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An Assessment of Senator Romney's Family Security Act: Would it Really Reduce Poverty?

Salvador Ortigueira and Nawid Siassi

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SALVADOR ORTIGUEIRA AND NAWID SIASSI*

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Abstract

We assess the Family Security Act—a plan presented by Senator Mitt Romney (R-UT) on February 4, 2021 to reform the tax/transfer system—in terms of its efficacy to achieve the stated objectives of increasing marriage rates and cutting child poverty at no cost to the government. The assessment is carried out through a microsimulation approach, using a dynamic model of savings, labor supply, household formation, and marital status. We find that while the plan would be highly effective at increasing marriage, it would reduce child poverty at the expense of increasing poverty among single-mother families and child deep poverty. Furthermore, the plan would entail a substantial cost to taxpayers. (JEL E21, H24, H31, J12)

Keywords: Family Security Act; household decisions; cohabitation and marriage; poverty.

*Ortigueira: School of Economic Sciences, Washington State University. E-mail: Salvador.Ortigueira@gmail.com; Siassi: Institute of Statistics and Mathematical Methods in Economics, TU Wien, Wiedner Hauptstrasse 8-10, 1040 Wien, Austria. E-mail: nawid.siassi@tuwien.ac.at.

1 Introduction

The $1.9 trillion Covid-19 relief package—passed into law on March 11, 2021 as the American Rescue Plan Act (ARPA)—includes an expansion of the Child Tax Credit (CTC) for one year, increasing the tax credit per child and making it fully refundable. The cost of this one-year expansion is projected to be roughly $110 billion.[1] Since this relief package was first unveiled there have been calls for the expansion of aid to families with children to be made permanent. Responding to concerns that the deterioration of the earnings potential of millions of U.S. workers caused by the Covid-19 outbreak may be long lasting or even permanent, President Biden's American Families Plan, presented to Congress on April 28, 2021, extends the CTC expansion through 2025.[2]

The expansion of the CTC has stirred a debate about the overall design of the tax/transfer system, in particular about the extent to which aid to low-income families should be in the form of work incentives (tax credits to low-wage earners) and/or in out-of-work income support (minimum guaranteed income). As part of this debate, and possibly in anticipation of the expiry of the current expansion of the CTC, various proposals to reform the tax/transfer system are already being put forth and discussed.

In this study we present an assessment of the Family Security Act (FSA), a proposal presented by Senator Mitt Romney (R-UT) on February 4, 2021 that has received a great deal of attention in the media and among policymakers.[3] As stated in the proposal, the FSA would enhance equal treatment for working and stay-at-home parents, and its main objectives are to:

- Promote marriage.
- Reduce child poverty.

The plan would overhaul the U.S. income support system for low- and middle-income households with children. Specifically, the plan would:[4]

- Replace the Child Tax Credit with a Child Benefit with no minimum income requirement or phase-in (so that families with no income would still be eligible for the child benefit).

[1]See Estimated Revenue Effects Of H.R. 1319, The American Rescue Plan Act of 2021, JCX-14-21, March 09, 2021 (Committee on Taxation of the U.S. Congress).

[2]Among those who raised concerns that the effects of the Covid-19 pandemic on workers' earning potential may be permanent is Treasury Secretary Janet Yellen (in testimony to Congress on March 23, 2021). von Wachter (2020) estimates the loss of lifetime earnings for a subset of vulnerable workers who lost their jobs as a result of the Covid-19 pandemic to be $2 trillion.

[3]Senator Romney's plan can be accessed at https://www.romney.senate.gov/romney-offers-path-provide-greater-financial-security-american-families.

[4]A more detailed description of how these changes would be implemented is provided in the next section.

- Simplify the Earned Income Tax Credit (EITC) through a family benefit independent of the number of children.
- Eliminate the Temporary Assistance for Needy Families program (TANF).
- Eliminate the *head of household* tax filing status. Non-married individuals must file as *single*, regardless of whether or not they have dependents.

To assess the Family Security Act we use a microsimulation approach, in which a dynamic model of the savings, labor supply, living arrangement, and marital status decisions of non-college educated workers with children is calibrated to a sample of U.S. households and simulated. The model is sketched in Section 3 below (for a detailed description of the model and the sample of households, see Ortigueira and Siassi 2021). We then compare the demographic and economic outcomes under the 2019 tax/transfer system (from now on referred to as the benchmark) with the outcomes that would emerge under the policies proposed in the FSA. It should be stressed that in our model household formation and marital status are endogenously chosen by utility-maximizing individuals, and consequently both choices are affected by the tax/transfer system they face. This makes our model especially suitable for assessing policy reforms aimed at promoting marriage. We can therefore offer predictions on how the Family Security Act would shape not only labor supply, income, and poverty, but also the composition of the population by household type: single mothers, cohabiting couples, and married couples.[5] The model also embeds in great detail the elements of the U.S. tax/transfer system, for both the benchmark and the FSA, including all the kinks and non-convexities stemming from individual income taxation, payroll taxes, and the means testing of transfers, as well as the differential treatment of filers/applicants according to their living arrangement and marital status.

2 The Family Security Act vs. the Benchmark Policy

The child benefit created by the FSA would pay families with children \$4,200 per child under six years of age, and \$3,000 per child for older children. (Our implementation of the child benefit in this study assumes the same benefit per child regardless of the age, namely \$3,400, which is the weighted average of \$4,200 and \$3,000 using the respective durations of the benefit.) The two charts in Figure 1 below compare the benchmark CTC (left chart) with the child benefit in the FSA (right chart). The three main features of the child benefit, relative to the benchmark CTC are: (1) an increase in the payout per child; (2) no minimum income requirement and phase-in (families with no income who do not file

[5]For the sake of clarity, a single-mother household is one formed by an unmarried mother and her children, with no partner present. By contrast, a cohabiting couple is a household formed by two unmarried parents who live together with their children.

taxes or whose income is too low to owe taxes would still collect the full child benefit); (3) it would be administered by the Social Security Administration, whereas the CTC is administered by the IRS.

The reform of the Earned Income Tax Credit proposed in the FSA is illustrated in Figure 2. The left chart displays the benchmark EITC, and the right chart the EITC contained in the FSA. This is a major reform of the EITC, which would remove the dependency of the EITC on the number of children, and would instead create four different schedules according to the type of family: (i) Single and childless; (ii) single with dependents; (iii) married and childless; and (iv) married with dependents. The credit phase-in rates would vary according to marital status but not according to the presence and number of dependents. This would amount to large reductions in the credit phase-in rates, especially for single mothers, which would contribute to increasing low-income workers' marginal tax rates. The proposed EITC is also less generous than the benchmark. For instance, a family with three children (either married or single) can collect a maximum credit of more than \$6,500 under the benchmark; however, the same family would collect a maximum credit of \$3,000 from the EITC in the FSA.

As already stated, the FSA would eliminate the Temporary Assistance for Needy Families (TANF), which prior to the Covid-19 pandemic was the only cash assistance program for low-income families with children. Recall that the proposed child benefit in the FSA would not require a minimum income and hence would become a quasi-universal income transfer to families with children (as shown in Figure 1 the child benefit would be phased out starting at income levels above \$200K for singles and at \$400K for married families). Finally, the FSA would eliminate the *head of household* tax filing status. Non-married individuals, regardless whether they have dependents, would have to file as *single*, which would amount to a lower standard deduction and higher taxable income and tax rates.

3 Our Framework for the Evaluation of the Family Security Act

We now briefly describe the main ingredients of the framework used for assessing the FSA. As noted earlier, in our model savings, labor supply, household formation, and marital status are endogenous choices that respond to changes in the tax/transfer system. Our framework therefore embeds the key trade-offs for assessing a policy reform like the FSA, whose main stated objectives include reducing poverty and promoting marriage.

In our model female and male adults are subject to non-insurable idiosyncratic risks, against which they can only partially insure through savings, managing labor supply, and by forming two-adult households. While the tax/transfer system provides additional insurance against labor market and fertility risks, it may crowd out private self-insurance by reducing savings, labor market participation, and the

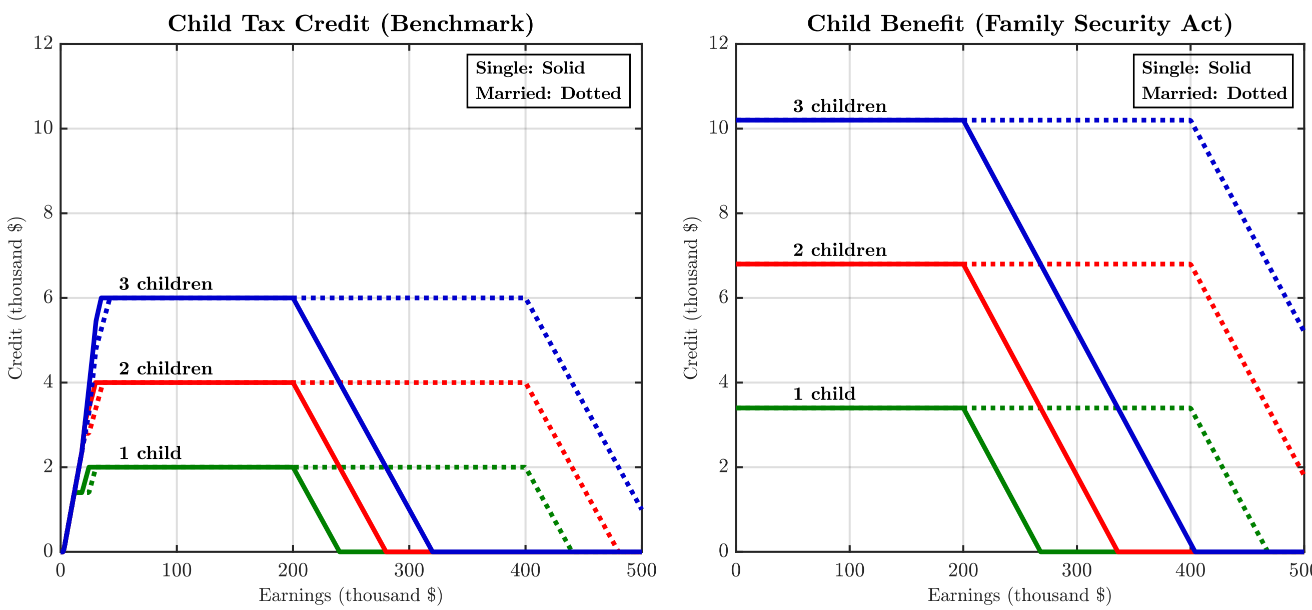

FIGURE 1. Left chart: Child Tax Credit (benchmark). Right chart: Child Benefit (FSA)

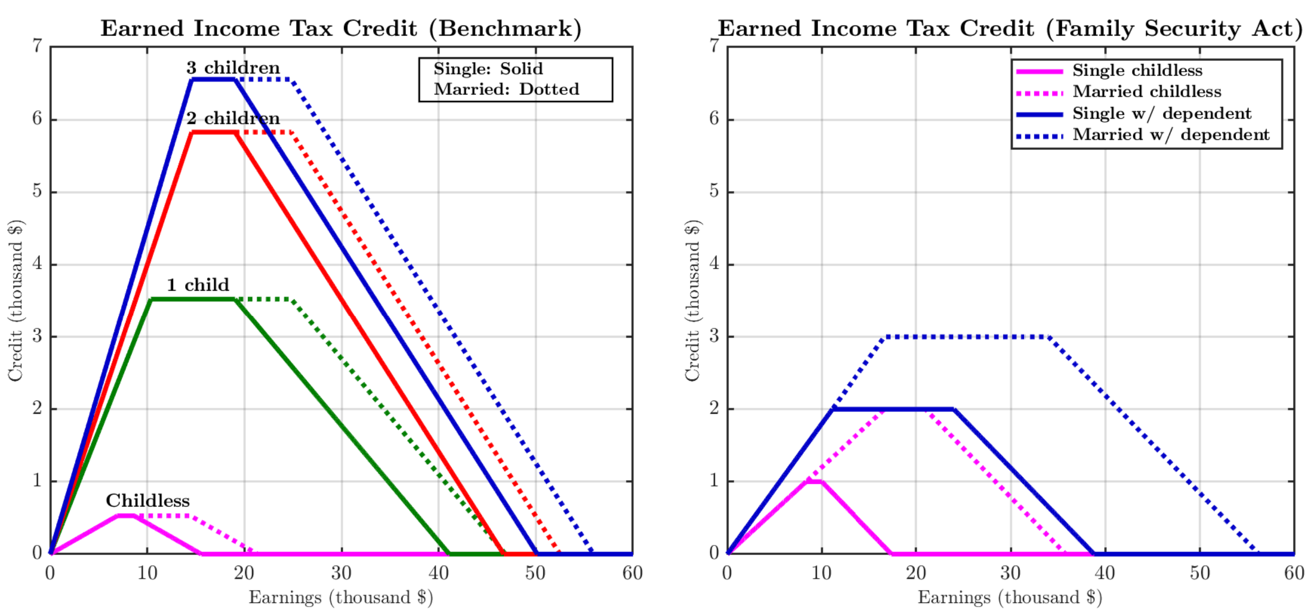

FIGURE 2. Left chart: EITC (benchmark). Right chart: EITC (FSA)

formation of two-adult households. In our model, when a two-adult household is formed, either as cohabitants or as a married couple, they are assumed to share risks (intra-household risk sharing) and to solve a joint decision problem. Provided with an opportunity to form a two-adult household, single mothers will choose to do so only if they are better off than if they continue as single mothers. Cohabiting couples get married as soon as they are better off than under cohabitation. The endogenous choices of both the living arrangement and marital status allow us to assess how tax/transfer reforms shape the composition of the population by household type. Also, since our model yields distributions of households by savings, hours worked, and earnings, we can assess how the tax/transfer system shapes inequality and poverty. The model is calibrated to match moments from a sample of one- and two-adult households with children formed by non-college-educated workers drawn from the Annual Social and Economic Supplement (ASEC) of the Current Population Survey (CPS), a representative survey of U.S. households. Our focus on households formed by non-college-educated workers with children is based on the higher prevalence of both cohabitation and poverty among this demographic group. To carry out our assessment of the FSA, we replace the benchmark tax-transfer programs with those proposed in the Act as described above.

4 The Demographic and Economic Effects of the Family Security Act

The effects of implementing the Family Security Act are presented in Table 1 below in terms of percentage changes from the values under the benchmark policy. By way of summary, let us start with the effectiveness of the FSA in meeting its stated objectives, namely, the promotion of marriage and the reduction of poverty.

- The FSA would be highly effective at promoting marriage. Our simulations yield a 16 percent increase in the marriage rate. The increase in marriages is explained by a reduction in cohabitation (the population of cohabitant couples falls by 45 percent).
- The effects on poverty are mixed. While the FSA would reduce child poverty from 14.3 to 11.6 percent, child deep poverty would increase. The FSA would reduce poverty among the population of married couples with children. However, poverty among single-mother families would increase from 26.5 to 45.5 percent, and deep poverty would triple.[6]

As shown in Table 1, single mothers' average disposable income would fall by 9 percent under the FSA. The reduction in the EITC rates and generosity, and the elimination of TANF would drastically

[6] For the calculation of poverty rates we follow the U.S. Census Bureau's poverty guidelines. For the calculation of deep poverty we also follow the Census Bureau in setting the income thresholds at 50 percent of those used to calculate poverty.

reduce the fiscal cost of these programs among single mothers. However, the new child benefit, along with the loss in tax revenue induced by the reduction in labor supply, would increase net transfers towards this population. Namely, the net transfer, on a per-family basis, would increase by 17.5 percent. On the other hand, married couples' average disposable income would increase by 3.4 percent, and the net contribution to the federal budget of this type of families, would fall by 84 percent, again on a per-family basis. Overall, the FSA would cost the government $1,114 per household in our population of interest (non-college educated families with children). This is a significant cost, far from the objective that the FSA would pay for itself.

We now explain the labor supply and marital status responses to the FSA. The labor supply responses are key to understanding the increase in poverty among single-mother families.

Labor supply. The labor supply responses presented in Table 1 show a large drop in the employment rate of single mothers (a 35 percent reduction from its value under the benchmark policy). By contrast, the employment rate among married mothers would increase by 5 percent, and it would remain roughly unchanged for married fathers. The fraction of two-earner married couples would increase by 7 percent. In short, the FSA would introduce large labor supply disincentives for single mothers, which would reduce their labor income and increase the incidence of poverty among this population. On the other hand, the FSA would incentivize work among married females, increasing their labor market participation and reducing poverty among married families.

To gain more insight on the work disincentives created by the FSA for single mothers we have calculated their participation tax rates at different levels of earnings (Figure 3). Participation tax rates (PTRs) provide a measure of the proportion of earnings taken away from the worker by an increase in taxes and/or by a reduction in benefits when the worker moves from non-employment to employment. The three charts in Figure 3 display the PTRs for single mothers with one, two and three children, respectively. The FSA would increase their PTRs. For example, under the benchmark policy a single mother of two children can get a work subsidy (negative participation tax rate) as high as 40 percent of her earnings. By contrast, under the FSA the maximum work subsidy would be only 10 percent. Also, under the benchmark policy work subsidies are positive up to $23K, whereas they already become negative (i.e. a tax) at $12K under the FSA. Single mothers earning between $25K and $30K would see an increase in the PTR of about 15 percentage points.

The elements in the FSA that reduce single mothers' work incentives are:

- The replacement of the Child Tax Credit by a Child Benefit that does not depend on work. As is clear from the left chart of Figure 1, at low levels of earnings the amount a tax filer collects from the CTC increases with earnings, thus reducing the marginal tax rate. In other words, since the

	Bench.	FSA (% change)		Bench.	FSA (% change)
Demographics			**Married couples**		
Lone mothers (%)	19.42	+0.32	Employment rate (%)		
Married couples (%)	71.22	+5.79	Females	59.80	+4.85
Cohabiting couples (%)	9.36	−44.75	Males	95.69	+0.88
New marriage rate†	11.45	+15.97	Two-earner HHs (%)	55.49	+6.76
Out-of-wedlock births (%)	55.91	−3.56	Avg. hours worked‡		
Child poverty (%)	14.27	−18.92	Females	1,645	−0.82
			Males	2,080	+0.23
Lone mothers			Avg. disp. income	56,180	+3.42
Employment rate (%)	83.36	−35.26	Poverty rate (%)	8.58	−83.33
Avg. hours worked‡	1,528	+7.85	EITC recipients (%)	44.31	+14.52
Avg. disp. income	29.505	−9.07	EITC costs*	1,741	−34.22
Poverty rate (%)	26.54	+71.40	SNAP + TANF costs*	1,150	−55.36
EITC recipients (%)	77.07	−41.23	Net contribution*	1,882	−84.28
EITC costs*	3,032	−73.57			
SNAP + TANF costs*	2,620	−14.57			
Net transfer*	5,482	+17.57			

TABLE 1—LONG-RUN EFFECTS OF THE FAMILY SECURITY ACT. *Notes:* †The new marriage rate is the number of new marriages in a given period divided by the number of unmarried mothers in that period. ‡Conditioning on positive hours. *Net transfer from (resp. net contribution to) federal budget per household in the relevant subpopulation.

amount of the CTC increases with the level of earnings, there is a positive substitution effect on the labor supply of low-earning single mothers. By contrast, under the FSA the amount collected from the Child Benefit (right chart of Figure 1) does not change with the level of earnings for those in the left tail of the earnings distribution. Out-of-work single mothers collect the same Child Benefit as working single mothers (up to $200K in earnings). This removes the positive substitution effect on the labor supply of low-earning mothers.

- The reduction in the EITC phase-in rates. The FSA would reduce the EITC phase-in rates by more than half (Figure 2). For example, for a single mother of two children the EITC phase-in rate would fall from 40 percent under the benchmark to 18 percent under the FSA, thus increasing marginal tax rates at low levels of earnings and reducing the positive substitution effects on labor supply.

- The elimination of the *head of household* filing status. Single mothers would have to file as *single*

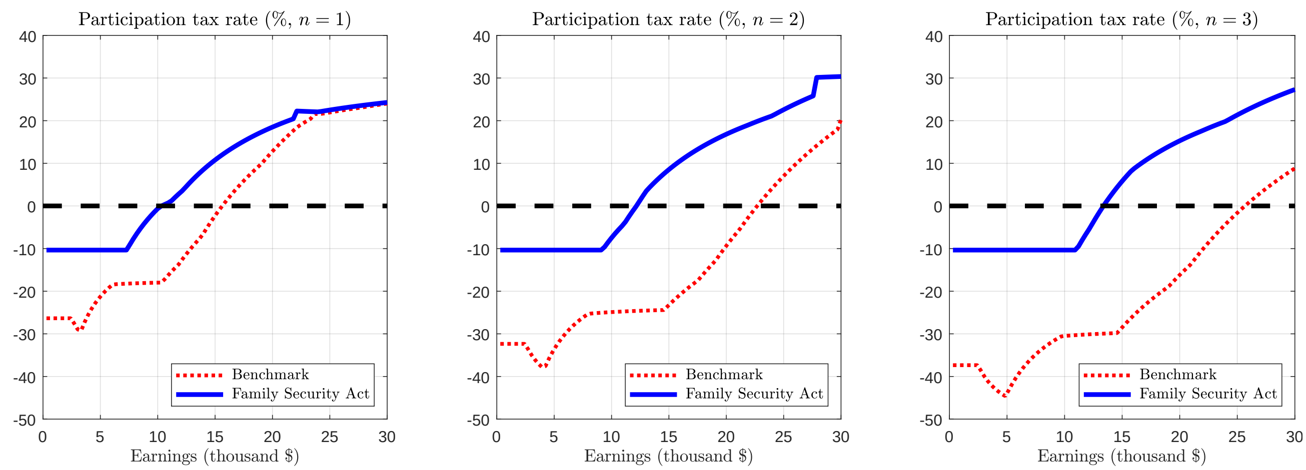

FIGURE 3. PARTICIPATION TAX RATES FOR SINGLE MOTHERS. *Notes:* For the calculation of the PTRs in this figure single mothers were assumed to be asset-eligible for TANF and SNAP. Single mothers with: one child (left chart); two children (middle chart); and three children (right chart).

under the FSA, which would reduce their standard deduction, and would increase their income tax rates (due to lower income thresholds for the second and third tax brackets). All this would increase their marginal tax rates and hence would discourage work.

The increase in the labor supply of married mothers that would result from the implementation of the FSA is explained by a reduction in their participation tax rates, especially for those whose husbands earn around $25K. The reason is that taxes and transfers for married couples are based on family earnings, and not on individual earnings, and therefore the participation tax rate of one spouse depends on the earnings of the other spouse. Thus, if a husband has a level of earnings around the end of the EITC plateau, his wife faces a high participation tax rate, as family earnings would place them in the EITC phase-out region (reducing their tax credit) or even making them ineligible for the EITC. The higher the generosity of the EITC at the plateau the higher the participation tax rate faced by the wife. Since the FSA would reduce the maximum EITC for married couples with children to $3K (from a maximum of almost $7K under the benchmark), it would reduce wives' participation tax rates. Note that this would affect mostly low-income married households.

Marriage rates. To illustrate how the FSA would change the marriage/cohabitation decision of couples with children, Figure 4 presents their optimal marital status regions in the space of the couple's labor productivities. There is an expansion of the marriage region relative to the same region under the benchmark policy. Low-income couples (i.e., those with low labor productivity) that are better off as cohabitants under the benchmark policy would marry under the FSA. For instance, low-productive couples where the male has labor productivity below 60 percent of the median choose cohabitation over marriage under the benchmark policy; however, these couples would choose marriage under the FSA provided the labor productivity of the female is at least 80 percent of the median female labor productivity. There is also a marked increase in marriage among couples with labor productivity above the median.

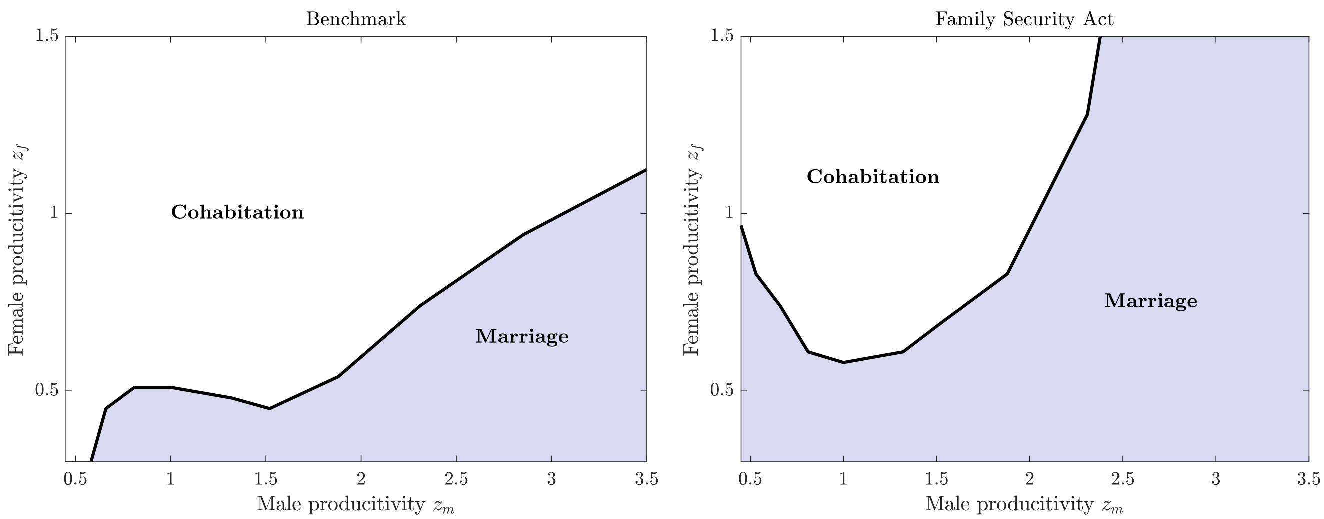

FIGURE 4. THE MARITAL STATUS DECISION OF COUPLES WITH CHILDREN. *Notes:* In the construction of this figure we assumed that couples have two children and pass the SNAP and TANF asset eligibility test.

The elements in the FSA that increase marriage are (1) the reduction in the EITC, and (2) the elimination of head of household filing status. A cohabiting couple can choose who claims the children as dependents. Under the benchmark policy, the one claiming the children files as head of household and, if eligible, can also claim the EITC. The couple member who does not claim the children as dependents must file as single and is not eligible for the EITC. This creates a cohabitation bonus for many low-income couples with children. This bonus increases with the generosity of the EITC and with the differential in the standard deductions and in the income tax brackets between the single and head of household filing statuses. Since the FSA eliminates the head of household filing status and reduces the EITC, it erodes the cohabitation bonus. As an illustration, consider a couple with two children whose only source of income is labor earnings. Assume the male earned \$19K and the female \$12K. Under the benchmark policy, if this couple chooses to cohabit and the male files as head of household and the female as single, the male's taxable income is \$650 (10 percent tax bracket) and he collects \$5,828 from the EITC; the female pays no taxes, as her earnings are below the standard deduction for single filers. If they choose to marry, their combined taxable income is \$6,600 (10 percent tax bracket) and they collect only \$4,521 from the EITC. Under the FSA, if they choose to cohabit and the male claims the children, he has to file as single. His taxable income would be \$6,800 and he would collect only \$2,000 from the EITC. If they choose to marry, their combined taxable income would be \$6,600 and they would collect \$3,000 from the EITC. Note that this example is given merely for the sake of illustration. In our model, the cohabitation/marriage decision is taken, jointly with the savings and labor supply decisions, to solve a dynamic, expected-utility maximization problem. The decision to marry is assumed to be non-reversible, as couples, once married, can no longer file their taxes using the head of household or single filing statuses.

5 Concluding Remarks

In this note we have assessed Senator Romney's Family Security Act, a proposal to reform the tax/transfer system to promote marriage and reduce child poverty. Compared to the tax/transfer system of 2019 (the benchmark), we find that this proposal would indeed increase marriage and reduce cohabitation (the population of non-college educated workers with children living as cohabitants would fall by 45 percent). However, despite a reduction in the child poverty rate, Senator Romney's plan would increase poverty among single-mother families and child deep poverty.

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