

## **Wisconsin's Welfare Spending: On the Trail of the Disappearing Surplus**

Wisconsin has often garnered positive national press coverage for the state's welfare reform initiatives. But in recent months several articles in the national media have portrayed the state's welfare reform spending in a less positive light.

Some of this more critical attention has stemmed from the following:

- A report issued in February by the National Campaign for Jobs and Income criticized Wisconsin and five other states for using federal funds from the Temporary Assistance for Needy Families (TANF) block grants to supplant state human service spending.
- A detailed analysis by the Rockefeller Institute of Wisconsin's human service spending from 1995 to 1999 found that state welfare and social service spending dropped by 14 percent after the implementation of W-2.
- A report issued in January by the Center on Budget and Policy Priorities found that at the end of the 1999 federal fiscal year Wisconsin had an accumulated "surplus" of \$321 million in unobligated or unliquidated TANF funds. Measured as a percentage of our state's total TANF allocations, this was the fifth highest TANF balance among all the states.

This paper examines Wisconsin's welfare spending, including trends in welfare and social service expenditures and the use of federal TANF funds to supplant state funding. We also consider Wisconsin's 1999 TANF surplus and how that surplus all but disappears in the current biennial budget.

### **The New Funding Paradigm**

The 1996 federal welfare reform law, known as the Personal Responsibility and Work Opportunity Reconciliation Act (PRWORA), radically changed the fiscal contract between states and the federal government for providing welfare services. Under the old AFDC system, each state and the federal government proportionately divided the cost or savings from any increase or decrease in the AFDC caseload. States had very little flexibility, but they were also partially insulated from the risk of higher caseloads during an economic downturn.

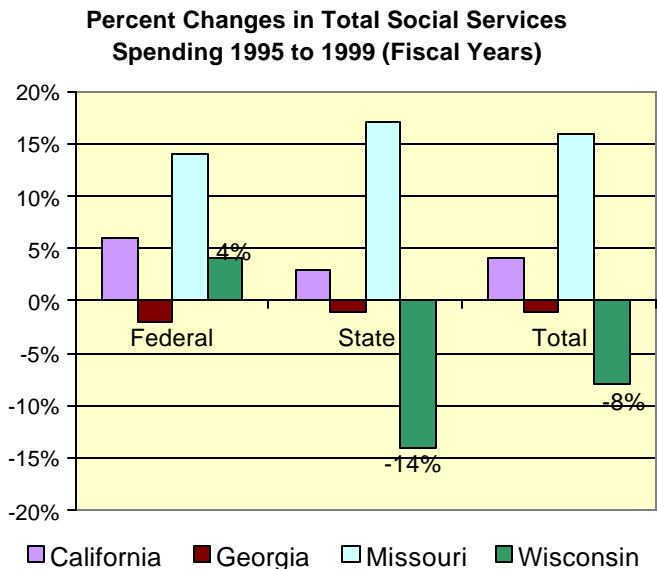
The PRWORA gave states more responsibility and far more flexibility in designing and implementing welfare services. It also put much more fiscal risk on the shoulders of the states, in return for the increased flexibility and for a guaranteed level of federal funding. This new welfare system provides the states with a relatively fixed TANF block grant, which they can use to develop new and innovative strategies to help poor families with children move into the workforce and climb the economic ladder. States accepted the gamble that if caseloads fell they would reap the benefits, and if caseloads increased they would bear the fiscal responsibility. The states agreed that they would meet "maintenance of effort" standards for sustaining a minimum level of state spending for

their low-income programs (equal to at least 75 percent of the pre-PRWORA state funding level).

### Welfare and Human Service Spending Trends

The Nelson Rockefeller Institute issued a study in February analyzing how spending on social services changed in four states in the wake of welfare reform (*Changes in State Spending on Social Services Since the Implementation of Welfare Reform*). The study examines expenditures for welfare and other social services in Wisconsin, California, Georgia and Missouri from 1994-95 through 1998-99. Although the purpose of the study was to examine the fiscal impacts of federal and state welfare reform initiatives, the Rockefeller Institute measured all social service spending – in order to see how states used the additional flexibility to shift spending among social service categories. (Note: health care expenditures were not included.)

The study found that among the four states analyzed, Wisconsin was the only one to significantly cut social service spending. The chart at right shows total federal and state social service expenditures in Wisconsin fell by 8 percent (\$101 million) from fiscal year (FY) 1995 to FY 1999. More specifically, the state share of funding for welfare and social services fell about \$122 million, or 14 percent, while federal spending increased by \$20.5 million. As a share of total Wisconsin general fund spending, social services fell from 10.9 percent in 1995 to 7.4 percent in 1999.



The Institute’s study illustrates that as welfare caseloads dropped dramatically in the four states, spending shifted from “poverty relief” to other low-income and social service programs. In Wisconsin, for example, state and federal spending for child care increased by \$100 million, or 168 percent, which was well above the range of increases in the three other study states (76 to 120 percent). Spending for employment and training in Wisconsin increased by \$22 million, or 20 percent, although that was a much lower growth rate than the range in the other states (52 to 111 percent).

In each of the four states there was a significant reduction (4.6 to 25.4 percent) in spending for “traditional low-income programs”. However, Wisconsin was the only one of the four states where that drop was not offset by a nearly equivalent or larger increase in other social service spending. Although state and federal spending for other social services did increase in Wisconsin by \$90 million (including \$50 million more for child protection), the study found that this increase was far surpassed by the \$191 million drop in spending for low-income programs.

## Supplanting State Funds

When the federal welfare reform law was being developed, one of the concerns of policymakers was that states might use the substantially enhanced flexibility with federal funds simply as a means of “supplanting” state funding. In other words, it was feared that the federal TANF funds would be used to pay for services formerly financed with state money – thereby freeing up state funds for tax cuts or other purposes. The drafters of the federal legislation built in “maintenance of effort” standards to reduce the potential for supplantation.

The Rockefeller Institute study concluded that “there is little evidence in these numbers of significant supplantation.” However, it cited Wisconsin’s practices as the clearest example of supplanting. In fact, Wisconsin’s aggressive efforts to use TANF funds wherever legally permissible to replace state funding are a key to understanding the Rockefeller Institute’s finding that Wisconsin decreased its state expenditures for social services by 14 percent from FY 1995 to FY 1999.

A report issued in February by the National Campaign for Jobs and Income (NCJI) reinforces the concerns about supplantation, stating that Wisconsin is one of six states that “have ‘gamed the system’ to divert TANF funds to pay for tax cuts and/or programs that do not benefit poor families.”

The NCJI report cited two prominent Wisconsin examples of this supplantation. The first is the decision by the Legislature last year to exploit a new loophole in federal law by using TANF funds to replace, on an annual basis, about \$48 million of state funds for the earned income tax credit -- to free up money for tax relief. In addition, for the last several years the state has transferred about \$32 million annually – the maximum allowed under federal law – into the Social Service Block Grant. These funds were then used to supplant state support for Community Aids, rather than to help the Community Aids appropriation keep up with inflation.

Another way in which the state has recently reduced its state GPR commitment to W-2 related programs is to fund an increasing portion of W-2 child care programs with TANF funds instead of Child Care Development Block Grant (CCDBG) funds. The federal funds for that block grant require a 40% state match. In the 1999-2001 budget bill the Governor and Legislature chose not to put up the matching funds necessary to draw down \$44 million in federal CCDBG funds. That decision enables the state to save \$31 million GPR, but it requires diverting \$75 million in TANF funds during the biennium to cover child care spending that could have been funded from the block grant.

Wisconsin has also used TANF funds on a smaller scale for numerous other social service and education appropriations (outside the Department of Workforce Development) that are either supplanting state funds or in lieu of potential increases in state funding. Examples in the current biennium include:

- \$3.7 million each year for Head Start (\$1.2 million replaces GPR, \$2.5 million net increase);
- \$1.4 million annually for aid to Milwaukee Public Schools (replaces GPR);
- \$1.8 million per year for adolescent pregnancy prevention services (replaces GPR); and

- \$1 million annually for immunizations (\$500,000 replaces GPR, \$500,000 is new funding).

The current budget also includes ten new TANF expenditures within the Department of Workforce Development (DWD), including many that are not traditionally associated with welfare programs and in the past probably would have been financed from other sources, such as GPR funds. Some examples include:

- \$7.5 million per year for Community Youth Grants;
- \$1.4 million annually for a DWD literacy initiative;
- \$1 million each year for nutritional services (\$500,000 replaces GPR, \$500,000 is new funding); and
- \$1 million annually for an AODA initiative.

### **Wisconsin's TANF Surplus**

A report issued in January by the Center on Budget and Policy Priorities (CBPP) examines the unspent welfare funds in all the states. The report shows that Wisconsin had a total of \$321 million in unspent TANF funds on September 30, 1999 – the close of the last federal fiscal year. This amounted to 34 percent of the total TANF funding our state had received since 1997, tying Wisconsin with Ohio for the fifth-highest percentage of unspent funds.

The progress that states are making in using their TANF surpluses is a matter of great interest to members of Congress, as well as for advocacy groups. The federal welfare reform law must be reauthorized by Congress by the end of 2002, when it “sunsets”. Many people are concerned that Congress may decide at that time to reduce significantly the amount of TANF funds allocated to the states, especially if the states continue to underutilize the TANF funding they are currently receiving. These concerns were reinforced by Congressional efforts last year to take back some of the welfare funding that has already been committed to the states.

In March of this year, Representative Nancy Johnson, chair of the Human Resources Subcommittee of the House Ways and Means Committee, sent a letter to all the governors on the subject of TANF funding and its future prospects. She noted that progress has been made by the states in increasing the use of TANF funds, but she cautioned that future TANF funds would be safeguarded only if states continue to make efforts to spend the funds they are now receiving. Her letter also expressed concern about the use of TANF funds to supplant state funding and the potential implications of that practice for Congressional support of maintaining the current TANF allocations.

### **How Much TANF Funding Is “Unspent”?**

Determining just how much TANF funding is “unspent” in any state is more difficult than one might suspect. The quarterly reports that each state must submit to the federal government include two types of unexpended TANF funds. The first category is “unobligated” funding, which represents the portion of a state’s TANF allocation that it has neither spent nor committed to spend. The second category is “unliquidated

obligations”, which are the funds a state has committed to spend but has not yet spent. An example of unobligated TANF funds is the amount that a state has contracted to grant to local administrators of welfare services (such as W-2 agencies), but which has yet to be spent or billed by that agency.

Although the CBPP report makes a persuasive case that it is important to look at a state’s unliquidated obligations as well as its unobligated TANF funds, the distinction between these two categories is still very important in Wisconsin. Of the \$321 million in the state’s TANF balance at the end of FFY 1999, only \$30.7 million was unobligated. Much of the \$290.4 million in unliquidated obligations represents funds that the state has contracted to give to the counties and local agencies administering W-2. While it is true that these funds have not been expended by the state, most of that money is not available to state policy-makers. On the other hand, there may still be an opportunity for input at the local level to influence how W-2 agencies use the “community reinvestment” portion of the unspent funding they will be receiving from the state.

### **The Declining TANF Balance: Where Is It Going?**

Ultimately, the issue of how much money was in Wisconsin’s TANF balance at the close of the last fiscal year is far less important than the question of how the unspent funds will be utilized in the 1999-2001 biennium. That question was largely answered in the fall of 1999 when the Legislature adopted the TANF spending package that was included in the biennial budget bill.

When the Governor put together his version of the biennial budget early in 1999, he estimated that the state would start the current state fiscal year with a TANF balance of \$133 million. However, by the time the full Legislature acted on the budget, that figure had grown to \$348 million – which surpasses the state’s annual TANF allocation of \$317.5 million. The substantial growth in the TANF balance represents amounts that the state was contractually obligated to pay W-2 agencies but which had not formally been “encumbered” and, therefore, had to be carried over into this biennium.

The fiscal challenge facing the Governor and the Legislature was to use this very large balance in the current biennium without committing the state to an ongoing spending level that is unsustainable. This is being done a variety of ways. At the risk of oversimplifying, these strategies can be put into three categories, which are discussed below: expanding or creating programs for TANF-eligible families, increasing the use of TANF funds to supplant state funding, and making one-time appropriations to draw down the surplus.

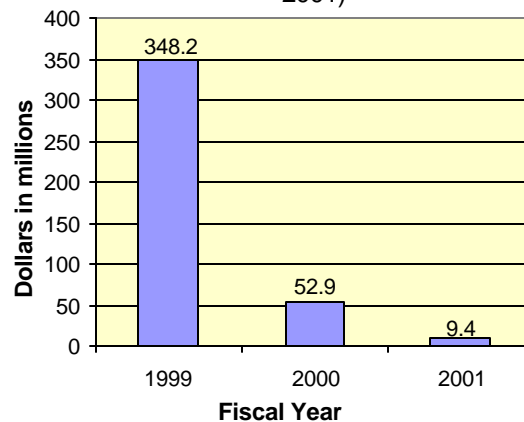
- *New and Expanded Programs* –The TANF surplus accumulated largely because of rapidly declining W-2 enrollment and lower-than-expected use of subsidized child care. This gave the state the opportunity to expand programs and create new ones for TANF-eligible families. For example, some of the TANF funding will be used to expand eligibility for child care subsidies and to reduce co-payments. Examples of new programs or services include \$7.5 million per year for Community Youth Grants, a like amount for the Early Childhood Excellence Initiative, and \$1 million annually for AODA services.

- *Increased Supplantation* – As we discussed above, for several years Wisconsin has been taking advantage of the flexible nature of the TANF block grant to use this funding to replace or reduce state funds in a number of human service or low-income programs. That practice became much more obvious in the 1999-2001 biennial budget. The clearest example is the use of about \$50 million per year (roughly 16 % of our annual TANF budget) to supplant state funding for the refundable portion of the Earned Income Tax Credit (EITC).
- *One-Time Appropriations* – The Governor and the Legislature were understandably concerned about increasing spending in a way that would not be sustainable. To avoid that, they approved a number of one-time appropriations or declining appropriations that result in nearly \$280 more in W-2 related expenditures in the first fiscal year than in the second year of the biennium. Much of this is accomplished by a one-time \$217 million appropriation to cover the contractual obligation to W-2 agencies carried over from the previous biennium (although \$95 million of that will be returned to the TANF fund as the “state profit” portion of the unspent contractual amounts). The budget also uses \$102 million in 1999-2000 to set aside a rainy day fund, more formally referred to as the “contingency fund and contract reserve”. In addition, the state drew down the TANF balance by another \$48 million by not only using TANF to pay for the EITC in both years of this biennium, but by also doing that retroactively for 1998-99.

The net result of the myriad of funding decisions in the biennial budget (Act 9) is a \$245 million increase in total W-2 related expenditures in 1999-2000, compared to the amount budgeted for the previous year. But that expenditure level will drop from nearly \$897 million in the first year of this biennium to about \$618 million in the second fiscal year.

As the chart at right illustrates, the TANF balance is projected to fall from \$348 million at the start of 1999-2000 to \$52.9 million at the end of the year, and then to only about \$9 million at the end of the biennium.

**Closing TANF Balances**  
(Actual -1999, Projected - 2000 & 2001)



### Community Reinvestment Funding

Although almost all of the state TANF surplus has been committed in the biennial budget bill, there are still substantial TANF funds up for grabs at the local level. W-2 agencies are in the process of drawing up and submitting plans to the state for the use of about \$80 million in “community reinvestment” funds.

### Conclusion

The new federal welfare reform law gives states far greater flexibility to design and implement innovative anti-poverty strategies. As welfare rolls have dramatically declined, states have been able to spend significantly less on the more traditional sorts of welfare services and more on other strategies to help low-income families become self-sufficient. But according to a February 2000 report by the National Campaign for Jobs

and Income (NCJI), “it appears that states are generally doing little that is particularly creative, and most are holding on to large amounts of unspent funds, despite the persistence of poverty and, for some families, deepening poverty.”

The NCJI report and another recent study by the Rockefeller Institute document that Wisconsin is one of a small handful of states that has taken advantage of its flexibility under federal law to use TANF funding for the purpose of supplanting state spending for various programs, such as the earned income tax credit. This supplantation helps account for the Rockefeller Institute’s finding that social service expenditures have declined in Wisconsin from 10.9 percent of state general fund expenditures in fiscal year 1995 to just 7.4 percent four years later.

Wisconsin finished the 1999 federal fiscal year with one of the largest balances of federal welfare funds among all states. That TANF “surplus” was tied for fifth highest, as a percentage of the state’s cumulative TANF allocations. However, much of that TANF funding was already legally committed to the W-2 agencies. Although it was technically “unspent” for purposes of federal reporting requirements, only a small portion of that surplus was available to state policy-makers putting together the current W-2 budget.

The biennial budget bill commits the state to a combination of one-time TANF appropriations and ongoing expenditure increases that will reduce the TANF balance from \$348 million at the start of the 1999-2000 fiscal year, to an estimated \$9 million at the end of the next fiscal year. However, the budget also contains a new \$102 million TANF rainy day fund, which gives the state a substantial cushion in the event that W-2 related expenditures are greater than anticipated.

Congress will be looking carefully at state TANF spending and balances next year, as it considers reauthorization of the federal welfare reform law. In light of the reductions in the TANF balance in the current biennial budget, it is unlikely that Wisconsin will be held up as an example of a state with an excessive TANF surplus. On the other hand, the extensive use of TANF funds in our state to supplant state funding could play into the hands of federal policy-makers who are interested in cutting the states’ TANF allocations.