

CalWORKs Community Service

What Does It Mean for California?

Background

Community service employment is a key component of the CalWORKs program. CalWORKs recipients will start to transition into community service in 1999-00. Although counties are responsible for designing and implementing community service programs, the state is responsible for program costs.

LAO Findings

- ❖ Current law authorizes counties to adopt either the “workfare” (work-for-your-grant) or the wage-based (the recipient’s grant is converted into wages) approach to community service employment. The Governor’s budget, however, limits funding to the costs of the workfare approach.
- ❖ Although the wage-based approach to community service (as compared to workfare) increases the income of participants, its cost-effectiveness is unknown.
- ❖ Excluding the private for-profit sector from participating in community service employment significantly reduces the number of potential employers, thereby increasing the difficulty of finding high-quality community service work slots.

LAO Recommendations

- ❖ We present three options—county funding, state/county shared funding, and state funding—for budgeting the incremental costs of the wage-based approach to community service. Among these options, we prefer state funding.
- ❖ The cost-effectiveness of wage-based community service should be evaluated in comparison to workfare, by establishing a CalWORKs demonstration program.
- ❖ Counties should be authorized to include private for-profit organizations as community service employers, thereby increasing the number of higher-quality community service job slots.



COMMUNITY SERVICE JOBS IN THE CALWORKs PROGRAM

BACKGROUND

In response to federal welfare reform legislation, the Legislature created the California Work Opportunity and Responsibility to Kids (CalWORKs) program, enacted by Chapter 270, Statutes of 1997 (AB 1542, Ducheny, Ashburn, Thompson, and Maddy). Like its predecessor, Aid to Families with Dependent Children, the new program provides cash grants and welfare-to-work services to families whose incomes are not adequate to meet their basic needs. Under CalWORKs, able-bodied adult recipients (1) must meet participation mandates, (2) are limited to five years of cash assistance, and (3) must begin community service employment after no more than 24 months on aid. Welfare recipients receiving aid when CalWORKs was implemented will be reaching the community service employment requirement in 1999-00.

This report (1) describes how community service employment fits within the CalWORKs program, (2) summarizes recent research and evaluations of community service programs, (3) examines the costs of operating the wage-paying and workfare approaches to community service, and (4) highlights significant issues that the Legislature will face in implementing and budgeting the community service phase of the CalWORKs program.

WHAT IS COMMUNITY SERVICE EMPLOYMENT?

In the context of this report, community service is work performed by recipients of public assistance that otherwise would have gone undone by employees in the public, private, or private non-profit sector.

There are two broad approaches to community service: workfare and wage-based community service. Under workfare, recipients are required to participate in community service as a condition of receiving their public assistance grant. Under wage-based community service, the recipient's grant is used to fully or partially offset wages that are paid to the recipient.

Many counties provide workfare (that is, a requirement to work in a county-provided job in order to receive a grant) as part of their General Assistance (GA) programs. Contra Costa County, for example, requires employable recipients (who are not otherwise working) to work in county-provided jobs within a few months of application for aid. A wide variety of county jobs are provided, such as paper recycling, clerical work, and roadside litter removal, as well as jobs in nonprofit organizations such as certain hospitals in the county.

THE ROLE OF COMMUNITY SERVICE IN CALWORKS

Community service employment is a key component of the CalWORKs participation mandate. For most recipients, the requirement commences when they have been on aid for 18 months. In general, the CalWORKs program requires that a parent must either find nonsubsidized employment or participate in education/training activities for a specified number of hours per week. After 18 months, or at a county's option of 24 months, the parent must meet his or her participation mandate either through nonsubsidized employment, community service, or a combination of the two. The weekly required hours of participation are as follows: (1) single parents must participate in approved work activities or training for a minimum of 26 hours per week in 1998-99 and 32 hours per week after July 1, 1999 (there is a county option to increase the requirement to 32 hours in 1998-99) and (2) one parent in any two-parent family must participate for 35 hours per week.

In addition to the 18 to 24 month time limit on receiving job training/education services prior to commencing community service, Chapter 270 established a five-year lifetime limit for receipt of a full grant. After five years on aid, a family's grant is reduced by the portion attributable to the adult.

Chapter 270 specifies that community service will (1) be performed in the public or private nonprofit sector, (2) provide participants with jobs skills that lead to unsubsidized employment, and (3) not displace anyone from a job. Counties must

develop community service plans that identify (1) unmet community needs that could be met through community service activities; (2) entities responsible for community service job development, fiscal administration, and case management services; and (3) supportive efforts—including job search, education, and training—that will be provided to participants.

Under the provisions of the CalWORKs legislation, the monthly compensation for community service is limited to the amount of the recipient's grant. Within this constraint, however, counties can adopt a wage-paying type of program (similar to a nonsubsidized job) rather than the traditional workfare approach. Specifically, counties have the option of "diverting" a community service participant's grant to an employer, to be used to pay for the recipient's wages. The employer could be the county itself, another government agency, or a private nonprofit firm.

WHAT ARE CALIFORNIA COUNTIES PLANNING FOR COMMUNITY SERVICE?

Most counties are in the process of developing their community service plans. Thus, few plans have been finalized. To our knowledge, San Francisco County is the furthest along in the process. The county indicates that it will operate a two-year pilot program, beginning in January 1999, that will provide a sample of their caseload (200 recipients) with wage-paying community service jobs in the private nonprofit sector. In the San Francisco pilot, three intermediary contractors will develop jobs with private nonprofit agencies throughout the county. The county Private



Industry Council (PIC) will serve as the employer of record and will process the payroll. Recipients will have their grants diverted to the PIC and paid out to them at the minimum wage. In addition, recipients will be eligible for the federal earned income tax credit (EITC). Based on the results of the pilot, San Francisco will determine its community service approach for the entire caseload.

INCENTIVES FOR RECIPIENTS TO WORK

One of the goals of CalWORKs is to move recipients from welfare to work and self sufficiency. Community service employment aids in

the transition to work by giving participants experience in actual work. In order to create an incentive to work, CalWORKs recipients are allowed to keep a specified portion of their earnings without a reduction in their grant level. This feature, known as the “earned income disregard” enables working grant recipients to keep the first \$225 of their earnings plus 50 cents of each additional dollar earned. In order to maintain strong incentives to work, it is important that nonsubsidized employment provide recipients more income support than community service employment (which is subsidized by the recipient’s grant).

WHAT DOES THE RESEARCH SAY ABOUT COMMUNITY SERVICE EMPLOYMENT PROGRAMS?

PAST PROGRAMS

Research on workfare programs for welfare recipients in the 1980s (in which recipients worked for their grants) did not find consistent positive effects on employment, earnings, or receipt of public assistance. The researchers indicated, however, that programs offered on a larger scale and with broader participation mandates could prove to be effective. We also note that better outcomes might be achieved if such programs were operated in the context of a time-limited aid environment, where the incentive to get a nonsubsidized job would be greater. Moreover, the research indicated that by assuming some public value from the output of the work,

the benefits exceeded the costs, from the perspective of the taxpayer.

MORE RECENT COMMUNITY SERVICE INITIATIVES

During the 1990s, many states and communities have incorporated community service employment into their welfare reform programs. Although some of these welfare programs have been evaluated, we are not aware of any evaluations that isolated the impact of different approaches to community service employment. Nevertheless, there are some preliminary findings on community service programs that—while not conclusive—are promising.

Vermont's Welfare Restructuring Project (WRP). The WRP approach to community service is similar to California in that single parents must commence community service after 30 months on aid (two-parent families after 15 months). In WRP, the community service job is wage-based rather than workfare. Preliminary results indicate that WRP has had a positive (though modest) impact on increasing earnings and reducing welfare receipt in comparison to a control group that was not subject to the community service work requirement.

New Hope Project. Located in Milwaukee, Wisconsin, the New Hope Project provides welfare recipients unable to find unsubsidized employment with a community service job paid at the minimum wage, as well as other support services and case management. Most of the positions are with nonprofit agencies, with the local PIC serving as the employer of record. Preliminary results (with a small sample) indicate that 43 percent of participants successfully used the community service position as a bridge from unemployment or unsteady employment to unsubsidized employment.

WHAT ARE THE BENEFITS OF THE WAGE-BASED COMMUNITY SERVICE APPROACH?

ADVANTAGES FROM THE RECIPIENT'S PERSPECTIVE

The primary advantage of wage-based community service is that it results in more income for participating families. There are two sources of additional income: the EITC and Food Stamps. First, by being paid a wage, rather than receiving a grant, participants are eligible for the EITC. For workers earning less than \$8,900 per year (\$741 per month), the EITC is equal to 40 percent of each dollar earned. (Once earned income reaches \$8,900, the credit is maximized and is then gradually phased-out as earned income exceeds \$11,600.) A participant earning \$624 per month (the maximum grant for a family of three) in a wage-based community service job would receive an EITC of about \$250 per month, or about \$3,000 per year.

A second benefit of the wage-based approach is that it results in additional Food Stamps because of the use of an earned income disregard. A participant earning \$624 per month is entitled to a maximum of \$302 in monthly Food Stamps, whereas a recipient of a \$624 grant receives a maximum of \$249 in Food Stamps. Thus, for a family of three, wage-based community service increases Food Stamp benefits by up to \$53 per month, or just over \$600 per year.

Figure 1 (see page 6) compares the income received by a three-person family engaged in either wage-based community service or workfare. As the figure shows, the family in wage-based community service has \$255 more per month in disposable income and Food Stamps. The figure also shows that the family in wage-based



Figure 1

**Comparison of Net Monthly Income
Wage-Based and Workfare Approaches**

1999-00

Family of Three (High-Cost County)

	Workfare	Wage-Based	Difference
Grant Income	\$624	— ^a	-\$624
Earned Income	—	\$624	624
Food Stamps	249	302	53
Earned Income Tax Credit	—	250	250
FICA Taxes	—	-48	-48
Net Monthly Income	\$873	\$1,128	\$255
Federal Poverty Guideline	\$1,138	\$1,138	
Percent of Poverty Guideline	77%	99%	

^a Assumes no earned income disregard, per LAO recommendation.

recipients to report to prospective employers that they have received wages rather than welfare grants. Receiving a paycheck rather than a grant may also increase recipients' self esteem and confidence in seeking a job in the labor market. Taken together, these factors could increase the chances that recipients will obtain nonsubsidized employment.

**ADVANTAGES FROM
THE GOVERNMENT'S PERSPECTIVE**

One benefit to government from the wage-based approach is the increase in sales tax revenues associated with expenditure of EITC funds by recipients within California. A second potential—and possibly more significant—advantage is the savings from reduced welfare payments that will result if wage-based community service is more effective than workfare in assisting clients to obtain nonsubsidized jobs. Both of these advantages are discussed later in this report.

community service is slightly below the federal poverty guideline, whereas the family in workfare is well below (77 percent of poverty level) the guideline. (We note that this example assumes no earned income disregard for the wage-based community service participant, which we discuss later in this report.)

Another potential benefit of the wage-based approach stems from the fact that it more closely resembles nonsubsidized employment. As such, it generates a more formal work history, allowing

WHAT IS THE COST OF A COMMUNITY SERVICE EMPLOYMENT PROGRAM?

The cost of a community service employment program depends on many factors, including (1) the number of recipients who need community service jobs, (2) what types of services are offered to participants, and (3) whether the positions will be wage-paying or workfare. Another issue in budgeting for community service is identifying which entities will pay for various cost components. In most instances, employers (private non-profit organizations and public agencies) will be receiving “free” labor with respect to employee compensation. There are, however, related costs that an employer or county welfare department might incur in connection with community service jobs.

COMMUNITY SERVICE CASELOAD

Estimating the number of community service slots that will have to be created is difficult due to uncertainty concerning (1) the pace at which recipients have been phased into the CalWORKs program since the enactment of Chapter 270, (2) whether counties will elect to extend the 18 month time limit for welfare-to-work services to 24 months, and (3) the extent to which welfare-to-work services and the imposition of community service requirements will result in increased unsubsidized employment among CalWORKs recipients, thereby reducing the need for community service slots.

CalWORKs Phase-In. Certain components of the CalWORKs program—including the five-year lifetime limit for cash assistance for able-bodied

adults—began in January 1998. Other provisions, such as the participation mandate and the 18 to 24 month time limit for welfare-to-work services prior to community service, begin when the client signs a welfare-to-work agreement. Counties were required to implement the participation mandates for CalWORKs *applicants* no later than April 1998, though some counties started as early as January 1998. Counties are required to phase-in *existing* recipients no later than January 1999. (Los Angeles County, with approximately 30 percent of the caseload, did not implement CalWORKs until April 1998.)

Community Service Job Phase-In. Based on these time lines, CalWORKs recipients may begin to transition into community service as early as July 1999 (18 months from January 1998) and as late as January 2001 (two years from January 1999).

After making certain assumptions regarding the phase-in, the Governor's budget for 1999-00 estimates that approximately 15,000 recipients will enter community service employment in January 2000, increasing to about 110,000 recipients by June 2000. The average monthly caseload for this six-month period is estimated to be about 61,000. These estimates assume that all counties extend the 18-month time limit to 24 months, and that all CalWORKs recipients that were on aid as of December 1997 had signed their welfare-to-work agreements by January 1, 1999.



We generally agree that most, if not all, counties will extend the time limit to 24 months, but we believe the caseload projection is too high because it does not reflect any noncompliance by the recipients nor delays in signing welfare-to-work agreements. Accordingly, we would reduce the administration's estimate by about one-third—to 40,000 average monthly cases.

COMMUNITY SERVICE COST COMPONENTS

Figure 2 identifies the major cost components for both workfare and wage-based community service. Because the purpose of the figure is to identify the "marginal" cost of providing community service, it does not include support costs (such as transportation and child care) or the cost of the grant (or wage) because these costs will be incurred by the county welfare department regard-

less of whether the recipient is in education/training (the first 18 months on aid) or in community service. Figure 2 also notes whether the costs would be required or optional (that is, at county discretion).

Common Costs. As noted in Figure 2, the cost of developing or creating a community service work slot is common to both the wage-paying and workfare approaches. Similarly, under either approach there will be a cost for providing supervision, although it is usually absorbed by the employer. An optional cost for both types of programs is for support services such as job coaching. Both the New Hope Project and the San Francisco pilot project include case management and job coaching. Although many observers believe that these types of support services may be essential to assist community service recipients in obtaining financial

independence, we are not aware of any evaluation that confirms this supposition.

Cost Differences. The costs for documenting or monitoring the number of hours worked, and for making the wage payments, would be handled differently under workfare and wage-based community service. Under workfare, time sheets would be forwarded to the county welfare department, which in turn would calculate the grant based on the

Figure 2

Community Service Cost Components

Cost Component	Workfare	Wage-Paying
Job development (creating the position)	Required	Required
Employee on-the-job supervision	Usually absorbed by employer	Usually absorbed by employer
Case management/job coaching	Optional	Optional
Hourly attendance monitoring	Required	(Part of payroll)
Payroll accounting	None	Required
Insurance-related costs (FICA, workers' compensation)	None	Required
Employee FICA reimbursement/expense allowance	None	Optional

number of hours worked. Specifically, if a client worked less than the required hours, the county would notify the client that his/her grant was to be reduced by the portion for the adult, until the client comes into compliance. Under wage-based community service, wage payment would be handled by the employer through a payroll accounting system.

A major difference between workfare and wage-based community service is employer costs for Federal Insurance Contribution Act (FICA) taxes that are paid to support the social security system, workers' compensation insurance, and possibly unemployment insurance. In most wage-based community service programs, these costs have been picked up by the government agency administering the program as an incentive for the employer to participate in the program. Typically, there are no such costs in workfare programs.

Another potential cost difference is that in a wage-based system, recipients might be provided a supplemental grant payment or expense allowance. Many programs recognize that recipients in wage-based programs must pay employee FICA taxes of 7.65 percent. In order for the recipients' take-home wages to remain at least equal to the grant to which they otherwise would be entitled, these programs either reimburse the FICA tax or provide a supplemental grant through an expense

allowance or an income disregard in calculating the grant. In Vermont, the supplemental payment is set at \$90 per month; it is intended to cover employee FICA taxes and other work expenses such as transportation. The State of Washington has a similar approach.

Vermont officials estimate that the incremental cost of operating a wage-based community service job slot compared to workfare is about \$170 per month. This amount includes the \$90 supplemental payment discussed above. If this payment were eliminated, the marginal cost of adopting a wage-based approach would be \$80 per month. Most of this \$80 monthly cost is for the employer share of FICA (7.65 percent of wages), workers' compensation, and payroll accounting.

GOVERNOR'S BUDGET ESTIMATE FOR COMMUNITY SERVICE

The Governor's budget for 1999-00 is based on the workfare approach to community service. The budget proposal for community service employment is about \$20 million. The cost for community service is based on an assumption of one hour of case management per month, with half of this time dedicated to creating the job slot. The budget assumes that employers will absorb all supervisory costs. Child care and transportation costs are included for all CalWORKs recipients who need them, including community service participants.



ISSUES FOR LEGISLATIVE CONSIDERATION

Implementation of community service within the CalWORKs program raises substantive policy issues as well as technical issues. Below we discuss six issues with particularly significant policy or fiscal implications.

EFFECT OF THE FAIR LABOR STANDARDS ACT ON CALWORKS

If the Fair Labor Standards Act (FLSA) applies to community service employment, the CalWORKs weekly work requirement could be significantly reduced in the absence of program changes. We review the policy implications of applying the FLSA and present alternatives for the Legislature.

Department of Labor

Guidance. In May 1997, the U.S. Department of Labor (DOL) issued a “guide” stating that federal employment laws—such as the FLSA, the Occupational Safety and Health Act (OSHA), Unemployment Insurance (UI), and antidiscrimination laws—apply to welfare recipients. Specifically, with respect to the FLSA, the DOL guide states that if welfare recipients are considered “employees,” they must be compensated at the applicable minimum wage.

Impact on Participation Requirement. If the FLSA applies to the community service jobs in CalWORKs, it could have a significant effect on the weekly participation requirement for participants. Figure 3 shows the maximum grant for various family sizes and the *maximum* number of hours per week that recipients could be required to work if they were compensated at the minimum wage, *using the grant as the total monthly wage*. (We note that these maximums will be applicable under the wage-paying approach to community service as well as the workfare approach, because the CalWORKs legislation limits total monthly compensation to the amount of the family’s grant.)

Figure 3

Effect of Fair Labor Standard Act on Community Service Work Hours

Region/Family Size	Maximum Grant	Maximum Hours Under FLSA ^a	Difference ^b
High-Cost Counties			
2 Persons	\$504	20	12
3 Persons	624	25	7
4 Persons	744	29	3
5 Persons	847	34	—
Low-Cost Counties			
2 Persons	\$479	19	14
3 Persons	595	23	9
4 Persons	708	28	5
5 Persons	806	32	—

^a Assumes minimum wage. Maximum hours determined by dividing monthly grant by the minimum wage (\$5.75 per hour) and the weeks per month.

^b Difference from CalWORKs 32-hour requirement

As indicated in Figure 3, if the FLSA is applicable, only families with five or more persons in high-cost counties (those with relatively high monthly grants) could be required to work in community service for the 32 hours required by the CalWORKs legislation. A single parent with one child—a large part of the CalWORKs caseload—could only be required to complete 18 or 19 hours of community service each week, or 13 to 14 hours below the state statutory level.

Under current law for the CalWORKs program, the balance between the hours worked in community service (as limited by the FLSA) and the 32-hour participation mandate would need to be backfilled with other activities such as education, training, or job search. Thus, while all recipients would have to participate for the same number of hours, the type of participation would depend largely on family size, and for most recipients would vary significantly from the Legislature's apparent intent with respect to community service employment.

Department of Social Services (DSS) Interpretation. As noted above, the DOL has indicated that the FLSA applies to welfare recipients if they are considered employees. The DOL defines employees very broadly but does make an exception for "trainees." Whether a community service participant is an employee or a trainee depends on "an assessment of the economic realities of the relationship between the worker and the putative employer."

The DSS concluded in the spring of 1998 that recipients engaged in CalWORKs community

service employment are trainees rather than employees and, therefore, are not subject to the FLSA. The DSS further states that, based on this finding, no case-by-case assessment of the "economic realities" of the specific community service position is necessary.

We question, however, whether DSS's interpretation is consistent with the DOL guidance, which lays out several criteria for determining whether a worker is a trainee or an employee. Specifically, in order for a position to be classified as training rather than employment, DOL specifies that (1) the training must be similar to that given in a vocational school and (2) employers derive no immediate advantage from the trainee's activities. We believe that most community service jobs developed by counties will require the participants to work on activities that benefit the employer. In many cases, community service participants may work side by side with regular employees. Typical community service employment situations are unlikely to resemble vocational education. Therefore, we believe that most CalWORKs recipients participating in community service will be employees, rather than trainees, and therefore would be subject to the FLSA, based on the DOL guide.

We asked the DOL if, for example, (1) filing and clerical activities at a county welfare department, (2) cleaning up a public park, and (3) assisting a nonprofit organization by serving side-by-side with its employees would be considered "training" or "employment." The DOL indicated that these activities would be considered employment.



Options for the Legislature. If the FLSA is applicable, the Legislature has four options with respect to maintaining or modifying the 32-hour participation mandate for community service:

- ◆ **Option One.** Retain current law, whereby counties would fill the difference between 32 hours per week and the maximum community service hours with other activities such as training or job search.
- ◆ **Option Two.** Increase the amount of the monthly grant for those participating in wage-based community service so that total wages would be sufficient to pay for 32 hours of participation. This approach, however, would result in significant additional grant costs to the state and counties and could reduce the incentive for individuals to find unsubsidized jobs.
- ◆ **Option Three.** Reduce the weekly participation requirement while recipients are in community service—for example, to 20 hours per week. This would eliminate most of the differential effects related to family size. This approach would

also result in significant state savings because counties would not have to provide backfill activities to complete the 32-hour requirement.

- ◆ **Option Four.** Combine Food Stamp benefits with the grant in determining the total compensation for the community service participant for purposes of FLSA compliance. Figure 4 shows that if the value of Food Stamp coupons is added to the grant, families with three or more persons could meet the 32 hours in the community service requirement. In order to count Food Stamp benefits as part of community service compensation, however, the state would have to align the Food Stamp program work requirements

Figure 4

**Effect of Adding Food Stamps to Grant
On Maximum Participation Hours**

Region/Family Size	Maximum Grant and Food Stamps	Maximum Hours at Minimum Wage ^a
High-Cost Counties		
2 Persons	\$706	28
3 Persons	873	35
4 Persons	1,029	41
5 Persons	1,163	46
Low-Cost Counties		
2 Persons	\$688	27
3 Persons	857	34
4 Persons	1,009	40
5 Persons	1,141	45

^a For families where the maximum exceeds 32 hours, participation would be limited to 32 hours pursuant to the CalWORKs legislation.

with the CalWORKs program and would need to obtain approval from the U.S. Department of Agriculture. Making these program changes would probably result in slightly higher costs for county administration. This approach would also result in lower Food Stamp benefits for CalWORKs recipients who are not cooperating with the participation mandate. This is because under current law, noncooperation results in removal of the adult portion of the grant, but does not result in reduced Food Stamp benefits.

Analyst's Recommendation. Of the four options listed above, we prefer option three (reducing the weekly participation requirement during the community service phase to 20 hours per week) or option four (combining Food Stamp benefits with the grant in determining total compensation for the community service participant for purposes of FLSA compliance) because we believe that these options are more likely to be cost-effective.

We support option three because it avoids the cost of providing backfill employment preparation activities (and the associated costs for support services like child care) that may not be cost-effective. We note that in our January 1998 report, *CalWORKs Welfare Reform: Major Provisions and Issues*, we recommend studying the cost-effectiveness of reducing the required hours of participation to 20 hours per week for families with children under age six. Under federal law, families with children over age six must participate

for at least 30 hours per week in order for the state to count them toward meeting the federal work participation rates. Thus, option three will make it slightly more difficult for California to achieve the work participation rates prescribed in federal law. We believe, however, that California would meet the overall participation requirement in 1999-00, even with this change.

As an alternative, we support option four because it maintains the participation mandate with no additional state costs for separate backfill activities.

MODIFY EARNED INCOME DISREGARD FOR COMMUNITY SERVICE

Under current law, CalWORKs recipients participating in wage-based community service (whereby their grant is diverted to an employer and paid to them as wages) would be entitled to the same earned income disregard available to recipients who obtain nonsubsidized jobs. Thus, they would receive their base grant paid out as wages plus a supplemental grant. Because the higher level of income will reduce the incentive to find nonsubsidized employment and substantially increase program costs, we recommend enactment of legislation to do one of the following: (1) eliminate the disregard for wage-based community service participants or (2) reduce the disregard down to an amount sufficient to reimburse recipients for the cost of employee FICA taxes.

CalWORKs recipients who obtain nonsubsidized employment are entitled to the \$225 and 50 percent earned income disregard. Under this system,



the first \$225 of earnings, plus 50 percent of each additional dollar of earnings, are disregarded (not counted as income) in determining the family's grant. Thus, a recipient from a three-person family who had earnings of \$611 per month—which is equal to the maximum grant—would still be entitled to a grant of \$418 per month. This structure is designed to encourage recipients to obtain nonsubsidized employment.

As noted previously in this report, current law permits counties to use “grant diversion” to provide wage-paying community service jobs rather than the work-for-your-grant workfare approach. Under grant diversion, a recipient's grant is diverted to an employer and paid out in wages. Based on our interpretation of current law, a CalWORKs community service participant who is receiving wages that are funded through grant diversion would be entitled to the same earned income disregard that is available to a recipient in a nonsubsidized job—the \$225 and 50 percent earned income disregard. Thus, a recipient from a three-person family who was receiving a grant of \$611 for her first 18 months on aid and who then commenced a wage-paying community service program, would have her monthly cash income increase to \$1,029 (wages of \$611 plus a grant of \$418)—the same as if the recipient were in a nonsubsidized job. We believe that this would substantially reduce the incentive to find nonsubsidized employment. Accordingly, we recommend that the Legislature eliminate or reduce the earned income disregard for community service participants whose grants are diverted and

paid to them in the form of wages. Adoption of this recommendation would increase the incentive for recipients to obtain nonsubsidized employment.

One approach would be to simply eliminate the earned income disregard for recipients that are participating in wage-based community service funded through grant diversion, as is the case for the workfare system. Under this approach, the wage-based community service participant's take-home pay would be less than the grant that he or she formerly received (because the employee must pay FICA taxes). However, if the EITC is taken into consideration, then the participant's total income would be greater than the grant that he or she received prior to entering wage-based community service.

An alternative approach would be to reduce the disregard. The Vermont program recognizes that recipients in wage-based community service must pay FICA taxes of 7.65 percent and face other work expenses such as transportation. As noted previously, Vermont set its disregard at \$90 for all families for the purpose of covering these costs. In Washington State, the disregard for participants in wage-based community service has been set at 20 percent of gross wages. This approach, however, increases program costs and may reduce the incentive to find nonsubsidized employment.

Analyst's Recommendation. In order to maintain the incentive to obtain nonsubsidized jobs, we recommend that the Legislature either eliminate the income disregard for community service participants whose wages are funded through grant

diversion, or reduce it to an amount sufficient to cover employee costs for FICA taxes (about \$50 per month for a family of three). We do not find a compelling need to use the disregard to cover other work expenses such as transportation because these costs are reimbursed under current law.

OPTIONS FOR BUDGETING COMMUNITY SERVICE EMPLOYMENT

The Governor's budget for 1999-00 assumes the workfare approach to community service, with no funding for the incremental cost of the wage-based approach. We present two alternative approaches to budgeting these incremental costs.

Under current law, the state pays for all CalWORKs employment service costs above the 1996-97 level. The Legislature, however, has not established a budgeting approach for community service.

The decision to provide either wage-based community service or workfare is made by the counties. The 1999-00 Governor's Budget, however, assumes the workfare approach to community service employment, with the state/federal block grant funding 100 percent of the associated costs and the counties having no share of costs. On the other hand, the budget provides no state/federal block grant funds to cover the incremental cost of the wage-based approach to community service for counties that choose this option. As a result, incremental costs would be borne exclusively by the counties. Below, we describe three approaches (including the Governor's budget) that

the Legislature could follow in budgeting the incremental cost of wage-based community service.

- ◆ **Local Funding (Governor's Budget).** The incremental cost of wage-based community service could be viewed as a program "enhancement," which counties could elect to fund with (1) the CalWORKs performance incentive payments that the counties receive from the state, (2) a redirection of resources from within the CalWORKs county block grant allocation, or (3) other local funds such as Welfare-to-Work grants allocated to PICs. We note that the Governor's budget includes about \$500 million in performance incentives in both 1998-99 and 1999-00 that the counties must expend within the CalWORKs program.
- ◆ **State Funding: Include the Incremental Cost in County Block Grants.** The incremental cost of wage-based community service could be viewed as a base program cost for CalWORKs employment services and incorporated into the funding model for the program. Under this approach, the incremental costs would be budgeted as part of the single allocation of state/federal block grant funds to counties for employment services. The total amount available would be based on an estimate of the caseload in counties that choose the wage-based option. This would help to ensure that the counties have sufficient funds to pay for wage-based



community service, but it would result in General Fund costs of up to \$20 million in 1999-00 (if all counties were to choose this approach).

- ◆ **Matching Program.** Another approach would be a middle ground, whereby the incremental costs are viewed as a program enhancement, but one that potentially promises sufficient benefits to warrant 50 percent state participation. Under this approach, the state would match dollar-for-dollar any investment by the counties in wage-based community service. To control costs, total available matching funds could be budgeted as a separate allocation and capped by the budget act appropriation. Individual county match limits, moreover, could be established whereby the total amount of matching funds a county may draw down is limited to a fixed percentage of its community service caseload.

Conclusion. Although all of the approaches to budgeting the incremental costs of wage-based community service discussed above have merit, we prefer option two—state/federal block grant funding of the incremental costs. The wage-based approach is specifically authorized by current law, provides substantial benefits to the recipient in the form of the EITC, and may provide a better bridge to unsubsidized employment and self-sufficiency. Accordingly, we believe it should be considered a base program cost and be fully funded in the budget for any county that elects this option.

ADDITIONAL SPENDING MAY BE SOURCE OF REQUIRED FEDERAL MATCH

To the extent the Legislature augments the Governor's budget to fund all or part of the incremental cost of the wage-based approach to community service employment, such additional spending would count toward the required state match for the federal Welfare-to-Work funds.

Under the federal Welfare-to-Work block grant program, California is to receive approximately \$363 million in federal block grant funds from the DOL. Because the federal matching ratio for this program is 2 to 1, California must expend \$181.7 million in state matching funds by September 2001. The state match must be over and above the CalWORKs maintenance-of-effort (MOE) requirement. For 1999-00, the Governor's budget proposal for CalWORKs is at the MOE floor, plus an additional \$25 million from the General Fund for part of the Welfare-to-Work match. When this proposed \$25 million for 1999-00 is added to the \$10.2 million expended for the match in 1998-99, an obligation to expend \$147 million in matching funds would remain. Thus, any additional spending on community service employment above the Governor's budget in 1999-00 would count toward the Welfare-to-Work match, and accordingly would reduce the amount of required matching funds that must be expended in future years.

EVALUATE THE COST-EFFECTIVENESS OF WAGE-BASED COMMUNITY SERVICE

Wage-based community service—when compared to the workfare approach—results in substantially higher incomes for participants, increases the flow of federal funds into California, and may provide a better bridge to unsubsidized employment, but also has higher administrative costs. Consequently, we recommend that the DSS establish a CalWORKs demonstration program to evaluate the cost-effectiveness of wage-based community service.

As discussed above, we recommend that the Legislature fully fund the incremental cost of the wage-based approach to community service for counties that elect this option. Nevertheless, for purposes of determining the best approach to community service, we believe the cost-effectiveness of the wage-based approach, in comparison to the workfare approach, should be rigorously evaluated.

Comparing the Costs and Benefits. Although wage-based community service raises the incomes of participants in comparison to workfare, it may not be cost-effective from the government's perspective. As noted above, providing wage-based community service adds program costs of about \$80 per month per recipient, or about \$1,000 per year. (We note that roughly \$100 of this annual incremental cost would be recouped from sales taxes related to the expenditure of the EITC on taxable items in California.)

As discussed earlier in this report, wage-based community service may result in increased nonsubsidized employment for participants. If this were the case, then the savings from lower welfare grant payments might outweigh the additional administrative costs of providing wage-based community service, thereby making the investment cost-effective to government. Without a formal evaluation, however, it is impossible to know whether this approach is cost-effective from the taxpayer's perspective.

Analyst's Recommendation. Because the cost-effectiveness of the wage-based community service approach, compared to workfare, is not known, we recommend enactment of legislation requiring DSS to conduct an evaluation of the wage-based and workfare approaches as a CalWORKs demonstration program. (Such demonstration programs are authorized by the CalWORKs legislation.) The evaluation should employ an "experimental" design whereby participants are randomly assigned to both approaches. The evaluation should compare the costs and benefits of the two approaches from the perspective of both the government and the participants. We suggest that it be conducted in at least four different counties reflecting geographic and demographic diversity. We estimate that such an evaluation would cost approximately \$1.5 million over a three-year period.



PERMIT COMMUNITY SERVICE IN THE PRIVATE FOR-PROFIT SECTOR

Current law restricts community service employment to the public and private non-profit sectors. In order to better use community service as a bridge to unsubsidized employment, we recommend the enactment of legislation to allow counties to use private for-profit organizations as community service employers.

The intention of community service is to provide a bridge to unsubsidized employment. The bridge could be indirect, whereby a participant gains skills during community service and then obtains unsubsidized employment with another organization. Alternatively, the bridge could be direct, whereby the participant is hired (without any subsidy) by the former community service employer.

Under current law, community service must be performed in the public and private nonprofit sectors. Excluding the for-profit private sector from participating in community service employment, however, (1) significantly reduces the num-

ber of potential employers and (2) increases the difficulty of finding high quality work slots, particularly in jobs that might closely resemble those in the private sector. It also precludes the possibility that a for-profit organization will choose to hire, as a regular employee, any of its own community service workers—a common way for community service employees to obtain unsubsidized jobs

The policy rationale for the current-law limitation apparently is that private for-profit firms should not benefit from the “free labor” of community service participants. We believe, however, that any “benefits” of this policy (in terms of avoiding the provision of free labor to the private for-profit sector) are outweighed by the “costs” that result from eliminating the majority of potential employers of CalWORKs recipients from participating in the community service program.

Based on these factors, we recommend that legislation be enacted to permit counties to place community service participants with private for-profit employers.



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Acknowledgments

This report was prepared by Todd Bland, with the assistance of Erik Skinner, under the supervision of Chuck Lieberman. The Legislative Analyst’s Office (LAO) is a nonpartisan office which provides fiscal and policy information and advice to the Legislature.



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