EITC, and public housing; however, there are some valuation issues associated with these benefits that need to be resolved. In addition, while relative poverty measures may be useful for cross-country comparisons, policy makers in the United States desire poverty measures that are tied to specific needs. He emphasized that there is a difference between obtaining a good statistical measure of poverty and using the measure to determine eligibility for government programs. If these two functions can be decoupled, it will be much easier to move forward. But it is still important to show the effect of government transfer programs. One way this might be accomplished is by showing poverty estimates according to pre-tax/pre-means-tested transfer income and post-tax/post-means-tested transfer income.