# A POLICY AGENDA for Social Capital

## social capital project

A project of the Joint Economic Committee — Republicans | Ranking Member Senator Mike Lee
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# An Introduction to A Policy Agenda for Social Capital from U.S. Senator Mike Lee

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The Social Capital Project is a multi-year research effort to investigate the evolving nature, quality, and importance of our associational life—namely, our families, communities, workplaces, and religious congregations. These institutions are critical to forming our character and capacities, providing our lives with meaning and purpose, and addressing the challenges we face in an increasingly disconnected world.

In our first volume, *An Overview of Social Capital in America*, the Project investigated American associational life, the distribution of social capital, and trends in social capital. In this volume, *A Policy Agenda for Social Capital*, the Project proposes specific policies to increase social capital through rebuilding civil society, making it more affordable to raise a family, increasing family stability, reconnecting Americans to work, and improving investment in youth.

The onset of the COVID-19 pandemic has placed unique pressures on our already fractured social fabric, making these recommendations more relevant than ever. *A Policy Agenda for Social Capital* provides recommendations for expanding opportunity and strengthening America's social fabric that are crucial to America's post-pandemic recovery and to its future.

**Mike Lee,**
*Ranking Member, Joint Economic Committee*

# The Wealth of Relations:

## Expanding Opportunity by Strengthening Families, Communities, and Civil Society

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Throughout its history, economics has been centrally concerned with capital. In his magnum opus, *The Wealth of Nations*, Adam Smith defined it as the portion of someone's possessions "which, he expects, is to afford him…revenue."[1] Until the second half of the 20th century, capital was analyzed primarily in its physical and financial forms: factories, machines, and equipment; stocks, bonds, and insurance contracts.

Over the past 60 years, Gary Becker and other economists have established the concept of "human capital"—personal attributes such as skills, knowledge, and personality traits.[2] Like other forms of capital, human capital reflects investment and is valuable (revenue-affording) to its possessor. Most obviously, it pays off in the labor market. But more broadly, human capital helps us achieve whatever our aims might be—economic or otherwise. Empathy and the ability to cooperate, for instance, facilitate the forming of close friendships, an important source of happiness in life.

In more recent decades, researchers and theorists have described another source of wealth: social capital. While not previously unknown to economists, social capital was first comprehensively analyzed by political scientist Robert Putnam.[3] It refers to the aspects of human *relationships* that may be expected to afford value to their possessors. Relationships inhere in social networks as well as in the institutions that people create together for specific purposes and in which they participate. These institutions are ubiquitous, ranging from families to schools to book clubs to unions to churches to athletic leagues.[4]

The social capital literature has suffered from inconsistent and imprecise definitions, and like human capital, the social variety presents complex measurement challenges.[5] Yet, in the same way that individual attributes are almost self-evidently of greater or lesser value, so, too, with relationships.[6] Relationships provide individuals happiness, identity, self-worth, knowledge, skills, financial support, emotional support, values, preferences, habits, and more. Webs of relationships also produce collective goods such as norms, institutions, civil society, and culture, which then, in turn, become part of the stock of social capital available to individuals embedded in these webs.

Even from the narrowest of economic perspectives, who we know, the institutions to which we are connected, and what they can do for us are obviously related to economic outcomes. We find jobs through our contacts. We develop skills (human capital) that pay off in the labor market through the mentorship of teachers, parents, and neighbors (reflecting the social capital inhering in those relationships).

Just as obviously, economic precursors affect the value of individual and community social capital. Economic development has created more-extensive but less-personal relationships at least since ancient Greeks adopted coinage and institutionalized market exchange within open-air agoras.[7] Today, a poor neighborhood with community members who have low attachment to the workforce will afford insufficiently valuable social capital to students living there who aspire to become a doctor.[8] A town experiencing a factory closing may see local businesses fail and an exodus of the most resourceful residents, leaving behind places where community is all but absent.[9]

For two years, the Social Capital Project within the Joint Economic Committee (JEC) has documented trends in associational life—what we do together—and its distribution across the country. With this evidentiary base established, the Project, now situated in the JEC Chairman's Office, turns to the development of a policy agenda rooted in social capital. Specifically, the focus of the Project will be to craft an agenda to expand opportunity by strengthening families, communities, and civil society.

The following sections of this paper offer a justification for our focus on opportunity and on social capital as a means to opportunity. Subsequently, we shift to discussing how public policy might affect the value and distribution of social capital. We introduce five policy goals around which the Social Capital Project's research will be organized. The conclusion previews how we will do so.

## OPPORTUNITY AS THE "LEADING OBJECT" OF PUBLIC POLICY

On the 85th anniversary of the Second Continental Congress's ratification of the Declaration of Independence, President Abraham Lincoln addressed a special session of the US Congress. The state of the Union was decidedly precarious. Lincoln had assumed office just four months earlier. In between, four states had seceded from the Union in the aftermath of the Battle of Fort Sumter, joining the seven that had formed the Confederate States of America prior to Lincoln's inauguration.

Lincoln asked Congress to authorize an increase in troops and funding sufficient to wage the Civil War, but he was also trying to win the hearts and minds of legislators—especially border-state legislators—in favor of the cause of the Union. His case was ultimately expressed in his assertion that "the leading object" of the federal government was "to elevate the condition of men; to lift artificial weights from all shoulders; to clear the paths of laudable pursuit for all; to afford all an unfettered start and a fair chance in the race of life."[10]

In other words, Lincoln's pitch to nervous and wavering Americans staring a bloody war in the face—his best case for patriotism and loyalty—was an appeal to the federal government's responsibility to remove barriers to opportunity.

Today's policy and political debates often revolve around opportunity and the role of public policy in expanding it. These debates are rendered less productive than they could be because of a number of short-sighted views. More effectively

promoting opportunity requires a broader and more subtle perspective that moves beyond the blind spots of the left and right.

For starters, there is a tendency to equate "opportunity" almost exclusively with *economic* outcomes—educational or financial success, for instance. Policymakers are too often blind to the reality that many people find happiness not in maximizing their years of formal schooling, standardized test scores, college ranking, seniority at work, or annual salary, but in enjoying their family life, being embedded in communities, feeling spiritually fulfilled, and having a sense of self-worth.

Many observers of the 2016 presidential primaries had a difficult time understanding the resonance of then-candidate Donald Trump's assertion that, "Sadly, the American Dream is dead." Tim Carney, in his important new book, *Alienated America*, argues that Trump's pessimistic appeal was attractive not because economic times were especially bad that year. What had died, in the view of his core supporters, was "the American Dream of robust community life."[11]

"The materialistic view of the American Dream," according to Carney, "misses the point." Instead, he speculates,

> the things we think *accompany* the American Dream are the things that really *are* the American Dream. What if the T-ball game, the standing-room-only high school Christmas concert, the parish potluck, and decorating the community hall for a wedding—what if those activities are not the dressings around the American Dream, but what if they are the American Dream?[12]

Just as there is too often a narrow focus on economic outcomes in debates about opportunity, discussions too often emphasize economic or personal barriers. Among political liberals, in particular, "lifting artificial weights" and "clearing paths" mostly mean giving more money to poor, working-class, and (increasingly) middle-class people. Hence the calls on the left for guaranteed jobs, a $15 minimum wage, universal child care, universal college, and a universal basic income guarantee.

In contrast, conservatives have tended to point to personal barriers to opportunity. Different income levels in adulthood, for instance, may be due to unequal economic resources growing up, but they also may be the product of different orientations, preferences, values, and personal strengths and weaknesses. Equalizing incomes will not necessarily change these differences.

However, the conservative perspective is not without its own problems. Conservatives have tended to wield the concept of opportunity defensively, affirming their support for "equality of opportunity" as against the "equality of outcomes" that they accuse liberals of seeking. The distinction is rooted in conservatism's view of people as mostly the captains of their own ships. Given that we have made great strides as a nation achieving formal political equality, the US is often thought to have realized actual equality of opportunity. If someone fails to realize her own definition of the good life—perhaps as a consequence

of problematic orientations, preferences, values, and weaknesses—many conservatives view this failure as a personal shortcoming.

Most conservatives would agree with Martin Luther King Jr. that "a productive and happy life is not something you find, it is something you make."[13] But we do not navigate our lives in isolation, we make a productive and happy life *with other people*. Supportive relationships and institutions are instrumental for expanding opportunity. In part, that is because they are instrumental in forming our orientations, preferences, values, and personal strengths and weaknesses.

That is to say, opportunity depends on social capital—what is available to us from our relationships with family, friends, neighbors, congregants, coworkers, and others. In particular, the people to whom we are born and around whom we live are consequential for our opportunities. "Artificial weights" are not only economic, not only personal, but social.

## SOCIAL CAPITAL AND OPPORTUNITY

Establishing the empirical importance of social capital is more difficult than it may seem at first glance. After all, we cannot see or touch social capital; we cannot measure it directly, and it has both quantitative and qualitative elements. Research on human capital has tended, until recently, to simply equate it with educational attainment or scores on tests of cognitive ability. As limiting as this convention is, the field of social capital research cannot even claim a conventional measure.

Moreover, it is difficult to establish causal relationships in social science even when looking at well-measured phenomena. Absent a randomized experiment—where half of participants are, for instance, given $50,000 while the other half are not—social scientists have limited options for understanding how the outcomes of two groups that differ on some attribute would change were there no such difference. The two groups may differ in any number of other ways, and those differences may be the real attributes that produce disparate outcomes.

Because we lack many experiments in which social capital is distributed randomly between people, we mostly are left with necessarily flawed studies that attempt to mimic an experiment using statistical methods.

One important exception is a paper by economists Raj Chetty, Nathaniel Hendren, and Lawrence Katz evaluating a policy experiment called "Moving to Opportunity."[14] Moving to Opportunity involved nearly 5,000 families in five cities and randomly gave public housing residents a rent subsidy to be used only in a low-poverty neighborhood, a subsidy with no such restriction, or no subsidy at all (beyond continuing to live in their public housing project). The study found that compared with remaining in place, moving to a low-poverty neighborhood in childhood (but not adolescence) increased college enrollment, lifted adult earnings by one-third, reduced single parenthood, and improved neighborhood quality in adulthood. Social capital's power burns slowly; the longer children lived in a low-poverty neighborhood, the better their outcomes. Fundamentally, the results point to the importance of the local networks and institutions to which children are exposed.

This paper is part of a series of studies illustrating the importance of social capital for the intergenerational mobility of children by Chetty, Hendren, John Friedman, and a number of their colleagues at the Equality of Opportunity Project (EOP) and now at Opportunity Insights.

In its seminal work on the subject, "Where is the Land of Opportunity?", the EOP found that intergenerational mobility varies widely across the country.[15] To measure mobility, the authors of the study ranked more than 40 million children and their parents by income percentiles. Places where two grown children from different families tend to be ranked more closely together than were their parents were considered to have high relative mobility. The authors found that areas with high levels of relative mobility also tended to produce higher-ranked adults from their low-income children. (That is, they produced what EOP calls simply, "upward mobility.")[16]

Many features of places seem to go along with high or low mobility, but the research of EOP and Opportunity Insights consistently has found measures of social capital to be among the most strongly related. Out of 34 features they examined in "Where is the Land of Opportunity?", the one most strongly related to upward mobility and relative mobility was the share of children in an area that was raised by a single mother. In second place as a predictor of upward mobility was a fairly limited index of social capital. Community rates of mobility were also higher where there were more religious adherents, fewer divorced adults, and more married adults, and where there was less economic and racial segregation.[17] All of these indicators bear on the value of social capital in an area.[18]

Research by the Social Capital Project confirms the EOP findings. Relative mobility is higher not only when states score better on our social capital index and when family unity is higher, but also the higher are their levels of family interaction, social support, community participation, and charitable giving.[19]

These relationships may or may not mean that social capital causes mobility. It may be that upwardly mobile families with high social capital simply tend to congregate together; if a community looks like it promotes mobility, it might just be because it is home to a lot of families who would be upwardly mobile anywhere. Chetty and Hendren have made a strong case that places do promote or impede mobility.[20] In one paper, they found that children who moved to better areas—places with high income mobility among permanent residents—had better long-term outcomes in proportion to the amount of time they spent there.[21]

It is even more difficult to establish that *specific features* of places affect mobility. In another paper, Chetty and Hendren first estimated the causal effect on mobility of living in each of hundreds of communities, such as Memphis or Salt Lake City.[22] To do so, they compared the adult outcomes of brothers who moved to an area but, because they differed in age, subsequently lived in it for different durations. This causal effect is distinct from the part of a place's mobility rate that simply reflects

the sorting of high- or low-mobility families into Memphis or Salt Lake City. Then, rather than looking at how community features were related to mobility, Chetty and Hendren looked at how they were related to the causal effect of living in Memphis, Salt Lake City, or some other community.

These analyses revealed that nearly two-thirds of the strong *correlation* between single parenthood and upward mobility was due to the fact that single parenthood was related to an area's causal effect on mobility. That is, communities with high rates of single parenthood tended to *be worse* for mobility than communities with low rates (not simply home to families with lower mobility). The relationship between an area's score on the social capital index and its upward mobility *entirely* reflected the causal effect of moving to the area rather than sorting. Social capital had the fourth-strongest relationship with area causal effects on mobility (out of 40 factors), while single parenthood ranked 10th. The share of adults married came in close behind at 15th place.

Chetty, Hendren, and their colleagues have also assessed the extent to which features of communities can explain unequal outcomes between men and women and between blacks and whites. One paper looked at why low-income girls have higher employment rates as adults than poor boys do.[23] The association between this employment gap and a community's rate of single parenthood when the boys and girls were children was the fifth strongest of 28 factors, and community marriage rates came in at sixth.

In yet another paper, the team looked at adults who, as children, were poor but lived in low-poverty neighborhoods. They found that black men had stronger upward mobility the more low-income black fathers there were in their childhood neighborhood.[24] This was true regardless of whether someone's own father was present, suggesting that even the family cohesion of other black children in the neighborhood affected them.[25] Meanwhile, having more low-income white fathers in the neighborhood did not increase the upward mobility of poor black children; nor did having more low-income black men who were childless. More low-income black fathers in a neighborhood also corresponded with higher future employment among poor black boys. The relationship between the number of low-income black fathers and future employment was much smaller for poor white boys and negligible for poor black girls.

The Chetty-Hendren-Friedman research on upward mobility suggests that our intuitions about social capital are correct. The nature of our relationships provides more or less value to us as we pursue our aims in life.[26]

## THE LIMITS OF PUBLIC POLICY

If social capital matters for opportunity, there remains the question of whether government—or the federal government specifically—should (or can) do anything to reduce social inequalities.

The extent to which government policy can expand opportunity or reverse America's deteriorating family and community life is, first and foremost, limited by our commitment to classical liberal principles of personal responsibility, individual choice, and freedom from state encroachment on private decision-making. One might argue that if free-willed individuals choose to act in ways that weaken community cohesion—by, for instance, relying more on markets to provide services such as child care and less on neighbors—so much the worse for communities.

What is more, practically speaking, public policies to change behavior have often proven ineffective or, worse, counter-productive. In the mid-1980s, after years of evaluating social policies, Peter Rossi declared with his "iron law of evaluation" that, "The expected value of any net impact assessment of any large scale social program is zero."[27] Further, his "brass law of evaluation" asserted that, "The more social programs are designed to change individuals, the more likely the net impact of the program will be zero." Almost thirty years later, David Muhlhausen ratified Rossi's observations in a comprehensive study of rigorously evaluated multi-site federal social programs. He reported, "the evidence overwhelmingly points to the conclusion that federal social programs are ineffective."[28]

Even worse, policies not primarily intended to change behavior—aimed at, for instance, providing greater income security—often nevertheless create perverse incentives for beneficiaries to act in ways that impede opportunity. Many safety-net programs include features that discourage work, marriage, and saving. Policies to mitigate risks often counterproductively generate more risk-taking—the phenomenon known as "moral hazard."

When the federal government expands the provision of goods and services on offer through social policy, it runs the risk of "crowding out" civil society—another potentially counterproductive effect of public policy. Increased reliance on government to address needs weakens the selfish rationale for community members to invest in social capital. Because individual investment in social capital often creates benefits for the entire community, such as norms of trust and reciprocity, the result may be the loss of communal benefits completely ancillary from the goods and services provided by government. Greater subsidy of child care might end up producing less volunteerism.

Any policy agenda to expand opportunity must confront these two constraints: the inadvisability of government intervention in many cases, and its frequent incompetence. However, even with these limitations, public policy can still influence our institutions of civil society in beneficial ways. Most obviously,

government can remove or reform policies that weaken institutions or that promote less desirable alternatives to them. It can also promote the bases for a flourishing civil society: strong families, a stable and growing economy, effective safety nets, and local decision-making. Finally, public policy can facilitate the identification and replication of successful interventions that promote opportunity.

## EXPANDING OPPORTUNITY THROUGH SOCIAL CAPITAL INVESTMENT

The concept of social capital encompasses an enormous amount of social and economic life. A place's social capital reflects the sum of all its relationships—between community members, between individuals and local institutions, and between members and those outside the community. To bound the types of policies under consideration, the Project has identified five broad goals related to opportunity, based on the past two years of its research.

These goals include making it more affordable to raise a family, increasing how many children are raised by happily married parents, connecting more people to work, improving the effectiveness of investments in youth and young adults, and rebuilding civil society.

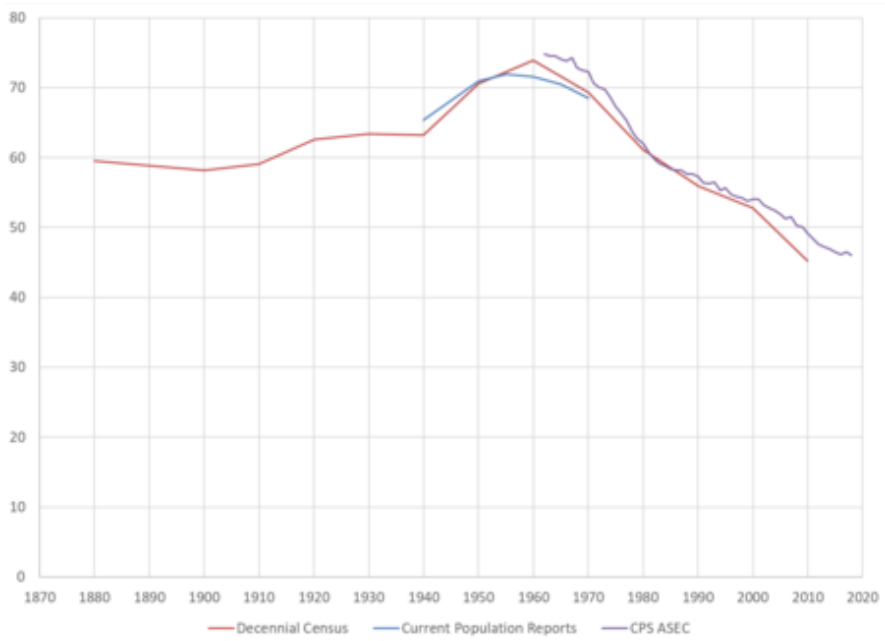
*Making It More Affordable to Raise a Family*

The most important source of social capital for most people is the family in which they are raised. As Yuval Levin has eloquently expressed, the "middle layers" of society—between the individual and the state—"begin in loving family attachments." From this base, the middle layers

> spread outward to interpersonal relationships in neighborhoods, schools, workplaces, religious communities, fraternal bodies, civic associations, economic enterprises, activist groups, and the work of local governments. They reach further outward toward broader social, political, and professional affiliations, state institutions, and regional affinities. And they conclude in a national identity that among its foremost attributes is dedicated to the principle of the equality of the entire human race.[29]

When families are unhealthy or diminishing in number, the social capital effects ripple across our other relationships and civil society, reducing happiness, hurting opportunity, and exacerbating inequalities. In particular, if a large or growing number of men and women cannot afford to start or expand a family in line with their preferences, that represents a profound loss that merits national attention.

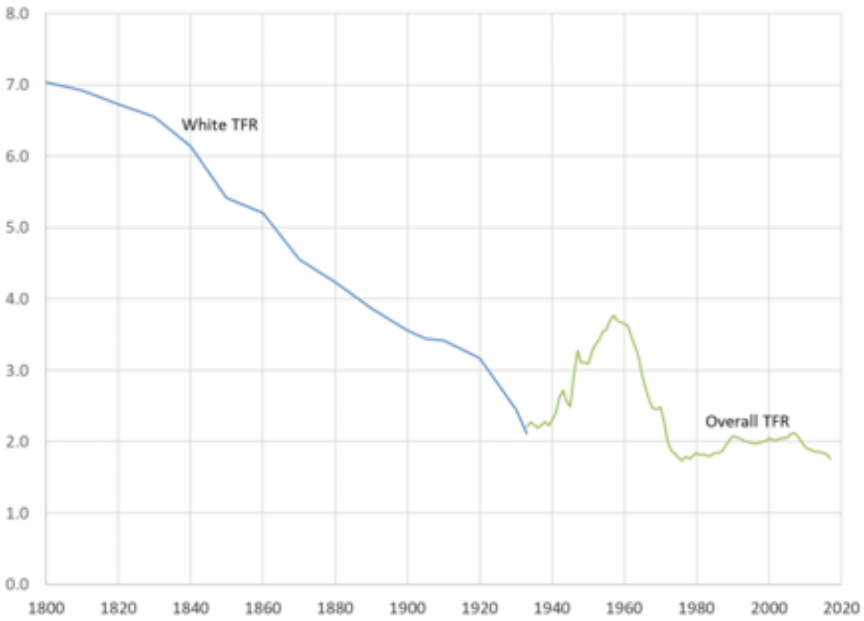
Figure 1. Percent of Women Married, 1880-2018




Source: Social Capital Project analyses.[30]

Both marriage and fertility have declined dramatically since the mid-20th century. The share of women married peaked around the mid-1950s (Figure 1), and marriage rates for single women have fallen steadily since 1950.[31] Fertility began falling in the late 1950s (though from a relative peak, since fertility was much higher for most of the 19th century—see Figure 2).

Figure 2. Total Fertility Rate, 1800-2017




Source: Social Capital Project analyses.[32]

Do these trends reflect a long-term increase in the cost of raising children? Or perhaps a deterioration in personal finances that has made fewer people—in particular, fewer men—marriage material? Has adequately-sized housing become prohibitively expensive? Has student loan debt scared off would-be newlyweds? If these explanations are behind the fall in marriage and fertility, then our economy would be deeply implicated.

However, the timing of these changes suggests a different explanation. Marriage and fertility both fell during the 1960s, a period of robust income growth for Americans of all walks of life. The steepest declines in both came before 1980. While marriage rates have continued to fall, the total fertility rate was 1.79 in 1977, and 40 years later, it was 1.77.[33] These trends are inconsistent with accounts focused on economic decline since the 1980s.

An alternative explanation that better fits the timing is that increased educational attainment and employment among women led to later and fewer marriages and births. Female labor force participation rose throughout the 20th century, but the sharpest rise came in the 1970s, when both marriage and fertility were rapidly declining.[34] The share of women getting four-year college degrees began to accelerate in the mid-1960s and the share in graduate school sharply rose after 1970.[35]

This historical development has expanded opportunity for women greatly. However, because men did not choose to take on more of the burden of home- or community-making, the shift has also weakened our associational life.[36]

That, in turn, likely has made it more difficult to raise a family. Because there are fewer stay-at-home parents today, two-worker families have increasingly had to rely on more formal (and expensive) child care arrangements. Because the workplace has not better accommodated two-worker families, their increasing number has led many to feel they face an inescapable time crunch. Long work hours and commutes lead to less family time at home.

Meanwhile, families that might prefer the traditional breadwinner/homemaker model may find they must sacrifice other wants to do so, as the dual-income families bid up the price of housing, health care, higher education, and other expenses. Many traditionalists will find their preferences unattainable.

Falling marriage (paired with an increasingly generous federal safety net) has also contributed to an explosion in single-parent families, which tend to be poorer than their two-parent counterparts.

If this story about the declining affordability of raising a family is correct, then policy should address the highest costs of raising a family while accepting that we are unlikely to return to mid-20th-century levels of marriage and fertility. It should focus in particular on lower-middle class, working class, and poor families, and it should not marginalize or penalize families wishing to pursue the traditional sole-

breadwinner model. Policy should also consider ways to increase family time. It should promote two-parent families and discourage single-parent families (see below). This story of changing family affordability, more so than the story of economic deterioration, also highlights the importance of choices and trade-offs. No one has a right to form their ideal family on their ideal schedule, and it is unreasonable to expect other taxpayers or employers to pay the cost of doing so.

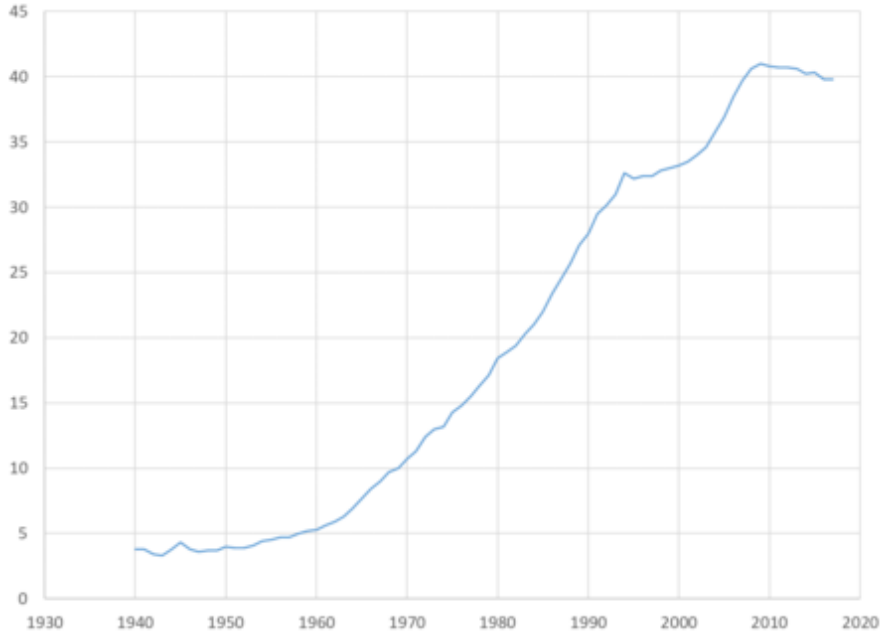
A third explanation for falling marriage and fertility combines the first two, asserting that economic deterioration is *behind* the increase in work among women. This explanation sees rising female labor force participation and infers that wives have had to bail out their husbands due to their falling wages and employment. While the timing of the changes in educational attainment, work, marriage, and fertility—and the broad pervasiveness of these changes across rich countries around the world—offer little support for this story, it, too, would call for bold policy reforms to address economic problems that apparently have been plaguing the developed world for half a century.[37]

Has it become less affordable to raise a family, or is it just too expensive for too many people, regardless of the change over time? Who faces affordability problems? Which of the three stories about the decline in marriage and fertility is right? And above all, what should be done to help Americans who cannot afford the family that they desire? The Social Capital Project will pursue these questions over the coming months.

*Increasing How Many Children are Raised by Happily Married Parents*

Partly because marriage has declined—including shotgun marriages following unplanned pregnancies—the share of children in married-parent families has steadily declined over the past 50 years.[38] In 1967, 88 percent of children were living with two parents, but that number had fallen to 69 percent by 2017. Half of children today will experience at least some time living without both parents.[39] The share of births that were to unmarried women rose from 5 percent in 1960 to 40 percent in 2017 (Figure 3).[40]

Figure 3. Share of Births to Unmarried Women, 1940-2017




Source: Social Capital Project analyses.[41]

There are good theoretical reasons to think that growing up with a single parent is, on average, disadvantageous for children. And indeed, hundreds of studies find that on just about every outcome, children who grow up with single parents do worse than children who grow up with married parents.[42]

However, the problem is that we do not know how today's grown children of single parents would have done if their parents had been induced, somehow, to marry or stay married. In fact, different forms of inducement would have affected different families. It is not reasonable to assume—as most social science research does—that the children of parents who would have been nudged to marry would later have the same outcomes as we see in the real world among the children of married parents.[43]

Consider identical twin studies, which compare the children of twin sisters, where one twin is married while the other is single. As in other studies, the children raised without a father present tend to do worse than those with two parents. This difference, by design, holds constant everything twin parents share in common (including all of their genes).

However, what we want to know is not how the children of the married twins compare with the children of the single twins, but how much better or worse the latter would have done with their father present. The married and single twins differ in some regards, as do their partners. Those differences might have affected child outcomes. We cannot simply assume that the single twins' children would have done as well as their cousins if only their fathers had been around.

At the very least, it seems reasonable to believe that if the single twins and their partners would have had marriages as happy as those of the married twins and their partners—with all of the benefits that would have brought to their children—they would have chosen to get or stay married. Alternatively, if they would have experienced high or even elevated conflict as a consequence of a nudge-induced marriage, their children might have done worse than they did in the real world raised by a single parent.[44]

The key is having *happily* married parents. We don't need to determine how well the academic literature estimates the typical effect on children of growing up with a single parent. We only need to stipulate that children generally are happier, healthier, and better prepared for life when they have two happily married parents rather than a single parent.

They get to see both parents every day, spend the holidays with both, and they don't have to feel guilty about spending or enjoying more time in one household than the other. Nor do they have to question whether they caused their parents to break up. They have a single set of household rules, a single bedroom and wardrobe. Their schedule does not depend on which parent they are staying with. They get engagement from both parents and avoid hearing parents acidly complain about each other. Their parents are less exhausted by childrearing. They get the material benefits of economies of scale and of higher family income. They are witness to what a loving relationship looks like and have first-hand evidence that such relationships are secure and sustainable. And they avoid having to adjust to the changing romantic lives of their mother or father—changes which can include disruptive remarriages and family-blending.

It is easy to see how much more valuable family social capital is likely to be in such families than in disrupted families. And in terms of community social capital, the Chetty-Hendren-Friedman team has uncovered suggestive evidence that being surrounded by more single-parent families can also hurt upward mobility independently of whether they grow up with both parents themselves.[45]

From a policy perspective, then, we want more children in happy married-parent families. That is subtly different than simply minimizing the share of children in single-parent families, and it stands in contrast to being indifferent about the kinds of families in which children are raised.

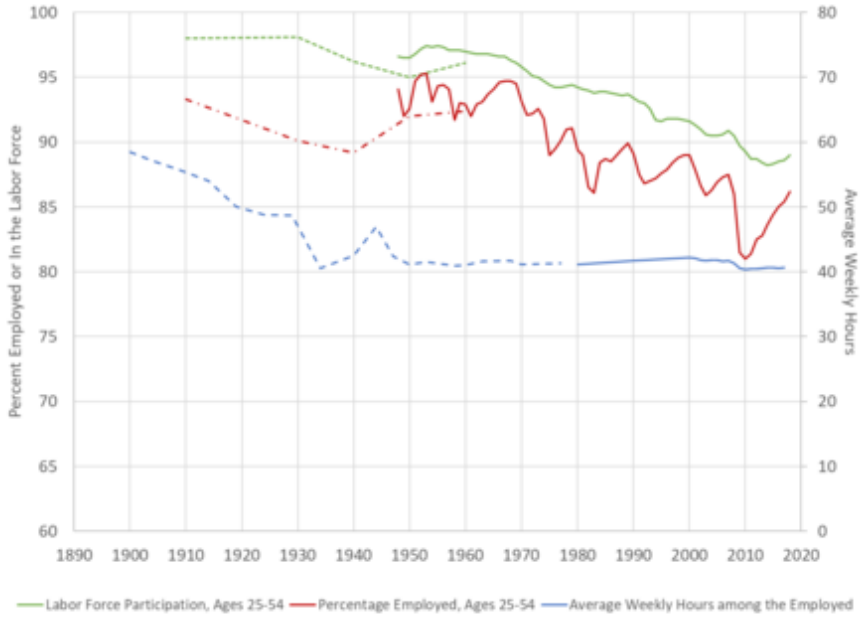
How to achieve this goal depends on knowing how we got here, where and among whom the two-parent ideal has receded, and how much we should blame economic hardship versus cultural change or the unintended consequences of public policy. It could entail a variety of strategies: fostering the conditions that lead to more happy marriages; assisting fragile families so that differences and conflicts may be effectively cooled and ultimately resolved; preventing unintended pregnancies; improving men's economic prospects to make them more "marriageable;" or removing penalties in the tax code

and in safety net programs that discourage marriage among those who would otherwise wed. We will explore these and other policy approaches during the rest of this Congress.

*Connecting More People to Work*

Accounts of rising single parenthood that emphasize economic decline tend to focus on trends in men's wages but also on the decline in the share of working-age men who have a job. This fraction has been falling since the late 1960s, driven by the decline in the share of men who are even looking for work. The top lines in Figure 4 show that the share of men ages 25 to 54 who were employed or actively looking for a job ("in the labor force") fell from 97 percent in 1953 to 89 percent in 2018.

Figure 4. Employment, Labor Force Participation, and Weekly Hours among Working-Age Men, 1900-2018




Source: Social Capital Project analyses.[46]

Should we worry about the decline in male labor force participation? Many observers fear that it reflects a deteriorating national economy. However, it is notable that labor force participation among working-age women soared 35 percent in 1948 to 77 percent by 1999, and it was still at 75 percent in 2018.[47]

Moreover, a number of studies find that relatively little of the decline in labor force participation can be attributed to men who have given up on finding a job or who say they want a job.[48] The biggest part of the story involves men who indicate they are disabled when asked in household surveys. Despite the attention given to the recent increase in mortality (driven by the opioids crisis)[49], most evidence

indicates that over the past 50 years, health has improved and work has become both less physically arduous and more accommodating of disabled employees.[50] Meanwhile, it has become both easier to qualify for federal disability benefits and more financially attractive to try.[51]

Indeed, one possible read of Figure 4 is that the decline in labor force participation is simply the latest manifestation of rising national affluence. The two lowest lines in the chart display average weekly hours worked for employed adult men. In 1900, that average was over 58 hours, but since the Great Depression it has hovered around 41 hours (except for an upward blip during World War II). Without rising productivity, it is unclear that workers could have won a 40-hour work week by the 1930s. Since the early 1950s, rather than a further decline in the work week, the nation has seen more and more working-age men opting out of employment—either temporarily or permanently. That may reflect higher earnings among wives, more generous federal safety nets, or reduced expectations of support from nonresident fathers on the part of single mothers who have earnings, government benefits, or both.

But even if declining work might not primarily reflect problems with the economy, it still should concern us. Arguing that falling labor force participation "is of a piece with the broader turn away from community in America," *New York Times* columnist Ross Douthat warns that

> the decline of work carries social costs as well as an economic price tag. Even a grinding job tends to be an important source of social capital, providing everyday structure for people who live alone, a place to meet friends and kindle romances for people who lack other forms of community, a path away from crime and prison for young men, an example to children and a source of self-respect for parents.[52]

Concurring, social analyst and incoming Manhattan Institute president Reihan Salam notes that family ties are weakening, worrying that, "those who find themselves disconnected from the world of market work find themselves socially isolated along many other dimensions."[53]

Social Capital Project research on "disconnected men" confirms these fears.[54] Compared with employed men, men out of the labor force are more socially isolated and less happy.[55] In our study, they believed more than employed men that they were left uninvited to do things by others, that they would have a hard time finding someone to help them with a move, that they had no one with whom to share their worries, and that they lacked anyone to turn to for advice related to personal problems. They were less likely to be married, to live with adults, or to live with children, and they were more likely to be divorced. Men out of the labor force were more likely to have ever been depressed and to have attempted suicide. The worse their score on an index of mental health, the less likely they were to have someone with whom they could confide in.

In addition to widespread reports of poor physical and mental health, our report turned up suggestive evidence that past incarceration and the threat of child support collection were additional employment challenges.

In future reports, the Social Capital Project will assess the causes of declining work and propose policies to reverse the decline. The goal should not be to increase employment rates indiscriminately, which would conflict with our interest in enabling more parents to afford to stay at home while their spouse works, if that is their preference. Nor should we be concerned about non-workers if they are enrolled in school or have enough resources to retire.

Rather, we will focus on idle able-bodied men and women. Our proposals will seek to reverse the deadening social disconnection that is subsidized by work-discouraging federal benefits, inflicted by government regulations that price many people out of employment, and exacerbated by economic policy that limits job creation and wage growth.

*Improving the Effectiveness of Investments in Youth and Young Adults*

If the families into which we are born made no difference to our adult outcomes, then poor children would be as likely as rich children to become well-off adults. For instance, one in five children raised in the poorest fifth would make it to the top fifth in adulthood, and one in five children raised in the top fifth would stay there. In reality, as few as one in 33 poor children rises to the top fifth, and two in five children starting at the top remain there as adults.[56] Almost half of poor children (46 percent) end up in the poorest fifth of adults.

As children age into adults, we tend to assign more responsibility to them for their outcomes. But what are we to make of this fact: entering kindergartners who are in the bottom fifth of socioeconomic status typically lag their peers in the top fifth on math test scores by the equivalent of 19 points on an IQ test?[57] And how are we then to feel about that gap still being the equivalent of 13 points between high school seniors who have a parent with a graduate degree and those whose parents did not graduate from high school?[58]

Such inequality of opportunity calls out for attention from policymakers of all ideological stripes.

Unfortunately, we have failed monumentally to narrow these gaps over time. In fact, they have remained essentially unchanged over at least 50 years.[59] Rossi's metallic laws of evaluation would predict nothing more; most of the social interventions we have tried have disappointed time and again.

For example, the Department of Education's What Works Clearinghouse has evaluated 385 different interventions designed to affect skills acquisition and behavior.[60] Of these, only 44 (11 percent) showed clear positive effects, meaning that the research was sufficiently strong and there was no contrary evidence

worth considering.[61] Another 54 (14 percent) were examined by multiple studies and showed "potentially positive effects," meaning that it was supported by a preponderance of the evidence, though that evidence might be less rigorous than the best study designs and some of it might fail to find effects. Another 25 percent of interventions showed potentially positive effects but were only examined by a single study.

In contrast, 41 percent of the interventions were deemed to have "no discernable effects," 3 percent had "potentially negative effects," and 5 percent had "mixed effects." This sampling of interventions is, unfortunately, likely to produce too optimistic a conclusion, since the vast majority of interventions are never studied, and those that are generally seem promising to begin with. Furthermore, studies finding positive effects of interventions routinely fail to replicate.[62]

One response would be to throw up our hands in defeat and live with a reality in which some children bear artificial weights on their shoulders as they attempt to traverse a path of laudable pursuit littered with debris.

We think Lincoln would throw a variety of strategies at the problem, and we think the strategies most likely to succeed will increase the effectiveness of investment in youth and young adults by parents and institutions outside the family. That is, we are most interested in strategies to increase the value of the social capital available to young people.

Over the course of this Congress, the Social Capital Project will explore ways to strengthen parents' ability to invest in their children. The policies we consider related to family affordability and family cohesion will be relevant for this policy goal. Other possible reports might promote residential mobility (to elsewhere within a local community or to a different part of the country), assess policies to expand educational choice, or highlight promising interventions that seek to improve parenting skills. Some of these interventions—such as programs that deliver information via text messaging—might be considered "social capital hacks," aimed at circumventing relationship-intensive strategies that are difficult to replicate or scale up.

The Project will also consider ways to improve the quality of investments provided by institutions outside the family. Many such institutions—schools being the most prominent—offer programs seeking to expand the opportunities of youth and young adults, to build their skills, and to alter their behavior. We are particularly interested in mentoring programs, which leverage relationships in an intensive way, as well as apprenticeships and other school-to-work programs. And since inequality of opportunity, as evidenced by test score gaps, appears early in life, we will pay close attention to early childhood interventions as well.

Often, our research will simply shine a light on private efforts that are succeeding, in order to encourage other private organizations to follow their lead. Other times, we may recommend local experimentation, potentially

federally funded. Given the low rate of success that social programs have demonstrated, however, government must evolve to emphasize more evidence-based policymaking—requiring evaluation of publicly-funded programs and strict accountability. Programs that cannot be shown to be effective should, quite simply, be shut down.

A variety of public and private organizations are compiling data on "what works" (and what doesn't).[63] It is not far-fetched to imagine someday having the equivalent of the Congressional Budget Office or Joint Committee on Taxation "scoring" social policy legislation in terms of the likely effectiveness it will have in achieving its intended goals.

We will also consider ways that policy might encourage a greater role for the private sector in funding interventions and discovering what does and does not work. Social impact bonds provide one model, where private organizations fund an intervention with the understanding that they will be paid a dividend by a governmental partner if the intervention produces public savings. If the intervention fails, the taxpayer loses nothing. Income share agreements offer a similar model, whereby private investors partially fund the costs of college in exchange for an agreed-upon portion of a student's future income. Income share agreements transfer risk from students to investors, and given the current problems with the student loan system, they could be attractive to many undergraduates.

There are any number of ways to increase the value of social capital accessible to youth and young adults through parental and institutional investment in them, and policymakers should be open to all of them.

*Rebuilding Civil Society*

In our flagship report, "What We Do Together," the Social Capital Project documented long-term declines in the health of American associational life along a number of dimensions.[64] Membership in a church or synagogue is down, as is attendance at religious services. Union membership has plummeted. Social interaction with neighbors and coworkers has declined. Rich, middle class, and poor are less likely to live alongside each other. Trust in our fellow man has eroded, along with trust in federal and state government, policymakers, and the media. Confidence in organized religion has fallen, as has confidence in banks, newspapers, big business, organized labor, and the medical system.

In short, our institutions of civil society have weakened and withered, and our relationships have become more circumscribed. Political polarization has deepened at the same time, increasingly taking a regional form that pits coastal cosmopolitans against heartland traditionalists. And, not unrelatedly, policymaking has become more concentrated in the federal government.

Rebuilding civil society will require a fundamental change in how we perceive policymaking. It will require policies that respect the strengths of localism while accounting for its weaknesses. That is to say, they must promote *subsidiarity*. Subsidiarity is a concept from Catholic social thought that recommends that if something can be more effectively done at a smaller, more local, and less centralized level than at a larger, more distant, and more centralized level, it should be.

Subsidiarity has a number of advantages. It leverages local expertise and relationships rather than relying on far-off and impersonal bureaucracies. It allows a diversity of solutions to respond to a diversity of situations across the country instead of relying on one-size-fits-all approaches handed down from the federal government. By giving more responsibility to local residents and institutions, it provides valuable roles to community members they might otherwise lack.

Further, by encouraging participation in local groups, subsidiarity provides us with firmly rooted identities, nurturing self-worth. That reduces the likelihood that people will cement their identities to non-local groups based on ideology or ethnicity that reinforce social and political polarization. By keeping decision-making and political authority at the local level, subsidiarity avoids the polarization that results when regional cultural polarization collides with federal politics. Finally, it forces local residents to interact to govern themselves, which then creates communal benefits. These benefits constitute social capital enjoyed by the whole community—strong institutions, dense and active social networks, and norms that encourage reciprocity and promote opportunity.

Unfortunately, there is a chicken-and-egg problem here for those who want to rebuild civil society through subsidiarity. Strong institutions, dense and active social networks, and norms of reciprocity themselves may be prerequisites for successful localism. But government (and markets) have crowded out civil society over the years, by serving specific needs that civil society used to fulfill (be they income support or personal services). By reducing social interaction, the number of groups to which we might belong, and what we get out of both, crowd-out has further debased our social capital beyond its taking over specific responsibilities. Members of “communities” have become less and less so. As a consequence, simply reintroducing responsibilities to civil society may fail. It may no longer be up to the task. Our social capital muscles may be severely atrophied.

It is not just—or even primarily—encroachment by the federal government that has reduced our need for civil society. Affluence has made social relationships less necessary, and as a result, we have chosen to invest less in them and more in our own happiness as individuals (happiness as we perceive it anyway). Affluence has allowed us to outsource the responsibilities we used to have toward one another to impersonal institutions, including the federal government, the personal service sector, private insurance and consumer credit companies, and the educational system. Affluence is also reflected in technological development,

which has allowed us to maintain relationships with far-flung friends and family as we de-prioritize getting to know our neighbors better.

In particular, affluence made greater female labor force participation possible by improving the ability of women to control their fertility as well as by making paid child care affordable and increasing household productivity to the point where homes could be maintained even with both husband and wife working for pay. These developments resulted not only in less home-making, but less community-making, because husbands did not take on the roles that wives increasingly turned away from. Affluence also made single parenthood more viable, as a generous-enough safety net came to substitute for fathers.

As if the challenges of rebuilding civil society were not enough, localism has shortcomings to which policy should attend. Some places are poorer than others, which means residents will need more help even as their state or locality is the least able to provide it. Relatedly, the business cycle creates problems for states and localities, which often have limited options for financing their costs through deficit spending during recessions. Furthermore, in competing to attract business or in trying to avoid attracting too many needy residents, states and localities may face various kinds of "races to the bottom." They may spend wastefully to bring in employment or stingily tighten the purse strings of safety-net spending.

Another problem for localism is that compared with a powerful federal government, states and localities may not be able to stand up to non-local business interests or dominant local businesses, which may exercise undue political power. Finally, sometimes federal policies can be superior to local ones—more effective (at running Social Security), more efficient (less inclined toward land use regulations or occupational licensing), or more just (in enforcing civil rights).

The Social Capital Project intends to think creatively about how policy—including federal policy—can rebuild civil society. First, federal policy can strengthen local institutions. It can leverage existing institutions and refrain from impeding their efforts. In particular, it can reduce barriers to church-based service provision using federal funds. It can also devolve more authority to local institutions in administering federal programs, and it can reduce its involvement in policies that could be better pursued locally. Policy can offer incentives for donations of time or money to local institutions. And it can create new institutions, such as worker co-ops that could provide portable benefits to employees.[65]

Policies at different levels could also promote trust in a community (restoring trust in police, for example, within minority communities), or they could promote pro-social norms, pro-opportunity norms, or information-sharing (about, for instance, job demand and availability). They could seek to increase social interaction, through investment in "social infrastructure" that brings people together (including libraries, parks, and shopping malls).[66] Policies could even attempt to influence patterns of social interaction by, for example, discouraging land use regulations and zoning that segregates by income (and inefficiently drives up the cost of living).

Finally, federal policies could counteract the problematic aspects of localism. The federal government could provide a limited degree of federal redistribution between rich and poor states. It could encourage individual savings so that states' residents aren't dependent on federal taxpayers during downturns. And it can ensure a baseline of civil rights protections to guard against the threat of discrimination.

By finding ways to rebuild local institutions of civil society and revive social interaction at the local level, the Social Capital Project hopes to catalyze a virtuous cycle of reinvestment in social capital to fulfill more and more needs—the mirror image of the vicious cycle that has incapacitated our ability to accomplish things with fellow members of our community.

## CONCLUSION

Social capital is a form of wealth to which policymakers have devoted too little attention. The benefits we get from it are as diverse as information, identity, financial and emotional support, and culture. It is the stuff of which life is made.

An important product of social capital is opportunity—opportunity to pursue whatever individual priorities we may hold dear. Public policy should aim to expand opportunity and to temper inequalities of opportunity. An important way it can do that is by strengthening families, communities, and civil society.

In the coming months, the Social Capital Project will release a series of reports—one for each of the five policy goals outlined above—providing an overview of the goal, outlining the nature of the policy problem, and summarizing different approaches to achieving the goal. With these complete, the Project will then issue a series of analyses and recommendations related to specific policy approaches. These narrower reports will sometimes recommend federal policy proposals in greater or lesser detail. Other times, they will suggest appropriate state and local policies. Still other reports will suggest actions that private organizations might take or highlight successful private efforts to address a policy goal. The result will be a coherent policy agenda to expand opportunity by shoring up families, communities, and civil society.

This agenda will necessarily be incomplete, but it should offer a policy menu of sufficient variety to appeal to policymakers with a range of priorities. It will, hopefully, inspire others to think more creatively about investment in social capital and how public policy might make us wealthier not just financially, but in terms of our relationships with each other.

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4. Other examples of institutions: fraternal organizations, arts centers, community gardens, farmers' markets, parades, festivals, block parties, museums, libraries, local businesses, and local governments.
5. For criticism of the concept see Steven N. Durlauf (2002). "On the Empirics of Social Capital." *The Economic Journal* 112(483): F459–79.; Steven N. Durlauf and Marcel Fafchamps (2004). "Social Capital." Working Paper No. 10485, National Bureau of Economic Research. http://www.nber.org/papers/w10485.; Michael W. Foley and Bob Edwards (1999). "Is It Time to Disinvest in Social Capital?" *Journal of Public Policy* 19(2): 141–73.; Alejandro Portes (1998). "Social Capital: Its Origins and Applications in Modern Sociology." *Annual Review of Sociology* 24: 1–24.; Joel Sobel (2002). "Can We Trust Social Capital?" *Journal of Economic Literature* 40: 139–54.
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12. Ibid, xiii.
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16. Chetty et al. (2014) referred to it as "absolute mobility," but a subsequent paper redefined that term to mean "having a higher income in adulthood than one's parents."

17. These correlations are estimated across aggregations of counties called "commuting zones." However, in one of their most recent papers, the Chetty-Hendren team finds strong correlations across census tracts—broadly, neighborhoods—between single parenthood and upward mobility. Raj Chetty, John N. Friedman, Nathaniel Hendren, Maggie R. Jones, and Sonya R. Porter (2018). "The Opportunity Atlas: Mapping the Childhood Roots of Social Mobility." Working paper.

18. Scholars have generally viewed the study of family structure as distinct from social capital research, but examining the nature of intra-family relationships should be seen as an inquiry into social capital.

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20. Raj Chetty and Nathaniel Hendren (2018a). "The Impacts of Neighborhoods on Intergenerational Mobility I: Childhood Exposure Effects." *Quarterly Journal of Economics* 133(3): 1107-1162. Raj Chetty, Nathaniel Hendren, and Lawrence Katz (2016).

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26. Similar research looking at other outcomes would be invaluable, and it is increasingly possible thanks to the data that the Chetty-Hendren-Friedman team have assembled. Their team, for instance, found that communities with higher scores on the social capital index and fewer children with a single mother actually have lower life expectancy among the poor people living there. (This study looks at the community of residence in adulthood rather than in childhood, however.) See Augustin Bergeron, Raj Chetty, David Cutler, Benjamin Scuderi, Michael Stepner, Nicholas Turner (2016). "The Association Between Income and Life Expectancy in the United States, 2001-2014." *The Journal of the American Medical Association* 315(4): 1750-1766. https://jamanetwork.com/journals/jama/fullarticle/2513561?guestAccessKey=4023ce75-d0fb-44de-bb6c-8a10a30a6173. Correlations are population-weighted and estimated by the Social Capital Project using data from the Opportunity Insights website (https://opportunityinsights.org/data/?geographic_level=0&topic=0&paper_id=573#resource-listing).

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30. The 1880-2010 trend is for women ages 18-54 and comes from the 1% samples of the decennial censuses, analyzed via the Integrated Public Use Microdata Series Online Data Analysis System, http://sda.usa.ipums.org/cgi-bin/sdaweb/hsda?harcsda+all_usa_samples. See Steven Ruggles, Sarah Flood, Ronald Goeken, Josiah Grover, Erin Meyer, Jose Pacas, and Matthew Sobek (2019). *IPUMS USA: Version 9.0* dataset (Minneapolis: University of Minnesota). https://doi.org/10.18128/D010.V9.0.

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43. This is a problem even conditioning on fairly gross demographic and economic characteristics, as research tends to do, which presents other methodological problems at any rate.

    The same problem recurs if we consider a different counterfactual and compare children born to unmarried parents to the *different* children who would have been born if the parents could have been nudged to delay fertility until they were married (potentially to other people).

    There is a symmetric problem with establishing the outcomes of children who grow up with two-parents under the counterfactual that their parents were induced to not marry or to divorce. Different inducements would affect different families. Moreover, it is unlikely that the real-world outcomes of the children of single parents are a good guide to the outcomes we'd see among the children of happily-married parents if a father or mother were somehow removed from the picture. The closest example we have to a randomized experiment is when a parent dies unexpectedly, but the effect of having a parent die on child outcomes is unlikely to resemble the effect of going through a parental divorce, for example. (And parental death is generally not random, being at least somewhat predictable from various demographic and economic factors.)

44. This issue generalizes to all social science inquiries involving human choice. It is very likely that the human subjects in a study have a better sense of what is best for them (or in this case, their children) than does the researcher observing them as data points.

45. Chetty et al. (2014) report that the correlation between a community's share of children with a single parent and its upward mobility was -0.76 and was still as strong as -0.66 if they estimated a community's mobility only from the children of married parents. Chetty, Friedman, Hendren, Jones, and Porter (2018) report that the correlation across neighborhoods between the share of single parent households

and upward mobility was -0.59, and it remained as strong as -0.52 if they only looked at the children of single parents. That is, even among the children of single parents, upward mobility is lower when there are more single parents in a tract. And as noted above, Chetty, Hendren, Jones, and Porter (2018) found that black men had stronger upward mobility the more low-income black fathers there were in their childhood neighborhood, regardless of whether or not their own father was present.

46. Percentage employed and labor force participation rate: From 1910 to 1960, estimates are for non-institutionalized men ages 25 to 54 who are not in the Armed Forces, and they come from the 1% samples of the decennial censuses, analyzed via the Integrated Public Use Microdata Series Online Data Analysis System, http://sda.usa.ipums.org/cgi-bin/sdaweb/hsda?harcsda+all_usa_samples. See Steven Ruggles, Sarah Flood, Ronald Goeken, Josiah Grover, Erin Meyer, Jose Pacas, and Matthew Sobek (2019). From 1948 to 2018, estimates are for the civilian non-institutionalized population of men ages 25 to 54, and they come from the Labor Force Statistics Database available at https://www.bls.gov/cps/.

    Average weekly hours: From 1900 to 1977, estimates are for employed men not in school, from John Owen (1976). "Workweeks and Leisure: An Analysis of Trends, 1948-1975." *Monthly Labor Review* 99(8): 3-8; John Owen (1988). "Work-time Reduction in the United States and Western Europe." *Monthly Labor Review* 111(12): 41-45. Both cited in Robert Whaples (2001). "Hours of Work in U.S. History." EH.Net Encyclopedia, edited by Robert Whaples. http://eh.net/encyclopedia/hours-of-work-in-u-s-history/. From 1980 to 2017, estimates are average usual weekly hours worked for employed men, and they come from the 1% samples of the decennial census and from the American Community Survey, analyzed via the Integrated Public Use Microdata Series Online Data Analysis System, http://sda.usa.ipums.org/cgi-bin/sdaweb/hsda?harcsda+all_usa_samples. See Steven Ruggles, Sarah Flood, Ronald Goeken, Josiah Grover, Erin Meyer, Jose Pacas, and Matthew Sobek (2019).

47. Ibid.

48. For a discussion, see U.S. Congress, Joint Economic Committee, Social Capital Project (2018). "Inactive, Disconnected, and Ailing: A Portrait of Prime-Age Men Out of the Labor Force." Report prepared by the Vice Chairman's staff, 115th Cong., 2nd Sess. (September 2018). https://www.jec.senate.gov/public/index.cfm/republicans/2018/9/inactive-disconnected-and-ailing-a-portrait-of-prime-age-men-out-of-the-labor-force.

49. On the opioids crisis, see U.S. Congress, Joint Economic Committee, Social Capital Project (2018). "The Numbers Behind the Opioids Crisis: Revised Utah Edition." Report prepared by the Vice Chairman's staff, 115th Cong., 2nd Sess. (October 2018). https://www.lee.senate.gov/public/_cache/files/4d849598-7f80-49a4-aa7f-5492ae5b8d90/the-numbers-behind-the-opioid-crisis-revised-utah-edition-final.pdf; and U.S. Congress, Joint Economic Committee, Social Capital Project (2017). "The Rise in Opioids Overdose Deaths." https://www.jec.senate.gov/public/index.cfm/republicans/office-of-the-vice-chair?ID=105269F4-5054-4B87-9ABF-40E5CB77E8B7.

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57. Assuming the standard deviation of the IQ test scores is 15 points. The math score gap between low and high socioeconomic status kindergartners entering school in 2010 was 1.25 standard deviations. See Emma Garcia and Elaine Weiss (2017). “Education Inequalities at the School Starting Gate: Gaps, Trends, and Strategies to Address Them.” (Washington, DC: Economic Policy Institute). https://www.epi.org/files/pdf/132500.pdf.

58. The math score gap between the children of parents with less than a high school education and the children of parents with graduate degrees is 0.882 standard deviations in 2015. See the NAEP Data Explorer tool at https://www.nationsreportcard.gov/ndecore/landing.

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# Rebuilding Civil Society

# The Space Between:

## Renewing the American Tradition of Civil Society

SCP REPORT NO. 8-19 | DECEMBER 2019

### INTRODUCTION: THE AMERICAN TRADITION OF ASSOCIATION

In the fall of 1727, a dozen young men—most of them tradesmen and artisans—began meeting on Friday evenings at the Indian Head Tavern in Philadelphia. They met to debate philosophy and current events and to exchange information and resources in the name of "mutual improvement."[1] They called themselves the "Junto Club" and were led by an ambitious, twenty-year-old printer. His name was Benjamin Franklin.

The Junto Club was part of an early response to the end of conventional, European systems of patronage and to the emergence of a dynamic commercial order driven by impersonal markets. Tradesmen increasingly turned to private institutions and to each other for mutual aid and credit.[2] Under Franklin's leadership, however, the Junto Club would not only support its members. It would go on to establish many of the landmark institutions of colonial Philadelphia: the first subscription-based lending library in British North America, Pennsylvania's first volunteer fire brigade, the American Philosophical Society, the Academy of Philadelphia (later the University of Pennsylvania), and the nation's first charity hospital.[3]

The practices that Franklin popularized in colonial Philadelphia not only made the "City of Brotherly Love" worthy of its name. They have continued throughout the history of the United States. For more than two centuries, Americans have organized themselves voluntarily to address their common problems. Many of the most consequential social movements in the United States, from abolition to temperance to civil rights, have been outgrowths of the American instinct to associate. It is one of American society's most striking qualities.

During his visit to the United States in 1831-2, Alexis de Tocqueville marveled at the associative patterns of American society. In the first volume of *Democracy in America*, he observed that,

> Americans of all ages, all conditions, all minds constantly unite. Not only do they have commercial and industrial associations in which all take part, but they also have a thousand other kinds: religious, moral, grave, futile, very general, and very particular, immense and very small; Americans use associations to give fêtes, to found seminaries, to build inns, to raise churches, to distribute books, to send missionaries to the antipodes; in this manner they create hospitals, prisons, schools. Finally, if it is a question of bringing to light a truth or developing a sentiment with the support of a great example, they associate. Everywhere that, at the head of a

> new undertaking, you see the government in France and a great lord in England, count on it that you perceive an association in the United States.[4]

Instead of patrons, Americans sought peers. In this bottom-up, participatory form of civic action, Tocqueville found that the institutional form of association could "fix a common goal to the efforts of many men."[5] American associations acted in lieu of government and private industry; they provided a place for the exercise of freedom, secure against external intrusion and individuals' atomizing tendencies and dedicated to the proposition that a whole could be greater than the sum of its parts. Above all, they instructed citizens in the art of self-government, instilling the democratic habits necessary to maintain the American republic.[6] In sum, associations provided the space between government and markets in which Americans, and the communities they formed, could flourish.

Tocqueville, however, saw associations as not merely useful or beneficial for democracy, but essential to it. Association alone was responsible for the myriad functions of a democratic society: "[T]he progress of all the others depends on the progress of that one."[7]

Even in our twenty-first-century American society, associational life ought to be at the center of thinking about our social order and public policy. As discussed in "The Wealth of Relations," the Social Capital Project is focused on expanding opportunity by revitalizing families, communities, and civil society.[8] This report is an overview paper for one of the five policy areas identified as a priority: rebuilding civil society. It lays out the nature of our diminished civil society, documents trends in its decline, and charts a path to its renewal.

### *Understanding Civil Society*

What we today call "civil society" is a descendent of the tradition that Franklin modeled and Tocqueville observed. Indeed, many of the institutions that are conventionally thought to compose civil society resemble those very associations that were so important in early America—churches, charities, unions, fraternal organizations, and the like. The instinct to collectively address common problems has not disappeared.

In important respects, however, American civil society has evolved over the last two centuries. Its organizations have become more professionalized and its associations less participatory as administrative responsibilities have shifted from local volunteers to headquartered professionals.[9] The result has been a change in the character of organizations. Their scope of interest often transcends local problems with the rise of international development and transnational non-governmental organizations. Membership less often entails leading a chapter meeting than merely writing a check or skimming a newsletter.[10] The *raison d'être* for civil society may not have changed, but its institutional form has evolved from a site of proximate community into a more tenuous web of communications and transactions.

*What Is Civil Society?*

To appreciate fully the scope and character of these changes requires a clearer sense of what "civil society" means. It can be a difficult concept to untangle. Though but a single term, it has been imbued with several distinct meanings: some structural, some functional, and some normative.[11]

Structurally, civil society constitutes a kind of "third sector" within society. It exists independently of both government, or the "public sector," and the market, or "private sector." This is not to say that the State and industry do not affect civil society. Non-profit organizations secure funding from government agencies and corporations, and they are shaped by public policy and the business cycle. Conceiving of civil society as a structurally independent third sector, however, helps to highlight these interactions with the public and private sectors and emphasize a distinct purpose of civil society: to secure public goods that the market and the State fail to provide.

Structural independence enables civil society to serve a distinct functional role as a set of "mediating institutions." In *To Empower People*, Peter L. Berger and Richard John Neuhaus described civil society as comprising "those institutions standing between the individual in his private life and the large institutions of public life."[12] Institutions—the durable social arrangements we create together to achieve common goals in the course of interacting with one another—are "instituted" for a variety of reasons. The mediating institutions "mediate" by securing for the individual a space for participation, membership, and belonging within the broader society. Where it may be impossible for an individual to directly shape, meaningfully participate in, or fully belong to mass society and its larger institutions—say, global commodities markets or the federal government—civil society provides its own institutions—schools, churches, clubs, and charities—to which one may belong and be an active participant. In this way, civil society is thought to prevent individuals' estrangement and alienation from mass society.

In addition to this functional role, civil society also serves a normative purpose: the transmission of particular habits, values, and norms. As the bipartisan Council on Civil Society has reported, the "essential social task" of the myriad associations that compose civil society is to "foster competence and character in individuals, build social trust, and help children become good people and good citizens."[13] This is most obviously seen in those institutions with explicitly pedagogical purposes, such as schools and churches. Nearly all associations, however, are organized around a particular vision of the good, and their members—be they volunteers in a charity, elected leaders in a fraternal organization, or congregants in a house of worship—are bound by this shared vision. Through participation and leadership, members of civil society are habituated in observing their shared values, cooperating with their fellow men, and ultimately in practicing self-government.

Each aspect of civil society is integral to its role in society and, in particular, its role in expanding opportunity. Its structural independence as a "third sector" helps

to highlight how the actions of government or the market affect its institutions. Its functional role as a set of mediating institutions underscores how it forms individuals' relationships with the rest of society. Its normative purposes illustrate how it shapes the habits and character of entire communities.

Civil society is both integral for social health and irreplaceable by the market or the State. It comprises institutions that facilitate what we do together beyond the home. Though often formed to provide material support and mutual aid, its principal contributions to society are immaterial. As articulated in the Social Capital Project's inaugural report, "What We Do Together," civil society holds our common life together by supplying "extended networks of cooperation and social support, norms of reciprocity and mutual obligation, trust, and social cohesion" and by "forming our character and capacities, providing us with meaning and purpose."[14]

### *Civil Society and Opportunity*

While a vibrant civil society may be an essential part of a healthy community, it also has an important role to play in expanding economic opportunity for all Americans. Indeed, civil society has the power to transform low-income neighborhoods into opportunity-rich communities. A burgeoning social science literature has highlighted the relationship between civil society and upward mobility.[15] For instance, economist Raj Chetty and his colleagues at Harvard University's Opportunity Insights have found strong, positive correlations between local community strength and the outcomes of children, especially low-income children, in adulthood. In particular, they found that the presence of civic associations, religious institutions, and non-profit organizations—as captured in social capital indices—is closely associated with higher rates of upward mobility.[16]

Even as research reveals its precise effects on economic opportunity, we understand intuitively the ways in which civil society can shape the lives and outcomes of low-income Americans. Every institution is guided by a statement of purpose: to provide shelter, afterschool care, cultural enrichment, or political activism. This is the means by which the institutions of civil society promote opportunity. Though not all organizations offer services that directly boost economic prospects—such as job training or tutoring—nearly all of their services are designed to meet a need. In that way, civil society as a whole contributes to the expansion of opportunity. Because civil society thrives in places where it meets a material need, it has the largest role to play in places where material needs are greatest.

Beyond the direct provision of material aid, the institutions of civil society act both as bridges to opportunity and as sites of character formation and instruction. These two-fold roles reflect the two different forms of social capital discussed in the academic literature: *bridging* and *bonding* social capital.[17]

In the first sense of *bridging* social capital, institutions help to cultivate relationships between people who may not otherwise meet but for their common

membership in an organization. Indeed, civil society—particularly its most participatory forms—serves as a locus of community life.[18] It increases social relationships and interactions, even across traditional lines of social segregation. Members develop relationships with those alongside whom they worship, compete, serve, learn, and work. Such patterns of social interaction are conducive to exchanging information and building trust, the social ingredients that may open doors to new opportunities, networks, and resources.

In the second sense of *bonding* social capital, institutions form and shape their members. Through formal rules and expectations or through informal peer pressure, active membership cultivates pro-social and pro-opportunity norms—such as honesty and reliability, perseverance and prudence, responsibility and reciprocity—that are difficult to acquire elsewhere. It also prepares individuals for more active participation in other spheres by socializing them and building non-cognitive skills. These qualities redound to a person's social mobility because our economy and society tend to reward such qualities. Membership in civil society is not a quick fix for opportunity, but rather a future-oriented investment that pays dividends in the long term.

If "the leading object" of the federal government, as Abraham Lincoln maintained, is "to elevate the condition of men" and "to afford all an unfettered start and a fair chance in the race of life," then the health of civil society ought to be considered a priority of public policy.[19] Civil society is an expansive concept, and its benefits extend beyond the confines of particular institutions, generating positive externalities for the wider community. For the purposes of public policy, however, civil society's narrower, opportunity-building effects should not be sacrificed for the sake of such broadly shared benefits—the alleviation of material want, the security of membership, the restoration of local authority and control. Civil society may exist for all, but it is especially vital for those individuals and communities with the fewest prospects and the greatest need.

### *The "Hollowing Out" of Civil Society*

Despite the scope of civil society, its actual force seems to have diminished. As the Social Capital Project reported in "What We Do Together," the United States' associational life and institutional health are in decline across a range of indicators.[20]

Though precise causes of the decline are difficult to delineate, it is at least partially attributable to the expansion of government, which evolved to serve specific needs that civil society used to fulfill. The dynamic occurred as early as the Great Depression when New Deal policies—namely social insurance and welfare—drove down faith-based charitable activities. An estimated 30 percent of charitable spending by churches and other faith-based organizations was "crowded out" by New Deal policies.[21] Empirical study of more recent public policy demonstrates that so-called "crowd-out" effects are a common feature of government spending and

programs.[22] The inverse dynamic also appears, such as increased church activity following a decrease in government expenditures.[23]

Yet government alone is not responsible for displacing civil society. The dynamism and innovation of the free enterprise economy have rendered membership in associations both less necessary and less desirable. As early as the 1930s, fraternal organizations witnessed a decline in membership that was caused, in part, by the emergence of commercialized insurance. Many of the early fraternal organizations, such as the Knights of Columbus, initially formed to provide life insurance to men whose life expectancies, due to dangerous occupations and poor healthcare, were shorter. Despite their discrete, original purpose, fraternal organizations expanded their activities and mission into charity, education, and other forms of mutual aid. Once the essential function was undertaken more cheaply and efficiently by business, however, the fraternal organizations lost their initial purpose and immediate appeal to working men and women.[24] Mutual aid is a product of necessity; once the need is satisfied elsewhere, only interest can keep a person attached.[25]

The crowding out of civil society by expansive government and markets is not entirely bad. It is partly a trade-off of rising American affluence that enables us to "outsource the responsibilities we used to have toward one another" as reported in "The Wealth of Relations."[26] The convenience and efficiencies gained have, in many respects, contributed to Americans' material well-being and sense of happiness; however, they have made the institutions of civil society less immediately important in American life. As sociologist Robert Nisbet observed, institutions "must seem important [...] but to *seem* important, they must *be* important [emphasis in original]" —which is to say, *necessary*.[27]

Such trends portend what might be called a "hollowing out" of civil society. In many cases, the physical structures that house associations—sanctuaries, lodges, meeting halls, and the like—have become literally hollow as membership declines. Meanwhile, as fewer Americans belong to civil society, we risk losing the shared norms and values supplied by it. In this sense, civil society could become figuratively hollow as well, its normative purpose losing cultural resonance. Tocqueville warned against this possibility even as he marveled at the vibrant associational life in America:

> The task of the social power will therefore constantly increase, and its very efforts will make it vaster each day. The more it puts itself in place of associations, the more particular persons, losing the idea of associating with each other, will need it to come to their aid: these are causes and effects that generate each other without rest.[28]

The ultimate consequence of the dynamic of crowd-out generating hollowing out was dire. Without associations, Tocqueville maintained, "civilization itself would be in peril."[29]

## THE STATE OF MEDIATING INSTITUTIONS

The extent to which civil society produces pro-social outcomes depends, of course, on Americans' relation to it. The Social Capital Project envisions at least four mediating institutions that can be renewed and better used either to address problems in lieu of government or to partner with government—especially local government—in the pursuit of common policy goals: neighborhoods, churches, schools, and voluntary associations. The Project also considers philanthropy to be a critical support reflecting the health of these institutions.

This section assesses the health of civil society, using survey data to measure Americans' levels of confidence and participation in its institutions and fundamental support system. In conjunction with relevant social science research, the data reveal how different institutions have evolved through time and how the American experience of associational life varies by demographics. As we endeavor to rebuild civil society, these findings should help us to chart a path forward.

### *Neighborhoods*

In *To Empower People*, Berger and Neuhaus wrote that "[t]he neighborhood should be seen as a key mediating structure in the reordering of our national life."[30] The neighborhood, as a mediating institution, involves a dimension of togetherness beyond oneself and even one's family. It is where we associate with those one-time strangers who become, in their own way, friends. As the Project has written elsewhere, "[t]he communities to which we belong develop the civic skills and social norms that reinforce reciprocity, trust, and cooperation."[31]

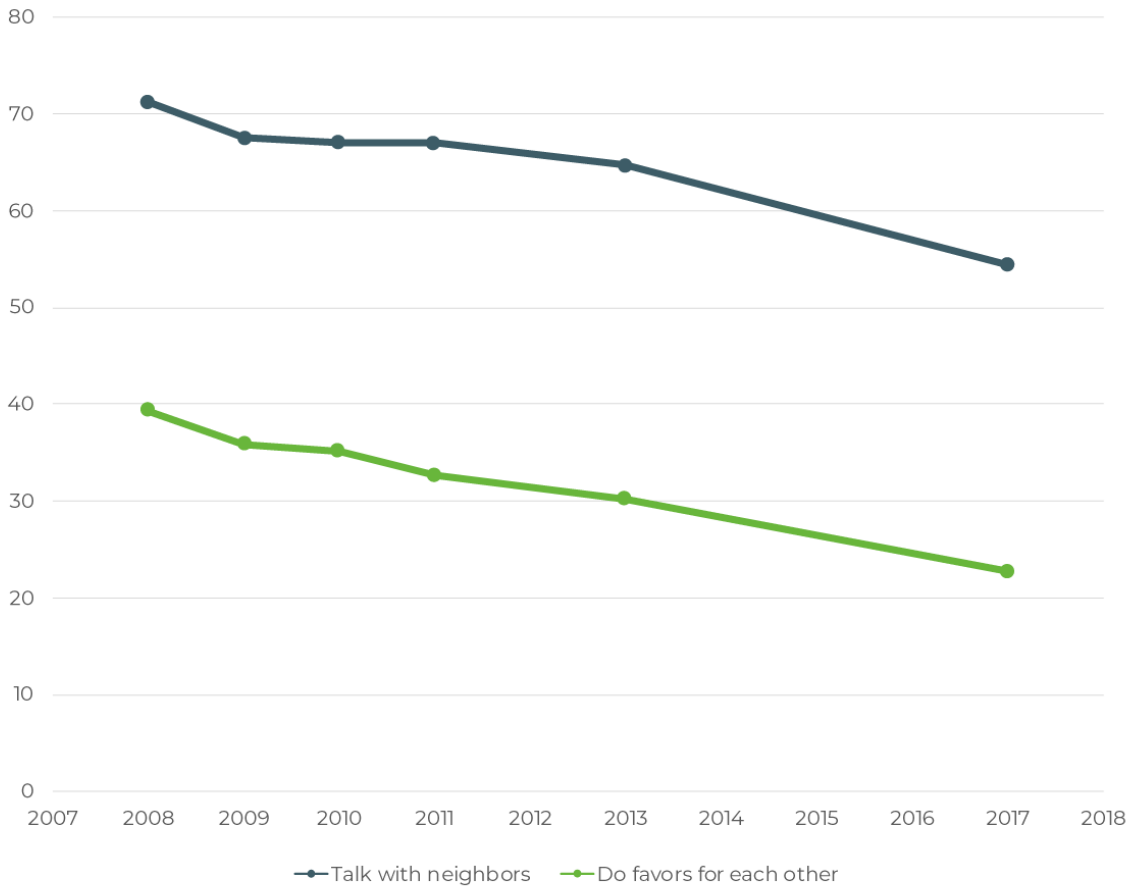
The cohesion of a neighborhood is an important indicator of a healthy associational life. Of course, not all neighborhoods are alike in this respect. The Project's initial report highlighted the advantages that tend to accrue to residents of healthy neighborhoods as well as the disadvantages—often in the form of residential segregation wrought by a toxic mix of policy and prejudice[32]—that other neighborhoods face.[33] The consequences of such underlying disparities for basic building blocks of associational life, such as trust and social interaction, reveal a troubling portrait of the American neighborhood today.

Americans are spending less time with their neighbors than they once did. From 1974 to 2018, the share of adults who reported spending an evening with a neighbor at least several times a month dropped from 44 percent to 29 percent.[34] In addition, since 2008, the Current Population Survey (hereafter, "CPS") has asked about respondents' informal interactions with neighbors, including how often they talk with their neighbors and how often they and their neighbors do favors for each other, such as watching each other's children or lending house and garden tools. From 2008 to 2017, the share of adults who reported talking with neighbors a few times a month or more fell from 71 to 54 percent, and the share who reported doing favors for their neighbors fell from 39 to 23 percent (Figure

1).[35] While members of certain education and racial groups—college-educated and white adults, for example—are more likely to report having these neighborly interactions, the declines are common to members of *all* of them.[36]

Though there are not comparable data further back in time, a 1948 Gallup poll suggests that neighborly interaction was once much more common.[37] Six in ten adults in that survey reported that they lent to or borrowed things from their neighbors. Seven in ten reported that they had them over to their house, and the same share reported that they accepted their packages or took messages for them. Nearly half reported that they did shopping for them. Four in ten reported that they looked after their children. The relatively high levels of neighborliness that we once enjoyed seem to be features of a bygone America.

Figure 1. Percent of adults who have informal interactions with neighbors a few times a month or more




Source: Social Capital Project analysis of CPS Civic Engagement Supplement, 2008-2011 and 2013; CPS Volunteer & Civic Life Assessment, 2017.

The Social Capital Project's past reports have offered reasons for the gradual disappearance of neighborly interactions. In "What We Do Together," the Project partially attributed the decline to falling population density associated with suburbanization.[38] Americans have also retreated over time from public amenities and "third places," such as the local bar, as we increasingly prefer the comfort of our own homes.[39] Advances in technology have encouraged social retreat as well. As the Project wrote in "The Wealth of Relations," technological development "has allowed us to maintain relationships with far-flung friends and family as we de-prioritize getting to know our neighbors better."[40] The rise of social media and other low-cost, in-home entertainment might also explain some of the decline in neighborly interactions over the past decade.

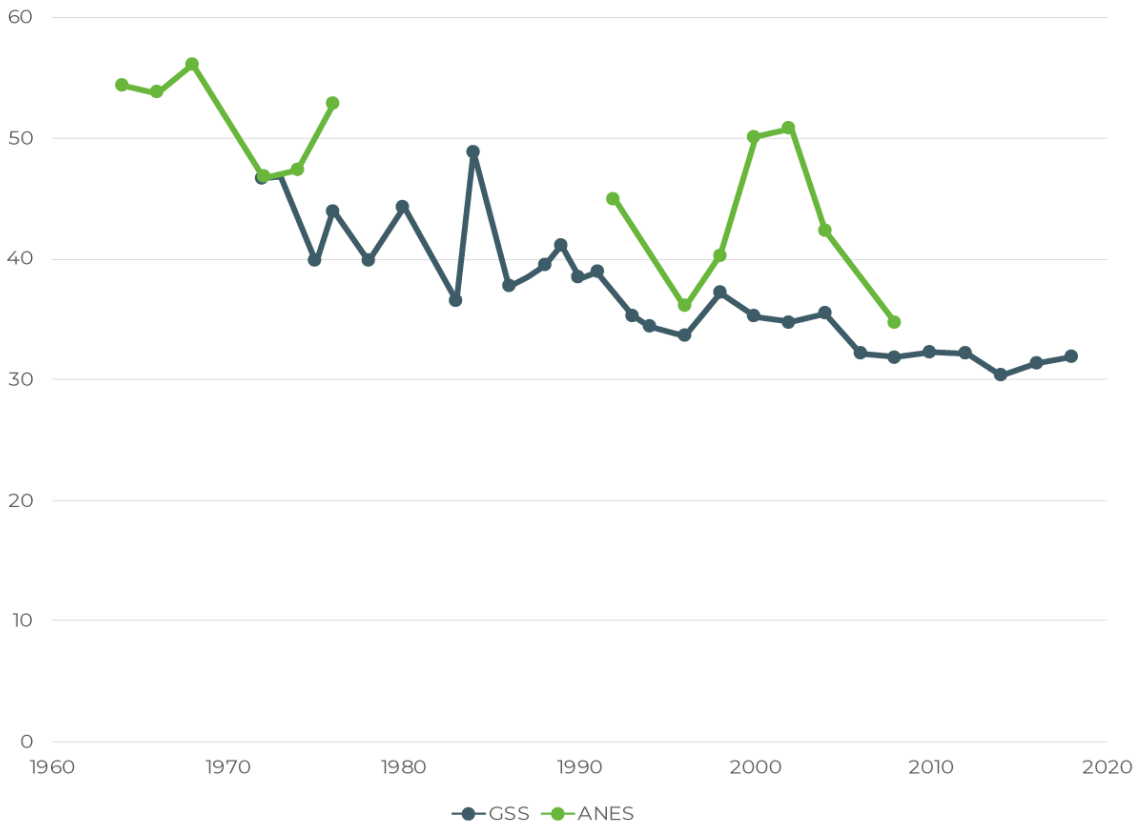
Moreover, we have generally come to rely on our neighbors less as our society has become more affluent and individualistic. Consider the difference between having dinner delivered and planning a dinner with neighbors. Rising affluence has given us greater independence in our everyday lives, but it may have come at a social cost for neighborhoods. Indeed, thinking about how to revitalize neighborhoods as institutions of civil society will require us to confront such trade-offs and reflect on what we value most.

In an earlier report, the Project warned that "[i]f we are connecting less with communities and people who are different than us, we could be more likely to see adversaries among those in whom we might otherwise find a neighbor."[41] There are limited survey data on the degree to which Americans trust their neighbors. The CPS shows that in 2013, 56 percent of adult respondents reported that they trust all or most of the people in their neighborhood. However, neighborhood trust levels vary by demographic group. For example, blacks and Hispanics, younger adults, and lower-income households reported less trust in their neighbors than whites, older adults, or higher-income households.[42] Newer survey data, such as the American Enterprise Institute's Survey on Community and Society, show similar disparities.[43]

We can gain more purchase on the state of trust by looking at trends in "social trust"—measured in survey data as the extent to which people agree that "most people can be trusted." While such measures are not specific to feelings about neighbors, it is likely that feelings of social trust are influenced by how trustworthy neighbors are perceived to be. These survey data show a clear correlation between social trust and self-reported happiness.[44] Research has also linked higher levels of social trust to community-wide benefits such as lower crime rates and greater entrepreneurship.[45] The benefits of social trust for individuals and communities help to explain why the Council on Civil Society argued that building social trust is an "essential social task of civil society."[46]

American civil society seems to be struggling in this regard. Social trust has eroded over the past several decades. In the 1960s, more than half of American adults agreed that "most people can be trusted," but that share had fallen to one-third by 2018 (Figure 2).[47] The decline occurred after social trust probably increased in the decades prior to 1960.[48]

Figure 2. Percent of U.S. adults who agree that "most people can be trusted"

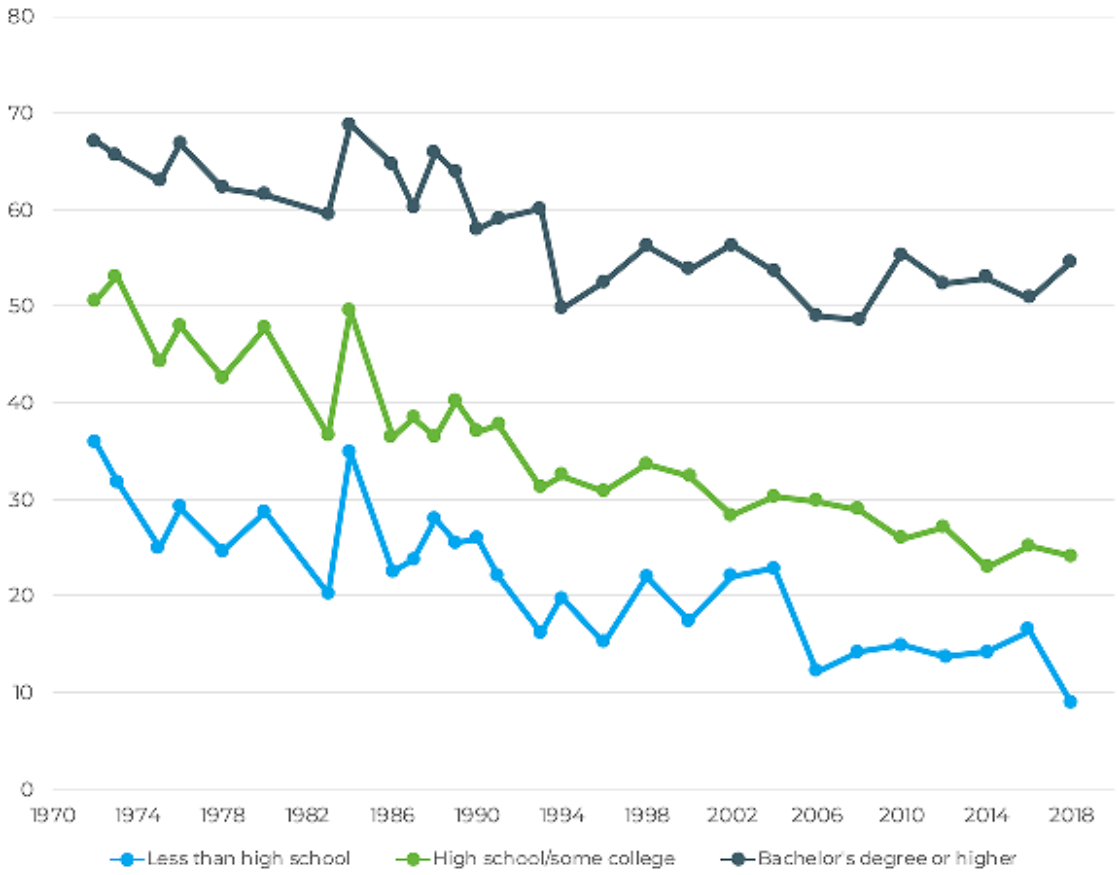



Source: Social Capital Project analysis of American National Election Studies, 1964-1976 and 1992-2008; General Social Survey, 1972-2018.

Because the General Social Survey (hereafter, "GSS") does not contain a continuous measure of household income, educational attainment must serve as a rough proxy and illustrates that levels of social trust vary widely by class. Since 1972, Americans with at least a college degree have reported significantly higher levels of social trust than those with a high school diploma or some college education and those without a high school diploma (Figure 3).

This educational "trust gap" has also widened over time. Although social trust among higher-educated adults has fallen from its 1972 level, it has remained relatively steady since the mid-1990s at around 50 percent or higher. Meanwhile, social trust continues to decline for less-educated adults. From 1972 to 2018, the percentage of adults agreeing that "most people can be trusted" declined by more than half for adults with a high school diploma or some college education, and plummeted from 36 percent to nine percent for those without a high school diploma. Over the same period, the gap in social trust between the college-educated and high school dropouts increased from 31 percentage points to 46 percentage points, or nearly a 50 percent increase.

Figure 3. Percent of adults who agree that "most people can be trusted," by educational attainment




Source: Social Capital Project analysis of General Social Survey, 1972-2018.

One possible reason for the growing disparity in social trust along class lines could be Americans' geographic sorting.[49] One aspect of the problem is "brain drain": the selective migration of the highest-educated residents of some states to a relatively small number of other states.[50] Another is increasing residential segregation within metropolitan areas that leaves the well-educated increasingly clustered in relatively tight-knit, affluent neighborhoods.[51] In other words, the relationship between education and trust could be tied to the social contexts in which people associate.

There also exists a disparity in social trust along racial lines.[52] In recent years, the level of social trust among white adults (39 percent) has been more than twice as high as that among black adults (17 percent) and Hispanic adults (16 percent).[53] These differences are not altogether surprising given America's history of race relations.

The future of civil society seems all the more harrowing in light of our weakened neighborhood ties. The informal networks of support and socialization among households were once a mainstay of American life, their value perhaps only appreciated now in their virtual absence in some places. The proximity of local and state governments, however, may point to a promising avenue for reform. Where trust between individuals is low, local solutions could build more cohesive and vibrant neighborhoods. In some places, that may mean lifting or reforming barriers to development, such as zoning codes, or private activity, such as licensing and registration laws. In others, it may mean directly partnering with neighborhoods to address a common problem as modeled by community policing policies. Regardless of the specific solution, the importance ought to be clear: if we cannot trust or help our neighbors, can we reasonably expect to enjoy fully our associational life?

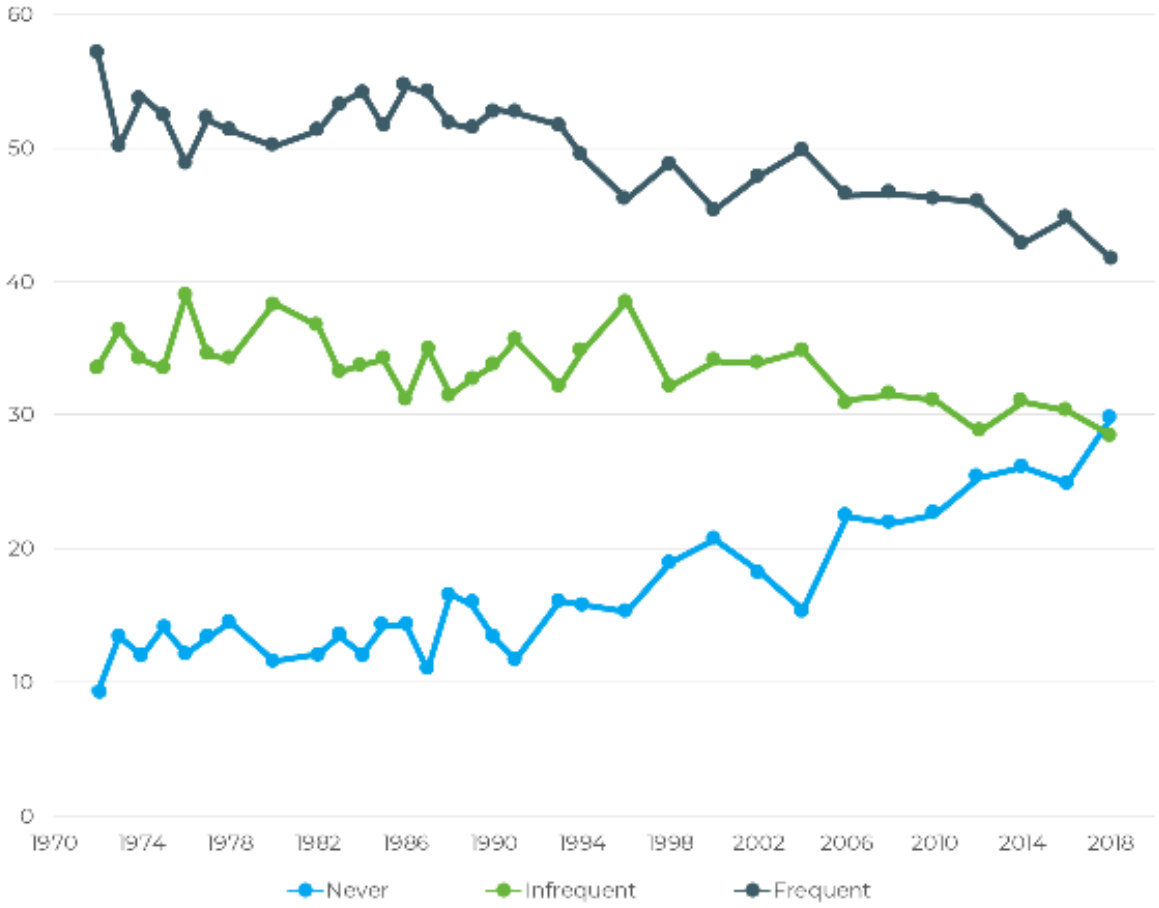
### *Churches*[54]

Churches are perhaps America's most prominent and active mediating institutions. Tocqueville described Americans' religion as "the first of their political institutions."[55] Compared to the rest of the Western world, America continues to be defined and shaped by a relatively robust religious life.[56] Americans who frequently attend religious services tend to be happier, healthier, and better spouses and parents and are more likely to engage in pro-social and community-building activities.[57] They also exhibit higher levels of volunteering, charitable giving, and participation in voluntary organizations than Americans who are less religiously involved.[58]

While much of the research suggests only correlation between active religiosity and positive outcomes, other work has suggested a causal relationship. For example, one study using GSS data finds that living in an area where more people share a particular faith leads to higher levels of religious participation as well as better economic and family outcomes.[59] The benefits of church membership appear to redound not only to attendees but to the larger community. For example, one study found a "halo effect" by which historic sacred places on average generate roughly $1.7 million for their local economies and estimated that 87 percent of the beneficiaries of such places' community programs were not themselves parishioners.[60]

Nevertheless, attachment to religious institutions has eroded over time. From 1972 to 2018, the share of adults who reported attending religious services once a month or more dropped from 57 to 42 percent (Figure 4). Over the same period, the share of adults who reported *never* having attended religious services tripled. If present trends continue, the share of never-attenders will overtake the share of frequent-attenders by 2032.[61]

Figure 4. Religious attendance among U.S. adults




Source: Social Capital Project analysis of General Social Survey, 1972-2018. "Frequent" attendance is defined as self-reported attendance at religious services at least once per month. "Infrequent" attendance is defined as self-reported attendance at religious services less than once per month.

These findings do not necessarily suggest that the most actively religious Americans are becoming detached from religious institutions. Rather, the decline in religious attendance has been concentrated among those with only a nominal attachment to organized religion.[62] GSS and Gallup data suggest that regular, weekly attendance has not changed significantly since the early 1970s, especially among Catholics and mainline Protestants. In fact, frequent attendance has increased among evangelicals.[63] In 2018, however, the share of Americans adults saying they have no religion surpassed both the share of evangelicals and the share of Catholics for the first time.[64]

Growing irreligiosity and deinstitutionalization have affected virtually all demographic groups. In 2014, the Pew Research Center found that

> [r]eligious commitment—as measured by respondents' self-assessments of religion's importance in their lives, frequency of prayer and religious attendance—has declined among men and women, college graduates and those with less education, married and unmarried respondents, people in every region of the country and people with various racial and ethnic backgrounds.[65]

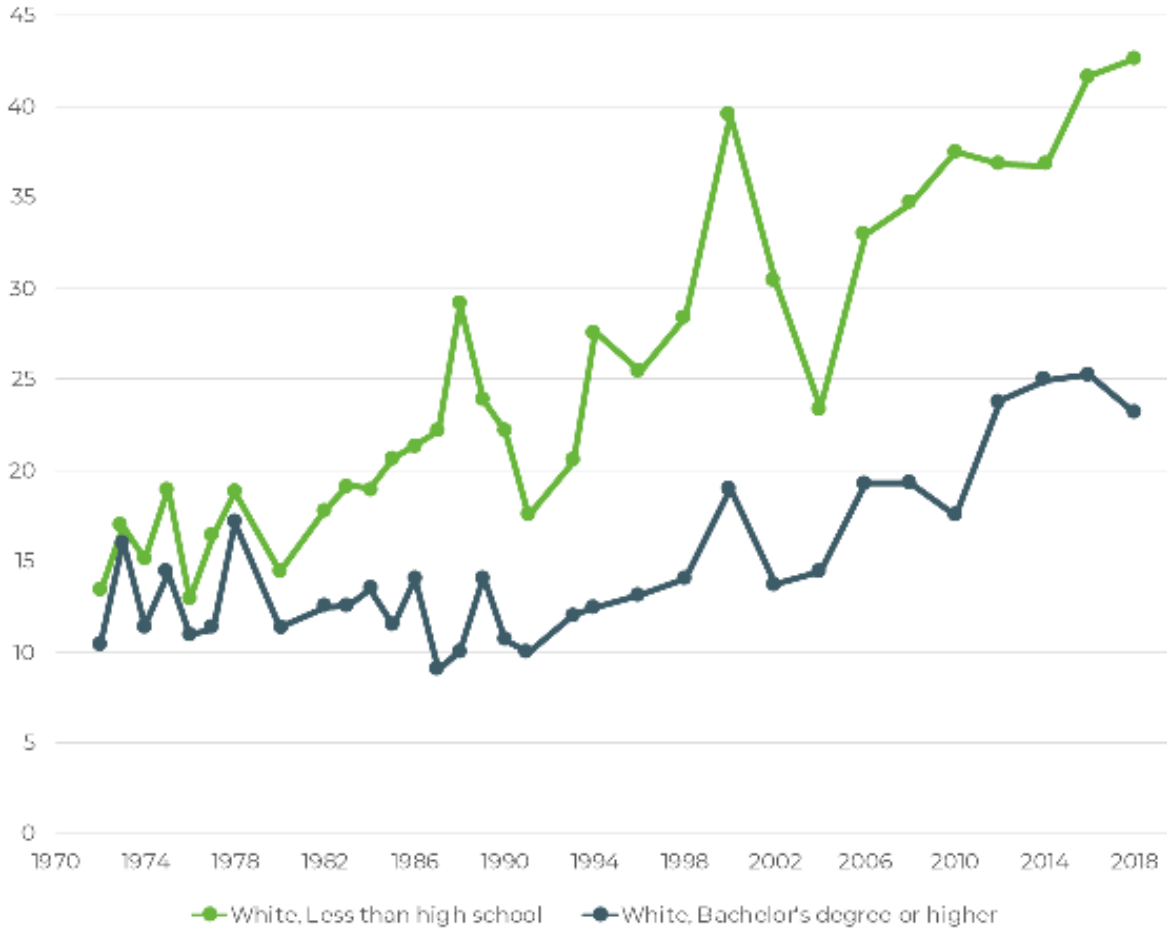
Still, certain groups report greater attachment to religious institutions. For example, monthly religious attendance among blacks (59 percent) and Hispanics (50 percent) has been higher than that of whites (40 percent) in recent years.66 Historically, religious institutions have played a vital role in the black community especially. Black churches served as hubs for volunteering and fundraising during the civil rights movement; indeed, the movement was infused with the language and traditions of black Christianity.[67] Black Protestants are also more likely than evangelicals or mainline Protestants to be involved in their churches beyond mere attendance—whether that be through participation in small groups or service in formal leadership or volunteer roles.[68]

In *American Grace*, Robert Putnam and David Campbell observe that, unlike white adults, black and Hispanic adults exhibit a strong relationship between their ethnic identity and religiosity, which tends to mute any effect on religiosity by education or class.[69] Likewise, sociologist W. Bradford Wilcox and his colleagues note that

> black and Latino religiosity is less likely to be stratified by class, given that churches have been an important vehicle for solidarity, community action, and political activity for blacks and Latinos of varying class backgrounds.[70]

Among white adults, however, there is substantial variation in religious attendance by educational attainment. Differences in the shares of white adults who say they *never* attend religious services demonstrate this most clearly (Figure 5). Among whites in 1972, the gap between the college-educated and high school dropouts who never attended religious services was only three percentage points. By 2018, the gap was nearly 20 percentage points—more than a six-fold increase. Growing religious deinstitutionalization among less-educated whites bodes poorly for their sense of belonging.

Figure 5. Percent of white adults who never attend religious services, by educational attainment




Source: Social Capital Project analysis of General Social Survey, 1972-2018.

While religious attendance is declining for both sexes, women have consistently reported a higher rate of attendance. Meanwhile, there is a paucity of men in the pews for all major U.S. religious groups.[71] Marriage, however, may affect attendance for men. While single men are least likely to report at least monthly attendance at religious services, married men are more likely to report attendance, at levels similar to single and married women.[72]

The focus on religious attendance in this section, as opposed to religiosity per se, is deliberate. It is meant to highlight how churches have declined in their role *as institutions of civil society*. This suggests that churches are operating less as the caches of community and social capital formation than they used to. Moreover, as Americans of all stripes have become more deinstitutionalized

from religion, public confidence in organized religion has waned. Public trust of clergy has fallen considerably,[73] and the share of adults reporting "a great deal" of confidence in organized religion has fallen across all levels of religious attendance since the early 1970s.[74]

There are multiple reasons for declining trust and participation in organized religion. For instance, cultural changes—including the sexual revolution and a greater emphasis on individualism—may have placed evolving values at odds with traditional church teachings.[75] However, the steady breakdown of religious institutions could be attributed to a failure of the institutions themselves, including such self-inflicted wounds as abuse scandals, political polarization, and enculturation.[76] Along the same lines, American churches may have accelerated the move toward secularization, as columnist Ross Douthat has argued, by favoring a more individualist, less community-oriented approach to participation.[77]

The trend of religious deinstitutionalization makes it less likely that individuals and families receive the benefits of membership. Given the complex nature of our society's religious commitments, deinstitutionalization might seem far beyond policymakers' jurisdiction. Of course, public policy cannot fix churches' internal problems. But policy influences the landscape within which churches and faith-based organizations operate, and it often does so in ways that prevent them from participating fully in civil society. Instead, policy should leverage these institutions wherever possible to achieve common goals. If we are concerned about how best to meet human needs, we must not ignore or downplay the role of churches or faith-based organizations in that collective effort.

### *Schools*

For many towns and neighborhoods in America, schools serve as the loci of community life. They often provide the physical places, or "social infrastructure," where people vote, hold community gatherings, or convene for sporting events.[78] In particular, schools that provide social services and other goods beyond the classroom are rightly thought of as "community hubs."[79]

School-related activities facilitate civic engagement and volunteerism that benefit an entire community. Regular school-based community service can improve students' civic skills,[80] and membership in school-based organizations can increase political participation in adulthood.[81] In addition, one study has shown that higher levels of, or increases in, "school social capital"—defined as a sense of belonging, comfort, and happiness in one's school—positively predict civic involvement in adulthood.[82]

Parents also experience civic benefits through involvement in their children's schools. In *Bowling Alone*, Putnam documented how parent volunteers in the U.S. kindergarten movement of the late nineteenth and early twentieth

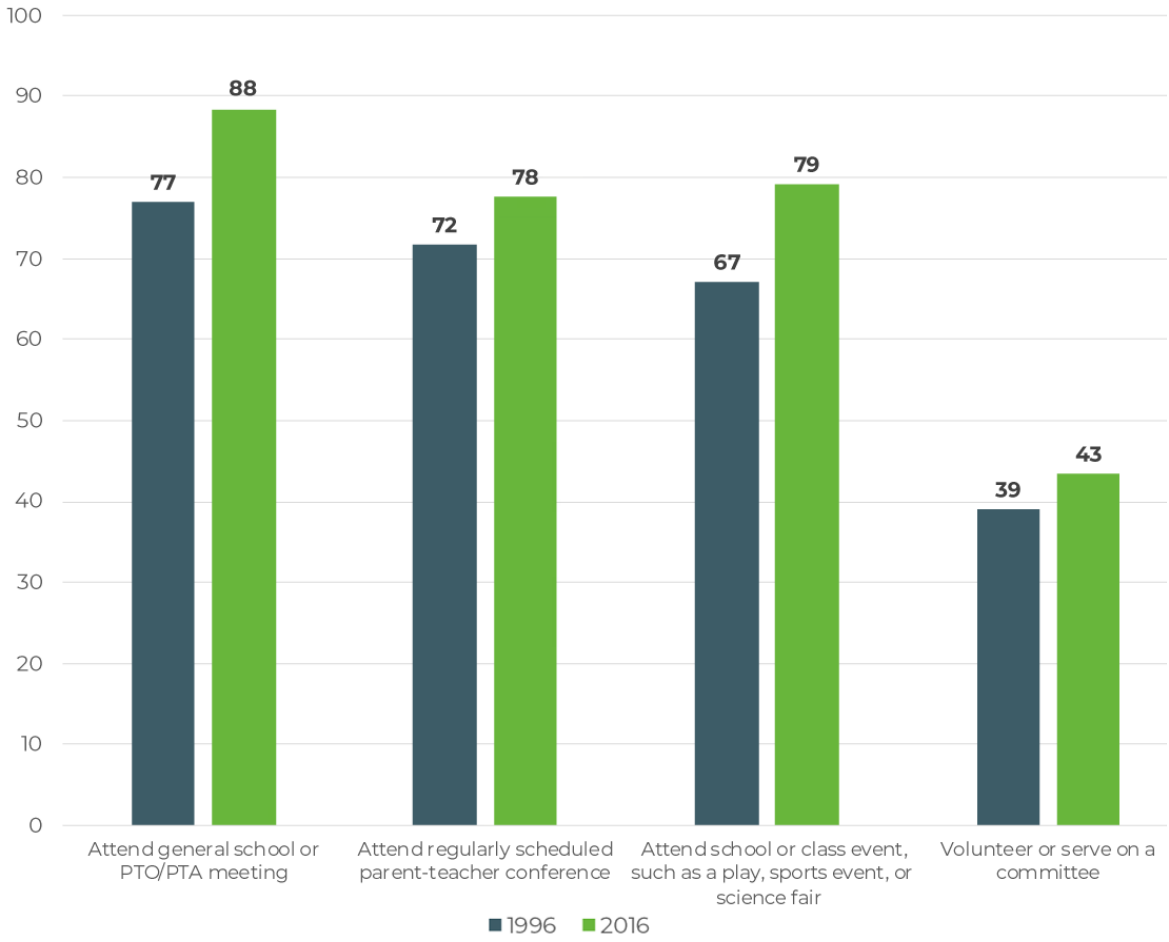
centuries created “an array of new forms of adult connectedness [around the kindergartens]—mothers’ clubs, sewing clubs, and so on.”[83] He described how a hypothetical couple starting a Parent Teacher Association (PTA) chapter at their child’s school can build civic skills and create social ties:

> People who might never have designed a project, given a presentation, lobbied a public official, or even spoken up at a meeting are pressed to do so… [Participation] also allows for the deepening of interpersonal bonds and “we-ness” between families and educators. On a more personal note, the PTA meetings are bound to establish, or strengthen, the norms of reciprocity and mutual concern among parents. These connections will almost certainly pay off in myriad unexpected ways in the future.[84]

Schools with more involved parents tend to have higher school quality, and children there generally have better educational and social outcomes.[85] Catholic schools, in particular, perform better precisely *because* of the embedded parental networks, rather than teacher or student characteristics.[86] Some researchers have suggested that Catholic school closures help to explain why social trust has fallen and crime rates risen in some inner-city communities.[87] Half of all Catholic schools in America have shuttered since 1960.[88]

However, there is reason for optimism. The National Center for Education Statistics has fielded the Parent and Family Involvement in Education (PFI) Survey since the 1990s.[89] The survey data—nationally representative of K-12 students and their parents—show that parents and guardians have become more actively involved in the life of schools over the last two decades (Figure 6).[90] Though parental involvement in some activities has only modestly increased from 1996 to 2016, the findings are still notable because they reflect *greater*, not less, participation in schools.

Figure 6. Percent of parents or guardians reporting participation in select school activities




Source: Social Capital Project analysis of Parent and Family Involvement in Education Survey, 1996 and 2016.

Though participation generally has risen over time across all subgroups, there remains considerable variation between subgroups. Parents of children who attend private schools are more involved than those whose children attend public schools; married parents are more involved than unmarried parents; parents of white children are more involved than parents of black or Hispanic children; and college-educated parents are generally more involved than less-educated parents. It may be the case that many parents wish to participate more in their children's schools but cannot because of inflexible work schedules, demanding time constraints, or other work and family circumstances.[91]

Nevertheless, for parents and their children, schools are increasingly becoming institutions around which associational life is based. Considering the negative trends in other institutions of civil society, the positive trends in parental

involvement are cause for at least some optimism. Enabling more parents to be involved in their children's schools and supporting schools in their many social roles could be ways of strengthening schools' place in civil society. For example, policies giving parents more workplace flexibility could allow greater participation in school functions, while local programs supporting extracurricular activities could bolster schools' function as centers of community life.

### *Voluntary Associations*

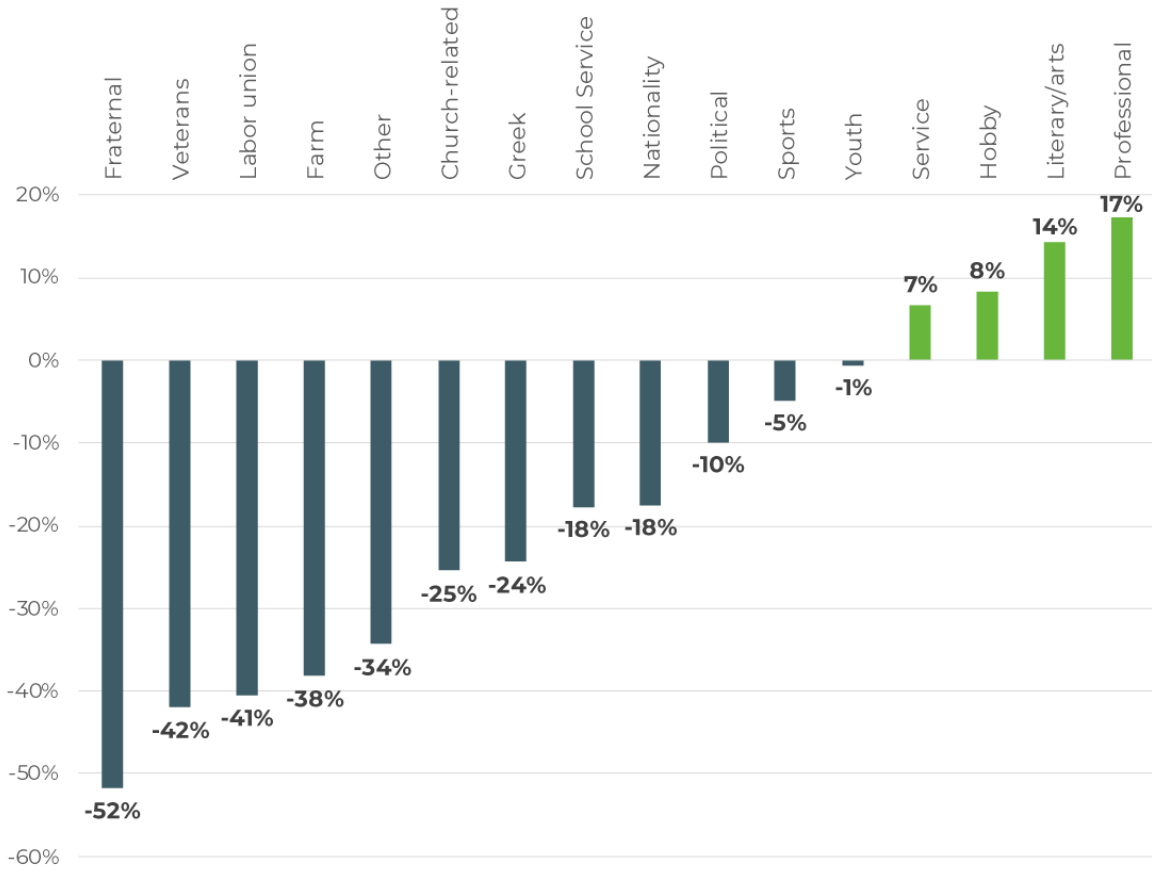
Any portrait of American civil society would be incomplete without a diversity of voluntary associations. These local groups can have wildly different functions and flavors, ranging from Rotary Club to Little League to the Knights of Columbus. A voluntary association is defined by the activity it facilitates: individuals freely meeting and interacting with one another. In Bowling Alone, Putnam distinguished voluntary associations from the "new associationism," noting that

> [t]he proliferating new organizations are professionally staffed advocacy organizations, not member-centered, locally based associations. The newer groups focus on expressing policy views in the national political debate, not on providing regular connection among individuals at the grass roots.[92]

Along with broader communal benefits, voluntary associations provide more tangible benefits even to those not directly involved. For example, from 2007 to 2011, fraternal organizations created an average of over $3.8 billion in benefits to the economy through their charitable and voluntary activities, and provided an average of roughly $500 million in charitable and community assistance.[93]

Voluntary associations, which often comprise local chapters within a larger organization, have been losing ground to national, professionally run organizations. While national nonprofit groups have multiplied over time, membership rates in national chapter-based associations, after increasing for most of the twentieth century, have fallen since the 1960s.[94] Likewise, formal membership in at least one of sixteen types of voluntary associations fell from 75 percent to 62 percent from 1974 to 2004, the most recent year of available data.[95] The decline has been especially pronounced among fraternal organizations, veterans groups, and labor unions (Figure 7).[96]

Figure 7. Percent change in membership rates for select organizational types, 1974-2004

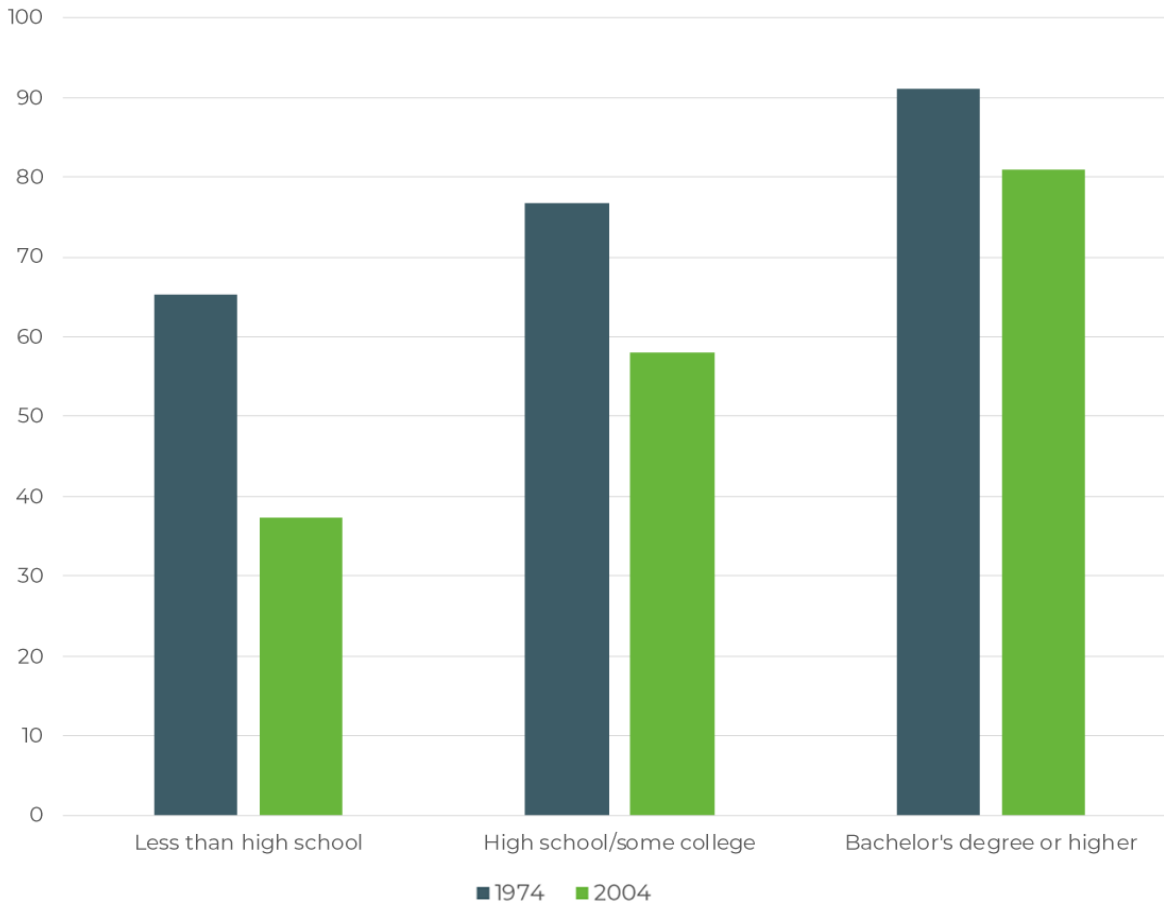



Source: Social Capital Project analysis of General Social Survey, 1974 and 2004. Note that the chart displays percent changes in membership *rates* – that is, the percent of adults who were members of an organization in a given year – and not absolute membership *numbers*.

National chapter-based veterans' organizations, such as the American Legion and Veterans of Foreign Wars (VFW), have waned significantly over the past few decades. For these organizations, the number of posts and members in their local chapters have dropped precipitously since the early 1990s.[97] As fraternal organizations' material functions have become less necessary and individualized alternatives to associational life—often involving technology—have proliferated, their social importance in Americans' daily lives has diminished.

Over time, membership levels have come to be associated with class.[98] Highly educated adults are most likely to report membership in voluntary associations, while membership has eroded among the least educated (Figure 8). A Public Religion Research Institute survey from 2016 found that working-class whites were less involved in voluntary associations than their college-educated peers.[99]

Figure 8. Percent of adults who are members of at least one voluntary association, by educational attainment




Source: Social Capital Project analysis of General Social Survey, 1974 and 2004.

Membership declines are also reflected in falling levels of active participation in voluntary associations. In *Bowling Alone*, Putnam documented several declines in measures of participation through the late 1990s.[100] For example, he found a 50 percent decline in the share of adults who served as an officer or committee member for a local club or organization from 1973 to 1994. From the mid-1970s to 1999, the number of club meetings the average American attended each year fell from twelve to five, and the share of adults who attended at least one club meeting in the previous year fell from 64 percent to 38 percent.[101]

Recent data suggest that these trends have either remained constant since the 1990s or worsened. The Civic Engagement Supplement to the CPS indicates that Americans were slightly more likely between 2008 and 2013 to serve as officers or be on a committee than in 1994, but that was less likely than in the 1970s or early 1980s.[102] Furthermore, just 24 percent of adults in 2008 reported attending a meeting of any group or organization in the previous year.[103] This suggests that,

from the late 1990s to late 2000s, the share of American adults who *never* attended club meetings rose even further—from two-thirds to three-fourths.

As noted above, some reasons for the declines in group membership and participation include crowding out by government programs or commercialized products and services, professionalization of large organizations, and rising individualism. We can see evidence of individualism even in the ways in which people engage. As Putnam notes, "cooperative forms of behavior, like serving on committees, have declined more rapidly than 'expressive' forms of behavior, like writing letters."[104] For his part, Putnam attributed the decline in civic engagement to work-life pressures, suburban sprawl, electronic entertainment, and generational change.[105]

The trend of voluntary associations fading from civil society should worry those who appreciate the inherent value of membership in such social-capital-building entities. Given the variety of causes for this decline, strengthening our voluntary associations, especially among the less-educated, will require a variety of solutions. Policies that reverse crowd-out could ensure that government is at least doing no further harm to these institutions. Other policies that prioritize local ties and expertise, or that encourage participation in voluntary associations, might also help to renew these mainstays of American associational life.

### *Philanthropy*

Charitable giving is generally not considered to be a mediating institution like churches or schools. Nevertheless, it is closely related to civil society, as both a diagnostic indicator and a stimulus, and therefore belongs in any complete portrait of American civil society.

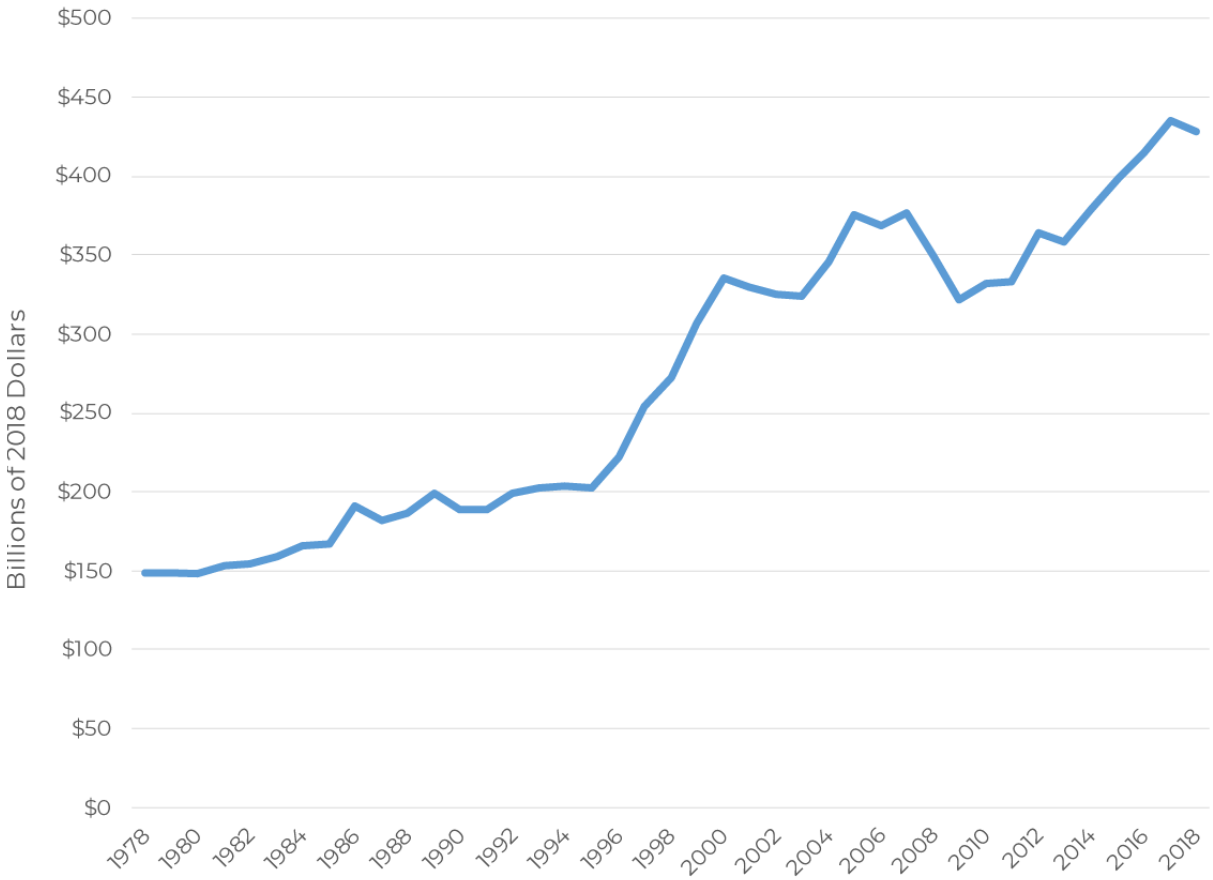
Because networks of interdependence tend to encourage charitable giving, philanthropy provides an additional lens through which to diagnose the health of civil society.[106] "Altruism," Putnam writes, "is an important diagnostic sign of social capital"—a thriving philanthropic sector, in other words, suggests that civil society is thriving as well.[107]

Philanthropy also serves as a stimulus, as it supports the institutions that create valuable social capital. Philanthropy funds civil society, providing direct financial support to social-capital-building organizations. Such support is particularly important when government is the only alternative funding source. When people support philanthropic causes themselves, government has less reason to do so, reducing the risk of crowd-out. Moreover, a vibrant philanthropic culture can strengthen norms and behaviors that tend to promote a healthier associational life, such as volunteering and cooperating. As Katherine Toran summarizes, "The consensus of empirical study seems to be that [donations of time and money] are complements: those who give more monetarily are also more likely to volunteer their time, and when the tax price of donations falls, gifts of time increase

alongside gifts of money."[108] Financial support of civil society may thus also bolster more conventional, non-financial means of support.

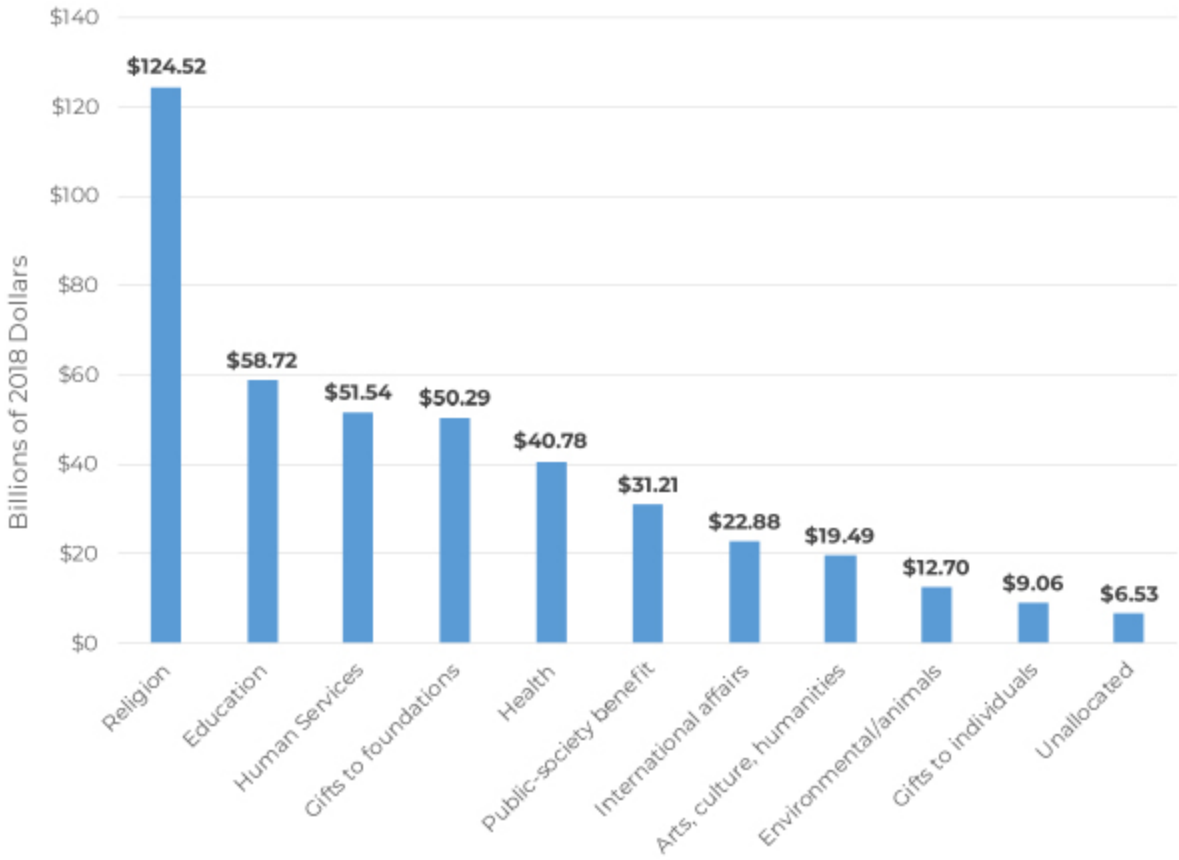
In some respects, philanthropy appears to be doing relatively well. Charitable giving has risen over time, reaching $428 billion in 2018, and the variety of missions it supports reflects the pluralism still present in civil society.[109]

Figure 9. Total Charitable Giving, 1978-2018




Source: Social Capital project analysis of Giving USA.

Figure 10. Composition of Charitable Giving by Sector, 2018




Source: Social Capital Project analysis of Giving USA.

As the Social Capital Project reported in "Reforming the Charitable Deduction," however, two trends should qualify too rosy a picture.[110] First, fewer Americans are giving to charity. From 2000 to 2014, the share of Americans giving to charity fell from 66 percent to 56 percent.[111] Such a pattern suggests that Americans, on the whole, may be less committed to civil society or may value it less than before. Second, individual giving has fallen in relative importance. Individuals' share of total giving has decreased from 83 percent in 1978 to 68 percent in 2018, with corporations, bequests, and especially foundations becoming more important.[112] While institutions are central to civil society's flourishing, foundations and corporations, no matter how generous, cannot replicate the individual's sense of belonging and membership that result from participation in, or support of, a cause.

Philanthropy may be in better condition than some of the institutions it funds, but the decline in widespread commitment to charity and the falling relative importance of individual giving provide further evidence of the erosion of civil society.[113]

*Summary: Institutions in Decline*

Taken together, the above diagnoses suggest that our mediating institutions are ailing – each in its own way and some more than others – but all contributing to an impoverished associational life. The task of concerned policymakers and citizens alike must now be to discern what can be done, not merely to shore up civil society against further decay, but to renew these institutions that were once so central to American life—and that could be again.

## PUBLIC POLICY: PRINCIPLES & RECOMMENDATIONS

The complex nature of civil society, and of its erosion, calls for a multifaceted response, one that engages matters often neglected by policymakers. While the task of rebuilding civil society may, at times, require new or unconventional policy approaches, it must nevertheless be grounded in older principles of governance that once enabled mediating institutions to flourish. To begin, policymakers must grapple with a nationwide decline in trust.

*Where Trust Resides*

As the role of the federal government expanded and the State assumed more of civil society's responsibilities, trust in the federal government eroded. From 1964 to 2018, the share of Americans who reported that they "trust the government in Washington always or most of the time" fell 59 percentage points—from 77 to 18 percent.[114] Several factors contributed to declining trust in the federal government, including political scandal, policy decisions, and party polarization. The contrast with local and state government, however, is striking. The share of Americans with a "great deal" or "fair amount" of trust in state government was at the same level in 2018 as it was in 1973 – 63 percent, albeit with variation over time. Americans' trust in local government, meanwhile, *increased* by 9 percentage points—from 63 to 72 percent—over the 45 years between 1973 and 2018.[115]

It is possible that the growing divergence between trust in national versus local government is due to a lack of knowledge or interest in the latter. With increased political polarization, the rise of a 24-hour news cycle, and the growing size and scope of the federal government, Americans likely pay more attention to national politics today. Or it could be that the divergence is just one part of a larger "optimism gap" between Americans' relatively positive views of their own lives and particular institutions and relatively negative views of more distant institutions and the country as a whole.[116] For instance, while a majority of Americans think that most Congressmen are corrupt, out of touch, and focused on the needs of special interests, they are much less likely to hold such views about their own member of Congress.[117] Regardless, it is still the case that state and local governments are closer and more accountable to the communities they serve.

*Recovering the Principle of Subsidiarity*

The lessons of crowd-out and declining trust in national institutions recommend a different way of thinking about public policy. A new approach should seek to decentralize policymaking and restore responsibilities to civil society, recognize the strengths of localism while acknowledging its weaknesses, see participatory bodies as the best sites for decision-making, and value membership as a good in itself. In other words, policy should recommit itself to the principle of subsidiarity.

Subsidiarity is a concept from Catholic social teaching affirming respect for the proper authority vested in local communities and governing bodies. It recommends that power and authority be devolved to the lowest appropriate level.[118] It calls for important administrative and policy decisions to be made nearest to interpersonal community and association, barring strong arguments to the contrary.[119] As a matter of public policy, the principle supplies a simple blueprint: policy should be decentralized and should delegate state functions to more local authorities.[120] The principle of subsidiarity does not apply exclusively to state power; it can also encompass non-governmental institutions. A national organization, for instance, may leave fundraising responsibilities to its local chapters. Nor must subsidiarity distinguish between state and non-state power. As the lessons of crowd-out reveal, many of the responsibilities assumed by government once belonged—and may rightly belong—to civil society. Subsidiarity supplies a basis on which those responsibilities might be restored.

As a principle for policymaking, subsidiarity offers many practical benefits. It leverages local networks and expertise, giving greater discretion to those more likely to have community-specific knowledge. This, in turn, enables tailored rather than one-size-fits-all policies, addressing diverse contexts with diverse solutions. In doing so, subsidiarity promotes experimentation, permitting each community, as Justice Louis Brandeis said of federalism, to "serve as a laboratory; and try novel social and economic experiments without risk to the rest of the country."[121]

Yet the greatest advantages of subsidiarity are not immediately practical. By vesting greater authority in local government, subsidiarity works against the polarizing tendencies of national politics, reducing the friction between regional factions, ideological camps, and cultural allegiances. Subsidiarity reorients individuals toward local associations and government, securing opportunities for membership, granting individuals greater responsibility, and empowering them to govern themselves. With this reorientation come the common goods associated with a vibrant associational life: norms of reciprocity and trust, thick social networks, and a sense of solidarity.

Though a twentieth-century Catholic concept, subsidiarity has been a *de facto* operating principle of American politics and society for much of our nation's history. Our federal system of government was designed to preserve a balance of authority between central and local powers. The Tenth Amendment expresses the principle matter-of-factly, ensuring that the federal government possesses only the powers delegated to it by the Constitution and that remaining powers are "reserved to the

States respectively, or to the people." Indeed, while the distribution of power across federal, state, and local government has evolved over time, American politics nevertheless adheres to a framework that protects regional autonomy within a national system. Moreover, local associations once filled important functions now assumed by government or the market—providing education, offering insurance, granting credit, and disbursing charity. In many areas of life, civil society was implicitly deemed the lowest appropriate level for action.

Subsidiarity could again be an operating principle of American life and a guide for public policy. The legal framework of federalism still exists, and despite its diminished health, civil society still supplies the very structures within which to pursue a policy of subsidiarity: mediating institutions. Policymakers could see these institutions as "alternative mechanisms" for delivering the goods and services that government already provides.[122] Where it does not delegate subsidiary functions to more local governments, the State could entrust them to mediating institutions.

### *Implications for Policymakers*

An approach to policymaking that appreciates the complex topography of our mediating institutions would delegate authority and responsibility to the most proximate, competent institutions—be they governmental or non-governmental—and aim toward a two-fold goal. First, it would seek to leave space for mediating institutions, removing policies and barriers that undermine them. Second, it should attempt, wherever possible and appropriate, to utilize mediating institutions for the delivery of public services and the realization of social goals.[123] It should actively seeks to incorporate civil society into public policy, not circumvent it.

Such a policy agenda does not fall neatly into a universal formula. It requires a careful analysis of local contexts. Indeed, as the lessons of crowd-out suggest, policymaking aimed at rebuilding civil society ought to be as much about striking the appropriate balance of responsibility as it is about carefully designing, efficiently implementing, and rigorously assessing programs. At the same time, policymakers should be careful that, in partnering with and incorporating civil society, they do not transform the character of the mediating institutions or expand the scope of government.[124]

Much like a gardener cultivating a plot of ground, the policymaker tending to civil society must account for a panoply of environmental factors.[125] A rocky, weed-ridden plot requires deliberate gardening to be fertile again, but tilling and weeding alone may not yield growth. Time, irrigation, and added nutrients may be required. Different ecosystems are hospitable to different plants, and different plants require different methods of cultivation—some require trellises, others grafts. *Thus*, the one-size-fits-all solution is often an invasive species like Kudzu or a cheap imitation like AstroTurf.

As with a gardener's efforts to cultivate a particular kind of environment, the work of policymakers hardly guarantees success in the task of rebuilding civil society. Too many factors simply lie beyond their control. But guided by the appropriate principles, policymakers can nevertheless cultivate the environment in which the diverse fruits of civil society are most likely to grow.

### *Applications to Public Policy*

With such principles in mind, the Project envisions four areas in which public policy might aid in the renewal of civil society: addressing crowd-out, spurring local innovation, empowering local decision-making, and rebuilding mediating institutions. More thought and consideration must be given to specific policies at all levels of government. Likewise, policymakers should not accept any proposal—regardless of its merits—without careful scrutiny and revision. The cause is the work of prudential policymaking, and it is a task of generations, not of a single moment in time. An early discussion about options that *could* be explored is the place to begin.

#### Addressing Crowd-Out

Policymakers should address the effects of crowd-out wrought by government. This crowd-out comes in two forms: direct and indirect.

Direct crowd-out stems from laws and regulations that inadvertently prohibit or limit the work of civil society. Institutions or even private individuals may seek to provide aid or services to those in need but find regulatory burdens too much to bear. Wherever possible, policymakers should repeal or reform such laws, in a way that preserves public safety while promoting the public good.[126]

Indirect crowd-out stems from public programs and services which assume functions otherwise performed by non-governmental organizations and do so more generously or efficiently. These effects can be more difficult to identify and to address for a number of reasons—some administrative, others political. Public programs exist to fill a purpose, and removing programs alone is unlikely to be sufficient for restoring the former workings of civil society. For example, some studies estimate that government spending only partially crowds out private charity, at a rate of less than one-to-one, suggesting that if government spending decreased, private charity would increase, but not by an equal amount.[127] Instead, policymakers should consider the unintended consequences of crowd-out when expanding existing or creating new programs.

Spurring Local Innovation

Though federal policymakers may not be qualified to design programs, they may be positioned to assist local efforts addressing social problems. In too many cases, the challenge is not to implement a solution, but to find one. As part of an effort to encourage experimentation, the federal government might consider new funding mechanisms or tools that lower the costs of innovation.

**Place-based, Tax-advantaged Investment**. Place-based investment programs seek to revive economically distressed areas by offering preferential tax treatment on certain new investments. The Tax Cuts and Jobs Act, for example, created Opportunity Zones, which use reduced capital gains taxes to encourage investment in roughly 9,000 low-income Census tracts.[128] Based on investment totals, Opportunity Zones constitute the largest federal community investment program in the modern era.[129] Research on past place-based investment schemes indicates that such programs have been generally ineffective in promoting economic opportunity.[130] To the extent that Opportunity Zones and other place-based programs correct their predecessors' deficiencies, they might have the potential to revitalize neighborhoods and expand opportunity. Future programs might consider incorporating social capital-oriented metrics into eligibility requirements or encouraging investments in social ventures, not merely conventional development projects.

**Social Entrepreneurship**. Policymakers might also encourage social entrepreneurship by replicating the funding models of successful philanthropies. Private philanthropists and institutional investors have adopted alternatives to the traditional grant-making process in recent years. One approach, "venture philanthropy," builds on a more results-oriented philosophy, seeking greater upfront research and partnership.[131] Compared to conventional philanthropy, the funding commitments are larger and longer-term, more oriented toward organizational growth and capacity, and conditional on intermediate results. The investor takes a more active role in managing the organization and activities it funds. For example, LIFT Philanthropy Partners in Vancouver, Canada, invested in KidSport Canada to expand its efforts to help poor children pay for registration fees and equipment for organized sports.[132] Another example is the Obama-era Social Innovation Fund, which gave money not directly to social-service organizations, but to venture philanthropy funds with established track records, according to specific performance criteria. It also included a private matching-funds requirement, to ensure that it was supporting what were truly public-private partnerships.[133]

Another model, known as "impact investing," supports start-up ventures that include a focus on social impact, often through a "microfinance" approach that targets smaller entrepreneurs lacking access to conventional credit channels.[134] Benefit Chicago, for example, is a program that combines funds from the MacArthur Foundation, the Chicago Community Trust, and individuals

and institutions investing through Calvert Impact Capital to seed a variety of commercial enterprises addressing unmet needs and social problems in the city.[135]

**Social Impact Bonds**. Social impact bonds (SIBs) are a pay-for-success investment tool that replicates equity investment in the non-profit sector. Private investors provide funds to a government agency or non-profit organization to fund a capital-intensive project addressing a social problem. They receive returns only if targeted outcomes are achieved, in which case the public agency passes on part of the savings realized by the intervention. An example of such a SIB is the Utah High Quality Preschool Program, an intervention that has successfully reduced the need for special education among an initial group of low-income preschoolers.[136] Policymakers could seek to replace conventional grant-writing with similar public-private funding options that reward success and innovation in the delivery of social services.

**Information sharing**. States, localities, and private actors should have access to public information about the success of programs and policies that receive public funding. Policymakers might consider the creation of a new clearinghouse or the expansion of an existing one, such as the Institute of Education Sciences' What Works Clearinghouse, which compiles and summarizes scientific research on education and human services programs, practices, and policies.[137]

**Evaluating Success**. Private organizations made eligible to administer programs should also be regularly evaluated for success through rigorous data-collection and empirical return-on-investment requirements. The incorporation of randomized controlled trials and other forms of "evidence-based policymaking" could help policymakers determine which organizations and practices deserve continued support and which do not.[138] Policymakers, however, must be careful not to use such studies merely as post facto support of predetermined policy conclusions.[139]

### Empowering Local Decision-Making

Alongside increased experimentation, federal policymakers can strengthen civil society and local initiatives by maximizing the flexibility of existing programs. Restoring greater autonomy to state and local governments, private organizations, and citizens ought to be a principal goal for a policy agenda committed to subsidiarity. In an effort to strike the appropriate balance between self-government, local accountability, and oversight, federal policymakers could consider a number of reforms to the ways that programs are currently funded and administered.

**Indirect Funding**. Unlike a funding structure in which government provides funds directly to an organization, indirect funding essentially enables government funds to flow through an individual beneficiary. Indirect funding options include, but are not limited to, vouchers, certificates, tax credits, and reimbursements for co-paid services. Vouchers, in particular, received considerable attention during

the George W. Bush administration. The Access to Recovery voucher program, for example, was one effort to expand the range of organizations available to addicts seeking drug treatment services.[140] In addition, educational voucher and tax credit programs are widely used across all levels of government. Such programs would be encouraged under a model of "educational pluralism."[141]

Indirect funding helps facilitate greater participation from faith-based organizations in the provision of public services. Because funding results from the "genuinely independent choice" of individual beneficiaries, the Supreme Court has ruled that indirect aid programs do not violate the Establishment Clause, even if the organizations receiving indirect funding offer services that include religious content.[142] In this way, the indirect approach enables faith-based organizations to retain the very features that make them effective in the first place.[143] A renewed emphasis on indirect funding as a model for public policy would expand the role of civil society in providing social services.

**Deregulation**. Eligibility requirements for organizations to receive public funding and even administer services can be onerous and exclusionary to the least professionalized and centralized organizations. Excessive regulations cause these organizations either to drown in a sea of red tape or to face greater operating costs, both of which make it difficult to compete with larger and better-funded organizations. An approach that reduces barriers to entry for private, faith-based, and other smaller community-based organizations would help to circumvent "the credentialism of public service bureaucracies" that limits the involvement of civil society.[144] As Stuart Butler wrote in *To Empower People*, "[t]he deregulation of mediating structures may well be much more important to these institutions than finding new ways to fund them."[145] To that end, policymakers might consider reevaluating existing eligibility and licensing requirements and focusing on more outcome-oriented qualifications.

**Local Administration**. Wherever practical, local institutions and populations should be used to administer health, education, and welfare programs. Federal and state governments could apply a "ZIP code test" to grantees—an official preference for organizations headquartered in or near their target populations' communities.[146] They might also institute "policy councils" of service providers and former beneficiaries to guide a local program, as is the case with Head Start.

**Fiscal Federalism**. "Fiscal federalism" refers to the system of revenue-generating and spending responsibilities across federal and state governments. In general, advocates of fiscal federalism have supported block grants as vehicles of reform. Block grants involve collecting revenues at the federal level and redistributing them—with varying levels of strings attached—to state governments. For example, the 1996 welfare reform converted the nation's largest cash entitlement program into a block grant with strong federal work-based performance standards; it has been widely credited with helping to reduce poverty, especially among children.[147] Similarly, in 2016, then-House Budget Committee Chairman Paul Ryan proposed "Opportunity Grants," which would have consolidated several

existing federal welfare programs into a more individually tailored block grant with certain requirements, such as time limits and work engagement.[148]

While intended to give states greater flexibility, block grants with few or no strings attached may misalign incentives. Some have argued that such grants represent "pseudo-federalism" because revenue collection and spending occur at different levels of government.[149] Instead, true fiscal federalism would see state governments fund and run their own programs.[150] One alternative approach could be to provide limited "equalization grants" only to states with below-average fiscal capacity and thereby potentially sidestep problems associated with traditional block grants.[151] Overall, any fiscal federalism approach should accord with the principle of subsidiarity while taking care to align existing incentives.

### Rebuilding the Mediating Institutions

In addition to reforms focusing on specific dimensions of civil society that cut across institutions, policymakers could explore measures aimed at the particular challenges of neighborhoods, churches, schools, and voluntary associations. Successful measures would stem from a recognition of the strengths, weaknesses, and functions of each.

**Neighborhoods**. Poor zoning and land-use regulations can create obstacles to a vibrant neighborhood. For example, single-use zoning, in which areas are designated for only one purpose, obstructs the diversity of functions that neighborhoods naturally develop. They can reduce aggregate economic output[152] and economic opportunity by raising housing costs, trapping low-skill workers in job deserts.[153] Land-use regulations also create a legal barrier to population density, forcing people to live farther from their neighbors than they otherwise would.[154] Promoting mixed-use zoning, and eliminating laws or regulations obstructing it, could improve cities' walkability and remove artificial barriers to neighborhood ties. Moreover, as the Social Capital Project noted in a recent report, zoning reform could expand educational opportunity.[155]

Policymakers might also consider creating tax credits or deductions to support innovative uses of neighborhood spaces. For example, former Senator Dan Coats and former Congressman John Kasich have proposed a "Compassion Credit" for people who open their homes to help those in need, including battered women, abused mothers, the homeless, hospice patients, and unmarried pregnant women. To ensure participants' safety, those wishing to open their homes would need referrals from non-profit organizations working in the same space.[156]

At the same time, policymakers could eliminate existing tax programs that create perverse incentives or harmful unintended consequences for neighborhoods. For example, the mortgage interest deduction, instead of encouraging homeownership, may simply encourage people to buy more expensive homes.[157] As the average new home size has increased by roughly 1,000 square feet from

1982 to 2015, neighbors have effectively been encouraged to live farther apart than they otherwise would.[158] Ending the deduction would be one way to ensure that policies are not unintentionally incentivizing a retreat from our neighbors.

**Churches and Faith-Based Organizations**. American churches are constitutionally protected from state interference, so the range of reforms available to policymakers is appropriately limited. However, some might consider building upon George W. Bush-era "charitable choice" policies, which expanded the eligibility of faith-based organizations for federal funding.[159] Agencies could be directed to identify barriers to faith-based organizations seeking public funding, including regulatory burdens and administrative capabilities, and potentially establish an explicit goal of funding parity between faith-based and secular organizations that achieve similar results.

**Schools**. While policy debates around education rightly focus on curricula, funding, and the degree of choice, policymakers concerned with schools as *mediating institutions* ought to direct their focus to ways of increasing parental investment and expanding students' opportunities beyond the classroom. For example, school systems might prioritize funding extracurricular activities—such as sports, service, and arts programs—that are expressly pro-social and involve parents and community partners, not merely school employees. School officials might explore models for publicly funded, school-based mentorship programs—particularly for at-risk youth—that recruit local volunteers. As a means of increasing parental investment and oversight, policymakers might also consider ways to reform committee and board structures, leveraging existing or nascent parental networks to have greater influence in locally controlled schools.[160]

**Voluntary Associations**. Some costs associated with volunteering can be tax deductible, such as the cost of traveling to a volunteering site or the cost of a uniform to volunteer at a particular charity.[161] Some states also offer tax credits or rebates for volunteers to specific causes.[162] States could consider expanding the range of volunteering causes subject to such credits in order to support activities that are considered primarily in the domain of civil society, rather than government.

Government regulations were the top challenge for nonprofits in 2018, according to one survey.[163] In some cases, laws may be preventing activities that nonprofits could otherwise perform. For example, a 2014 report found that 21 cities had restricted food-sharing with the homeless.[164] States or localities could create taskforces to identify laws or regulations obstructing activity in the nonprofit sector, akin to the Texas Sunset Advisory Commission, but with a more specific focus.[165] Such efforts, however, must be careful not to enable fraudulent organizations or remove necessary guardrails against nonprofits' activities.[166]

**Philanthropy**. The federal tax code's charitable deduction allows itemizers to deduct the value of charitable contributions to qualifying tax-exempt organizations. The deduction, however, applies only to itemizers—as opposed

to those who take the standard deduction—making it effectively unavailable to most taxpayers, especially lower-income taxpayers. As the Project has written in a previous report, reforms to make the deduction universally applicable would ensure that all taxpayers' donations are protected from taxation and reduce the risk of government crowding out philanthropy.[167]

## CONCLUSION: RESTORING THE SPACE BETWEEN

Renewing the American tradition of civil society will require a change in both disposition and focus. Policymakers must approach the task with a sense of epistemic humility, recognizing the limits of our knowledge and the particularity of each case—namely the place, scale, purpose, and ability of our mediating institutions. What succeeds in one setting may fail in another. Policymakers must therefore study the unique challenges and opportunities of particular institutions.[168] They must beware the "pretence of knowledge" by which one presumes to know more about a given institution than its own members.[169] And they must recognize that no amount of policy experimentation can replace citizens dedicated to their own communities.

As a matter of focus, renewing civil society will also require an expanded notion of what opportunity means. As the Project has argued elsewhere, opportunity encompasses more than upward mobility. It also involves the full person's participation in community and the many relationships that make such participation possible.[170] Too narrow an understanding of opportunity has too often led to policies that, whatever the intentions, have rendered our mediating institutions impotent or redundant. To rebuild civil society, policymakers must recognize a fuller meaning of opportunity, one that includes the ability to form and maintain the relationships and communities constituting the American Dream. It is this opportunity rightly understood, to modify a Tocquevillian phrase, that policymakers must seek to expand.

With the right approach and principles, perhaps we will achieve a widespread recommitment to our mediating institutions and a restoration of the space between individuals and the institutions of mass society. It is that space that has defined and enriched the American experiment in self-government. But Americans cannot simply wait for a new, doubtless very different, Benjamin Franklin, to renew our tradition of civil society for us. It is rather for us to be dedicated to the work that he and his peers advanced: the flourishing of our associational life and the institutions that secure it.

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35. Social Capital Project calculations using data from the 2008-2013 CPS Civic Engagement Supplement and the 2017 CPS Volunteer & Civic Life Assessment. Trend lines in Figure 1 interpolate across years with no data (2012, 2014-2016). The estimates potentially reflect survey changes that affect their comparability over time. The 2008 through 2013 surveys were conducted in November, while the 2017 survey took place in September. The 2017 survey was also considerably longer than the earlier surveys. Finally, the wording of the questions in Figure 1 changed in 2011 and in 2017.
36. Between 2008 and 2017, the share of adults who said they and their neighbors do favors for each other at least a few times a month fell among whites (42 to 25 percent); blacks (35 to 18 percent); Hispanics (34 to 20 percent); those with at least a college degree (41 to 24 percent); those with a high school degree or some college (40 to 22 percent); and those with less than a high school degree (37 to 22 percent). Over the same period, the share of adults who said they talk with their neighbors at least a few times a month similarly declined among whites (74 to 59 percent); blacks (69 to 47 percent); Hispanics (62 to 45 percent); those with at least a college degree (76 to 60 percent); those with a high school degree or some college (70 to 52 percent); and those with less than a high school degree (65 to 48 percent).
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44. Using an index of social trust from a 2000 survey, Charles Murray demonstrated that middle-aged white adults who were very high in social trust were three times more likely to report being "very happy" than those who were very low in social trust. See Charles Murray, *Coming Apart: The State of White America, 1960-2010* (New York: Crown Forum, 2012), 266-7. Additionally, General Social Survey (GSS) data show that 39 percent of adults of all races who reported being "very happy" agreed with the statement that "most people can be trusted," compared to 17 percent among adults who reported being "not too happy." (Social Capital Project calculation using 2010-2018 waves.)

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52. In addition to there being racial differences in social trust, the racial distribution in the U.S. has changed—which research suggests may have implications for social trust. U.S. Census data show that the nonwhite share of the population has grown considerably over time, rising from 16.5 percent in 1970 to 39.6 percent in 2018, and is projected to exceed 50 percent by 2042. See U.S. Census Bureau, "A Look at the 1940 Census," 11; William H. Frey, "Less than half of US children under 15 are white, census shows," The Brookings Institution (June 24, 2019). A sizeable body of literature has shown that neighborhoods with more ethnic diversity tend to have lower levels of trust among residents of all races. See, for example, Robert Putnam, "*E Pluribus Unum*: Diversity and Community in the Twenty-first Century: The 2006 Johan Skytte Prize Lecture," *Scandinavian Political Studies* 30, no. 2 (June 2007): 137-174; Tom van der Meer and Jochem Tolsma, "Ethnic Diversity and Its Effects on Social Cohesion," *Annual Review of Sociology* 40 (July 2014): 459-478; Alejandro Portes and Erik Vickstrom, "Diversity, Social Capital, and Cohesion," *Annual Review of Sociology* 37 (August 2011): 469-471.

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# Reforming the Charitable Deduction

SCP REPORT NO. 5-19 | NOVEMBER 2019

American civil society has long recognized that to whom much is given, much is required. Amidst rising living standards and improving material conditions, Americans have impressed foreign observers, all the way back to Alexis de Tocqueville, with their altruism and commitment to social causes beyond themselves. Complementing this generosity has been Americans' can-do attitude of self-reliance. Tocqueville was struck by how, in the absence of an aristocracy or government administration capable of improving their communities, Americans united to do so themselves.

In other words, Americans have been able to support their communities because of their material success, and they have had to because no other institution could do so. Both tendencies of so much of America's associational life—generosity and self-reliance—are particularly manifest in American philanthropy, of which Tocqueville wrote, "I often saw Americans make great and genuine sacrifices for the public, and I remarked a hundred times that, when needed, they almost never fail to lend faithful support to one another."[1] Americans' charity has allowed nonprofits and other voluntary institutions to play a central role in American life by caring for basic needs and providing public goods ranging from education to the arts.

However, as our report "What We Do Together" illustrates, the U.S. is suffering from long-term declines in its associational life.[2] As we wrote in "The Wealth of Relations," "Our institutions of civil society have weakened and withered, and our relationships have become more circumscribed."[3]

Reversing these trends and rebuilding civil society will require capitalizing on the strengths of America's associational life to address its weaknesses. One way of doing so is to reform policy so that less of the charitable giving of Americans is subject to taxation. Doing so would be more consistent with the principle that people should not be taxed on money they give away.

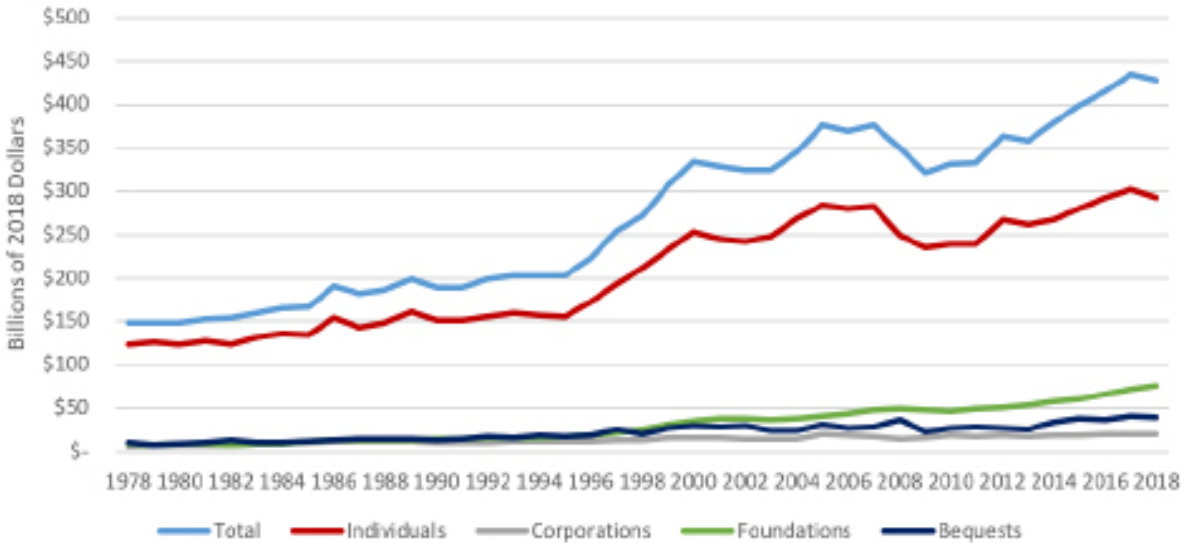
The U.S. tax code has long had a charitable deduction for these reasons. However, current policy has a number of flaws that limit its impact and are in need of reform. The decline in civil society only strengthens the importance of protecting charitable institutions and giving from undue taxation.

Reforming the charitable deduction captures the spirit of the Social Capital Project's approach to policymaking. As we noted in "The Wealth of Relations," rebuilding civil society will require promoting subsidiarity, the principle of pursuing our goals at a local, decentralized level where possible. An improved charitable deduction would recognize that individuals and the institutions they support can often fulfill their purposes more effectively, and be more attuned to the particular needs of each person or community, than can any government agency. To that end, this paper considers trends in charitable giving and their implications for civil society, discusses the flaws of the current charitable deduction, and proposes reforms to make tax policy fairer toward charitable giving and civil society.

## BACKGROUND: TRENDS IN U.S. CHARITABLE GIVING

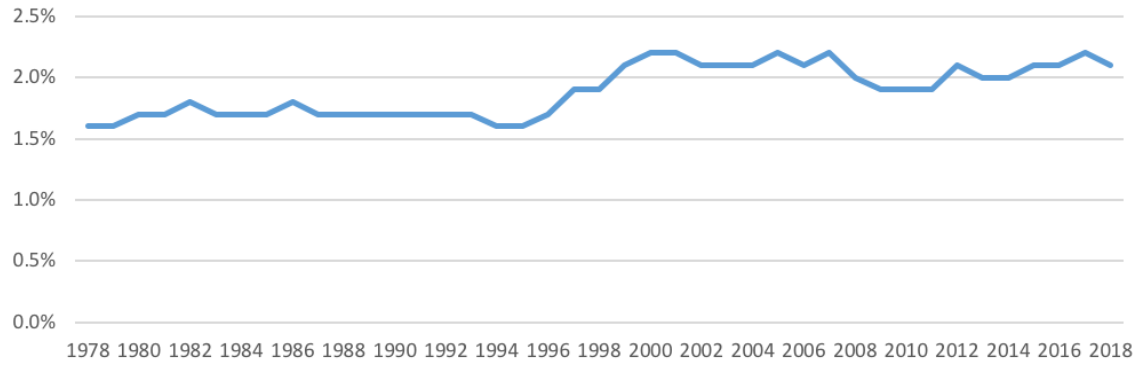
When it comes to charitable giving, Americans have much to celebrate. In 2018, the U.S. ranked fourth in the Charities Aid Foundation's *World Giving Index*, and total annual giving has risen in most years for the last half century, to $428 billion in 2018, as shown in Figure 1.[4] Giving as a percent of GDP has also risen, from 1.6 percent in 1978 to 2.1 percent in 2018, as shown in Figure 2.

Figure 1. Giving by Source, 1978-2018




Source: Giving USA. Estimates of individual giving include itemized and non-itemized charitable contributions.

Figure 2. Giving as a Percent of GDP, 1978-2018

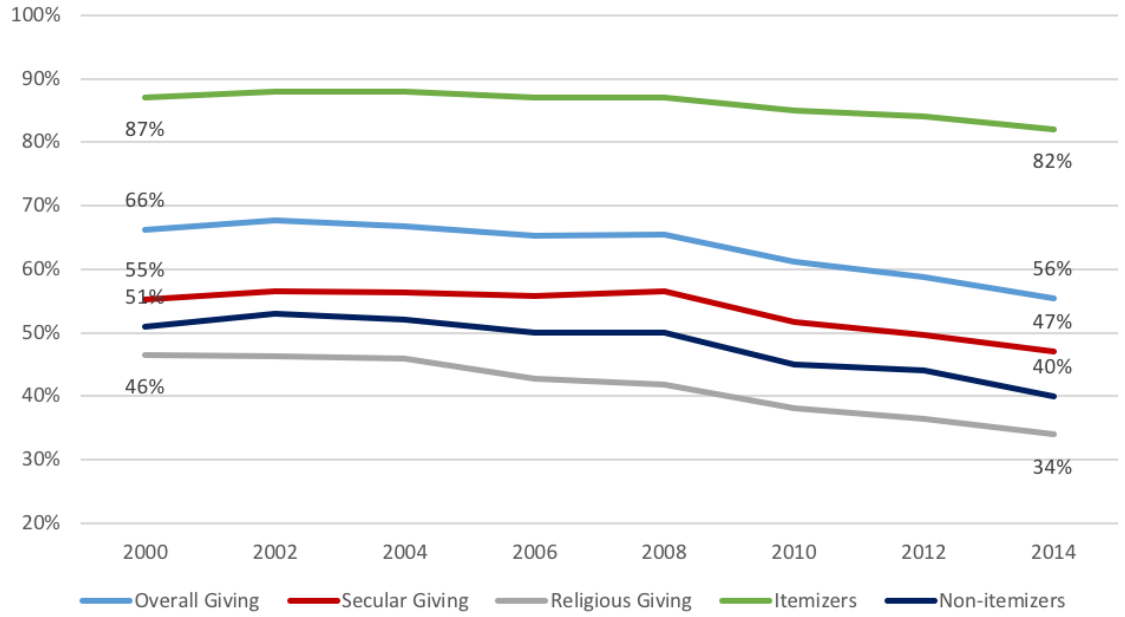



Source: Giving USA.

However, behind these figures lie two disconcerting trends.

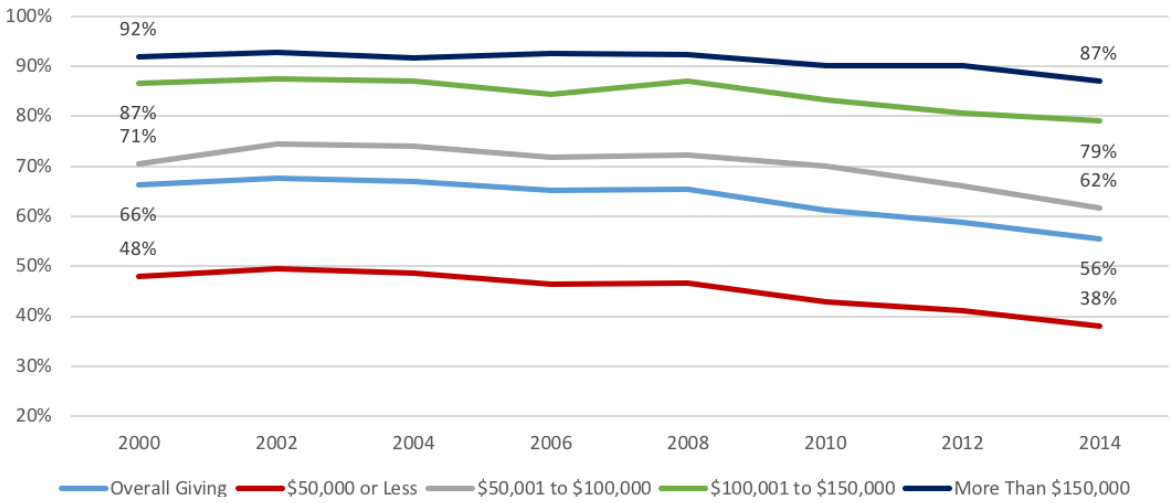
First, while total giving has increased, the percent of Americans giving has decreased, from 66 percent in 2000 to 56 percent in 2014. In other words, growing donations are coming from a shrinking share of the population. As Figures 3 and 4 illustrate, the drop has been particularly pronounced among non-itemizers, those giving to religious causes, and lower-income Americans, although the trend is also apparent for itemizers, those giving to secular causes, and higher-income Americans.

Figure 3. Percent of Households Giving to Charity by Itemizing Status and Cause, 2000-2014




Source: Nonprofit Quarterly and United Way analyses of University of Michigan's Philanthropy Panel Study. Estimates of itemizers include those who gave but did not claim the deduction or did not know if they claimed the deduction.

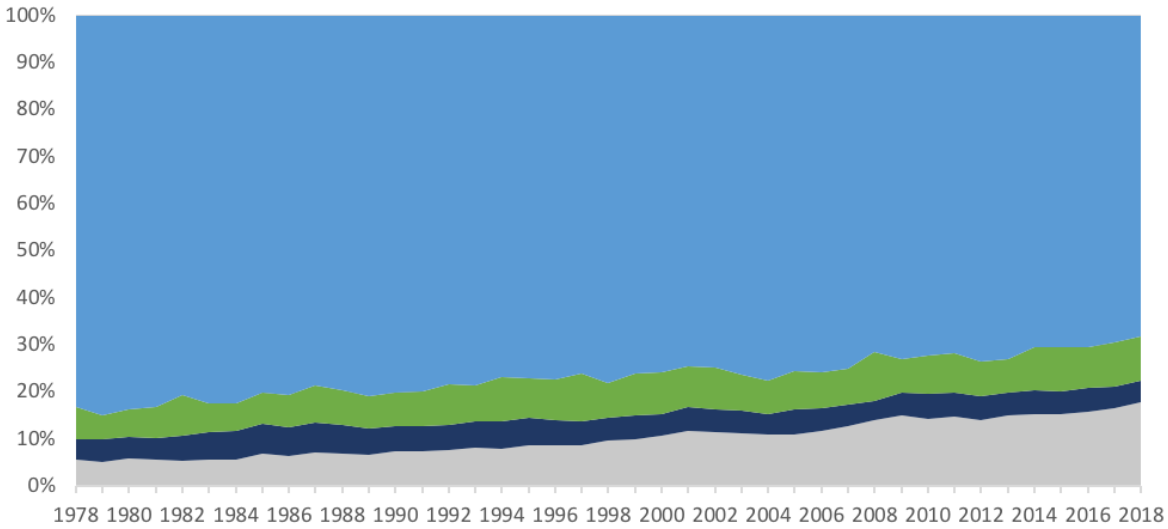
Figure 4. Percent of Households Giving to Charity by Income, 2000-2014




Source: The Chronicle of Philanthropy analysis of University of Michigan's Philanthropy Panel Study.

Second, while total individual giving has increased over time, its *share* of total giving has decreased by 18 percent, from 83 percent in 1978 to 68 percent in 2018. Meanwhile, the share of giving coming from corporations, bequests, and especially foundations has increased, as shown in Figure 5. In other words, the relative importance of individuals' giving has fallen, and the relative importance of other sources has risen.

Figure 5. Composition of Giving by Source, 1978-2018




Source: Giving USA. Estimates of individual giving include itemized and non-itemized charitable contributions.

As total giving is increasing, one might wonder whether the declines in the percent of Americans giving and in the share of giving from individuals are really worrisome trends. Perhaps what matters is not the *source* of giving, but the *amount*; and by that standard, American giving is thriving like never before.

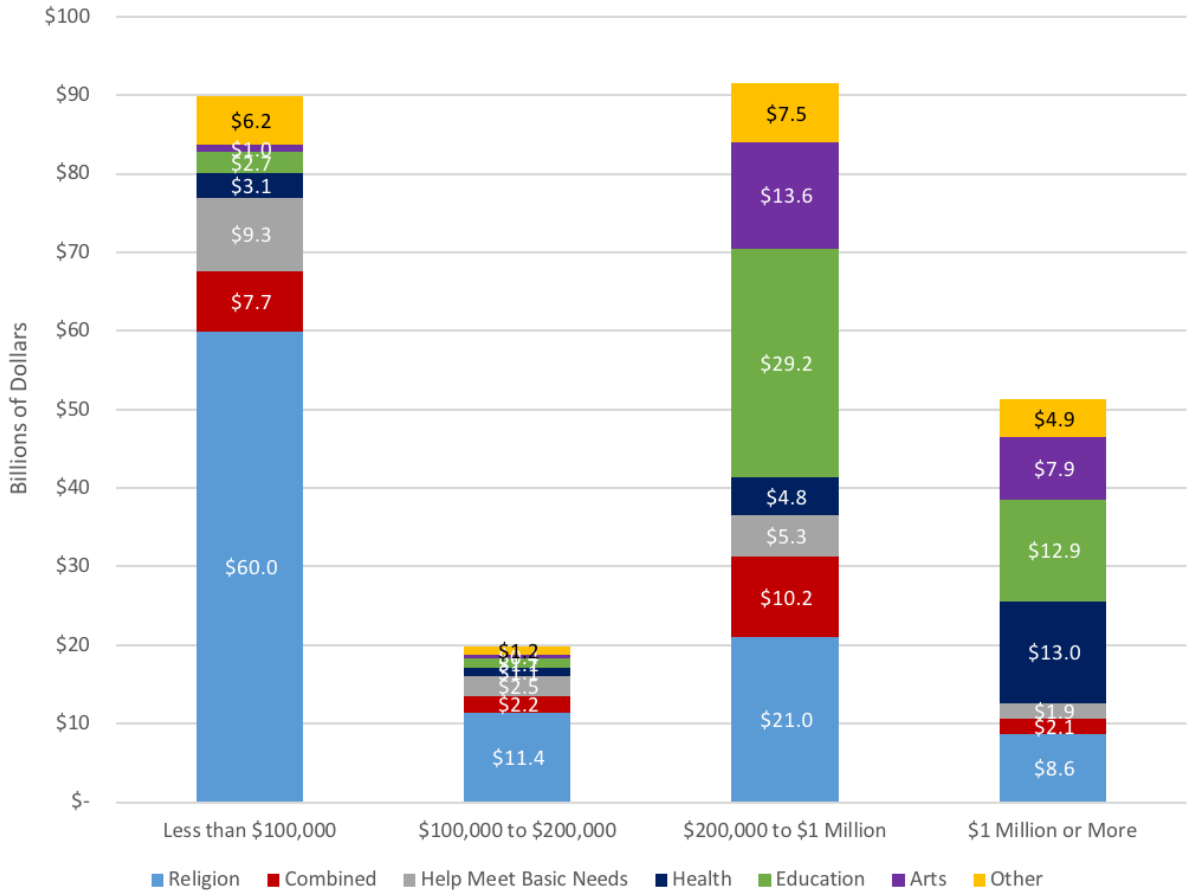
However, with regard to social capital, it is not enough to look simply at the financial support that makes possible the caring for basic needs, the stability of community institutions, the provision of public goods, and so on. As we wrote in "The Wealth of Relations," "Individual investment in social capital often creates benefits for the entire community, such as norms of trust and reciprocity."[5] Such benefits to our associational life come in addition to the material benefits that individual investments or contributions provide, and they require widespread buy-in. A shrinking share of donors, no matter how generous, cannot replace widespread altruism and commitment to improving a community.

In the same report, we also wrote, "When the federal government expands the provision of goods and services on offer through social policy, it runs the risk of 'crowding out' civil society—another potentially counterproductive effect of public policy. Increased reliance on government to address needs weakens the selfish rationale for community members to invest in social capital."[6]

The same concern can be raised about foundations and corporations. Just as government might be able to provide goods or services typically provided by civil society, but fail to foster community attachment as the latter does, so other large-scale entities like foundations and corporations may support important causes without providing the community spillover effects that result from individual contributions. To the extent that individual charitable giving both evinces and contributes to social capital, declines in the percentage of Americans giving and in the share of giving coming from individuals are causes for concern and relevant policy matters.

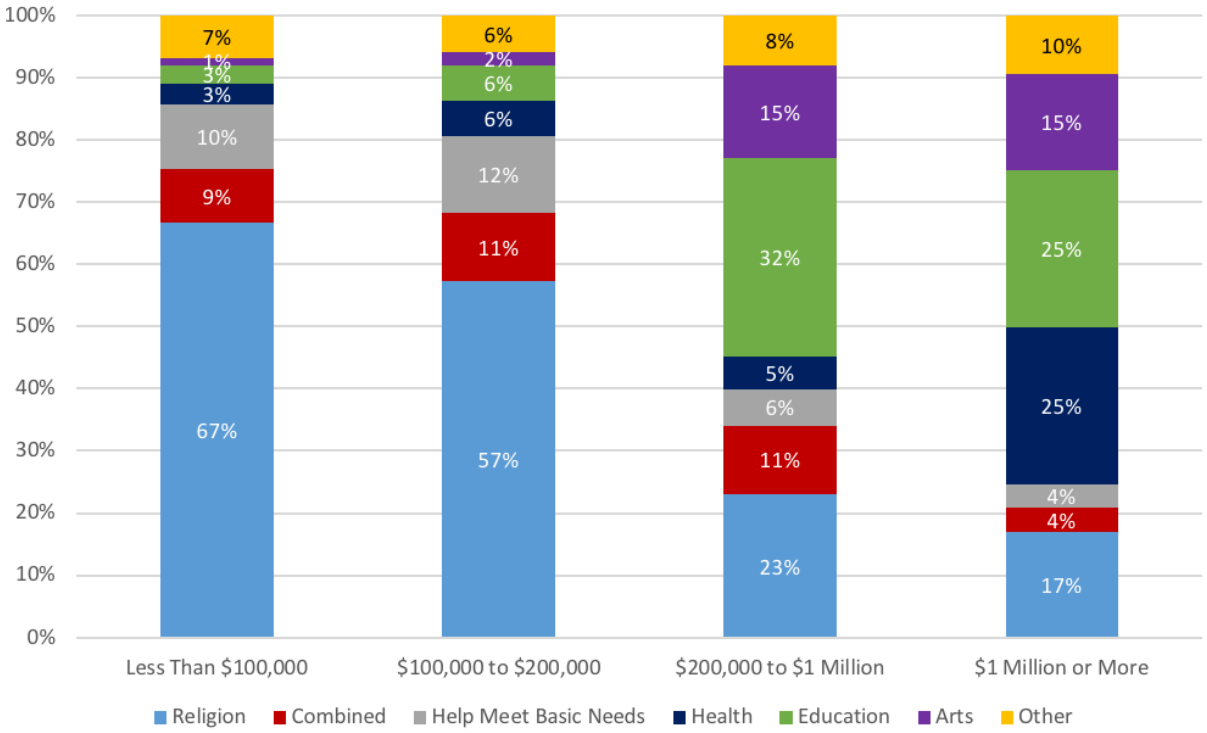
A final reason for the significance of changes in the composition of givers is that the causes people support vary with income, as illustrated in Figures 6 through 9. For example, people making under $200,000 devote a greater share of their giving to religion and meeting basic needs, while people making $200,000 or more devote a greater share of their giving to education and the arts.[7]

Figure 6. Allocation of Charitable Dollars by Income Group, 2005



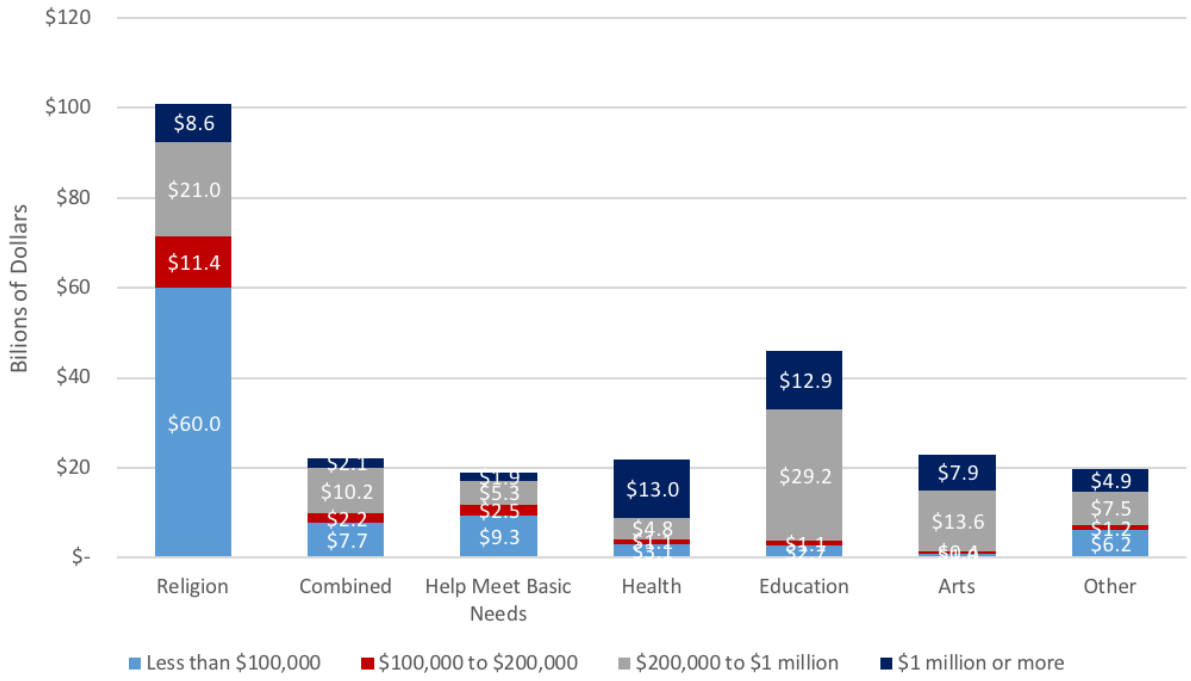

Source: Center of Philanthropy at Indiana University.

Figure 7. Share of Allocation of Charitable Dollars by Income Group, 2005



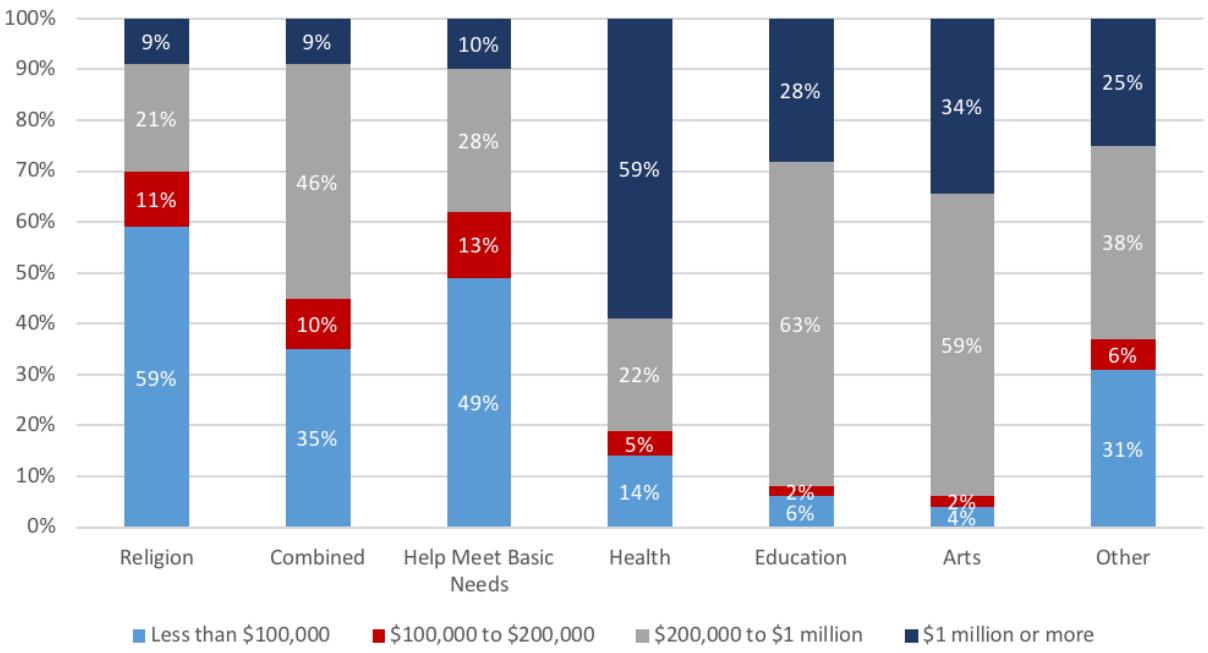

Source: Center of Philanthropy at Indiana University.

Figure 8. Allocation of Charitable Dollars by Cause, 2005




Source: Center of Philanthropy at Indiana University.

Figure 9. Share of Allocation of Charitable Dollars by Cause, 2005




Source: Center of Philanthropy at Indiana University.

Increased individual giving among a shrinking share of the population, and an increase in the average annual charitable gift, suggest that higher-income Americans are increasingly driving individual giving.[8] The variation in giving is even more pronounced among the very richest Americans, as Ken Stern has noted in *The Atlantic*:

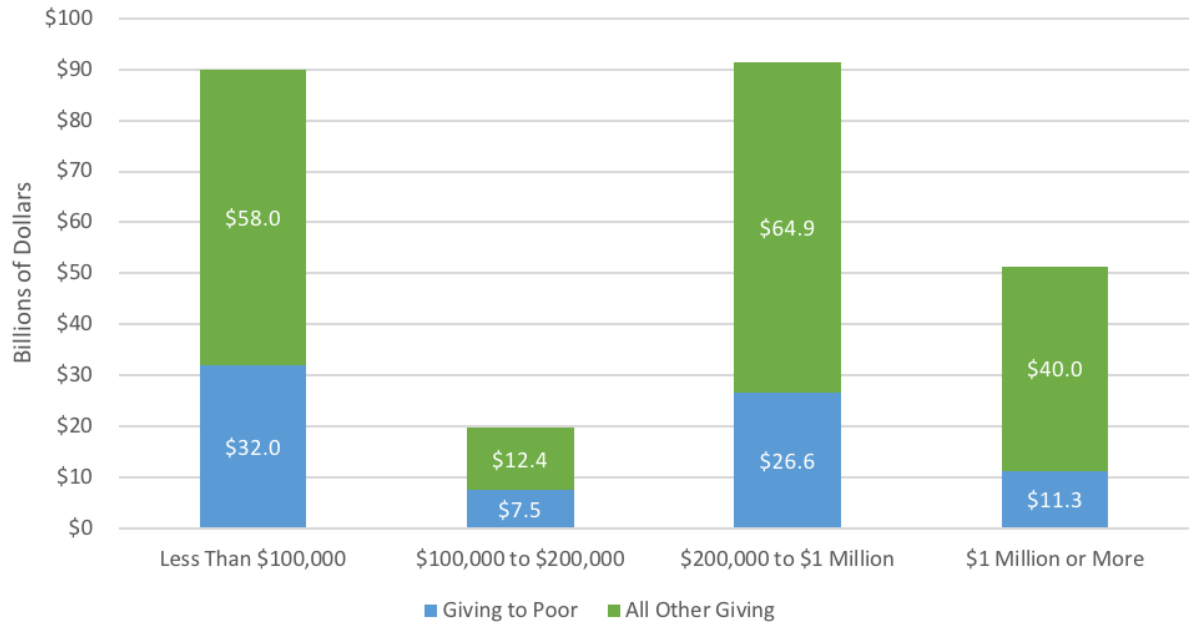
> Of the 50 largest individual gifts to public charities in 2012, 34 went to educational institutions, the vast majority of them colleges and universities, like Harvard, Columbia, and Berkeley, that cater to the nation's and the world's elite. Museums and arts organizations such as the Metropolitan Museum of Art received nine of these major gifts, with the remaining donations spread among medical facilities and fashionable charities like the Central Park Conservancy. Not a single one of them went to a social-service organization or to a charity that principally serves the poor and the dispossessed. More gifts in this group went to elite prep schools (one, to the Hackley School in Tarrytown, New York) than to any of our nation's largest social-service organizations, including United Way, the Salvation Army, and Feeding America (which got, among them, zero).[9]

It is not just that the social benefits of giving are endangered when fewer people maintain the norm of giving, then; the very causes being supported are likely to change as higher-income Americans increasingly drive individual giving.

That worsens the problem of crowd-out of civil society because lower-income and middle-class Americans are more likely to direct their giving toward service and

assistance to the poor—an area where government crowd-out has been especially severe. Figure 10 replicates Figure 6, but with giving divided into all giving to the poor and all other giving. The former category includes not only meeting basic needs, but also giving towards other sectors that support those in poverty, such as church food banks and donations to private schools to provide financial aid. Those making $200,000 or more give a smaller share of their donations to support the poor—29.1 percent of those making between $200,000 and $1 million and 22 percent of those making over $1 million, versus 35.6 percent for those making less than $100,000 and 37.5 percent for those making between $100,000 and $200,000. Those in lower income groups, then, give greater support—both in absolute terms and as a percent of their total giving—to a sector in which charity lowers the need for government support and therefore reduces the risk of civil society becoming crowded out.

Figure 10. Allocation of Charitable Dollars to Poor by Income Group, 2005




Source: Center of Philanthropy at Indiana University.

For several reasons, then, not only the amount of giving, but the source, matter for the health of philanthropy and civil society.

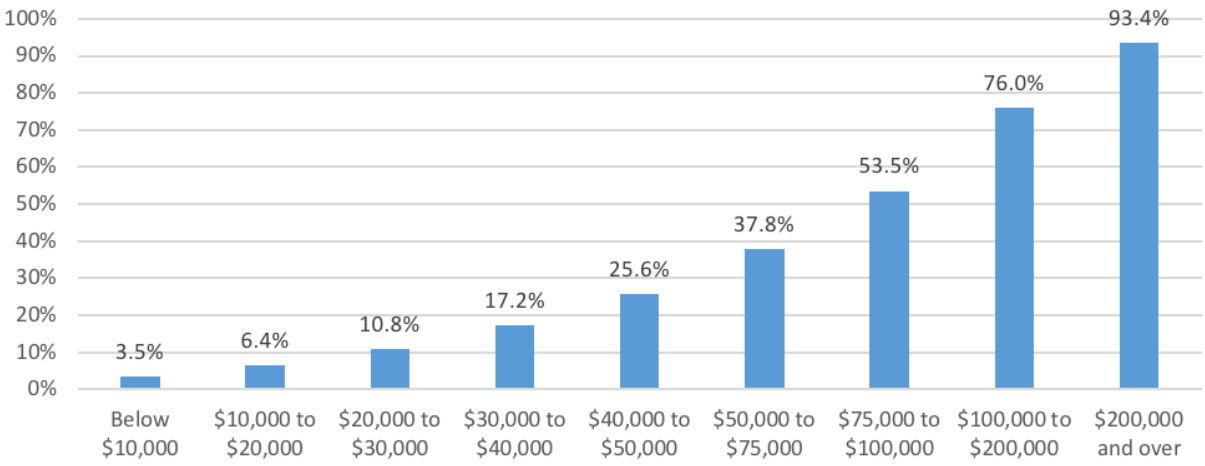
It is important to emphasize that these trends have been developing for some time and thus do not depend on the Tax Cuts and Jobs Act's (TCJA) impact on giving. A number of reforms, particularly the near-doubling of the standard deduction and the reduction of marginal tax rates, have led to predictions or concerns that the TCJA would reduce charitable giving, including charitable deductions.[10] If such immediate concerns prove unfounded, the longer-term trends discussed above would remain causes for concern. If the TCJA does prove to harm giving, the case would only be stronger for reforming policy affecting philanthropy. The most prominent such policy—the charitable deduction—offers much room for improvement.

## OVERVIEW OF THE CHARITABLE DEDUCTION

The charitable deduction allows itemizers to deduct the value of their charitable contributions to qualifying tax-exempt organizations, up to 60 percent of adjusted gross income (AGI). In 2018, the charitable deduction for individuals reduced federal revenue by $54.1 billion.[11] Under its current design, however, the charitable deduction is not available to all taxpayers. As a "below-the-line" deduction, reported on a line that comes after a tax return's AGI calculation, it is available only to itemizers.

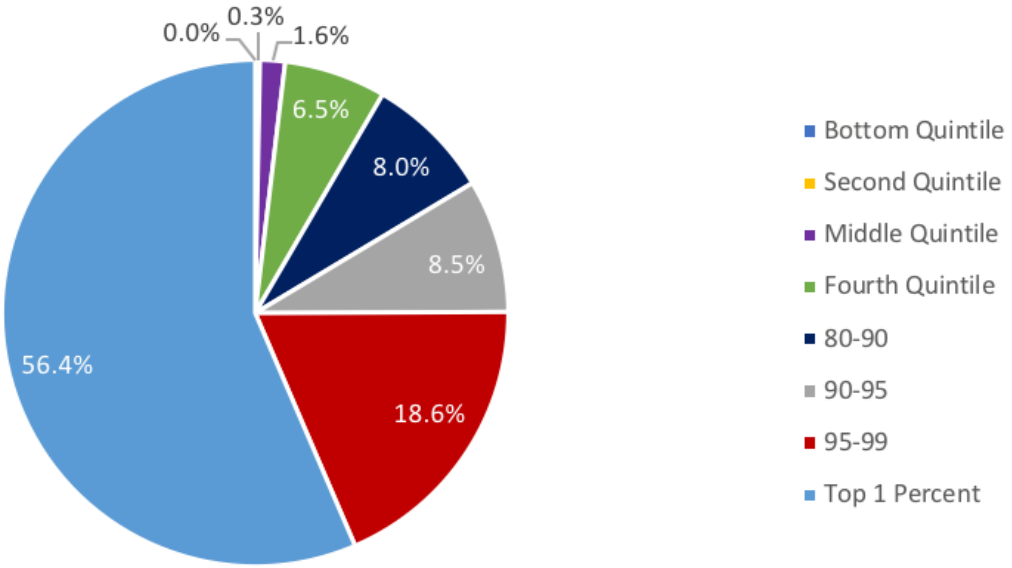
Because itemizers tend to have higher incomes, as shown in Figure 11, the charitable deduction overwhelmingly goes to higher-income taxpayers. Only 9 percent of the charitable giving that avoided taxation because of the deduction occurred within the bottom four quintiles in 2018, while more than half came from the top 1 percent of Americans, as Figure 12 illustrates.

Figure 11. Share of Itemizing Taxpayers by Income Group, 2016




Source: Internal Revenue Service.

Figure 12. Share of the Charitable Deduction Going to Income Quantiles, 2018

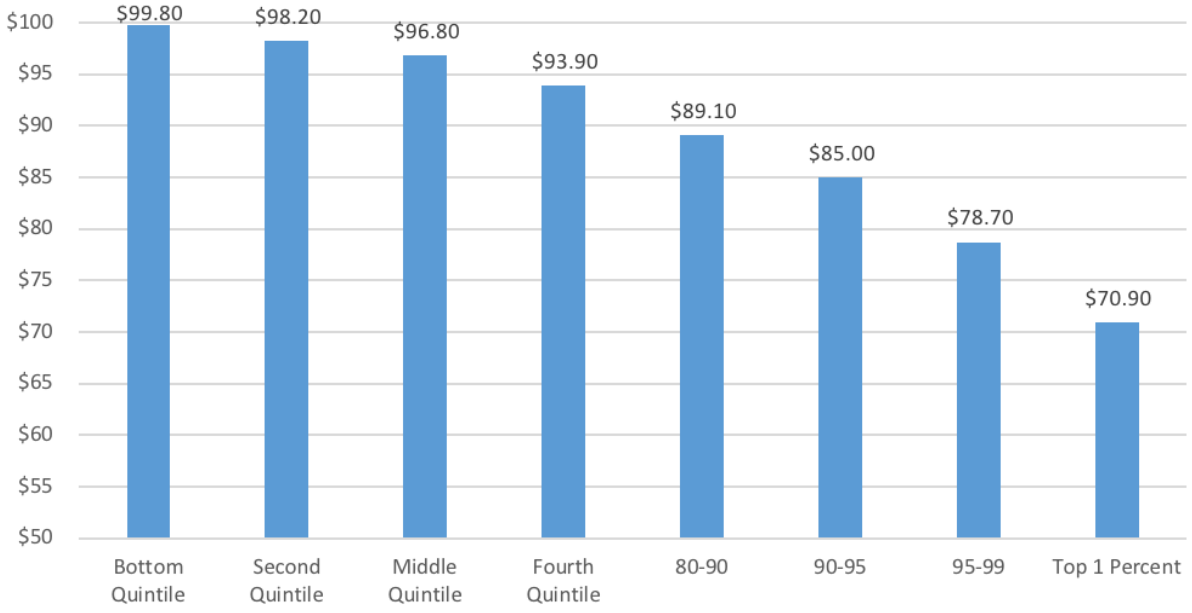



Source: Tax Policy Center.

One might respond that this is exactly the distribution to expect; higher-income Americans have more money to give, so are responsible for a greater share of total giving, so naturally receive a greater share of the deduction.

It's true that even with a charitable deduction that applied equally to all taxpayers, a higher-income person who donated more would see a greater absolute reduction in tax liability than would a lower-income person who donated less. Even so, the after-tax price of giving (the value of donations minus the deduction) declines with income—in other words, the dollar-for-dollar cost of donating falls. This is the case both because higher-income taxpayers generally have higher tax rates and because they are more likely to itemize. Thus, even if low- and high-income taxpayers donated the same amount and itemized, the latter would still receive a greater charitable deduction, as shown in Figure 13.

Figure 13. Average After-Tax Price of $100 Donation by Income Percentile, 2018




Source: Tax Policy Center.

To be clear, the drawback is that the deduction does not apply to all taxpayers; that the deduction disproportionately goes to higher-income taxpayers is a consequence of its design but not itself an intrinsic flaw. Giving ought to be safeguarded against taxation among lower-class Americans as much as among upper-class Americans.

Indeed, giving among lower-income Americans is if anything more important, for two reasons. First, as noted previously, Americans in lower income brackets give a greater share of their donations to the poor—in fact, those making $100,000 or less are responsible for 49 percent of all giving to meet basic needs (Figure 9)—and it is those donations that are more likely to prevent government crowding out. If the deduction is effectively unavailable to lower-income taxpayers, tax policy is penalizing much of the giving that holds back government intervention.

Second, to the extent that lower-income people are often less attached to their communities, as Timothy P. Carney has argued in his book *Alienated America*, the salutary spillover effects of contributing to civil society by giving to charity are needed even more dearly there.[12] And yet it is among lower-income Americans that the percent of people giving has fallen most (Figure 3).

## REFORMING THE CHARITABLE DEDUCTION

Under current policy, non-itemizers are fully taxed on income that they give away to charitable causes (and itemizers are taxed on some of that income). This treatment is unfair, discourages giving, and weakens civil society. One reform option is to make the charitable deduction more widely available. Perhaps the most common proposal for reform is moving the deduction "above the line," making it available to both itemizers and non-itemizers. Other above-the-line deductions already exist, such as those for retirement account contributions and student loan interest payments; this reform would simply give the same treatment to the charitable deduction.

Moving the deduction above the line would increase total giving but reduce federal revenue. A 2018 study by Alex Brill and Derrick Choe at the American Enterprise Institute (AEI) estimated that replacing the current charitable deduction with an above-the-line deduction would increase giving by $21.5 billion in 2018 and reduce revenue by $25.8 billion.[13]

While an above-the-line deduction would treat lower-income donors more fairly with respect to their charitable giving, it would still result in their having a higher after-tax price of giving compared with today's itemizers. Because higher-income taxpayers generally have higher tax rates, the effective cost of their donations would still be lower.

A second option for reform would be to transform the deduction into a credit worth some percent of the value of a taxpayer's total giving. For example, with a 25 percent credit, someone's tax liability would fall by 25 percent of the value of all donations, regardless of tax rates or the size of the donations. However, unless made refundable, the credit would apply only in as much as someone has income tax liability. The same AEI study estimated that replacing the charitable deduction with a 25 percent nonrefundable tax credit would have a greater impact on giving and a greater reduction in revenue than the above-the-line deduction: it would increase giving by $23.3 billion in 2018 and reduce revenue by $31.1 billion.[14]

A credit approach has also been estimated to have a larger positive effect on the number of new donors compared to an above-the-line deduction. A 2019 study of various ways to penalize giving less among non-itemizers while leaving the current deduction unchanged found that a 25 percent tax credit, of the options considered, would most increase the number of households giving, both overall and at all income levels except the top 1 percent.[15]

## CONCLUSION

Rebuilding civil society is no small task. In some cases it will require exploring unorthodox ideas and experimenting with new approaches. But it will also require evaluating the policies we already have in place to see how they could

be improved. Reforming the charitable deduction to treat donors more fairly and penalize giving less is one such opportunity.

Those who argue that but for government overreach, civil society would be flourishing, should be asking exactly which government policies need correction, and the charitable deduction should be high on the list. A reformed charitable deduction would be a means of making our tax code fairer, a precautionary defense against one obstacle to civil society, and a step towards a renewal of America's voluntary institutions.

## APPENDIX: ADDITIONAL EFFICIENCY CONSIDERATIONS AND NET IMPACT ON GIVING

While people give to charity for many non-tax-related reasons, the cost of giving is certainly part of their decision-making. Therefore, when weighing the effects of changes to the charitable deduction, policymakers must consider how reforms might increase new donations, affect tax revenues, and implicate taxpayer compliance and administrative costs.

For example, if someone would donate $100 without the deduction and $150 with it, then the deduction's practical impact is concentrated in the decision to give the additional $50. To concentrate the impact on new donations, a deduction or credit could set a floor on donations, such that only giving above a certain amount qualifies. If someone would give $100 even without a tax credit or charitable deduction, then a more efficient provision would apply only to the amount above $100.

A floor could be set at either a dollar amount or a percent of AGI. For example, with a 2 percent floor, someone making $50,000 would take the deduction or credit only for giving above $1,000, while someone making $100,000 would do so only for giving above $2,000. Recent studies have generally considered floors of $500 or $1,000, or 1 or 2 percent.[16] As average giving is worth roughly 2 percent of income, a 2 percent floor would concentrate the deduction or credit at above-average giving.[17]

A tax provision with a floor, while producing more giving than the current deduction, would have a smaller effect on giving and reduce revenue by less than one without a floor. The AEI study cited earlier estimated that an above-the-line deduction with a floor of $500 for single filers and $1,000 for married filers would increase giving by $19.1 billion in 2018 and reduce revenue by $14.6 billion; a 25 percent credit with a floor of $500 for single filers and $1,000 for married filers would increase giving by $20 billion in 2018 and reduce revenue by $15.4 billion. In both cases, only with a floor would the increase in giving exceed the reduction in revenue.

A floor set to a percentage would have an advantage over a floor set to a dollar amount: it would be equally valuable at all incomes. A floor set to a dollar amount would set a high bar for low-income givers and a low bar for higher-income givers, whereas a floor set to a percent would ensure that the deduction or credit scales with income. One potential downside of a percentage floor, however, is that it could prove more complicated to taxpayers, who would have to calculate the level at which it takes effect. Any confusion could reduce the provision's impact.

There is the possibility that a floor would motivate people to bunch their donations to benefit from the provision. For example, instead of annually giving an amount that falls below the threshold, one might give twice as much every two years so that at least part of the donation passes the threshold. However, evidence suggests that with a low floor, any bunching effects would be minor.[18] Additionally, even a floor that motivates some bunching would be a more efficient provision in terms of producing new charitable giving than the current deduction, with no floor at all.

A floor would be more efficient in two respects. First, simply by reducing the amount of giving qualifying for the deduction or credit, a floor would have a smaller effect on revenues. According to the AEI estimates, an above-the-line deduction without a floor reduces revenue by $11.2 billion more than a deduction with a floor, for only a $2.4 billion greater impact on giving. Similarly, a 25 percent credit without a floor would reduce revenue by $15.7 billion more than a credit with a floor, for only a $3.3 billion greater impact on giving. Only with a floor does a deduction or credit boost giving by more than it reduces revenue.

Second, a floor would reduce administrative costs associated with a provision. Applying a provision to all giving, even small donations, would greatly increase administrative complexity. As Joseph Rosenberg et al. have noted, "Even if it audited more returns, the IRS has almost no ability to determine if, say, one really put money in the collection basket or made contributions to people knocking at the door. Spending hundreds or thousands of dollars of IRS personnel time on one return to go after a few dollars of tax for a person donating moderate amounts is not economical."[19] A floor would greatly reduce the need to monitor charitable giving to ensure compliance, preventing the provision from becoming an administrative boondoggle.

A final question is whether to maintain the ceiling, or cap, that currently exists on giving. With a cap, taxpayers stop receiving any tax benefits once their donations pass some threshold. The deduction currently has a cap at 60 percent of AGI (temporarily increased from the pre-TCJA level of 50 percent), so the deduction does not apply to giving in excess of 60 percent of AGI.

Justifications for the cap tend to appeal to the desire to make the deduction more equal by limiting the value of the deduction to the wealthy, who can afford to donate more (both in absolute terms and as a percent of AGI) and

therefore stand to benefit more from the deduction.[20] A cap would also reduce tax revenues less, like a floor, by reducing the amount of giving subject to the deduction or credit. But whereas a floor can encourage giving, a cap removes the incentive to give past a threshold.

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# Accountability for Bad Apples:

## Police Reforms to Restore Faith in Institutions

SCP REPORT NO. 3-21 | MARCH 2021

Institutions—the organizations and formalized relationships we create to jointly accomplish mutually valued objectives—are a vital source of social capital. They strengthen communities, encourage social support, and establish our way of life. Unfortunately, as documented in the Social Capital Project's flagship report, *What We Do Together*, Americans' confidence in these institutions has declined dramatically over the past 50 years.[1] We are less confident in federal and state government, mass media, banks, newspapers, organized religion, public schools, organized labor, big business, and the medical system. Averaging across seven different institutions, Gallup reports that the share of Americans reporting "a great deal" or "quite a lot" of confidence in them fell from 44 percent in 1973 to 27 percent in 2018.[2]

Declining confidence in institutions is one of the most important indicators of the deterioration of associational life in America. When we lack faith in the organizations we have formed together to achieve our ends, we are correspondingly less likely to attempt to do things together. We are less inclined to cooperate with those institutions or to feel a part of something bigger than ourselves.

As suggested by Yuval Levin, a key reason for eroding confidence in institutions is that there is too little accountability for people operating within them, who have become too removed from the roles they are supposed to serve.[3]

Law enforcement provides an immediately relevant example. In 2004, 64 percent of Americans indicated to Gallup that they had "a great deal" or "quite a lot" of confidence in the police. Yet in June of last year, the figure stood at 48 percent.[4] The diminished standing of police is part of the more general decline in the standing of institutions. Police officers, by and large, serve the public admirably, keeping Americans safe and doing so professionally. There is, however, a long history of breaches of the public trust by officers who did not live up to their calling. From the abuse that led to the riots in Watts and numerous other cities in the 1960s, to the beating of Rodney King by Los Angeles police and the unrest that followed their 1992 acquittal, to George Floyd's death at the hands of law enforcement last year, police misconduct continues to be a public flashpoint.

The widely publicized deaths of Floyd, Taylor, and several other Black Americans over the past few years have weakened trust, sparked outrage, and led to widespread demands for increased police accountability across the nation. These also have led to peaceful protests, violent riots, and increased attacks on law enforcement. A 2018 survey from the Pew Research Center revealed that 61 percent of people believe that police officers act unethically some or most of the time, and 45 percent do not think that police officers face serious consequences for unethical behavior.[5]

Confidence in law enforcement officers is especially low among racial minorities. While 72 percent of White Americans believe that police officers treat racial and ethnic groups equally at least some of the time, only half of Hispanics and one third of Black Americans believe the same. Similarly, a 2016 survey from the Cato Institute found that Black Americans (73 percent) and Hispanics (54 percent) are far more likely than Whites (35 percent) to believe that police are too quick to use lethal force. Black Americans are also twice as likely as White Americans to know someone physically abused by police and to say that police tactics are generally too harsh.[6]

These racial disparities in perception reflect real differences in treatment given the same circumstances.[7] As would be expected if diminished faith in institutions leads people to withdraw from them, groups with low confidence in the police are less likely to cooperate with them. For example, Emily Ekins of the Cato Institute reports that Black Americans are much less likely than Whites to say they definitely would report a crime.[8] Obviously, this is no recipe for improving community safety.

This mistrust in law enforcement on the part of Black and non-Black Americans has led to "defund the police" movements across the nation. Their proposals range from reforming police departments and focusing on community policing to calls for reducing police funding and allocating more dollars for social or job services. The most radical of these proposals call for the elimination of police departments altogether and has led to the demonization of police officers across the country.

America is facing a crisis of conscience. Completely abolishing police, however, would be an extreme response that would make our nation and communities less safe. First, exposure to violence is associated with a host of negative outcomes, including poor mental and physical health, problematic behaviors, poor academic performance and educational attainment, and even poor cognitive development.[9] Police help to reduce violence and prevent these outcomes. According to academic research on police hiring grants in 2009, cities that experienced a 3.2 percent increase in police saw a 3.5 percent reduction in crime.[10]

Second, a small number of officers make up the majority of complaints of wrongdoing. One study of eight cities assessing complaints filed from 2004 to 2008 found that 14 percent of police officers accounted for essentially all complaints alleging improper use of force, and just four percent accounted for half the complaints.[11]

Indeed, some experts have suggested that one reason murders, shootings, and gun violence were up last year is that "violent criminals have been emboldened by the sidelining of police," due to "blowback" in the wake of Floyd's death.[12] Yet, Americans undoubtedly fare better when crime is reduced, both individually and collectively. As demonstrated in *The Geography of Social Capital in America*, violent crime rates at the county level are strongly negatively correlated with social capital.[13] This reflects the inability to maintain social order, meaning that crime has negative ramifications for community wellbeing.

The key is therefore to increase accountability for bad apples while preserving the benefits that police on the whole provide to American communities.

Accomplishing this goal would require a multitude of policy changes: reforming police unions, changing state and national laws that unreasonably shield police from liability, and removing the perverse incentives currently in place that encourage bad behavior.

## THE HARM CAUSED BY POLICE UNIONS

Police unions shield bad apples from accountability by leveraging their power to protect the small minority of officers who have betrayed the public trust. All unions are intended to protect their members, but in so doing, they create costs for members and non-members alike. To the extent that they protect their own members from losing employment and grant special protections—without regard to work output, skill, and job performance, based solely on union membership—unions can be said to make society and the economy less innovative and efficient. Where this occurs, it makes private-sector union members less accountable employers, and employers less accountable to consumers.[14]

In the case of public-sector unions (like police unions), the same dynamic has potential to make union members less accountable to the government entities they serve, which in turn are rendered less accountable to the taxpayers who pay their salaries. Public-sector unions accumulate power as a consequence of the monopolistic nature of government services, but also due to the relationship between public-sector unions and the public officials they help elect. This relationship can produce a serious ethical issue, as union members often have the opportunity to vote for and otherwise support the very politicians who are in charge of their contract negotiations.[15] Unions consistently rank among the most politically active organizations in both local and national elections, often using the money collected from union dues to fight against policies that could otherwise improve government efficiency, but might jeopardize the job security of some union members.[16]

Police unions provide officers protections that prevent accountability. Derek Chauvin – the Minneapolis police officer who killed George Floyd – had previously faced at least 18 complaints of misconduct without facing any serious discipline.[17] From 2012 to 2020, only 12 Minneapolis officers faced discipline out of 2,600 misconduct complaints. Shockingly, the most serious of those 12 disciplinary actions was a 40-hour suspension.[18] Quite predictably, some portion of all complaints filed against police officers will ultimately be deemed meritless. Significantly, however, the protections offered by police unions extend far beyond those necessary to shield officers from frivolous or unfounded complaints.[19]

In Parkland, Florida, Sergeant Brian Miller was rehired with full back-pay two years after being fired for neglect of duty for failing to intervene in the Douglas High School shooting and *waiting 10 minutes before he even radioed for help*.[20] Similarly, police unions came to the defense of New York Police Department

officer Daniel Pantaleo after he killed Eric Garner with a chokehold, which had been banned by the department for over 20 years.[21]

A 2017 investigation from the *Washington Post* also found that 45 percent of officers fired for misconduct in Washington, D.C. were rehired on appeal, as were 62 percent of officers fired in Philadelphia and 70 percent of officers fired in San Antonio.[22] Based on a review of 36 police departments, the study concludes that just under one quarter of all officers fired for misconduct are rehired, often by arbitrators, on appeal.[23]

Furthermore, an examination of police prosecutions from 2009 to 2010 found that, out of 8,300 credible reports filed against 11,000 officers, only 3,283 resulted in criminal charges. Only about 1,000 of those officers were convicted, and only 36 percent of those convicted were eventually incarcerated. Among the officers accused of either excessive force or killing a civilian, only 7 percent were charged with a crime. Comparing conviction rates of law enforcement to the general public, the study found that, overall, officers face conviction rates and incarceration rates half that of the overall population.[24]

Collective bargaining plays a significant role in shielding police officers from the consequences of their misconduct, exacerbating mistrust in the police. In a review of 178 police union contracts, Stephen Rushin found that 88 percent included at least one provision acting as a barrier to disciplinary action. These provisions "limit officer interrogations after alleged wrongdoing, mandate the destruction of officer disciplinary records, ban civilian oversight of police misconduct, prevent anonymous civilian complaints, indemnify officers in civil lawsuits, or require arbitration in cases of disciplinary action." For instance, contracts may enforce mandatory waiting periods before an investigation may occur, require that officers see the evidence against them before being interrogated, prohibit interrogation if too much time has elapsed after an incident, and limit the consideration of disciplinary records in future employment actions.[25]

Furthermore, mandating that disciplinary action be decided through closed-door arbitration often results in reduced disciplinary penalties against officers found guilty of misconduct.[26] One review found that 73 percent of police union contracts allowed for decisions to be appealed to an arbitrator, 70 percent gave arbitrators extensive power to revisit previously decided cases, and over half gave officers or unions the power to select that arbitrator. [27]

Several studies have gone further to demonstrate a causal link between these police union protections and police misconduct. Utilizing the fact that police union formation in the United States was staggered both over time and locality, researchers Rob Gillezeau, Jamein Cunningham, Donna Fair, and Alex Thomson estimate that gaining access to collective bargaining rights is predicted to increase police killings of civilians by about 60 to 70 per year.[28] Additional research suggests that cities with increased police protections, measured both by union contracts and state laws protecting police, are more likely to experience increased instances

of police abuse and police killings of unarmed civilians.[29] Finally, an examination of police misconduct in Florida before and after sheriffs' deputies were granted collective bargaining rights found that collective bargaining led to a 40 percent increase in complaints of violent incidents, which implied an increase of roughly 12 violent incidents per year across the 58 agencies examined.[30]

A recent survey from the Cato Institute revealed that the American public is largely against these union protections. For instance, 84 percent of those surveyed opposed erasing police records of misconduct after a set period of time, and 62 percent opposed collective bargaining related to police misconduct.[31]

It stands to reason that, by reducing the cost of bad behavior for rogue police, excessive police union protections weaken the trust between communities and the officers sworn to protect them. Booker Hodges, the assistant commissioner for the Minnesota Department of Public Safety, said it best by acknowledging that "a union is required to represent an officer, but … publicly defending an officer who has clearly violated our oath of office strains neighborhood relations and erodes trust."[32]

## REFORMING POLICE UNIONS FOR GREATER OFFICER ACCOUNTABILITY

Several reforms can be made to police unions in order to establish greater accountability among police officers, which is the first step to rebuilding trust between officers and the communities they serve. First, state legislatures could limit the ability of unions to negotiate favorable conditions around disciplinary procedures that unfairly advantage their members.[33] As demonstrated through research, these union protections are positively associated with increased instances of violence.

In some cases, courts may limit police unions' abilities to negotiate on terms and conditions of employment related to employee accountability, for instance by following the example of New York. In 2006, the New York Court of Appeals ruled that "police discipline may not be a subject of collective bargaining." Instead, the court ruled that police discipline falls under the authority of individual municipalities.[34]

Absent court action, some suggest that Congress could take action to increase police union accountability.[35] While policing is and ought to be first and foremost a local issue, the federal government has become increasingly involved with policies that directly impact local police departments. Data show that federal funding to state and local governments for the "administration of justice" has soared from roughly $570 million in 1990 to a projected $8 billion in 2021.[36] This increase in funding of over 1,000 percent reflects an immense rise in federal influence over local policing.

Federal funding directly impacts local police departments in a number of ways. In 2020, the Bureau of Justice Assistance (BJA) provided state and local law enforcement agencies with $343 million through the Community Oriented Policing Services (COPS) program, which awards grants for hiring new officers, training, and other police support functions.[37] Since 1994, the COPS program has provided funding to 13,000 jurisdictions, and each year thousands of police departments continue to apply.[38]

Similarly, the BJA awards $340 million annually on average to the states through the Edward Byrne Memorial Justice Grant (JAG) Program to support law enforcement, courts, corrections, drug treatment programs, victims assistance, and mental health programs.[39] Additionally, in 2019, states received $3.1 billion in federal grants for "public order and safety."[40]

The extent of federal involvement in state and local law enforcement (through funding and otherwise) should itself be re-evaluated, given that (1) the Constitution does not delegate police powers to the federal government, but to the states, and (2) federal intrusion has a known tendency to blur lines of accountability for state and local law enforcement agencies.

While proposals exist that would condition federal grant money on accountability measures,[41] ideally, states and localities should take it upon themselves to increase police accountability. For instance, they could mandate that collective bargaining agreements for police be made public and bar features of police union contracts that discourage accountability. These barriers include:[42]

- Limits on interrogations – *e.g.*, how soon they may occur after an incident, how long they may last, and what types of questions may be asked – and limits on internal investigations;
- Policies granting officers access to some or all evidence against them before being interrogated;
- Policies mandating that misconduct cases must be resolved through arbitration, which denies the public access to information about the officer's misconduct and the resolution reached;
- Clauses giving unions sign-off on departmental policy changes;
- Policies mandating the elimination of officer misconduct records after a certain period of time; and
- Policies preventing prior misconduct records from being considered in future misconduct cases or from being available to new prospective employers if the officer moves to a different department.

Given the recent instances of police abuse and overwhelming public support for police reform, it is likely that some unions would willingly comply with these measures. Already, three major police unions in California have released their own proposals calling for national use of force standards, public websites

tracking use-of-force incidents, and a national database of former police officers' misconduct records that can be made available to future employers. They are also calling for an "early warning system" to identify at risk officers in need of additional training and mentoring, which, if enacted, could be a model for police departments across the country.[43] While not a perfect remedy, studies have shown that early warning systems have been effective at reducing problematic police officer behaviors in departments that have adopted them.[44]

## OTHER CONSIDERATIONS FOR POLICE REFORM

Unreasonable union protections are a driving factor behind the lack of police accountability, however they are not the only issue. Therefore, reforms should be considered at the local, state, and federal levels to encourage greater accountability and transparency.

### *Federal Reforms*

As previously mentioned, the federal government provides significant support to police departments through federal grants.[45] So long as the federal government continues to have such an active role in state and local policing, some analysts argue that conditioning federal grants on accountability and transparency measures could help to change officer behavior.[46]

For instance, federal funds could be conditioned on localities reporting officer misconduct statistics to the Federal Bureau of Investigation (FBI) to be incorporated into the National Use-Of-Force Database, and the federal government could establish uniform reporting requirements for these statistics.[47] The government could also condition grant money on police departments providing whistleblower protections to officers that report misconduct or mandating that officers report misconduct if they see another officer use unreasonable force.[48]

Another important step could involve the establishment of a database of police officer misconduct records, like the one ordered in President Trump's Executive Order on Safe Policing for Safe Communities.[49] A database of this kind would ensure that (a) misconduct records are not lost or destroyed when officers move to different departments, and (b) new employers have access to officers' entire histories before making hiring decisions.

Aside from simply conditioning grants on accountability and transparency requirements, the level of federal support for police departments could be responsive to a set of performance metrics. These metrics could include the number of misconduct cases at a department, complaints against officers, or officer convictions for abuses.[50] It is worth considering, however, that conditioning federal support on misconduct metrics of this kind could have the indirect effect of discouraging police departments from pursuing misconduct cases at all.[51]

The federal government could also establish best practices for policing and police training for federal law enforcement officers, specifically regarding use of deadly force, no-knock raids, and how to appropriately interact with individuals suffering from mental health issues or addiction. These could serve as a model to states and local law enforcement agencies for how police officers should be trained.

It is worth noting that use-of-force standards have not always been effective at lessening police violence. For instance, New York City banned chokeholds in 1993, two decades before the death of Eric Garner. Similar bans have existed in Chicago, Philadelphia, and Houston for years, but have largely been ineffective.[52]

Another consideration for increasing police accountability at the federal level is to reform qualified immunity. Normally, public officials can be held liable for civil damages if they violate an individual's civil rights in violation of 42 U.S.C. § 1983.[53] Qualified immunity, however, defined through the Supreme Court's interpretation of § 1983, shields public officials from civil liability if the victim cannot prove that the public official violated "clearly established law." According to the Supreme Court, law can be considered "clearly established" only if a prior court ruled on a case with identical circumstances; otherwise a "hypothetical reasonable official" would not have known that her conduct violated the individual's civil rights.[54] This type of defense, known as "qualified immunity," can be used as a defense only in civil cases, not in criminal prosecutions.

In instances of police abuse, qualified immunity has been invoked to shield officers from litigation after the killing of unarmed victims and other misconduct. For example, qualified immunity has protected a police officer who slammed a victim to the ground, breaking her collarbone, as well as an officer who released a police dog on a suspect after surrender.[55]

These and other recent events have led to calls for the elimination of qualified immunity. The Supreme Court, however, has acknowledged that some type of liability protection for public officials is necessary to discourage timidity.[56] Nevertheless, more than half of Americans agree that, without some kind of protections, police officers may be too afraid of legal action to faithfully execute their responsibilities – an increasingly important consideration as violence against law enforcement officers continues to escalate.[57]

Balancing the need to protect those who lay their lives on the line for our communities with the need for greater individual accountability poses a significant challenge. Congress is free to reform and codify the terms of any protection it chooses to provide by statute, including qualified immunity, and it should study the various proposals offered to improve the standard through Congressional action – including potential proposals to hold municipalities who fail to discipline officers liable for officer misconduct instead of individual officers.

A final consideration for reform would be civil asset-forfeiture laws. Currently, police may seize private property that is connected to alleged criminal activity

if an individual is suspected of a crime, regardless of whether that individual is found guilty. In fact, one study found that 80 percent of individuals subject to civil asset forfeiture were never eventually charged with a crime.[58] It is only after the suspects are found not guilty that they can attempt to retrieve their property, but it is not automatically returned to them; property owners bear the burden of establishing their innocence and retrieving their property. Furthermore, current federal law incentivizes state law enforcement agencies to seize private property and turn it over to the federal government. If they do so, states may keep as much as 80 percent of the proceeds of that forfeited property. Civil asset forfeiture laws could be amended to prevent police from seizing private property until after a suspect is convicted of a crime, and the federal government could eliminate "equitable sharing" programs with state law enforcement that provide profit incentives for the unreasonable seizing of private property.[59]

### *State Reforms*

Unions are not the sole providers of special protections for police officers; states have passed their own laws safeguarding police from the consequences of their actions. The first set of protections, called civil service laws, protect at least 80 percent of all public officials by heavily regulating their hiring and firing – a large reason why the layoff rate is so low in the public sector.[60] By making it exceedingly difficult to fire police, civil service laws are also a significant barrier to police accountability. Over time, these laws have expanded to also regulate "demotions, transfers, layoffs and recalls, discharges, training, salary administration, attendance control, safety, grievances, pay and benefit determination, and classification of positions."[61] The protections awarded from state civil service laws empower public officials to challenge any action by their employer that would substantially affect them, including possible disciplinary action. States could follow the leads of Florida, Georgia, and Texas by eliminating civil service protections for public officials.[62]

The second set of state protections for police officers are awarded through Law Enforcement Officers' Bills of Rights (LEOBRs). LEOBRs specifically protect officers during disciplinary investigations. For instance, laws in Maryland – the first state to pass a LEOBR law – prevent civilians from investigating police officers, limit officer interrogation procedures, and allow police officers to remove civilian complaints from their personnel files after three years. Similarly, California's LEOBR laws bar the use of polygraphs when interrogating police officers, and Illinois prevents citizens from filing anonymous complaints against police officers.[63] Fourteen states currently have LEOBR laws, and as many as 11 other states are considering similar legislation.[64] Reforming LEOBR laws could be considered as another way to increase police accountability.

Furthermore, states could roll back Marsy's law protections for police officers. These protections, originally meant to protect victims' rights to privacy, have been interpreted by the courts to protect police officers as well. The courts' interpretations give officers the same rights as victims, allowing them to shield

their identities after use-of-force incidents, avoid public scrutiny, and conceal their prior misconduct records or history of abuse from the public.[65] To date, 11 states have passed Marsy's law protections including California, Florida, Georgia, and Ohio.[66] Rolling back these protections would pave the way for new rules mandating that officer misconduct records be made public after an abuse of power.[67]

Finally, states could consider reforming their pension systems to bar officers from receiving pensions if they are convicted on certain criminal charges, for instance killing a civilian.[68] Currently, only 15 states have policies revoking or reducing police officer pensions after they are convicted of a felony related to misconduct, even though research finds that pension forfeiture laws are positively associated with lower rates of police misconduct.[69]

### *Local Reforms*

Local reforms are perhaps the most important. Policing is a decentralized, community activity; there are more than 12,000 local police departments in the United States with more than 800,000 police officers.[70] Local leaders, including local police departments, have greater knowledge of specific issues plaguing their communities and therefore are more adept at finding solutions. Similarly, Americans care more about issues facing their own communities than problems elsewhere.[71] While federal and state governments can reform current laws that provide perverse incentives for police or set guidelines for localities to follow, changing the culture of police misconduct can only be accomplished through the actions of individual officers and communities.

Reform can occur in a variety of ways. For instance, 76 percent of individuals support moving "some money currently going to police budgets into better officer training, local programs for homelessness, mental health assistance, and domestic violence."[72] It is important to consider, however, the impact of reducing police funding on officer recruitment and retention, officer morale, and local crime to ensure that communities do not suffer from higher crime rates.

Alternatively, communities could more heavily rely on social workers, mental health experts, and other practitioners to respond to some community crises. For example, the police department in Eugene, Oregon has operated with local nonprofits for over 30 years to deploy social workers – instead of police officers – when crises call for a different type of expertise. The program has resulted in significant public safety cost savings and established worthwhile trust in the community.[73] This result is undoubtedly beneficial; previous Social Capital Project research has demonstrated that, as social trust within communities rises, so does self-reported happiness.[74]

Ultimately, it is up to each individual police department to reform its own policies and cultures that encourage abuse of force by police and discourage police accountability. Worthwhile reforms could include improving officer

training around de-escalation and disengagement techniques, improving field training programs, instituting "duty to intervene" orders, and creating cultures where excessive use of force is not only frowned upon, but expected to be met with disciplinary action.[75] For example, the Dallas Chief of Police implemented a duty to intervene order two weeks after the killing of George Floyd, mandating that officers stop or attempt to stop other officers when they witness inappropriate use of force.[76]

Additionally, some suggest that localities could create boards with significant civilian representation to review instances of deadly use of force and give them the power to compel testimony and documents.[77] While these boards may increase accountability, it is also worth considering their potential negative ramifications. For instance, if civilian review boards abuse their power, it could discourage police officers from taking actions necessary to protect their communities.

The movement toward community policing is also gaining momentum. Community policing is a different model of law enforcement based on trust. It has two components: community partnership and problem solving. Community policing requires police to develop positive relationships with the community, involve the community in crime control and prevention, and identify the community's specific concerns as well as the most appropriate remedies for them, which do not always involve police.[78] As such, community policing strengthens both bonding social capital – the relationships between individuals in the same group, i.e. between friends, coworkers, and neighbors – and bridging social capital – the relationships between individuals in different groups, i.e. between police officers and community residents. Both bonding and bridging capital are important for rebuilding civil society. According to research, bonding capital encourages community trust while bridging capital promotes perceptions of legitimacy. In terms of policing, "those individuals living in neighborhoods with high levels of bridging capital are more likely to define police behaviors as promoting procedural justice," while bonding capital "influences resident willingness to cooperate with the police."[79]

An often-cited example of community policing is Camden, New Jersey. Five years after shifting to a community-policing model in 2013, Camden's murder rate fell to its lowest level since 1987. Similarly, the number of robberies, assaults, violent crimes, property crimes, and non-fatal shootings in Camden have fallen every year since. According to one officer, "when you have (community policing and transparency) as a value within your organization, the community tends to know. You can feel the difference."[80]

## CONCLUSION

As public trust in institutions has fallen, civil society has suffered. One of the most apparent examples of this today is Americans' declining confidence and trust in the police. Recent instances of police abuse have led to widespread demands for action. The most recent – the killing of George Floyd – inspired peaceful protests, violent riots, and brought the nation to a turning point. Restoring trust in law enforcement requires meaningful police reform.

This paper demonstrates that controversial protections provided by police unions are a driving factor behind the lack of police accountability today. These protections shield police officers from disciplinary action and act as a barrier to investigatory due process. In fact, empirical research demonstrates a causal link between union protections and police abuse. The first step toward reform, therefore, is to increase transparency around police union policies and access to prior histories of officer misconduct, as well as to roll back unreasonable union protections shielding bad apples from discipline.

Reforming police unions, however, will not be enough. There are myriad other barriers to police accountability also in need of reform, including qualified immunity, federal policies encouraging civil asset forfeiture, and state laws that reduce accountability even further. It is the responsibility of the federal and state governments to resolve these issues.

Ultimately, the success of police reform will depend on the actions of communities. Citizens must—and do—recognize the contributions that police officers make, day-in and day-out, to keep the streets safe. But police officers have a duty to serve the communities they patrol and the residents of those communities whose tax dollars employ them. Even the most dedicated officers contribute to the erosion of community trust when they look overlook wrongs committed by bad apples or support the efforts of unions to protect them. Removing barriers to police accountability would help to prevent harmful police actions by officers who fail to live up to their duty, thus helping to increase trust in an institution largely made up of honorable men and women who serve to protect America's communities.

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# Making it More Affordable to Raise a Family

# Priced Out:

## Why Federal Tax Deductions Miss the Mark on Family Affordability

SCP REPORT NO. 1-20 | MAY 2020

Housing expenses are often the biggest single financial barrier to starting a family. Aspiring or expectant parents often require a greater amount of livable space to accommodate a new family member. In many parts of the country, that space comes at a premium. This increase in housing consumption is often coupled with a move from rental housing to owner-occupied housing.

However, skyrocketing home prices in recent years have made it difficult for many young adults to take this critical step. Particularly difficult is getting together a down payment, a large and growing challenge for young would-be homeowners. This report argues that tax policy aimed at making homeownership more affordable has increased the wealth of older Americans who own their homes, but by increasing home prices it has made homeownership less attainable for younger families, impeding family formation.

The problem is ultimately a product of the timing of income and spending over the life cycle. Prior to the COVID-19 epidemic, Americans were earning more than ever—typically enough to cover their housing costs over the long run, and to do so more easily than they did in the past. This will eventually be the case again once the epidemic recedes. However, even in normal times there are short- and medium-run mismatches between when income is earned and saved and when it is most needed. For example, people tend to earn the most in middle age, but they have expenses throughout their lives. This presents a challenge for young families, whose household heads have not yet reached middle age. While they have strong future earning prospects and can amortize most of their home costs over a long period at low mortgage interest rates, they are relatively short on liquid savings that could be used towards a home purchase.

Public policy interacts with these life cycle timing issues; there are tradeoffs between making life easier at one age versus another. Sometimes, this is clearly intended: for example, under Social Security, one remits payroll taxes to the government during prime earning years in order to receive benefits in retirement. However, sometimes this can happen in an unintended manner: a seemingly-age-neutral policy may affect different age groups in different ways.

Federal tax policy interacts with housing affordability through itemized deductions on Schedule A of Form 1040—particularly, the deductibility of property taxes and the deductibility of mortgage interest. While these itemized deductions are available to taxpayers of any age, they have a differential impact, on average, on the finances of taxpayers in different age groups.

While these deductions are intended to increase housing affordability and are a boon to current homeowners, they can have the perverse effect of increasing the price of existing homes, making it hard for young would-be-homeowners looking to buy for the first time. Theoretical models predict such an increase, especially in high-priced cities with relatively inelastic housing supplies. Furthermore, the curbing of the property tax and mortgage interest deductions in the 2017 Tax Cuts and Jobs Act (TCJA) slowed house price growth, consistent with those model predictions.

There is a strong family affordability case for avoiding policies that increase home prices. Even if mortgage interest deductibility and property tax deductibility do make housing less costly for many Americans over the course of the life cycle by reducing the after-tax cost of monthly mortgage and property tax payments, they also engorge home prices. This time structure for the expenses—a bigger up-front cost, followed by cheaper after-tax monthly payments—is not a favorable schedule for Americans under 45, who have plenty of earning years remaining but relatively fewer savings.

Evaluated through the lens of family affordability, this is a failure. People under 45 are responsible for 99.75% of births in the United States.[1] Their families are most likely to be growing, and they are most likely to need more space. If public policy is to have an effect on the timing of house payments, it should make that timing more favorable to people in the under-45 age bracket, not less. At a minimum, it should do no harm. Therefore, this report recommends the continued limitation of housing-related tax deductions, especially at the higher end of the market where they are most likely to be capitalized into higher home prices.

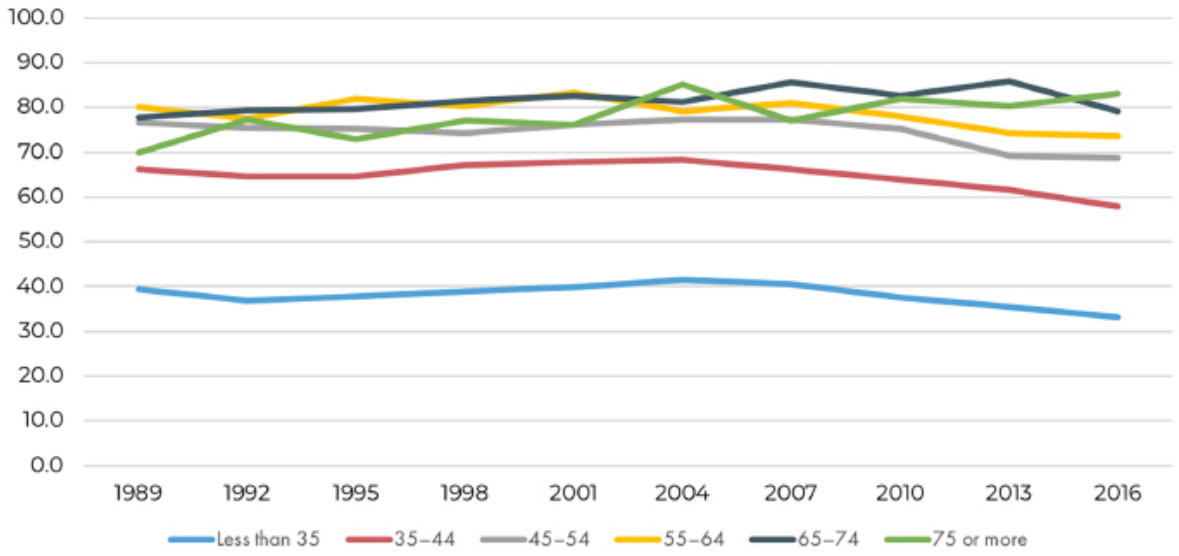
## THE STATE OF HOMEOWNERSHIP BY AGE, 1989-2016

Homeownership provides some important benefits over the alternative of rental housing. Owner-occupied housing aligns the interests of owner and occupant, allowing for efficient decision-making and eliminating the tenant-landlord conflicts that can arise from renting. This eliminates some of the ongoing transaction costs of rental arrangements, where both renter and landlord may need to insure or self-insure against conflicts with a counterparty. Homeownership also confers some financial benefits that would not be available to renters; for example, rather than devoting a stream of taxable income to paying rent, owners receive a stream of in-kind income—the ability to live in the house—that goes untaxed. Finally, owner-occupied units also tend to provide a step up in quality: they are larger in relative terms than rental units and more customizable.

For young married couples looking to start a family, upsizing to an owner-occupied home is often an important and useful life milestone. However, a look at the last thirty years of data shows that younger Americans are less likely to be homeowners than they were in the past. The following analysis uses the Federal Reserve Board's Survey of Consumer Finances (SCF), a triennial survey with detailed data on household income and net worth between 1989 and 2016.

A comparison of homeownership between the oldest and most recent years of the survey shows that all age groups younger than 65 were less likely to own their primary residence in 2016 than people of the same age were in 1989. Most of this decline in homeownership came after the 2008-2009 housing crisis. Rather than recovering to pre-crisis norms, homeownership continued to decline for working-age households, all the way through the 2009-2020 expansion.

Trends in Homeownership by Head of Household Age




Source: Federal Reserve Board Survey of Consumer Finances, Table 9, https://www.federalreserve.gov/econres/scfindex.htm

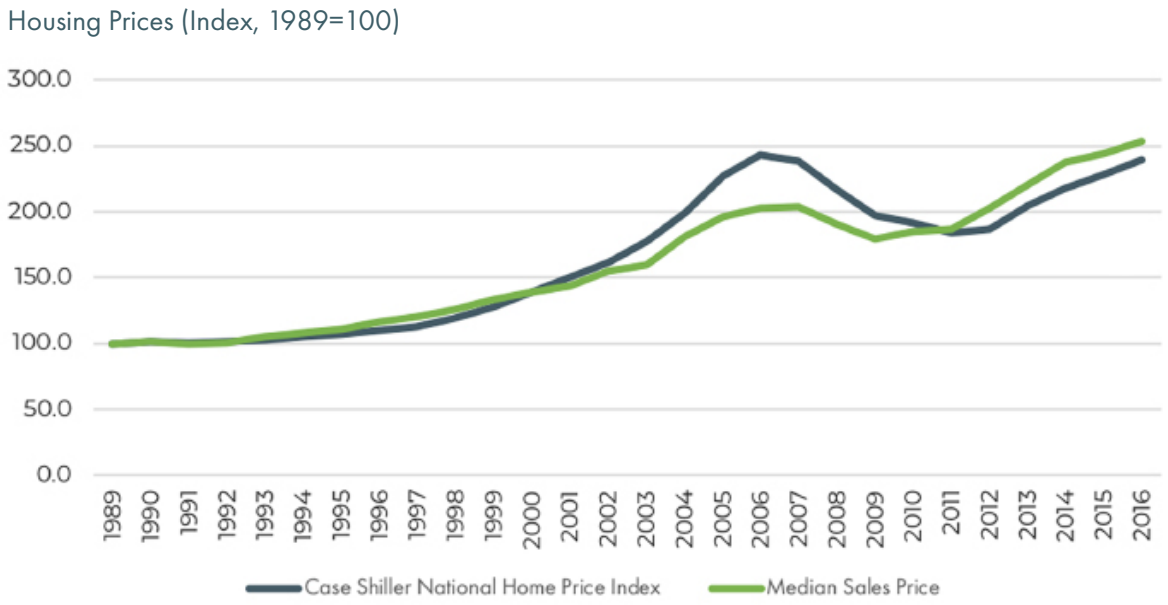
The declines in ownership among those less than 35 years old and ages 35-44 should be a particular cause for concern. While their low ownership rate could be a personal choice, many younger people aspire to own and see it as a prerequisite for key life steps such as marriage or parenthood.[2] While most people do eventually achieve homeownership later in life, it often comes substantially later than marriage or parenthood—and later than similar families would have owned in 1989.

## THE STATE OF HOUSING AFFORDABILITY FOR YOUNG FAMILIES, 1989-2016

The most obvious barrier to homeownership is cost. The purchase can typically be divided into two categories of expense: the up-front expense of the down payment and the recurring expenses of debt service and property taxes. Up-front expenses are paid with accumulated wealth, and the recurring expenses are paid with future income. While families have some flexibility in theory to shift expenses between these two categories (for example, by lowering or increasing the percentage of money down) there are limits to this flexibility. Most first-time homeowners can only afford a small down payment, but lenders may require mortgage insurance or increase the interest rate for buyers who put less money down.

Two major long-run trends have affected housing affordability since 1989: an increase in home prices and a decrease in long-term interest rates. The former trend has made down payments more difficult, but the latter trend has made it easier to finance the remainder of the principal through recurring payments.

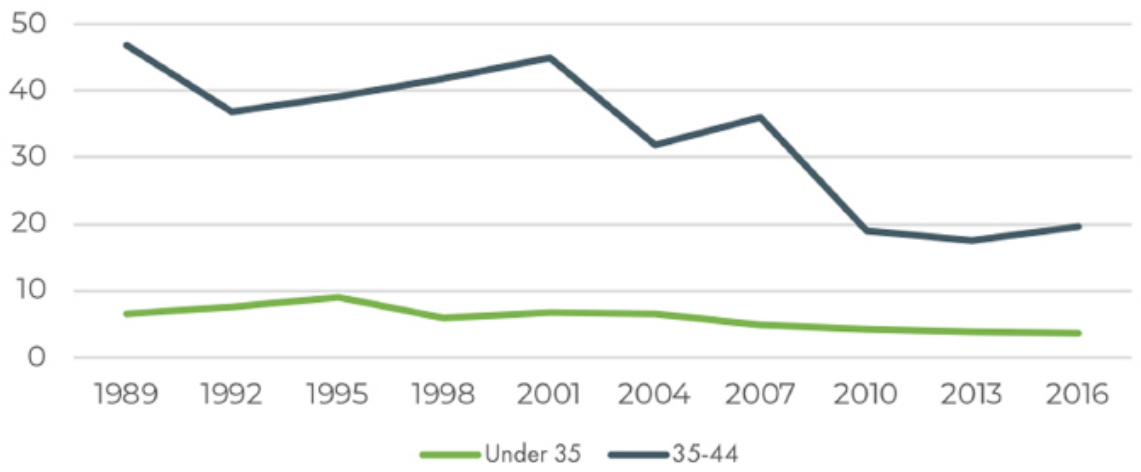
From 1989 to 2016, the price of homes more than doubled. The median new residential sale was $305,125 in 2016, up from $120,425 in 1989.[3] This was a fast increase in prices: 153 percent over 27 years. A more sophisticated method from economists Karl Case and Robert Shiller, known as repeat-sales indexing, tracks price changes found in multiple sales of the same home. It shows a smaller increase of 140 percent, suggesting that some of the increase in median home prices is attributable to improved quality.




Source: S&P/Case-Shiller U.S. National Home Price Index, retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/CSUSHPINSA; U.S. Census Bureau and U.S. Department of Housing and Urban Development, Median Sales Price of Houses Sold for the United States, retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/MSPUS

This rise in home prices has made it more difficult for young families to afford a down payment. The chart below shows median net worth for young households as a percentage of median home price—in other words, the percentage down payment they could afford if their net worth were typical and applied entirely to the purchase of a typical home. Net worth for a family with a household head under 35 was 6.5 percent of the median home price in 1989, but just 3.6 percent in 2016. For households whose head was between 35 and 44, that percentage fell from 46.8 percent to 19.6 percent over the same period.

Median Net Worth as a Percentage of Median Home Value, by Age of Household Head

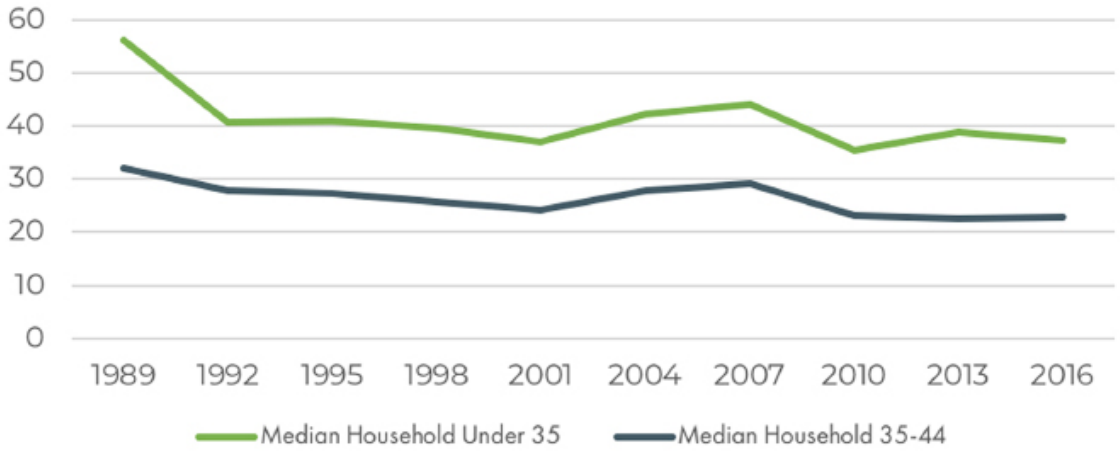



Source: Federal Reserve Board Survey of Consumer Finances, Table 4, https://www.federalreserve.gov/econres/scfindex.htm; U.S. Census Bureau and U.S. Department of Housing and Urban Development, Median Sales Price of Houses Sold for the United States [MSPUS], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/MSPUS.

The declining ratio of net worth to home value is matched by the trend in actual down payments for first-time buyers as reported by the National Association of Realtor's Profile of Home Buyers and Sellers (HBS). The median first-time buyer made a 10 percent down payment in 1989, but just 6 percent in 2016.[4] In other words, buyers are financing a greater portion of their home purchases.[5]

On this front, there is much better news: despite the increase in home prices, monthly mortgage payments have become more affordable. This affordability is driven by rising incomes and falling interest rates. In 2016 the average 30-year fixed mortgage was 3.65 percent, down from 10.32 percent in 1989.[6] The 153 percent rise in average home prices corresponds to just a 29 percent increase in the nominal monthly payment on a 30-year fixed mortgage after the drop in interest rates is taken into account. As nominal incomes have risen by considerably more than this, the debt service payment has become more affordable.

Debt Service Payment on a Median Home as a Percentage of Household Income




Note: Assumes a 90 percent LTV ratio and a 30-year fixed mortgage at average rates

Sources: U.S. Census Bureau and U.S. Department of Housing and Urban Development, Median Sales Price of Houses Sold for the United States [MSPUS], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/MSPUS, April 1, 2020. Federal Home Loan Mortgage Corporation, 30-Year Fixed Rate Mortgage Average in the United States [MORTGAGE30US], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/MORTGAGE30US, April 1, 2020. Federal Reserve Board Survey of Consumer Finances, Table 1, https://www.federalreserve.gov/econres/scfindex.htm. Author's Calculations.

These measures of housing affordability ultimately yield some mixed conclusions on affordability. Today's under-45 workers have more skills and more expected future income than has any generation that came before. But future opportunities are not "cash in the bank" unless leveraged into a mortgage, and high leverage comes with risks and drawbacks.

In the Joint Economic Committee report *The Wealth of Relations*, one factor discussed in declining family formation is increased educational attainment. Education is a deeply worthwhile end in itself and often instrumentally useful for increasing labor productivity. However, it also creates tradeoffs and challenges that did not exist in the past.[7] Education takes time and effort; forgoing work opportunities in exchange for schooling can make it hard to build financial wealth early in one's career, even if it is extremely beneficial later on.

Another trend that makes this comparison more complex is household size, which has declined since 1989. Americans are marrying later. This mechanically reduces wealth per household by reducing the number of adults per household. The relationship can be causal in both directions—marriages help build wealth and economies of scale in housing, but wealth-building is often seen as a prerequisite for marriage.

This analysis has a few limitations. It uses a simple nationwide median home price, which obscures some details of interest. Median home quality has likely risen, as implied by the Case-Shiller index; square footage has also risen.[8] Attempting to hold housing quality constant by using the Case-Shiller index would show 2016 to be slightly more affordable than is suggested in the above analysis of the median.

Housing market conditions are also quite diverse across geography. Some areas are cheap even as nationwide house prices have risen; others are expensive even if the purchase is financed at low rates.

Finally, median is not an ideal measure for cost to young families; younger households who are often first-time buyers are likely to face lower prices for older, smaller homes. The median home price was $257,000 in 2019, but it was just $215,000 for first-time buyers.[9] The typical home purchased by a first-time buyer was 1,620 square feet, versus 1,850 square feet among homebuyers generally.[10] While the analyses in this section are based on new single-family homes, new homes as a whole constituted just 14 percent of home sales in 2016, down from 29 percent in 1989.[11] The median purchase price of new homes in 2019 was $329,750, while it was just $245,000 for previously owned homes.[12]

The overall question of whether homes have become more or less affordable to the average young American household is a difficult one that hinges on how the terms are defined. However, there is strong circumstantial evidence that down payments, not monthly payments, are the greater financial challenge for first-time homebuyers.

## THE INTERACTION BETWEEN FEDERAL TAXES AND HOME PRICES

The federal income tax code includes two deductions that interact with housing: the deductibility of mortgage interest and the deductibility of residential property taxes. The latter is part of a broader policy of limited deductibility of state and local taxes.

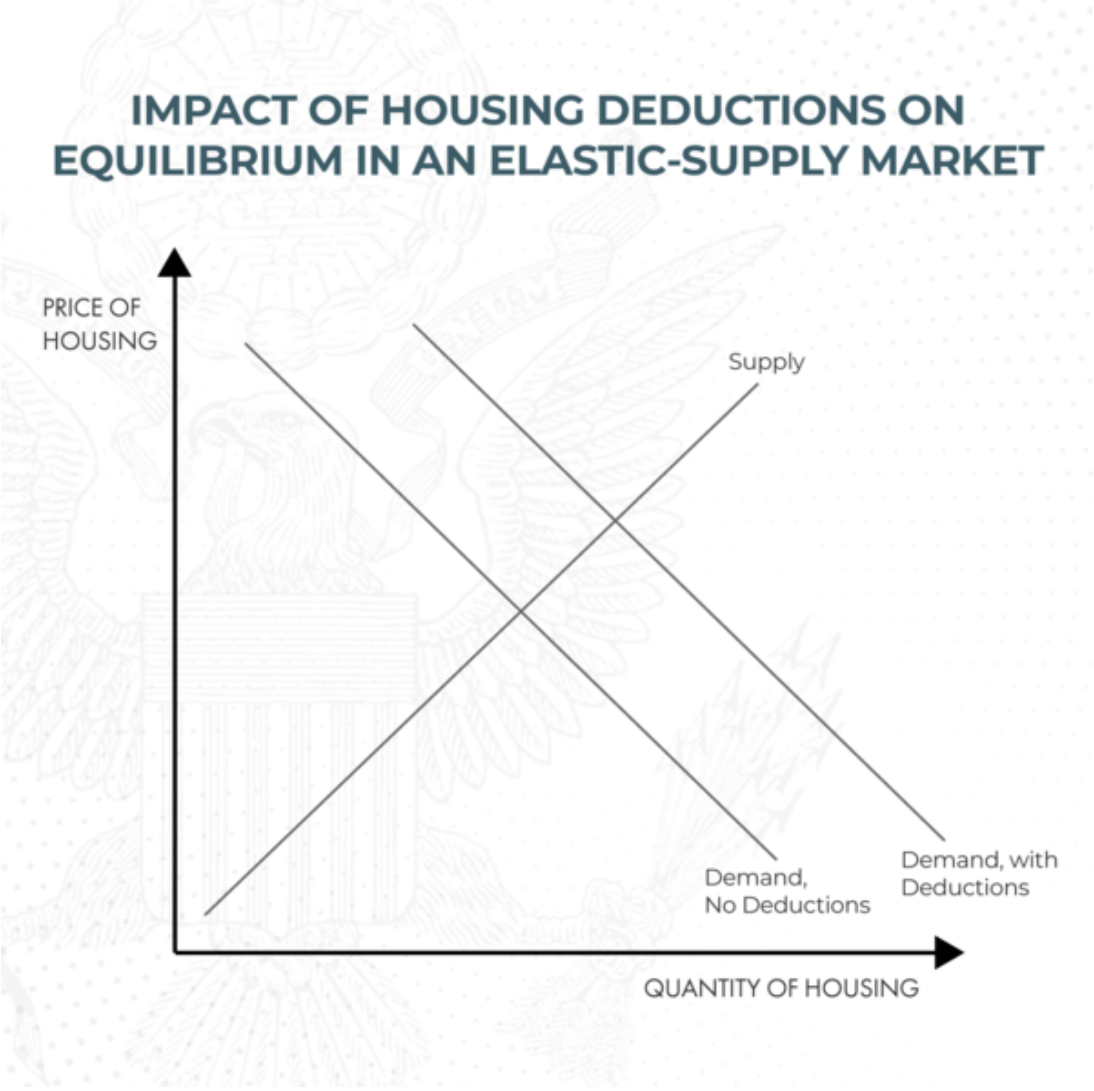
The mortgage interest deduction allows taxpayers to deduct the portion of housing debt service payments attributable to interest, not principal repayment. Its value only applies to the interest on the first $750,000 of principal of a home. For example, someone who had $1.5 million in debt would be able to count only half of the interest paid towards the mortgage interest deduction. The state and local tax deduction allows taxpayers to deduct up to $10,000, combined, of all state and local taxes, including residential property taxes.

These two deductions both pertain to the ongoing expenses of housing; they are both tied to periodic payments associated with homeownership, not with

the initial purchase price. They can soften the monthly payments, effectively reducing those payments by the marginal tax rate to which the deduction applies. By contrast, these deductions do not help with the down payment. Their first-order effect is to help with the easier part of paying for a home, not the harder part.

It is also useful to consider second-order effects. The second-order effect is that people become willing to pay more for homes, knowing that the tax benefits on monthly payments are available. A more formal model of this behavior is available in the Appendix, but it can be understood relatively simply: a home that comes with some associated tax deductions is surely more valuable to its owner than the same home in the absence of the deductions.

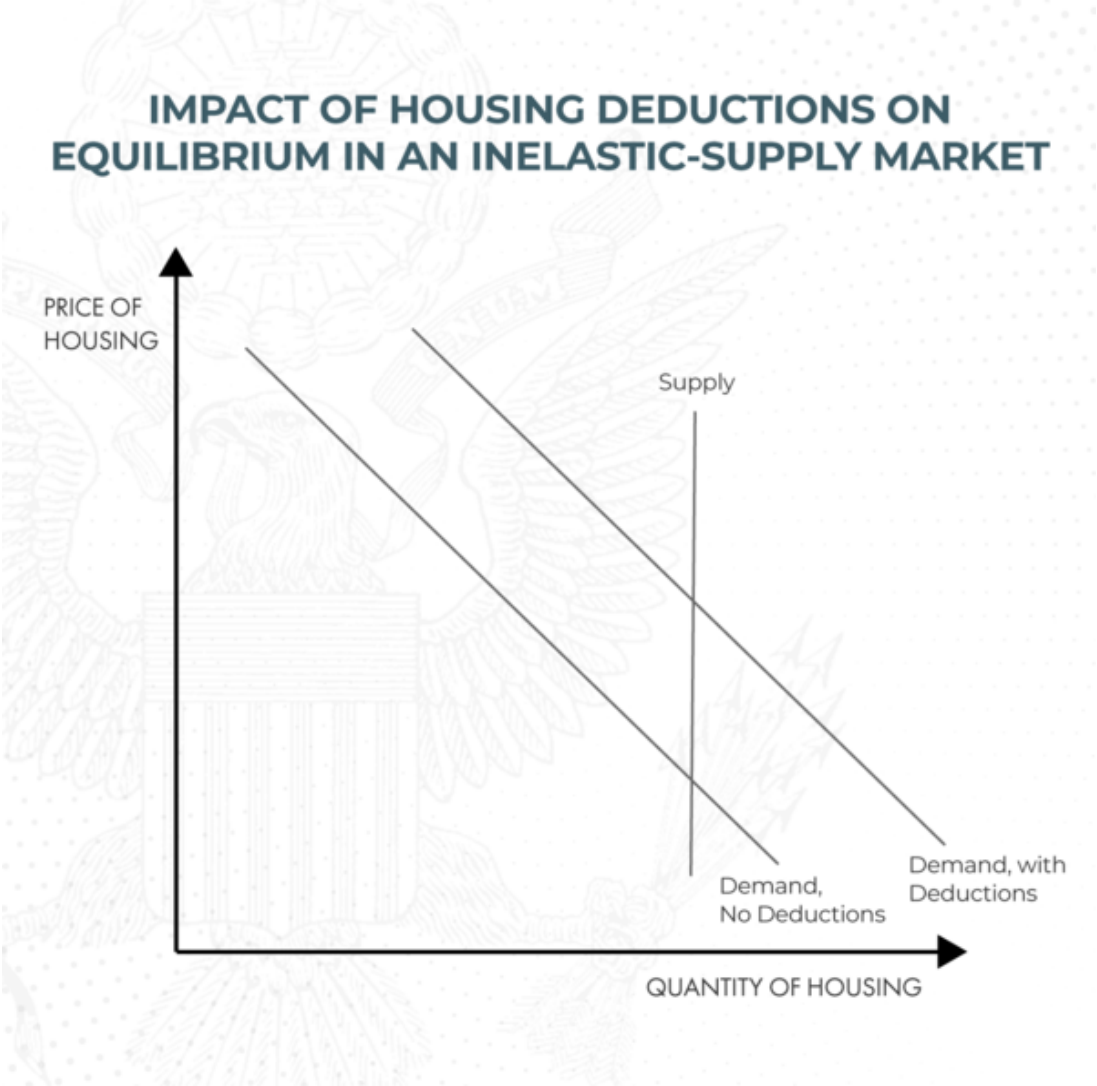
Finally, one can consider third-order effects; how does the housing market respond to the increased demand from buyers? This could—in theory—increase the supply of housing by drawing more housing into production. In the ideal case, the policy would have an effect similar to the one pictured below:



In this example, houses are more desirable with tax deductions, and users' willingness to pay is increased. This willingness to pay flows through to the housebuilding industry, making it more profitable. The housebuilding industry responds by increasing quantity supplied. Under these circumstances, the policy potentially achieves the goal of supplying more housing—particularly, owner-occupied housing.

Even in this best case, there are caveats; home prices still rise somewhat, potentially making down payments more difficult for first-time buyers. Additionally, "quantity of housing" could expand by offering larger homes to the people who can already afford homes, not by increasing total home quantity.

Moreover, this best case—as our label for it suggests—is not the only possibility. Consider a city in which all homes are already built, and construction of new residential dwellings is effectively prohibited through zoning or other laws. In this case, supply is inelastic. By definition, it is impossible to expand housing supply.



In such a market, tax deductions increase the willingness to pay, just as they did before, but the benefit becomes embedded entirely in the price of the home, and no new construction happens. In this case, the economic incidence of the deduction is entirely on the incumbent homeowner. The homeowner can, of course, sell the home—and the right to the associated tax deductions—to another person, but he or she will be able to charge extra for that privilege.

Under this specific circumstance, the housing tax deductions fail—and fail spectacularly—at making housing more available or affordable for families. An obvious way to demonstrate this is to note that there are no new homes; by definition, housing has not become more available.

It is also not more affordable; every dollar of the deductions is capitalized into the value of the home. This makes the down payment—the difficult hurdle for young families, even in median neighborhoods—more expensive than it would be otherwise. The affects aren't entirely bad. If potential homebuyers succeed at getting together the down payment, they benefit some from tax deductions on the back end; but those tax deductions are a privilege they paid for in the purchase price of the home, and the net benefit to a new homebuyer is zero.[13]

Some parts of the United States are closer to the first model, and new housing is built regularly. Other parts of the United States are closer to the second model, and new housing construction is mostly impossible because of zoning regulations. In general, increases in rules and restriction on land use tend to be associated with higher housing prices.[14] In a few metropolitan areas, such as San Jose, this is particularly acute.

The hallmark of a high-demand inelastic-supply area is extraordinarily high housing prices—ones that greatly exceed the cost of construction. High prices suggest that it would be profitable to bring more supply online, if it were possible to do so. Enduring high prices suggest that there are significant barriers to bringing new supply into the market.

To sum up the positive predictions from this analysis so far: there is good reason, in economic theory, to expect that itemized tax deductions raise the price of houses and do so particularly in expensive areas with an inelastic housing supply, such as San Jose. Removing or limiting these tax deductions, by contrast, would lower the price of houses, or at least slow their growth.[15]

## THE EMPIRICAL RELATIONSHIP BETWEEN TAXES AND HOME PRICES

Some of the best-known empirical work on the relationship between mortgage interest deductibility and the housing market comes from a National Bureau of Economic Research (NBER) study of a major Danish tax reform in the 1980s, which curbed mortgage interest deductibility. The study found that the limitation on mortgage deductibility had no effect on the quantity of homeownership, but it did cause people to scale back square footage, and it reduced home prices. The effect on prices was larger than the effect on square footage.[16]

The results of this study suggest that mortgage interest deductibility does not help more people become homeowners, but that it does engorge the price of homes generally and finance the construction of larger homes than would have otherwise been constructed. These empirical results are consistent with the theoretical models described previously.

The United States recently passed a tax reform bill which can once again test the hypothesis. The tax reform passed by Congress in 2017 limited itemized deductions, changing the tax treatment of housing in ways not dissimilar from the Danish reform described above. This 2017 tax reform, the Tax Cuts and Jobs Act (TCJA), made three important changes to the tax code that affected housing:

- It limited the mortgage interest deduction to apply only to the first $750,000 of principal, rather than the prior limit of $1,000,000. This means that on any loan whose outstanding principal is greater than $750,000, an additional marginal dollar of borrowing does not result in an increase in mortgage interest deduction allowed;
- It limited deductibility of state and local taxes to the first $10,000. This means that for any taxpayer who would already reach this limit, home value at the margin does not trigger any new property tax deductibility;
- It nearly doubled the standard deduction. For example, for married couples, the standard deduction rose from $13,000 to $24,000.

The last change requires some explanation. While the first two changes are explicit reductions in housing-related tax deductions, the last change is an implicit one. The first two deductions are known as “itemized deductions” in the federal tax code. The standard deduction is an alternative to itemized deductions; taxpayers must pick one or the other. In an economist’s language, the standard deduction is the opportunity cost of taking itemized deductions. Itemized deductions are only valuable insofar as they exceed the value of the next best alternative, so the increase in the standard deduction reduced the share of taxpayers who itemized, and it also made itemization less valuable in relative terms for those who still did itemize.

It is also worth noting that these changes, collectively, applied substantially more to expensive houses in high-income areas. Most taxpayers, even prior to TCJA, chose the standard deduction rather than itemized deductions; they got no value out of the deductions that were curbed.

Furthermore, the explicit caps on these deductions were high. The limit on mortgage interest deductibility, for example, applies to houses more than twice the national median price. The limit on state and local tax deductibility also applies only to the kind of high-income household that would have at least $10,000 in state and local taxes—a far above-average tax burden.

Coupling these facts about TCJA's policy provisions with the typical models of housing prices, or the empirical results from Denmark, we can make testable, empirical predictions about what the consequences of the law would be. The TCJA should reduce home prices in areas with expensive housing—or at least cause them to grow more slowly than they would otherwise.

These empirical predictions, so far, have been borne out by the reality. The state of housing across the United States—especially at the high end of the scale, where TCJA's changes are most relevant—has changed substantially since the bill was passed.

The analysis below focuses on high-priced homes, not because their affordability matters more than low-priced homes, nor because young families would be expected to buy them as starter homes. Rather, the high end of the housing market is the focus, first, because that was the price range to which TCJA's provisions most strongly applied, and therefore, the range for which TCJA is an interesting experiment. Second, a focus on the high end shows how deeply unmoored the mortgage interest deduction's actual effects were from anything resembling greater "affordability." While the deduction was ostensibly a universal policy to help with homeownership, an extraordinary portion of its value was capitalized into expensive lots in exclusive neighborhoods.

The best way to see how TCJA changed the housing market is to look at the trends that were in place prior to its enactment. Home prices had begun to recover from the 2007-2009 crisis around the beginning of 2012. From that point until the end of 2017, the prices of all homes grew—but the prices of high-quality homes in high-cost areas grew faster than average. There was a divergence, or a widening of the spread in house prices.

Annualized Price Growth for Zillow Top Tier Homes by Metro Area, Jan 2012-Jan 2018

Source: Zillow ZHVI Top Tier Time Series, https://www.zillow.com/research/data/

The data for this chart come from the Zillow Home Value Top Tier time series, which looks specifically at homes in the 65th to 95th percentile for their metropolitan area. The data for the pre-TCJA housing recovery show that high-priced metropolitan areas (MSAs) had somewhat faster price growth than the rest of the country. The most exceptional data points are San Jose and San Francisco, which were already first- and third-most expensive even at the beginning of the recovery, and then first and second in growth for the next six years. Even without these exceptional cities, though, there was still a modest trend of home values in expensive areas outpacing those in less-expensive areas.

While these fast-rising prices were good news for incumbent homeowners, they were bad news for would-be buyers; particularly, for young people with good future prospects but not nearly enough liquid wealth to pay exorbitant prices.

At the end of this period, TCJA was signed. From 2018 to 2020, the trend reversed itself entirely. Low-cost areas began to catch up.

Annualized Price Growth for Zillow Top Tier Homes by Metro Area, Jan 2018-Jan 2020

Source: Zillow, Author's Calculations

After TCJA, the entire character of the U.S. housing market changed. Formerly-unstoppable markets at the high end slowed, and moderate-priced cities like Boise and Salt Lake City began to shine.

These outcomes strongly suggest the theories about the incidence of the tax deductions were right: in high-cost low-elasticity markets where the deductions were most relevant, they were capitalized into the values of the homes. Removing the deductions appears to have—at least temporarily—slowed the frenetic house price growth in these places.

The evidence from TCJA so far suggests that housing-related tax deductions were counterproductive prior to 2017. Imagined at their best, these deductions would have made the monthly payments on a humble four-bedroom home more affordable for a couple of 33-year-olds with two children. However, in reality, much of the value of the deductions was capitalized into the values of million-dollar homes in the expensive neighborhoods of expensive cities, further driving up their prices. The actual effects of housing deductions—at least, the parts sensitive to TCJA's limitations—were contrary to the original vision.

Furthermore, the evidence from the higher-priced homes affected by TCJA is suggestive of what might happen if similar tax reform applied to lower-priced homes as well. It is possible that home prices would fall, making the owner-occupied market easier to break into.

## POLICY IMPLICATIONS OF THE RELATIONSHIP BETWEEN TAXES AND HOUSE PRICES

The major policy implication of the analysis above is that the itemized tax deductions for housing—at least at the high end, as currently structured—are a failed policy. The first-order effect of these deductions is to improve owners' abilities to make recurring payments (which have grown relatively more affordable over time) but not down payments (which have grown relatively less affordable over time.) While improving home affordability is a laudable goal, these deductions may not be helping in the most effective way.

The second-order effect of these deductions is to raise people's willingness to pay for housing, increasing prices, enriching incumbent homeowners, and making it harder for liquidity-constrained new families to break into the market. These second-order effects are not particularly desirable, as they put an additional load on first-time homebuyers.

In a subset of markets—the elastic ones—a third-order effect exists: higher willingness to pay may help bring new housing supply online. If so, the deductions would improve housing quantity and quality in the United States, and therefore make it more affordable to raise a family. (Though even in these markets, some of the value of the benefit will likely be captured by existing homes, rather than be allocated to producing new ones.) However, in the inelastic markets with sky-high prices, further tax deductions are merely captured by wealthy incumbent homeowners.

The limitations on housing itemized deductions in TCJA were therefore a good policy choice. If a policy like the mortgage interest deduction is truly about increasing housing affordability, then high-dollar markets are not a fruitful target; they are already unaffordable, often from limited supply, and adding deductibility for a bit more interest is will not address those issues. The limits on these itemized deductions should be made permanent.[17]

Furthermore, mortgage interest deductibility could be limited further; for example, the Family Fairness and Opportunity Tax Reform proposal from Senator and Joint Economic Committee Chairman Mike Lee expanded the mortgage interest deduction's eligibility at the low end, but restricted it to a maximum of $300,000 in principal.[18]

These limitations are, of course, revenue-raising, and therefore at their strongest when used in balance with more successful family affordability measures that return those revenues back to families. For example, Senator Lee's proposal expands the Child Tax Credit and counts it against families' combined income and payroll tax liabilities. Indeed, any measure designed to give young families a break and build more wealth could be effective in helping them get over the down payment hurdle.

The federal tax code's current provisions to improve housing affordability have a mixed record at best. If they help housing affordability, they do so at the wrong time. Empty-nesters, whose children have grown and left the household, are wealthier than they have been in the past. However, younger adults hoping to start a family are not doing as well. Federal tax policy should perhaps account for this reality—or at least, not make it worse. The current slate of itemized deductions is ineffective in achieving the goal of family affordability, and the system is therefore ripe for reform.

## *Appendix: Formally Modeling the Relationship between Tax Deductions and Willingness to Pay*

House deeds are a property right. The property right confers a consumption benefit—in that one can live in the house, and this is valuable—but these deeds also come with many costs and tie up money that could be invested elsewhere; absent the gains one gets from living in homes, they are relatively poor investments.

One way to analyze homeownership is to balance the benefits of living in the home against its relative weakness as a financial investment. The price of the home should rise or fall until the benefits of living in it perfectly offset the financial drag, or "user cost."

A "user cost" expression for a marginal dollar of housing in the United States can be expressed like this:[19]

$$UC = LTV(1-\tau)\, r_m + (1-LTV)(1-\tau)\, r_e + (1-\tau)b + (1-\tau)\,\delta_p + \tau\delta - \pi$$

Where UC is user cost per unit of purchase price, LTV is loan-to-value ratio, $\tau$ is the federal tax rate, $r_m$ is the mortgage interest rate, $r_e$ is the opportunity cost of equity, b is the risk premium on the real estate, $\delta_p$ is the property tax rate, $\delta$ is the economic depreciation on the home, and $\pi$ is the expected rate of capital gains on the home.

This particular statement of the formula assumes that the user is able to take itemized deductions for that dollar of home price. Without the two itemized

deductions, the terms where federal taxes interact with property taxes or mortgage interest disappear:

$$UC=LTVr_m+(1-LTV)(1-\tau)\ r_e+(1-\tau)b+\tau_p+\delta-\pi$$

As both of the terms pertaining to itemized deductions are negative, the user cost per dollar of housing falls with these deductions—or rises without them. As stated above, in equilibrium the total user cost is roughly equal to the value of living in the home. This means that—according to this model, a home's deed becomes more valuable the more tax deductions it is associated with, and less valuable with fewer tax deductions. According to this model, at least, tax deductions should increase people's willingness to pay higher prices for the homes.

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# Saving for Social Capital

SCP REPORT NO. 2-20 | MAY 2020

## INTRODUCTION

Relationships produce benefits for us every day—emotional fulfillment, practical information, rules to live by, and the like. In this sense, the "social capital" we possess is much like the financial capital that we own. Savings and investments, like relationships, also produce benefits, allowing us to mitigate economic risks, giving us shelter from the elements, and increasing our future capacity to afford necessities. Financial capital, in fact, underpins social capital. Savings allow us to form and expand families and to surround ourselves with neighbors and institutions that enrich our lives. Savings make homeownership possible, which invests us more deeply in the community. Savings sustain many institutions of civil society, from clubs to schools to churches.

Unfortunately, under current tax policy, saving and asset-building are disadvantaged relative to spending, with the exception of certain government-approved savings goals. What is more, the savings vehicles that promote those goals largely fail to benefit lower-income and working-class Americans, in part due to the many rules and restrictions on their use.[1]

Universal savings accounts (USAs) may provide a solution: USAs generally exempt either contributions or distributions from taxation, rebalancing tax policy so that saving is on equal footing with spending.[2] Unlike traditional tax-neutral savings vehicles, USAs allow saving for all goals, not just government-approved ones.

USAs may help Americans be more financially independent while also fostering greater voluntary mutual aid. As we noted in a previous Social Capital Project report, lower- and middle-income Americans tend to give to different kinds of charities than upper-income Americans (who benefit more from existing savings vehicles), and a greater share of their donations go toward poverty alleviation.[3] Asa result, the social capital benefits of USAs are likely to be significant. This report will outline important characteristics of USAs and propose reforms that make themost of their associated benefits.

## EXISTING SAVINGS ACCOUNTS AND THEIR LIMITATIONS

When people choose between immediately consuming their income or saving it, they will often require an incentive to save, both because the appeal of consumption is strong and because inflation will often make their income less valuable in the future. Earnings on saved income are the incentive to defer consumption. Savings are then invested by others in productive ways that make economies richer.

Current consumption is taxed only once at the federal level, but in general, future consumption (in the form of savings and investment) is taxed twice—first on the

dollars funding savings and again on the earnings from it. The double taxation of savings makes consumption relatively more appealing, which reduces investment and thereby economic growth in the future. A tax on social capital—a head tax, say, on each relationship—would produce less investment in social capital, with costs to individuals and society as a whole. So, too, does a tax on savings reduce the benefits of financial capital to individuals and the economy.

The exception to this tax policy bias in favor of current consumption involves a variety of savings accounts. However, each has a particular purpose, completewith eligibility standards, withdrawal penalties for non-designated purposes, age limits, time limits, and other restrictions. Table 1 provides a list of the most common types of savings accounts.

Table 1. Current Savings Accounts in the Tax Code

| | Expected Term Length | Contributions or Distributions Taxed | Income Eligibility Limit | Age Limit | Contributions of Earned Income Only[1] | Time Limit | Penalty for Ineligible Use or Early Withdrawal | 2020 Contribution Limits[2] |
|---|---|---|---|---|---|---|---|---|
| *Retirement* | | | | | | | | |
| Defined Benefit Plan (Pensions) | Long | Distributions | No | Yes; 62[3] | Yes | No | Yes | N/A |
| Defined Contribution Plan (401(k), 403(b)...) | Long | Distributions | No | Yes; 59½[3] | Yes | No | Yes | $19,500 |
| Traditional IRA | Long | Distributions | No[4] | Yes; 59½[3] | Yes | No | Yes | $6,000 |
| Roth IRA | Long | Contributions | Yes | Yes; 59½[3] | Yes | Yes[5] | Yes | $6,000 |
| *Education and Disability* | | | | | | | | |
| Qualified Tuition Plan (529s) | Short-Medium | Contributions | No | No | No | No | Yes | $15,000[6] |
| Coverdell ESAs | Short-Medium | Contributions | Yes | Yes[7] | No | No | Yes | $2,000 |
| ABLE Account[8] | Varies | Contributions | No | No[9] | No | No | Yes | $15,000[6] |
| *Health and Dependent Care* | | | | | | | | |
| Dependent Care Flexible Spending Account | Short; "use or lose" | Neither | No | No | Yes | Yes[10] | N/A[11] | $5,000 |
| Health Flexible Spending Account | Short; "use or lose" | Neither | No | No | Yes | Yes[10] | N/A[11] | $2,750 |
| Health Savings Account[12] | Varies | Neither[13] | No | No[13] | No | No | Yes | $3,550 self-only; $7,100 family |

1. IRS definition of "earned income" varies according to the type of account.

2. Some accounts allow additional "catch-up" contributions for those age 50 and older. Some plans, such as SIMPLE 401(k)s, have lower contribution limits.

3. Age limits for retirement plans specify the earliest access without IRS penalty in usual circumstances. There may be separation-from-service or other consideration. In addition, retirement funds cannot be kept in tax-deferred retirement accounts indefinitely;with the exception of Roth IRAs, there are required minimum distributions by age 70½ for those who turn 70 by July 1, 2019, or by age 72 for those who turn 70 after that date.

4. No income eligibility limit to contribute, but the tax deductibility depends on income.

5. Cannot withdraw earnings within five years of the first contribution without penalty.

6. Overall contribution limits may vary by state, but $15,000 is the federal limit, above which the gift tax applies.

7. Account must be established before beneficiary turns 18 and balance must be used before beneficiary turns 30.

8. ABLE accounts are intended to help with disability-related expenses, but as section 529A plans, they allow rollovers from 529 plans.

9. Qualifying disability must occur or have occurred before age 26.

10. Must use within eligible expense period or lose the funds.

11. Funds are plan administered and must be approved for payments and reimbursements.

12. Excludes Archer and Medicare Advantage Medical Savings Accounts.

13. Qualified distributions are tax free. Unless age 65 or older (or disabled), non-qualified HSA distributions are subject to a penalty.

The requirements for saving within these accounts are elaborate and often excessive. For education-related savings accounts, like 529s, earnings must be used by or on behalf of the beneficiary for ***qualified*** education expenses associated with an ***eligible*** educational institution.[4] Contributions to health savings accounts (HSAs) are allowable only if the account-holder is enrolled ina high-deductible health plan, which may not be universally available or work for every individual or family situation.[5] Not all employers offer retirement plans, and if they do, they may not extend the benefit to all positions.[6] Taxpayers must have specific types of taxable income to contribute to an Individual Retirement Account (IRA).[7]

Additionally, qualifying distributions and exceptions to penalties are highlyspecific to the particular savings account; for example, 401(k)s and their equivalents can have different rules from one employer to the next.

Claiming an exception can be risky, and individuals can incur a penalty if they do not meet the established threshold for claiming an exception. For example, if a filer takes an early distribution in order to cover medical costs, but incorrectly estimates adjusted gross income, or the distribution is too large relative to the medical cost, she will still have to pay a partial or full penalty on the excess. The penalty is a tax on the distribution ***in addition*** to the income tax on distributions,if applicable.

It is not clear why the government should make saving so complicated, or favor specific savings goals over others. Saving for a rainy day, a new home, or a new baby are no less meritorious than the existing reasons currently favored. As the American Enterprise Institute's Alan Viard notes,

> We have an array of complicated rules to measure and tax the income from saving and another array of complicated rules to remove the tax from dozens of types of savings that Congress has singled out for favorabletreatment. Meanwhile, the large portion of national saving done outside tax-neutral accounts faces the income tax's saving penalty, impeding economic growth.[8]

The many restrictions and excessive complexity of current savings accounts create barriers to saving and reduce their use, especially among families whohave fewer resources.

Furthermore, the existing system of separate, government-favored goals including retirement, health, dependent care, and education effectively penalizes account holders for saving for the wrong goal. If an individual diligentlysaved in an HSA, for example, only to realize that those savings would be better vested in a 529 for her child's education, that savings is not transferable. Plans change; unfortunately, the allowable uses of assets in savings accounts do not.

## UNIVERSAL SAVINGS ACCOUNTS AND THEIR BENEFITS

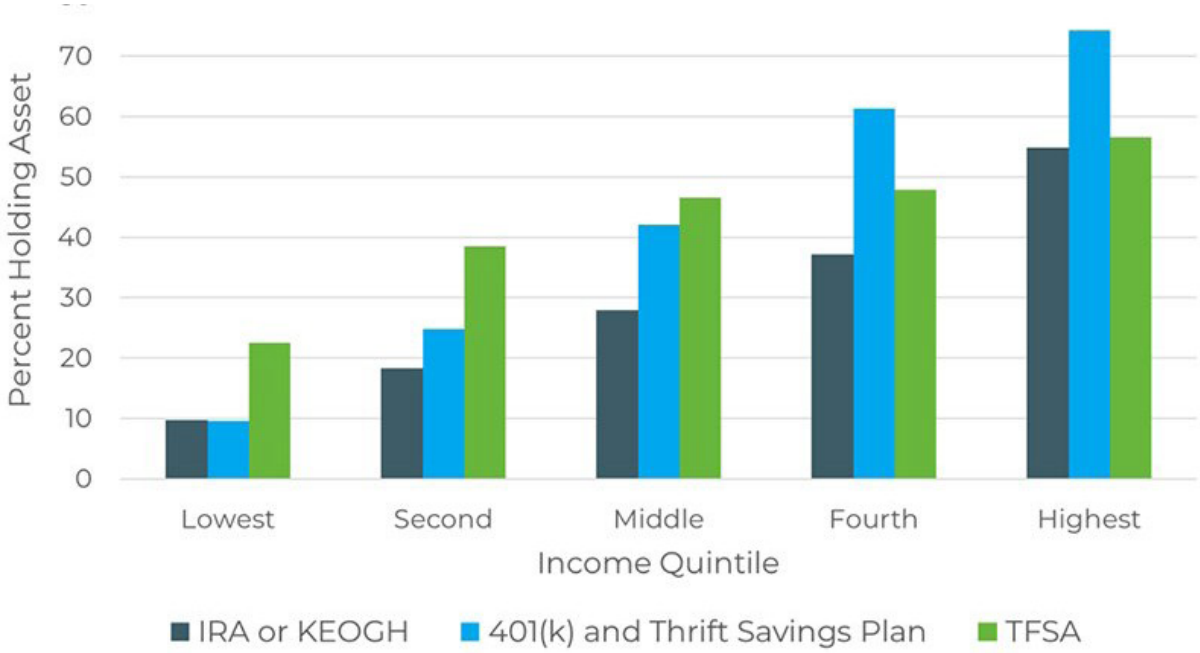
Universal savings accounts (USAs) could allow earnings on after-tax contributions to accumulate tax-free, as they do in Roth IRAs.[9] This feature would restore tax neutrality by taxing savings only once. Unlike other savings accounts in the tax code, USAs would promote saving for any purpose over any time horizon without penalties, restrictions, or paperwork to justify saving to the federal government.

In addition to offering impartiality and flexibility, universal savings accountswould increase the accessibility of savings opportunities.

USAs would be accessible by design. Unlike some savings accounts, such as health flexible spending accounts or pensions, USAs would be portable—not tied to a single employer. Additionally, USAs would provide an alternative savings vehicle for those who do not have access to employment-based health and retirement savings accounts. Unlike current saving accounts, there would be no barriers to opening a USA. Nor would there be restrictions on the use of savings from USAs, making them especially accessible to low- and middle-income Americans vulnerable to negative income shocks.

In the United Kingdom (UK) and Canada, taxpayers across the income distribution broadly participate in universal savings accounts. Individual Savings Accounts (ISAs) were created in the UK specifically to induce greater savings among low- and moderate-income groups[10] Over 2016 and 2017, 71 percent of ISA holders had less than $38,000 in annual income (in US dollars).[11] Similarly, 56 percent of the participants in Canada's Tax-Free Savings Accounts (TFSAs) had less than $37,000 in annual income in 2017.[12] Over half of Canadian taxpayers in the top fifth of post-tax income and over 20 percent of those in the bottom fifth hold a TFSA (Figure 1).[13]

Figure 1. Percent of Canadians and Americans Participating in Selected Savings Accounts, 2016, byIncome Quintile




Source: Statistics Canada. Table 11-10-0057-01 Survey of Financial Security (SFS), https://www150.statcan.gc.ca/t1/tbl1/en/ tv.action?pid=1110005701; U.S. Census Bureau, Survey of Income and Program Participation, 2014 Panel, Wave 4, https:// www.census.gov/data/tables/2016/demo/wealth/wealth-asset-ownership.html. Canadian quintiles are based on the post-taxincome of tax units, while US quintiles are based on the pre-tax quintiles of households.

In contrast, while Americans in the top income quintile are about as likely to have an IRA as Canadians in the top quintile are to have a TFSA (and more likely to have a 401(k) or Thrift Savings Plan), Americans in the bottom two quintiles are only half as likely to be IRA holders as their Canadian counterparts are to have TFSAs (Figure 1). Nevertheless, research reinforces what the Canadian data demonstrate—that the poor do have the capacity to save.[27]

## USAS AND SOCIAL CAPITAL

In addition to the key features listed above, USAs also have the potential to expand access to valuable social capital. Savings self-evidently make it more affordable to start and to expand a family. By promoting economic stability, savings is likely to benefit family stability. And more savings is likely to translate into greater charitable giving, which would be expected to strengthen civil society.[14]

Further, there are strong reasons to think savings increases the value of social capital in various other ways. While the research examining this question is not well-developed, there is a modest literature consistent with the idea that financial capital produces more valuable social capital.[15]

Most of this evidence focuses on homeownership, which is a key rationale for saving and itself involves saving (via building up home equity). Compared with renting, homeownership is associated with greater residential stability.[16] Would-be movers who own their home must either sell it or rent it out, which makes moving more difficult than for renters. Homeownership is also associated with greater access to neighborhood amenities, including neighborhood safety.[17]

If families who own their homes tend to live in more desirable neighborhoods and to remain in them longer, the value of the social capital available to them is likely to be greater than is the case for renters. One reason that valuable neighborhood social capital may be promoted by homeownership is that owners are more likely than renters to maintain and invest in their property, which can result in more attractive and aesthetically pleasing neighborhoods.[18]

Being invested in one's neighborhood—even out of purely selfish concerns about home values—also may lead to greater civic engagement. Homeownership is associated with greater participation in local organizations and greater voting at the local level.[19] One study found that more savings in 1968 was associated with slightly higher "connectedness" in 1972, as measured by an index of survey items to do with relationships to relatives, neighbors, and organizations.[20]

Savings may also increase the value of social capital to which children have access. Homeownership can provide access to better schools, and the residential stability that homeownership promotes minimizes school changes, which have been found to worsen academic outcomes.[21] Not only homeownership, but saving generally appears to increase access to higher-quality neighborhoods: families with higher non-housing wealth are more likely to live in neighborhoods with high rates of homeownership.[22] If homeownership increases civic engagement, that can make parents more networked than they otherwise might be, which can benefit their children.[23]

Assets may alter parenting by reducing stress and changing aspirations for children.[24] Homeownership appears to accelerate marriage and to reduce divorce.[25] By serving as a sort of collateral in the event of a failed marriage, joint homeownership between spouses can encourage not only marriage and marital stability, but greater child investment that may come from one spouse investing less in their own career.[26]

## CREATING UNIVERSAL SAVINGS ACCOUNTS

The accumulation of financial capital, then, has many benefits, one of which is the accumulation of valuable social capital. Universal savings accounts would promote such capital accumulation.[28] The remainder of this report outlines how USAs could be developed from current savings accounts in the tax code.[29]

USAs would be funded from after-tax contributions, but the earnings on those contributions would never be taxed. This arrangement would ensure there is no guesswork regarding taxes deferred upfront or taxes owed on withdrawals. Subject to the annual limits described below, contributions to USAs would be allowable for

everyone without regard to their income, and they could be made from unearned income.[30] Owners of USAs could withdraw earnings tax-free and penalty-free at any time for any purpose, and they would never be required to make withdrawals.[31] All adults at least 18 years old would be eligible to contribute to an account.

Financial institutions sponsoring USAs could be expected to develop a range of options for those wanting to participate. They might include plans oriented toward particular savings goals, such as college or retirement, or different age groups. There would be plans for people with different levels of risk tolerance and other portfolio preferences. Sponsors might feature plans that gradually invest more conservatively over a pre-specified period for those who intend to withdraw savingsat a known time.

With the creation of USAs, policymakers would sunset Roth IRAs, ABLE accounts, Coverdell ESAs, and 529 accounts, all of which feature post-tax contributions and tax-free accumulation of earnings.[32] All amounts in these accounts could be rolled over into a USA at any time. In addition, amounts could be rolled over from defined contribution plans such as 401(k)s and from traditional IRAs, subject to income taxation first.[33]

Apart from rollovers, USAs would be subject to an annual contribution limit initially equal to $35,000 less the total contributions to defined contribution plans and traditional IRAs.[34] In the event someone had access to a 401(k) and maxed out her contributions to it ($19,500), that would leave $15,500 available to contribute to a USA. That is slightly higher than the current annual contribution limit to a 529 or ABLE account. Someone contributing the maximum amount to a traditional IRA ($6,000) but with no 401(k) contributions would be able to contribute up to $29,000 to a USA.[35] Like the availability of rollovers from defined contribution plans and traditional IRAs, this policy might encourage a longer-term shift from plans where the distributions are taxed (and penalized for non-approved uses) to USAs, which could ultimately simplify the savings-related provisions of the tax code further.

Any adult could contribute to anyone else's USA. These contributions would count toward the beneficiary's annual contribution limit, and contributions to others' accounts would be subject to the gift tax if applicable. Parents would not be ableto transfer unlimited amounts to their grown-child's USA for college expenses, but they could still pay for those expenses out of their own USA. (Parental payments oftuition are not subject to the gift tax.)[36]

Beneficiaries of safety net programs generally are subject to restrictive limits on the assets they may hold (often around $2,000), in order to prevent fraud and protect benefits for those who need them. But these asset tests may discourage upward mobility and efforts to escape cyclical poverty and dependence on welfare. Studies suggest these limits discourage beneficiaries from saving, and limited savings can make it harder for poor families to deal with emergencies, such as an expensive car repair, or child care in the face of unpredictable work schedules.[37]

To ensure lower-income Americans have an opportunity to build savings through USAs without penalty, safety net policies could accommodate a certain level of savings in a USA before making an individual ineligible. Other policies could be implemented simultaneously to reduce abuse, such as counting imputed annual earnings from USA savings as income in assessing program eligibility.[38]

## CONCLUSION

Social capital is often created and deepened using a currency that is not denominated in dollars—relying instead on the essential resources of trust, empathy, solidarity, and fellow-feeling. However, while not strictly necessary for building social capital, money can greatly facilitate it. Whether it is used to start a family, to surround children with supportive neighbors, or to shore up institutionsof civil society, savings promotes social capital.

Social capital is often created and deepened using a currency that is not denominated in dollars—relying instead on the essential resources of trust, empathy, solidarity, and fellow-feeling. However, while not strictly necessary for building social capital, money can greatly facilitate it. Whether it is used to start a family, to surround children with supportive neighbors, or to shore up institutionsof civil society, savings promote social capital.

The tax code should not be a vehicle for policymakers to incentivize their preferred behaviors at the expense of others. It should not be used to promote social goals. Many people would agree that social capital is important, but that does not justify subsidizing it through tax breaks.

However, the tax code's imbalanced treatment of spending and saving actually discourages saving. By putting a thumb on the scale in favor of spending, current tax policy thereby poses a barrier to social capital investment. Universal savings accounts would help rectify this bias. Relative to the jumble of existing savings accounts available in the tax code, USAs would also make savings more accessible, impartial, flexible, and portable.[39]

Most importantly, USAs would assist families as they pursue their own savings goals throughout life, and they would finance the creation and deepening of valuable relationships and institutions throughout American society. They would promote charitable giving to help Americans in need, and they would help lower-income Americans help themselves.

More consumption means less investment—in social capital no less than in financial capital. Many Americans may prefer consumption over investment, and that is their own business. The problem is that tax policy penalizes investment. And social capital deepening—with all its benefits for individuals and society—suffers as a consequence.

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33. While some might advocate sun-setting defined contribution plans and traditional IRAs too, many Americans might prefer to retain these accounts. They might believe they will be in lower tax brackets when older than when they are younger, or they might fear that the federal government could institute taxes on USA earnings in the future.

34. The limit should be increased to account for inflation each year and for the annual increase in 401(k) contribution limits.

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# Expanding Child Care Choices:

## Reforming the Child and Dependent Care Tax Credit to Improve Family Affordability

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Strong families are the backbone of a healthy society, which is why the Social Capital Project (SCP) has a stated goal of "making it more affordable to raise a family."[1] Many parents or would-be parents cite child care as a key component of family affordability: a 2018 poll found the most commonly given rationale among respondents who said they had or expected to have fewer children than they considered ideal was their belief that "child care is too expensive."[2]

The issue of child care intersects with other SCP goals of connecting people to work and increasing the effectiveness of investments in youth. For married parents, child care may be seen as necessary, optional, or irrelevant, depending on the parents' occupations and other objectives. For single parents, child care is virtually a necessity if they are to participate in the labor force. For children, high-quality child care has the potential to boost outcomes, but facilities that are not top-tier may not elicit the same results – and could even harm development.[3]

Preferences for work and family life vary widely across American families. Some parents rely on formal care, which for the purposes of this paper is a regular child care arrangement, most often in a center, which can be operated by a for-profit or not-for-profit entity subject to certain state regulations. Others rely on informal care, often provided by friends, family members, or neighbors, which may or may not be a commercial transaction, but is not run as a business. Still others rely on a stay-at-home parent. However families care for their children, government policy should be neutral toward the choices families make about balancing the competing demands of work and home life.

But our current tax code strays from that neutrality, and the Child and Dependent Care Tax Credit (CDCTC) is biased towards the needs of dual-earner families that use formal care. The credit could be reformed to ensure that families with a stay-at-home parent, families that do not utilize formal child care arrangements like center-based day care, and families that prefer to allocate income toward other aspects of care (including diapers, formula, educational resources, etc.) are not disadvantaged.

Policymakers could repurpose the CDCTC as a young child supplement for the Child Tax Credit (CTC) and offer up to $1,500 to parents of children ages 0-5 to spend on the expenses associated with the care and raising of young children. This would provide families with more of the flexibility they need, keep more of parents' hard-earned money in their pockets, and improve affordability for many families that are ignored by existing policy.

This paper will briefly examine the evidence on child care affordability and the evolving need for child care, and conclude with a discussion of how a young child supplement could more flexibly and fairly address the affordability needs of parents with young children.

## UNPACKING THE RISE IN OBSERVED CHILD CARE COSTS

Improving the tax code's treatment of child care expenses first requires understanding some of the cost pressures on parents. It is common to hear concerns about an "affordability crisis" in child care, with some observers even concluding that "the whole system is broken."[4] One influential report estimated that "in 33 states and the District of Columbia, infant care costs exceed the average cost of in-state college tuition at public 4-year institutions."[5] But the story is more complicated than the reported figures suggest.

To start, roughly half of all working mothers with young children do not pay for child care, whether due to a flexible work schedule, care provided by a family member or friend, school-based programming, or other arrangements.[6] Beyond that, the data on prices for child care are far from perfect. A national survey of state-based child care resource and referral agencies relies on self-reporting of prices by the hour, week, month, or year, converted to the cost of full-time care.[7] Thus the sticker price, while eye-popping, does not always reflect the actual costs incurred by families.

The fraction of households spending a high fraction of their household income on child care has also been cited as heralding "relentless" child care costs.[8] But that figure also requires some explanation. In late 2016, the Administration for Children and Families (ACF) defined "affordable" co-payments in child care as costing families no more than seven percent of a family's income, down from the previous benchmark of ten percent.[9]

ACF based the affordability threshold on the monthly average share of income spent on care by families with children under age 15, which has hovered around seven percent since the mid-1980s. But young children will always be more expensive to care for than older ones, with the average share of income spent on care for children below age five standing at 10.5 percent.[10] Taken at face value, this would suggest the average family with young children is already spending "unaffordable" amounts of income on child care based on the fact that the constructed seven percent threshold includes older, and cheaper to care for, children. And, like many affordability thresholds, the ACF benchmark is somewhat arbitrary. For instance, it does not consider that for higher income families with more discretionary income, spending more than seven percent of household income on child care may be a reasonable and affordable choice.

When child care cost averages are reported, they can be skewed by outliers in this high-income group and thus paint a misleading picture. For example, the Census Bureau reports that families' average weekly child care expenditures rose by 71 percent between 1985 and 2011 (from roughly $205 to $350 per week, in constant 2019 dollars).[11] A 2015 paper by Chris Herbst re-evaluated the Survey of Income and

Program Participation (SIPP) with an eye towards understanding how child care cost pressures impact different families in different ways.

Using the median, or statistical midpoint, rather than the simple average, Herbst found that the weekly child care expenditure rose by only 16 percent from 1990 to 2011, with the bulk of the increase coming from parents who were married, college-educated, and in upper income brackets.[12]

Still, it is possible that parents are paying more for more hours of care, and this is behind rising expenditures. To test this, Herbst estimates the median expenditure per hour and finds an increase of 14 percent, similarly concentrated in the same subgroups. This evidence suggests wealthy families that spend a lot of money on high-quality care may skew the reported average cost of child care.

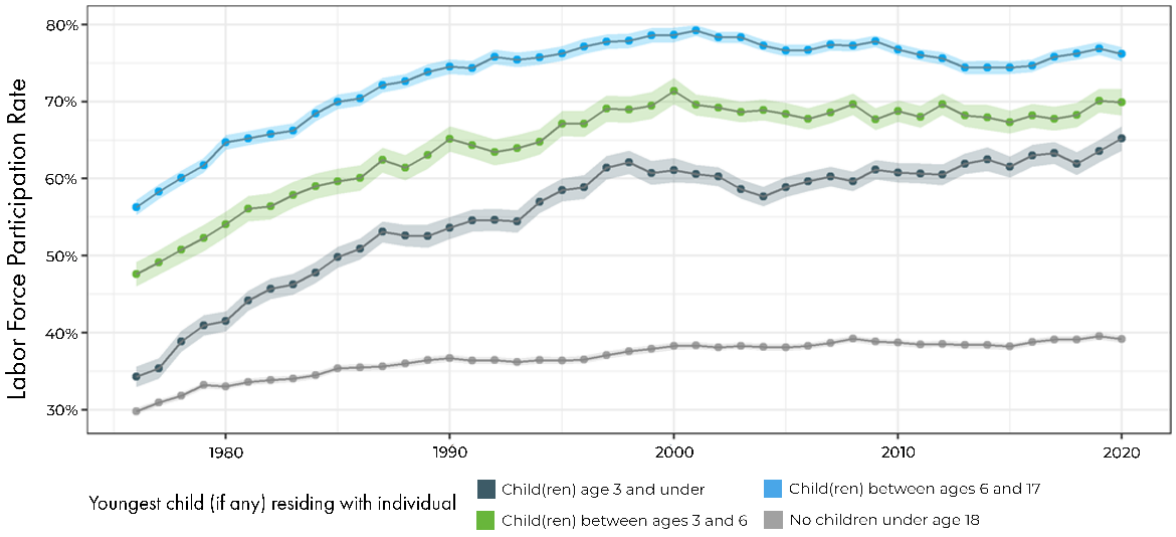
This is not to downplay the very real cost pressures facing families. But understanding the technical construction of the headline figures reminds us some figures can obscure just as much as they illuminate. Child care is a labor-intensive good, and it occupies a greater share of household income in urban areas, particularly among the college-educated and the very poor. But these families should arguably not be favored or advantaged by public policy simply because of their location or child care choices. And large-scale approaches to solving the child care "affordability crisis," such as universal child care proposals, operate from a set of assumptions about the demand for child care, and its cost, that ignore the varying attitudes and needs of parents.

## DIVERSE CHILD CARE PREFERENCES ARE ILL-SERVED BY CDCTC

While the market for child care operates differently in different parts of the country, the need for child care has become increasingly prevalent as female labor force participation increased in the post-World War II era. As women's educational attainment increased and career options expanded, American families became more likely to have both parents in the workplace. As late as the early 1970s, about one-third of families operated on a male-breadwinner model, but by 1994 the share of families with that structure had fallen to 16.2 percent.[13]

The expansion of female labor force participation included mothers with children of all ages, though those with children under six worked less than those with school-aged children.[14] In 1975, 39 percent of women with children under 6 were in the labor force; by 1998, their participation rate had reached 65 percent, where it has remained mostly unchanged since.[15] Mothers with children of all ages have seen their participation rate largely stabilize over the past two decades, though the recent impact of the coronavirus has negatively affected women's employment.[16]

Figure 1: Labor Force Participation Among Women, 1976-2020
*By presence and age of youngest child*

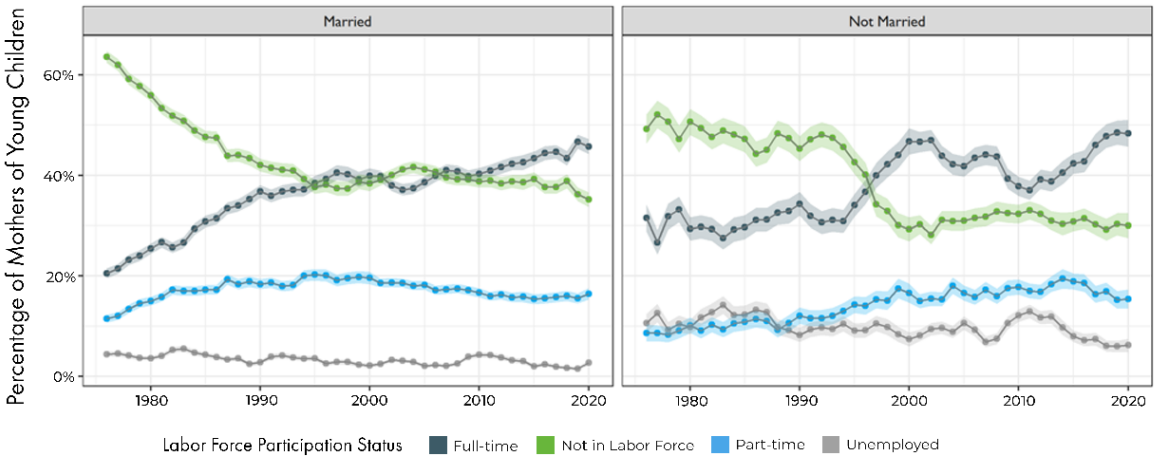



Shaded areas represent 95% confidence interval.
Data: Annual Social and Economic Supplement of the Current Population Survey, via IPUMS-CPS, University of Minnesota.

In addition to varying over time, child care needs can vary by family structure. Single mothers, who make up about a quarter of households with children, need formal or informal child care in order to earn income.[17] Poor families, which are disproportionately headed by single mothers, spend roughly four times the share of their income on child care compared to higher-income families.[18] Meanwhile, married-couple families sometimes have the option of a spouse providing care at home – in 2017, almost 30 percent of married mothers of children under 18 with a working husband did not work.[19]

Some parents choose to spend those early years in part-time or flexible working arrangements, some rely exclusively on center- or home-based child care, and some stay out of the labor force altogether.[20] In polls, a plurality of mothers express a desire for flexibility rather than full-time careers relying on full-time child care: A 2015 Gallup poll found that 56 percent of women with a child at home said they would prefer to stay home and care for their family, including 54 percent of mothers currently working.[21] A 2013 Pew study reported that "only 23 percent of married mothers today say their ideal situation would be to work full time."[22] And while the percentage of married mothers with children at home who work full-time has risen since the 1970s, a majority of that demographic still either work part-time or not at all.

Figure 2: Labor Force Status Among Mothers of Young Children, by Marital Status
*Among women with children under 5, 1976-2020*




Shaded areas represent 95% confidence interval.
Data: Annual Social and Economic Supplement of the Current Population Survey, via IPUMS-CPS, University of Minnesota.

Taken together, this evidence emphasizes the need for considering a wide degree of heterogeneity in families' needs and preferences in any child care policy, while also acknowledging that these needs may continue to change, and policies should be flexible as a result.

## REFORMING THE CDCTC

Although the needs of families vary, the current treatment of child care in the tax code tends to assume a one-size-fits-all approach and leaves much to be desired. The CDCTC, the primary child care-related benefit in the tax code, "provides a credit worth between 20 percent and 35 percent of child care costs up to $3,000 for a child under 13, or up to $6,000 per household. Higher credit [reimbursement] rates apply to families with lower adjusted gross income."[23] To claim the credit, all parents in the household must be working (head of household for a single parent or both filers for married couples).[24]

One issue with the CDCTC is that a significant portion of the benefit may be passed through to child care providers rather than parents. Economic theory suggests, and empirical work with other tax credits supports, that much of the generosity of the credit could be passed from the consumer to firms through higher prices, depending on the relative elasticities of supply and demand in the child care market. Theoretically, the subsidy will benefit the more inelastic market actor, or the market actor less able to change their behavior.

While parents may seem to be more inelastic, and thus would stand to benefit, they also have the option of pursuing informal care, changing their work schedules, or not working at all. Firms, on the other hand, are often highly regulated, facing licensing requirements, staff ratios, and other regulatory constraints that make their supply less elastic, as evidenced by the waiting lists that characterize many child care facilities, particularly in urban areas.[25] A recent paper finds that "child care tax credits are passed through to the child care provider in the form of higher prices and wages," at about sixty cents on the dollar, with larger pass-throughs observed in urban areas and among higher-income populations.[26]

Another issue with the CDCTC is that the current structure results in a benefit that is highly skewed towards higher earners. Currently only 4.2 percent of all filers (or 12.7 percent of families with children) receive a benefit from the credit, according to the Tax Policy Center.[27] While households making $100,000 or more comprised 18 percent of tax filers in 2017, they made up 42 percent of returns claiming the CDCTC, and received 43 percent of the total dollar amount.[28] In addition to requiring that all parents be working, the CDCTC requires the taxpayer provide a social security or employer identification number for the caretaker, which increases the administrative burden on parents who wish to claim the credit for spending on less formal care arrangements.

To address many of these issues, Congress could consider eliminating the CDCTC and repurposing the funds for an up-to $1,500 young child supplement as part of the Child Tax Credit to parents of children age 0-5. The credit could be made refundable against income and payroll taxes, along similar lines as was proposed by JEC Chairman Sen. Mike Lee during negotiations over the Tax Cuts and Jobs Act in 2017.[29] The current maximum amount per child, $1,050, was set by statute in 2001 and has not been adjusted for inflation since then. A credit of $1,500 would approximately update the figure for inflation and ensure that no parents, regardless of child care status, are left worse off.

In proposing a similar age-targeted credit, the Urban Institute notes the design would "target additional public resources where they seem to make the most difference: early childhood… [and] provide families with the flexibility to nurture their children as they think best."[30] Reforming the credit in this way also ameliorates some of the potential problem of pass-through identified above. If parents are able to spend their CTC young child supplement on a wide variety of expenses related to the care of young children, economic theory suggests, child care facilities will not capture as much of the value of the credit through higher prices.

A simple estimate suggests that a supplemental CTC for children age 0-5 would result in an additional net tax expenditure of $24.1 billion. This accounts for the existing $4.7 billion in tax expenditures on child care that currently exist.[31] This static analysis assumes that families do not change their work behavior to respond to how the expanded credit may phase in or out.[32] A more sophisticated model from the Urban Institute, using a more generous phase-in rate, estimates a FY20 tax expenditure of $27.3 billion.[33] The estimated cost of a supplemental

CTC could be offset by reducing other budget items and capping other tax expenditures. Congress will have to weigh the benefits of the reform, including its potential to stabilize working- and middle-class families and equalize treatment across work-life situations, against its budgetary costs.

Far more working- and middle-class families would see a tangible benefit under this proposal than under the current CDCTC. Using Herbst's estimate for the median weekly expenditure of $118 (in 2019 dollars), a back-of-the-envelope calculation estimates that 50 weeks of child care costs the median family with a young child and an employed mother $5,950. Holding all else equal, families who receive the full $1,500 and choose to spend it all on child care would see their out-of-pocket spending drop by one-fourth.

In addition to mitigating some of the other CDCTC-specific issues, reforming the CDCTC this way would remove the implicit penalty against single-breadwinner households or those who seek flexible and informal child care arrangements. This would be a substantial improvement over proposals that would simply increase the amount of the CDCTC, which requires all parents to be working and requires the child care provider to list a taxpayer or employer identification number, limiting parents' flexibility.

One drawback from transforming the CDCTC into a young child supplement would be that dependents of other ages would no longer benefit. Currently, the CDCTC can be used to reimburse spending on dependent children under 13 years of age or a spouse or dependent incapable of caring for himself or herself. However, less than four percent of CDCTC benefits are used on care for those over 13,[34] and only 22.8 percent of families with children age 6 to 14 pay for any type of child care.[35] Employer FSAs could still be permitted to cover those expenses, and universal savings accounts – proposed elsewhere by the Social Capital Project – could also be helpful.[36]

## CONCLUSION

The issue of child care touches a bundle of related issues that reflect how we value family life and work. All parents face different trade-offs in making decisions that intersect with this Project's goals of making it more affordable to raise a family, connecting people to work, and investing in youth. As such, it seems important for Congress to keep in mind the principle of equal treatment – both across the income spectrum and between families who make different work-life decisions – in child care policy. Making it easier for families to raise children in the manner they deem best, especially in the important years of early childhood, strongly recommends a federal approach that disentangles tax benefit provision from a given family's choice of how to prioritize home and work.

There is no one-size-fits-all answer to questions about increasing labor force attachment, investing in children, and making it more affordable to raise a family. As such, there should be no one-size-fits-all preference in direct spending or the tax code. Government cannot guarantee peace of mind or the satisfaction of every parent's preferences about work-life balance. Nor can it invest in large-scale programs, like universal child care, without putting an unavoidable finger on the scale towards certain scripts about family and work.

Instead, public policy should empower families to achieve their desired preferences about work and family without favoring any one choice over another. In this respect, reforming the CDCTC could make existing policy more even-handed, make child care more affordable for more families, and better support parents of young children in pursuing the work-life situation they desire.

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## ENDNOTES

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9. U.S. Department of Health and Human Services, Administration for Children and Families, Office of Child Care, "45 CFR Part 98: Child Care and Development Fund (CCDF) Program," Final Rule, Federal Register 81, no. 190 (Sept. 30, 2016): 67438-67595, https://www.govinfo.gov/content/pkg/FR-2016-09-30/pdf/2016-22986.pdf
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11. Laughlin 2013, Fig. 5 (conversion into 2019 dollars by author, using https://data.bls.gov/cgi-bin/cpicalc.pl)
12. Chris M. Herbst, "The Rising Cost of Child Care in the United States: A Reassessment of the Evidence," IZA Discussion Paper No. 9072 (May 2015), http://ftp.iza.org/dp9072.pdf
13. By 2017, the share of families with a male-breadwinner had ticked back up to 18.6 percent. JEC analysis of Current Population Survey-Annual Social and Economic Supplement, via IPUMS.
14. Francine D. Blau and Lawrence M. Kahn, "Female Labor Supply: Why Is the United States Falling Behind?" American Economic Review: Papers and Proceedings (2013), 103(3): 251-56, https://pubs.aeaweb.org/doi/pdfplus/10.1257/aer.103.3.251
15. U.S. Census Bureau, "Table F-15. Work Experience of Husband and Wife--Married-Couple Families with Husband Working, by Presence of Children Under 18 Years Old and Median and Mean Income," Historical Income Tables: Families (2017), https://www2.census.gov/programs-surveys/cps/tables/time-series/historical-income-families/f15.xls. N.B.: There are also some fathers who stay at home with children, but they make up less than ten percent of stay-at-home parents. Source: U.S. Census Bureau, "Figure SHP-1B: Number of stay-at-home parents among opposite-sex married couple families with children under 15," https://www.census.gov/content/dam/Census/library/visualizations/time-series/demo/families-and-households/shp-1b.pdf
16. For more on the coronavirus pandemic's disproportionate impact on female workers, see Eleni X. Karageorge, "COVID-19 recession is tougher on women," U.S. Bureau of Labor Statistics Monthly Labor Review (Sept. 2020), https://www.bls.gov/opub/mlr/2020/beyond-bls/covid-19-recession-is-tougher-on-women.htm
17. Knop Mahonty 2018.
18. Laughlin 2013, Tab. 6.
19. U.S. Census Bureau, Historical Income Tables, Table F-15.
20. Laughlin 2013.

21. Lydia Saad, "Children a Key Factor in Women's Desire to Work Outside the Home," Gallup (Oct. 7, 2015), https://news.gallup.com/poll/186050/children-key-factor-women-desire-work-outside-home.aspx

22. Pew Research Center, "Modern Parenthood," (March 14, 2013), https://www.pewsocialtrends.org/2013/03/14/modern-parenthood-roles-of-moms-and-dads-converge-as-they-balance-work-and-family/

23. Elaine Maag, "Understanding Child Care Subsidies in the Tax System," Tax Policy Center (May 25, 2017), https://www.taxpolicycenter.org/publications/understanding-child-care-subsidies-tax-system/full

24. Although parents must work, they do not need to itemize their deductions.

25. Luke P. Rodgers, "Give credit where? The incidence of child care tax credits," Journal of Urban Economics (2018) 108: 51-71. https://www.sciencedirect.com/science/article/abs/pii/S0094119018300792

26. Cf. Rodgers 2018, although one critic has noted Rodgers controls for individual incomes in his specification, which may be a function of the prices individuals face, thus biasing the estimate. See Gabrielle Pepin, "The Effects of Child Care Subsidies on Paid Child Care Participation and Labor Market Outcomes: Evidence from the Child and Dependent Care Credit," personal working paper (Sept. 30, 2019), http://econ.msu.edu/seminars/docs/Pepin_Deng.pdf

27. Maag 2017.

28. Internal Revenue Service, "Table 3.3. All Returns: Tax Liability, Tax Credits, and Tax Payments," SOI Tax Stats - Individual Income Tax Returns Publication 1304 (Complete Report), https://www.irs.gov/pub/irs-soi/18in33ar.xls

29. Office of Sen. Mike Lee, "Sens. Lee and Rubio to Introduce Child Tax Credit Refundability Amendment," Press Release (Nov. 29, 2017), https://www.lee.senate.gov/public/index.cfm/2017/11/sens-lee-and-rubio-to-introduce-child-tax-credit-refundability-amendment. Another option policymakers could pursue is setting the phase-in rate higher (21 versus 15 percent) for the first $7,000 of income to account for federal unemployment (FUTA) taxes.

30. Elaine Maag and Julia B. Isaacs, "Analysis of a Young Child Tax Credit," Urban Institute (Sept. 2017), https://www.taxpolicycenter.org/sites/default/files/publication/144276/analysis_of_a_young_child_tax_credit.pdf

31. The current annual tax expenditures for existing child care subsidies, including the CDCTC and tax benefits for employer-provided Flexible Savings Accounts (FSAs) for child and dependent care, which total $4.7 billion. See Joint Committee on Taxation, Estimates of Federal Tax Expenditures for Fiscal Years 2020-2024 (JCX-23-20), Nov. 5, 2020. https://www.jct.gov/publications/2020/jcx-23-20/

32. The cost estimate is based on the current phase-in and phase-out limits of the current CTC; Goldin and Michelmore (2020) find that 34 percent of children who receive the full CTC, 38 and 30 percent of children who are in the phase-in and phase-out regions, respectively, and 34 and 27 percent of children whose families make too little or too much to receive any CTC, respectively, are aged 0-5. Scaling their average CTC payment for each segment of the population by the proposed young child supplement produces a naïve estimate of about $28.8 billion. Jacob Goldin & Katherine Michelmore, "Who Benefits From the Child Tax Credit?" NBER Working Paper No. 27940 (Oct. 2020), https://www.nber.org/papers/w27940. Making the young child supplement fully universal for children age 0-5, regardless of earnings or refundability, would cost $36.2 billion ($1,500 for each of the 24.2 million

children under 6 in the U.S.)

33. Option 3 in Maag and Isaacs 2017.
34. Margot L. Crandall-Hollick, "Child and Dependent Care Tax Benefits: How They Work and Who Receives Them," Congressional Research Service (March 1, 2018), R44993, https://fas.org/sgp/crs/misc/R44993.pdf
35. Laughlin 2013, Tab. 6.
36. U.S. Congress, Joint Economic Committee, Social Capital Project, "Saving for Social Capital." Report prepared by Chairman's staff, 117th Cong., 2nd Sess. (May 2020). Social Capital Project Report No. 2-20. https://www.jec.senate.gov/public/index.cfm/republicans/analysis?ID=2D14ADC0-B531-441F-A86C-96F190F97F99

# Increasing Family Stability

# Demise of the Happy Two Parent Home

SCP REPORT NO. 2-17 | JULY 2020

*Who are you? What have you become?* Throughout our lives, we are enmeshed in a network of social relationships that influence us, for better or for worse. Most of our relationships have some value to us, else we would not be in them. They constitute social capital—a form of wealth every bit as valuable as financial or human capital.

Family relationships are the first a person experiences in life. Children are nurtured, taught, and socialized in the family, and from there learn to relate to others and participate in the broader society. A stable family offers the emotional security a child needs for healthy development. As Princeton University sociologist Sara McLanahan has noted:

If we were asked to design a system for making sure that children's basicneeds were met, we would probably come up with something quite similar to the two-parent ideal. Such a design, in theory, would not only ensure that children had access to the time and money of two adults,
it also would provide a system of checks and balances that promoted quality parenting. The fact that both parents have a biological connectionto the child would increase the likelihood that the parents would identify with the child and be willing to sacrifice for that child, and it would reduce the likelihood that either parent would abuse the child.[1]

As sources of valuable social capital, few relationships are as important as the family ties between parents and children. However, as with other features of our associational life, family ties have been weakening for several decades.[2] Today, around 45 percent of American children spend some time without a biological parent by late adolescence.[3] That is up from around one-third of children born in the 1960s and one-fifth to one-quarter born in the 1950s.[4] Even more strikingly, among the most disadvantaged socioeconomic groups, even fewer children are raised in continuously intact families. Single parenthood is experienced by two-thirds of the children of mothers with less than a high school education and by eighty percent of black children. This inequality in family stability contributes to but also compounds economic inequality.[5]

This report examines the state of family stability in the United States and describes policy approaches to ensure that more children are raised by two happily married parents. This policy goal is one of five identified by the SocialCapital Project in our essay *The Wealth of Relations*, as central for expandingopportunity by shoring up families, communities, and civil society.[6] Future reports will propose specific policies toward this end.

## INTACT FAMILIES AND OPPORTUNITY

Researchers have well established that children raised by married parents do better on a wide array of outcomes. They have stronger relationships withtheir parents, particularly with their fathers.[7] They are also much less likely to experience physical, emotional or sexual abuse.[8] They have better health, exhibit less aggression, are less likely to engage in delinquent behavior, have greater educational achievement, and earn more as adults.[9] They are also far less likely to live in poverty.[10]

Rigorously establishing the ***causal*** importance of family structure is far from straightforward, however. Few studies are up to the task. And among the most rigorous studies, about half find the estimated effects of experiencing single parenthood are not large enough to reliably say they are real rather than artifacts of imprecise statistical methods.[11] It is surely the case that many children are harmed by family disruption. But other people raised by single parents may have had worse outcomes if their parents had married or stayed married. People raised by two happily married parents would almost surely have done worse if their family had been disrupted. But the alternative for people who were raised by single parents would not necessarily have been being raised by two ***happily*** married parents.[12]

The basic methodological problem is that we cannot observe these "counterfactual" outcomes—what would have happened if a person's family situation had been different. A few papers are better able to address this problem by looking at specific subsets of children whose parents' family decisions were affected by specific features of their environments. Two examples reveal the importance of considering "what would have happened" when we think about the effect of single parenthood on child outcomes.

The first paper, by Keith Finlay and David Neumark, looked at the effects of growing up with a never-married mother on high school graduation rates.[13] In their study, they isolate the impact on children who would have grown up with a married mother but for the fact that she lived in a state with a high incarceration rate (after accounting for crime rates), leading to fewer men available to marry. The results indicate that these children would have been no better off—or possibly even worse off—if their mothers had married. This finding makes intuitive sense. The counterfactual for these children if the state incarcerationrate had been lower would have been living with a father with a high criminalpropensity. Such men are unlikely to be positive influences on their children.

A second paper, from Austrian researchers, considered whether experiencing a parental divorce affects a range of outcomes.[14] They isolated impacts on children who would have been raised by both their parents if not for the fact that their fathers' workplaces had relatively high numbers of women similar in age to the father and working in the same occupation. That is, these children experienced divorce because their fathers were more likely to enter into an extramarital affair simply by virtue of circumstances that make an affair more likely. The study found that experiencing divorce worsened educational, employment, and health

outcomes for this subset of children. Again, the results make sense: many of these children may have been in what seemed to them to be fairly healthy families, and the divorces they experienced were likely to have involved a great deal of acrimony and pain.

The relevant policy question—for which we lack good answers based on rigorous research—are what share of children would have ended up better off (and by how much) in the counterfactual where their parents had married or stayed married. To know that, we would need to understand what caused specific parents not to marry or to divorce and how things would have been different hadthese causes not led to family disruption.

What is self-evident—without consulting research—is that more children would fare better if more were raised by their married parents within a healthy relationship. As the Social Capital Project wrote in its earlier report, The Wealth of Relations, compared with children of single parents, children with happily married parents

> get to see both parents every day, spend the holidays with both, and they don't have to feel guilty about spending or enjoying more time in one household than the other. Nor do they have to question whether they caused their parents to break up. They have a single set of household rules, a single bedroom and wardrobe. Their schedule does not depend on which parent they are staying with. They get engagement from both parents and avoid hearing parents acidly complain about each other. Their parents are less exhausted by childrearing. They get the material benefits of economies of scale and of higher family income. They are witness to what a loving relationshiplooks like and have first-hand evidence that such relationships are secure and sustainable. And they avoid having to adjust to the changingromantic lives of their mother or father—changes which can include disruptive remarriages and family-blending.

*The Wealth of Relations* also noted that cutting-edge research by Harvard economist Raj Chetty and his colleagues implies that growing up surrounded by family stability is also beneficial to children:

> the team looked at adults who, as children, were poor but lived in low-poverty neighborhoods. They found that black men had stronger upward mobility the more low-income black fathers there were in their childhood neighborhood. This was true regardless of whether someone's own father was present, suggesting that even the family cohesion of other black children in the neighborhood affected them. Meanwhile, having more low-income white fathers in the neighborhood did not increase the upward mobility of poor black children; nor did having more low-income black men who were childless. More low-income black fathers in a neighborhood also corresponded with higher future employment among poor black boys. The relationship between the number of low-income black fathers and future employment was much smaller for poor white boys and negligible for poor black girls.

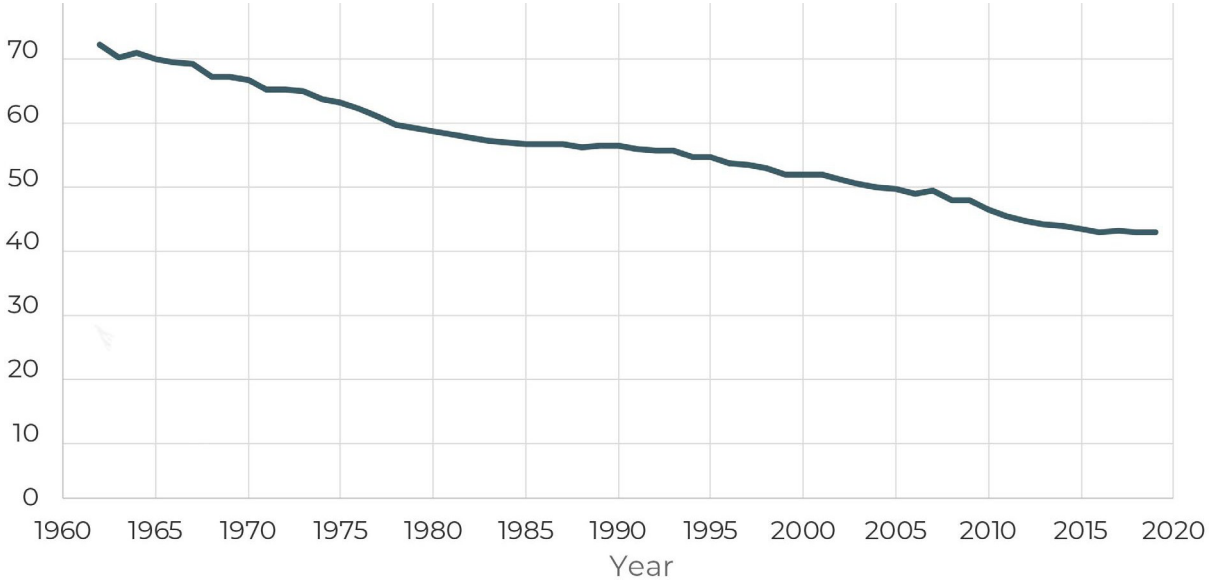
The social capital inherent in a child's relationships to her parents will be more valuable when both are part of her life and when they have a healthy relationship with each other. And social capital available to children is more valuable to the extent that they are surrounded by other healthy family relationships.

## FAMILY STABILITY HAS DECLINED

However, American families are far less stable today than in the past. Fewer Americans are married, more romantic relationships take place outside of marriage, more marriages end in divorce, and ultimately, more children are born into or raised outside of intact families.

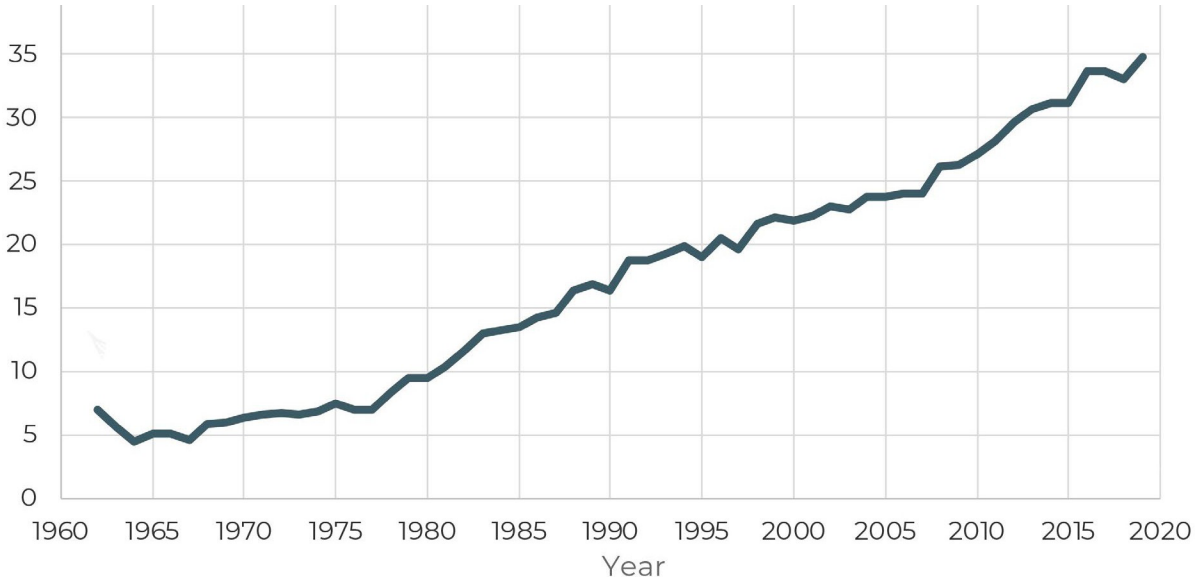
Although most Americans still marry or say they would like to marry, marriage is not nearly as common as it was in previous generations.[15] Overall, between 1962 and 2019, the percentage of women ages 15-44 who were married dropped from 71 percent to 42 percent (Figure 1).[16] Furthermore, Figure 2 shows the percentage of women ages 30-34 who had never married increased from 7 percent in 1962 to 35 percent in 2019.[17]

Figure 1. Percent of Women Ages 15-44 Who are Married, 1962-2019




Source: Social Capital Project analyses of data from the Annual Social and Economic Supplement to the Current Population Survey, using the Integrated Public Use Microdata Series Online Data Analysis System. Separated women are included as married.

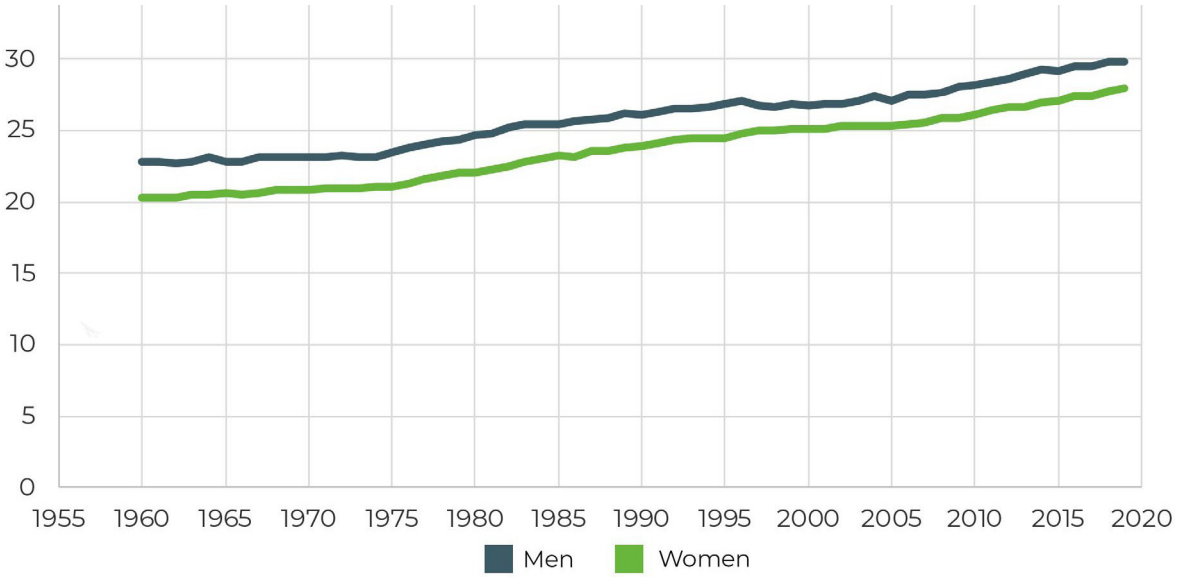
Figure 2. Percent of Women Ages 30-34 Who Have Never Married, 1962-2019




Source: Social Capital Project analyses of data from the Annual Social and Economic Supplement to the Current PopulationSurvey, using the Integrated Public Use Microdata Series Online Data Analysis System.

In 1960, there were 74 marriages per 1,000 unmarried women ages 15 and older, but as of 2018 that rate had declined by more than half to 31 per thousand.[18] Peoplespend less of their life married, as the median age at first marriage in the United States has steadily climbed from 20 and 23 for women and men, respectively, in 1960 to a median of 28 and 30, respectively, in 2019 (Figure 3).[19]

Figure 3. Median Age at First Marriage by Sex, 1960 to 2019



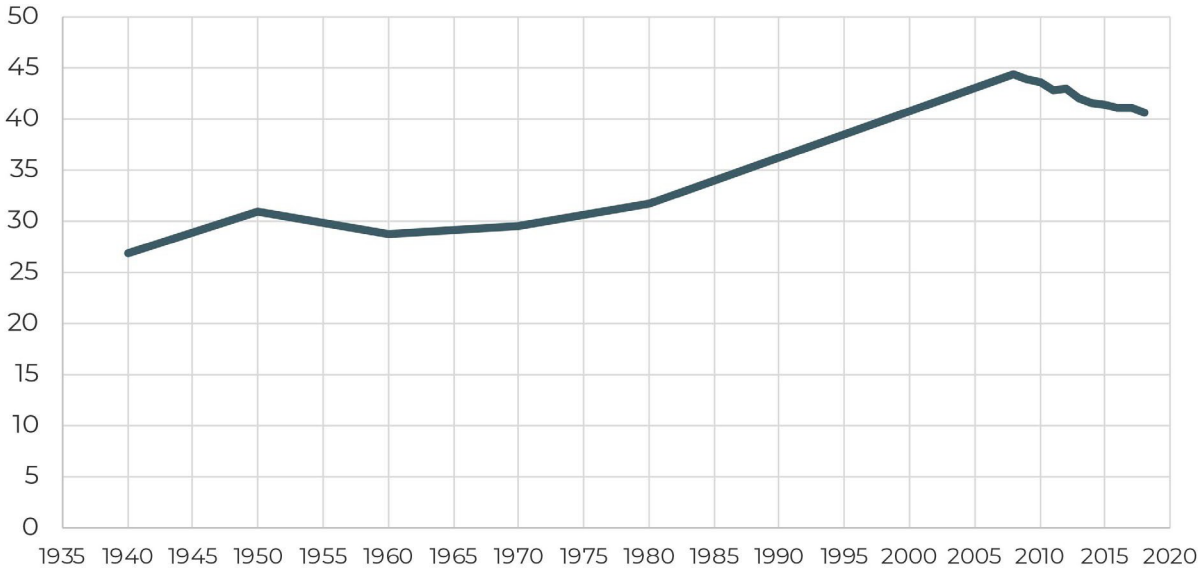

Source: U.S. Census Bureau, "Estimated Median Age at First Marriage, by Sex: 1890 to the Present," Historical Marital Status Tables,Table MS-2, https://www.census.gov/data/tables/time-series/demo/families/marital.html.

The decline in marriage is due not only to increasingly delayed marriage and to the rise in never-married adults, but also to higher divorce rates. In 1960, the divorce rate was 9 per 1,000 married women, and that rate increased through the 1960s and 1970s, reaching 23 per 1,000 by 1980.[20] Comparable estimates are surprisingly difficult to obtain after 1980, but by 2010 the divorce rate probably was somewhat lower (21 per 1,000), and it fell further to 17 per 1,000 by 2018.[21] Any post-1980 drop was confined to the under-35 population.[22] (In the past decade, divorce has also fallen among those in their late thirties and early forties, but the rate remains elevated relative to 1980.)[23]

Furthermore, the overall divorce rate after 1980 may have declined only because the Baby Boomers aged out of the part of the life cycle where divorce is most common. When Sheela Kennedy and Stephen Ruggles considered what would have happened had the population not aged between 1980 and 2010, they found that divorce rates would have risen about as much between 1990 and 2010 as between 1970 and 1980.[24]

Because divorce rates have fallen during the part of the life cycle when divorce is most common, it may be that today's post-Millennials, when they are the age of today's Baby Boomers, will be less likely than Boomers to have divorced at some point in their lives (conditional on having been married). Kennedy and Ruggles estimated that ever-married Americans in their 20s or early 30s in 2010 were less likely to have divorced than their same-age counterparts in 1980. However, as noted, their marriages will likely be at greater risk for divorce when they are older than used to be the case. (Divorce rates among older women increased between 1980 and 2010 then stabilized.)[25]

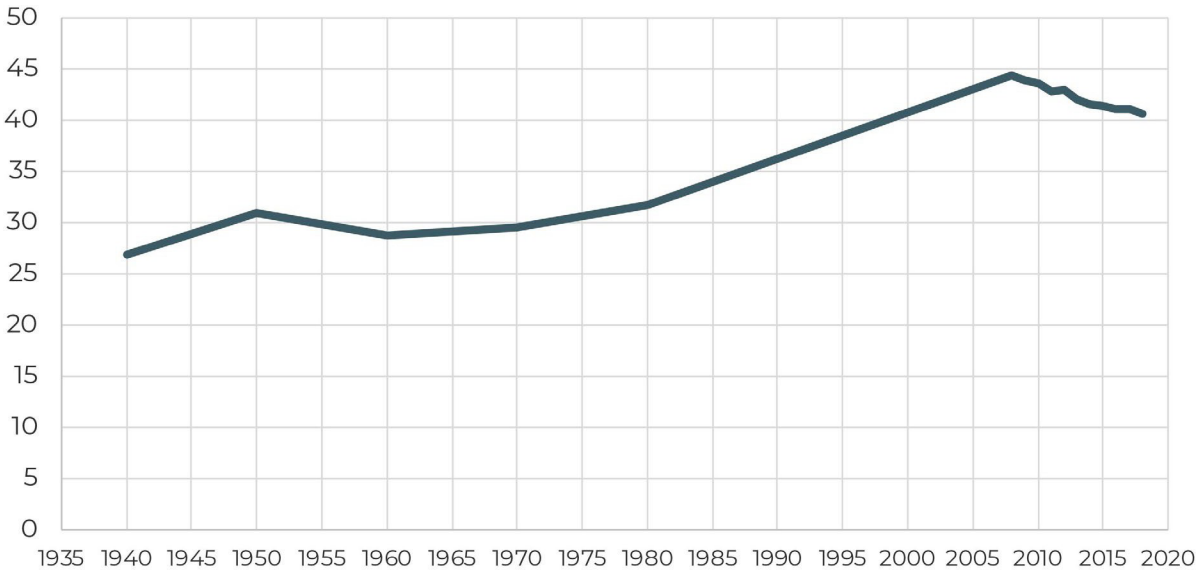
Figure 4. Percent of Ever-Married Women Ages 50-54 Who Ever Divorced, 1960 to 2018




Source: Social Capital Project analyses of Integrated Public Use Microdata Series microdata from the decennial census and American Community Survey.[26]

As marriage has declined, couples have become more likely to cohabit as unmarried couples. In the 1960s, less than one percent of couples living together were unmarried—a figure that rose to 5 percent by 1990 and stood at 12-13 percent as of 2019 (Figure 5).[27] Furthermore, marriage is much more likely to be preceded by cohabitation today than in the past. Among women ages 19 to 44 who married between 1965 and 1974, just 11 percent had cohabited with their husbands prior to marriage, but that number jumped to 32 percent among those who married between 1975 and 1979 and continued to soar thereafter. For the past two decades, two-thirds of new marriages have been preceded by cohabitation.[28]

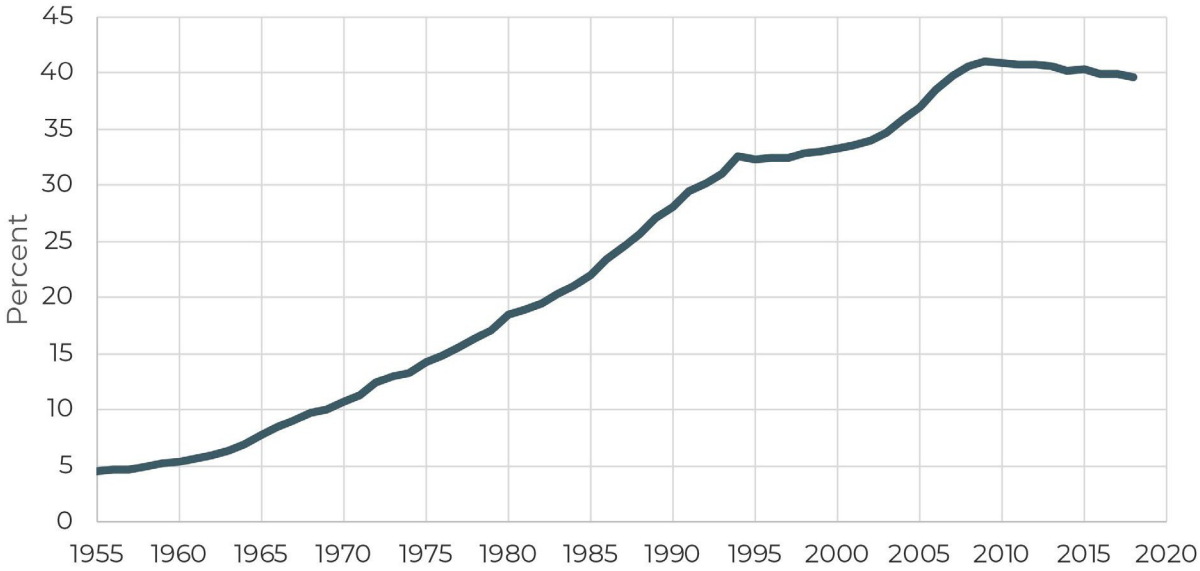
Figure 5. Percent of Adults Cohabiting as a Percent of Adults Living with a Partner, 1967-2019




Source: Social Capital Project analyses of Census Bureau tabulations. See https://www2.census.gov/programs-surveys/demo/ tables/families/time-series/adults/ad3.xlsx. There are breaks in the series between 1995 and 1996 (prior to 1996, cohabiters werenot identified directly) and between 2006 and 2007 (prior to 2007, only cohabiters of household heads were identified).

The decline in marriage and the increase in cohabitation has led to substantial growth in unwed childbearing. The percent of births to unmarried mothers has jumped from five percent in 1960 to 40 percent today (Figure 6).[29] That is only slightly below the peak of 41 percent in 2009.

Figure 6. Percent of Births to Unwed Mothers, 1960-2018



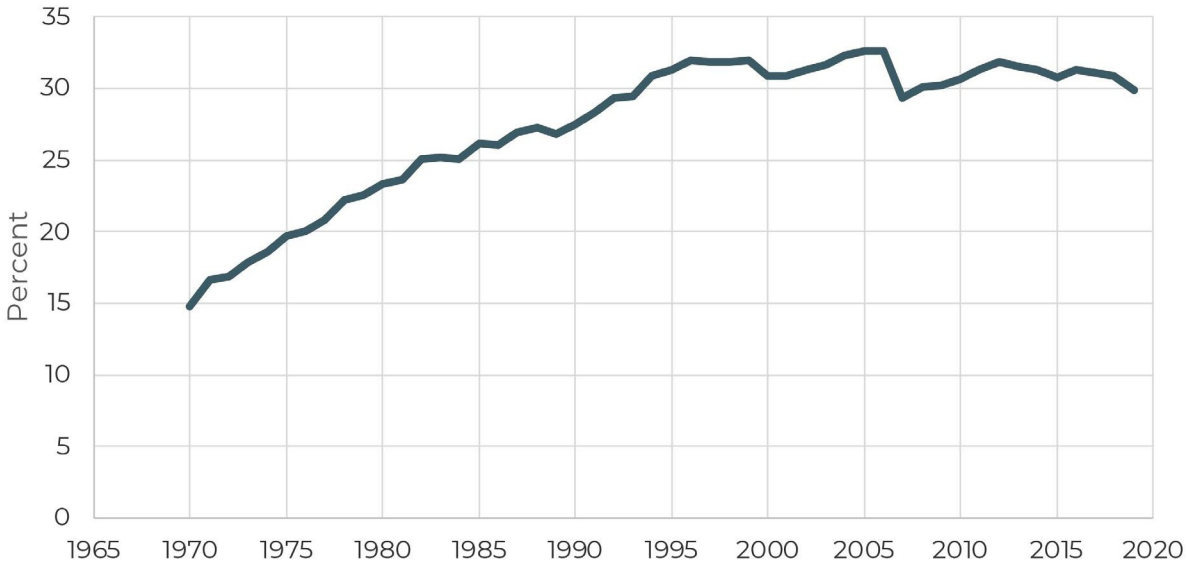

Source: Centers for Disease Control and Prevention, National Center for Health Statistics, various National Vital Statistics Reports. See note 29 for details.

This increase in unwed births is due not only to the decline in marriage overall, but also to the decline in "shotgun marriages" or post-conception/pre-delivery marriages, as we show in a previous report.[30] In the early 1960s, births produced by nonmarital conceptions followed a shotgun marriage 43 percent of the time, but today fewer than 10 percent involve a shotgun marriage. In fact, besides the decline in marriage rates overall, which increased the pool of women "at risk" for an unwed birth, the decline in shotgun marriage has been the largest contributing factor to the rise in unwed births.[31] It has been the single most important factor contributing to rising unwed childbearing among women under thirty.

While unmarried mothers are often cohabiting with the father of their child at the time of the child's birth, cohabiting relationships are far less stable than marriages. In a 2007 study researchers found that 50 percent of children born to cohabiting parents experienced a maternal partnership transition by their third birthday, compared to just 13 percent of children in married-parent families.[32] Thus, children born into households where the parents are not married are much more likely to see their parents break up.

The combination of unwed births and divorce has led to a marked rise in the share of children living with a single parent. Fifty years ago, in 1970, 85 percentof children lived with two parents, four percent of children lived with a divorced single parent, while another one percent lived with a never-married parent.[33] (The rest lived with only one married parent present, had a widowed parent, or lived with neither parent.) In 2019, just 70 percent lived with two parents.[34] Roughly 10 percent lived with a divorced single parent, and close to 15 percent lived with a never-married parent.[35]

Figure 7. Percent of Children Living without One or Both Parents, 1970-2019




Source: Social Capital Project analyses of published Census Bureau tables on Historical Living Arrangements of Children. https://www2.census.gov/programs-surveys/demo/tables/families/time-series/children/ch1.xls. "Parent" refers to biological,step, or adoptive parents. The Current Population Survey was changed in 2007 to better identify both parents.

It is true that some children of never-married parents live with their cohabiting parents. However, some children living with married parents have experienced a divorce or were born to a single mother but live with a parent and stepparent. Some will experience divorce later in childhood. As noted above, nearly half of children have spent part of their childhood without at least one biological parent, up from around one-third of children born in the 1960s. Since unwed childbearing has become so much more common, the duration of childhood spent without both parents has increased even more than these figures would suggest.

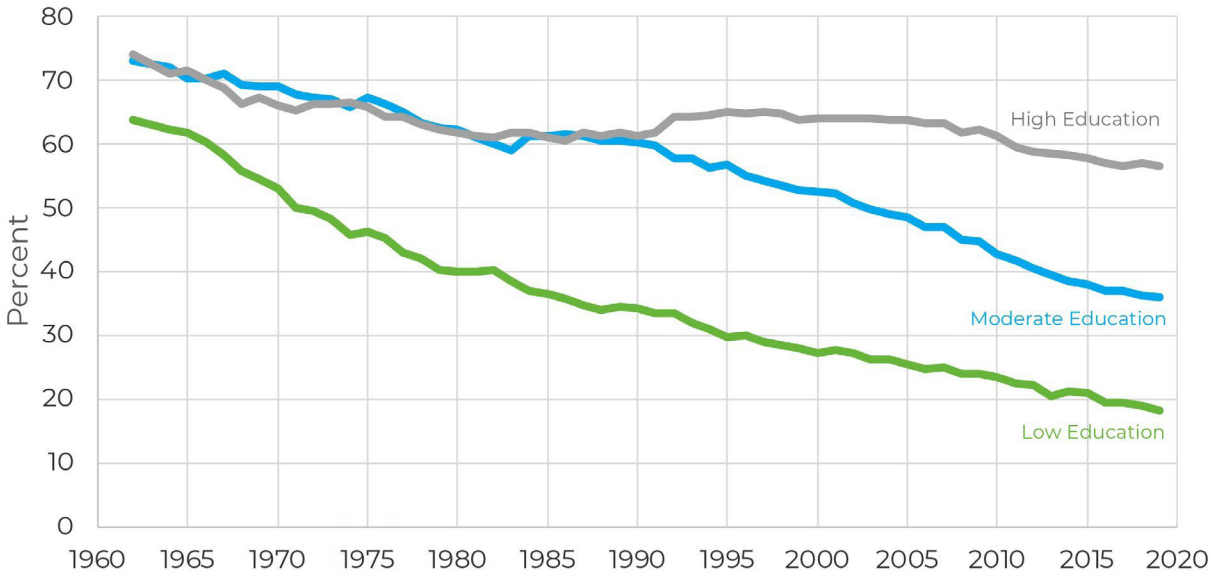
Family instability in the United States has also led to an increase in the percent of Americans who have children with multiple partners, creating complicated relationships across households. Nearly 16 percent of all parents in the United States have children with more than one partner, and in 20 percent of all marital or cohabiting relationships, at least one of the partners has children with more than one partner.[36] Furthermore, fathers with multi-partner fertility are less likely to say they feel close to their children and are more likely to have failed toestablish paternity for at least one of their children.[37]

## THE SOCIOECONOMIC DIVIDE IN FAMILY STABILITY

Although family instability has increased among all Americans, family instability is far more common among the non-college-educated. The highly educated marry more often, stay married more often, and rarely bear children outside of marriage. (We define highly-educated as being in roughly the highest quintile of educational attainment, low education as being in roughly the lowest quintile of educational attainment, and moderate education as those in the remaining quintiles.[38]) Family stability also varies by race.

As of 2019, 57 percent of highly-educated women ages 15-44 were married, compared to only 36 percent of moderately-educated women and 18 percent of women with low education (Figure 8).[39] These differences were much smaller in the mid-1960s, with less than ten percentage points separating the three groups in 1964.

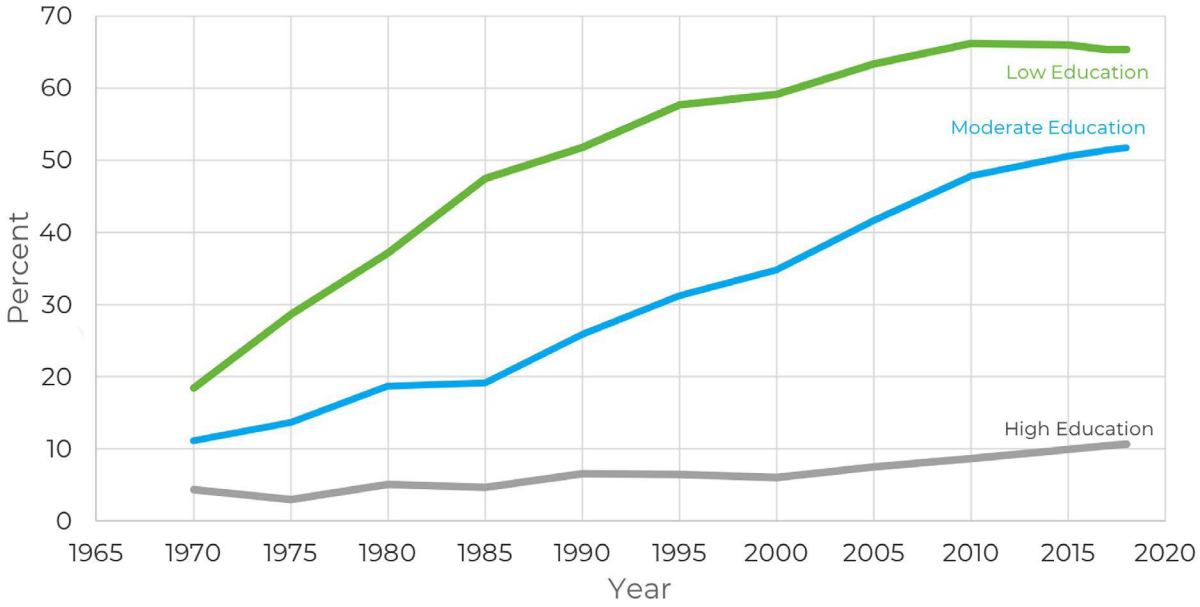
Figure 8. Percent of Women Ages 15-44 Who are Married, 1962-2019, by Education Level




Source: Social Capital Project analyses of Current Population Survey data. See notes 16, 38 and 39 for more details.

Two-thirds of births (65 percent) among women with low education occur outside of marriage as of 2018 along with half (52 percent) of births to moderately-educated women (Figure 9). Among highly-educated women, however, just 11 percent occur outside marriage.[40] While the share for highly- educated women rose modestly over the past 50 years (by roughly 6 percentagepoints), the increases for the less-educated groups were dramatic.

Figure 9. Percent of Births to Unwed Mothers, 1970-2018, by Education Level



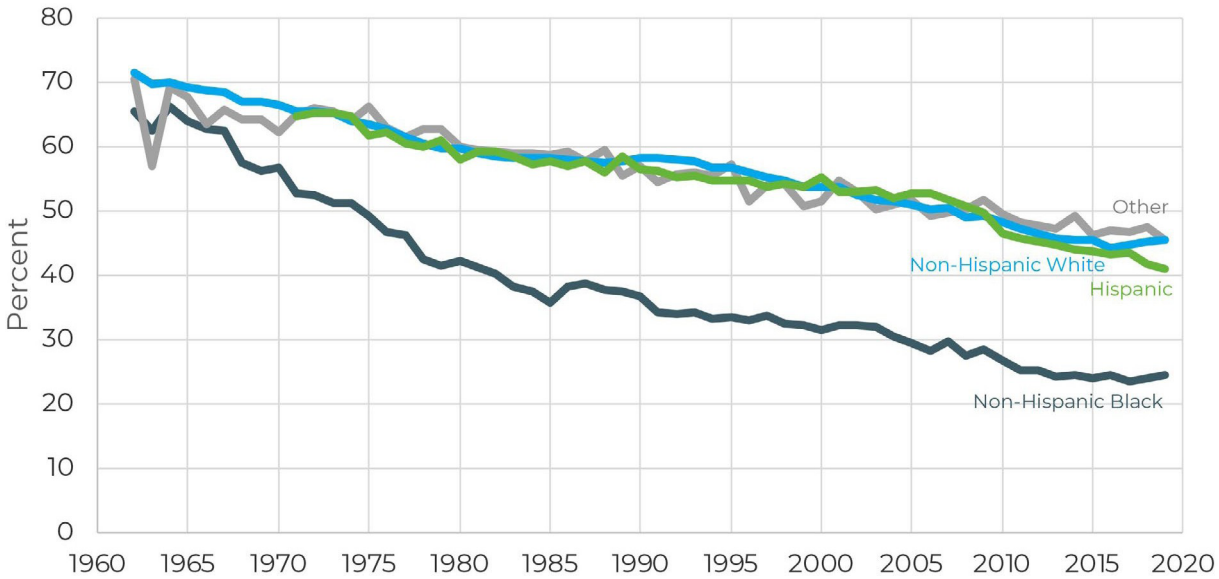

Source: Social Capital Project analyses of National Vital Statistics Natality Birth Data 1970-2018, National Bureau of Economic Research, accessed July 2, 2020, https://data.nber.org/data/vital-statistics-natality-data.html. See notes 38 and 40 for details.

The decline in "shotgun marriage" has been particularly steep among the two less-educated groups of women, as we discuss in a previous Social Capital Project report.[41] In 2007, only 2 percent of births resulting from nonmarital pregnancies followed a shotgun marriage among those with low education levels, down from 26 percent in 1977; among moderately-educated women, the figure was only 8 percent in 2007, down from 34 percent in 1977. However, among the highly educated, 27 percent of 2007 births resulting from nonmarital pregnancies followed a shotgun marriage, down only modestly from 34 percent in 1977.

A high rate of unwed childbearing is not the only factor contributing to greater family instability among non-college-graduate adults. Those with less education are also more likely to divorce.[42] Women with a bachelor's degree and married for the first time are very likely to be married for a long time; 78 percent will still be married 20 years later. However, among women entering their first marriage who have some college but no bachelor's degree, it is as likely as not that their marriage will end within 20 years. Among women with no more than a high school diploma, just 40 percent will still be in their first marriage after 20 years.

Family instability differences between racial groups in the US are also striking. In the early 1960s, the share of women who were married was quite similar for non-Hispanic whites, non-Hispanic blacks, Hispanics, and other women. Roughly 65 to 70 percent of women ages 15 to 44 in each group were married in 1962 (Figure 10). Marriage rates subsequently declined across racial groups, to the point where fewer than half were married in 2019; however, marriage declined much more among African American women than among the other groups; by 2019, fewer than a quarter (24 percent) of black women between the ages of 15 and 44 were married.

Figure 10. Percent of Women Ages 15-44 Who are Married, 1962-2019, by Race




Source: Social Capital Project analyses of data from the Annual Social and Economic Supplement to the Current PopulationSurvey, using the Integrated Public Use Microdata Series Online Data Analysis System.

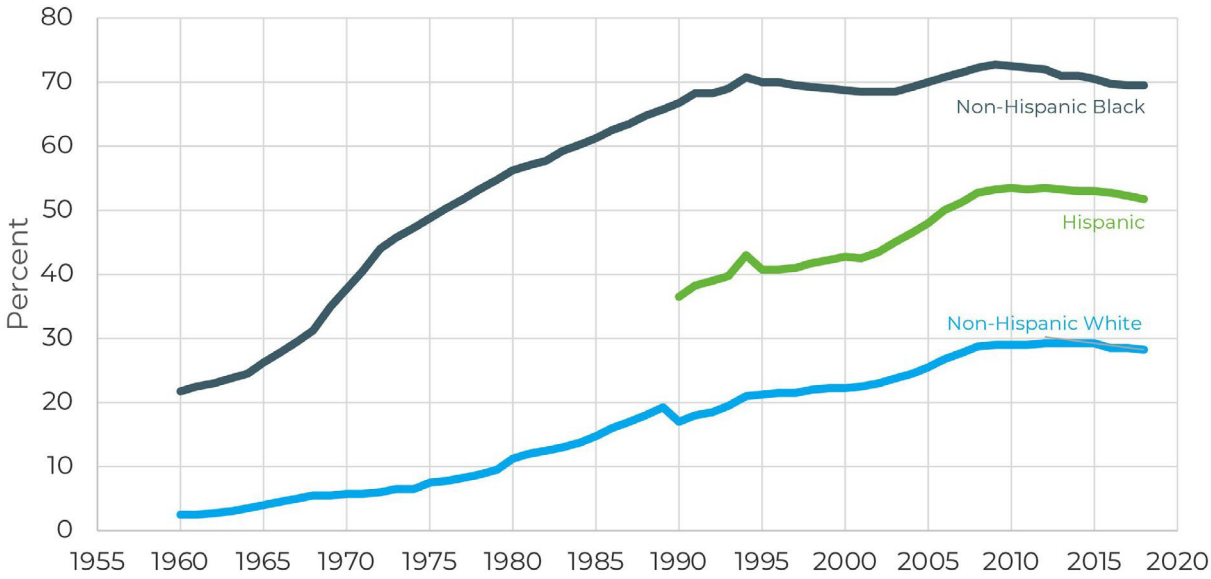
These patterns are no less dramatic looking at the share of women ages 30 to 34 who have never married. In 1962, fewer than 10 percent of such womenin any racial group had never married; by 2019, 28 to 37 percent of non-blackwomen in their early 30s had never been married, but that was true of 64 percent of black women.[43]

Racial differences in shotgun marriage have narrowed over time, however. In 2007, 13 percent of non-Hispanic white births resulting from a nonmarital conception followed a shotgun marriage, compared with 3 percent of non-Hispanic black births. In 1962, the figures were 51 and 29 percent, respectively. (However, blacks remained much more likely than whites to be faced with the decision to have or not to have a shotgun marriage. Three in four births—73 percent—to black women in 2007 involved nonmarital conceptions, compared with 38 percent for non-Hispanic whites.)[44]

African-American women are also more likely to have a marriage end in divorce. Nearly two-thirds (63 percent) of first marriages among black womenwill end in divorce within the next twenty years. That compares with 47 percent for non-Hispanic whites, 46 percent for Hispanics, and just 31 percent for Asian Americans.[45]

Although unwed childbearing has increased a great deal across all racial groups,it is higher among black and Hispanic women than white women (Figure 11). Over two-thirds of births to black women (69 percent) are to unwed mothers, and over half (52 percent) of births to Hispanic women are. Among non-Hispanicwhite women, the figure is just 28 percent, though that was up from only 2 percent in 1960.

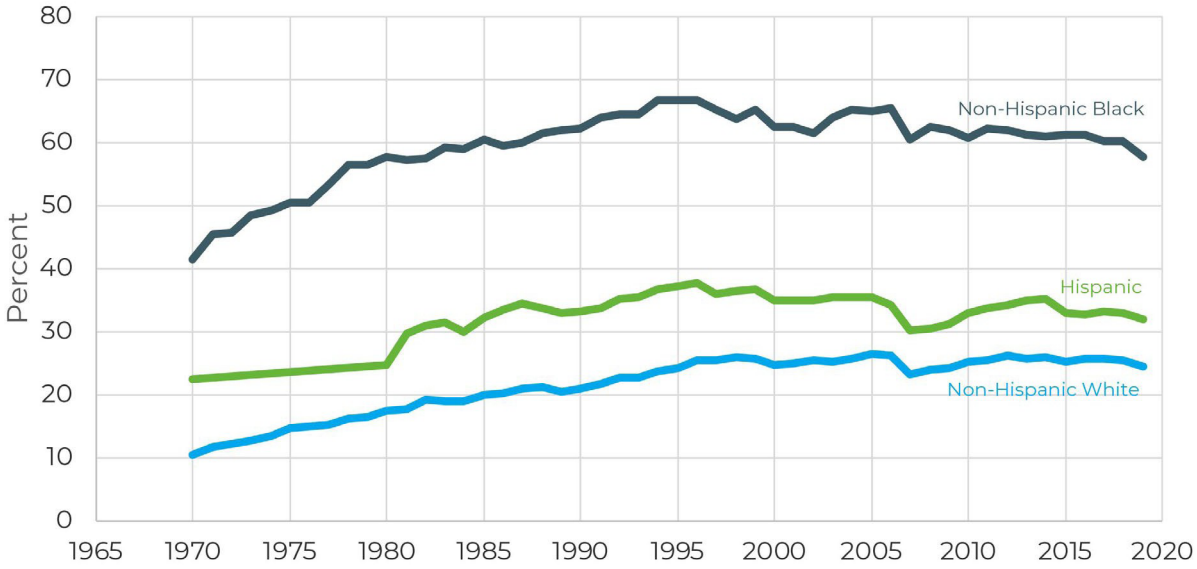
Figure 11. Percent of Births to Unwed Mothers, 1960-2018, by Race




Source: Social Capital Project analyses of National Vital Statistics Natality Birth Data 1970-2017, National Bureau of EconomicResearch, accessed January 31, 2020, https://data.nber.org/data/vital-statistics-natality-data.html. See note 29 for details.

As a consequence of all these patterns, African American children are especially likely to live apart from one or both of their parents compared withother children (Figure 12).[46] Roughly six in ten black children are apart from atleast one parent—about twice the share of non-Hispanic white and Hispanic children. This proportion appears in Figure 12 to be down from the mid-1990s high, but breaks in the time series, including a significant one between 2006 and 2007, overstate the true decline.

Figure 12. Percent of Children Living without One or Both Parents, 1970-2019, by Race




Source: Social Capital Project analyses of published Census Bureau tables on Historical Living Arrangements of Children, TablesCH-2, CH-3, and CH-4. https://www.census.gov/data/tables/time-series/demo/families/children.html. "Parent" refers to biological,step, or adoptive parents. The Current Population Survey was changed in 2007 to better identify both parents.

## WHAT IS DRIVING RISING FAMILY INSTABILITY AND THE SOCIOECONOMIC DIVIDE IN MARRIAGE?

While the trends in family instability and the variation across socioeconomic groups are unambiguous, it is much less clear what has caused these patterns. One leading explanation is that they reflect a worsening in the economic fortunes of men—the so-called "marriageable man" hypothesis, first proposed by sociologists William Julius Wilson and Kathryn Neckerman.[47]

The hypothesis proposes that men must meet some economic threshold that makes them "marriageable" to women and that fewer men have surpassed that bar over time. It assumes that the decline in marriage is primarily a result of fewer women wanting to marry the men on offer (rather than fewer men wanting to marry). The decline in marriage is then said to have increased single parenthood, by some combination of (1) more unmarried women at risk of a nonmarital pregnancy, (2) fewer shotgun marriages as a result of men being less economically attractive as husbands, and (3) more divorces for the same reason.[48] The low marriageability of the men on offer to poorer women is also said to explain why family stability is so much lower among more disadvantaged socioeconomic groups.

A number of studies have found an association across geographic areas between male employment and the prevalence of marriage, and research also consistently finds that men who are employed or have higher earnings are more likely to be married or to marry.[49] These studies are rarely able to convincingly make a strong causal case. Indeed, it might be argued that where marriage is weaker as an institution, men change their behavior in ways that worsens their economic outcomes.[50] Robert Lerman and Bradford Wilcox's research suggests that men's employment rates would be higher if the marriage rate were the same today in 1980. In their words,

> When young men and women replace formal commitments with informal relationships or none at all, work becomes less urgent, especially for men, who have historically taken all kinds of jobs to support their families. With no wife or children to support, men become less focused on the job market.[51]

Another study finds evidence that the liberalization of divorce and increased economic opportunities for women have reduced the incentives for men to make themselves more marriageable.[52]

Consistent with these lines of reasoning, rigorous research finds that marriage causally increases men's wages.[53] One study comparing identical twins who differ in their marital statuses estimates that marriage increases wages by about one-fourth.[54] A weakening of the institution of marriage might have reduced men's perceived obligations and changed their incentives, thereby leading to less "marriageability" in the form of lower employment rates and wages.

Moreover, separate from point-in-time analyses, very few studies have considered the extent to which the ***decline*** in marriage or the rise in single parenthood can be explained by a decline in economic circumstances of men. Most worrisome trends in family stability began in the 1960s or earlier, during the so-called "Golden Age" of the American economy. Beyond that discrepancy, the conclusion of David Ellwood and Christopher Jencks, writing in 2004, is almost certainly applicable today: "men's real wages have not changed enough over the past generation to explain much of the change in family structure, even among the least educated."[55] In fact, this conclusion is even more compelling today, because male wage trends have been much more positive over the past twenty-five years than they were in the preceding quarter century.

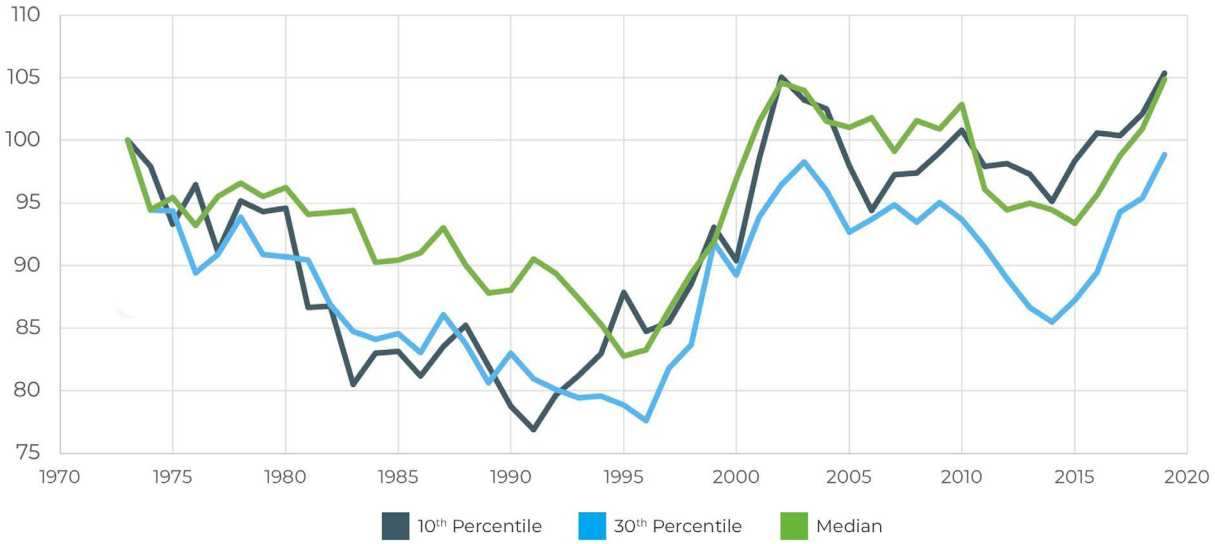
### *Have Men Become Less Marriageable?*

Whether there is anything to the marriageable men hypothesis depends centrally on the thresholds for marriageability that women have applied and how many men have been able to reach those thresholds. The simplest threshold might be that men must bring to the table at least a minimum level of purchasing power. One way to assess whether fewer men have achieved that level is to consider trends in inflation-adjusted after-tax hourly compensation

among young men, as in Figure 13.[56] We confine our analysesto non-Hispanic men to isolate trends in marriageability from changes in population demographics over time.[57]

The chart displays three trends for non-Hispanic men between the ages of 25 and 29—one for median pay (where half of men make more and half make less),one for the 30th percentile of pay (where 70 percent of men make more), and one for the 10th percentile of pay. Hourly pay is available in this data only back to1973. In Figure 13, all pay rates are scaled so that the 1973 rate is equal to 100.

Figure 13. After-Tax Hourly Compensation of Non-Hispanic Men Ages 25-29, 1973-2019




Source: Social Capital Project analyses of Current Population Survey data. See end note 56.

The inflation-adjusted hourly pay of young non-Hispanic men declined sharply between 1973 and the early- to mid-1990s. At its low point, in 1995, the median was down 17 percent. (The 1973 level was probably higher than it had even beento that point.[58]) The 10th and 30th percentiles fell as much as 22 to 23 percent.[59]

One caveat to these twenty-year trends is that in supplemental analyses not shown here, we found that these large declines were much less pronounced among middle-aged men. Among non-Hispanic men between the ages of 35 and 44, median hourly take-home pay dipped below the 1973 level in 1974 and 1996, but it was otherwise always at least as high as in 1973. Through the mid-1990s, the 30th percentile was never more than 5 or 6 percent lower than in 1973 and was above the 1973 level from 1975 to 1989. The 10th percentile fell more consistently between 1973 and the mid-1990s, but it bottomed out only 11 to 12 percent lower than in 1973. Even among men ages 30 to 34, the median never fell by more than 10 percent, and the 10th percentile was never lower than 16 percent of its 1973 level.

Part of the drop in pay for younger men appears to reflect an increase in post-secondary schooling, which might have altered the timing of career earnings. Staying in school longer can be expected to increase lifetime earnings, but in the short-run, pay might be lower than it would have been had a person gainedyears of work experience rather than being in school. It may take a few years for the benefit of extra schooling to exceed the cost of foregone work experience.[60]

The deep recessions between 1973 and 1975 and between 1980 and 1982, as wellas the more moderate recession from 1990 to 1992, may have hurt hourly pay rates, though by reducing employment, they had a bigger impact on annual pay. Falling productivity growth and accelerating inflation (through the early 1980s) also hurt men's pay during this period.

Another likely contributor to declining pay among men was the shift from an era in which men were often sole breadwinners to one with many more two- earner households. The pervasiveness of the idea that a husband should be able to raise a family on one income may have translated into men—especiallyworking-class men—enjoying "breadwinner rents" in excess of the pay that their productivity would have justified. Previous research has suggested that men's pay outpaced their productivity during the decades of the twentieth century that marked the high point of the American labor movement, which had as a primary goal securing a "family wage" for male workers.[61] As married women became more attached to the labor force in the 1970s, the rationale for paying a man enough to raise a family on one income became difficult to justify, especially as economic competition from abroad became more intense. Finally, as noted above, the decline in marriage itself may have reduced men's hourly pay by weakening the sense of obligation to support a family that men faced.

Regardless of the causes, it does appear that fewer young men would have been able to meet a fixed absolute threshold for marriageability over the course of the 1970s, 1980s, and early 1990s. However, the simplest version of this hypothesis runs into a problem after the mid-1990s, as the pay of young men has recovered over the past 25 years. This quarter century has been marked by two strong periods of wage growth—the late 1990s boom, and the recent, pre-pandemic expansion—and by the Great Recession. Median pay exceeded its 1973 level from 2001 to 2010 (except in 2007), and in 2018 and 2019. Like the median, pay at the 10th percentile was higher than ever before in 2019 (essentially at its 2002 level), though last year the 30$^{th}$ percentile remained a percentage point lower than in 1973.

While Figure 13 is based on hourly pay, it might be argued that marriageability is a function not of earnings per hour but annual earnings. After all, someone can spend much of the year out of work even if their hourly pay is as high as ever. Employment among prime-working-age men has declined steadily over time, so perhaps the focus on hourly pay is missing the declining marriageability story.

We use hourly pay here precisely to avoid complications around declining employment rates, which are widely misunderstood. There is a cyclical component to employment that reflects changes in labor market conditions, but over the past fifty years, this component has been less important than the long-term decline in the share of men seeking work. While many observers interpret this decline in prime-age "labor force participation" as an indicator of falling demand for male labor at a given rate of pay, the evidence is stronger that it reflects declining labor supply—fewer male workers who want a job at prevailing pay rates.[62]

Indeed, the fact that hourly pay is as high as ever is one indication that falling demand is not the main culprit, but it is not the only one. Research suggests that men who want a job or are not working because they have given up hope of finding a job account for only a small fraction of the decline in prime-age male labor force participation over the long run. Most of the decline involves disabled men and able-bodied men who tell government surveyors they do not want a job.[63]

For comparison, Figure 14 provides the trend from 1973 to 2018 in non-Hispanic men's after-tax annual compensation.[64] The basic story is the same as when hourly pay is tracked. The trend reflects the business cycle more over the first twenty years than is the case for the hourly pay trend, and the low points for the 10th and 30th percentiles shift back to the early 1980s double-dip recession. The 30th percentile of annual compensation declined by 25 percent by 1982, and the 10th percentile was one-third lower in 1983 than in 1973. Despite these striking drops, annual pay subsequently recovered. The median was higher in 2018 than in any previous year, and in the twenty-year period from 1998 to 2018, it was higher than in 1973 in all but six years. The 30th percentile finally exceeded its 1973 level in 2018.The 10th percentile was higher than in 2018 only in 1999 and 2001.

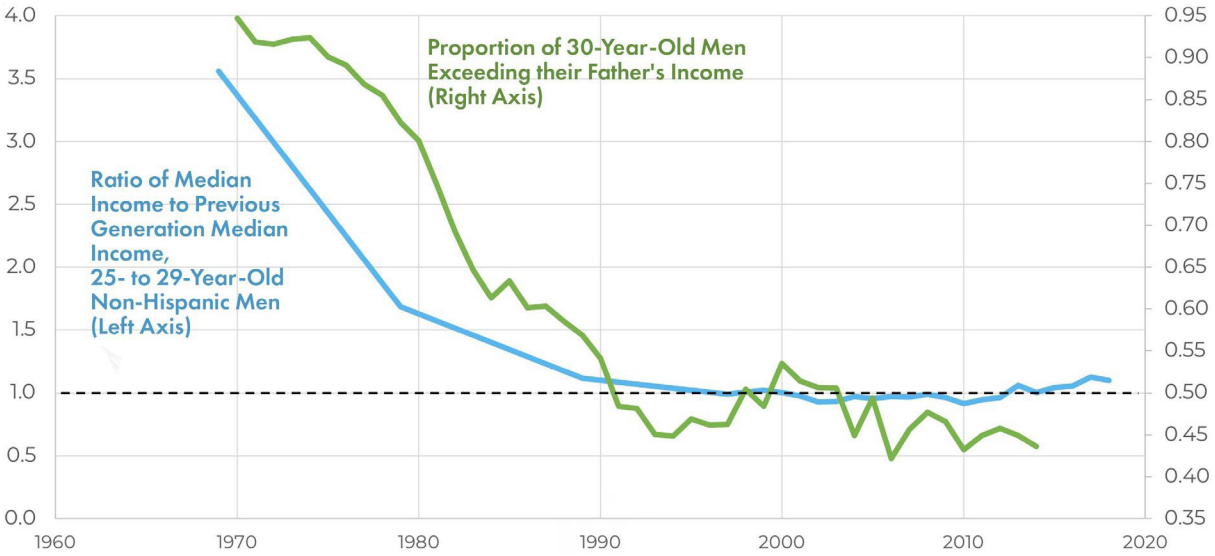
Figure 14. After-Tax Annual Compensation of Non-Hispanic Men Ages 25-29, 1973-2018

Source: Social Capital Project analyses of Current Population Survey data. See end note 64.

Clearly a simple story about absolute thresholds determining marriageability cannot explain the fact that marriage rates are so much lower today than in 1973 and single parenthood so much higher, since male pay is about as high asit was then. It is possible that the earlier, roughly 20-year, decline in male pay reduced marriage and increased single parenthood over the 1970s, 1980s, and early 1990s, and then cultural or other factors continued these trends once pay started rising again. But there is nothing in the marriageable men hypothesis as typically stated that would predict an asymmetric response of marriage to men's economic circumstances, where declining pay reduces marriage but rising pay does not increase it. Perhaps men born in the 1950s and 1960s were less marriageable, single parenthood became more normal, and men born in the 1970s and 1980s were socialized by their parents into different attitudes about marriage and single parenthood.

The marriageable men hypothesis may fare better if more nuanced thresholds are invoked. One possibility is that what matters is how men are doing relative to how the previous generation of men were doing. Harvard economist Raj Chetty and his research team have found that the share of men with individual income that exceeds their father's at the same age fell dramatically over time.[65] Figure 15, based on our modification of their estimates, shows that while 95 percent of thirty-year-olds in 1970 exceeded their father's income, by 2014 just 44 percent did (see the right axis).[66] In only five years after 1990 did half of men surpass their father, a threshold shown by the bolded dashed line.

Figure 15. Generational Mobility of Young Men, 1969-2018



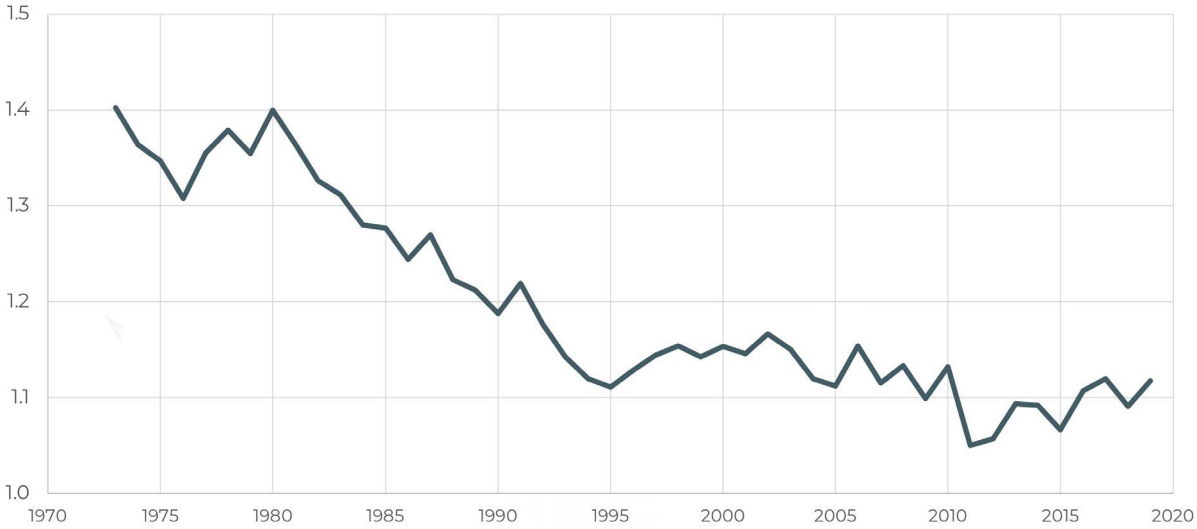

Source: Social Capital Project analyses using data from Chetty et al. (2017) and the Integrated Public Use Micro-data Series(IPUMS) Online Data Analysis System. See end notes 66 and 67.

The trend is similar if one instead computes the ratio of two median annual individual incomes—that of non-Hispanic men ages 25 to 29, and that of non-Hispanic men the same age thirty years earlier (also shown in Figure 15).[67] Men in their late 20s in 1969 earned 3.6 times what their counterparts did in 1939. By 1979, the ratio had plummeted to 1.7, indicating that young men were 70 percent richer than young men in 1949 were. The figure was just 12 percent by 1989. At some point in the 1990s, the ratio reached one, indicating that the median personal income for young men was no higher than for young men thirty years earlier. The ratio dipped below one from 2001 to 2012. (Note, however, that these estimates do not take taxes into account, which have fallen over time.) In 2013, the median late-twenty something male was finally once again better off than his counterpart thirty years earlier. That remained the case in 2018, though only barely.

The dramatic declines in Figure 15, however, primarily reflect how poor men were around 1940 and 1950, which made it relatively easy for men around 1970 and 1980 to exceed those incomes. Marriage rates were high and single parenthood rare in the 1940s and 1950s. Further, it is difficult to imagine that young women in 1979 looked at men who were 70 percent richer than the previous generation of young men had been and found them wanting because they were not 260 percent richer (as was the case for young men ten years earlier). And the ratio of medians was about the same in 2018 as in 1989, though marriage kept falling during this period, and single parenthood kept rising.

Another possible threshold for marriageability is that a husband should make sufficiently more than his would-be wife. Figure 16 shows the trend in the ratio of two hourly pay medians—that of non-Hispanic men ages 25 to 29, and that of non-Hispanic women in the same age range.[68] In both 1973 and 1980, the male median was 40 percent higher than the female median, but the ratio dropped fairly steadily from 1980 through 1995. In both 1995 and 2019, men had an 11 to 12 percent advantage over women. That stability, while family instability continued to rise, weakens the case that marriageability is about what men make relative to women.

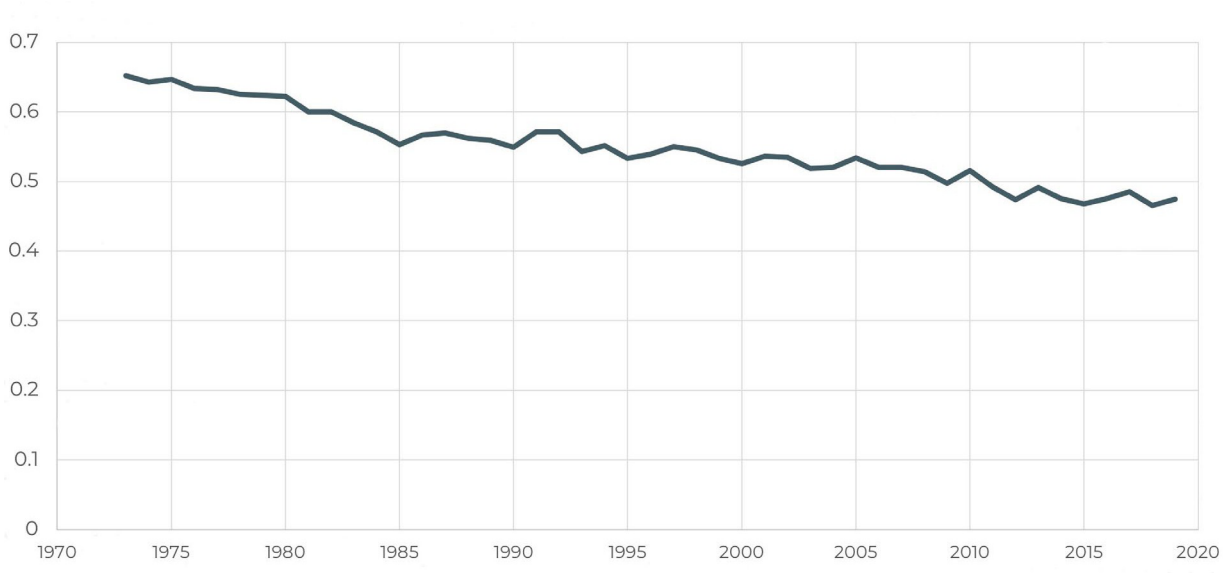
Figure 16. Ratio of Male-to-Female Hourly Pay, Non-Hispanics Ages 25-29, 1973-2019




Source: Social Capital Project analyses of Current Population Survey data. See end note 56.

Income inequality has become a focus of many public commentators and policymakers in recent years both generally and specifically in regards to its effect on marriage.[69] If marriageability thresholds for men in the bottom half of the distribution are tied to what upper-middle-class men make, then fewer suchmen have been marriageable over time. (See Figure 17.) In 1973, the median pay of non-Hispanic men in their late 20s was 65 percent the pay of the 90$^{th}$ percentile of such men. By 2019, it was only 47 to 48 percent. Unlike the other trends examined, this trend is more or less continuous over the period. However, given that the median is no lower today than in 1973, it reflects the rise of pay higher up. It is unclear why the potential wives of men in the bottom half of the pay distribution would be more likely to marry someone in 1973 than in 2019 just because upper-middle-class men were doing a lot better by 2019.

Figure 17. Ratio of 90th Percentile to Median Hourly Pay, Non-Hispanic Men Ages 25-29, 1973-2019




Source: Social Capital Project analyses of Current Population Survey data. See end note 56.

The evidence, then, suggests that men are no less marriageable by the most straightforward metrics than they ever were. Analyses that suggest otherwise tend to suffer from one of two serious mistakes. Many show trends in hourly wages or annual earnings by educational attainment rather than for different percentiles.[70] Since educational attainment has risen over time, trends among men with, for example, no more than a high school diploma will compare a larger group of men in 1973 to a smaller group of men with lower skills today. That results in a downward pull on the trend in pay that reflects nothing more than an apples-to-oranges comparison between a relatively advantaged group and a relatively disadvantaged group. It is like comparing today's 10th percentile to the 40th percentile fifty years ago. Other studies use estimates that overstate the extent to which inflation has eaten into rising income.[71] Many analyses makeboth of these errors.

It should not be surprising that the marriageable men hypothesis is too simplistic to explain the decline in family stability. The United States has experienced dire economic circumstances, such as the Great Depression, without the kind of family change that the country has experienced over the past 50 to 60 years.[72] Even if the hypothesis is held to apply asymmetrically to the 1970s, 1980s, and early 1990s, the fact that rising male pay since the early 1990s has not translated into a reversal of family decline should give pause to policymakers who would seek to revitalize the family through economic means. (And again, the earlier decline in "marriageability" may have been a reflection of weakened incentives to marry rather than the effect of changing economic opportunities among men.)

*An Alternative Hypothesis: Affluence Diminishes Social Capital*

In contrast to the marriageable men hypothesis, which is premised on worsening economic conditions, the Social Capital Project has argued that rising family instability is actually a byproduct of the nation becoming richer.As discussed in our flagship report, ***What We Do Together***, a wide variety of indicators suggest that "associational life" in America has withered over the past half century.[73] We do less together, with our neighbors, our coworkers, and other members of our local communities. Family connections have also become more frayed. In doing less together over time, the stock of valuable social capital available to us has diminished.

***What We Do Together*** argued that declines in our associational life, including family decline, are the consequence of rising affluence. Americans can afford to satisfy more of their needs through paid services and commercial insurance. The ability to save and opportunities to insure risks and smooth income have increased. There is less need to rely on grandparents for child care or neighbors for help with ambitious projects or churches and unions for financial support in hard times. And in material terms, it has become less important to have a spouse, a co-parent, or in-laws.

Affluence also led to Americans aiming higher up Maslow's hierarchyof needs.[74] Earlier generations did not have the luxury of taking their basic material needs for granted. Today, however, Americans can devote considerable attention to self-fulfillment, privacy, and individualist pursuits.[75] Relationships, including marriages, became more about the satisfaction gained by the parties involved and less about broader societal obligations.[76] As Americans have become wealthier, the opportunities for self-fulfillment have proliferated: education, career, dating, hobbies, and travel, to name a few. Marriage and childrearing must compete with these alternatives, which has proved difficult as the transition to adulthood has extended into the twentysomething years.[77] Advances in personal technology have made it easy to substitute pornography or no-strings dating for sexual gratification within marriage (or even within committed nonmarital relationships).[78]

This emphasis on self-fulfillment was a driving factor behind expanded professional pursuits for women, which was also facilitated by advances such as cheaper home appliances and processed food and the ability to afford child care (to say nothing of the development of more effective birth control). For well-educated women, the opportunity cost of getting married too soon or to the wrong person or of having children became magnified. Marriage and fertility rates fell correspondingly.

The new birth control methods, along with legalized abortion, also undermined the view that nonmarital sex was wrong and to be avoided.[79]In a more general sense, by reducing the consequences of risky choices, affluence eroded support for moral constraints that impeded the self-realization and freedom of well-off Americans who could manage risk well. Rising opportunities for well-educated single women made single parenthoodless financially disastrous for them. More women could afford divorce, and that reduced the stigma surrounding it. Increased demand for divorce led to liberalized divorce law, making the trend self-reinforcing.[80]

Affluence was also behind the increased purchasing power of the young baby boomers, spawning the counter-cultural changes in 1960s and 1970s music and fashion.[81] Those changes further eroded traditional moral codes. Scientific discoveries and rising economic security also contributed to secularism's advances, undermining traditional morality and weakening involvement with religious institutions.

If American declines in family life and associational life more generally were caused by affluence, then there is a paradox requiring explanation: why does associational and family life remain stronger today among the well-off than the worse-off?[82]

Even in 1960, family instability was more common among lower-income Americans than upper-income Americans. The opportunity cost of an unwed birth has been and remains lower for disadvantaged women than for advantaged women in the sense that, for them, an unwed birth does notas often mean the delay or forfeiture of education or career goals. That can weaken vigilance about avoiding unwed pregnancies.[83] Also, for women whose lives are chaotic and unstable, motherhood, even without a stable relationship,may add a great deal of meaning to their lives.[84] For some couples, the same sorts of personal challenges that lead to employment problems can also produce relationship problems. For others, the stresses of poverty exacerbate the usual relationship challenges common to all couples.

But rising affluence has also affected the associational and family life of those with greater and fewer resources differently. Among the relatively advantaged, private safety nets have remained strong and have even grown stronger. The incomes of men and women have both increased significantly, and individuals looking around at their extended families, friends, and neighbors have seen the incomes of those in their networks rising as well. Professional opportunitieshave expanded, especially for skilled women.

With stronger private safety nets, well-off men and women have been able to relax their commitment to inconvenient moral constraints. However, these moral constraints have historically served to protect the more vulnerable of society, who are less well-positioned to manage risk, from the consequences of unwed childbearing, divorce, and single parenthood. Affluence and individualism also weakened the attachment of the well-off to institutions and to neighbors.

Lowered commitment on the part of the well-off to moral constraints and institutions has had implications for less advantaged men and women, however. Without buy-in and enforcement from the well-off, commitment tomoral constraints such as delaying sexual activity until marriage weakened among the vulnerable too, but with greater consequences. Since the poor have less of a financial stake in marriage, moral codes and cultural norms were always more important for enforcing marital stability among the disadvantaged than among the advantaged.[85]

With reduced participation in and funding of institutions by those with resources, those institutions became less able to serve the vulnerable (who wereusually even less likely than the advantaged to participate in those institutions). Rising economic segregation also meant that whatever moral or institutional leadership might have been provided by the well-off followed them to enclaves often far removed from the social worlds of the less well-off.[86] The church pews remained fuller in more affluent communities than elsewhere, but those communities were ever further from the disadvantaged Americans who needed them.[87] Regardless, greater individualism made the have nots less interested in what the haves thought about their choices anyway.

Traditional moral guardrails, thus, became less effective as protective barriers against calamity among Americans with fewer resources. While the well-off could manage the greater risks of, say, nonmarital sex adequately, many other people could not. Incorrect or inconsistent use of contraception produced many more nonmarital pregnancies among them than among either well-off Americans or the worse-off Americans of earlier generations (who were more tightly bound by taboos against nonmarital sex). The availability of birthcontrol and abortion reduced pressure on men to enter shotgun marriages orprovide child support, since they could argue, conveniently, that childbearing was a woman's "choice."[88] Increased nonmarital births and declining expectations of marriage became more common and self-reinforcing.

Institutional decline, the breakdown of traditional morality, and economic segregation (concentrating the stresses and challenges of poverty) sowed distrust among less advantaged Americans. That distrust extended to relationships between men and women, exacerbating the decline in marriage in impoverished communities.[89] The result has been the paradox of rising affluence weakening the families and associational life of Americans across the socioeconomic spectrum, but doing more damage among the least affluent.

*The Role of the Expanding Public Safety Net*

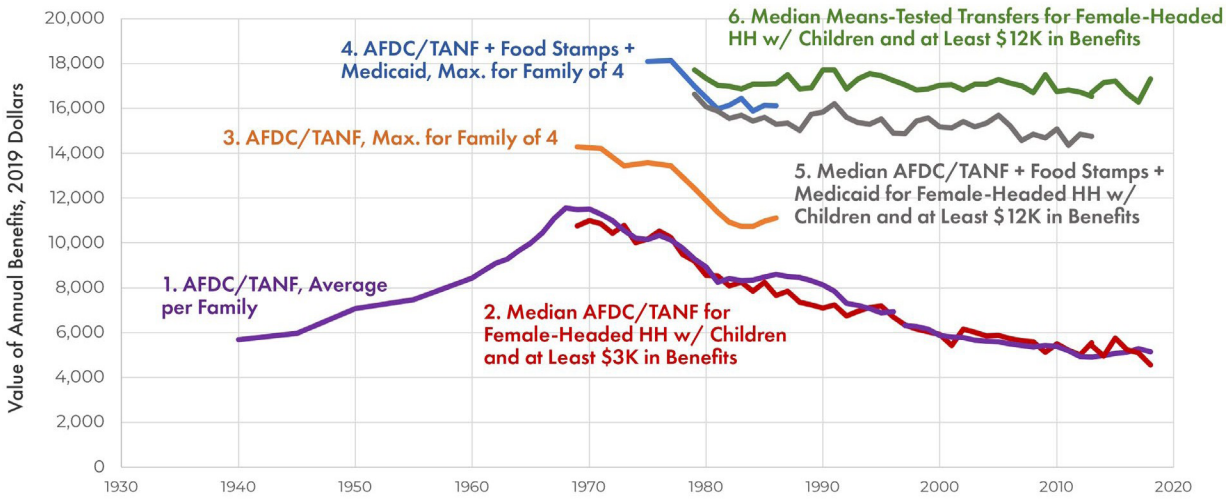
Another effect of rising societal affluence was the replacement of private safety nets with a public one. An affluent and non-judgmental polity sought to mitigate the greater risk caused by weakened institutions by substitutingan expanded public safety net at the federal level. But public "anti-poverty" programs often exacerbated the problem of family instability by making single parenthood a more viable option and by discouraging marriage among those receiving benefits.

Ever since Charles Murray's landmark 1984 volume, Losing Ground, critics of the safety net have warned that antipoverty policy might promote single parenthood.[90] A safety net marginally reduces the costs of single parenthood, nonmarital childbearing, and divorce. It also can create a significant tax on marriage because the addition of a spouse with income typically reduces safety net benefits, and if he has only modest earnings or unsteady employment, the trade-off may not be worthwhile. The evidence on this question—as for so many of the important empirical questions discussed in this report—has proven elusive. Most of it has focused on changes in the primary cash transfer programs available to single mothers—Aid to Families with Dependent Children (AFDC) and its successor, Temporary Assistance for Needy Families (TANF).[91] Single parenthood continued to increase in the 1970s and beyond, even though the inflation-adjusted value of AFDC and TANF benefits fell significantly.

But the means-tested welfare system consists of more than 80 programs that provide cash, food, housing, medical care, and social services to poor and lower-income Americans.[92] Most all of these programs penalize marriage, suchthat when household income increases, welfare benefits decrease.[93] The AFDCand TANF research is inadequate for assessing whether the expansion of the entire safety net over time has affected trends in family instability.

In Figure 18, Line 1 shows changes in the average value of AFDC and TANF over time.[94] The monthly AFDC benefit (shown in the chart annualized by multiplying it by 12) peaked in 1968 in inflation-adjusted terms. It fell steadily thereafter, eventually settling under TANF at less than half its high point andlower than in 1940. Line 2 reinforces this conclusion with a different measure from a different source, showing from 1969 to 2018 the annual amount actually received by the median female-headed household with children, among those who received at least $3,000 in benefits (in 2019 dollars).[95] The two trends align remarkably well.

Figure 18. Annual Value of Federal Benefits Available to a Female-Headed Household, 1940-2018




Source: Social Capital Project analyses of various sources. See end notes 94-98.

But while cash transfers to single-parent families became less generous after 1968, the overall benefits on offer to them continued to increase sharply. The food stamp program grew steadily, especially after an expansion in 1971. Medicaid was enacted in 1965 and expanded thereafter. Figure 18 also shows the trend from 1969 to 1986 in the maximum AFDC benefit for a family of four (Line 3) and from 1975 to 1986 in the maximum total benefit from AFDC, food stamps, and Medicaid for a family of four (Line 4).[96] Comparing Lines 1 and 3 shows that the maximum AFDC benefit for a family of four follows the same trend as the average AFDC benefit for all families over the years in which bothare available. We will use this similarity in the next chart to extend Line 3 back to 1940.

Comparing Line 3 to Line 4 shows how much more valuable food stamps and Medicaid are over and above AFDC. Again, the trends for the two lines are similar.

Line 5 comes from the annual benefit data used in Line 2. It reassuringly suggests that we can extend Line 4 into the recent past. Line 5 provides, from 1979 to 2013, the median value of the annual sum of benefits from AFDC or TANF, food stamps, and Medicaid among female-headed households with children who received at least $12,000 in combined benefits.[97] The levels line up reasonably well over the years they have in common from 1979 to 1986, but moreimportantly, the trends do. Taken together, Lines 4 and 5 suggest the same long-term decline in the value of means-tested benefits available to single-mother families that Lines 1 and 2 imply, but from a much higher late-1960s peak.

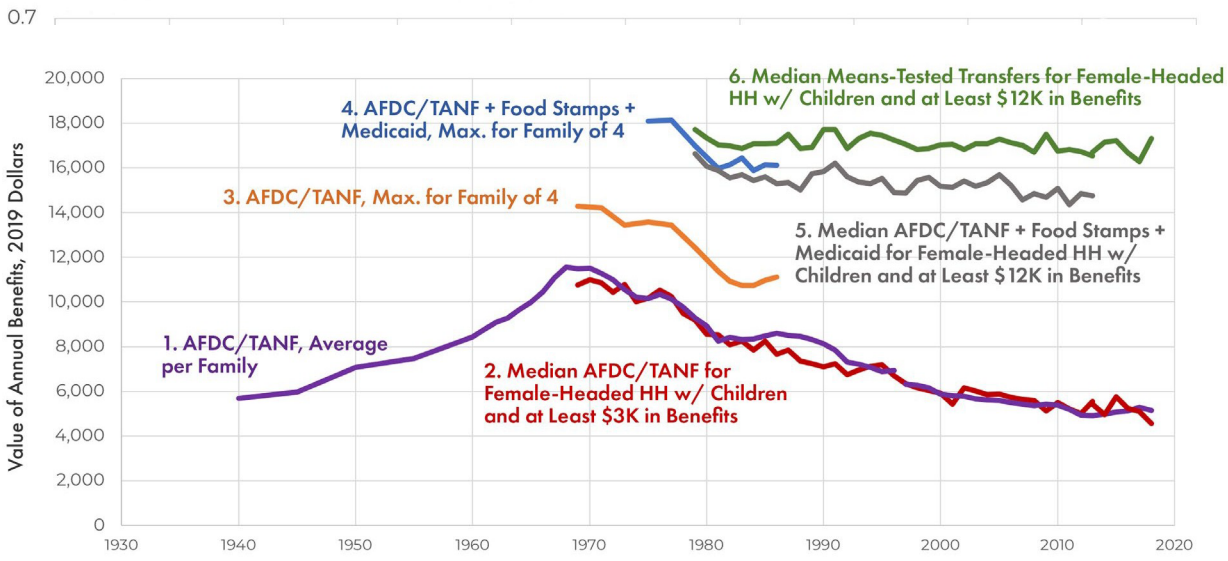
Finally, Line 6 takes other safety-net benefits into account, from 1979 to 2018. It again shows the annual median among female-headed households with children that have at least $12,000 in total benefits, but this time it includes a variety of other cash and noncash means-tested benefits.[98] This comprehensive measure declines less than the other measures.

Using the information in Figure 18, we can create a rough long-term trend in the value of federal safety-net benefits. While we lack earlier estimates for benefits other than AFDC, few were available in 1965. Medicaid had just been enacted, while the food stamp program was much smaller than it was after the 1971 expansion. The program extended nationwide only in 1974, and until 1977, beneficiaries had to purchase food stamps. The Supplemental Security Income (SSI) program began in 1974. Other programs were generally small or non-existent in 1965.

Lines 3 and 4 are directly comparable measures in principle, both relating to maximum benefits for a family of four. Since Lines 1 and 3 follow the same trend during the years in which both are available, we use the pre-1969 trend for Line 1 to extrapolate Line 3 back to 1940. Next, we connect the extrapolated1965 estimate for Line 3 to the 1975 estimate for Line 4. Finally, we extrapolate Line 4 from 1979 to 2018 using the trend for Line 6.

Figure 19 shows the resulting line, which we use as a rough but realistic representation of the increase in safety net benefit generosity over the past 80 years. Since the amounts underlying the figure represent different concepts, we set the 1940 estimate at 100 and index other years to it. Figure 19 reveals a sharp rise in the value of federal safety net benefits over time, which is obscured by focusing on the trend in AFDC and TANF. The value of the safety net for single-mother families is 133 percent higher today than in 1940, and 56 percent higher than in 1960.

Figure 19. Annual Value of Federal Benefits Available to a Female-Headed Household vs. NonmaritalBirth Rate, 1940-2018




Source: Social Capital Project analyses of various sources. See end notes 94-98.

The other line in Figure 19 indicates that the nonmarital birth rate has roughly doubled since 1960. The rate rose steadily into the early 1990s and remained high thereafter (with a temporary spike prior to the Great Recession).[99] The increase in nonmarital births lags the increase in benefits by roughly 15 to 20 years between 1975 and 1990.

All else equal, more than doubling the standard of living achievable from the federal safety net would be expected to encourage more women to choose single parenthood over marriage. Between 1979 and 2013, we estimate that the 30th percentile of young non-Hispanic men's annual compensation was,on average 48 percent higher than the typical safety net benefit package received by single mothers. Through the safety net alone, a single mother can achieve about two-thirds of the standard of living she could get from marryinga sole breadwinner at that compensation level. The safety net would put her about one-third higher, with no additional income, than the 10th percentile of male compensation.[100]

To be clear, the claim is not that single mothers can achieve affluence relying on the safety net. Their economic circumstances are challenging and would be difficult to navigate for most middle-class Americans. But the affluence of the nation has afforded a safety net that has reduced poverty significantly for single mothers and their families. At the margin, more women are able to substitute federal benefits for the income a husband would have provided them in the past.

These estimates are necessarily rough. Much work remains in sorting out and apportioning blame for the decline in family stability and its disproportionate impact on the disadvantaged. Economic insecurity and instability may have an important role. But the case for what might be called the "culture of affluence" has been unduly neglected relative to accounts that overstate the decline in men's economic standing. One aspect of this culture is that childbearing is said to be the choice of the mother, and thus fathers bear less responsibility for their children. Another is a federal safety net that not only makes it more possible for a woman to raise a child without a father but also encourages couples to remainunmarried. The combination is a troublesome mix for family stability.

Because any understanding of why family stability has declined must be incomplete and tentative, it is worth considering a range of policy options to reverse this decline.

## STRENGTHENING FAMILY STABILITY

How to address the decline in family stability and its unequal consequences across different groups? Paternalists and libertarians will disagree as to whether it is appropriate for policy to encourage or discourage some behaviors over others. Liberals and conservatives will vary in their position toward hot-button cultural issues such as family planning. Apart from moral considerations, there is the practical question of whether policies are effective in reducing nonmarital pregnancies, encouraging marriage, or reducing divorce. This section discusses four broad strategies that might be pursued in order to increase the likelihood that children are raised by happily married parents. Those strategies include messaging, social programs, financial incentives, and other policies.

### *Messaging*

One strategy policymakers and private actors can pursue is to amplify messages that advance the goal of family stability. Such efforts might involveformal public or private media campaigns or more informal shifts in public discourse and rhetoric.

Previous media campaigns related to family stability have commonly targeted the issue of teenage pregnancy. For example, in 2013, New York City launched a public education campaign directed at teen pregnancy, with advertisements posted in subways and bus stops throughout the city. The campaign aimed to deliver strong messages based on provocative data points about the potential consequences of teen pregnancy.[101] Media campaigns might also be usefully organized around other messages related to family stability, such as the riskiness of too-close work relationships or pornography consumption.

Media campaigns often may be constructively organized as public-private partnerships. The private National Campaign to Prevent Teen and Unplanned Pregnancy, worked with states and localities to develop messaging, resulting in government-sponsored media campaigns in a number of states.[102] As another example outside the issue of family stability, the U.S. anti-smoking campaign was led by the federal government, but private groups such as the Heart Association produced advertisements across various media.[103]

Other private efforts can also convey messages conducive to family stability. The popular reality television shows ***16 and Pregnant*** and the ***Teen Mom*** spin-offs—which follow pregnant young women through their pregnancies, births, and experiences as new mothers—were not created intentionally as part of a campaign against teen pregnancy. But they may have effectively served that purpose. In particular, ***16 and Pregnant***, which aired from 2009 to 2014 and was highly popular among American teenagers, may have resulted in a significant decline in teen births—a decrease of 4.3 percent between mid-2009 through 2010.[104]

The example of *16 and Pregnant* highlights the potential role of cultural messages in changing behavior. Toward this end, politicians, celebrities, and other influential people should use the "bully pulpit" to communicate messages that promote family stability. Then-Senator Barack Obama's 2008Father's Day speech, in which he highlighted the importance of present fathers, serves as a praiseworthy model.[105]

In this regard, it is unfortunate that while highly educated Americans are more likely to have stable marriages and to have children within those marriages, they too often demonstrate an "unwillingness...to preach what they practice."106 One recent report showed that well-educated Californianspersonally embrace values and practices that are more conducive to family stability, but at the same time they are more ideologically permissive than less-educated Californians in their attitudes about families.107 While oftenwell intentioned, the current reluctance among members of the upper class to "talk the walk" actually does a disservice to those who could benefit from hearing constructive messages about stable families.

What is more, the increasing segregation of upper- and upper-middle- class Americans from their less-advantaged counterparts translates into a diminished ability to demonstrate and communicate the importance of choices that promote family stability to those who would benefit from their example.108 And even if residential segregation were not a problem, advocating for choices to promote family stability is fraught with discomfort. Critics of the New York City campaign, for example, alleged that it stigmatized teenage parents.109 So much trickier is advocacy when it must draw on the meager "bridging" social capital remaining after decades of increasing social separation by class.

### *Social Programs*

Another way to increase family stability is to help people develop the skills and knowledge necessary to prepare for, build, and maintain healthy marriages and families. Programs that aim to change behavior by providing such instruction include healthy marriage and relationship education (HMRE) programs, fatherhood programs, and programs that focus on teen pregnancy prevention.

There are a variety of HMRE programs for individuals and couples at various life and relationship stages. The federal Healthy Marriage and Relationship Education Initiative provides competitive grants to states for such programs. In addition, all states receive funding from the Temporary Assistance for Needy Families program that can be used for HMRE programs, though few states allocate funds for such efforts.[110] The aims of such programs include improving conflict resolution skills, co-parenting strategies, relationship satisfaction, marital commitment, and other outcomes.

Programs designed to change behavior often fail to have significant impacts, and many critics have argued that programs funded by the Healthy Marriage and Relationship Education Initiative are ineffective.[111] Evaluations of some of the earliest federally-funded HMRE programs showed few promising results, with programs that were targeted to unwed parents particularly ineffective.[112]A more recent evaluation of two HMRE programs showed modestly positive results, however.[113] Research indicates that programs directed to married couples appear to be more effective than those aimed at unwed parents.[114] Overall, the broader literature evaluating healthy marriage and relationship education is mixed but shows that these programs can have modest effects on relationship quality and sometimes on relationship stability, even among disadvantaged participants.[115]

A handful of states have utilized their own funding for HMRE programs. Some states have implemented healthy marriage initiatives that focus on making marriage education widely available. Utah and Oklahoma have operated the most ambitious of these initiatives.[116] Some states have pursued premarital education promotion policies, in which states provide a financial incentive to engaged couples to participate in premarital education.[117] Finally, a few states have proposed or implemented policies that require couples filing for divorce to participate in divorce orientation education as a prerequisite to divorce.[118]

At a more local level, some communities have healthy marriage initiatives that aim to make healthy marriage and relationship education widely available.[119] There are also private faith-based efforts to provide marriage education. Communio is a faith-based community marriage education effort that supports churches in fostering "strong communities by focusing on building relationship ministries that grow and support healthy marriages and strong families."[120] In Jacksonville, Florida—one of the cities receiving funding, where nearly100 churches and local organizations have been involved—divorce declinedmarkedly over the first two years of the initiative, although it has not been rigorously evaluated.[121]

In addition to HMRE programs, the federal government also funds education programs that promote responsible fatherhood. A 2018 evaluation of four such programs, found a few small effects on fathers' outcomes, but mostly confinedto one of the four locations. These outcomes included participation with children, nurturing behaviors toward them, knowledge of the child support system, employment status, and reported financial well-being.[122] For most outcomes measured, however, there were not significant differences between those who participated in the program and those who did not.

A third category of social programs aimed at increasing family stability are those that focus on teen pregnancy prevention. Although only a small portion—11 percent—of unwed births annually are to teenage young women, teen births are nearly always to unwed mothers.[123] And nearly one in four unmarried first births are to young women under 20 years of age.[124] The federal government has supported programs to prevent teen pregnancy since the 1980s. Some of this funding is directed specifically towards sexual risk avoidance education (also known as abstinence education), which is based on the principle that sexual abstinence is the only acceptable standard for high school-age youth.[125] Comprehensive sex education does not necessarily take a position on whether youth should abstain from sexual activity in high school and focuses more on contraception.[126]

There is a great deal of controversy surrounding this type of education, and states and school districts have varying requirements for sexuality education curricula.[127] Some sexual risk avoidance programs and comprehensive sex education programs seem to have modest effects on teen sexual activity and pregnancy rates, but most have been found ineffective.[128]

*Financial Incentives*

Given the generally disappointing performance of social programs, a more effective way to increase family stability may be to provide clear financial incentives. Opportunities along these lines include safety net reforms to reduce marriage penalties and otherwise discourage family instability, providing additional tax benefits for married couples, and strengthening childsupport enforcement.

The U.S. safety net consists of many programs providing cash, food, housing, medical care, and social services to low-income Americans. By reducing the cost of single parenthood, more generous safety net programs may incentivizeit. Reforms to those programs taking the form of time limits or work requirements could reduce single parenthood by making these programs relatively less appealing.

Another way to express how safety net programs affect marriage is to note that nearly all of them contain marriage penalties, or incentives that deter marriage.[129] Because benefits generally decline as household income increases, and because marriage usually increases household income, low-income parents who marry often stand to lose safety net benefits. One possible solution is to increase programs' income limits, though doing so would further undermine work incentives and greatly increase the safety net's scope and cost, which is already roughly $1 trillion annually.[130] Alternatively, safety net policy could disregard spousal earnings more generously when determining eligibility for benefits. But that, too, could encourage more peopleto rely on the safety net. Once again, pairing work requirements or time limits with greater generosity toward married parents in safety net programs would mitigate these downsides.

Two other reforms that were part of the landmark 1996 welfare overhaul are also relevant. States were given the option to implement "family caps," which limit the availability of higher benefits when additional children are born. About a dozen studies of this state option and of state experiments before 1996 produced mixed evidence on their effects, however.[131] The welfare reform legislation also required teenage recipients to live with a responsible adult and attend school. The so-called "minor parent provision" appears to have reduced teen childbearing and could be extended to other safety net programs to further discourage teen births.[132]

Alternatively, safety net program work requirements could be adjusted for married couples where they currently exist, particularly where time limits already mitigate the risk of long-term benefit receipt. For example, married parents receiving benefits from the Temporary Assistance for Needy Families (TANF) program currently are required to work more hours than single-parent families to fulfill the program's work requirement. The Welfare Reform and Upward Mobility Act, sponsored by Joint Economic Committee Chairman MikeLee in previous Congresses, proposed eliminating this marriage penalty by making the required hours of work the same for married-parent families and for single-parent families.[133]

The Earned Income Tax Credit (EITC) is one of the largest cash assistance safety net programs, costing almost $60 billion in fiscal year 2018.[134] It has separate benefit schedules for single and married tax filers. The schedules for married couples could be made more generous to address the existing marriage penalties within the EITC that cause benefits to be lower when many couples are married than when they are single.[135] (Though, some lower-earning couples receive a higher EITC when married than when single.)

Policymakers could also consider introducing tax benefits that would resemble marriage bonuses but could be justified on tax-neutral grounds.[136] For example, EITC benefits for married couples could be expanded significantly more than is necessary to rectify within-EITC marriage penalties. That might be justified on the grounds that it would mitigate marriage penalties in other means-tested safety net programs, encouraging people to marry by offsetting the loss of benefits from these programs.

Similarly, the Child Tax Credit (CTC), which reduces tax liability for parents, could be expanded for married couples.[137] Since the CTC only goes to families with earnings, it too mitigates marriage penalties in safety net programs by mitigating the loss of means-tested benefits when someone marries a workingspouse. Alternatively, an expansion could be justified on the grounds that parents are unfairly double taxed.[138] Parents who raise children are effectively taxed twice to support senior entitlements—once through payroll taxes, like everyone else, but again through the cost of raising the children whose payroll taxes will continue supporting the system. To combat this "parent tax penalty," Joint Economic Committee Chairman Mike Lee has advocated the expansion of the CTC, a goal partially fulfilled by provisions in the Tax Cuts and Jobs Act of 2017. The parent tax

penalty is imposed on a single parent raising her child alone, but it is imposed on both parents in a married couple, both of whom bear the costs of childrearing.[139] This "triple tax" merits a higher CTC for married couples.

A final way of supporting family stability through financial incentives is to strengthen child support enforcement. Stronger child support enforcement would make unwed and noncustodial fatherhood less attractive to men, and thus could decrease the likelihood that a man fathers a child outside of marriage or leaves his wife. However, stronger child support enforcement may increase a mother's willingness to have a child outside of marriage or divorce.[140]

In terms of nonmarital childbearing, child support enforcement's disincentivizing effect on men seems to be stronger than the incentivizing effect on women. Child support enforcement also appears to reduce the likelihood men will have children with multiple partners.[141] However, stronger child support enforcement appears to decrease the likelihood unwed parents marry and increases the likelihood that a mother will have another non-maritalbirth with another partner.[142]

*Other Policies*

Policy approaches that are not explicitly designed to boost marriage or reduce unwed childbearing could also hold promise for increasing family stability. These policies generally try to mitigate obstacles that might prevent families from staying together or being formed in the first place.

One such approach is aimed at improving career prospects for younger Americans, especially young men. As we have seen, the evidence is unclear as to whether male marriageability is an important explanation for rising family instability. Regardless, many Americans clearly view financial security as a prerequisite for getting married or having children.[143] Social Capital Project research has found that men who are not in the labor force tend to have unstable families; they are less likely to be married but more likely to have children with multiple partners.[144] Therefore, efforts to improve economic opportunities could help people meet their expectations regarding work and marriage, could make men more attractive as potential partners and fathers, and thus may lead to greater family stability.

As is generally the case, successful interventions are often disappointingly rare, and the same is true of programs that might be expected to increase male marriageability. But at least one model merits serious consideration based on rigorous evidence. Career Academies are small learning communities established within urban high schools that combine academic, career, and technical education organized around specific career themes. They are intentionally integrated with local employers to provide work-based learning opportunities in fields with demonstrated local demand. Though not designed to directly improve marital and family outcomes, a randomized evaluation of

Career Academies found that participants were significantly more likely than non-participants to be married and living independently with a partner and children eight years after high school graduation.[145]

Another policy approach to increasing family stability involves reforms to state divorce laws. The legal regime of no-fault divorce played a role in the divorce revolution of the 1960s and 1970s.[146] Divorce rates have declined since then, but as shown above, that largely reflects the aging of the population into life stages with relatively low divorce risk. Reforms to state divorce laws—such as requiring classes or extended waiting periods for divorcing couples (with exceptions for cases of domestic violence)—could encourage spousal reconciliation and increase family stability.[147] Policy changes that make divorce harder to obtain, however, could discourage entry into marriage as well.[148]

Another potential contributor to family instability is pornography. Although the effects of pornography on developing minds or romantic relationships have not been studied in great depth, the balance of longitudinal research shows a negative correlation between pornography use and relationship quality and stability.[149] Considering the proliferation of pornography access, including among youth, policymakers and the public should at least have a better understanding of its potential adverse effects. To that end, Congress could fund a comprehensive study that examines the effects of pornography use onhuman development and relationship health, particularly among youth.

A final set of policies is focused not on single parenthood or divorce but on placing children removed from neglectful or abusive homes into stable, healthy family situations. Unfortunately, children often languish in the current foster care system.[150] There were 437,283 children in the foster care system at the end of fiscal year 2018—the first year of decline in the foster care caseload since it began rising in fiscal year 2012.[151]

Despite the need to move these children into stable homes, federal and state policies all too often inhibit this process. States should take care to ensure that their legal systems are efficiently moving foster children into stable homes instead of delaying this process, as sometimes is the case. In addition, while faith-based organizations have provided foster care and adoption services throughout the nation's history, some, such as Catholic Charities of Boston, havehad to close down due to state laws that discriminate against their religious beliefs. State policymakers should remove these and other unnecessary regulations that restrict the supply of foster and adoptive parents. At the federallevel, JEC Chairman Mike Lee introduced the First Amendment Defense Act in 2018, which would prohibit the federal government from discriminating against individuals and groups based on their beliefs about marriage. Senator Michael Enzi and Representative Mike Kelly introduced the Child Welfare Provider Inclusion Act in 2019, which would prohibit states that receive federal Title IV foster care funding from discriminating against foster care and adoption providers based on their religious or moral beliefs about marriage.[152]

## CONCLUSION

The Social Capital Project has documented the myriad ways in which associational life has deteriorated over the past fifty years. Nowhere is this decline more worrisome than in the realm of family stability. Relationships have becomethinner and more fragile in many aspects of life, and the value of the social capitalavailable to us has diminished as a result. But for children, there is no substitute for the benefits that come from strong family bonds.

Unfortunately, family instability has increased to the point where it is the norm for many Americans today. Troublingly, those most likely to experience family disconnection are the least-advantaged among us. While family instability does not necessarily doom a child to poorer life outcomes, it often means greater disconnection in the most intimate of human relationships and less social capitalof the strongest type.

Changing the course of family stability will likely require substantial effort, giventhe magnitude of the challenge in many American communities today and the pervasiveness of the decline. Compounding matters, our understanding of what got us here is woefully incomplete. It should be no surprise, then, that policymakers have yet to find a way to reverse the troublesome trends documented in this report. Until we get a better sense of what has caused family breakdown to worsen and of what policies are effective at reversing breakdown, policymakers will need to experiment with a variety of approaches. Toward the end of strengthening families—the source of so much potential happiness or sadness in our lives—Americans of all backgrounds and perspectives must cometogether and make headway on this most important modern-day problem.

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29. U.S. Department of Health and Human Services, Centers for Disease Control and Prevention, National Center for Health Statistics, Nonmarital Childbearing in the United States, 1940-99 *National Vital Statistics Reports* 48, by Stephanie J. Ventura and Christine A. Bacharach, October 18, 2000, "Number, rate, and percent of births to unmarried women and birth rate for married women: United States, 1940–99," Table 1, accessed May 1, 2017, https://www.cdc.gov/ nchs/data/nvsr/nvsr48/nvs48_16.pdf; U.S. Department of Health and Human Services, Centers for Disease Control and Prevention, National Center for Health Statistics, *Births: Final Data for 2018 National Vital Statistics Reports* 68, by Joyce A. Martin et al., accessed January 13, 2020, https://www.cdc.gov/nchs/data/nvsr/nvsr68/nvsr68_13-508.pdf.

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30. Social Capital Project, Joint Economic Committee, "Love, Marriage, and the Baby Carriage: The Rise of Unwed Childbearing," December 11, 2017, https://www.jec.

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31. Ibid.
32. Cynthia Osborn and Sara McLanahan, "Partnership Instability and Child Well-Being," *Journalof Marriage and Family* 69, no. 4(November 2007): 1065-1083.
33. Social Capital Project analyses of Census Bureau data. Historical Living Arrangements of Children, Tables CH-1, CH-5, and CH-6, accessed January 23, 2020, https://www.census.gov/ data/tables/time-series/demo/families/children.html.
34. The Current Population Survey changed in 2007 to better identify both parents in a household, creating a noticeable discontinuity in Figure 7. Because families were simpler in 1970, comparing the 1970 and 2019 estimates is probably unproblematic. But the steepness of the increase between 1970 and 2007 shown in the chart probably overstates the increase in the share of children living without a parent by a small amount, because families became more complicated and it became more difficult over time to identify parents.
35. The most recent published figures are for 2014 and indicate that 9 percent of children are living with a divorced single parent and 13 percent are living with a never-married parent.
36. U.S. Census Bureau, Department of Commerce, Economics and Statistics Administration, ***Multiple Partner Fertility Research Brief***, by Lindsay M. Monte, ***Current Population Reports***, March 2017, accessed April 16, 2019, https://www.census.gov/content/dam/Census/library/ publications/2017/demo/p70br-146.pdf.
37. Ibid.
38. To create the three education categories, we first estimated the distribution of educational attainment for women 15-44 during each year between the early 1960s and the present, using the Annual Social and Economic Supplement to the CPS. Then we defined three categories of educational attainment in each year, attempting to the extent possible to keep each group the same relative size. That is, "low education" in earlier years corresponds to fewer years of schooling than "low education" in more recent years, but roughly the same share of women is in this group every year. We then assigned women to one of the three categories based on her educational attainment.
39. Social Capital Project analyses of data from the Annual Social and Economic Supplement to the Current Population Survey, using the Integrated Public Use Microdata Series Online Data Analysis System. In 2019, "low" education for women ages 15-44 was defined as less than a high school degree (18 percent of women), "moderate" education for women ages 15-44 was defined as a high school degree or some college (49 percent of women), and "high" education for women ages 15-44 was defined as a bachelor's degree or higher (33 percent of women). In 1962, "low" education for women ages 15-44 was defined as less than a $10^{th}$ grade education (25 percent of women), "moderate" education for women ages 15-44 was defined as a $10^{th}$ grade education up to a high school degree (58 percent of women), and "high" education for women ages 15-44 was defined as more than a high school degree (17 percent of women).
40. In 2018, "low" education for women ages 15-44 was defined as less than a high school degree (18 percent of women), "moderate" education for women ages 15-44 was defined as a high school degree or some college (50 percent of women), and "high" education for women ages 15-44 was defined as a bachelor's degree or higher (32 percent of women). In 1970, "low" education for women ages 15-44 was

defined as less than a 10th grade education (19 percent of women), "moderate" education for women ages 15-44 was defined as a 10th grade education up to a high school degree (60 percent of women), and "high" education for women ages 15-44 was defined as more than a high school degree (21 percent of women).

41. Social Capital Project, Joint Economic Committee, "Rising Unwed Pregnancy and Childbearing across Educational and Racial Groups," February 14, 2018, https://www.jec.senate.gov/public/index.cfm/republicans/analysis?ID=A075A2E2-5CD0-406B-86B8- E44BB7A8FD6B.

42. Wendy Wang, "The link between a college education and a lasting marriage," Pew Research Center, December 4, 2015, accessed April 16, 2019, https://www.pewresearch.org/fact- tank/2015/12/04/education-and-marriage/.

43. Social Capital Project analyses of data from the Annual Social and Economic Supplement to the Current Population Survey, using the Integrated Public Use Microdata Series Online Data Analysis System, https://sda.cps.ipums.org/cgi-bin/sdaweb/hsda?harcsda+all_march_samples. (Flood et al., Integrated Public Use Microdata Series, Current Population Survey: Version 6.0, 2018.) Separated women are included as married.

44. Social Capital Project, Joint Economic Committee, "Rising Unwed Pregnancy and Childbearing across Educational and Racial Groups."

45. Wendy Wang, "The link between a college education and a lasting marriage," Pew Research Center, December 4, 2015, accessed April 16, 2019, https://www.pewresearch.org/fact- tank/2015/12/04/education-and-marriage/.

46. Social Capital Project analyses of Census Bureau data. Historical Living Arrangements of Children, Tables CH-2, CH-3, and CH-4, https://www.census.gov/data/tables/time-series/demo/ families/children.html.

47. William Julius Wilson and Kathryn M. Neckerman, "Poverty and Family Structure: The Widening Gap between Evidence and Public Policy Issues," in Sheldon H. Danziger and Daniel H. Weinberg eds., ***Fighting Poverty: What Works and What Doesn't*** (Cambridge, MA: Harvard University Press, 1986). See also William Julius Wilson, ***The Truly Disadvantaged: The Inner City,the Underclass, and Public Policy*** (Chicago: University of Chicago Press, 1987).

48. One study finds that for nonmarital births, the most important change has been a decline in shotgun marriage rather than a general decline in marriage that leaves a larger pool of single women at risk of pregnancy. See Paula England, Lawrence L. Wu, and Emily Fitzgibbons Shafer, "Cohort Trends in Premarital First Births: What Role for the Retreat from Marriage?" ***Demography*** 50(6): 2075-2104, 2013.

49. For reviews, see Daniel Schneider, Kristen Harknett, and Matthew Stimpson, "What Explains the Decline in First Marriage in the United States? Evidence from the Panel Study of Income Dynamics, 1969 to 2013," ***Journal of Marriage and the Family*** 80: 791-811, 2018 and David T. Ellwood and Christopher Jencks, "The Uneven Spread of Single-Parent Families: What Do We Know? Where Do We Look for Answers?" in Kathryn M. Neckerman, ed. ***Social Inequality*** (New York: Russell Sage Foundation, 2004).

50. One study that may successfully address this reverse causality problem exploits arguably exogenous geographic variation in male employment losses due to the impact of Chinese imports. It finds that where men's employment declined, marriage and fertility fell and single motherhood rose. David Autor, David Dorn, and Gordon Hanson, "When Work Disappears: Manufacturing Decline and the Falling Marriage Market Value of Young Men," ***AER: Insights*** 1(2): 161-178, 2019.

A second study that looks at exogenous changes in employment across geographic areas, however, finds that where men's wages rose due to the fracking boom, fertility rose but marriage did not become more common, so nonmarital births increased. Melissa S. Kearney and Riley Wilson, "Male Earnings, Marriageable Men, and Nonmarital Fertility: Evidence from the Fracking Boom," ***The Review of Economics and Statistics*** 100(4): 678-690, 2018.

51. Robert I. Lerman and W. Bradford Wilcox, "For Richer, For Poorer: How Family Structures Economic Success in America," American Enterprise Institute, 2014, https://www.aei.org/ research-products/report/for-richer-for-poorer-how-family-structures-economic-success-in- america/.

52. Ariel J. Binder, "Why Bother? The Effect of Declining Marriage Prospects on Employment of Young Men," unpublished paper, https://e9b0558e-7a7d-4b8e-a3c1-ed599eb209e5.filesusr. com/ugd/c393c3_05e158873a17488a928ec618cf49364a.pdf.

53. W. Bradford Wilcox and Nicholas H. Wolfinger, "Men & Marriage: Debunking the Ball and Chain Myth," Institute for Family Studies, 2017, https://ifstudies.org/ifs-admin/resources/men- and-marriage-research-brief.pdf.

54. Kate Antonovics and Robert Town, "Are All the Good Men Married? Uncovering the Sources of the Marital Wage Premium," ***American Economic Review*** 94(2): 317-21, 2004.

55. Ellwood and Jencks (2004), 7.

56. Social Capital Project analyses. The analyses begin with Current Population Survey data. For earlier years, these data come from the May Supplement for the years 1973 to 1978, andfrom the Outgoing Rotation Group files for 1979 to 1993, both from the Unicon Research Corporation. In more recent years, the CPS data are from the outgoing rotation groups in the Basic Monthly Survey files provided by the Minnesota Population Center at the University of Minnesota through their Integrated Public Use Microdata Series website at https://doi. org/10.18128/D030.V6.0. The samples have been modified to consistently include only private or government wage and salary workers (no self-employed business owners) who were employed (at work or absent from work during the survey week) and were in an outgoing rotation group. For workers who were paid by the hour, reported hourly pay is used. Where unavailable, hourly pay is estimated by dividing the usual weekly earnings before deductions by the usual number of hours worked, both for the worker's principal job. Our estimates were very similar to those independently estimated by the Economic Policy Institute from CPS data (Economic Policy Institute, State of Working America Data Library, "Median/average hourly wages," 2019 [updated February 20, 2020]).

    The hourly pay estimates are adjusted in three ways. First, we put them in constant 2019 dollars by adjusting them for inflation using the Personal Consumption Expenditures (PCE) deflator. (For the case for using the PCE deflator, see Appendix 2 of Scott Winship, "Poverty after Welfare Reform," Manhattan Institute, 2016, https://media4.manhattan-institute.org/ sites/default/files/R-SW-0816.pdf.) We then multiply them by a ratio that compares the sum of (1) wages and salaries and (2) employer fringe benefits to wages and salaries, using the aggregate figures for employees from the Bureau of Economic Analysis's National Income and Product Accounts (NIPA) Table 2.1 (lines 3 and 7). Employer contributions to government social insurance (employer payroll taxes) are not included. While these compensation figures are for workers in the aggregate, we apply them to the hourly wages at the $10^{th}$, $30^{th}$, and $50^{th}$ percentiles of young non-Hispanic men.

    The assumption that the aggregate ratio of compensation to wages is the same as the ratio at these percentiles (for the demographic group in which we are

interested) is only problematic for trends insofar as the extent to which this assumption is wrong varies over time. We compared our ratios for 1979 and for the year from 2009 to 2019 to two external sources that provided information about the ratios for different parts of the wage and salary distribution. For 1979 evidence, see Timothy Smeeding, "The Size Distribution of Wage and Nonwage Compensation: Employer Cost versus Employee Value," in Jack E. Triplett, ed. ***The Measurement of Labor Cost*** (Cambridge, MA: National Bureau of Economic Research, 1983). Smeeding shows, in Table 6.6, the share of wage and salary income accounted for by fringe benefits (nonwage compensation excluding legally required employer contributions, primarily toward government social insurance) for workers earning different amounts. For the lowest paid group (the bottom 15 percent), compensation was 4 percent higher than wages and salaries, and for the group that includes the median worker, compensation was 10 percent higher than wages and salaries. The adjustment we make assumes that compensation is 11 percent higher for the $10^{th}$ and $30^{th}$ percentiles and the median.

For 2009-to-2019 evidence, we turned to the Bureau of Labor Statistics Employer Costs for Employee Compensation tables at https://www.bls.gov/ncs/#tables, which allow one to compare fringe benefits (excluding legally required contributions) to wages and salaries at the $10^{th}$ percentile of compensation and the median compensation level. These ratios range from 11 to 12 percent for the $10^{th}$ percentile and from 34 to 37 percent at the median. The ratios we use range from 16 to 17 percent for both.

At the tenth percentile, then, our ratios have the effect of overstating compensation at the $10^{th}$ percentile, but by a similar amount in 1979 as in 2019. Thus, the trend should not be effected greatly (at least between 1979 and 2019). At the median, our 1979 estimate is likely to be accurate, but our 2019 compensation estimate is probably too low. Thus, our figures likely understate median wage growth. One caveat is that these external estimates of compensation-to-wages are for workers in the aggregate rather than for young non-Hispanic men. A second is that fringe benefits are valued at employers' costs, while employees might value these benefits differently than they would cash (more flexible but taxed). Smeeding estimates the distinction makes little difference in 1979.

The third adjustment to our estimates is to apply a tax rate in each year to bring them closer to take-home pay. To do this, we used the Annual Social and Economic Supplement to the Current Population Survey (using data from Unicon for 1979 to 2013 and from IPUMS from 2014 to 2018). This data allowed us to estimate, for each year, each family or lone individual's annual market income and its federal income taxes, state income taxes, federal payroll taxes, and retirement payroll deduction (for federal workers). Dividing the latter by the former gave us family-level tax rates. We estimated the $10^{th}$, $30^{th}$, and $50^{th}$ percentiles of family tax rates for non-Hispanic men ages 25 to 29 who were in families with market income. Note that even if these tax rates were based on individuals and on wage and salary income alone, the $10^{th}$, $30^{th}$, and $50^{th}$ percentiles of the tax rate distribution are not quite the same thing as the tax rates paid by workers at the $10^{th}$, $30^{th}$, and $50^{th}$ percentiles of the hourly pay distribution. But the difference is likely to be small. (We also created individual tax rates for men who were the only member of their family with any market income and then estimated the $10^{th}$, $30^{th}$, and $50^{th}$ percentiles of individual tax rates for non-Hispanic young men. The results were very similar.) We apply the tax rates for each percentile in each year to the hourly wage estimates and then add compensation (which is untaxed) back to the post-tax wage.

We apply the 1979 tax rates back to 1973, and we apply the 2018 rates to 2019. In reality, individual income tax rates were somewhat higher in 1973 for the bottom

half of tax units (https://taxfoundation.org/us-federal- individual-income-tax-rates-history-1913-2013-nominal-and-inflation-adjusted-brackets/) while payroll tax rates were slightly lower (https://www.ssa.gov/OACT/ProgData/taxRates.html). The net result is that the average combined federal income and payroll tax rate was likely not to have changed much. See, for instance, the tax rate for the middle fifth (Figure 1 at https://web. archive.org/web/20161018142652/http://www.whitehouse.gov/sites/default/files/Buffett_Rule_ Report_Final.pdf). Marginal income tax rates and payroll tax rates did not change between 2018 and 2019, and the average taxes paid in the bottom half was unlikely to have been much changed in 2019 compared with 2018.

57. Rising immigration has added to the ranks of lower-paid men over time because immigration over the past 40 years has disproportionately involved men with low levels of formal education relative to native-born men. As a consequence, the aggregate trend for men looks worse than was actually experienced by either native-born men or immigrants, a phenomenon known as Simpson's Paradox. Ideally, one might address this issue by separating analyses for native-born and immigrant men so as not to conflate changes in the pay commanded by men with changes in the composition of the population of men. The data on which Figure 13 is based do not allow for that, as immigration status is first measured in the CPS in 1994. However, Hispanics are identifiable in the data all the way back to 1973, and since so much of the increase in immigration has come from Latin America, separating self-identified Hispanics from the analyses is a second-best strategy for addressing compositional change. (Our analyses of Pew Research Center estimates indicate that 59 percent of the net increase in the foreign-born population between 1970 and 2017 is accounted for by rising Latin American immigration. See https://www.pewresearch.org/hispanic/2019/06/03/facts-on-u-s-immigrants/. Its share of the increase in the foreign-born population with relatively low levels of formal education would be larger.)

    We do not show estimates for Hispanics because the trend is substantially affected by Simpson's Paradox. The rising share of Hispanic men accounted for by immigrants conflates trends in the pay received by native-born Hispanics and immigrant Hispanics with changes in the immigrant share of Hispanics.

58. This is true both for the average hourly earnings of production and nonsupervisory workers (https://fred.stlouisfed.org/graph/?g=q6e8), which combines male and female workers ofall ages, and for the median annual wage and salary income of men ages 25-29. For the latter, see, e.g., Steven Ruggles, "Patriarchy, Power, and Pay: The Transformation of American Families, 1800-2015," ***Demography*** 52(6): 1797-1823, 2015, Figure 12.

59. When we used pre-tax hourly wage and salary earnings (excluding fringe benefits) and included Hispanics, the $10^{th}$, $30^{th}$, and $50^{th}$ percentiles of 25- to 34-year-olds' men's pay fell by 23 to 26 percent by the mid-1990s.

60. College enrollment rose rapidly in the 1970s, and we found that a measure of potential work experience for non-Hispanic men in their late 20s and in the bottom half of the pay distribution fell by nearly one year (11 percent) between 1973 and 1978.

    Using the CPS data, we constructed a measure of potential years of work experience that subtracted an estimate of years of schooling from a man's age (and then subtracted six from that to reflect pre-school years). We found that potential work experience among non- Hispanic men ages 25 to 29 who had hourly pay below the median fell substantially between 1973 and 1978, from 8.5 to 7.6 years (or 11 percent).

    Young workers with a year less experience would be expected to make less than their predecessors did five years earlier, all else equal. While their educational attainment was higher than that of their predecessors, it could be that increased

education did not fully offset lower work experience by age 30. The trends for middle-age men might look stronger than for younger men because the payoff for men who attained higher levels of schooling had time to show up by the time men were in their late thirties or early forties.

Complicating this explanation is the fact that hourly pay continued to fall even as potential work experience rose between 1978 and 1990 (though never returning to its 1973 level).

61. Scott Winship, "Policy Options to Address Slow Income Growth and Improve IncomeMobility," ***Business Economics*** 51: 97-104, 2016.

62. Scott Winship, "Declining Prime-Age Male Labor Force Participation: Why Demand- and Health-Based Explanations are Inadequate," Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, Virginia, 2017, https://www.mercatus.org/system/files/ winship-labor-force-participation-mercatus-v1.pdf. Scott Winship, "What's behind Declining Male Labor Force Participation: Fewer Good Jobs or Fewer Men Seeking Them?" Mercatus Research, Mercatus Center at George Mason University, Arlington, Virginia, 2017, https://www. mercatus.org/system/files/ winship_malelaborparticipation_mr_v2.pdf.

63. Ibid. See also the review in Social Capital Project, "Inactive, Disconnected, and Ailing: A Portrait of Prime-Age Men Out of the Labor Force," U.S. Congress Joint Economic Committee, Office of Chairman Mike Lee, https://www.jec.senate.gov/ public/index.cfm/republicans/2018/9/ inactive-disconnected-and-ailing-a-portrait-of-prime-age-men-out-of-the-labor-force.

64. Social Capital Project analyses of the Annual Social and Economic Supplement to the Current Population Survey. The estimates through 2013 come from the Unicon Research Corporation, while those for more recent years are from files provided by the Minnesota Population Center at the University of Minnesota through their Integrated Public Use Microdata Series website at https://doi.org/10.18128/D030.V6.0. From these files, we estimate the $10^{th}$, $30^{th}$, and $50^{th}$ percentiles of earnings (wages and salaries and self-employment earnings from businesses or farms). We adjust these figures to account for inflation, fringe benefits, and taxes in the same way as for hourly pay.

    The earnings of self-employed men are incorporated in the annual estimates, while Figure 13 includes only men working for an outside employer. Men without any earnings in an entire year are excluded from the estimates in Figure 14, because we cannot know what their earnings would have been had they worked (and some of these men, such as the severely disabled, should properly be excluded from analyses of work-based "marriageability"). However, men who exit or enter the labor force partway through the year are included in these estimates and will bias overall earnings levels downward versus what we would see with everyone's annual pay observed.

65. Raj Chetty, David Grusky, Maximilian Hell, Nathaniel Hendren, Robert Manduca, and Jimmy Narang, "The Fading American Dream: Trends in Absolute Income Mobility Since 1940," ***Science*** 356(6336): 398-406, 2017.

66. The basis for our estimates is the series in their Online Table 3, "Absolute Income Mobility by Child Birth Cohort, Parent Income Percentile, and Gender," in Column KU of their Excel spreadsheet at https://opportunityinsights.org/wp-content/ uploads/2018/04/table3_absmob_by_cohort_parpctile_gnd.xlsx. This series uses the Consumer Price Index to adjust incomes for inflation. The CPI is known to overstate inflation, which understates income growth over time. The PCE deflator is a more accurate measure of inflation, but the Chetty team only provide absolute mobility

estimates using this deflator for family income, combining men and women. We compute, for each year, the ratio of absolute family income mobility using the PCE deflator to absolute family income mobility using the CPI. The former comes from their Online Table 4, "Alternative Estimates of Absolute Income Mobility by Birth Cohort," Column D,at https://opportunityinsights.org/wp-content/uploads/2018/04/table4_robustness_by_cohort. xlsx. The latter come from their Online Table 1, "Fading American Dream: Baseline Estimates of Absolute Mobility by Parent Income Percentile and Child Birth Cohort," Column CY at https://opportunityinsights.org/wp-content/uploads/2018/04/table1_national_absmob_by_cohort_ parpctile.xlsx. We apply these ratios to the CPI-based estimates for men in each year.

67. Social Capital Project analyses of decennial census and Current Population Survey data using the Integrated Public Use Microdata Series (IPUMS) Online Data Analysis System. See Steven Ruggles, Sarah Flood, Ronald Goeken, Josiah Grover, Erin Meyer, Jose Pacas and Matthew Sobek. IPUMS USA: Version 10.0 [dataset]. Minneapolis, MN: IPUMS, 2020. https://doi. org/10.18128/D010.V10.0 and Sarah Flood, Miriam King, Renae Rodgers, Steven Ruggles and J. Robert Warren. Integrated Public Use Microdata Series, Current Population Survey: Version 7.0 [dataset]. Minneapolis, MN: IPUMS, 2020. https://doi.org/10.18128/D030.V7.0. The 1969 data point compares the 1969 and 1939 median annual wage and salary income of non-Hispanic men ages 25 to 29 who are not in school, using the decennial censuses for 1970 and 1940. (Personal income is unavailable in the 1940 census.) The 1979 data point compares the 1979 and 1949 median annual personal income of non-Hispanic men ages 25 to 29 who are not in school, using the decennial censuses for 1980 and 1950. The 1989 data point is from the same source, comparing 1989 and 1959 medians. The estimates for 1997 through 2018 rely on the Annual Social and Economic Supplement to the Current Population Survey for the years 1998 through 2019, comparing median personal income of non-Hispanic men ages 25 to 29 who are not in school in years separated by three decades (e.g., 1997 and 1967,..., 2018 and 1988). The estimates for 1997, 1998, and 1999 compare non-Hispanics in those years to all young men 30 years earlier, because Hispanics are identifiable only in the 1971 survey (1970 income). All incomes are adjusted for inflation using the PCE deflator.

    Note that these personal income measures differ from the earnings measures in Figure 14 in that they are pre-tax and do not include employer fringe benefits as income. On the other hand, they include other forms of cash income beyond earnings, such as interest and dividends and transfer payments.

    See also Steven Ruggles, "Patriarchy, Power, and Pay: The Transformation of American Families, 1800-2015," ***Demography*** 52(6): 1797-1823, 2015, Figure 13.

68. See note 56. We did not attempt to compute separate fringe benefit or tax estimates for men and women, so the ratios compare male and female hourly wage and salary income. Trends in the male-to-female ratio using the $10^{th}$ or $30^{th}$ percentiles look very similar.

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class-families-are- more-fragile-today/.

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75. Brink Linsdey, ***The Age of Abundance: How Prosperity Transformed America's Politics andCulture*** (New York: Harper Collins), 2007.

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91. The research on this question has produced inconsistent and mixed results. An early literature on AFDC indicated that the generosity of benefits had no effect on marriage and fertility. However, that conclusion weakened as researchers subsequently produced stronger evidence. Compare Robert Moffitt, "Incentive Effects of the U.S. Welfare System: A Review," Journal of Economic Literature 30(1): 1-61,1992 and Robert A. Moffitt, "The Effect of Welfare on Marriage and Fertility," in Moffitt ed., ***Welfare, the Family, and Reproductive Behavior: Research Perspectives*** (Washington, DC: National Academies Press, 1998). Though the studies were hardly definitive, by 2003, the leading expert, Robert Moffitt concluded in a review of the AFDC evidence that, "although there is still considerable uncertainty in the literature and there remain a large number of studies reporting insignificant estimates, this reading of the literature leads to the conclusion that welfare is likely to have some effect on family structure." See Robert A. Moffitt, "The Temporary Assistance for Needy Families Program," in Moffitt ed., ***Means-Tested Transfer Programs in the United States*** (Cambridge, MA: National Bureau of Economic Research), 2003.

    Reforms to the AFDC program ramped up in the early 1990s, when states were granted waivers to experiment with different reforms. Other policy changes at the federal level culminated in the passage of an overhaul of the welfare system in 1996. AFDC was transformed into TANF. Reviews of the research on state waivers and TANF have also found mixed evidence See James P. Ziliak, "Temporary Assistance for Needy Families," in Robert A. Moffitt ed., ***The Economics of Means-Tested Transfer Programs in the United States, Volume 1*** (Chicago: University of Chicago Press, 2016); Rebecca M. Blank, "Evaluating Welfare Reform in the United States," ***Journal of Economic Literature*** 40(4): 1105-1166, 2002; Rebecca Blank, "What We Know, What We Don't Know, and What We Need to Know About Welfare Reform,"in James P. Ziliak, ed. ***Welfare Reform and Its Long-term Consequences for America's Poor*** (Cambridge, UK: Cambridge University Press, 2009); Jeffrey Grogger and Lynn A. Karoly, ***Welfare Reform: Effects of a Decade of Change*** (Cambridge, MA: Harvard University Press, 2005); Charles Murray, "Family Formation," in Rebecca Blank and Ron Haskins, eds., The New World of Welfare (Washington, DC: Brookings Institution, 2001); Leonard M. Lopoo and Kerri M. Raissian, "U.S. Social Policy and Family Complexity," ***The Annals of the American Academy of Political and Social Science*** 654(1): 213-230, 2014; Rebecca Maynard, Elisabeth Boehnen, Tom Corbett, Gary Sandefur, and Jane Mosley, "Changing Family Formation Behavior Through Welfare Reform," in Robert A. Moffitt, ed., ***Welfare, the Family, and Reproductive Behavior: Research Perspectives*** (Washington, DC: National Academy Press, 1998).

    Because so many reforms in the 1990s occurred at once (both within AFDC and TANF and in other safety net programs), it is difficult to tease out the effects of individual reforms or combinations of reforms, though a number of waiver experiments were evaluated using randomized controlled trials. They, too, produced mixed results. See Grogger and Karoly, 2005; Murray, 2001; Blank, 2002; Maynard et al., 1998.

92. Robert Rector and Vijay Menon "Understanding the Hidden $1.1 Trillion Welfare System and How to Reform It," The Heritage Foundation, April 5, 2018, accessed July 9, 2020, https://www. heritage.org/welfare/report/understanding-the-hidden-11-trillion-welfare-system-and-how- reform-it.

93. Chris Herbst finds, for example, that a $1,000 increase in the maximum Earned Income Tax Credit (EITC) benefit—a refundable tax credit that functions as a cash assistance program for low-income workers—decreases new marriage rates by roughly 5 percent. See Chris M. Herbst, "The Impact of the Earned Income Tax Credit on Marriage and Divorce: Evidence from Flow Data," ***Population Research and Policy Review*** 30(2011): 101-128. Katherine Michelmore finds that single mothers receiving EITC are 2.5 percentage points less likely to get married. See Katherine Michelmore, "The earned income tax credit and union formation: The impact of expected spouse earnings," ***Review of Economics of the Household*** 16(2018): 377-406. W. Bradford Wilcox, Joseph Price, and Angela Rachidi examined the effect of marriage penalties from three means-tested welfare programs (food stamps, Medicaid, and Temporary Assistance for Needy Families) on unmarried couples with young children. They found that marriage penalties did not influence marriage among those at the lowest income levels, but they did find that marriage penalties effected couples whose incomes were closer to the benefit cutoff line. Furthermore, these researchers found that 30 percent of Americans reported knowing someone who decided not to marry due to marriage penalties. W. Bradford Wilcox, Joseph P. Price, and Angela Rachidi, "Marriage, Penalized: Does Social-Welfare Policy Affect Family Formation?" American Enterprise Institute and Institute for Family Studies, July 26, 2016, accessed April 17, 2019, http://www.aei.org/publication/marriage-penalized-does- social-welfare-policy-affect-family-formation/. Also see U.S. Department of Health and Human Services, Administration for Children and Families, Office of Family Assistance, "Marriage Penalties in Means-Tested Tax and Transfer Programs: Issues and Options," OFA Report 2019- 01, 2019, by W. Bradford Wilcox, Chris Gersten, and Mary Myrick, accessed July 9, 2020, https:// www.acf.hhs.gov/sites/default/files/ofa/hmrf_marriagepenalties_paper_final50812_6_19.pdf.

94. Estimates from 1940 to 1996 use monthly averages across families for AFDC and multiply them by 12 to annualize them. The averages are taken from Table 9.G1 of the Social Security Administration, Office of Policy, Office of Research, Evaluation, and Statistics, "Annual Statistical Supplement to the Social Security Bulletin, 2005," SSA Publication No. 13-11700, 2006, https://www.ssa.gov/policy/docs/statcomps/supplement/2005/supplement05. pdf. Estimates from 1997 to 2013 also multiply by 12 monthly averages across families for TANF. They are taken from various years' "Characteristics and Financial Circumstances of TANF Recipients," from the U.S. Department of Health and Human Services, Office of the Administration for Families and Children, Office of Family Assistance, https://www.acf.hhs.gov/ ofa/resource-library/search?area%5B2377%5D=2377&topic%5B2353%5D=2353#?area%5B2377%5D=2377&topic%5B2353%5D=2353. They represent fiscal years rather than calendar years. In both cases, the nominal amounts were inflated to 2019 dollars using the PCE deflator.

95. These estimates are from Social Capital Project analyses of the Annual Social and Economic Supplement to the Current Population Survey. This data source has included information on receipt of "public assistance" income since 1968, which covered income received in 1967. The benefits for all members of a single mother's household were counted. The underlying analyses are based off of Scott Winship, "Poverty after Welfare Reform," Manhattan Institute, 2016, https://www.manhattan-institute.org/html/poverty-after-welfare-reform.html.

    We use the median amount of public assistance benefits received among female-headed households with children and at least $3,000 in benefits (in 2019 PCE-

adjusted dollars). This ensures that the trend in benefit amounts is not dominated by cyclical factors, since the amount in Figure 18 is an annual amount and can be affected by the state of the economy (which affects the number of months of receipt). The trends are very similar using other thresholds such as $6,000, so long as they are not so high as to identify a relatively atypical group. The fact that the level lines up so well with Line 1 in the chart makes it useful for presentation, but it is the confirmation of the trend that is most important in using this second data source.

96. Both lines are from Table 3 of Moffitt, 1992. Moffitt shows the amounts in 1982 dollars, adjustedusing the PCE deflator; I convert to 2019 dollars using the same deflator. The 1982 PCE index value was subject to revisions after Moffitt's paper was published, so the conversion is somewhat imprecise. Furthermore, the Medicaid component of benefits in Line 4 was adjustedfor inflation using state-specific medical care price indices related to the Consumer Price Indexrather than the PCE deflator. We multiply the estimates by 12 to annualize them.

    Line 3 shows maximum monthly AFDC benefits for a family of four with no other income. Moffitt cites unpublished data from the Office of Family Assistance and an unpublished appendix from Richard Kasten and John Todd, "Transfer Recipients and the Poor During the 1970s," in Richard Zeckhauser and Derek Leebaert, eds. *What Role for Government?* (Durham, NC: Duke University Press, 1983), 60-77.

    Line 4 shows, for each year, the sum of (1) the maximum food stamp benefits for a family of four with no other income, (2) 70 percent of the maximum AFDC benefit, and (3) 36.8 percent of the Medicaid insurance value for a family of four. The last component equals the average Medicaid expenditures across AFDC adults plus three times the average Medicaid expenditures across AFDC dependent children, divided by the number of AFDC adults. The reduction of the second two components appears to account for benefit reduction rates when a recipient of food stamps receives AFDC or Medicaid. For the food stamp estimates, Moffitt cites personal communication from Thomas Fraker as well as U.S. House of Representatives, "Background Material and Data on Programs within the Jurisdiction of the Committee on Ways and Means," Washington, DC: Government Printing Office, 1989, p. 1126. For Medicaid estimates, he cites unpublished data from the U.S. Health Care Financing Administration.

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    We use a threshold of $12,000 in benefits rather than the $3,000 threshold used for Line 2 for two reasons. First, $3,000 is a much lower level when considering all of these benefits, so it captures many households that receive relatively few benefits and is thus more affected by changes in the business cycle. Second, the resulting levels line up with Line 4 well, which makes it useful for presentation, but it is the confirmation of the trend that is most important in using this data source.

98. Total safety net benefit estimates come from Social Capital Project analyses of the Annual Social and Economic Supplement to the Current Population Survey. The measure includes Supplemental Security Income (SSI) benefits beginning in 1976 (1975 income), and a variety of noncash benefits since 1980 (1979 income). The noncash benefits include (through 2013) Medicaid, food stamps, housing subsidies,

school breakfasts and lunches, and energy assistance. The measure also includes the value of the federal Earned Income Tax Credit from 1979 forward. Information on Medicaid is unavailable after the 2014 data (2013 income). While the 1979-to-2013 estimates are from microdata developed by the Unicon Corporation, the 2013-to-2018 estimates are from IPUMS microdata (which does not include Medicaid values for any year). If Medicaid could be included after 2013, the level would be affected, but not necessarily the trend. It may seem surprising that the post-2013 estimates are not higher than the earlier estimates that include Medicaid. The explanation is that in both periods, medians are conditioned on receiving at least $12,000 in benefits, with benefits including Medicaid in earlier years, but the $12,000 threshold excluding Medicaid benefits in the more recent years.

The benefits for all members of a single mother's household were counted. For further details on how these were valued, see Scott Winship, "Poverty after Welfare Reform," Manhattan Institute, 2016, https://www.manhattan-institute.org/html/poverty-after-welfare- reform.html. Not included in the measure are other cash transfers such as Social Security benefits, including survivor and disability benefits; unemployment compensation; workers' compensation; veterans' payments, including retirement benefits; railroad and black lung survivor and disability benefits; and federal educational assistance. Nor are two noncash benefit programs: the Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) and Medicare. Nor is the Additional Child Tax Credit, the refundable part of the Child Tax Credit that goes to filers with no federal income tax liability.

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corrected many tax-related high-income penalties, addressing penalties for lower-income couples should be a higher priority.

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# A Place to Call Home: Improving Foster Care and Adoption Policy to Give More Children a Stable Family

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Family relationships are a fundamental source of social capital in a person's life. A stable and healthy family life is crucial to healthy child development and is associated with a variety of positive outcomes.[1] Unfortunately, some children experience only instability and family discord. Sometimes birth parents, knowing they are ill-equipped to provide the emotional and financial security a child needs, place their children in foster or adoptive families that provide enriching relationships and a stable home environment children would otherwise lack.

Tragically, the need for foster and adoptive families is great. In 2018, more than 400,000 children were in foster care, and 18,000 youth left foster care without a permanent home. While the nation's foster care caseload declined between 2000 and 2012 and the number of children who aged out of foster care without a permanent family has also decreased substantially since 2009, the foster care caseload began to increase steadily after 2012.[2] The number of children and youth in foster care is higher today than it has been in nearly a decade.[3]

Although sometimes foster children are subsequently able to reunite with their biological parents, some are not able to return to their biological parents and require a permanent, adoptive home. For these children stability is especially important, because children who go through multiple foster care placements are worse off than those who experience fewer placements.[4] Foster children who age out of the system without a permanent family experience substantial challenges in life.[5]

Fortunately, many Americans are willing to provide foster care, adopt foster children, or both. In fact, far more Americans are looking to adopt than there are children in need of adoption.[6] Although many children in the foster care system have special needs that make it more difficult for them to find families, many Americans are willing to provide foster care for these children and adoptions of special needs children have increased a great deal over the last few decades.[7] There are also many private organizations across the United States, including faith-based organizations, dedicated to helping foster children find good homes. Still, there are several issues that stand in the way of connecting foster and adoptive children with loving homes. These include a child welfare system that is often unsupportive of foster parents, government actions that are pushing faith-based foster care and adoption providers out of service, child welfare systems that keep foster children languishing in temporary placements when they would benefit from permanent adoptive placements, and policies that fail to support infant adoption when expectant parents do not desire a child or when it is unlikely expectant parents will be able to provide safe care.

Government and civil society should work together to help ensure that children in need find loving homes. This can be accomplished by increasing the pool of adoptive and foster parents, protecting faith-based adoption and foster care, providing qualifying foster children with permanent adoptive placements, and supporting infant adoption as a valid and loving option.

## ISSUE 1: PROSPECTIVE AND CURRENT FOSTER AND ADOPTIVE PARENTS LACK AGENCY SUPPORT

Many Americans are interested in or open to becoming foster or adoptive parents. Roughly a quarter of Americans say they have considered becoming a foster parent, and among Americans who have never adopted, roughly a quarter say they have considered it.[8] However, according to one study, only 8 percent of people who inquire about becoming foster parents eventually become licensed.[9] The majority of those who do become licensed foster parents cease their service relatively quickly. According to a study by the U.S. Department of Health and Human Services, roughly one half to two-thirds of foster parents discontinued their service within one year of having their first foster child placed in their home.[10] In another study, researchers found that 25 percent of new foster homes stop providing service in less than four months.[11]

While foster parents quit for many reasons, foster parents and prospective foster parents often report a lack of support from child welfare agencies.[12] In a 2007 Harris Interactive study researchers found that over half of respondents who had considered foster parenting or adopting reported that the social services agency was either not responsive at all or only slightly responsive.[13] The researchers also found that 75 percent of adults who had ever fostered or adopted reported dissatisfaction with the support they received from the child welfare agency either prior to or after placement.[14] Similarly, in a study of current and former foster parents, researchers found that the main reason foster parents dropped out of the system was a lack of responsiveness from caseworkers and a lack of agency support.[15]

Another issue is that although foster parents play a crucial role in the child welfare system, states use very little of their federal or state foster care funding for recruiting foster parents. This may reflect an overall lack of focus on foster parents by the child welfare system.[16] Furthermore, most states do not have benchmarks to measure agencies' success at recruiting and retaining foster parents. According to a 2002 U.S. Department of Health and Human Services survey of foster care program managers, only 21 of 41 managers said their states had recruitment goals, and of the 21 managers reporting that their state had recruitment goals, only 13 states had developed indicators to measure the success of their recruitment strategies.[17] Furthermore, the federal Child and Family Services Review, conducted by the U.S. Department of Health and Human Services to examine state foster care agencies, does not measure recruitment and retention outcomes, such as success in licensing foster parents, the rate of foster parent attrition, or the percent of licensed foster parents who have children placed in their care.

Given the many poor reviews of the foster care system from former foster parents and prospective foster parents, it appears that states and agencies can do a better job of supporting the people who are providing or will potentially provide the day-to-day care for children under the agency's watch. Improving the system's treatment of foster parents would likely increase the number of prospective parents who become licensed as well as the number of licensed foster parents who continue to provide service, thus increasing the number of foster homes available to children.

## RECOMMENDATION: IMPROVE THE FOSTER CARE SYSTEM TO BETTER SUPPORT FOSTER AND ADOPTIVE PARENTS

States and agencies can implement several reforms to improve their relationships with foster parents to increase the likelihood foster parents will be successful.

### *Measure State Recruitment and Training Efforts*

Agencies should focus more on recruiting and retaining foster parents, setting benchmarks and regularly measuring their progress in these areas. A June 2020 executive order issued by President Trump requires that the secretary of the U.S. Department of Health and Human Services "develop a more rigorous and systematic approach to collecting State administrative data as part of the Child and Family Services Review."[18] The executive order mentions specifically collecting data on the average retention rate of foster parents, the number of families available to foster, and the length of time it takes to complete foster care certification. The federal Child and Family Services Review should also measure the number of foster parents who become licensed and the percent of foster homes that have children placed in them.

Furthermore, while states spend very little of their federal or state foster care funding on recruiting or retaining foster parents, states spend a significant portion of their foster care funding on administrative costs. However, there is no correlation between administrative spending and outcomes for children or the quality of services agencies provide.[19] States that spend an excessive amount of funding on administrative costs without an improvement in recruiting and retaining foster parents or in increasing the proportion of children placed should receive less federal funding.

### *Improve Agency Engagement with Parents*

Agencies can work to improve their relationships with prospective and current foster parents. Several agencies throughout the nation have received grants to pilot various plans for improving foster parent recruitment. Agencies can learn from other states and implement strategies to improve their support of foster parents and to remove unnecessary barriers to becoming a foster parent.

***Use targeted recruitment strategies.*** Researchers have found that 35 percent of licensed foster parent homes do not have a child placed in them, possibly due to

foster families not being willing or able to provide care to the particular children available, such as those with special needs.[20] Agencies may be able to improve the likelihood that foster parents have children placed in their care by using targeted recruitment strategies. They can focus their recruitment efforts on individuals who would be most likely to succeed in fostering the children in need of homes in their specific agencies. For example, some agencies have focused recruitment efforts on individuals with similar characteristics to those who have been successful foster parents in the past.[21]

Another way to improve the match between foster parents and foster children is by providing information to prospective foster parents early on about the children in need of homes. The Denver Department of Human Services developed a website, for example, to provide information to prospective foster parents about the children in need of care, as well as to provide realistic information about foster parenting. The agency found that the website was their most effective recruiting tool and that families recruited through the website were more likely to follow through with the licensing process because the information provided on the website was realistic and helpful.[22]

Furthermore, to improve and increase recruitment, some agencies have hired program coordinators to lead community-based recruitment teams, while others have assigned staff specifically to seek out family members and fictive kin who would be able and willing to foster.

***Improve service and treat parents as partners.*** Given the number of prospective and active foster parents who report poor communication with the child welfare agencies, improving customer service is likely an important area for agencies to focus on to improve recruitment and retention. Improving customer service could include hiring or assigning agency staff to work specifically with foster families as they navigate the application process, ensuring that families have the necessary support as they fill out forms and obtain required documents, and providing help to potential foster families to identify community resources available to them. Agencies can set goals to return phone calls to foster parents and prospective foster parents in a timely manner (e.g., within 24 hours), as well as implement customer service training for agency staff. Some agencies have put actions like these into place and seen improvements in the number of families who complete the application process and receive licensure.[23]

Agencies should also conduct exit interviews with families leaving the foster care system to get a better sense of what is impeding foster parents' success, as one agency in Texas did as part of their pilot strategy to improve recruitment.[24] Given the high rate of attrition in the foster care system, agencies should make sure they know why parents leave so they can address issues accordingly. This much-needed feedback loop does not exist for some agencies. Agencies can also conduct listening sessions to gather information on what type of support foster families need.[25]

Other potential ways to improve the relationship foster parents have with the agency as well as their satisfaction with foster parenting include giving foster parents a greater voice in children's case planning, keeping foster parents informed of children's court dates and allowing foster parents a voice in such proceedings, giving foster parents greater freedom in approving activities for children, and simply maintaining frequent contact with foster parents.[26] Furthermore, an agency can recruit and train a pool of respite care providers so that foster parents have others readily available to them to help provide support.[27]

***Involve private organizations.*** Private organizations can act as another useful resource in recruiting and supporting foster families. Agencies can partner with churches and other faith-based organizations, businesses, and universities, among others, to help find families who would be able and willing to provide care, to provide training, and to support foster families.
Churches and faith-based organizations generally believe in helping the needy and have provided care to orphaned children for generations. For example, a core Christian duty is to help the orphaned.[28] Faith leaders have access to and relationships with families from their congregations, which may make families more likely to be receptive to the invitation to foster or adopt. Families involved in a religious community have a built-in support network to help with the burdens foster parents shoulder, and congregations also usually have available volunteers who may be able to assist in recruiting, training, and supporting foster families.[29]

There are a variety of faith-based groups supporting foster efforts already. For instance, a faith-based group in Arkansas, The CALL, has helped recruit nearly half of the foster families in the state.[30] According to one study, over one third of the families recruited by The CALL said they would not have become foster parents without the organization.[31]

One Church One Child is another faith-based effort. It was founded in Chicago in 1980 by an African-American Catholic priest who was concerned about the number of African-American children in the foster care system. One Church One Child partners with churches to find adoptive homes for children, with the goal of finding at least one family per church to take in a child. The organization now has multiple locations throughout the country and has placed at least 140,000 children in adoptive homes.[32]

The support faith-based groups provide may result in more successful foster parenting. One study found that foster parents recruited through church or religious organizations foster 2.6 years longer than other foster parents.[33] Another study found that foster parents often indicate that religion or church support are resources that help them successfully foster parent.[34] Thus, partnerships with faith-based groups can prove valuable to helping foster parents have a successful experience and ultimately to help children have more stable placements.

Agencies can also work with businesses and universities to recruit foster parents, to encourage family leave policies for adoptive and foster parents, to collect and analyze data, and so forth. Furthermore, there are private organizations that specifically focus on matching foster children with families. For example, Family

Share is an organization that maintains a database of parents licensed to provide foster care and adoption. They then use data analytics to match children with parents.[35] This approach can help improve the matches between foster parents and children, so that children are more likely to find a stable family situation as well as to find a family more quickly.

## ISSUE 2: BURDENSOME REQUIREMENTS MAY DETER QUALIFIED FOSTER PARENTS

Besides a lack of support from the foster care system, foster parents and prospective foster parents sometimes face burdensome requirements for becoming foster parents. This can include lengthy trainings, educational requirements, and bringing a home into compliance with state standards for foster homes. While it is important to ensure that children are placed in safe homes with competent foster and adoptive parents, some requirements seem unnecessary to providing safe care to children and may simply lead to fewer otherwise-qualified people being able to provide service.

### *Burdensome Foster Parent Trainings*

Most states require prospective foster parents to complete a specific number of hours of training before a child is placed in their home, as well as to complete a certain number of hours of training while in service. The number of hours vary, ranging from 6 to 36 hours for pre-service training, for example, although not all states have a specified number of hours of training required.[36]

While foster parents report that trainings can be useful, the extent of what is required may make it prohibitive for some people to serve as foster parents. In the 2002 report of foster care providers by the U.S. Department of Health and Human Services, 13 of the 41 foster care managers who responded said that training requirements can be a barrier to recruiting foster parents. In the 13 states reporting, the length of training for prospective foster care parents lasted between 9 and 12 weeks, and in 12 states the training period was greater than 12 weeks. The foster care managers also noted that foster parents in rural areas have limited accessibility to training sessions.[37]

### *Unreasonable Educational Requirements*

Education requirements may also be a barrier to foster parenting. There are a handful of states that require foster parents to hold a high school diploma or GED.[38] Virginia goes so far as to require foster parents either to hold a high school diploma or GED while having a year of experience providing care to children in the age range of children being placed in the home, or to hold a bachelor's degree in a field related to family services, child development, social work, or education.[39]

While it is necessary that foster parents demonstrate the maturity and skills needed to parent, as well as the ability to communicate with child welfare agency

and medical providers, holding a particular educational degree is not needed to be a good parent. Furthermore, the majority of parents in the United States do not possess a college degree, let alone a college degree in a field related to social work or family science. It seems unnecessarily prohibitive to hold a foster parent to a standard that the vast majority of American parents do not meet.

*Unnecessary Home Requirements*

Some foster parents and caseworkers report that requirements regarding the physical characteristics of the home can make it burdensome for people to provide foster care.[40] All states have such requirements. While some of these requirements make sense for protecting the child's wellbeing, others seem overly burdensome and exceed standards that would be required for most parents to provide a safe home for their children.

For example, Wyoming does not allow children of any age to share a bedroom if they are of the opposite sex. Some states not only require a foster home to have a fire extinguisher but they require fire extinguishers to be placed on every floor of the home. Other examples of strict home requirements include: locks for all medications in the household as well as for household chemicals; First Aid kits for the house and the car that contain a specific list of items; emergency contact information available in the vehicle in which children are transported; gates or doors to all stairways in the home unless a child is over the age of five; no cords on window coverings; foster children not being allowed to sleep on a bunk bed or trundle bed; and quarterly fire drills conducted by foster parents that must be reported to the agency.[41] Some states require that if the home a child will occupy is rented, the family have renters insurance.[42]

While states should be concerned with keeping foster children physically safe, some home requirements can and should likely be removed. It makes little sense why infants or toddlers of the opposite sex should not be allowed to share a bedroom. Furthermore, given that most renters in the United States do not hold renters insurance and many are good parents it is unclear why foster parents need to possess this type of insurance.[43] While preparing children to know what to do in case of fire is important, it seems highly unlikely that even a small minority of families in the United States conduct quarterly fire drills with their children.

In 2019 the U.S. Department of Health and Human Services released model foster home standards.[44] States are not required to follow the standards, but they are required to submit an explanation if they do not.[45] The model standards may make foster parenting more feasible for families in urban areas, such as by not requiring foster parents to own a car or for their homes to meet certain square footage requirements. The standards also keep educational requirements to a minimum.[46] Some states have eased their requirements in response, such as by increasing the maximum number of foster children who can reside in a foster home simultaneously. On the other hand, the federal model standards are overly proscriptive in some areas. For example, they include specifics on swimming pool safety and physical exams for foster parents and require foster parents to have recycling service if it is available.[47]

## RECOMMENDATION: ELIMINATE UNNECESSARILY BURDENSOME REQUIREMENTS FOR FOSTER PARENTING

States and agencies should review requirements for foster parents and eliminate requirements that have little to do with being a committed parent that provides safe care. Burdensome requirements may have the benefit of incrementally safer and better experiences for foster children who find homes, but they have the cost of reducing the number who are placed.

### *Improve the Foster Parent Training Process*

Agencies can work to make sure training sessions for prospective and current foster parents are useful and that the length of time required for trainings is not overly protracted. Making trainings more accessible—such as through providing trainings online, streamlining trainings into fewer sessions, and implementing listening sessions and gathering feedback from foster parents to determine whether trainings are useful—can improve the training experience for prospective and current foster parents.[48]

States could also offer dual licensing for people who are interested in both foster parenting and adoption so that interested individuals have the option of qualifying for both simultaneously. A dual licensing strategy can cut down on redundancy for many families, considering that 50 percent of children adopted from foster care are adopted by their foster family.[49]

### *Remove Unnecessary Education and Home Qualifications*

Keeping foster children safe while in care is important, but some of the requirements for parents as well as some of the home safety standards go beyond the mark. For example, while it is important for agencies to ensure that foster parents are able to provide competent care for children, some requirements, such those requiring a particular education degree, seem excessive. If a person can successfully complete the application process, trainings, home study, background checks, and so forth, it makes little sense that a foster parent should be required to hold a particular education degree. States should remove requirements for foster or adoptive parents to hold a diploma or degree. Furthermore, they should examine other personal requirements for foster parents and eliminate those that are excessive.

Furthermore, while agencies have a clear interest in ensuring that a foster child is placed in a physical dwelling that is safe, some state requirements seem simply to be unnecessary barriers. States should reexamine their standards and determine which requirements are excessive or unnecessary and remove or reform those requirements that may simply be standing in the way of good potential foster parents. States should have the flexibility to set their own standards and any federal or national model standards should keep requirements to a minimum.

## ISSUE 3: FAITH-BASED PROVIDERS HAVE BEEN EXCLUDED FROM PROVIDING FOSTER CARE AND ADOPTION SERVICES

For much of the nation's history, faith-based foster care and adoption agencies have played an active role in helping children in need find homes.

Faith-based providers—many of them quite large— continue to fill this role today.[50] For example, Bethany Christian Services has more than 100 offices in 33 states and the District of Columbia, as well as several locations internationally.[51] Bethany Christian Services placed nearly 6,500 children in foster or adoptive homes in the United States in 2018 and provided pregnancy counseling services to nearly 3,000 clients.[52] Catholic Charities provides similar services nationwide. Between 2006 and 2016 it provided adoption services to 82,000 children.[53] In 2016, 45 percent of adoption placements made by Catholic Charities were for children with special needs.[54] Beyond providing placement services, faith-based groups are also involved in foster care and adoption through activities such as providing trainings for prospective foster and adoptive parents, providing financial support to foster and adopted children, and recruiting foster and adoptive parents.[55]

However, in some states and cities, faith-based foster care and adoption providers have been compelled to stop providing these services. This is due to sexual orientation and gender identity laws that would require them to place children with same-sex couples, which would conflict with these providers' religious beliefs about marriage.

Catholic Charities in Boston stopped providing foster care and adoption placements in 2006, due to sexual orientation laws and the state's legalization of same-sex marriage that would require them to place children with same-sex couples.[56] Catholic Charities in Washington, D.C. ceased their foster care and adoption services in 2010 for the same reason.[57]

A few years later, in 2011, Illinois started requiring foster care and adoption providers to place children with unmarried couples, including same-sex couples. As a result, Catholic Charities ended its contract with the state and foster children were sent to other agencies.[58]

More recently, in 2018, the city of Philadelphia told Catholic Social Services that the agency must either be willing to place children with same-sex couples or stop providing foster care services. Because Catholic Social Services would not agree to the city's request that the agency place children with same-sex couples, Philadelphia ultimately ended its partnership with the organization.[59] This occurred the same year that Philadelphia experienced an increase in their foster care caseload and had issued an urgent call for 300 more foster families.[60] Catholic Social Services filed a lawsuit against the city but lost at both the federal district and appeals courts. Earlier this year, however, the Supreme Court announced it would hear the case in fall of 2020.[61]

Faith-based foster care providers in Michigan are also embroiled in lawsuits involving similar matters.[62] Although Michigan passed a law in 2015 to accommodate faith-based foster care and adoption providers' beliefs about marriage, the state is no longer enforcing the law.[63] The fate of Michigan's religious liberty protection for faith-based foster care and adoption providers hangs in the balance as the Supreme Court considers the Philadelphia case.

It is difficult to know for sure what the effect of losing faith-based adoption and foster care providers has been on outcomes such as the number of foster care placements and the number of available foster homes, but it is likely to be substantial. In Illinois, as a result of the state ending its work with faith-based foster care and adoption providers, between 2,000 and 3,000 children were displaced from faith-based adoption agencies and moved into other agencies.[64] As noted earlier, a faith-based group in Arkansas, The CALL, is responsible for recruiting nearly half of the foster families in the state, and a third of foster families recruited by the organization said they would not have become foster parents without the organization.[65]

Besides challenges at the state level, federal challenges to faith-based adoption and foster care providers also exist. The Obama Administration implemented a rule that made federal foster care funding contingent on an agency being willing to place children with same-sex couples.[66] However, in the fall of 2019, the Trump Administration issued a new rule to reverse the Obama Administration's regulation.[67]

In 2019, the U.S. House of Representatives passed the *Equality Act*, which would prohibit federal funds from going to agencies that do not comply with sexual orientation and gender identity laws (and are thus unwilling to place children with same-sex couples).[68] Furthermore, the House Ways & Means Committee held a hearing in late February of 2020 investigating a faith-based organization that had received an exemption from the Obama era rule, as well as examining the Trump Administration's ruling to undo the Obama regulation.[69]

## RECOMMENDATION: PROTECT THE RELIGIOUS LIBERTY OF FAITH-BASED FOSTER CARE AND ADOPTION PROVIDERS

There are a variety of bills that have already been introduced in Congress to protect religious liberty that would support faith-based organizations' ability to serve foster and adoptive children. Furthermore, in the June 2020 Executive Order on foster care, President Trump required that the secretary of the U.S. Department of Health and Human Services provide guidance to federal, state, and local agencies making it clear that faith-based agencies are eligible to partner with government agencies on an equal basis, according to the First Amendment.[70]

Members of Congress have introduced legislation to protect religious liberty regarding individuals' and organizations' beliefs about marriage. For example, Senator Mike Lee (R-UT) introduced the *First Amendment Defense Act* in 2018, which would prohibit the federal government from discriminating against individuals or organizations based on their religious or moral beliefs about the definition of marriage.[71] Specifically, the act would prohibit the federal government from considering an individual or organization's beliefs about marriage for purposes of providing grants, granting accreditation or licensure, or determining an organization's tax status.[72]

Furthermore, Senator Michael Enzi (R-WY) and Representative Mike Kelly (R-PA) introduced the *Child Welfare Provider Inclusion Act* in 2019. This act would prohibit states that receive federal Title IV foster care funding from discriminating against foster care and adoption providers based on their religious or moral beliefs about marriage.[73]
Finally, states should pass laws to protect organizations' and individuals' free exercise of religion in regards to their beliefs about marriage. Several states have passed such laws and others should follow suit.

## ISSUE 4: CHILDREN LANGUISH IN FOSTER CARE WHEN THEY WOULD BE BETTER SERVED BY PERMANENT PLACEMENT

Foster care plays an important role for children who need to be removed from their homes due to abuse or neglect. But foster care is not a permanent placement and children should not be left to languish in temporary care. Children who remain in the foster care system for long periods of time are more likely to drift through multiple foster care placements or to age out of foster care without a permanent family, both of which are associated with lower wellbeing.[74]

When a child enters foster care, child welfare agencies should take steps expeditiously to determine a permanency plan for the child. Making a timely case plan is especially important for very young children who are in the developmental stage of forming attachment with their caregiver.[75] (The largest age group of children entering the foster care system are children under the age of one.)[76]

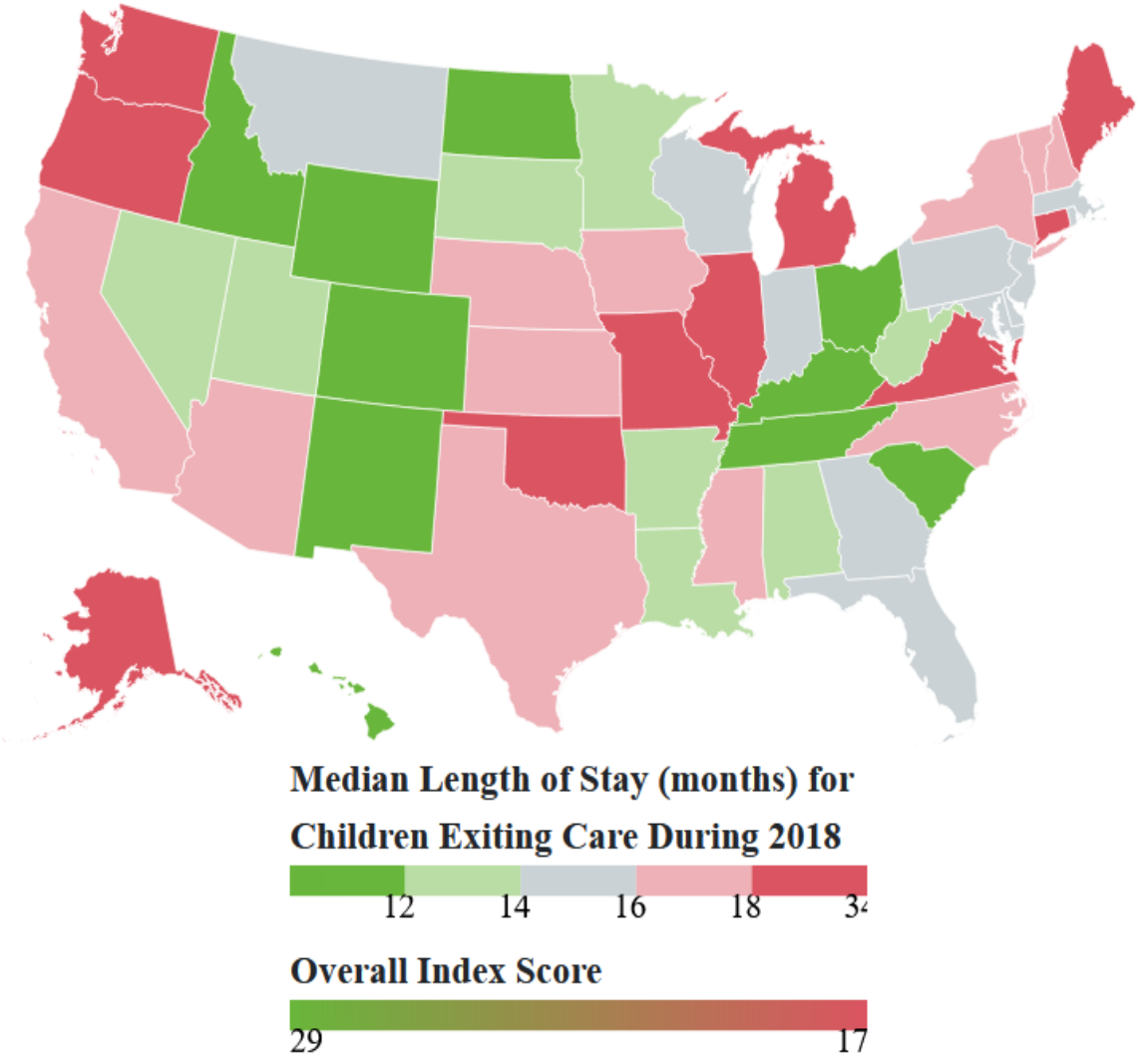
Under federal law, children are required to receive a permanency hearing within 12 months of being placed in the foster care system, in which the court determines whether the child's case plan will be reunification with his or her parents, termination of parental rights and adoption, legal guardianship, or "another planned permanent living arrangement."[77] However, some states report that it can take months to get a trial scheduled due to backup in the system.[78]

Some states do better than others at moving children to permanency (see Figure 1). For example, the median length of stay for children in foster care is 5.6 months in New Mexico, according to the most recent data, whereas it is 24.1 months in Washington, D.C. When it comes to moving children into adoptive homes, in Utah

47 percent of children are adopted in under two years, whereas in Illinois only 33 percent of children are adopted in less than two years. In Wyoming only 1 percent of foster youth age out of the system without a permanent placement, whereas in Washington, D.C. 51 percent do.

In states that are less effective at moving children to permanency, three issues may be to blame: weak enforcement of the *Adoption and Safe Families Act*, poor incentives in the Title IV-E foster care funding, and non-compliance with the *Multiethnic Placement Act*.

Figure 1. Foster Care and Adoption Ranking Variables by State, 2018: Median Length of Stay in Foster Care, Percent of Children Adopted in Less Than Two Years, Percent of Children Who Age Out of Foster Care Without a Permanent Placement, and Percent of Foster Care Entries That Are Re-entries




Source: U.S. Department of Health and Human Services, Administration for Children and Families, Child Welfare Outcomes Report Data, 2018, https://cwoutcomes.acf.hhs.gov/cwodatasite/.

*Weak Enforcement of the Adoption and Safe Families Act "15 of 22" Rule*

Federal law requires that if a child has been in the foster care system for 15 of the past 22 months, the agency must file for termination of parental rights so that a child can be adopted. There are exceptions to this rule: for instance, states can exempt children from the 15 of 22 rule if a child is living with kin, the agency has not made sufficiently reasonable efforts to reunify the child with his or her parents, or the court determines that it is not in the best interest of the child for parental rights to be terminated.[79]

Congress established the 15 of 22 rule in the *Adoption and Safe Families Act* of 1997. The act was implemented as part of the Title IV-E foster care program, which provides funding to state foster care systems. Policymakers were concerned about the major growth of children in foster care that took place in the 1980s and 1990s and feared that children were remaining in the system too long.[80]

Prior to the *Adoption and Safe Families Act*, Congress passed the *Adoption Assistance and Child Welfare Act* of 1980, which mandated that states make reasonable efforts to rehabilitate biological parents before terminating their parental rights. The *Adoption and Safe Families Act* of 1997 defined what "reasonable efforts" are and exceptions to the requirement for aggravated circumstances, such as in cases of chronic abuse, abandonment of the child, or sexual abuse.[81] Proponents of the 1997 legislation argued that the 1980 law leaned too heavily towards rehabilitating parents, leaving too many children to languish in the system when it was unlikely a parent would be fit to provide care again or be able to do so within a reasonable amount of time. They also argued that children were too often returned to unsafe family situations.[82]

After the 15 of 22 rule was implemented as part of the *Adoption and Safe Families Act*, more children were adopted and the foster care caseload began to decline.[83] While these were promising changes, there is room for improvement. As of 2018, the median length of stay in the foster care system was still 13.2 months, and the mean length of stay was much higher (19.7 months). This indicates that there are outliers who remain in the foster care system for much longer than the median length of time.[84] Relatedly, a substantial number of youth age out of the foster care system without finding a permanent placement: 18,000 youth aged out of the foster care system in 2018.

States are not required to collect data on agencies' compliance with the 15 of 22 rule, thus it is challenging to determine how often the rule is bypassed and for what reasons.[85] However, a 2002 report from the Government Accountability Office (GAO) indicates that in nine states that provided data (only nine states were able to provide data because most had not collected it), the 15 of 22 rule was bypassed more than it was applied. Furthermore, researchers find that states rarely used the aggravated circumstances provision to expedite termination of parental rights.[86]

Although states are not required to collect data on agencies' use of the 15 of 22 provision, the federal government does collect some information on how this rule is applied. As part of the federal Child and Family Services Review, the Children's Bureau reviews a minimum of 65 foster care cases per state per review period. (Reviews have taken place between 2001 and 2004, 2007 through 2010, and 2015 through 2018.) During the latest review period, reviewers found that states filed for termination of parental rights in just over half—52 percent—of applicable cases they reviewed. In 26 percent of applicable cases where termination of parental rights was not filed, no reason was given regarding why an exemption was made.[87] Furthermore, in the U.S. Department of Health and Human Services 2010-2013 report to Congress on Child Welfare Outcomes, the department reported that in 2013, of the cases who had been in the foster care system for at least 15 of the past 22 months, only 14 percent had seen the termination of parental rights so that the child could become legally free for adoption.[88]

In the 2002 GAO report, seven states provided data on their reasons for bypassing the 15 of 22 rule. These reasons included: they believed parents would rehabilitate soon, the child was in the care of relatives, the child would not consent to termination of parental rights, the parent had not received sufficient services, or the child was living in long-term foster care, where the child welfare agency retains care of the child rather than seeking more permanent options, like adoption or reunification.[89] While these may be appropriate reasons for exempting a case from the time limit, they may be problematic at times. A court may expect a parent to rehabilitate soon but that might not happen. A state may commonly fail to provide services to a parent in a timely manner. Or long-term foster care—which is a last resort—may too often be the default plan rather than seeking an adoptive home for the child.

Some argue that the allowable exceptions to the 15 of 22 rule make the rule too weak and that such exceptions should be removed or tightened.[90] Others argue that parents should have more time to rehabilitate.[91] The frequency with which agencies and courts bypass the time limit suggests that states have sufficient ability to make exceptions.

The field of social work typically views terminating parental rights negatively, seeing it as a failure and a tool of last resort.[92] This perspective likely contributes to the frequency with which agencies fail to file for termination of parental rights in accordance with the 15 of 22 rule. While it may be appropriate in some cases to allow parents more time to reform, agencies must not fail to consider a child's sense of time and his or her developmental needs, which may not fit with the parent's recovery timeline. It is common for parents of children in foster care to have to work through drug addiction, for example, which can be a long process and one that varies in length by individual.[93] If a parent is not progressing through the various stages of recovery or is failing to comply with their recovery plan, children should not be required to languish in temporary placements.

It is especially important agencies do not delay permanency for infants. Developing a secure attachment to a caregiver during infancy is critical to healthy child development.[94] Languishing in a temporary foster care setting can

interfere with this stage. Earlier versions of the *Adoption and Safe Families Act* included timelines for termination of parental rights based on a child's age, but this provision ultimately failed.[95] However, states have the authority to implement shorter timelines for termination of parental rights than the federal law dictates.

*Poor Incentives in the Federal Foster Care Funding Structure*

Another factor leading to increased time in foster care may have to do with how federal Title IV-E foster care funding is allocated to states. Title IV-E is an open-ended entitlement, meaning that states receive funding based on the number of children in their foster care system. Because states receive more funding for having a larger foster care caseload, states may be incentivized to keep their foster care caseloads high rather than to move children into permanent placements in a timely manner.[96]

*Non-Compliance with the Multiethnic Placement Act*

Furthermore, some agencies' failure to comply with the *Multiethnic Placement Act* may increase the time children spend in foster care. The *Multiethnic Placement Act* was passed in 1994 and prohibits delaying or denying adoption placements based on race, color, or national origin. Although some research indicates that children adopted by parents of a different race may struggle with their racial identity, researchers also find that children in transracial adoptions have similar levels of self-esteem compared to children adopted by parents of the same race.[97] Overall, the research appears to indicate that children in transracial adoptions adjust as well as children adopted by same-race parents.[98] Agencies have violated the *Multiethnic Placement Act* at times, however, and anecdotal evidence suggests that some agencies continue to circumvent this law.[99]

In the early 2000s, the U.S. Department of Health and Human Services' Office of Civil Rights found that Ohio and South Carolina were violating the *Multiethnic Placement Act* in various ways, including subjecting parents to a higher level of scrutiny if the parent was a different race than the child, assessing the racial composition of the neighborhood of prospective foster families, and matching children with parents based on skin tone.[100] Prospective foster parents complain of similar problems happening today in some agencies.[101] In a 2008 study of social workers in child welfare, researchers found that nearly two-thirds said that using race as a factor in adoption placement is an ongoing practice.[102] Unfortunately, failure to comply with this law could leave children to languish in foster care longer than necessary or even deny children an adoptive home.

## RECOMMENDATION: PROVIDE QUALIFYING FOSTER CHILDREN WITH PERMANENT ADOPTIVE PLACEMENTS

Federal and state governments can implement several reforms to increase the number of qualifying foster children in permanent adoptive placements.

### *Require States to Collect Data on Use of the 15 of 22 Rule and Implement Fast-Track Provisions for Young Children*

While the Child and Family Services Review asks states to report on their use of the 15 of 22 rule, states are not required to collect data on agencies' compliance with the rule. States should be required to collect and report data regarding how the 15 of 22 rule is used and be held accountable for violating the rule. President Trump's June 2020 executive order on foster care requires the secretary of the U.S. Department of Health and Human Services to assess states' compliance with federal timelines for termination of parental rights and reiterates that when states are not in compliance the secretary shall make use of his authority to withhold funding if states do not improve.[103]

In addition, Congress should hold hearings to understand how the 15 of 22 rule in the *Adoption and Safe Families Act* is being implemented. They should examine whether the frequent use of exceptions to the 15 of 22 rule is appropriate or whether states are bypassing the rule in cases when it should be applied. Furthermore, Congress should examine why states rarely use the aggravated circumstances provision, which allows states to fast-track termination of parental rights when children have experienced extreme situations, such as chronic abuse or abandonment.

For infants in the foster care system, timely permanency is especially crucial, given the importance for infants to develop a secure attachment with a caregiver. States should implement shorter timelines for termination of parental rights for infants, rather than requiring infants to wait in foster care for 15 months out of a 22 month period. As an example, in Arizona drug abused infants are required to have a permanent placement within one year of entering the foster care system.[104]

### *Reform Funding to Improve Incentives*

The nature of Title IV-E funding should be changed so that it does not present a perverse incentive for states to maintain children in the foster care system. Rather than basing a state's foster care funding on the number of foster care children in their system, states should receive a fixed amount of funding based on the population of children in the state.

In addition, Congress should continue the Adoption Incentives Program, which is part of the *Adoption and Safe Families Act* of 1997. This program rewards states for increasing the number of children adopted from foster care above a baseline.

In 2014, Congress expanded this program to add rewards for increasing the number of children placed in guardianships.[105] However, adoption placements are usually better than guardianships, since guardianships do not confer full parental rights. Congress should return this program to solely an adoption incentives program, or at least make the reward for a guardianship placement substantially less than the amount rewarded for an adoption.

*Enforce the Multi-Ethnic Placement Act*

The *Multiethnic Placement Act* prohibits child welfare agencies from delaying or denying placement on the basis of race, color, or national origin. President Trump's June 2020 executive order on foster care requires the secretary of the U.S. Department of Health and Human Services to conduct a study on how the *Multiethnic Placement Act* is being implemented nationwide, and also requires the secretary to update guidance on the implementation of the *Multiethnic Placement Act*.[106] These are good steps forward. Additionally, Congress should require states to collect data on courts' compliance with the *Multiethnic Placement Act* and report that data to the U.S. Department of Health and Human Services. States that fail to comply with the requirements of the *Multiethnic Placement Act* should have their Title IV funding reduced proportional to the frequency with which their courts are failing to comply with the law.

*Ensure that Foster Parents Are Aware of the Laws*

If foster parents are aware of the 15 of 22 rule and the provisions of the *Multiethnic Placement Act*, they will be able to help keep agencies accountable, as foster parents are one of the parties directly affected by these laws. If foster parents are informed, they can be whistleblowers if agencies fail to terminate parental rights in a timely manner or if agencies are delaying or denying foster or adoption placements on the basis of race. President Trump's June 2020 executive order on foster care requires the secretary of the U.S. Department of Health and Human Services to "publish guidance regarding the rights of parents, prospective parents, and children with disabilities (including intellectual, developmental, or physical disabilities)."[107] In addition to this, Congress should require agencies to inform prospective and current foster parents about the *Multiethnic Placement Act* and the 15 of 22 provision in the *Adoption and Safe Families Act*.

## ISSUE 5: INFANT ADOPTION IS MISUNDERSTOOD AND UNDER-SUPPORTED

The largest age group of children entering the foster care system are children under the age of one.[108] In FY 2018, 19 percent of children entering foster care were less than a year old. Furthermore, children under the age of one are the most likely to be maltreated and approximately half of all fatalities from child abuse are among children under the age of one.[109] While many infants who enter the foster care system will reunite with their parents, many will be placed in adoptive homes.[110] Over a quarter of the children in the foster care system waiting for adoption are children who entered foster care when they were less than a year old.[111]

While infants make up a large portion of children who enter the foster care system, infant adoption is rare, and infant adoption has dropped significantly over the last several decades.[112] Only five percent of children adopted from foster care were under the age of one in 2018.[113]

Some children who end up in foster care within their first year of life would likely have been better off if they would have been placed for adoption at birth rather than removed from their homes shortly thereafter due to abuse or neglect. While there were about 18,000 infant adoptions in the United States in 2014, more than twice that number—45,535 children under the age of one—entered foster care that year.[114]

Helping women understand that adoption is a potentially beneficial option when they are not prepared or willing to parent may help reduce the number of infants who end up in the foster care system or experience abuse or neglect. Women sometimes express negative perspectives on adoption, however, although their concerns may be based on a lack of information.[115] Researchers find that expectant mothers who prefer not to be a parent (in that they were seeking an abortion but were denied one because they were too far along in their pregnancy) often believe it is not right to give up their child or that there are already too many children waiting for adoption. Some women also express fear that they would constantly be worried about their child's wellbeing.[116]

It may help expectant mothers to know that the vast majority of adoptions today are open adoptions or semi-open adoptions, meaning that birth mothers can have at least some contact with their child.[117] Furthermore, expectant mothers may be more likely to consider adoption when they know that there are many families looking to adopt. According to the 2015-2017 National Survey of Family Growth, over 900,000 women are currently seeking to adopt, which is far more than the number of infant adoptions that take place (just over 18,000 in 2014).[118] Also, it may help women to know that while mothers who place their child for adoption do report grief, the majority ultimately say they are satisfied overall with their decision.[119]

*Recommendation: Support Infant Adoption Awareness*

The federal government used to fund the Infant Adoption Awareness Training program, which was implemented to address a lack of adoption awareness among pregnancy counselors.[120] The program was established in the *Public Health Services Act* of 2000 for the purpose of providing information about adoption to expectant mothers who receive services from government and private pregnancy clinics "on an equal basis with all other courses of action included in nondirective counseling for pregnant women." The program provided funding for staff in public and non-profit health clinics that serve pregnant women, including Title X family planning clinics and federally funded health clinics.

However, in 2011 the Obama Administration shifted funding for the Infant Adoption Awareness Training program into the Adoption Opportunities program, which focuses on various strategies to promote adoption, such as promoting adoption for children in foster care. Unlike its predecessor, Adoption Opportunities is not designed specifically to support training on infant adoption for expectant mothers. In FY 2017 the Trump Administration authorized $750,000

in Adoption Opportunities funding for Hospital-Based Adoption Support Services. This grant supports training for hospital staff who provide pregnancy and adoption information and referrals, and the grantee uses a curriculum from the Infant Adoption Awareness Training program.[121]

Congress should consider whether the Adoption Opportunities program is effective and whether some of its funding should be diverted back to the Infant Adoption Awareness Training program. Providing expectant mothers who have crisis pregnancies with information about adoption might help women who are not prepared or willing to parent avoid having their children placed in foster care down the road.

In addition to adoption counseling in health centers, states and communities could fund media campaigns to address common concerns or myths about adoption as well as to promote adoption as a positive option.

Some states require public schools to teach students about adoption, sometimes including this information in family life education or sexuality education courses.[122] More states should include information about adoption in their curriculums to help students understand that adoption can be a positive choice for those who may not be in place where they can parent. Utah, Virginia, Nebraska, Michigan, and Louisiana all have some type of adoption education requirement in their schools.[123]

## CONCLUSION

Hundreds of thousands of American children are in the foster care system and are in need of loving homes. Fortunately, many Americans are willing to provide care to children in need, and many private organizations throughout the United States, including faith-based organizations, lend their efforts to serve these children on a daily basis. Unfortunately, the system designed to help children sometimes presents significant barriers to connecting children with those willing to provide loving homes. Furthermore, by threatening the religious liberty protection for faith-based foster care and adoption providers, many state governments are hampering civil society's efforts to serve these children.

Child welfare agencies should work to support foster parents rather than neglecting them or making it harder for them to serve as foster parents. Federal, state, and local government should protect faith-based organizations' ability to provide foster care and adoption services to children in need. Furthermore, courts and child welfare agencies should work to move children into permanent placements in a timely manner, rather than allowing children to languish in the foster care system. Leaders should also support and promote infant adoption as a positive option when expectant parents are unlikely to be able to provide safe homes.

Children in the foster care system face a significant social capital deficit. Fortunately, many Americans are willing to open their hearts and homes to enrich the lives of these children and to see that they are not permanently left alone. Increasing the opportunity for disconnected children to find loving bonds should be a priority of civil society and government.

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# Connecting More People to Work

# Reconnecting Americans to the Benefits of Work

SCP REPORT NO. 5-21 | OCTOBER 2021

## INTRODUCTION

Employment during our working years provides the income that affords us the things we value in life and most Americans work hard to put food on the table every day. But while few people would profess that they live to work, it is also not the case that most people simply work to live. Seven in ten workers say they would "enjoy having a paying job even if I did not need that money," and over a quarter affirm that their "main satisfaction in life comes from work."[1]

Workers derive meaning and purpose from employment. The workplace offers the chance to associate with others and form affirming and satisfying relationships. Those relationships provide material and immaterial benefits to workers; that is to say, they constitute valuable social capital.

In the absence of work, people and communities suffer. Those outside the labor market (neither working nor looking for work) fare worse than their employed counterparts, as we found in our report, "Inactive, Disconnected, and Ailing: A Portrait of Prime-Age Men Out of the Labor Force."[2] Prime-age men who are out of the labor force are more socially isolated and less happy than employed men. At the community level, the disappearance of work can lead to depopulation, brain drain, and the decline of other institutions of civil society.

Unfortunately, American men have become increasingly disconnected from the world of work, a trend going back many decades. As the American Enterprise Institute's Nicholas Eberstadt noted in his May 2019 testimony before the Joint Economic Committee, the employment-to-population ratio for prime-age men is near levels seen in the Great Depression-era.[3] Among women, a long, steady increase in labor force participation also reversed course over the past twenty years.

In June 2020, the National Bureau of Economic Research officially demarcated February 2020 as the start of the pandemic-induced recession.[4] Much of the content in this report will refer to a timeframe that preceded the pandemic, with recognition that we have much left to learn about the effects it will leave behind on our health, communities, and economy. We can only speculate how much the pandemic will change the world of work. Whether temporary or long lasting, the economic disruptions may accelerate promising pre-pandemic trends such as more flexible work options and remote work, while also possibly compounding the decades-long decline in male labor force participation and other labor market

trends. In September 2021, overall employment remained about five million jobs short of its pre-pandemic level, a worrying sign for many Americans' connection to work.

Although this report mainly focuses on the pre-pandemic period, understanding this history is critical to understanding the future of the labor market. This report summarizes trends in the American labor market, considers the possible explanations for declining labor force participation, and explores a number of possible reforms that could promote employment for the able-bodied. It is primarily concerned with prime working-age adults (ages 25 to 54) whose disconnection from the world of work is not due to their getting an education, being happily retired, preferring to raise a family, or being physically or mentally incapable of work. Many women and men outside the labor force lead productive, valuable, and happy lives, however, work does seem to increase life satisfaction, social connectedness, and self-esteem.[5] Work is a means to promote wellbeing, not an end in itself. At the same time, no one has the right to expect taxpayers to support them if they are able to support themselves and their families but choose not to work.

The reasons that so many men have fallen out of regular employment is important. One worrying hypothesis is that declining employer demand for workers, especially low-wage workers, has depressed wages and diminished the market incentive to work. As this report will argue, there is stronger evidence that a shrinking supply of labor is the dominant trend, as more workers choose not to supply their labor due to changing preferences and external incentives. Less labor market work among students, full-time parents, or early retirees is not an immediate concern. Rising inactivity among men with the capacity for independence who subsist in large measure on government transfers requires careful reforms to encourage a return to the self-sufficiency of work.

Our examination of disconnection from work begins with an overview of trends that affect the supply of and demand for labor.

## A TRANSFORMED LABOR FORCE

The U.S. labor force evolved in countless ways over the course of the last century and through the beginning of the twenty-first century. The most notable changes include:

- An aging workforce (and an aging population more generally),
- Increasing participation of women in the labor force,
- Rising educational attainment among Americans,
- Growth in the share of the workforce comprised of immigrants,
- A technology and trade driven shift from a largely agrarian economy, to one dominated by industrial production, to an economy primarily involving services,
- Changes in the skill requirements of jobs, and
- Increasing numbers of men disconnected from the labor force.

*Skewing Older Over Time*

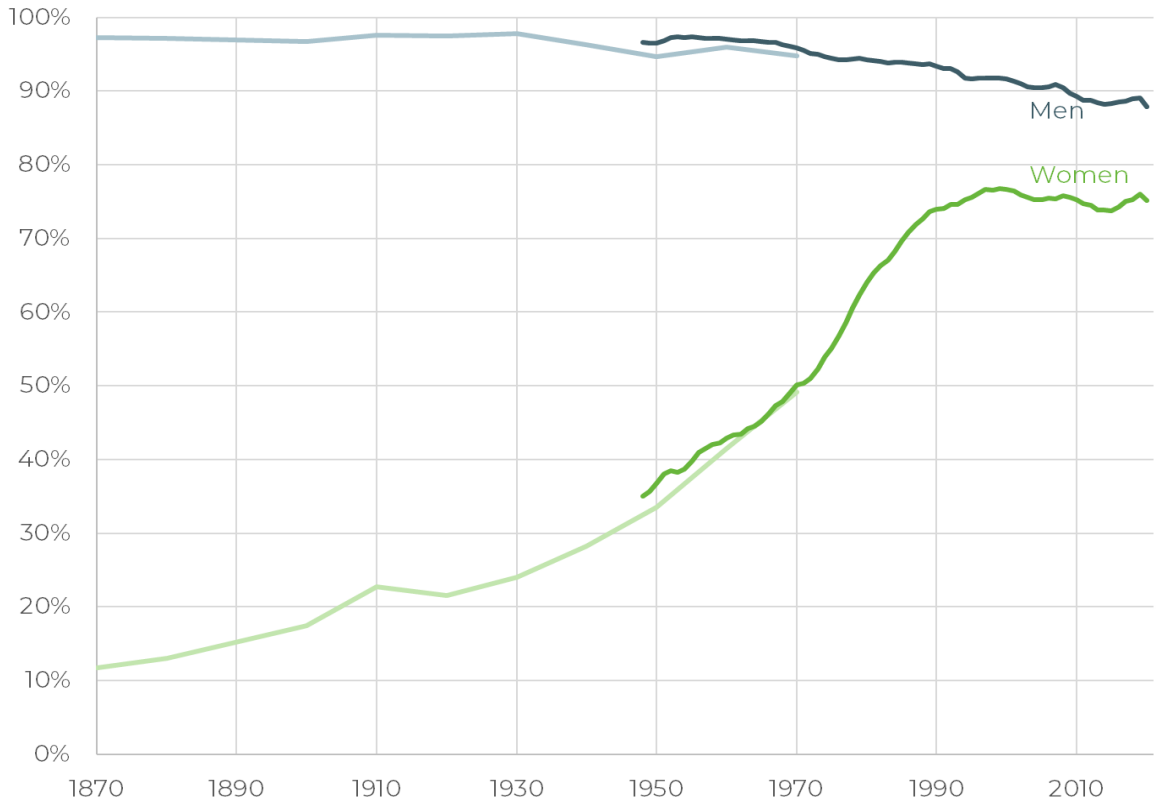
The Bureau of Labor Statistics (BLS) reports that, since the late 1990s, older workers remained in the workforce longer while the youngest workers are increasingly delaying entry.[6] As older Americans delay retirement, BLS projects that workers aged 65 and older will account for 8.6 percent of the workforce by 2026 (up from 5.8 percent in 2016). Older Americans with more education are disproportionately extending their work lives because high-skill jobs themselves are usually more gratifying and less physically demanding.[7] As for younger Americans, most 16- to 19-year-olds, and increasingly 20- to 24-year-olds, are forgoing work in favor of obtaining additional years of formal education. As a result, the share of 16- to 24-year-olds not in education, employment, or training (referred to as NEET) remained largely unchanged between 1998 and 2014. However, the share of 16- to 24-year-olds with only a high school diploma who are NEET increased from 8 percent to 12 percent over the same period.[8]

Focusing on the prime working-age population (ages 25 to 54), as we do in the following sections, allows us to set aside these trends among the youngest and oldest workers, which are driven by changes in health, longevity, and school enrollment.

*More Women in the Labor Force*

Among the most consequential changes in the American economy has been the steady entrance of women into the labor force (Figure 1). Over the last half of the twentieth century, the female labor force participation rate (LFPR) more than doubled. Among prime-age women, it rose from 35 percent in 1948, to 45 percent in 1965, to 55 percent by 1975 and 65 percent by 1981. It peaked in 1999 at 77 percent, before temporarily declining, and in 2019 it neared the peak again at 76 percent. As American women steadily joined the labor force, their male counterparts slowly exited, a point we will discuss below. The pandemic reduced LFPR among prime-age women by a percentage point to 75 percent in 2020, about the same rate as in 2017. LFPR for prime-age men fell by more than a percentage point in 2020, dipping below 88 percent and marking a record low.

Figure 1. Prime Working-Age Labor Force Participation Rates by Sex, 1870-2020

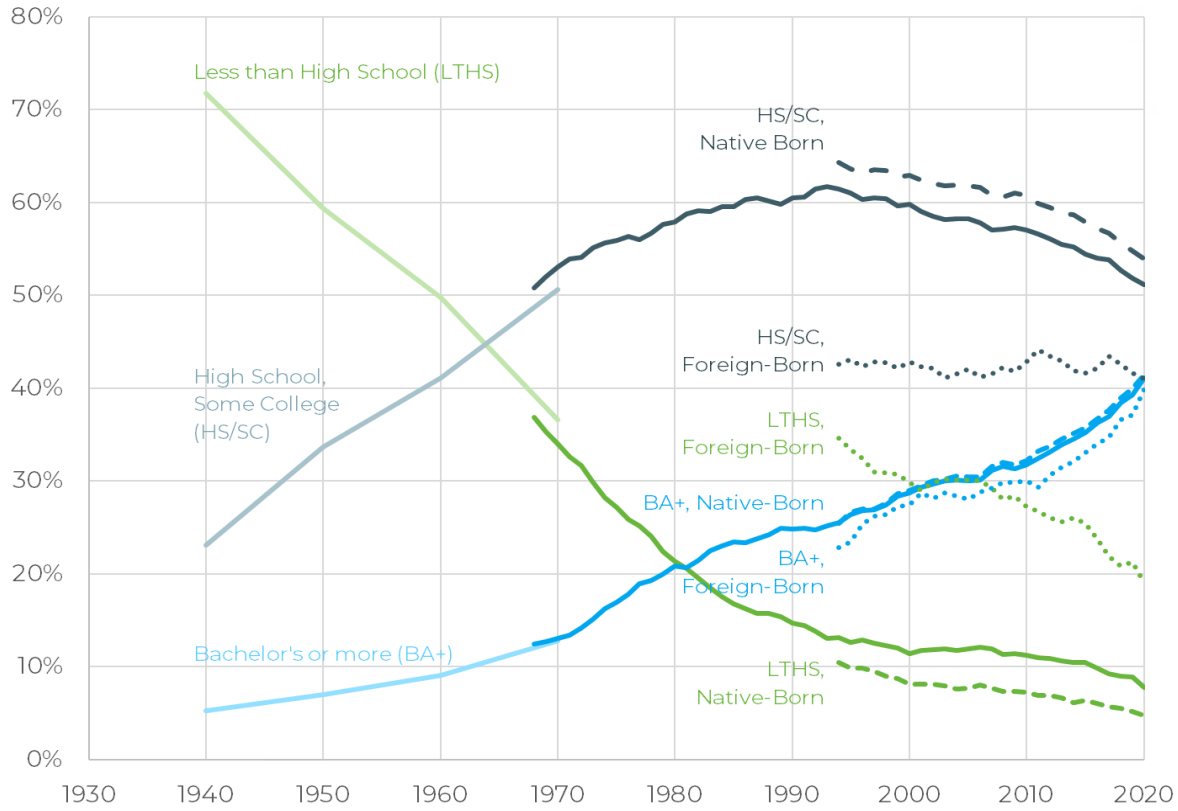



Source: Social Capital Project analyses of decennial census data and tabulations of Bureau of Labor Statistics estimates.[9]

*More Education and Changes in Participation by Education*

In 1940, only 5 percent of prime working-age Americans had been in college for at least four years, while 72 percent had less than twelve years of schooling (Figure 2).[10] The share with at least four years of college (BA+) more than doubled by 1970 to 13 percent and more than doubled again by 2000 to 29 percent. In 2020, 41 percent of prime working-age Americans have a bachelor's degree or a graduate degree. Over the same period, the share with less than twelve years of schooling fell to 8 percent and fell to 5 percent among native-born Americans. Today, the median prime working-age American has at least some post-secondary education, while in 1940 a similar person had no more than an eighth-grade education.

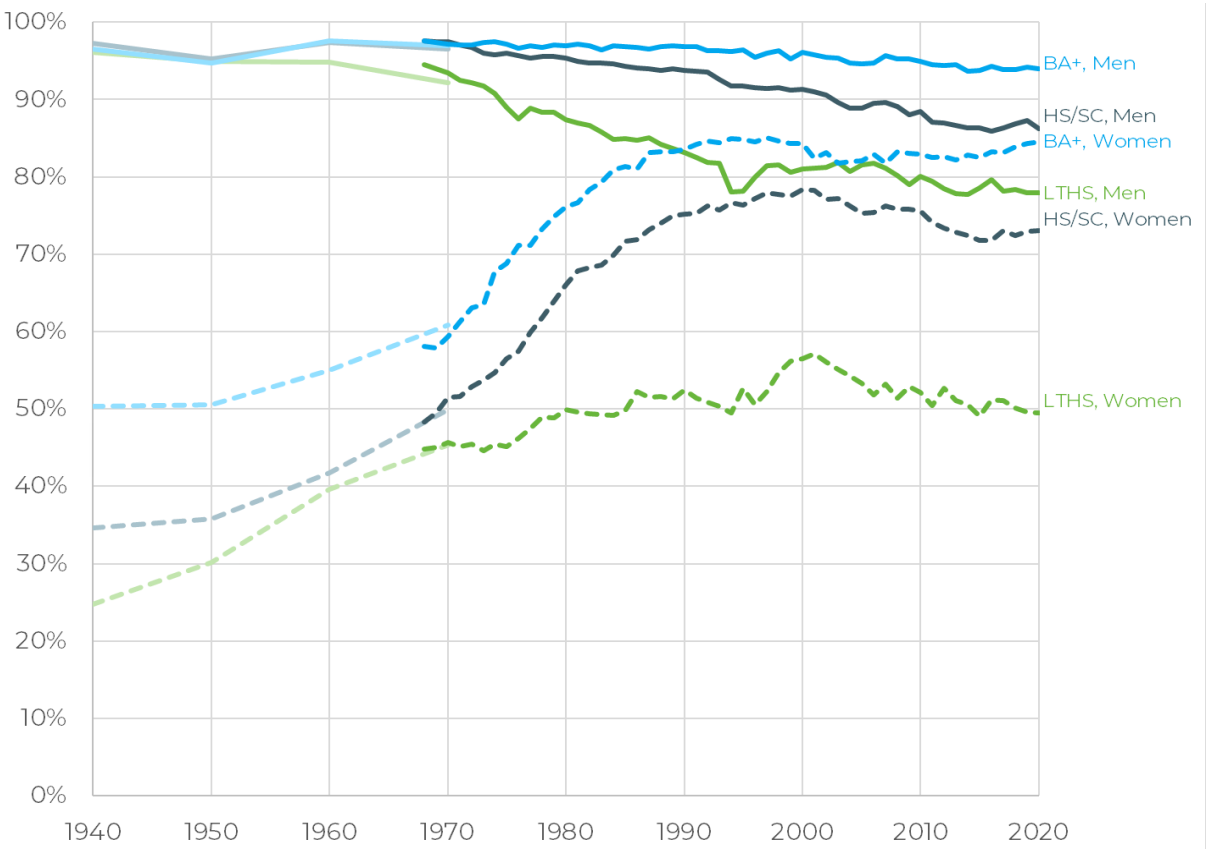
Figure 2. Composition of Prime Working-Age Educational Attainment, 1940-2020




Source: Social Capital Project analysis of decennial census and Current Population Survey data. See endnote 9.

As Americans have become more educated, labor force participation trends differ for those with more and those with less schooling. Figure 3 shows that labor force participation rises with education, and the participation trends for men and for women follow the same broad pattern as in Figure 1, regardless of education level. However, the decline in male labor force participation and rise in female participation vary by level of schooling.[11]

Figure 3. Prime Working-Age Labor Force Participation by Sex and Educational Attainment, 1940-2020




Source: Social Capital Project analysis of decennial census and Current Population Survey data. See endnote 9.

In 1940, labor force participation was nearly identical for prime working-age men across all education levels, differing by just 1 percentage point. By 2020, participation had only declined to 94 percent for men with a bachelor's degree, but fell to 86 percent for those with a high school diploma or some college attendance, and 78 percent for those with less than a high school degree.

Among women, participation in the labor force was unequal in 1940 across educational categories, but participation rose for all three groups through the 1990s. Women without a high school diploma fell behind other women over time. In 2019, the most educated women were near peak participation and were more likely to be in the labor force than the least-educated men. That remained true in 2020 as well, even as labor force participation rates declined across demographic groups.

Interpreting these trends is difficult because of rising educational attainment across the entire population. While Figure 2 does not break trends out by sex, in 1940, three in four working-age men lacked a high school diploma, and barely one in 20 had a bachelor's degree. Today, just 9 percent are in that lowest category and over one-third have at least a bachelor's degree. Labor force participation fell

substantially among men who drop out of high school, but very few men drop out today, and therefore those that do drop out may be presumed to be less attractive employees relative to men in 1940 who did not graduate high school. Similarly, college graduates are a less rarified group today than they were in 1940, so it may be unsurprising that their labor force participation rates fell somewhat. Educational trends for women are similar. We will return to the complications raised by trend analyses for different educational groups when we investigate wages below.

### *Larger Foreign-Born Population*

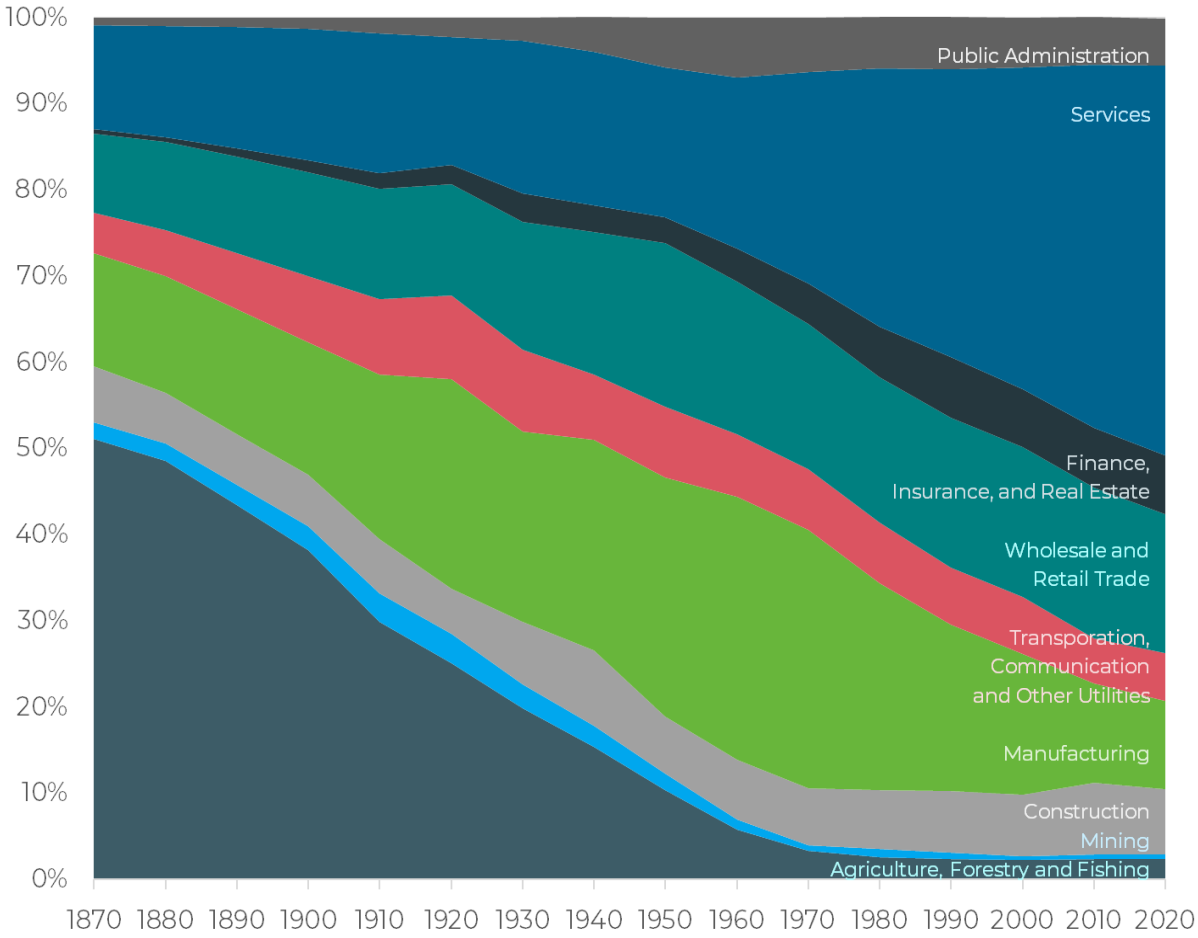
Trends for those with less than a bachelor's degree would look even worse if not for the higher rates of labor force participation among the foreign-born population. This group can be tracked only since 1994, but the foreign-born share of the working-age population roughly doubled since then, rising from under 12 percent to 22 percent in 2020.[12] Between 1994 and 2020, the labor force participation rate among working-age native-born men without a high school diploma fell from 74 percent to 65 percent, but among their foreign-born counterparts, participation rose from 87 to 90 percent. That was nearly as high as the participation rate in 2020 of native-born male college graduates (94 percent).[13]

As shown in Figure 2, the foreign-born working-age population is about as likely as native-born Americans to have a bachelor's degree or more, but it is much less likely to have a high school education. In fact, roughly half of working-age men without a high school diploma today were born outside the United States. Due to low birth rates among native-born Americans, it is expected that by 2024, immigration will account for the majority of U.S. population growth, which will continue to change the education composition and average wage measures of the labor force.[14]

### *Shift from Production to Service*

The share of jobs in agriculture and related services fell from over half of prime-age labor force participants in 1870 to less than one in twenty by 1970 (Figure 4).[15] Though the share was continuously falling, the number of workers in agriculture peaked in 1910. In fact, there were more agriculture-related workers in 1950 than there were in 1870, and there are only 25 percent fewer today.[16] Rather than the agricultural sector shrinking in absolute terms, it simply grew by much less than other sectors and much less than the total workforce. Similarly, the largest share of prime-age workers were in manufacturing between 1930 and 1970, with a peak in 1960, yet the number of prime-age manufacturing workers peaked in 1990. Today there are still more manufacturing workers than in 1950.[17] Since the 1960s, manufacturing lost ground relative to the service sector and wholesale and retail trade industries.

Figure 4. Distribution of Employment by Industry among Prime-Age Workers, 1870-2020

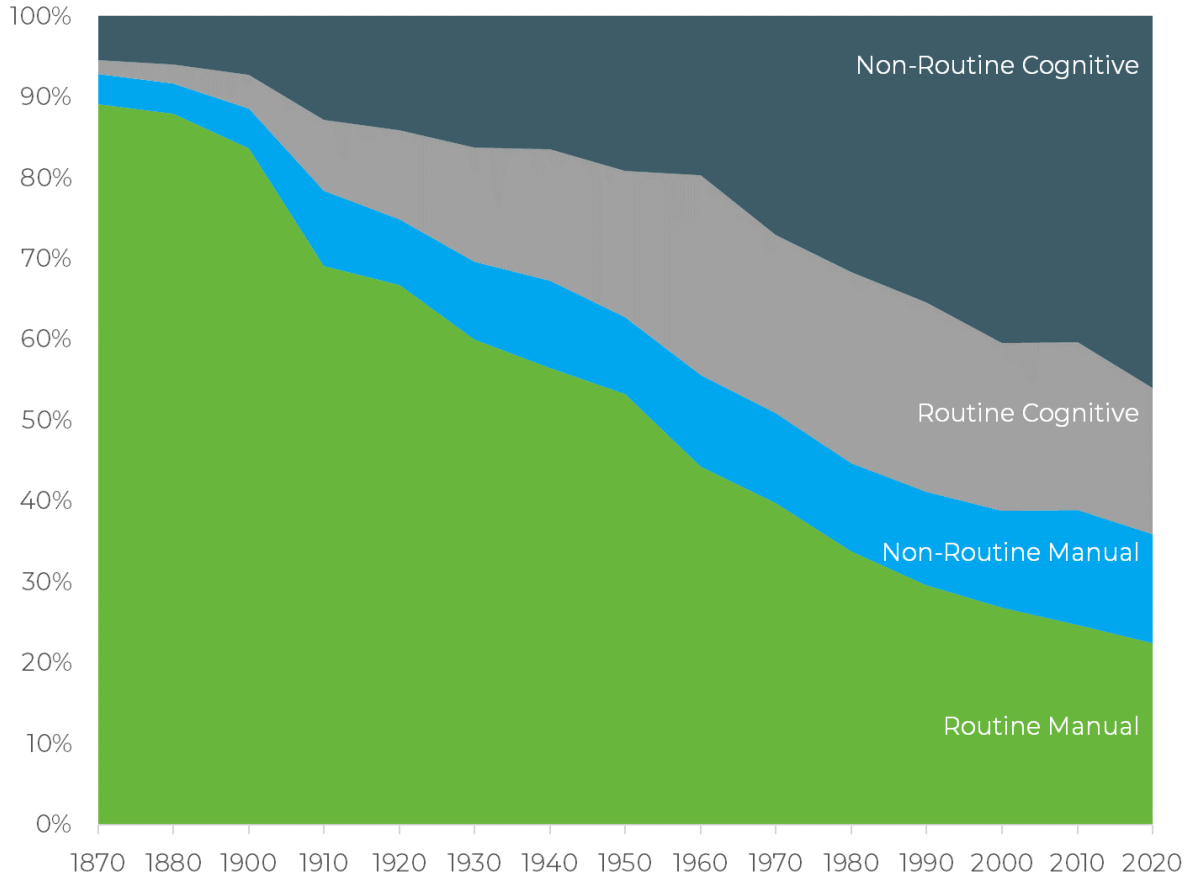



Source: Social Capital Project analyses of decennial census and Current Population Survey data. See endnote 14.

### *Shifts in the Skill Requirements of Jobs*

Occupational skills are most often organized along two dimensions, grouping occupations into four types: non-routine cognitive (management, professional, and technical jobs), non-routine manual (service jobs), routine cognitive (sales and office jobs), and routine manual (production, transportation, materials moving, natural resources, construction, and maintenance jobs).[18]

Figure 5. Distribution of Employment by Occupational Skill Set among Prime-Age Workers, 1870-2020




Source: Social Capital Project analyses of decennial census and Current Population Survey data. See endnote 16. "Routine manual" includes production, transportation, materials moving, natural resources, construction, and maintenance jobs. "Non-routine Manual" includes service jobs. "Routine Cognitive" includes sales and office jobs. "Non-routine Cognitive" includes management, professional, and technical jobs.

Over the long run, the clear picture is a decline in the number of routine manual jobs relative to cognitive jobs, especially non-routine cognitive jobs.[19] Non-routine jobs, both cognitive and manual, grew faster over recent decades than jobs that involve routine work.[20] In 1960, just under half (44 percent) of prime-age workers were in routine manual jobs, compared with just one-fifth (20 percent) in non-routine cognitive jobs. In 2020, those figures have flipped: 23 percent of prime-age workers are in routine manual jobs and 45 percent are in non-routine cognitive jobs, as shown in Figure 5. This reversal corresponds with changes in the educational attainment of the prime-age workforce. Figure 2 shows that from 1960 to 2020, the share of the prime-age population with less than a high school education fell from around 50 percent to less than 10 percent, while the share who graduated from college rose from less than 10 percent to 40 percent.

*The Rise of "Disconnected Men"*

Prime-age men's LFPR peaked at over 97 percent in 1955, slowly declined to 90.5 percent in 2008, and then dropped to 88 percent by 2014, as indicated in Figure 1. It inched up from there, but pre-pandemic it was only 89 percent in 2019. With the onset of the pandemic-induced recession in 2020, prime-age male labor force participation fell below 88 percent in April 2020, a record low. The pandemic may have worsened decades-long trends in declining workforce attachment, especially among lower-income prime-age workers.[21]

Men who are not in the workforce are also increasingly less likely to seek employment. Since 1964, there have been more jobless prime-age men who are not looking for work than jobless prime-age men who are actively looking for employment. This has been true in every year except 1982 and 1983. Even during the COVID-19 pandemic when unemployment reached 14.8 percent, on an annual basis, the growing population of inactive men still outnumbered those actively looking for work in 2020.[22] Until the early 2010s, there were typically only one or two inactive prime-age men who were not looking for work for every one prime-age man looking for work. In 2019, there were four times as many prime-age men out of the labor force as there were unemployed and looking for work.[23] Inactivity among prime-age men has risen over time, and risen significantly in the more recent past.

Prime-age men not looking for work are unlikely to have recent ties to an employer and are unlikely to have recently engaged in looking for work. One study found that among prime-age men out of the labor force in a given week in 2015, only 17 percent had participated in the labor force at some point in the previous year.[24] The proportion of prime-age men with these weakened ties or no recent connection at all to work or looking for work is growing. The share of men in their prime working years who neither worked nor looked for work in the previous year rose from 4 percent in 1976 to 10 percent in 2019.[25] These men are disconnected from work altogether.

Another way to think about the inactive population is by differentiating between workers who are entirely inactive and those who cycle in and out of the labor market. Economist John Coglianese finds that these "in and out" workers account for anywhere between 20 percent and 40 percent of the decline in participation among prime-age men between 1984 and 2011.[26] Our research suggests that men who cycle in and out of the labor force are concentrated in households with another worker.[27] By comparison, men who drop out entirely are more likely to live alone and receive transfer income, or government benefits.[28]

A large majority of the out of work force prime-age male population, 82 percent, does not have a bachelor's degree.[29] In the last twenty years, inactivity rose the most among men without a college degree and among those who previously earned low wages.[30] These men are disproportionately likely to live in rural localities—particularly in the Southeast.[31]

## COSTS OF DISCONNECTION

While each of the labor market trends above are interesting and interrelated, the unprecedented rise of disconnected prime-age workers will be a major focus of the remaining report. For men, this trend goes back half-a-century. Receding female workforce participation began in the last few decades. Mothers may have experienced some of the largest employment impacts of the coronavirus pandemic, although early data suggests employment has since rebounded considerably for women, bringing their employment losses in line with those experienced by men.[32]

Many men outside the labor force have legitimate reasons, including school, retirement, or taking care of home and family—in 2017, 13 percent were in school, 9 percent were taking care of family members or homemakers, and 6 percent were retired. Still many other men outside the labor force are unambiguously disabled, and others receive disability payments but would have worked in past eras—as of 2017, just under half (47 percent) of prime-age men out of the labor force described themselves as disabled. Still, about a quarter (24 percent) of inactive men fall into none of the above categories.

For men in the latter category, labor market disconnection represents a tremendous loss of economic potential, and carries equally steep social costs. Rather than channeling time toward community-supporting activities (volunteering or caring for loved ones) or self-improvement (education or job training)—disconnected men tend to withdraw. In "Inactive, Disconnected, and Ailing," the Social Capital Project reported that disconnected men are twice as likely as employed men to say that they do not get invited to do things, would find it hard to get help with a move, and do not have someone available to share fears and worries.[33] Only half are married and living with a spouse—compared to two-thirds of employed men—and a quarter live alone.[34] They spend nearly 30 percent of their time alone and fill much of their days consuming media through television, video games, and the internet.[35]

Prolonged idleness can bring terrible consequences. Many disconnected men subsist on government benefits while their skills atrophy and their potential as workers, husbands, fathers, and citizens diminishes. Detached from the labor force, these men lose what work brings: economic independence, but also the respect of others and self-assurance associated with it. Survey data show that disconnected men are less satisfied, less happy, more stressed, and more depressed than their employed counterparts.[36]

This crisis cannot be attributed primarily to economic discouragement or an absence of available jobs. In February 2020, just two percent of prime-age men out of the labor force met the official definition of a "discouraged worker"—someone who wants a job, is available to work, and who looked for work in the past year but has not looked in the past four weeks due to economic reasons. In June 2020, that figure was still under three percent.[37] Only six percent of men who

were inactive throughout 2018 indicated that the main reason they did not work was that they could not find a job,[38] and the men who could not find a job account for very little of the rise in non-working men over the long run.[39] In fact, the evidence suggests that three quarters of men outside the labor force in a given week prefer not to work (at least at the jobs on offer).[40]

Many disconnected men experienced challenging childhoods and unstable home life. Interviews with 30-36 year-old men by the BLS found that "Nonworkers not only are more disadvantaged in many aspects of their current lives—such as education, health, incarceration, and finances—but they also were disadvantaged earlier in their lives in terms of family and neighborhood background."[41] Male non-workers were less likely to grow up with two parents, and more likely to have a mother who gave birth as a teenager, to experience higher neighborhood poverty, to experience gun violence between ages 12 and 18, and to be arrested before age 18. Many of these characteristics echo issues associated with family instability highlighted in the Social Capital Project report, "The Demise of the Happy Two-Parent Home."[42] The BLS data also suggests that health issues and incarceration are the two most likely explanations for the inactivity of prime-age men.[43] These non-workers are also more likely to be financially supported by a parent they live with and to receive government transfers themselves or with a spouse or partner.[44]

Men who are voluntarily out of the labor force presumably know best whether or not they would be happier working. Many of these men may be in school, full-time parenting, or enjoying early retirement. Policymakers should not worry about these men. To the extent that there are inactive men with the capacity for independence who subsist in large measure on government transfers, policymakers should prioritize removing disincentives to work from government programs and investigate other ways to encourage a return to work. The economy would be more productive and civil society more vibrant if inactive workers could be reintegrated into the workforce.

## EXPLANATIONS FOR DECLINING LABOR FORCE CONNECTION

Why are fewer prime-age Americans in the labor force? While the question sounds simple, the answer is far more complex. The explanations generally include some combination of declining employer demand for workers, especially for workers with lower levels of educational attainment, and shrinking supply, as more workers choose not to supply their labor, due to changing preferences or external incentives.

Many popular demand-side explanations blame weak wage growth, technological change, and international trade as key forces that have an outsized effect on workers without a higher education. There may be some truth in these accounts. Relative to those with high educational attainment, Americans with less schooling may be less in demand than they were fifty years ago. Properly analyzed, however, the evidence does not suggest that these demand-side forces have made it significantly more difficult to find well-paying jobs even for those with less-

marketable skills. Prior to the pandemic, the tight labor market delivered broad benefits to working Americans, with especially large wage gains accruing to the lowest wage workers.[45] Meanwhile, analysts often overlook explanations that emphasize changes in worker preferences, the incentives faced by workers who rely on government assistance, and other government-imposed barriers to work.

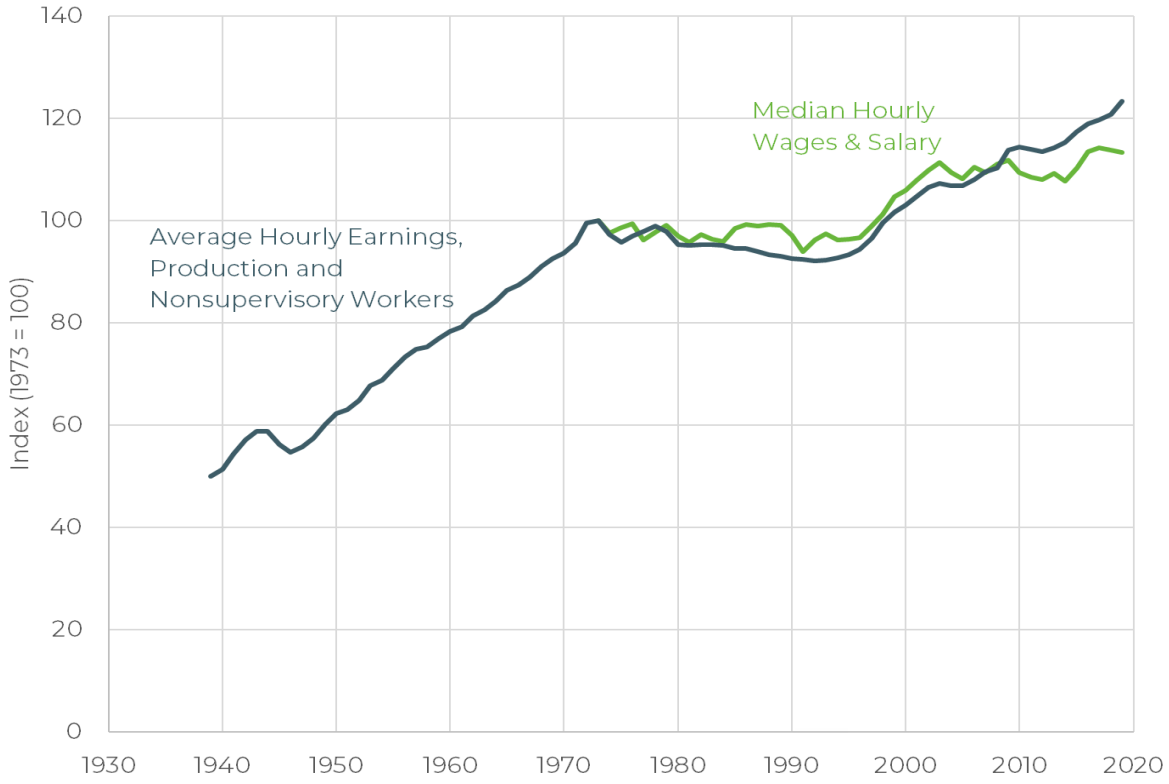
*Declining Pay for Workers with Less-Marketable Skills?*

If demand fell for workers whose skills command less in the labor market, we would expect that hourly wages should have fallen over time. And it is easy to find studies that report wages are indeed falling. One investigation in a leading economics journal recently reported, "for groups without a college degree, real hourly earnings were substantially lower in 2015 than they were in 1973" among prime-age men.[46] As we will see, while some measures of some men's pay declined from around 1970 through the early 1990s, they subsequently fully recovered, even among lower-wage workers. While relative stagnation is not cause for celebration, this finding does cut against the narrative that more men would be participating in the labor force if not for declining pay. Additionally, women's pay grew steadily during this time.

Analyzing wage trends is complicated due to changes in the makeup of the workforce over the years. The data for median wage and salary trends begins in 1973, making any longer-term trends for prime-age workers more difficult to determine. And given that 1973 represents a relatively high benchmark before declining until the 1990s, comparisons of wages today to 1973 obscure the growth since the early 1990s.

Figure 6 provides historical context. The chart shows hourly wage trends for the typical worker over the 80-year period from 1939 to 2019.[47] The trend line extending farthest back in time is not confined to prime-age Americans, but it is limited to subsets of private workers. It shows averages for these subsets in each year rather than medians. Fortunately, as is evident in the chart, this trend appears to be a good proxy for the median wage trend for prime-age workers, which is the shorter trend line in Figure 6.

Figure 6. Trends in Real Hourly Wages for the Typical Worker, 1939-2019




Source: Social Capital Project analyses. See endnote 47 for details.

World War II complicates the data from the earliest years, but from 1946 to 1973, wages rose 83 percent over 27 years after taking inflation into account, or 2.3 percent per year. From 1973 to 2019, median hourly pay rose just 13 percent over 46 years, or 0.3 percent per year.

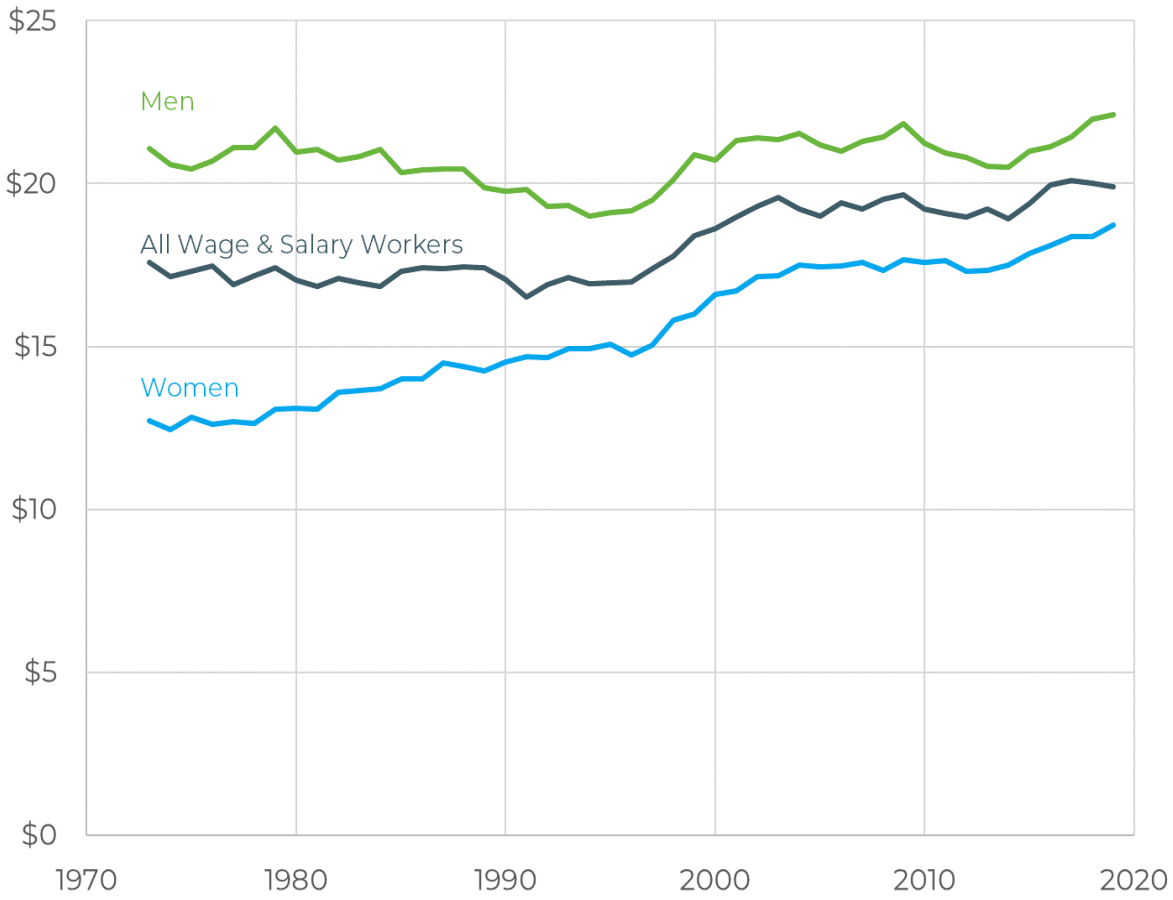
Note that a 13 percent change in the median does not mean that the typical worker in 1973 was only 13 percent better off after 46 years. The median worker is the one in the middle, better off than half of workers and worse off than half. The 1973 median worker was not still at the median in 2019. Most workers see their pay rise over time as they gain more experience and secure better jobs; a twenty-year-old in 1973 retiring at 66 in 2019 would only rarely have seen an increase in pay as low as 13 percent. A 13 percent change in the median simply means that the worker in the middle in 2019 was 13 percent better off than the worker in the middle in 1973.

Importantly, the period since 1973 encompasses two very different eras. From 1973 until 1991, median hourly pay actually fell six percent. But since 1991, it rose 21 percent. That amounts to an increase of only 0.7 percent per year, however—well short of the growth seen in the immediate post-war decades.[48] While the year 1973 constitutes an obvious inflection point for growth in pay, using 1973 as

a breakpoint for wage growth analysis systematically negatively biases post-1973 wage growth figures as compared to using any other year.

This overall post-1973 trend conceals variation important for interpreting changes in the labor force. The middle line in Figure 7 re-displays the trend in median hourly pay from Figure 6 and combines men and women. However, Figure 7 reveals that the experience of these two groups differed dramatically.[49] The pay of the typical woman, though lower than for the typical male worker throughout the period, rose by 47 percent from 1973 to 2019. It even rose in the earlier period—by 12 percent between 1973 and 1989 (both business cycle peaks). Undoubtedly, this increase reflects the increasing opportunities enjoyed by women over the 1970s and 1980s. Women—especially married women—moved into occupations beyond the traditional ones to which many were confined in an earlier era, and they accumulated more work experience than in the past.

Figure 7. Trends in the Real Median Hourly Wages of Prime-Age Workers by Sex, 1973-2019



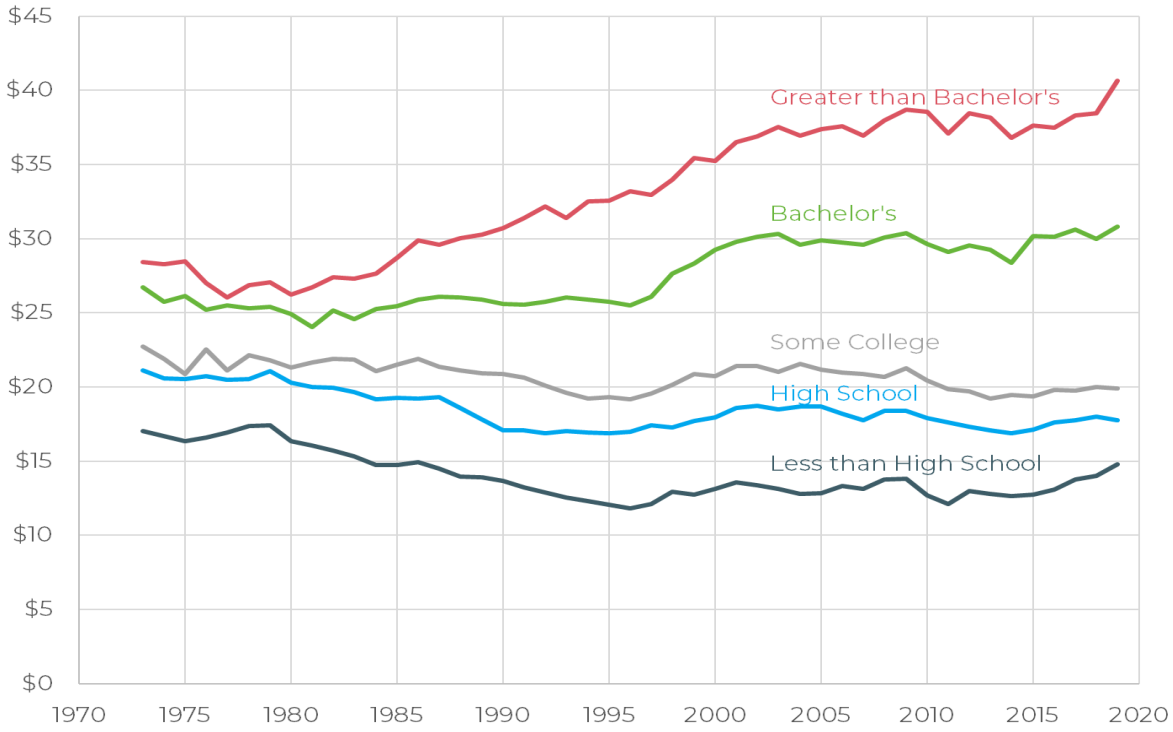

Source: Social Capital Project analyses of Current Population Survey data. See endnote 47 for details.

Among prime-age men, the story was less rosy. Pay rose by just 5 percent, and that reflects a recovery from a 21-year period of decline. At its low point, the hourly pay of the typical male worker had fallen by 10 percent. But from 1994 to 2019, men saw an increase of 17 percent—not far off of the 25 percent increase among women. Whatever the causes of wage "stagnation," they operated primarily to reduce wages among men during the 1970s, 1980s, and during the recession of the early 1990s. Despite the ups and downs of the business cycle, the trajectory of pay over the past 25 or 30 years has been upward for both men and women.

The rest of the wage analyses in this section focus on the pay of male workers, since their trends have been a significant driver of policy discussions around inactive workers and connections to work. Trends in women's pay and work participation are also an important topic of study. However, it is men who have experienced the biggest and longest-running declines in historical levels of work participation and some researchers claim these same men have experienced declining pay. Female workers have benefited from fairly consistent wage growth over the same time period.

To investigate the possibility of declining pay for some workers, researchers tend to focus not on overall wage trends but on the different trends among prime-age men according to educational attainment. Figure 8 displays median wage trends for prime-age men at five different levels of educational attainment.[50] The chart indicates that wages were lower in 2019 than in 1973 among men who lacked a four-year college degree—down 13 percent among those lacking a high school diploma, down 16 percent among those with a diploma but no other schooling, and down 12 percent among those with some college but no bachelor's degree. Between 1973 and 2019 wages rose 15 percent among prime-age men with a bachelor's degree but no graduate degree, and they rose 43 percent among those with a graduate degree.

Figure 8. Trends in the Real Median Hourly Wages of Prime-Age Men by Educational Attainment, 1973-2019

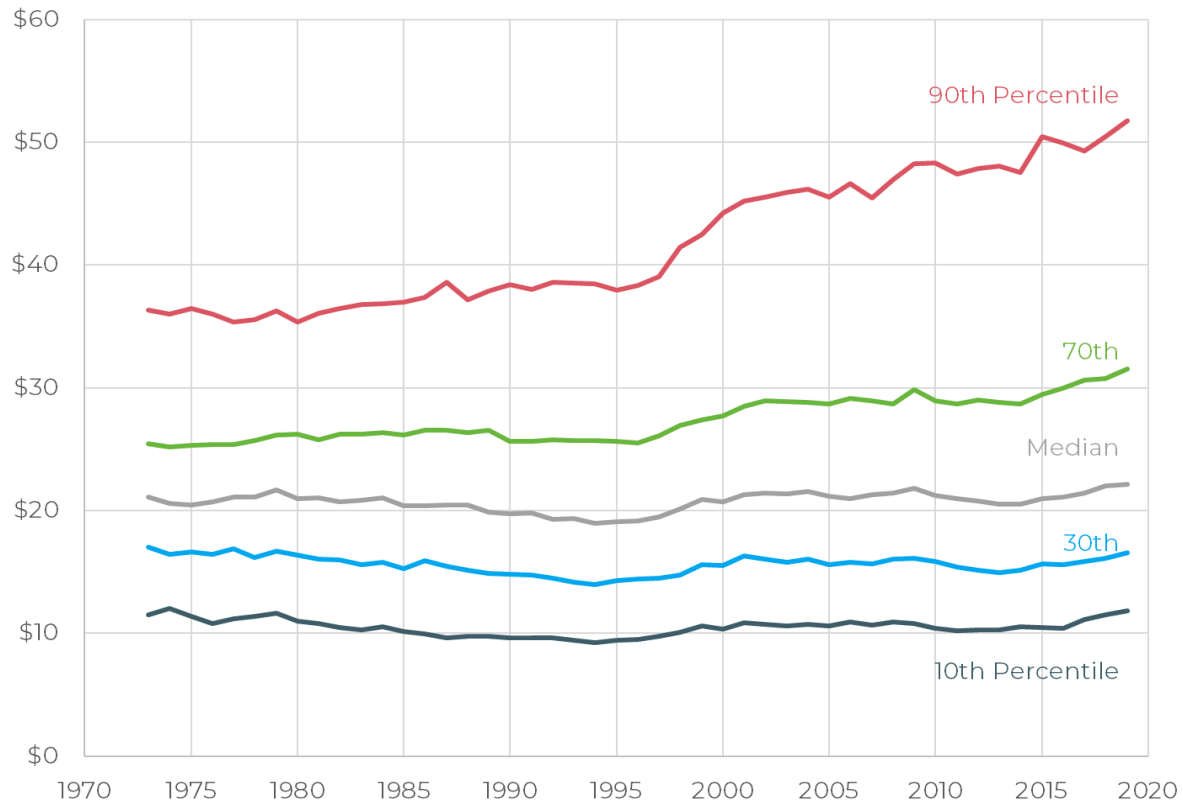



Source: Social Capital Project analyses of Current Population Survey data. See endnote 47 for details. Educational attainment is based on years of schooling completed through 1990 (less than 12, 12, 13-15, 16, more than 16) and on a combination of highest grade completed and degree attainment thereafter (first grade up to twelfth grade but without a diploma, high school diploma or GED, some college but no more than an associate's degree, bachelor's degree, master's/professional/doctoral degree).

However, analyzing wages by educational attainment ignores the fact that, as Figure 2 shows, the workforce is growing more educated over time which changes the composition of the education groupings. For instance, looking at men without a high school diploma means assessing the wages of the least-educated 30 percent of men in 1973 but the least-educated 10 percent of men in 2019. The group became much more disadvantaged over time, so all else equal, its pay would have fallen even if the pay of the bottom 30 percent did not. Similarly, in 1973, 19 percent of men were in one of the top two groups, but nearly 38 percent were in 2020. Therefore, the men in those top groups were less "elite" in 2020 than 47 years earlier.

A better way to assess wage trends for less- and more-advantaged workers is to look at wages at fixed points of the wage distribution. The median wage earner is the one in the middle of the distribution. The earner at the 10th percentile is the one with higher wages than 10 percent of workers but lower wages than 90 percent of workers. Figure 9 shows wage trends for prime-age men at different percentiles. As indicated above, the median male worker saw a wage increase of 5 percent between 1973 and 2019. Below the median, the 10th percentile of wages rose 3 percent, and the 30th percentile fell 3 percent. Above the median, wages grew by 24 percent at the 70th percentile and by 42 percent at the 90th.

Figure 9. Trends in the Real Hourly Wages of Prime-Age Men by Wage Percentile, 1973-2019



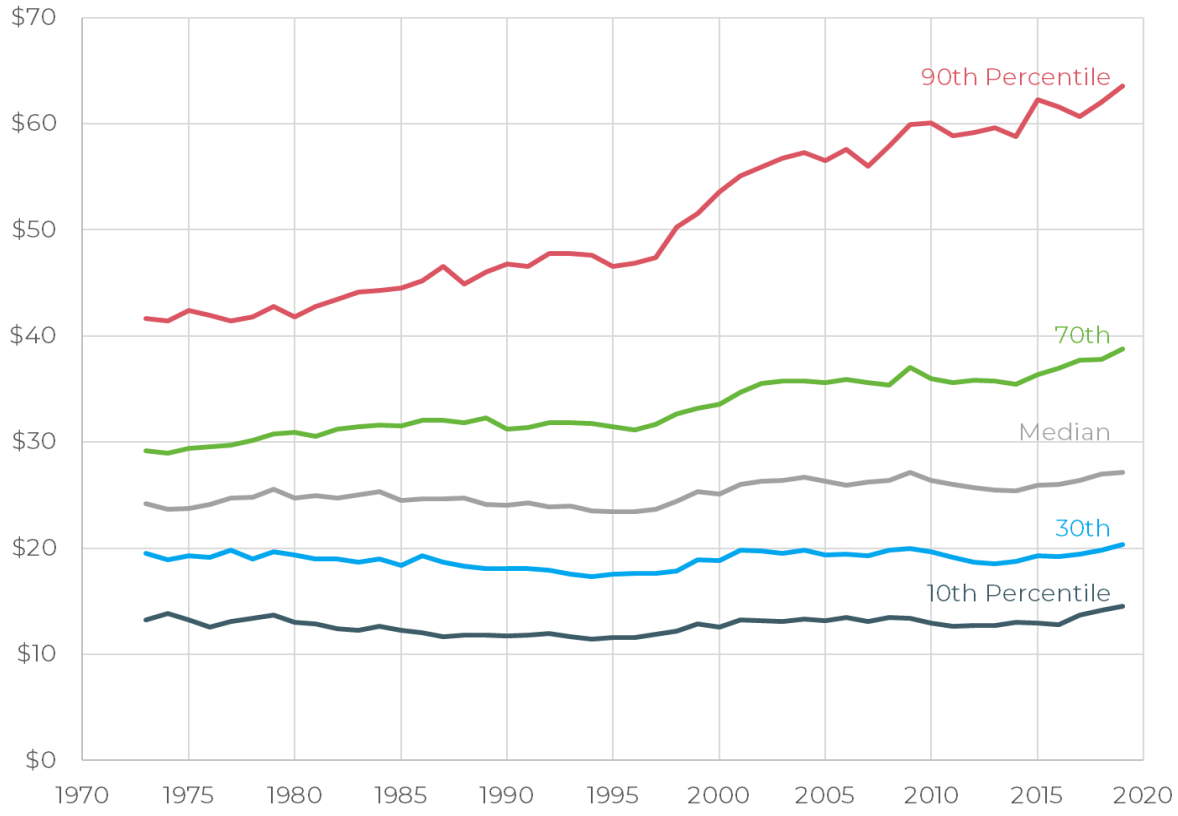

Source: Social Capital Project analyses of Current Population Survey data. See endnote 47 for details.

After 1994, the 10th percentile rose by 28 percent and the 30th percentile by 18 percent. Measuring from the high-water mark of 1973 to 1994, no one did well; even the 90th percentile of male pay rose only 6 percent, and the 70th percentile increased by just 1 percent. At the 10th percentile, hourly pay was 20 percent lower in 1994 than in 1973. The fact that men at the top did poorly over this period complicates explanations for wage stagnation that focus on manufacturing jobs, globalization, and the decline of union power, all of which usually predict wage divergence or polarization rather than a period of little change at all. Each of these explanations of wage trends tend to describe largely constant forces before and after 1994. Thus, theories that predict wage polarization or wage stagnation only among lower-wage workers struggle to account for the earlier period of consistent pay stagnation across all income groups. The sudden divergence in the mid-1990s does not fit the typical story.

Another issue missed by wage trends is that over time, non-wage compensation became a greater share of pay. Non-wage compensation includes employer contributions to employees' health and other insurance, contributions to retirement savings, and the payroll taxes they pay toward federal and state social insurance programs. These contributions were 13 percent of compensation in 1973 but 19 percent in 2019.[51] Figure 10 shows the same percentiles as in Figure 9,

but this time wages at each percentile are adjusted upward by the same factor to account for non-wage compensation growth.[52] This factor adjustment still likely underestimates the growth in compensation, particularly for the lower deciles for whom non-wage compensation often makes up a larger share of total compensation.[53]

Figure 10. Trends in the Real Hourly Compensation of Prime-Age Men by Percentile, 1973-2019



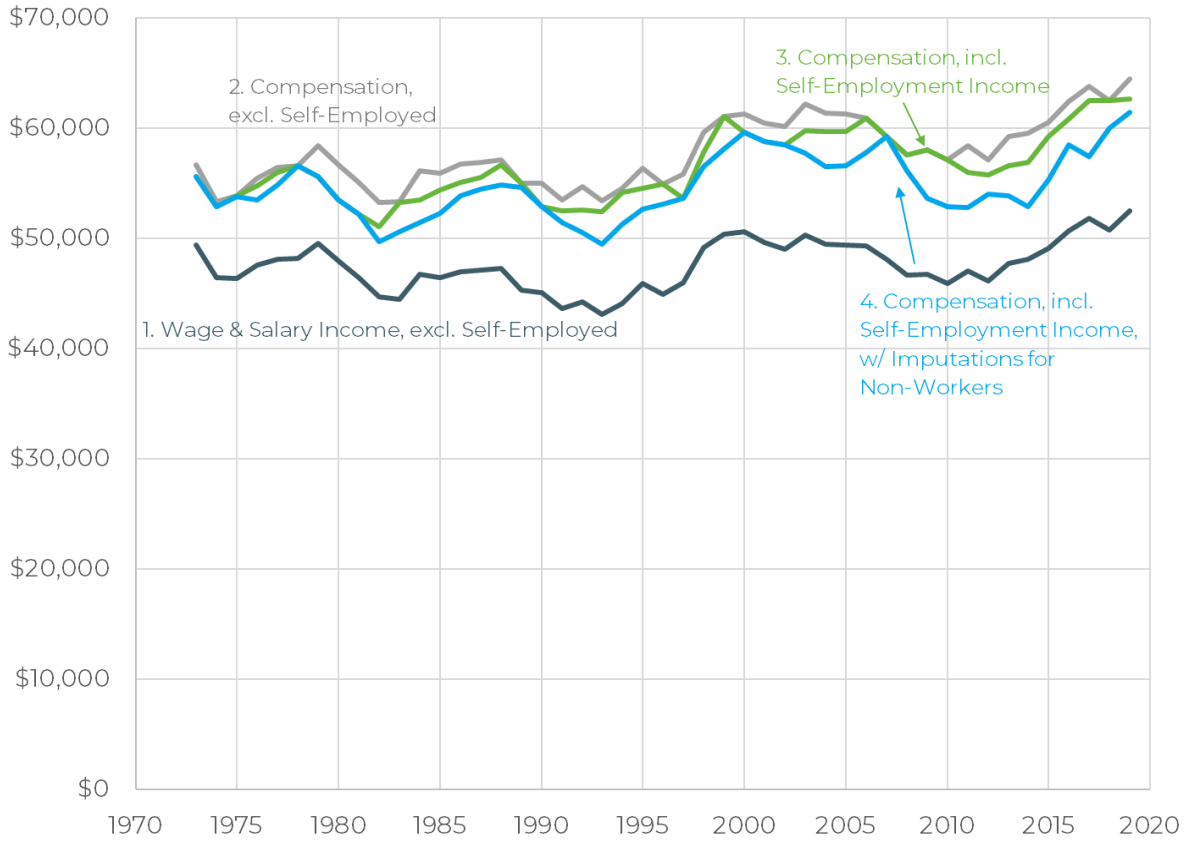

Source: Social Capital Project analyses of Current Population Survey data. See endnote 52 for details.

Broader measures of compensation show more growth than a simple accounting of only wages. While median hourly wages among prime-age men rose 5 percent from 1973 to 2019, median hourly compensation rose 12 percent. At the 10th percentile, wages rose 3 percent and compensation rose 10 percent during the same time period. Instead of falling, the 30th percentile of hourly compensation rose by 4 percent, and the 70th and 90th percentiles rose by 33 percent and 52 percent.

One potential problem with using hourly wage and compensation trends is that they fail to capture changes in the annual hours that prime-age men work. Further, they do not account for the self-employed. Annual compensation can measure financial well-being more accurately for some workers if they choose to work additional hours or take on part-time work to supplement their other income.

Rather than showing trends in hourly wages, Figure 11 displays the trend in median annual earnings.[54] Line 1 shows the trend in annual wage and salary income among those who have no self-employment earnings. From 1973 to 2019, the increase in the annual median was 6 percent, compared with a 5 percent rise in the median hourly wage of prime-age men. Adding nonwage compensation (Line 2) leads to a 14 percent increase (compared with 12 percent for hourly compensation).[55] It turns out that adding the self-employed (and their earnings) to this sample does not change that conclusion: median annual compensation (Line 3) rises 13 percent.[56] At the 10th percentile (not shown), median annual compensation (including the earnings of the self-employed) rose 4 percent, compared with 10 percent for the 10th percentile of hourly compensation among employees. In this case, lower annual compensation compared to the hourly measure is likely because more workers at the 10th percentile do not work consistently throughout the year or work fewer hours overall.

Figure 11. Trends in Real Median Annual Earnings of Prime-Age Men, 1973-2019




Source: Social Capital Project analyses of the Annual Social and Economic Supplement to the Current Population Survey. See endnote 54 for details.

A final criticism of the trends shown in this section is that we cannot observe the compensation of non-working prime-age males who have dropped out of the labor force. It may be that the only reason compensation seems to have risen is

because would-be workers with low compensation are more likely to drop out of the data. In this telling, demand for less-skilled workers may have fallen, but the charts above fail to show it because they only look at men who continue to work.

Line 4 of Figure 11 attempts to address this criticism by displaying a counterfactual trend. Respondents in the Current Population Survey data who did not work in the previous year are asked why they did not work. The possible answers include inability to find work, being sick or disabled, taking care of home or family, going to school, retirement, being in the Armed Forces, or "other." Imagine that nonworking men who were disabled, sick, retired, or said they were nonworking for 'other' reasons not listed did not become a larger group between 1973 and 2019 relative to workers. Further, imagine that all these additional men who would have been working would have been below-median workers had they held down jobs. Finally, imagine that in every year all men with no earnings who said they could not find work had worked at below-median compensation. Line 4 in Figure 11 attempts to say what the trend in prime-age male compensation would have been under those counterfactual circumstances.

According to this counterfactual trend, the annual compensation of prime-age men still would have risen by 11 percent (instead of 13 percent).[57] Note too that annual compensation estimates include men who worked part of the year before leaving the workforce, some with no intention of coming back anytime soon. For such men, their annual compensation is a poor indicator of what they command in the labor market, and if such men grow more common in the data over time, it will tend to pull the compensation trends downward. If pay growth is stronger for men with stable connections to the workforce, then the counterfactual of annual compensation may also conceal the growth in pay among below-median workers with consistent labor force connections. Given this, the growth in annual compensation over time is very likely understated for men consistently participating in the workforce.

In summary, the bulk of the evidence suggests an upward trajectory of pay over the past 25 or 30 years for men and even more so for women. Following a long post-WWII boom, wage growth paused before returning to a respectable growth path in the 1990s. By choosing arbitrary time intervals, or narrowing the analysis to constantly shifting education cohorts, it is possible to tell a more pessimistic story. However, even these more stagnationist formulations tend to show constant, rather than declining pay. The reality of any given worker's wage trajectory is likely even rosier as medians and averages fail to tell the story of an individual's wage growth over their career or resulting from skill acquisition and work experience.

### *Pay Lagging Productivity?*

Still other explanations for declining male prime-age participation sidestep whether pay increased and instead assert that pay should have increased faster than it did. Many analysts claim that wage growth has decoupled from worker productivity, so that workers increasingly make less than the value of what they

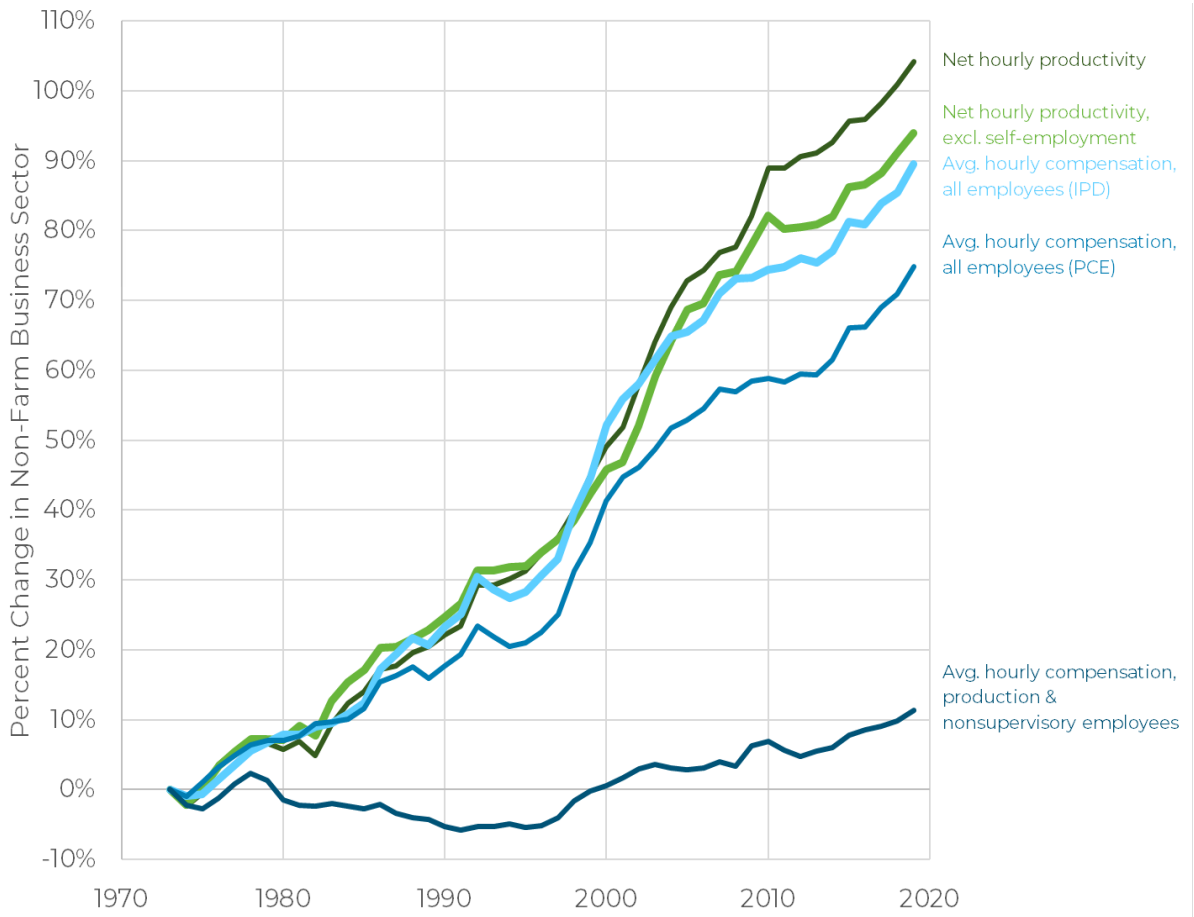
produce. Had pay risen as fast as productivity, more people would have stayed in the workforce. However, aggregate and median pay seem to have kept up with their comparable measures of productivity.

In order to properly assess how worker productivity tracks with pay, a number of adjustments need to be made in order to compare like with like. This means using average hourly compensation of all workers, adjusting compensation and productivity for inflation with the same price index, and using a productivity measure that excludes activities not associated with production.[58]

Productivity measures the total production of the economy divided by the total hours worked—if the economy can produce more goods and services with fewer person-hours, productivity increases. Measures of compensation represent what is given in exchange for time spent working. Choosing the best variables to approximate these definitions is crucial in order to appropriately measure the link between compensation and productivity. For economic production, the measure best suited for comparison with compensation is Gross Domestic Income (GDI), which measures the total income paid to produce things and approximately equals GDP, which measures total purchases. Several components of GDI should still be excluded as they are not related to income paid for production (i.e., depreciation, net indirect taxes, rental income allocated to homeowners, and proprietor's income). Self-employment income should also be excluded from the production measure because it is not captured in the measurements of hourly pay. For the most comprehensive measure of hourly compensation it must include not just wages and salaries but also benefits, such as employer-provided health care, that are a growing portion of workers' earnings. Both variables must be adjusted using the same inflation measure, as differences stemming from the use of two different price indices may obscure the trends.

Figure 12 walks through each of these adjustments to the productivity and compensation data, updating work by labor economist James Sherk.[59] The two bolded lines below (light green for adjusted productivity and lightest blue for adjusted compensation) use the same implicit price deflator to show how wages and productivity remain closely associated with one another. The top green line shows growth in net hourly productivity for all workers including the self-employed. Proponents of the pay-productivity gap often present just the top line and the bottom dark blue line showing average hourly compensation of production and nonsupervisory workers. By using a broader measure of workers (medium blue line) and using more accurately comparable measures of inflation, the pay-productivity gap all but disappears. The medium blue line is adjusted using the Personal Consumption Expenditures (PCE) index which approximates inflation for the things people regularly purchase. The lightest blue line is adjusted using the implicit price deflator (IPD) a better measure of price changes for the things Americans actually produce and is more directly comparable to measures of the associated changes in productivity. Comparing the lightest blue line to the light green line, more accurately aligns net hourly productivity with average hourly compensation using the same implicit price deflator and a similar universe of workers.

Figure 12. Adjusting for Proper Comparison of Compensation and Productivity Growth




Source: Social Capital Project analysis and James Sherk, "Workers' Compensation: Growing Along with Productivity," Heritage Foundation, May 31, 2016, https://www.heritage.org/jobs-and-labor/report/workers-compensation-growing-along-productivity.

The pay-productivity gap is the subject of extensive research, with a number of high-quality studies confirming that compensation and productivity have not significantly diverged over time.[60] While some of this research shows some divergence after 2000, others confirm the continued close association shown in Figure 12.

Former Treasury Secretary Lawrence H. Summers and Anna M. Stansbury find that the link between productivity and compensation remains intact for both the median and average worker, despite a degree of weakening since 2000.[61] Similarly, Robert Z. Lawrence notes that wages are associated closely with productivity over the 1970-2000 period and likely through 2008 when measured properly.[62] Measuring over the 1973-2016 period, former Council of Economic Advisers (CEA) Chairman Jason Furman notes that when measured properly, evidence at both the macro and micro levels demonstrate that productivity growth and wage growth are connected.[63]

Not only is overall growth of hourly compensation and productivity nearly in lockstep over the 1973-2007 period, but median hourly compensation gains for women in particular nearly tracked net productivity gains over the same timeframe, complicating theories that typical worker pay has stagnated.[64] Economist Evan Soltas also examines the link between labor compensation and productivity at the industry level, finding that changes in productivity at this more detailed level explain nearly all of the changes in hourly labor compensation over the 1987-2013 time period.[65] Supporting Soltas' findings, additional research shows that the relatively slow productivity growth of the average firm in a given sector masks the most productive firms' productivity gains, including within the manufacturing and services sectors.[66] The widening dispersion of industry and firm productivity growth rates can also be observed at the worker level; measures of median pay have not grown as quickly as overall productivity.[67] This does not mean that an individual worker's pay is disconnected from productivity. If we had a measure of median productivity it might very well track median pay.[68] In essence, the majority of the evidence shows that workers continue to be paid for what they can produce but differences in productivity growth between firms and across sectors may be increasing.

This also means that, contrary to many claims, labor's share of income mostly held steady over time. As Sherk and others note, labor's share of net nonfarm business income has been remarkably stable since measurement first began in 1973. The evidence of the stability of labor's share of GDP is so strong that the Congressional Budget Office builds the stability of the labor share of GDP into forecast models, assuming a reversion to the long-term average since World War II.[69] This is yet another affirmation of worker wages keeping pace with productivity, as this share would have fallen dramatically if wages and productivity did in fact "de-couple."[70]

Even though the link between productivity and worker wages remains intact, productivity has slowed, particularly since the Great Recession, averaging 1.5 percent growth annually between 2007 and 2020.[71] Productivity growth was also relatively slow in the 1973-1990 periods, growing an annual average of less than 2.0 percent. The productivity slowdown in the 1970s is not just a U.S. phenomenon but a poorly understood global trend that could be due to technological change, changing regulatory environments, aging populations, or other external factors.[72]

In the years since the Great Recession, changing demographics—namely an aging population—may be partly to blame for slow productivity growth in the U.S. Notably, recent research from Adam Ozimek, Dante DeAntonio, and Mark Zandi suggests that much of the decline in the undergirding of innovation and technological improvements that drive productivity growth is slowing down due to the large demographic influence of older workers impeding the adoption of technological improvements. They find evidence that, across states and industries, an aging workforce slows productivity growth by a quarter to a full percentage point.[73] The authors argue that this effect is large enough to explain a significant portion of slowing productivity growth and subsequent wage growth. They expect the trend of an older population to continue to slow the adoption of disruptive

technologies that drive productivity for some time. There is some initial evidence that older workers retired at a record pace in 2020, at least in part due to the pandemic, although the relative permanence of this trend or the magnitude of its effect on productivity is highly uncertain.[74]

### *Skill-Biased Technological Change Affecting Distribution of Labor Compensation?*

Even if wages have not decoupled from productivity, another line of research suggests that increasing technological advances may have lowered the demand for and potential return to certain types of low-skill jobs.

Beginning in the late 1990s, a theory of skill-biased technological change (SBTC) was used to explain increasing wage inequality. While wages across the distributions were still growing, the highest-paid workers have seen the fastest wage growth (Figure 10). First posited in 1998 by David Autor, Lawrence Katz, and Alan Krueger, the early theory of SBTC claimed that technological advancements increase demand for higher-skilled workers. As the supply of highly-educated workers fails to keep up with the constant march of technology fueled demand, firms must pay a wage premium to high-skill, typically highly-educated workers with a college degree.[75]

While still widely discussed, this early formulation of SBTC has failed to explain key wage trends in the 1990s and 2000s, namely the proliferation of computerization during an era of declining wage inequality.[76] Promoters of the early theory reformulated their explanation in a "tasks-based framework" where computerized automation creates a cheap substitute for easily routinized manual and cognitive work.[77] The task-based framework is characterized by a prediction of "job polarization" where demand for middle-skill jobs, such as in white-collar clerical and blue-collar production sectors, decline as automation and increasing global integration allow lower-wage workers in foreign countries to displace workers in industrialized countries.[78] The same technological advancements also increase relative demand for cognitive and manual non-routine work.[79] This dynamic is said to lead to a hollowing out of the labor market as job polarization at the top and the bottom increase.

Like early formulations of the SBTC story, the task-based theory faces a number of compelling critiques. A number of researchers find that the decline in what are termed middle-skill jobs is mild at worst, failing to conjure the dramatic disappearance that the word "polarization" implies. In a comprehensive review of wage trends and the SBTC literature, Lawrence Mishel, Heidi Shierholz, and John Schmitt conclude "that occupational employment trends give only limited insight and leave little imprint on the evolution of the occupational wage structure, let alone the overall wage structure."[80]

Economists Harry Holzer and Robert Lerman find little evidence for a hollowing out of the job market. They show that middle-skill jobs as a share of all jobs shrunk

by 7 percentage points between 1986 and 2006, but the relatively modest decline was almost entirely compensated for by increases in high-skilled jobs. Low-skill job shares only increased by 1 percentage point.[81] Extending Holzer's and Lerman's analysis to 2019 reveals that high-skill jobs now comprise about the same share of U.S. employment as middle-skill jobs, continuing the trend of occupational up-skilling, not hollowing out.[82] In 2020, as the pandemic led to the loss of many low-skill service sector jobs, the share of middle-skill jobs remained the same as in 2019, and the share of high-skill jobs gained two percentage points. There are still more middle-skill jobs today than in 1986, but they grew the slowest by comparison; high-skill jobs doubled and low-skill jobs grew by one-third.

Jennifer Hunt and Ryan Nunn break workers into high-, mid- and low-wage buckets and find that over the long-run "the shares of workers in the top and bottom [wage] groups generally move in opposite directions over the longer term as well, with the share in the top group rising markedly and the share in the bottom falling slightly."[83] The analysis also finds that there is so much wage variation within detailed occupational categories that looking at occupational groups is not useful for drawing conclusions about wage trends. Mishel, Schmitt, and Shierholz similarly show that "occupational upgrading" has been occurring since 1950, during times of rising and falling median wages and wage inequality.[84] These results taken together illustrate how a decline in the share of middle-skill jobs does not necessarily lead to a decline in the share of middle-wage jobs. More broadly, shifts in occupational trends are not indicative of polarization and polarization cannot account for shifts in wage patterns.

A SBCT-adjacent theory maintains that the economy is too dynamic and disruptive. That labor force participation has fallen steadily as workers fail to keep pace with the rapid shifts in industry, technological progress, and subsequent changes in skill requirements. While we cannot dismiss narratives regarding economic insecurity and discouraged workers outright, it is critical that we avoid misattributing the cause of labor trends to the wrong economic phenomena.[85] In the case of economic dynamism, the data suggest that the problem may be too little, not too much.

Dynamism across the American economy declined steadily over the last three decades on many different and meaningful margins. Brookings Institution research shows that labor market fluidity—encompassing job creation and destruction, job switching, and interstate migration—has been in decline since the 1980s and fell by double digits since the 1990s.[86] The new firm establishment rate declined by 41 percent between 1978 and 2018.[87] Fewer existing firms exit the market each year and the private sector job creation rate declined sharply between 1998 and 2008.[88] Workers also are switching jobs less often, and when people do switch jobs, the separation is initiated by the employee 60 percent of the time, suggesting stability in a majority of work arrangements.[89]

Instead of an economy that is changing so rapidly that workers are falling behind, the opposite seems more plausible. Worker productivity and wages might be

better served from a more dynamic work environment. While technological change has certainly shifted the type and distribution of work over time, it does not seem to have meaningfully hollowed out middle-skill jobs or consistently affected the distribution of wages in any significantly measurable way.

*Trade Exposure Pulling Down Pay and Slowing Job Growth?*

Global trade is also often blamed for putting downward pressure on wages in some low-skill sectors and contributing to job losses in some types of American manufacturing. It is true that American firms now operate in an increasingly globalized trade environment, and American workers compete with and complement the relatively abundant low-skilled labor supply in developing economies. However, the simultaneous rise of idle prime-age men and American industries facing new competition from abroad does not necessarily mean one trend caused the other.

Increasing global trade has well-known trade-offs. Foreign-made goods mean lower input and inventory costs for American businesses, which can lower the cost of domestic manufacturing and boost net U.S. employment and real wages.[90] This outcome also translates into lower prices and greater savings for American consumers.[91] Yet, some American companies unable to compete with their foreign counterparts are forced to close, shrink, or move elsewhere—all of which may require lay-offs. In the face of greater competition, the more resilient domestic companies often rise to the challenge, responding with greater domestic investment and new innovations that carry benefits for American workers and consumers.[92] Competing popular narratives surrounding American trade policy tend to emphasize some of these trade-offs at the expense of others.

One trade narrative draws heavily on work by David Autor, David Dorn, Gordon Hanson, and their colleagues that analyzes the effects of China's entrance to the World Trade Organization (WTO) and subsequent increasing trade with China in the early 2000s—often called the "China shock." The research highlights the costs of trade liberalization, especially for individuals with relatively lower wages, little job experience or transferable skills, and less attachment to the labor force.[93] In a 2016 paper, Autor and co-authors find that the rapid increase of Chinese imports from 1999 to 2011 is associated with between 10 percent and 20 percent of the drop in manufacturing employment.[94] Andrew Bernard, Bradford Jensen, and Peter Schott find that imports from low-wage countries account for 14 percent of the drop in manufacturing employment between 1977 and 1997.[95] If policymakers take these estimates at face value, trade with China and other lower-wage countries only explain at most one fifth of the job losses during the period studied.

However, the often cited Autor-Dorn-Hanson conclusion that increasing trade explains depressed domestic employment is at minimum overstated and possibly misleading. For instance, economist Jonathan Rothwell examines the same Autor-Dorn-Hanson data but accounts for differing macroeconomic trends throughout time and by location. Rothwell shows, after making these

adjustments, that the original effects on employment, labor force participation, and wage growth are not significant.[96] In her PhD research, economist Ildikó Magyari shows that firms exposed to Chinese imports reduced some parts of their U.S. business footprint but, contrary to the conventional wisdom, expanded in other areas. Firms exposed to trade with China actually created more net American manufacturing and nonmanufacturing jobs than non-exposed firms during the time studied.[97]

The often striking results that show job losses due to trade in particular sectors or for particular types of workers focus exclusively on losses due to trade without broadening the analysis to account for the winners of increased trade. Distributional questions aside, theoretical and empirical trade research almost unanimously find that expanded trade between countries increases total wealth for the citizens on both sides of the exchange by exploiting differences in comparative advantage and resource endowments.[98] Faced with new international competition, firms specialize in what they do best, relative to their competitors, which can cause labor markets to shift in ways that displace some workers while providing new opportunities for others, which increases productivity across the board.

Distributional questions are important, and at the same time should not be used to overlook the broad-based benefits of cheaper American manufacturing inputs and consumer goods as well all the net job gains in other sectors. Researchers from the Federal Reserve Bank of St. Louis, Lorenzo Caliendo, Maxmilliano Dvorkin, and Fernando Parro find that the China shock increased net U.S. welfare, but did so unevenly.[99] Their research shows how job losses tend to be concentrated in specific places, such as California, which has a high share of China-exposed computer and electronics jobs, and job gains tend to be geographically spread out in construction and services sectors. The concentrated job losses, while painful, were only temporary; in the long run, the researchers find that industry productivity gains and the ability of U.S. workers displaced by trade to find new employment with higher wages increased the welfare of workers in 96 percent of state- and sector-specific labor markets. Similar research from Spencer Lyon and Waugh, as well as Zhi Wang and co-authors, report positive results of trade exposure from China, finding that it increased aggregate welfare and produced net American job creation. They find that a minority of workers see no welfare effects or small declines in wages and job opportunities, especially lower-wage workers who compete more directly with foreign workers.[100]

Proponents of increasing trade often emphasize the net-benefits of trade to American workers and consumers, as well as the benefits to global markets. Critics of increasing globalization often fixate on the minority of workers who were exposed to additional competition due to an increase in trade with China and other nations. The disproportionate effect of trade adjustment on middle- and low-skill manufacturing workers and their communities should be acknowledged as likely a temporary contributor to prime-age men leaving the labor market. While some estimates suggest that trade disruptions immediately following

China's entrance into the WTO may explain 10 percent to 20 percent of the labor force participation trend between 2000 and 2008, trade exposure is not likely an ongoing drag on prime-age male labor force participation. [101] The effects of the China Shock were a one-time phenomenon and by 2008 workers had largely adjusted to the new normal.[102] Indeed, subsequent research estimates that, post China shock, imports across all countries are positively associated with the creation of domestic manufacturing jobs because they reduce the cost of U.S. production.[103] Therefore, it is likely that removing barriers to trade with other countries in the future would encourage net job creation with more limited distributional variation in where jobs are created and lost.[104]

*Government Programs and Policies Making Work Less Attractive?*

Weakening employer demand and a deteriorating job market seem unlikely to explain a significant portion of the decline in prime-age male labor force participation given the discussion in the preceding sections. Supply-side factors can help fill much of this disconnect. Instead of looking primarily at employers, it may be more illuminating to place workers and the incentives they face at the center of the analysis.

One key piece of evidence that suggests labor force trends are driven largely by workers, not employers, is that the decline in prime-age labor force participation has been mostly voluntary, as told by the men themselves. Three out of four disconnected men say they do not want a job,[105] and only 12 percent of inactive, prime-age, able-bodied men said they wanted a job or were open to it in 2014.[106] If more men are genuinely choosing to stay home with the kids, go to school, or retire early, policymakers should not be concerned. However, government policies may be tipping the scales toward inactivity and away from work.

Policymakers should take note if would-be workers' inactivity is indeed enabled or encouraged by poorly structured government benefits or made more likely by unnecessary barriers to work. This is likely the case for the 41 percent of prime-age men who personally receive government assistance and are inactive for reasons other than disability, retirement, education, or homemaking.[107] In addition to the inactive population, a growing number of Americans in general receive government assistance, despite improving pre-pandemic economic conditions. The share of working-age Americans living in households between the 20th and 50th income percentiles who receive safety net benefits increased from 20 percent to about 30 percent between 1998 and 2014.[108] This growth in safety net benefits likely makes non-work more attractive and has contributed to declining labor force participation.

A significant body of empirical evidence suggests that government transfers—especially those without work requirements—tend to lower employment.[109] For example, labor force participation and earnings fall after receiving housing assistance,[110] losing Medicaid coverage increases employment[111] and gaining the

coverage can reduce it,[112] and the introduction of the food stamp program in the 1960s and 1970s decreased employment significantly.[113] A series of temporary income support trials also find that disincentives to work generally increase with the size and duration of the benefit, although the effects are often smaller than predicted.[114] More recent evidence following the Great Recession shows how the expansion of safety net benefits undermined the rewards to work, creating employment losses and delayed economic recovery.[115] These empirical investigations usually evaluate the effects of just one program at a particular time, instead of the effects of participating in multiple programs simultaneously, which is the reality faced by many households.[116]

When policymakers think about the incentives created by safety net and other transfer programs, they are best analyzed as one system rather than distinct programs. One attempt to look holistically at these incentives models lifetime marginal tax rates after accounting for features of the tax system and eleven of the largest transfer programs at both the federal and state level.[117] The marginal tax rate is the tax rate paid on the next unit of income earned. Different from average tax rates, marginal rates speak more directly to incentives, answering the question, "If I earn one additional dollar, how much will I get to keep?" In many states, earning $1 too much can result in the loss of thousands of dollars in personal or family Medicaid benefits. This holistic approach finds that "one in four low-wage workers face lifetime marginal net tax rates above 70 percent, effectively locking them into poverty."[118] The current system of federal and state benefits can, through a system of disincentives, discourage poor Americans from working and stand in the way of upward mobility.

Not only is there evidence that welfare programs harm labor market outcomes, there is evidence that some of the worst effects can be mitigated through better program design. Attaching work incentives to assistance programs has shown some success at reducing the inherent disincentives. The experience following the 1990s-era welfare reform is particularly instructive. Requiring work for able-bodied recipients of previously unconditional transfers reduced caseloads and increased employment, although disentangling the effects of other simultaneous reforms is challenging.[119] The most definitive evidence shows benefits for single mothers, especially low-income single mothers. Single mothers were less likely to receive assistance, significantly more likely to work, and less likely to live in poverty following the addition of work requirements to welfare.[120] These effects have been found to persist for decades following the reforms and translate to increases in food security for subsequent generations.[121]

In addition to government benefits acting as a barrier to work, federal, state, and local regulations can also disproportionately harm low-skilled workers. In the aggregate, there is a strong measurable relationship between increases in regulatory restrictions and increased poverty across states.[122] Similarly, at the top of the wage distribution, high-income, high-status professions in law, finance, and medicine have institutionalized a system of government granted privileges that protect their professions from reasonable competition.[123] Other barriers to work,

such as occupational licenses and restrictions on home-based businesses, create obstacles that restrict workers' ability to supply their labor in their desired field.

Regulations can also dampen the demand for workers. By raising costs for employers, many regulations make it unprofitable to hire lower-skilled, lower-paid workers. Labor regulations and minimum wages increase the amount of marketable value a worker must provide their employer in order to be worth employing. By raising the cost of employment, government policy can effectively set a floor under which certain workers are simply not employable. At the same time, government benefits can make work and investment in skills development less attractive, which ultimately makes workers less competitive in a labor market that—due to employment laws and regulations—requires a relatively high level of value creation in order to secure employment.

## POSSIBLE POLICY APPROACHES

The possible policy approaches to connect more Americans to work generally fit into three broad categories: remove barriers to work, fix disincentives to work, and bolster incentives to work. The policies that follow are by no means an exhaustive list, but offer a selection of policy options that may be worth exploring in further detail.

### *Remove Barriers to Work*

Unnecessary or over burdensome regulations can create barriers for American workers trying to gain entry into more stable and better paying professions. Wide-ranging rules increase the cost of moving interstate for a higher paying job, stand in the way of new micro-business formation, discourage successful small businesses from expanding, and make it more challenging for the previously incarcerated to reenter the workforce. At every level of government, policymakers should consider ways to reduce and streamline these government-imposed barriers to economic opportunity.

#### *Occupational Licensing*

Occupational licenses are regulations that require workers to obtain a government-mandated license to legally offer goods or services for pay. These laws are often premised on a need for consumer-protection, and they ostensibly provide a way of ensuring quality or safety in specialized professions such as nurse practitioners. However, most licensing requirements are overly burdensome and act as state-enforced cartels that protect government-privileged industries from price and quality competition. There are few good reasons for governments to require hundreds of dollars in fees and thousands of hours of education for animal breeders, auctioneers, dance instructors, bartenders, cosmetologists, door repair contractors, florists, interior designers, landscapers, tour guides, or upholsterers.[124]

Licensing hurts Americans in two important ways. First, it denies the ability to choose lower-cost, unlicensed alternatives that could make essential services, such as childcare, more affordable.[125] Second, licensing is a barrier to work; it bars lower-income, young, and less educated workers from offering services as an enterprising way to start a new career and work themselves out of poverty, and it increases the costs of moving to areas with better opportunities which often have different licensing systems.[126]

The share of workers who are required to hold a state license has risen five-fold since the 1950s, from 5 percent to 25 percent in 2008.[127] Two-thirds of the growth comes from new licensing requirements rather than employment growth in previously licensed industries. In many of these cases, states can simply eliminate unnecessary and unproductive occupational licensing requirements. For licenses that are deemed necessary for health and safety, states and Congress can expand reciprocity so that similar licenses and credentials are portable between jurisdictions. Examples include the Nurse Licensure Compact (a multi-state license) which is currently available in 33 states,[128] and the Interstate Medical Licensure Compact (multi-license acquisition), which grew from 9 states in 2015 to 29 states, plus the District of Columbia and Guam, in 2019.[129] Interstate compacts could allow states to mutually recognize licenses or expedite licensure if someone has a license in a partner state.[130]

While the majority of licenses are mandated by states, there can be a role for federal occupational licensing reform. Senator Mike Lee's *Military Spouse Licensing Relief Act* would allow military spouses to use their occupational license in a new jurisdiction after being transferred for military service, and the previously introduced *Alternatives to Licensing that Lower Obstacles to Work* (ALLOW) Act would eliminate unnecessary occupational licensing requirements in the District of Columbia and federal parks.[131] Senator Lee's *Tougher Enforcement Against Monopolies* (TEAM) Act would also address uncompetitive practices by state and local licensing boards and encourage less restrictive regulatory alternatives where possible.[132] These federal reforms could serve as a model for reducing unnecessary barriers to employment across the country.

*Zoning for Homebased Businesses*

Similar to occupational licensing, local zoning of home-based businesses can also limit work opportunities. The coronavirus pandemic highlights the wide range of personal and professional services that can be carried out from home, if the law allows. In the latest survey of business owners, over half of firms were home-based businesses and six in ten firms without paid employees were home-based businesses.[133] These small businesses tend to be run by people who struggle to fit traditional work relationships, such as single parents, the disabled, the otherwise unemployed, and caregivers.[134] However, many cities' zoning regulations drive these entrepreneurs underground or discourage them altogether by effectively banning would-be home-based businesses through outright prohibitions, size restrictions, or other burdensome requirements.[135]

Arizona's *Home-Based Business Fairness Act* proposal[136] provides a useful example of how states can protect small-scale community entrepreneurs' ability to operate home-based businesses that do not negatively affect the local neighborhood.[137] In general, states and cities could update their home-based business regulations to exempt small, informal operations and add flexibility for growing small businesses.[138] The Small Business Administration also outlines tax compliance burdens on home-based businesses that could be streamlined, such as simplified depreciation schedules for a home office, taxes associated with the sale of the home, and onerous documentation for equipment that is not used exclusively for business.[139]

*Barriers to Flexible Work*

Estimates suggest that between 10 and 35 percent of U.S. workers participate in the gig economy, meaning that they have nontraditional, flexible employment arrangements.[140] Therefore, barriers to flexible work threaten the employment and lifestyles of millions of U.S. workers.[141] Surveys suggest that these workers, many of whom are independent contractors, overwhelmingly prefer their arrangement over a traditional employment arrangement due to the flexibility it allows. [142] For instance, independent workers are disproportionately likely to be caregivers to their children or parents.[143] Similarly, women in the gig economy report that the primary benefit of nontraditional work is the flexible working hours.[144]

Despite the benefits of flexible work, numerous barriers exist preventing workers from connecting to nontraditional employment opportunities. For instance, states such as California, New Jersey, and Massachusetts have all sought to impose regulations that reclassify independent contractors as traditional employees, which subjects employers to higher costs and severely limits options for individuals seeking flexible work.[145] Legislation also exists in Congress that would expand worker reclassification on a national scale,[146] and the Biden Administration recently rolled back Department of Labor (DOL) protections shielding independent contractors from reclassification.[147] Second, current tax law harms workers in flexible employment arrangements by limiting their access to tax-advantaged savings accounts relative to traditional employees.[148] Finally, individuals without formal employment arrangements lack access to employer-sponsored benefits like health insurance and retirement savings accounts, which discourages some workers from taking advantage of flexible work.

Instead of seeking to make every business and their workers conform to a traditional one-size-fits-all employment relationship, policymakers should take steps to decrease uncertainty surrounding flexible work, for instance by reinstating the DOL's rule clarifying the definition of independent contractors. Furthermore, universal savings accounts (USAs) would be valuable resources for workers in nontraditional employment arrangements.[149] USAs would empower all workers to save for the future by giving them access to a tax-advantaged savings vehicle not tied to any single employer, and one from which they could withdraw from at any time and for any reason without penalty.[150] Finally, portable benefits

would give workers access to health insurance and other types of benefits that would follow them from job to job, regardless of their employer.[151]

*Non-compete Agreements*

Like licensure, non-compete agreements may create barriers to opportunity—particularly for low-wage workers—by limiting job switching, an effective way to increase earnings quickly.[152] Unlike state-enforced licensing, non-compete agreements are private legal contracts that, when agreed to, prevent employees from working at firms in competition with their current employer for some period of time. If non-compete contracts lower worker bargaining power, reduce beneficial job-switching, and induce covered workers to abandon their chosen occupation, they may present additional frictions that result in worker discouragement and possibly inactivity.[153] However, non-compete clauses can benefit workers by creating an environment where the benefit of additional costly employee training can be internalized through the employment contract.[154] Where non-compete clauses are used to protect trade-secrets, they can be an important protection for innovation and research.

Policymakers should study the effects of non-compete agreements more closely to determine their relative costs, benefits, and potential reforms. Many workers are notified of and asked to sign a non-compete only after accepting a job offer. Requiring upfront disclosure of a non-compete before the worker accepts the job could improve worker-employer matching, similar to Oregon and New Hampshire, where non-compete contracts are void if they are not included in "the original terms of employment."[155] The Economic Innovation Group (EIG) highlights a number of more restrictive policy options that states may consider, including: "garden leave" provisions that compensate a worker for abiding by the non-compete; bans on non-competes for low wage workers and specific high-skill jobs; and outright non-compete and no-poach bans.[156]

*Reintegration of Ex-Prisoners*

One of the impervious barriers to stable employment in America is a criminal record. An estimated 12 percent of men are current or former felons[157] and the formerly incarcerated make up one-third of disconnected prime-age men.[158] Those who are currently incarcerated and not included in labor force statistics, represent a similarly large loss of economic potential. Within a few years, more than half of former offenders will revert to criminal activity and face re-arrest.[159] This revolving door of the criminal justice system has many causes, but at a basic level, it stems from a failure to reintegrate individuals into communities and employment. Connecting the formerly incarcerated to communities and work is perhaps one of the most consequential public policy levers available to reverse the trend of prime-age male inactivity.

A myriad of federal, state, and municipal programs exist alongside non-profit organizations to facilitate reentry, supply health services, supervise, and offer educational opportunities and employment assistance. These include the recent re-expansion of Pell Grant eligibility to prisoners, the Bureau of Prisons' "Ready to Work" initiative, and the Department of Labor's dual efforts: the Reentry Employment Opportunities and the Federal Bonding Program, the latter of which helps insure businesses that are willing to hire the formerly incarcerated. Research shows that not all public programs have demonstrated success. For example, research shows that the success of publicly subsidized training and employment in most cases is limited to only the first couple years post-incarceration.[160] The research literature on reentry and recidivism, however, suggests that social ties to family, work, and community are among the most significant indicators of, and means for, reintegration.[161] Steady employment, in particular, is considered an effective means of both encouraging pro-social, lawful behavior, as well as discouraging criminal activity.[162] To that end, a number of private initiatives, including The Last Mile and Dave's Killer Bread Foundation, help inmates learn valuable skills in prison and facilitate "second chance" hiring for private businesses that might otherwise overlook those with a criminal record.[163]

In addition to social stigmas, however, the formerly incarcerated face a number of legal barriers to employment and opportunity, including legal restrictions to working in certain occupations, obtaining a driver's license, securing housing, and receiving public assistance.[164] Future reforms should therefore address these structural barriers to employment opportunities. As with occupational licensing reform more broadly, legal bans on hiring individuals with a criminal record or effective bans by occupational licensing boards could—depending on the nature of the occupation—either be removed entirely or revised to provide a safe, legal path to employment for eligible individuals.[165] Criminal background checks, as well as requiring offenders to identify their previous incarceration on job applications, may also be overly discriminatory. Yet research shows solutions like "ban the box" for criminal records on job applications worsen employment outcomes particularly for young Black men, as employers resort to pre-existing biases when an applicant's criminal record is no longer available.[166] State and local governments could form a dedicated task force or launch a review of regulations that restrict the employment opportunities of the formerly incarcerated and evaluate whether they might be reformed. They could also explore ways to alleviate the direct costs and risks associated with hiring an offender, such as pursuing reforms to employment law to reduce negligent hiring liability.[167]

Regardless of the reforms considered, policymakers ought to balance the goals of reintegration and employment with the protection of public safety and employers' rights. Likewise, they ought to be sensitive to concerns about special treatment and openhandedness. Just as a criminal record should not entail a life sentence of unemployment, it should also not be a voucher for free education. Instead, public policy should be oriented toward securing equal opportunity for the formerly incarcerated and rebuilding connections to the American workforce and civil society.

*Employer Mandates*

Regulatory requirements, tax obligations, and compliance costs associated with employment create uneven costs that dampen the ability to hire. As noted in a previous JEC Republican analysis, with few narrow exemptions,[168] payroll contributions, tax reporting and remittances, unemployment compensation, retirement benefits, rigid safety and health standards, the *Fair Labor Standards Act* (FLSA), which includes regulations on overtime pay and the minimum wage, "collectively require compliance beginning with just one employee."[169] Other requirements kick in at arbitrary thresholds, such as the requirement for employers with 50 or more employees to offer health coverage under the *Affordable Care Act*.[170] Some regulatory burdens are relatively fixed costs that weigh heaviest on small employers and become less costly on a per-employee basis for firms with larger payrolls, while others, such as payroll taxes, add similar costs to each new hire.

While establishing a standard of safety and well-being may be necessary in some industries, rigid, universal rules can prevent potential employees and employers from making alternative work arrangements that may be more mutually beneficial and situationally appropriate. Particularly in light of the pandemic, a number of reforms could improve employment opportunities and flexibility for workers. For example, Senator Lee's *Working Families Flexibility Act* would allow hourly workers to choose paid time off instead of overtime pay.[171] Policymakers should also consider more fundamental reforms to Social Security and Medicare that could lower the burden of payroll taxes, health care reform that would repeal the employer mandate, and devolution of many labor regulations to state governments.

*Fix Disincentives for Work in Safety Net Programs*

Providing an effective social support system to protect the most vulnerable Americans from poverty is critical. However, compared to the relatively targeted programs in the earliest iterations of the U.S. safety net, safety net programs today are less targeted and the share of the working-age population receiving at least one means-tested benefit has increased significantly over previous years.[172] The means-tested welfare system is large and complex, comprised of approximately 90 programs that provide assistance such as: cash, food, housing, medical care, and social services. Most of these programs undermine work by providing assistance without requiring employment or work preparation for those who are able-bodied. These programs make non-work a viable alternative to work for some Americans.

Connecting people to stable work is among the most effective poverty preventions available. In 2019, only 2 percent of full-time workers lived in poverty.[173] Reforms in the 1990s, including the *Personal Responsibility and Work Opportunity Reconciliation Act* (PRWORA), shifted from providing unconditional cash-aid to those in poverty to requiring work for able-bodied recipients, recognizing that while people may know best how to use funds on themselves, they do an

even better job with their own earnings. The reforms in 1996 established work requirements and time limits in the Temporary Assistance for Needy Families (TANF) program, curtailing welfare assistance as an unlimited entitlement and creating a template for future welfare program reforms.

More reforms are needed. Work requirements in TANF have become less binding over time and enforcement varies significantly by state.[174] Nearly all other government means-tested programs lack any work requirements.

The following sections review specific reform opportunities targeted to improve work incentives for the work-capable prime-age population in TANF, the Supplemental Nutritional Assistance Program (SNAP, formerly the food stamp program), Medicaid, Supplemental Security Income (SSI), Social Security Disability Insurance (SSDI), and unemployment insurance (UI). These programs differ in who they target, but they are all federal programs that provide benefits to those with low or no income. TANF, SNAP, Medicaid, and SSI are considered "means-tested programs," in that individuals qualify based on their income and assets. Eligibility does not require a history of work. SSDI and UI are funded by payroll taxes and require a person to have a sufficient history of employment to qualify.

*Temporary Assistance for Needy Families*

TANF, along with SNAP, is one of the few federal means-tested welfare programs that includes a work requirement.[175] Formerly known as the Aid to Families with Dependent Children program (AFDC), the 1996 act reformed the program by inserting work requirements and time limits, renaming the program, Temporary Assistance for Needy Families (TANF). The reform requires states to engage approximately half of their able-bodied adult TANF recipients in work or work preparation activities and added a two consecutive year limit and a five-year lifetime limit for benefit eligibility. As the name of the program indicates, TANF is targeted to families, the majority of which are headed by single parents, mostly mothers.[176] After the 1996 reform, employment rates among low-income single mothers increased substantially and child poverty declined.[177]

The 1996 reform was a significant step that moved the U.S. welfare system towards a work-first approach. However, the reform only added work requirements for half of able-bodied recipients in one welfare program. Because the law was written in a way that allowed states to reduce the percentage of their caseload required to participate in work in various ways, TANF's work requirement has become weaker over time.[178] States have also found ways to fulfill the work requirement without actually engaging people in work or work activity. In most states, fewer—and sometimes far fewer—than half of the able-bodied TANF caseload is working or participating in work activity.[179]

To build on the progress of the 1996 reform, Congress could strengthen TANF's work requirement by expanding eligibility for mandatory work and narrowing the loopholes exploited by states. These types of reforms would restore and improve TANF's goal of promoting self-sufficiency through work.

*Supplemental Nutritional Assistance Program*

One of the largest means-tested programs, SNAP provides a benefit to purchase food for eligible, low-income individuals and households. The number of SNAP recipients increased dramatically following expanded eligibility in 2008 and the Great Recession. Since then, enrollment has remained high. The program covered almost 40 million people in 2020, and was close to 40 million prior to the COVID-19 pandemic, although it dipped to 36 million in 2019, down from 41 million in 2018.[180] In 2019, childless, non-elderly, non-disabled adults represented more than 12 percent of participants.[181] In 2005, less than 4 percent of the nearly 25 million participants were childless, non-elderly, non-disabled adults.[182]

Access to SNAP benefits likely creates disincentives to work, as the majority of participants are not required to work or participate in work programs. One quasi-experimental study found that when immigrants receive access to food stamps they work less.[183] Combined with other means-tested programs, participants can face marginal tax rates of well over 50 percent.[184]

SNAP's work requirement applies only to able-bodied adults without dependents (ABAWDs). ABAWDs are limited to 3 months of SNAP benefits within a 36-month period unless they are working or participating in a work program. However, states can waive a portion of their ABAWD caseload from the work requirement, and during times of high unemployment states are able to receive a full or partial waiver from the work requirement.[185] In 2019, the USDA's Food and Nutrition Service finalized a rule—currently suspended due to the pandemic—that restricts states' options to waive SNAP work requirements for ABAWDs.[186]

In 2014, during a period when the Obama Administration was allowing states to waive work requirements for all ABAWDs, Maine decided to forgo the waiver, such that ABAWDs in Maine were once again subject to the work requirement. Maine expanded its employment training programs to ensure everyone would have a way to fulfill the work requirement if they could not find employment.[187] As a result, Maine's ABAWD caseload dropped by half as people left the rolls. The significant drop in cases suggests that many of the previous beneficiaries had other means of support through family or non-reported income sources and others who were incentivized to work were no longer eligible for benefits due to higher incomes.[188]

States should consider building on Maine's efforts, promoting work for ABAWDs rather than accepting waivers for work requirements. Because SNAP is nearly completely funded with federal taxpayer dollars, federal reforms are also necessary to strengthen work requirements. Senator Lee's *Welfare Reform and Upward Mobility Act* expands work requirements for SNAP, requiring all able-bodied adults without dependents to engage in work or work activity as a condition of receiving benefits. The act would also require the majority of able-bodied adults with dependents on SNAP to engage in work activity.[189]

Beyond strengthening work requirements in SNAP and in TANF, the *Welfare Reform and Upward Mobility Act* strengthens program integrity by better aligning state incentives for administration of work requirements. It also caps total welfare spending to limit the growth of welfare and in turn helps more able-bodied Americans transition to work by shrinking the relative size of welfare over time.

*Medicaid*

Medicaid provides health care coverage for low-income individuals and families. It is the largest means-tested benefit program in the U.S.[190] Beginning in 2014, Medicaid eligibility was expanded to virtually all citizens and legal residents under age 65 and living in families with incomes below 138 percent of the federal poverty level, if states chose to do so.[191] Despite an almost decade-long decline in the pre-pandemic poverty rate, the share of the civilian noninstitutional population, age 26 to 54, covered by Medicaid or other means-tested public health coverage increased by almost 50 percent between 2010 and 2018, rising from 10 percent to 15 percent.[192]

Implementing work requirements for able-bodied prime-age adults covered by Medicaid could alleviate current work disincentives implicit in the existing benefit program. Because health care services are generally not denied to those in need, health program work incentives may not be as effective as other work requirements in promoting work or improving beneficiary independence.[193] However, paired with strong reforms in other areas, continued experimentation with Medicaid work requirements could provide significant benefits.

Prior to the pandemic and President Biden's administration, 10 states had received waivers to implement Medicaid work requirements for able-bodied adults in their prime working years.[194] Nondisabled men on Medicaid are estimated to work an average of 13 hours per week but with large variation, with many working more than 20 hours and others not working. One study suggests that the average number of work hours among Medicaid beneficiaries would nearly triple if all nondisabled Medicaid beneficiaries were required to work at least 20 hours per week.[195] Male recipients who work their way off Medicaid could benefit from almost $1 million more in lifetime earnings compared to Medicaid recipients who do not increase work.

*Block Granting Welfare*

Instead of specific reforms to individual programs, some have proposed replacing current welfare programs with consolidated block grants to states. One recent proposal from then-House Budget Committee Chairman Paul Ryan would create a unified block grant to states, replacing 11 welfare programs and devolving administration of programs to states, including SNAP, TANF, major housing assistance programs, and community development block grants.[196] The intention is to encourage innovation among the states in ways to help low-income people

and reduce the existing maze of government welfare programs. Under the unified block grant, Congress could set requirements for abled-bodied work and the federal government would work with states "to agree on measures of success and evaluation by a third party to conduct an objective assessment of the plan."[197] States would determine how best to use the block grant funding to meet the federal requirements in their state.

Encouraging states to lead on welfare innovation and reform is a good principle. However, states do not have strong incentives to properly steward the welfare system because the federal government provides the vast majority of funding. If a block grant approach does not have sufficiently strong and enforceable work requirements, it could lead to states doing even less to promote work and self-sufficiency. Strengthening work requirements requires state government commitment to requiring work or work activity. Requiring states to contribute more of their own funding to welfare programs could also increase their motivation to discourage long-term dependence and promote self-reliance.

*Social Security Disability Insurance*

The SSDI program was originally intended only for disabled workers age 50-65 deemed unable to work but subsequent expansions of the criteria included eligibility for those under 50, those with temporary disability, relaxed medical screening, and other changes that make SSDI easier to obtain and more attractive to do so, such as automatic enrollment into Medicare after two years of receiving disability benefits.[198] SSDI program awards doubled in the fifteen years between 1988 and 2003 and expanded again during the Great Recession.[199] As of December 2019, 39 percent of more than 3.8 million disabled beneficiaries were ages 25-54.[200]

The business cycle also effects SSDI applications. High unemployment rates between 2008 and 2012 likely resulted in over 400,000 new beneficiaries, about 9 percent of all program entrants during the period.[201] These otherwise temporarily unemployed workers are often subsequently trapped in the SSDI program as it has an explicit anti-work requirement. SSDI includes a number of provisions that rule out returning to the workforce even for those capable of doing so with accommodations or on a provisional or part-time basis. For example, earning more than $1,310 a month can result in losing all benefits.[202] Reforms to SSDI could reconnect a large number of potentially work-capable beneficiaries to the labor force who currently face strong work disincentives, or alternatively, face strong incentives to seek benefits in the first place.[203]

The "medical-vocational grid" guidelines for determining benefit eligibility are outdated and need to be updated for the twenty-first century.[204] Advances in medicine and other technologies make accommodations for disability on the job more feasible and expand the types of jobs available to people of different abilities. With the increased prevalence of working from home during the pandemic, new work opportunities may become available for disabled workers who are better able to work from home, particularly if commuting or finding an employer to provide

accommodations in the workplace was previously difficult.[205] Some factors considered for determining disability such as age, language proficiency, and education level could be eliminated from the grid altogether.[206]

Policymakers may also want to enable temporary and partial benefits scaled by earnings potential for those who otherwise face the "all-or-nothing" benefits under the current program structure, to enable those who have a disability or temporary impairment to continue working. [207] The UK's "Pathways to Work" Program and Denmark's elimination of the permanent disability designation for those under 40 years old provide valuable lessons for U.S. reforms wishing to encourage capable beneficiaries to reconnect with opportunities in the labor force.[208] Lastly, incentives for state operators could be improved by reforming the federal funding formula and improving state vocational rehabilitation, such as expanding specialized workforce training resources and improving incentives for employers to retain and rehabilitate partially disabled workers.[209]

*Supplemental Security Income*

SSI is a means-tested program targeting the aged, blind, or disabled, such that these individuals are "unable to engage in any substantial gainful activity (SGA) by reason of any medically determinable physical or mental impairment expected to last for at least 12 months or to result in death."[210] While SSDI is targeted to the disabled who have an employment history, SSI does not require a history of work for eligibility. The SSI population is low income and most SSI recipients do not have ties to an employer.[211]

The share of working-age persons, 18-64, receiving SSI grew by roughly 20 percentage points to 57.5 percent between 1974 and 2019.[212] Program recipients are nearly evenly split between men and women.[213] Nearly 40 percent of all SSI recipients are age 26 to 59, totaling 3.2 million prime-age persons as of December 2019.[214] SSI caseload growth has been driven by policy changes that have made eligibility determinations more subjective, rather than due to declining health among U.S. adults.[215]

For SSI recipients who do work, the earnings limit for non-blind workers is $1,310 per month for 2021, the same as SSDI.[216] Because program eligibility is based on proof of inability to work and the earnings thresholds are not designed to encourage the self-sufficiency of regular work, only 6.9 percent of all prime-age blind and disabled SSI recipients have market income.[217] Like SSDI, SSI could be reformed to encourage work among recipients. The medical grid criteria could also be updated to remove factors that are not related to disability (education, language proficiency, and age), as well as to reflect jobs in the modern economy. Ultimately, SSI should take a work-first approach, focusing on helping those with disabilities find work opportunities and improve their job skills whenever possible.

The SSI program also covers 1.1 million children as of 2019, many of whom remain beneficiaries their entire life.[218] To set these children up for a successful life, the

direct cash payment to families could be converted into a flexible spending account that could be used to pay for specific goods and services related to the child's needs. As it stands, the SSI program for children is a very generous cash assistance program without work requirements for adult parents. The program undermines incentives to acquire work skills that will allow maturing children to engage in work as adults and fails to achieve one of its intended goals: to increase the likelihood that children with special needs become self-supporting adults.

Congress could also consider fully eliminating SSI for children, as there are multiple other programs available to support low-income families with children, including Medicaid, that serve a similar functional purpose. If there are treatments or health care needs Medicaid does not cover, families could receive SSI funding in a flexible spending account to cover specific uncovered needs. Changing SSI for children into a benefit designated specifically for certain services and items for children is less likely to undermine work than is a direct cash benefit and could also better ensure children receive the help they need to become self-supporting adults.

*Unemployment Insurance*

Unemployment insurance (UI) is a joint state-federal program, financed by a payroll tax, which offers benefits to covered workers who are involuntarily separated from their job. Under federal guidelines, each state determines eligibility, coverage and financing, most often replacing around 50 percent of lost wages for about 26 weeks. During recessions, as it did following the coronavirus pandemic, Congress regularly supplements the state programs by boosting wage replacement rates and extending the length of coverage. The design of the unemployment insurance system can incentivize workers to delay looking for a new job, crowd out other sources of income, such as spousal income, and reduce the incentive for workers to save for a rainy day.[219] The UI benefits during the pandemic were large enough to exceed wages for many workers even after being scaled back to $300 a week. This suggests that—even in the best case—many workers faced an explicit anti-work incentive.[220]

Longer periods of unemployment are shown to have "a strongly negative effect on the likelihood of subsequent employment."[221] As a result of its design, the UI system may incentivize longer periods of unemployment, which then make it harder to reenter the workforce, and more likely that the long-term unemployed become disconnected entirely.

One way to maintain a mandatory UI system and align personal financial incentives to return to work would be to create personal unemployment insurance savings accounts. Economist Veronique de Rugy proposes that the accounts are funded by employers and individually owned by workers who could draw on the balance during periods of lost income.[222] Because the accounts could also be used to supplement retirement income or be transferred to heirs, there would be an incentive to conserve use of the benefits and hasten a return to work.[223]

Other less systemic reforms that work within the current UI system could include providing lump-sum payments to beneficiaries upon becoming re-employed to motivate a quicker return to work; requiring that beneficiaries go to their local unemployment office to pick up benefits and connect with case management services; and loosening the conditions for "acceptable employment" after a particularly extensive job search.[224]

### *Expand Incentives to Work*

Where it is not possible to entirely eliminate government-imposed barriers, such as those occupational licenses deemed necessary for health and safety, some may choose to look to more activist policies to induce additional labor supply. In other areas where technological change or increasing trade exposure might have contributed to declining work among some men, policymakers could choose to study the best program designs to help better align worker skills with employer needs. These categories of reforms are likely second- or third-best solutions that paper over underlying issues caused by other government programs or policies.

#### *Wage Subsidies*

Where work requirements and scaled-back welfare spending for the able-bodied are not enough to encourage disconnected men to rejoin the labor force, public policy might be able to increase the rewards to labor and strengthen the incentives for work.

Boosting wages may seem to call for a straightforward policy reform: increase the federal minimum wage—currently at $7.25—so that it encourages more Americans to work. The consequences of such a policy would likely create an additional barrier to employment, and make it more attractive but more difficult for disconnected men to leave the sidelines. Although the minimum wage literature is contested, many studies find negative consequences for workers.[225] For example, recent evidence indicates that minimum wage increases reduced overall employment—particularly for low-wage, low-skill workers.[226] Furthermore, the effects of the minimum wage on employment differ considerably across geographies with varying costs of living, potentially hurting those regions with more tenuous workforce connections the most.[227] In fact, evidence suggests that minimum wage increases can worsen the health outcomes of out-of-work men and can incentivize low-income youth to drop out of school, which lowers their future earning potential.[228] As a policy measure to serve disconnected men, a federal minimum wage increase may cause more harm than good.

An alternative approach to increase wages without reducing labor demand is a government-funded wage subsidy to increase workers' take-home pay. Unlike cash benefits, wage subsidies ipso facto require work to receive the benefit and provide an additional incentive for those out of the labor force to seek employment. There are a number of forms of wage subsidies, both tried and untried, and not all of them are created equal.

Since its introduction in 1975, the Earned Income Tax Credit (EITC) grew to become the largest federal cash-transfer program for low-income families. Especially after the 1996 welfare reform, the EITC became one of the government's primary tools to support poor families, with 25 million eligible workers and families receiving about $61 billion in benefits in 2019.[229] As a refundable income tax credit, the EITC acts as an indirect wage support, the cost of which is borne by taxpayers, not employers. This has the effect, unlike a price floor or minimum wage, of increasing the labor supply without decreasing employer demand. It also calibrates the size of the subsidy to annual earnings and concentrates aid to parents with children. By being considerably less generous to single filers without dependents, it does not provide the same incentives to idle, prime-age men, many of whom are unmarried and childless.

The EITC is thought of by many as a policy success: incentivizing additional work, compensating for the negative employment effects of the payroll tax, and as an anti-poverty tool. The credit may have "substantial effects" on labor supply decisions among low-income parents—especially single mothers.[230] Some argue that a "large share" of the "unprecedented increases" in work among low-income women through the 1990s was attributable to the EITC,[231] though the magnitude of its effect remains in contention. Other factors, such as welfare reform and a healthy labor market, may explain much of the observed increases in labor supply.[232] EITC expansion for childless workers enjoys bipartisan support as President Barack Obama and House Speaker Paul Ryan endorsed identical expansion plans in 2016.[233] However, two recent state-level expansions of the EITC for childless workers—a well-targeted reform for inactive men—showed very small or no impact on employment, no increases in earnings, and did not impact other crucial indicators of well-being.[234]

Despite its popularity, the credit is not without its share of problems. The complex credit structure results in large overhead costs at the Internal Revenue Service, although administrative costs are not as high as other welfare programs.[235] Meanwhile, administrators struggle with basic compliance—particularly around individuals claiming non-resident dependents—and report an estimated 25 percent rate of improper payment.[236] As an annual, lump-sum payment, it operates like a government check in the mail, not an actual subsidy in each paystub. A little-used periodic payment option was available until 2010 when it was discontinued as recommended in President Obama's FY 2010 budget proposal due to "extensive non-compliance by employers and workers."[237]

The EITC may also not generate the desired outcomes for program participants. By increasing labor supply, the EITC may decrease the bargaining power of low-wage workers, which has been shown to slow market wage growth.[238] There is also some limited evidence that the credit's phase-out range may pose a modest work disincentive for some workers, as beneficiaries reduce their total number of hours worked in order to maximize their earnings with the credit.[239] These negative effects are mitigated by the credit's complexity and are consequently difficult to see in the data.[240] Its real value also varies by geography. This means that eligibility

and phase-out ranges have stronger incentives in low-cost regions than in high-cost ones.[241]

The EITC could be reformed in a number of different ways to address low attachment to the labor force. A pro-worker EITC reform, for example, would remove marriage penalties and could be more generous to single, childless workers who are at risk for dropping out of the labor force altogether. However, the latter change might reduce their incentives to marry. Other potential reforms include an extended phase-out range to limit the disincentives of the current "earnings cliff." Congress and the IRS could also address fraud by simplifying the credit and adopting a standard method for claiming dependents across programs. Reforms could also experiment with alternative approaches to the wage subsidy model, such as periodic payments or a payroll tax credit. These and other reform proposals merit further consideration, research, and evaluation.

Given the challenges endemic to income tax credits, some have proffered a more direct wage subsidy as a preferable alternative.[242] Instead of lump-sum payments from the IRS, employees would receive a government-funded subsidy payment directly in their regular paycheck. An incentive based on hours worked, rather than annual income, may also present distinct advantages for workers looking to take on an additional job or work extra hours because they would not risk reduced benefits. A direct wage subsidy is not without its own challenges and limitations. Not all of the benefits, for instance, will go directly to workers. As is demonstrated by the EITC, employers could capture the value of the subsidy by lowering market wages and letting the government pay the difference. The "wage-support tool offers distinct administrative challenges," such as costly new administrative infrastructure and new burdens on employers.[243] Furthermore, complexity arises when annual income is not considered, such as in cases where workers have a second job, do not work full-time or year-round, or work as an independent contractor.[244] Nonetheless, some policymakers may want to experiment with new forms of wage subsidies to determine their feasibility and to measure their effect on employment and labor force participation.

In the search for flexible and simple policy interventions, policymakers should avoid the trap of deprioritizing work in the pursuit of a panacea. A Universal Basic Income (UBI), for example, has been proposed as a straightforward solution to unemployment of low-wage, low-skill workers.[245] While a UBI features administrative simplicity and greater flexibility for beneficiaries, it is, at best, apathetic to the social costs associated with being disconnected from the workforce and other institutions of civil society. As an unconditional benefit, it contains an implicit work disincentive and could function in the ways that SSDI and SSI effectively do: as long-term unemployment insurance.[246] Indeed, UBI and other unconditional benefit proposals are often motivated by flawed analysis that accepts a demand-side explanation for inactivity and reflects either an inability or an unwillingness to address the needs of America's disconnected and out of work men. Instead of the palliative care of UBI, policymakers should adopt a surgical approach for disconnected men's diagnosis. Removing disincentives to work

in existing programs, removing government-imposed barriers, and reforming existing wage subsidies could be practical places to start.

*Better Matching Skills to Employer Demand*

Another way to expand employment opportunities is to invest in human capital to help jobseekers become more employable. Even in economies where demand for labor is strong, the available workforce may lack the skills necessary for the jobs available. This so-called "skills gap"—a mismatch between the skills employers seek and the skills jobseekers possess—is often overstated as a market failure or blamed for broader labor-market trends, as reviewed in the section above on skills-based technological change. In the absence of government interference, there are strong private incentives for workers to build the skills their employers require and for employers to help current and future employees acquire in-demand skills.

To the extent there are workers who need help reskilling, the politically popular and seemingly easy solution of government-subsidized or government-run career and technical education programming has, at best, mixed success.[247] Rigorous evaluations of current government employment and training programs find that the benefits tend to be small and, in some cases, have made participants worse off. For example, the Trade Adjustment Assistance (TAA) program provides benefits and retraining for qualifying workers who have lost their job due to increased foreign imports. The most recent program analysis concluded that four years after enrollment in the program, "TAA participants had lower earnings than the comparison group."[248] In a 2019 review of the more than 40 different government workforce programs, the CEA found that job training programs are "largely ineffective" and that, in light of their costs, they "have a negative net benefit."[249] The poor results of these programs may actually be a positive sign. In most studies the control population—the workers who do not enroll in the program—tend to find jobs and advance in careers without the government assistance, making it difficult to measure any benefit from the government-subsidized program. Often, the market alternative is as good, or better than what the government has to offer.

Still, there have been a few successful models of workforce development programs that emerged in recent years and could inform federal policy. The "sector-based training" approach involves collaboration between employers in a high-demand industry, expert training providers, and intermediaries who facilitate the collaboration.[250] Rigorous evaluation of sector-specific training programs show some success but may be challenging to scale nationwide.[251] More than three decades of making and remaking federal training programs should remind policymakers that there is no panacea, but that considerable reforms to existing programs so that services are more responsive to employer needs and local markets, could show promise in helping some Americans find new purpose and opportunity in work.

Similar reforms have also taken place to better orient federally recognized apprenticeships to employer demand. Before the Biden Administration ended the initiative in February 2021, the Department of Labor developed a new industry-recognized apprenticeship program designation (IRAPs), in addition to the more formal Registered Apprenticeship designation. These programs include paid work, work-based learning, and participants receive at least one industry-recognized credential with which to pursue future employment opportunities.[252] Registered Apprenticeships "substantially" increase participant earnings, likely because they incorporate a diverse group of stakeholders, including trade associations, employer groups, educational institutions, state and local governments, non-profit organizations, and labor unions.[253] Registered Apprenticeships comprise only a small portion of the overall private training and development infrastructure. In total, private employers make up about half of the more than $1 trillion spent on post-secondary education and training each year. Federal outlays for job training make up less than 2 percent.[254] If policymakers think they can improve the private system of skills development, things like flexible approaches to accreditation could serve as a model for other workforce development programs.[255]

Federal policy could also address rules that govern private funding of skills development and training. Taking on new student debt is not financially viable for many Americans seeking occupational training—particularly in the case of a mid- or late-stage career change. One promising avenue for funding support is an Income-share Agreement (ISA), whereby students pay nothing upfront but agree to pay some portion of their income post-graduation for a specific period.[256] The fast-growing, online coding bootcamp, Lambda School, adopted the ISA model,[257] as have some major universities, such as Purdue and Clarkson.[258] ISAs have the possibility of realigning incentives of education institutions, making revenue contingent on student outcomes, while also reducing the risks of default for students.[259] Federal policymakers could consider legislation that clarifies the legality and enforceability of ISAs to reduce investor uncertainty.[260]

Another important way that federal policy could support workforce development and re-skilling efforts is through accreditation reform. Non-degree credentials and work-experience programs are already quite popular and effective for workers without a college degree. An estimated thirty-two percent of the American working class has a license or certificate from such a program.[261] Yet there exists no framework by which to evaluate and compare the effectiveness of non-degree programs and credentials. Moreover, unaccredited programs are ineligible to receive federal aid.[262] Federal policymakers could consider new models of federal funding that pair financial aid with quality-assurance measures, such as Virginia's FastForward program.[263] Other reforms might transform the accreditation system, such as Senator Lee's Higher Education Reform Opportunity (HERO) Act, which—in addition to streamlining federal aid, realigning education providers' incentives, and providing greater transparency into student success—enables states to accredit any post-secondary institution.[264]

*Additional Ways to Connect More Americans to Work*

Some of the reforms suggested thus far could provide immediate improvements to workforce connections as the pandemic fully recedes, providing a better foundation for the post-pandemic labor market. Monetary policy and organized labor are two remaining factors that affect workforce connections.

*Stable Monetary Policy*

One important criterion for keeping consistent connections to work is macroeconomic stability. While some unemployment or non-employment is structural, at least some is a product of the business cycle. This cyclical unemployment can be mitigated with a stable and consistent monetary policy. A recent Social Capital Project report, "Stable Monetary Policy to Connect More Americans to Work," suggests that a monetary policy that stabilizes nominal income would allow for a more stable labor market. This is because wages—which are difficult to adjust and often based on longer-term contracts—do not have to adjust much on average if aggregate nominal income growth is stable.[265] The rest of the economy can then set prices around those anchored expectations.

While this policy idea is mainly about creating stability to avoid short-run instances of disequilibrium in labor markets and mitigating short-run economic effects, it may also help in the longer run. Spells of unemployment may create atrophy in worker skills and social capital that then make it harder for the worker to get a job later. In this way, sufficiently-damaging cyclical unemployment can eventually become structural. The mitigation of cyclical unemployment through stable monetary policy may therefore help some long-run structural trends—though of course, other structural problems like health, education, and government disincentives may remain.

It is particularly important to consider this relationship, where short-run unemployment may turn into lingering long-run nonemployment through atrophy and hysteresis, in the recovery from the COVID-19 pandemic. Losing work experience—in some cases more than a year's worth—may cause longer-run structural damage. It is therefore imperative to return to full employment as quickly as possible.

*Labor Reform*

Organized labor historically served an important albeit adversarial role in the building and maintenance of connections to work among its members.[266] Labor unions secured worker benefits and protections, negotiated higher wages, and built a sense of solidarity among members. Today, however, private-sector union membership is at an all-time low with only 6.3 percent of workers listed as union members.[267] Labor unions were not designed to adapt to global competition, advanced technologies, fractured industries, and diffuse labor markets—much less a post-industrial "gig economy" in which there exists no traditional employer.

Policy leaders and union leadership should consider ways in which unions can evolve to meet the needs of twenty-first century, predominantly post-industrial workers.

Unions could offer distinct advantages over employers, governments, and other organizations in the provision of various benefits and services. For example, unions could connect employers to workforces and offer low-cost or free job training and professional development programs to workers in coordination with employers, universities and community colleges, and industry associations. They could advocate for member interests in the industry, provide individual career development and advancement like a professional association, and support for individual worker negotiations. Moreover, unions could have greater flexibility in the provision of low-cost portable insurance and benefits to its members such as malpractice and employment insurance as well as life, retirement (e.g., defined-contribution plans), and health insurance coverage.

There are a few ways federal policy could encourage experimentation. Reform of federal labor law could remove unions' "exclusive representation" privileges and permit direct worker negotiations with management. Eliminating exclusive representation privileges—the mandate that unions represent every employee of a business, regardless of whether the employee is a union member—would require unions to compete to attract their membership by offering useful services.[268] Reform could also institute "paycheck protections" to restrict unions' ability to use revenues from union dues for political activities without workers' express consent. "Right-to-work" provisions could also be incorporated into federal policy and thereby prevent workers from being fired for not being a union member. Such reforms would permit workers to organize on a members-only basis and with a more cooperative relationship with management.[269] Congress could also permit state and local governments, firms, and unions to opt out of certain federal labor laws to encourage experimentation with alternatives to existing standards that accomplish the purpose of the law. This type of policy experimentation could decentralize decision-making and recognize that the needs and interests of workers vary by state, locale, and firm.[270]

## CONCLUSION

At a time that is particularly fraught with concerns that our institutions no longer provide an opportunity for everyone to achieve their life ambitions, some may be disenchanted with the idea that work can enrich their livelihoods and provide upward mobility. For others, insurmountable obstacles may prevent them from obtaining meaningful work or starting a business.

While there are a myriad of reasons postulated about why fewer Americans in their prime earning years are attached to the labor force, it seems clear that low-wage and low-skill workers are now less willing to supply their labor than relatively higher skilled, higher wage counterparts. These reasons have less to do with increased difficulty in finding well-paying jobs, shrinking middle-skill

jobs, insufficient pay for productivity, or exposure to trade. Increasing prime-age disconnectedness likely has more to do with demographic shifts, changing worker preferences, state and federal regulatory barriers, and increased attractiveness of federal and state supports. In addition to these longer running trends, Americans are still confronting the effects of a once-in-a-century global pandemic that dramatically and unevenly upended labor markets in ways that are still not fully understood.

Reconnecting inactive workers to the labor force will require careful consideration of poorly-designed federal benefits, wide-ranging regulations that exclude would-be workers from the labor market, and labor laws that restrict employee freedoms to work on their own terms. Policymakers must not forget that work can provide more than a paycheck; it can offer self-respect, a chance to thrive through personal achievements, and an opportunity to deepen community ties that build the foundation for robust social capital and a strong civil society. By revitalizing connections to work, we simultaneously strengthen families, communities, and civil society.[271]

Ultimately, work is a means of promoting wellbeing, not an end in itself. Improving connections to work and increasing the attractiveness of work, particularly among those most at risk for idleness or isolation, can significantly improve the economic, social, and mental well-being of disconnected Americans.

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## ENDNOTES


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(Steven Ruggles, Sarah Flood, Ronald Goeken, Josiah Grover, Erin Meyer, Jose Pacas, and Matthew Sobek. IPUMS USA: Version 11.0 [dataset]. Minneapolis, MN: IPUMS, 2021. https://doi.org/10.18128/D010.V11.0). Less than high school indicates someone went no further than 11th grade, BA Plus indicates four or more years of college. We use the 1% samples for 1940-1960 and the 1% Form 1 metro sample for 1970. Estimates for 1968 to 2020 from the Current Population Survey Annual Social and Economic Supplement via the Integrated Public Use Microdata Series Online Data Analysis System, https://sda.cps.ipums.org/sdaweb/analysis/?dataset=all_march_samples. (Sarah Flood, Miriam King, Renae Rodgers, Steven Ruggles and J. Robert Warren. Integrated Public Use Microdata Series, Current Population Survey: Version 8.0 [dataset]. Minneapolis, MN: IPUMS, 2020. https://doi.org/10.18128/D030.V8.0.) Less than high school indicates a person went no further than 11th grade (1968-1991) or attended 12th grade but received no diploma (1992-2020). BA Plus indicates four or more years of college (1968-1991) or bachelor's degree or higher (1992-2020). We combine categories between LTHS and BA Plus into high school/some college (HS/CS), which includes 12th grade (unless "no diploma" is indicated, as noted above) through 3 years of college, because of the coding change in the CPS in 1992 and because CPS trends did not line up well with decennial census and American Community Survey (ACS) trends when keeping "high school only" and "some college" as separate categories. All estimates are for adults ages 25-54 and all exclude adults living in group quarters.

When we include 2020 data from ASEC, there may be limitations in its comparability to previous years due to the pandemic. ASEC shows LFPR rising for prime-age women in 2020 (when it is conducted in February-April of the year with bulk of it conducted in March when non-response was abnormally high, particularly among lower income groups), counter to BLS data (which covers the full year of 2020).

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    The trend for the average hourly earnings of production and nonsupervisory workers from 1939 to 2019 primarily comes from the Bureau of Labor Statistics Current Employment Statistics website at https://www.bls.gov/ces/data/. The estimates for 1964 to 2019 are annual averages for all private production and nonsupervisory workers, taken from the database that may be queried from that website (Series CEU0500000008). The trend is backcasted to 1947 using annual averages for all private production workers, obtained from Figure 4B of the Economic Policy Institute's *State of Working America* (Mishel, Lawrence, Josh Bivens, Elise Gould, and Heidi Shierholz (2012). *The State of Working America, 12th Edition*. Ithaca, N.Y.: Cornell University Press. http://www.stateofworkingamerica.org/index.html%3Fp=28476.html. See https://www.epi.org/publication/understanding-the-historic-divergence-between-productivity-and-a-typical-workers-pay-why-it-matters-and-why-its-real/#epi-toc-11 for additional detail on their methods.) The trend is further backcasted to 1939 using annual averages for workers in the durable-goods-producing sector, available via the CES website (Series CEU3100000001). Trends from 1939 to 1947 are also available for workers in the manufacturing sector and in the nondurable-goods-producing sector, but compared with the durable-goods-producing sector, these trends do not align as well from 1947 to 1964 with the private

production trend.

The hourly pay estimates are put into constant 2019 dollars by adjusting them for inflation using the Personal Consumption Expenditures (PCE) deflator. (For the case for using the PCE deflator, see Appendix 2 of Scott Winship, "Poverty after Welfare Reform," Manhattan Institute, 2016, https://media4.manhattan-institute.org/sites/default/files/R-SW-0816.pdf.) The EPI estimates are deflated using a different index, the CPI-U-RS, so we first convert them to nominal dollars before applying the PCE deflator.

48. Using the average hourly earnings measure for production and nonsupervisory workers, the increase from 1991 to 2019 was 34 percent, or 1.0 percent per year. But rising inequality among such workers raises the average more than the median among all wage and salary workers, making it decreasingly accurate as an indicator for the "typical" worker.

49. Social Capital Project analyses of Current Population Survey microdata. See endnote 47.

*50.* *Ibid*. In 1992, the educational attainment variable changed from one that reflected years of schooling to one that reflected degree attainment for those with schooling beyond high school.

51. Computed from the National Income and Product Accounts Table 2.1. Included in non-wage compensation are "Contributions consisting of employer payments (including payments-in-kind) to private pension and profit-sharing plans, publicly administered government employee retirement plans, private group health and life insurance plans, privately administered workers' compensation plans, and supplemental unemployment benefit plans, formerly called other labor income," as well as "Employer contributions for government social insurance as well as payments by employees, the self-employed, and other individuals who participate in government social insurance programs." See https://www.bea.gov/help/glossary/supplements-wages-and-salaries.

52. Social Capital Project analyses of Current Population Survey data. See endnote 47 for details. We multiply hourly wages for each percentile in each year by the ratio of compensation to wages in the Bureau of Economic Analysis's National Income and Product Accounts (NIPA) Table 2.1 (lines 2 and 3). Compensation includes employer fringe benefits to wages and salaries and employer contributions to government social insurance (employer payroll taxes). While these compensation figures are for workers in the aggregate, we apply them to the hourly wages at the 10th, 30th, 50th, 70th, and 90th percentiles of prime-age men.

The assumption that the aggregate ratio of compensation to wages is the same as the ratio at these percentiles (for prime-age men) is only problematic for trends insofar as the extent to which this assumption is wrong varies over time. In previous work, we compared similar compensation-to-wage ratios for 1979 and for the years from 2009 to 2019 to two external sources that provided information about the ratios for different parts of the wage and salary distribution. (See Rachel Sheffield and Scott Winship, "The Demise of the Happy Two-Parent Home," Social Capital Project, US Joint Economic Committee of Congress, 2020, https://www.jec.senate.gov/public/index.cfm/republicans/2020/7/the-demise-of-the-happy-two-parent-home#_edn56.) For 1979 evidence, see Timothy Smeeding, "The Size Distribution of Wage and Nonwage Compensation: Employer Cost versus Employee Value," in Jack

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For 2009-to-2019 evidence, we turned to the Bureau of Labor Statistics Employer Costs for Employee Compensation tables at https://www.bls.gov/ncs/#tables, which allow for the comparison of fringe benefits (excluding legally required contributions) to wages and salaries at the 10th percentile of compensation and the median compensation level. These ratios range from 11 to 12 percent for the 10th percentile and from 34 to 37 percent at the median. The BEA estimates (again, excluding employer contributions to social insurance for comparability) range from 16 to 17 percent.

At the tenth percentile, then, our ratios have the effect of overstating compensation at the 10th percentile, but by a similar amount in 1979 as in 2019. Thus, the trend should not be affected greatly (at least between 1979 and 2019). At the median, our 1979 estimate is likely to be accurate, but our 2019 compensation estimate is probably too low. Thus, our figures likely understate median wage growth. One caveat is that these external estimates of compensation-to-wages are for workers in the aggregate rather than for prime-age men. A second is that fringe benefits are valued at employers' costs, while employees might value these benefits differently than they would cash (more flexible but taxed). Smeeding estimates the distinction makes little difference in 1979.

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Line 2 adjusts the estimates in Line 1 by multiplying them by a ratio that compares

annual compensation to annual wages and salaries, using the aggregate figures for employees from the Bureau of Economic Analysis's National Income and Product Accounts (NIPA) Table 2.1 (lines 2 and 3). See the Figure 10 note for details.

Line 3 adds self-employment earnings from businesses and farms to annual compensation (adding to earnings for men shown in Line 2 if they have such income and adding men to the group shown in Line 2 whose earnings only come from self-employment). Line 4 adds some men who had no earnings as below median earners to account for the possibility that earnings trends are biased by declining labor force participation. It does so by assuming that the share of nonworking men who were disabled, sick, retired, or said they were nonworking for 'other' reasons not listed did not become a larger group between 1973 and 2019 relative to workers. It holds this share constant within three age groups (25-34, 35-44, and 45-54). It also adds back to the data, as below-median earners, all men in each year who did not work because they said they could not find a job.

55. Estimating annual compensation involves the same ratio adjustment described above for hourly compensation.

56. No compensation adjustment is made to the earnings of the self-employed.

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# Stable Monetary Policy to Connect More Americans to Work

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## INTRODUCTION

Deep recessions are not only economic, but social disasters. Lost income makes it less affordable to start and maintain families. Layoffs disconnect people—often already-marginalized people—from the labor force, depriving them of the social ties, emotional stability, and structure that come with working life. Both financial and personal investment into the institutions of civil society decline. Some of these wounds heal with the labor market during recoveries. Others leave long-lasting—even permanent—scars.

After the longest expansion on record, culminating in low unemployment rates not seen in half a century, the coronavirus pandemic plunged the United States overnight into a severe recession. While the ongoing downturn was clearly produced by an external shock unrelated to the state of the economy or economic policy, such recessions have, in recent decades, tended to be the exception rather than the rule. Just as more effective public health policies might have headed off the current recession, better economic policies might have averted many recessions in the past, including the Great Recession, and could prevent future recessions.

Avoiding future costly downturns like the Great Recession should be a top priority of economic policy. This report will trace the ways that monetary policy, in particular, can be improved to avoid the mistakes of the recent past and the consequences of those mistakes. Monetary policy in the United States is implemented by a central bank, the Federal Reserve, with objectives established for it by Congress.

It might be ideal if federal policymakers could ignore monetary policy, or somehow put it on autopilot, leaving people free to exchange good and services without government having to concern itself with the amount of currency in the economy or interest rates. Unfortunately, short term conditions can change in ways that cause spending to grow more slowly or fall, creating a shortage of currency in circulation. As discussed below, the long-term nature of contracts and the related tendency of prices and wages not to fall during downturns can prevent quick market corrections. Consumers, lenders, employers, and other market participants may then react by continuing to slow their spending, prolonging the downturn. Eventually, the economy will return to a healthy equilibrium and adjust to new price levels, though potentially with large temporary economic costs in the form of joblessness. These costs can be avoided if, early on, central banks increase the supply of currency in circulation.

At other times spending will rise too quickly relative to what the economyis producing. The currency issuer can head off painful disequilibria characterized by inflation by reducing the supply of currency.[1]
Thoughtful analysts bucking convention have envisioned a world of competing currency offerings by private and public institutions, and questioned the economic, policy, and constitutional underpinnings of theFederal Reserve. This report does not address those arguments; rather,
it proceeds from the premise that the Federal Reserve will remain the monopoly issuer of currency. Given this role, it has to make decisions about how much currency to supply to the economy and when. Rules that anchor the currency supply to some economic benchmark promotepredictability and stability for the consumers and investors who use the currency. They also remove discretion from Federal Reserve officials, whosedecision-making is unavoidably influenced by the biases and pressures that affect even the most hard-headed analysts.

The best anchor for monetary policy decisions is nominal income or nominal spending—the amount of money people receive or pay out, whichmore or less equal out economy-wide. Under an ideal monetary regime, spending should not be too scarce (characterized by low investment and employment), but nor should it be too plentiful (characterized by high and increasing inflation). While this balance may be easier to imagine than to achieve, this report argues that stabilizing general expectations about the level of nominal income or nominal spending in the economy best allows the private sector to value individual goods and services in thecontext of that anchored expectation, and build long-term contracts with a reasonable degree of certainty. This target could also be understood as steady growth in the money supply, adjusted for the private sector's abilityto circulate that money supply faster or slower.

Unfortunately, Federal Reserve policy from 2007-2018 erred too far towardscurbing the growth of nominal spending—a stance known colloquially as"too tight" monetary policy. The result was a long, persistent "output gap," or shortfall in GDP relative to what the economy could have produced with more ample nominal spending. While not the only policy problem of the time period, the output gap was a clear consequence of the Federal Reserve's choice of policy anchor and its level of commitment to the anchor.

The mass unemployment that followed the 2008 financial crisis was an economic disaster whose effects will be felt for years to come. Americanslost trillions of dollars of income and tens of millions of years of work. The job losses were also concentrated among disadvantaged groups, increasing inequality along the dimensions of both education and race.

This era is useful to study because it can inform policy in future recessions, including, to some extent, the current one. A well-chosen and consistent monetary policy anchor will not solve every problem—and certainly not ones directly related to public health—but it can facilitate the execution
of financial and business contracts and shore up the social contract bylowering uncertainty about the future.

## CHARACTERISTICS OF OUTPUT GAPS

Output gaps are the difference between actual output (what the economy produces) and potential output (the maximum amount the economy could produce sustainably over the long term with the general price level in equilibrium.)

The second half of this definition is a difficult counterfactual, one that can never be fully established as fact, but it is useful conceptually and at least somewhat measurable. The economy includes some long-run or "structural" unemployment; there was still some unemployment in 2007, and there was still some at the top of the 2020 economic peak. But there is also short-run or "cyclical" unemployment, which manifests in times of financial turmoil and thenrecedes as the economy improves.

Output gaps essentially involve the cyclical unemployment: the work and income lost to the business cycle. To the extent that output gaps aremeasurable, one could measure them in person-years of work lost, or cumulative GDP lost over time.

The most recent example of a typical large output gap comes from the 2008-2009 recession, when 8.7 million nonfarm jobs were shed. The output gap then persisted for about a decade; the jobs were not immediately regained, but rather, slowly added back over a period of many years.

Output gaps are frequently concurrent with—but distinct from—recessions. Recessions are typically defined through periods of output contraction (for example, two quarters of consecutive decline.) Output gaps are conceptually different from output contraction; they concern levels, not growth rates. An economy with an output gap is an economy that is smaller than it would be under normal financial conditions; and this could be the case regardless of whether it is growing or contracting at the moment.

It is possible to have a recession without an output gap; for example, an economy suffering from population loss could contract without having a problem of unemployed resources. It is also possible to have an output gap without a recession. For example, if many workers lost jobs due to a financial crisis, and the economy began gradually putting them back to work, one could see positive growth even as many were still jobless. There was an output gap well into the current recovery. Even an entirely recessionless period could includean output gap; for example, low aggregate demand could cause joblessness for many workers—and therefore, an output gap—even while productivity gains for other workers create enough growth to overcome that weakness and produce a positive aggregate growth number.

This report focuses on output gaps because they are undesirable, and they could be mitigated with commitment to a nominal income anchor.

*Output Gaps Begin with Slowdowns in Spending*

Output gaps tend to begin with a slowdown, or even a decrease, in spending throughout the economy. A sudden and sharp decrease, like that of 2007-2009, is known as an aggregate demand shock. Under such conditions, individuals and firms choose to hold more cash or government debt, and spend less on consumer goods or investments.

Spending is determined by both private-sector conditions and monetary policy conditions. For example, if new information shows that some private-sector investments or loans are riskier than people previously thought, they may respond by lending less to the risky private sector and holding more of their savings in riskless, government-issued financial assets. However, the government has some influence on this decision as well through the setting of short-run interest rates. If it sets interest rates higher than economic fundamentals warrant, people will park more of their money with the government to earn a risk-free return, and spend less money on investment and consumption; if the government sets interest rates relatively low, people will spend more.

Whatever the cause, a spending pullback in consumption and investment is almost by definition a reduction in nominal GDP, as those two components—consumption and investment—comprise the vast majority of GDP. Unless either foreigners or the government purchase more on net to offset a pullbackin spending from the private sector, nominal GDP must necessarily fall.

While nominal GDP is not the same as real GDP, there is a strong correlation between the two measures in practice. A fall, or even a slowdown, in nominal GDP often results in an output gap.

*Output Gaps are Disequilibria, Not Efficient Market Outcomes*

Shocks to nominal GDP (money spent) create shocks to real GDP (goods and services purchased), and output gaps, because they throw prices into disequilibrium. When nominal spending becomes scarcer, prices set prior to that scarcity will be too high. Consider a sharp drop in nominal spending likethat of the 2007-2009 demand shock. Prices set to be efficient and market- clearing in 2007, prior to the demand shock, were not efficient by the end of 2009. However, because many prices are slow to adjust—or, more colloquially, “sticky”—the old, too-high-for-2009 prices persisted despite their inefficiency, and markets failed to clear.

The pre-shock prices in such a situation function like a price floor in a basic microeconomic supply-and-demand model; if a price is set above the point at which supply and demand meet, there will be a surplus of producers willing to sell at the price, but a shortage of buyers. Fewer goods and services will be purchased or sold.

The most important of the prices thrown out of equilibrium by an unstable market are the prices for labor: wages, salaries, and benefits. By the end of 2009,there was a surplus of producers willing to sell their labor at prevailing wage levels, but a shortage of buyers. Put more simply: there was unemployment.

*The Market Cannot Adjust Immediately to Demand Shocks*

Markets are often resilient to some shocks, updating prices quickly and reaching new equilibria. It is worth asking why markets do not update quickly in response to aggregate demand shocks. If the economy efficiently employs resources at one level of nominal spending, why is another not equally good? Why can't prices just scale down by an appropriate factor, leaving the real economy—the amount of goods and services produced—entirely unchanged?

If this were possible, and every single dollar-denominated quantity changed by the same amount in the economy all at once, that would be fine and life would go on unchanged. However, in practice such immediate adjustment to a shock to nominal GDP is impossible. Free markets depend on long-run contracts, implicit and explicit. Job offers, mortgages, bonds, and leases all come with expectations—or even formal obligations—that last months, years, or decades into the future. Because these contracts cannot adjust, equilibria in the private sector cannot immediately adapt to unexpected changes in overall nominal spending.

Consider, in particular, the labor market, which is unusually slow to adapt. One might assume that it is at least legally possible for many employers to cut wages—and that their employees might, in the absence of better options, accept such cuts. In practice, this rarely happens. Empirically, wages are "sticky," and especially, "sticky downward." Research into wage changes for individual workers show that very few workers have their wages cut, but a large number of workers each year end up with a precisely zero change in their nominal wage.[2] [3] This distribution suggests that firms are reluctant to cut wages.While each employer has its own reasons, one clear reason to avoid cutting wages is that it is acrimonious to ask workers to accept the cuts.

Recent research extends the empirical evidence of sticky wages further, and shows that even for new hires—for employment contracts that do not even exist yet—employers are unlikely to cut wages for a particular job title during contractions.[4] There are many plausible ways to explain this behavior, but the simplest is that employers value some sort of equity between the new hires and incumbent employees of the same job.

Even unemployed workers—at least, those not immediately desperate for money—may contribute to the sticky wage phenomenon through aversion topay cuts when they take a new job. A worker who earned a particular salary inthe past may expect that salary again, even from a new employer.

Whatever the reasons for the empirical fact of sticky wages, the evidence is clear that nominal wage levels can endure for years without reaching equilibrium; if a wage level is too high to be market-clearing, the labor market will wait as long as it takes for that level to clear markets once more. In the meantime, though, unemployment will endure.

The same sort of dynamics affect other prices. A landlord might want to offer new customers lower rent in order to take units off the market, but doing so might require her to lower prices for her existing renters. So instead, vacant apartments take longer to fill.

Finally, firms often require the useful information embodied in other firms' prices in order to update appropriately. When a firm picks the optimum or equilibrium price for its own products, it does so not just based on the state ofthe economy as a whole, but also based on the asking prices of input goods used in the production process, or the listed prices of competing products. If all prices are thrown out of equilibrium at once—as happens in a recession—a firm cannot adjust completely to new conditions because of sluggish price adjustments from other firms.[5]

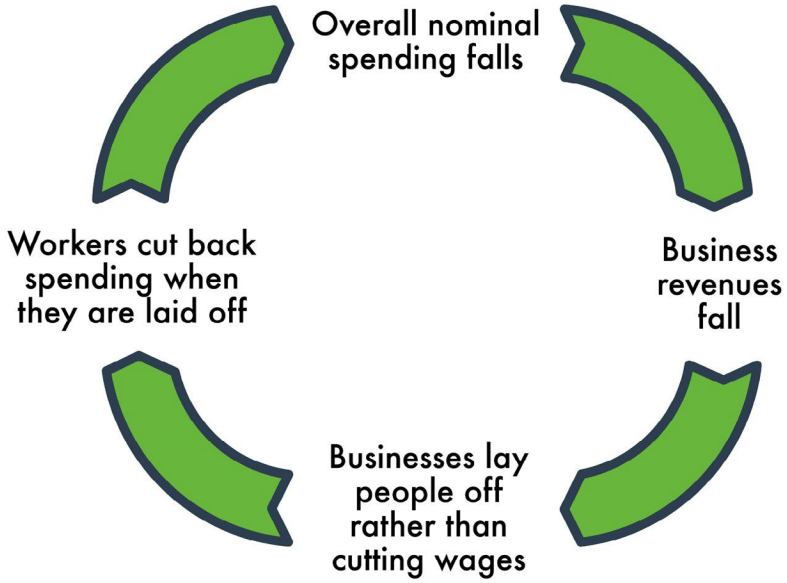
One feature—perhaps even the defining feature—of well-functioning free markets is that firms and individuals do not need to independently calculate the value of every good or service they purchase, sell, or compete with. They can instead take prices from others as a given and respond accordingly.
This channel breaks down during recessions, because all prices are out of equilibrium at once.

For example, a retailer might see signs of a recession when sales fall. It knows it must adjust its prices downward to keep its inventory moving. However, the wholesale prices of its inventory remain—at least for now—unchanged.
The retailer reduces its prices modestly, but not too much, in order to protect its margins. Later on, it becomes clear that the retailer's suppliers are also struggling to move their products in the recession, and they cut prices as well. Then, and only then, can the retailer cut prices further, spurring sales while still making a reasonable margin on its sales. Rather than a single price adjustmentto restore equilibrium, the retailer has to go through a slow, iterated process where firms react to each other's price updates.

Simple economic models use a frictionless theory of the economy where smart agents update their prices immediately to address surpluses or shortages. Certainly, that is the rational thing to do, and people attempt to do it as fast as they can. However, it is more difficult than it looks on paper. Norms, contracts, loss aversion, and difficulties in gathering information all combine to create substantial inertia in overall price levels.

*Feedback Loops Compound the Problems of Demand Shocks*

A second reason that markets struggle to handle aggregate demand shocks is that demand shocks generate what economists call general equilibrium effects; disequilibria in money and wages are powerful enough to change the nature of the whole economy. Therefore, in analyzing the problem, it is not enough to note that too-high prices result in over-supply and under-demand for labor. One must then consider the impact this unemployment has on the economy as a whole, and any second-order results springing from that impact. In the case of cyclical unemployment, some of the major second-order results reinforce, rather than mitigate, the original problem. Spending in the economy falls, demand for labor falls, people become unemployed because of sticky wages, and then spending in the economy falls further because unemployed people spend less.




This kind of feedback loop can be extraordinarily powerful; it is the primary mechanism by which problems in mortgages in the mid-2000s ultimately resulted in millions of job losses for people in unrelated industries. The cycle shown above is not the only feedback loop present in recessions; for example, businesses cut back spending on capital goods in addition to labor, out of naturalfears that the capital good will not be a worthwhile investment with the economyin a downward spiral.

In fact, all throughout the economy, individuals and firms can respond to aggregate demand shocks by cutting back spending further. Savers shift their earnings from risky new investments in new or marginal capital to bidding up the prices of safer, less productive, assets. Consumers—even those who still holdjobs—decide to tighten their belts and hold more cash or cash equivalents, and eschew new loans.

One of the most powerful feedback loops can come from government policy; if the central bank is sluggish to respond to a demand shock, and maintains short-run interest rates at a too-high level, then government creates additionaldemand-side failure by offering lenders much better terms than the private

sector; it then becomes increasingly advantageous for savers to park their money with the federal government, rather than putting it to work funding more productive private-sector investments.

While not all of the general equilibrium effects of demand shocks are self-reinforcing, many of them are—and powerful enough that the problem can quickly run away from policymakers and become painful to resolve.

*Summary*

The description of output gaps above ultimately leads to two points about them: first, that output gaps are a considerable problem, and second, that they are related to the federal government policy choices in issuing currency.

Sharp, unexpected changes in the path of nominal spending—or demand shocks—throw prices out of equilibrium throughout the economy. Layoffs born of this problem are not efficient "creative destruction," or the magic of efficient markets at work; instead, they are glitches in the system of currency issuance, interacting with contract law, norms leading to sticky prices, and individually rational behavior creating feedback loops. Government compounds, rather than alleviates, this problem, when it offers attractive risk-free returns—essentially, above-market rates—on government assets during demand shocks, crowding out or deterring private spending.

Conditional on a policy framework where the federal government issues financial assets and legal tender, there must be some rules—implicit or explicit, mandatory or discretionary—that determine when government-issued financial assets are issued, and what they can be redeemed for.[6] These rules are monetary policy, and the government necessarily has one, whether it wants to or not.

Currency issuers must be aware of this consequence: the financial assets they issue create a "hurdle rate" for the currency's users; holding onto thoseassets is a choice for households and firms, one that competes directly withthe alternatives of holding private-sector financial assets or directly and immediately purchasing goods or services.

If government is to issue financial assets, it should do so in a way that minimizes distortions. As the harms of output gaps are severe, government should make sure that its issuance of financial assets does not unintentionally distort markets and create output gaps unnecessarily.

## THE PAIN OF OUTPUT GAPS IS INTENSE AND CONCENTRATED AMONG THE MOST ECONOMICALLY DISADVANTAGED

We can reliably make at least two quantitative claims about output gaps: the first is that they are especially large economic policy problems. The second is that the pain from output gaps is unevenly distributed; those who lose their jobs suffer a great deal more than those who retain their jobs, or had savings in cash or bonds.

### *Output Gaps Constitute a Large Economic Inefficiency*

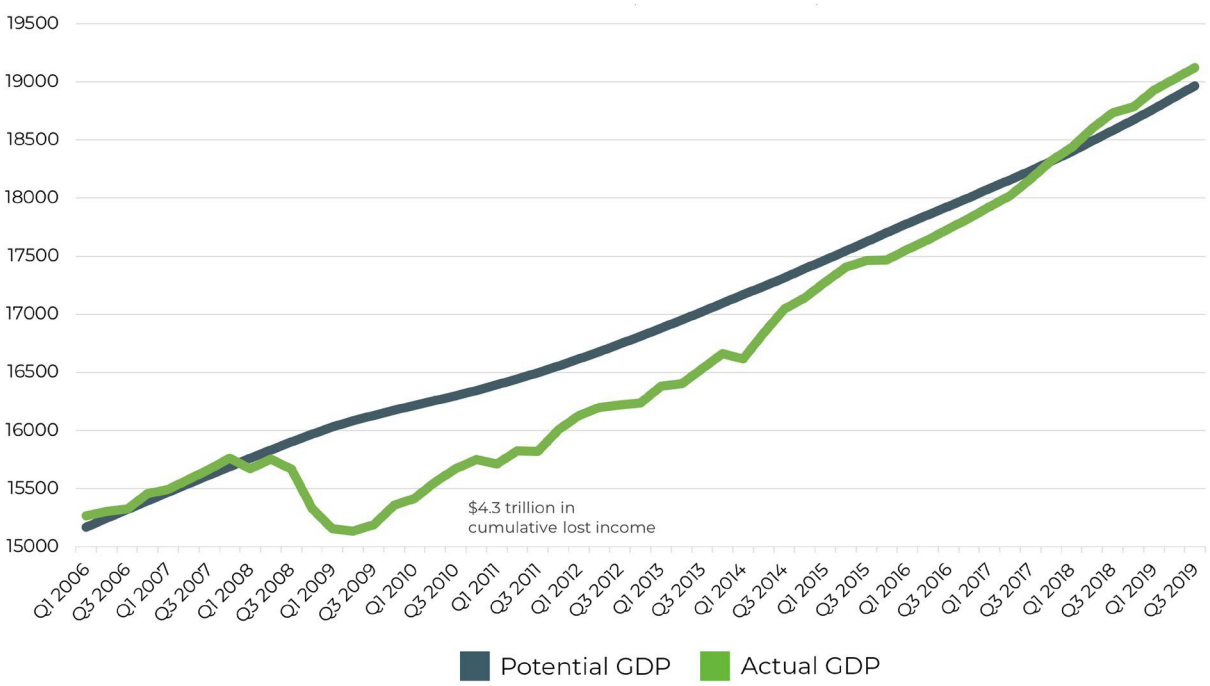
When economists speak of inefficiency, they usually think of suboptimal production; a worker produces one good rather than another, even though the second good would better maximize overall well-being. Inefficiency happens for a variety of reasons—regulations, taxes, monopolies restricting supply, environmental externalities—and it can be a serious problem.

However, suboptimal production is still production. It typically creates producer and consumer surplus—just not as much surplus as the most efficient outcome would have. By contrast, under an output gap, there are workers who remain unemployed entirely.
Output gaps are also more important than any industry-specific policy problem because they affect many or all industries simultaneously. The scale of job loss from the Global Financial Crisis—8.7 million lost, even as population grew— was orders of magnitude larger than other individual policy problems in the U.S. economy. More importantly, it remained large for years afterwards; the depressed levels of employment persisted.

### *Estimating the Total Cost of Last Decade's Output Gap*

Below are the official figures for actual GDP and potential GDP, as estimated by the Bureau of Economic Analysis (BEA) and Congressional Budget Office (CBO) throughout the recent decade. The CBO's measure of potential GDP is based primarily on assumptions about how fast productivity is expected to grow, and on how many people it expects could be employed sustainably without accelerating inflation. Multiplied together, these two factors produce potential GDP.[7]

Figure 1. Actual and Potential GDP (Billions of Chained 2012 Dollars)




Sources: U.S. Congressional Budget Office, Real Potential Gross Domestic Product [GDPPOT], retrieved from FRED, FederalReserve Bank of St. Louis; https://fred.stlouisfed.org/series/GDPPOT; U.S. Bureau of Economic Analysis, Real Gross DomesticProduct [GDPC1], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/GDPC1

One conventional measure of the cumulative cost of the output gap throughout the years quantifies the area between the curves from the start of the output gap to the end. By this measure of potential, the output gap began in the first quarter (Q1) of 2008 and ended in the third quarter (Q3) of 2017. By the CBO estimates, $4.3 trillion of income was foregone relative to potential.

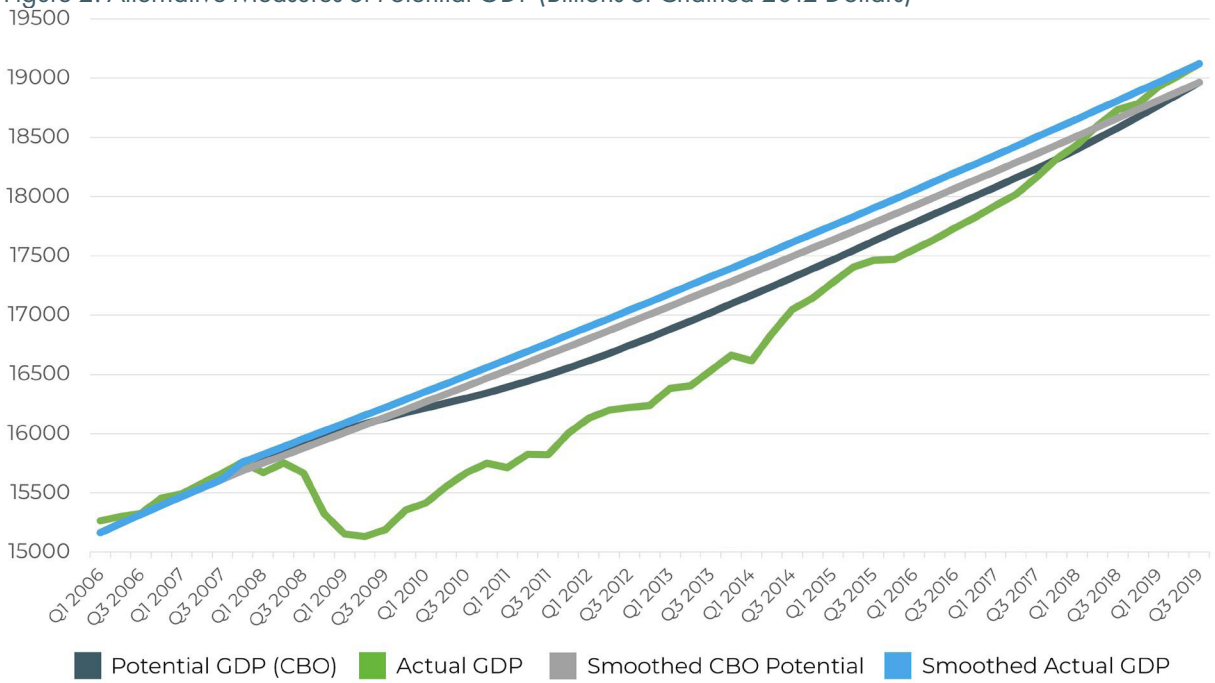
This number is immense. It is also likely a deep underestimate. Recent research shows estimates of potential GDP are correlated with demand shocks; in other words, we misidentify some of the business cycle as permanent change in the economy and understate potential GDP during recessions.[8] This would cause us to systematically underestimate the size of output gaps; for example, we might say a worker is structurally unemployed, only to see them return to work after the economy improves again.

There is good reason to believe this happened in the particular case of the 2007-2019 output gap. First, because the phenomenon described is actually visible on the chart of CBO's estimate of potential GDP. Rather than continuing upward at a roughly-steady exponential pace, it actually bends a little bit down towards actual GDP during the recession. Second, because the CBO bases its estimateof potential output heavily on its assumptions about the natural state of the labor market, and it got those assumptions wrong. In the early 2010s, CBO raisedits estimate of the long-run natural rate of unemployment, thereby assuming that

the economy had less potential than it really did. This assumption proved incorrect by the late 2010s when unemployment fell to historic lows, so CBO revised it back downward.

With the benefit of hindsight, we can come up with a better estimate of the latent potential of the 2010s US economy. The graph below shows two simple estimates of how potential GDP may have been higher between Q4 of 2007 and Q3 of 2019. The first estimate is a simple exponential growth path between the CBO's potential GDP estimates from those two quarters. In other words, it removes the "bend" in the CBO chart. A second, more aggressive estimate assumes the Q4 2007 and Q3 2019 figures are full employment, and draws an exponential growthpath between them to estimate potential output.

Figure 2. Alternative Measures of Potential GDP (Billions of Chained 2012 Dollars)



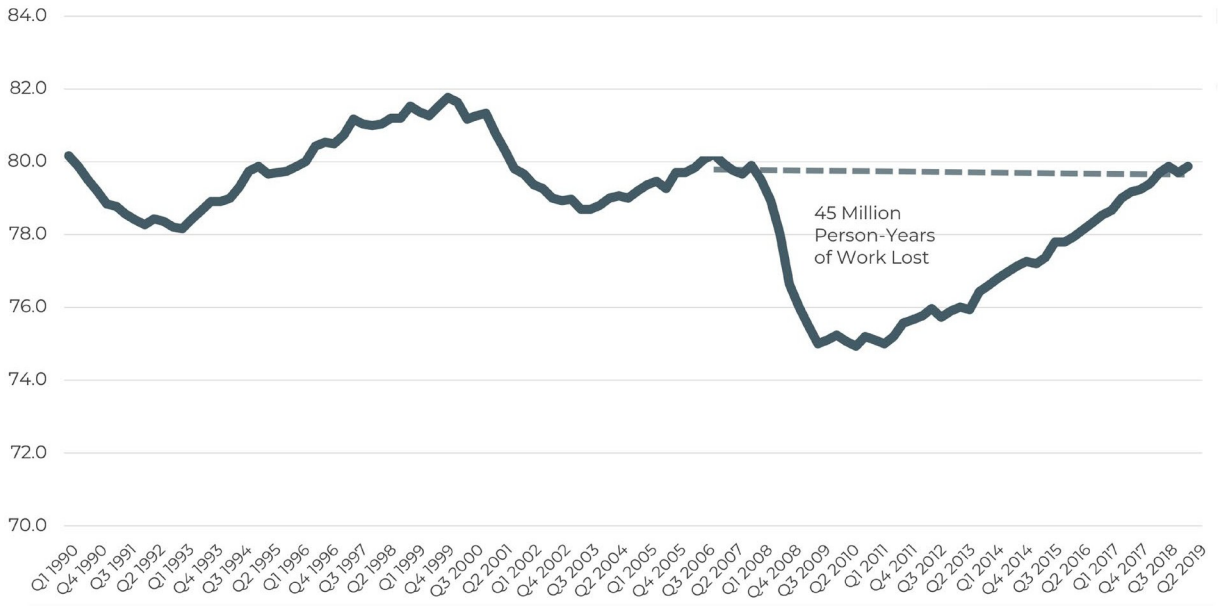

Sources: U.S. Congressional Budget Office, Real Potential Gross Domestic Product [GDPPOT], retrieved from FRED, FederalReserve Bank of St. Louis; https://fred.stlouisfed.org/series/GDPPOT; U.S. Bureau of Economic Analysis, Real Gross DomesticProduct [GDPC1], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/GDPC1

All three measures of potential output are reasonably similar for many purposes; however, if we do not allow potential output to "bend" downward—if we do not excuse possibly-cyclical unemployment as structural—we find the cumulative output gap to be larger than the CBO's estimate would suggest. Under the smoothed-out version of CBO potential we find the cumulative cost of the output gap to be $5.6 trillion. Under the more aggressive assumption, the cumulative cost of the output gap was $6.8 trillion.

Even the aggressive assumption—that GDP should have grown smoothly between 2007 and 2019 rather than having a big hole in the middle—is reasonable, and in fact may be a conservative estimate of the costs of the output gap. If there is a "hysteresis" effect—that is, we missed out on skill-building and capital investment due to the crisis—then productive capacity could have been even higher in 2019 if that hysteresis had not occurred.

There is another way to quantify the output gap, though, one that may be more meaningful in a social sense: this measure is denominated in jobs for workers of prime working age. In both 2007 and 2019, the share of prime-age (that is, 25-to-54-year-old) individuals with a job reached 80.2 percent. While this was not an all-time high, it was relatively close to the all-time high set in 2000.

Figure 3. Employment-Population Ratio, Age 25-54




Sources: U.S. Bureau of Labor Statistics, Employment-Population Ratio - 25-54 Yrs. [LNS12300060], retrieved from FRED, FederalReserve Bank of St. Louis; https://fred.stlouisfed.org/series/LNS12300060

Let us assume that this rate of employment is natural—that it would have been sustainable in the long run, absent the disequilibrium from the financial crisis. If this is the case, then 45 million person-years of work were lost among prime- age U.S. workers.

This estimate—despite its size—may be conservative: it does not include job losses for workers 55 and older—some of whom describe themselves as retired, but may have preferred to continue working under better circumstances. It also assumes—perhaps wrongly—that employment highs of the late 1990s and early 2000s are no longer an appropriate benchmark for full employment.

Nonetheless, even under conservative assumptions, the output gap in the United States since 2008 has been gargantuan; cumulatively over the period, in terms of both jobs and GDP, the lost output is greater than the annual output of Germany.

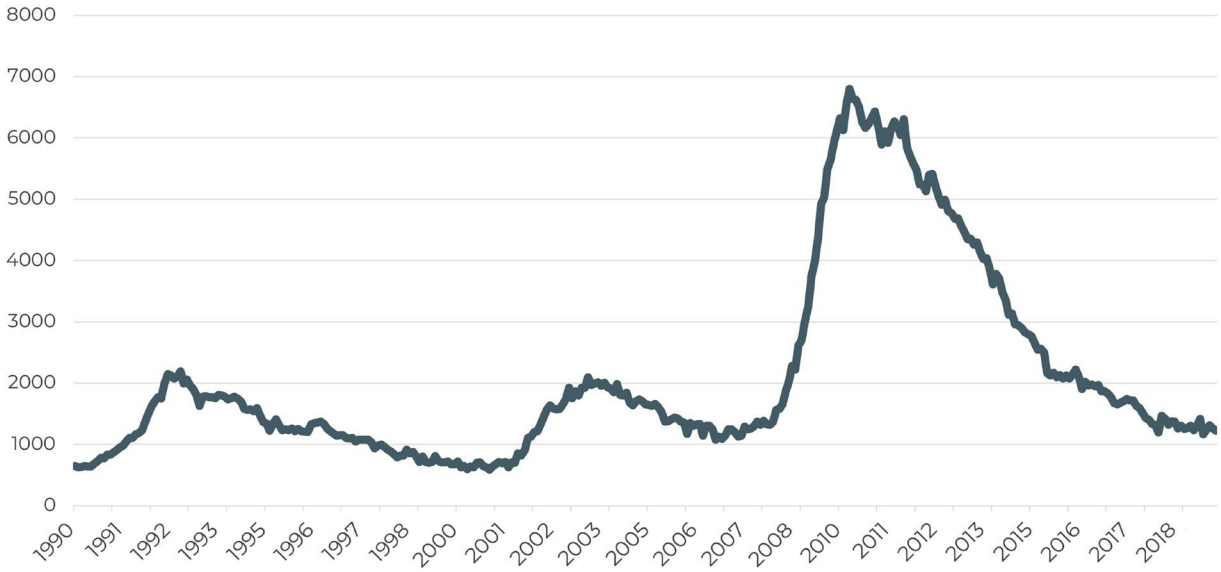
*The Concentration of Output Gaps*

It is also important to note that these losses were concentrated especially hard among particular Americans. One could imagine an evenly-distributed output gap—each individual loses two weeks a year worth of paid work, and suffers five percent lower income than they would have otherwise—but that is not the way that output gaps manifest in practice.

Instead, some people have their hours and income cut entirely through layoffs—or, more abstractly, through the absence of job offers that would otherwise havebeen extended in a better economy. Meanwhile, other workers are able to hold onto their existing jobs at their existing pay and hours.

One way to see the unequal distribution of unemployment is to observe the catastrophic rise in unemployment of 27 weeks or longer. At the peak of the output gap almost 7 million Americans reported being unemployed for morethan half a year. In other words, of the 45 million person-years of employmentlost due to the output gap, much of it was concentrated among especially unfortunate workers.

Figure 4. Unemployed 27 Weeks & Over, Thousands of Persons

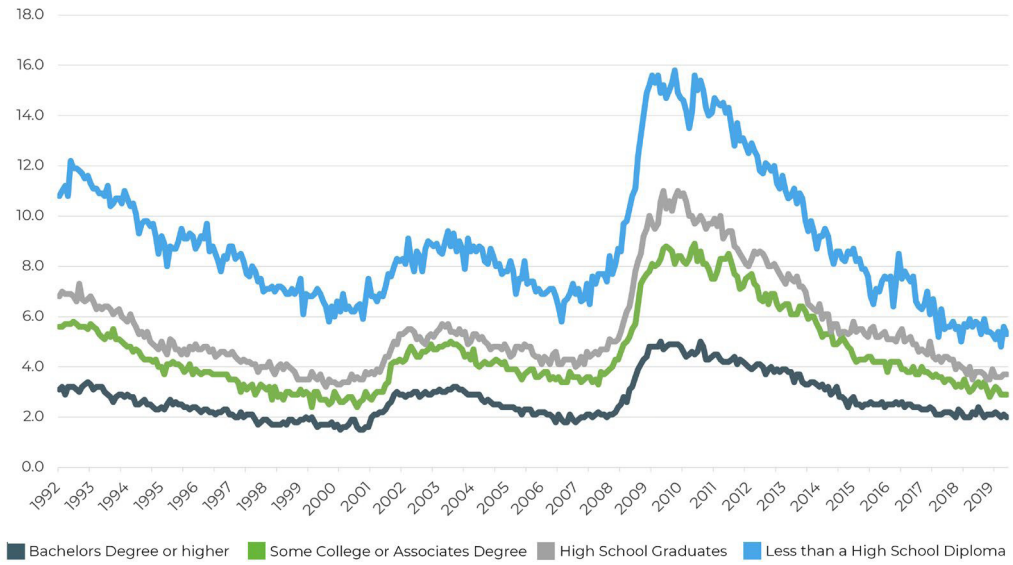



Sources: U.S. Bureau of Labor Statistics, Number Unemployed for 27 Weeks & Over [UEMP27OV], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/UEMP27OV

It is also important to note that the unemployed are not a random cross-section of the population. Rather, unemployment is concentrated among particular groups—typically, ones that already start at a disadvantage. Output gaps have an outsize negative impact on lower-education individuals and minorities—but conversely, those same workers stand to benefit more from a recovery.

A chart of unemployment rate by education shows that the most recent business cycle had a larger impact on less-educated individuals than on more-educated individuals. For example, the unemployment rate for those without a high school diploma rose and fell by about ten percentage points during the recession and the subsequent recovery. For college graduates, this figure was about three percent. College graduates and less-educated individuals both felt the same effects directionally, but the magnitude for less-educated individuals was greater.

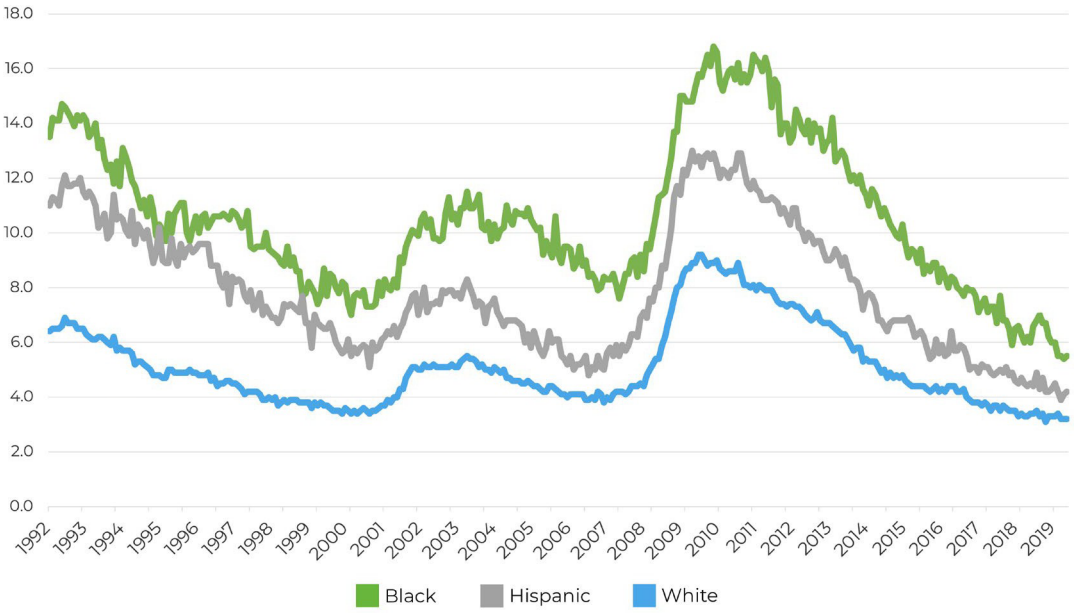
Figure 5. Unemployment Rate by Education




Source: U.S. Bureau of Labor Statistics, Unemployment Rate by Education [LNS14027662, LNS14027689, LNS14027660,LNS14027660], retrieved from FRED, Federal Reserve Bank of St. Louis

A similar story can be told by race. While unemployment rose for all groups during the financial crisis, and fell gradually throughout the recovery, the magnitude of the swing was considerably larger for black or Hispanic workers than for white ones. For example, while the business cycle involved about a fiveor six percentage point swing for white workers, it was a nine point swing for black ones.

Figure 6. Unemployment Rate by Race or Ethnicity




Source: U.S. Bureau of Labor Statistics, Unemployment Rate by Race [LNS14000003, LNS14000006, LNS14000009], retrieved fromFRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/LNS14000003

Both the analysis by education and the analysis by race reveal a kind of "last in first out" labor market: the demographic groups that generally have higher levelsof unemployment are the most sensitive to the business cycle.

This characteristic of the business cycle can unfortunately lend itself to some policy errors: one can credibly blame unemployment on structural factors, even when the cyclical component is more important. For example, one could say that the unemployed tend to be less-educated and have fewer skills. While this is true, unemployment can be multi-causal—both cyclical and structural—and tothe extent that the cyclical component can be addressed, it should be.

### *The Social and Psychological Impact of Output Gaps*

It is important to see the output gap as not just a loss of income, and not just as a loss of work, but also as a loss of the social capital that comes from financial stability and participation in working life.

As explored in previous research by the Joint Economic Committee's Social Capital Project, there are social and psychological benefits from inclusion in theworking world. In the project's Wealth of Relations paper, we note that inclusionin the world of working adults helps people build other sorts of social ties.[9]

Robert Putnam's bestseller Bowling Alone compiles a variety of evidence on the subject. Colleagues can account for a majority of a worker's daily conversations, and a substantial fraction of their friends—though typically not as many close friends as from other sources. Workplaces can also serve as recruiting grounds for other organizations in civil society. While Putnam believes workplaces cannot

replace the social ties that come from other civil society organizations, they do create connections to friends and organizations.[10]

In The Once and Future Worker, Oren Cass writes that work helps build skills useful in other areas of life, imposing structure and practice in "mundane but essential disciplines." He also argues that skill-building and self-reliance help build a sense of worth and self-respect.[11]

The strongest evidence of the value of work is perhaps in the alternative: the absence of work. A report by the Social Capital Project examining the lives of prime-age men without jobs shows that they are likely to self-report poorer mental well-being, fewer friends, and even lower participation in civic activities such as churchgoing.[12] One could hope that non-employment would free people's time up to help them build more social ties. However, on average, this does not seem to be the case; the non-employed, and especially non-employedmen, tend to struggle to find fulfilling uses of their time.[13]

In the relationship between employment and social capital, causality likely runs both ways; while those with more social capital are likely better at finding work, evidence also suggests that joblessness and income insecurity cause a decline in social relations. Job loss from recessions is associated with a rise in depressive symptoms.[14] Output gaps are also associated with a fall in parenthood[15] and delayed household formation.[16]
Furthermore, civil society more broadly suffers: the recent recession was associated with a decline in charitable giving, one that was slow to recover and even greater than would be expected by the drop in income alone.[17] Furthermore, survey results from the National Conference on Citizenship show that 72 percent of respondents reported cutting back time spent on volunteer work in the recession, and that 66 percent of respondents felt people were responding to hard times by looking out for themselves, not others.[18]

In some studies, output gaps are associated with a rise in suicides,[19] though this is contested.[20] While overall alcohol use—like most economic activity—declines in recessions, binge drinking rises.[21] The bulk of the evidence suggests that illegal drug use also increases in recessions due to personal stress, even despite a reduced ability to pay.[22]

All in all, output gaps cause not just lasting economic damage, but lasting social damage as well. The scars from our most recent output gap will take a long time to heal.

## MONETARY FAILURES OF THE GREAT RECESSION OUTPUT GAP

The output gap beginning in 2007 was unusually long-lasting and deep. By the Congressional Budget Office's estimates, it lasted for ten years and reached six percent of GDP.[23] Both of these problems were attributable in part to the Federal Reserve's too-tight monetary policy, a decade-long series of errors. These errors all ran in the same direction, curbing spending too much. This helped cause,

deepen, and lengthen the output gap. It is, of course, easier to identify these errors with the benefit of a dozen extra years of hindsight that contemporary decision-makers did not have. Indeed, many of the points belowhave already been acknowledged by past or current Federal Open Market Committee (FOMC) members. However, these mistakes are described here to better inform future choices.

*2007-2008: Scope Creep and Underreactivity*

In 2007-2008, the Federal Reserve made four major conceptual errors that contributed substantially to the crisis.

- Slow reaction to a worsening employment situation, starting in 2007;
- Overemphasis on oil prices, which are often (as in this case) un-representativeof the overall demand-side situation;
- Scope creep: attempts to cut down the housing market in 2007, even at the expense of the rest of the economy; and
- Constricted credit for the public at-large even as financial institutions got emergency lending and bailouts.

Underreactivity to Struggling Labor Markets

In the abbreviated telling of the 2008 financial crisis, the financial turmoil precedes the mass unemployment. For the most part, this was true; the most harrowing months of job loss came after the collapse of Lehman Brothers in September 2008. However, the labor market had stalled by 2007 and was clearly weakening.

In fact, the weakening labor market likely caused some of the later financial turmoil; with better job prospects, more people could have repaid mortgages, bolstered falling house prices, and provided equity and risk tolerance to capital markets.

Consider how four different measures of employment fared between their 2007 peaks and December of 2008, when the Federal Reserve finally exhausted its conventional policy tools and lowered rates all the way to zero.

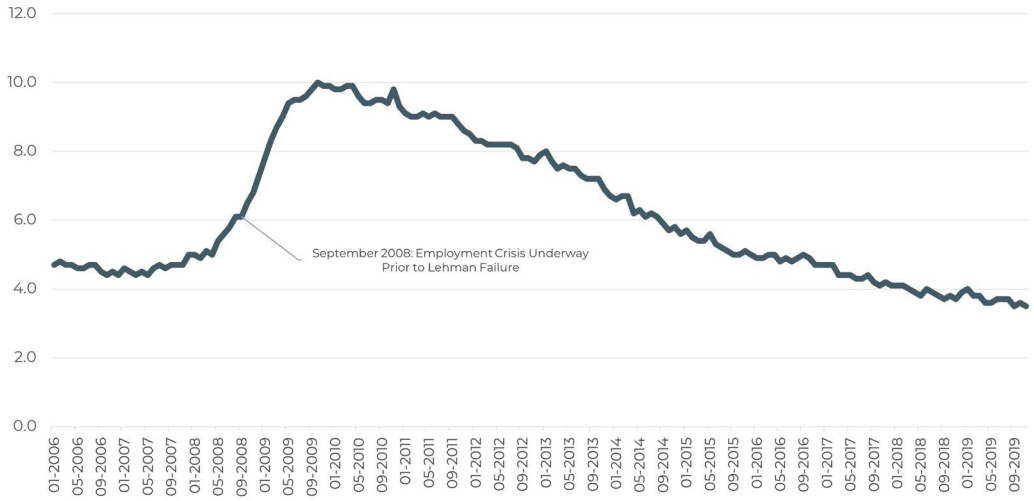
Beginning with the employment-to-population ratio among individuals age 25-54, or “prime-age employment-to-population ratio, in January of 2007, the ratio sat at 80.3 percent—off of its all-time highs, but strong. By March 2008, when Bear Stearns failed, it had dipped below 80 percent for good. By September 2008,when Lehman Brothers failed, the ratio had fallen below 79 percent. In December2008, when rates finally hit zero, the figure stood at 77.6 percent.

Figure 7. Employment Population Ratio (Age 25-54)

Source: U.S. Bureau of Labor Statistics, Employment-Population Ratio - 25-54 Yrs. [LNS12300060], retrieved from FRED, FederalReserve Bank of St. Louis; https://fred.stlouisfed.org/series/LNS12300060

The civilian unemployment rate told a similar story; in May of 2007, it was 4.4 percent—again, not its all-time best, but still good. By the time of the Bear Stearns failure, it was 5.1 percent. A particularly bad month in 2008 with a half-percent rise was largely ignored.[24] In September, when Lehman failed, the unemployment rate reached 6.1 percent, and by the time the Federal Reserve took interest rates to zero in December 2008, the unemployment rate was 7.3 percent.

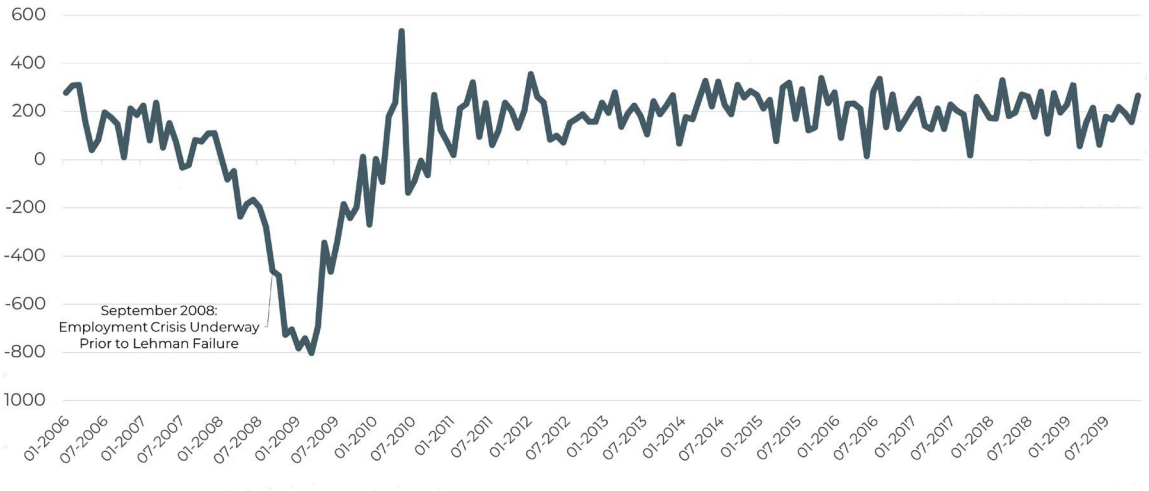
Figure 8. Unemployment Rate




Source: U.S. Bureau of Labor Statistics, Unemployment Rate [UNRATE], retrieved from FRED, Federal Reserve Bank of St. Louis;https://fred.stlouisfed.org/series/UNRATE

Nonfarm payrolls also showed distress: in the summer of 2007, two months showed negative payroll growth. In 2008, every single month except for January reported negative payroll growth—in other words, by December of 2008, when the Federal Reserve finally moved the federal funds rate to zero, the economy was in its eleventh consecutive negative-job-growth month.

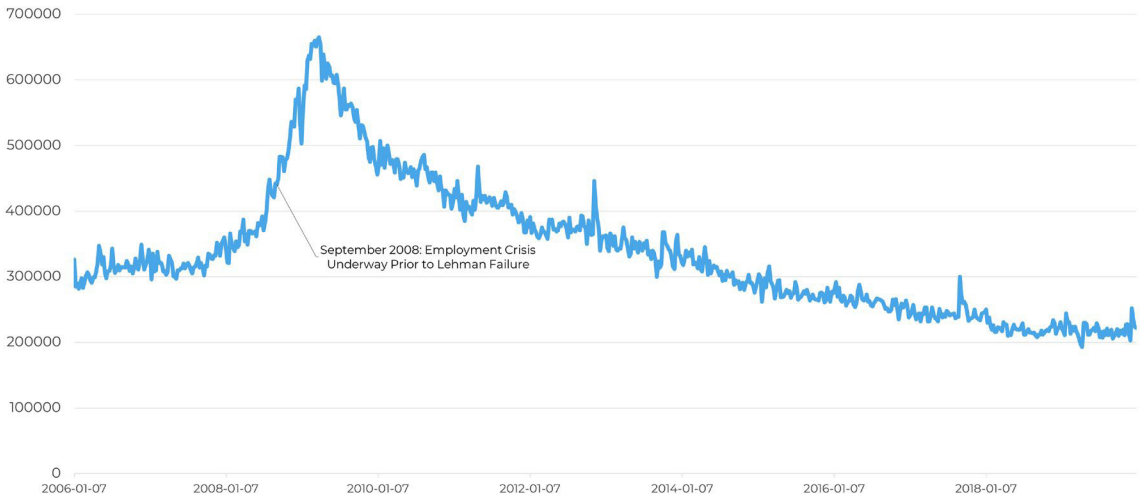
Figure 9. Change in Nonfarm Payrolls by Month (thousands)




Source: U.S. Bureau of Labor Statistics, All Employees, Total Nonfarm [PAYEMS], retrieved from FRED, Federal Reserve Bank of St.Louis; https://fred.stlouisfed.org/series/PAYEMS

A final measure of extreme distress is the weekly initial unemployment claims data. Initial claims of 300,000 per week were normal during the 2007 economy. By the time of the Bear Stearns fire sale in March, this count had accelerated to 368,000—the worst number since the aftermath of Hurricane Katrina. By the summer, though, this level would look positively ordinary; August yielded numbers worse than Katrina. November yielded numbers worse than the September 11th attacks. These were not one-off events, though—these were repeated weekly events. Despite seeing these numbers almost in real time, week after week, the Federal Reserve lowered rates only gingerly.
By the time it reached zero in its December meeting, the economy had experienced the five worst weeks of the century to date, and had experienced them consecutively.

Figure 10. Initial Unemployment Claims




Source: U.S. Employment and Training Administration, Initial Claims [ICSA], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/ICSA

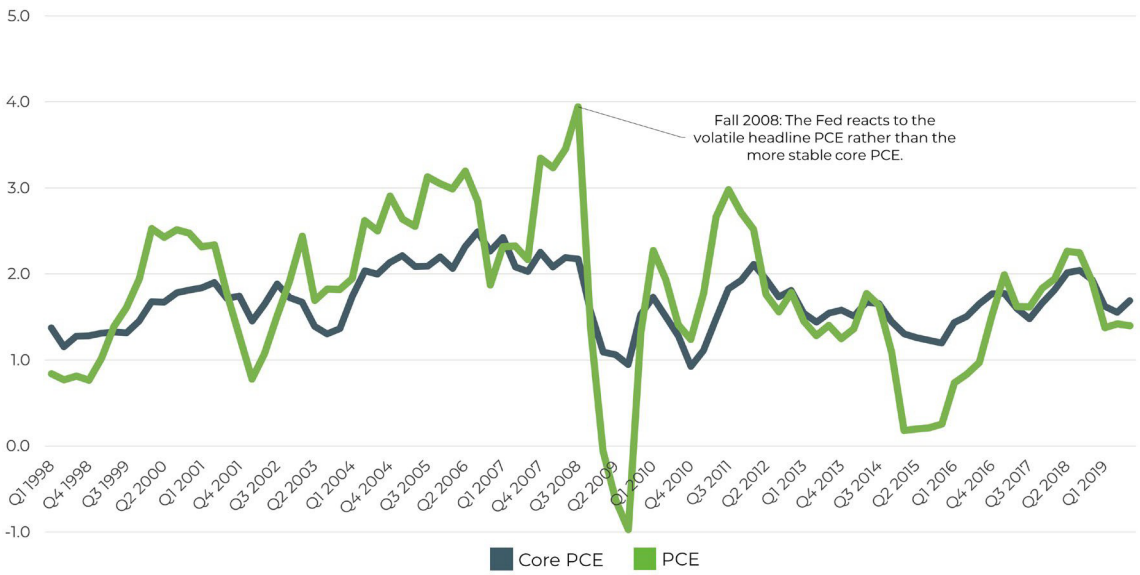
The Federal Reserve consistently underreacted to deeply-troubling numbers in four different indicators of employment—all of which were telling the same story. Until the very last month of 2008, there were conventional policy tools available to slow or reverse these terrible job losses. In any month prior to December 2008, the Federal Reserve could have lowered rates by more, unleashed more spending into the economy, and saved some jobs.

Overemphasis on Inflation—Especially Oil

One reason the Federal Reserve reacted so slowly to a deteriorating employment situation in 2007-2008 was undue attention to inflation—and particularly, inflation in energy prices. While maintaining stable inflation is one of the two components of the Federal Reserve's dual mandate, the Federal Reserve has long held that "core" personal consumption expenditures (PCE) inflation—which excludes volatile commodities like oil from its basket—is often more informative for determining the state of aggregate demand.[25]

While the Federal Reserve forgot this lesson during 2008 and focused strongly on rising oil prices, it is in fact a lesson worth remembering. To understand whyFederal Reserve economists have often preferred the Core PCE measure, it is worth comparing the difference between it and the ordinary PCE measure.

Figure 11. PCE Price Indices (Percent Change from Year Ago)




Source: U.S. Bureau of Economic Analysis, Personal Consumption Expenditures Price Index [PCECTPI, PCEPILFE], retrievedfrom FRED, Federal Reserve Bank of St. Louis

One obvious way they differ is that Core PCE is a much more stable series. Butto understand why Core PCE is genuinely more informative for the Federal Reserve's purposes, it helps to consider what the Federal Reserve's dual mandate is fundamentally about: it is about keeping a stable relationship between spending of the domestic currency and domestic productive capacity. For example, if too much spending chases too little productive capacity, inflation can run away from

the central bank. In contrast, the converse can produce deflationary spirals and output gaps. Navigating a steady path between these two extremes is the principal challenge for any currency issuer.

Unlike the price of domestic services, commodity prices are not really about this domestic monetary balance. Commodity prices are defined by global supply and demand, and they can often move separately from demand-side price level trends. Oil does this—but oil is also such an important commodity that it can dramatically shift overall price levels. These idiosyncratic changes in oil prices create noise in inflation data that is not particularly correlated, in the long run, with the outcomes the Federal Reserve cares about. For these reasons, the Federal Reserve often ignores oil shocks. However, it failed to ignore them in 2008.

In Chairman Bernanke's account, he describes the August 2008 meeting this way:

> At the same time, we could not completely dismiss inflation concerns. Oil priceshad fallen to $120 per barrel from their record high of $145 in July. However, staffeconomists still saw inflation running at an uncomfortable 3½ percent in the second half of the year. Even excluding volatile food and energy prices, the staff expected inflation to pick up to around 2½ percent, more than most FOMC members thought was acceptable.[26]

Bernanke did not completely agree with this view, but he did have to accommodate it. The Federal Reserve held interest rates steady in August 2008, with a single dissent favoring a rate increase. Bernanke writes that if anything, "the 10-1 vote understated rising hawkishness on the Committee."[27]

It is true that all else equal, lower inflation would certainly have been better; but the Federal Reserve had a dual mandate, and collapsing financial markets and rising unemployment were far more unacceptable than slightly-off-target core inflation.

One particularly strong account of the Federal Reserve's fixation on 2008's oil-driven inflation comes from journalist Matt O'Brien. Counting the mentions of inflation and unemployment—the two halves of the dual mandate—he finds that the former dominated the discussion by a 10:1 ratio until the September meeting, followed by a 5:1 ratio at the September meeting.[28] This is extraordinary because—as O'Brien notes—inflation expectations were not particularly high, and collapsed immediately after the Federal Reserve's surprisingly-hawkish September statement was released. The statement contained the following passage:

> The downside risks to growth and the upside risks to inflation are both of significant concern to the Committee. The Committee will monitor economic andfinancial developments carefully and will act as needed to promote sustainable economic growth and price stability.[29]

This statement came in the third straight quarter of recession, as unemploymenthad climbed 1.7 percentage points and two major financial institutions had failed. The predicted inflation never materialized, and the U.S. would experience substantial deflation by the following year.

Scope Creep

Housing prices rose substantially leading up to 2006. However, the housing market began to decline in 2006, as the Federal Reserve hiked interest rates to an eventual high of 5.25 percent. Housing starts peaked in January of that year, and residential construction employment in March.

A decline in housing starts or construction employment was not per se a problem; throughout 2006, growing employment in other sectors roughly compensated for the decline in housing employment. The Federal Reserve noted—likely correctly—that the late-2005 prices were too high, and saw the initial stall in housing markets in 2006 as a welcome development.

In 2007, though, economy-wide employment began suffering, suggesting that the rate hikes were beginning to constrict the overall economy, not just the housing market. The Federal Reserve, to its credit, noticed the reversal and began to cut rates in September 2007. However, it underreacted—as described above—in part because it had begun to see curbing the housing market as a goal in itself: a strange sidetrack into policy beyond the scope of the central bank's mandate. As then-Chairman Bernanke recalls the September meeting:

> As in August, we again discussed the issue of moral hazard—the notion, in this context, that we should refrain from helping the economy with lower interest rates because that would simultaneously let investors who had misjudged risk off the hook. Richard Fisher warned that too large a rate cut would be giving in to a "siren call" to "indulge rather thandiscipline risky financial behavior."[30]

While this particular view was not entirely representative of the Federal Reserve as an institution, moral hazard was discussed in the context of interest rate decisions. Moreover, in his book Shut Out, Kevin Erdmann notes that the Federal Reserve as a whole would issue statements describing the weakness in the housing market as a "correction," suggesting a kind of normative view that housing prices should fall.[31] The Federal Reserve kept this language even well into the decline of employment measures. The focus on moral hazard and housing prices largely detracted from attention to an ailing labor market.

Where's My Bailout?

All of these problems with the 2007-2008 Federal Reserve came together—the underweight on employment, the overweight on inflation (particularly, dubious non-core inflation measures) and the tendency to micromanage rather than reactto the broader picture—when banks began to struggle and fail.

The Federal Reserve clearly understood the need for monetary injections into struggling financial institutions. However, it actively rejected the idea that the restof the economy—which was also struggling—might need the same.
In the middle of March 2008, Bear Stearns failed. The Federal Reserve made

two choices that month: it chose to help finance the purchase of Bear Stearnsby JPMorgan, injecting some liquidity into capital markets, but it almost simultaneously chose to set the federal funds rate at 2.25 percent for the rest of the country. Setting aside Bear Stearns for a moment, we should consider what that rate meant: it gave would-be spenders or would-be lenders the option of parking their money with the government for 2.25 percent, rather than spending or lending it to someone else in the private sector. It was a choice to constrain spending and credit. 2.25 percent was still a cut—a choice to constrain credit by less than before—but a choice to constrain credit nonetheless.

Injecting capital into financial markets does increase spending and stem job losses. What is curious, though, was the use of such extraordinary measures when ordinary measures were nowhere near exhausted. Consider how Bernanke aptly explained the reasoning for the Bear Stearns bailout:

> Wall Street and Main Street are interconnected and interdependent, I explained. "Given the exceptional pressures on the global economy and financial system, the damage caused by a default by Bear Stearns could have been severe and extremely difficult to contain," I said. And the damage would have surely extended beyond financial markets to the broader economy. Without access to credit, people would not be able to buy cars or houses, and businesses would not be able to expand, or insome cases, even cover current operating costs. The negative effects on jobs and incomes would be fast and powerful.[32]

This explanation is exactly correct, especially regarding access to credit: which iswhy it is all the more remarkable that the Federal Reserve was still constraining credit with its interest rate policy. Credit was constrained for any borrower who could not offer lenders better terms than the 2.25 percent risk-free return offered by the federal government—and in a time of financial turmoil and weak employment, lending was risky, so that risk-free 2.25 percent looked quite good. Creditors lent less for cars and houses and businesses, and the lack of credit had negative effects on all three of these sectors.

Much of the controversy over the economics of the Bear Stearns bailout focusedon moral hazard. The real question is why the Federal Reserve took actions that,as Paul Volcker described it, "extend[ed] to the very edge of its lawful and impliedpowers"[33] when perfectly ordinary, legal, and powerful operations for providing credit were also available. The most plausible explanation, based on Federal Reserve communications in 2008 and the description of the August meeting foundin Bernanke's memoir, was that rates were kept high because of inflation concerns.

Taken separately, the bailout and interest rate decisions are coherent. But together, it is difficult to square them. As the Federal Reserve told it, spending enabled by emergency below-market-rate liquidity injections to Bear Stearns was good spending that helps Main Street, while spending enabled by a federalfunds rate of (for example) 1.75 percent would have been bad spending that would spur inflation.

This pattern of easier credit for troubled financial institutions but tighter credit than necessary for the rest of us continued throughout 2008: as George Selgin documents, the Federal Reserve actually took care to offset its emergency operations' effect on overall demand. Increases in credit to troubled banks were matched with corresponding decreases in credit elsewhere in the system.[34] In Bernanke's words, this was done to "keep a lid on inflation."[35]

One tool in this offsetting process was interest on excess reserves (IOER). In October of 2008, the Federal Reserve began paying IOER.[36] This policy induced banks to hold reserves and earn interest from the government rather than lending to private-sector individuals or institutions. This constrained credit for the private sector, outside of the banks that were rescued with below-market-rate lending.[37]

Bernanke made an important point in his defense of the Bear Stearns bailout, about the interdependence of Wall Street and Main Street. Bernanke explains one direction of the dependence, but the opposite direction is just as valid; better credit to ordinary spenders on cars and houses could have helped many of the struggling financial institutions, and prevented the outcome that the Federal Reserve feared: additional bank failures and the need for additional bailouts.

Bernanke often notes that he had sympathy for those who asked him, "Where's my bailout?"[38] Perhaps the Chairman was constrained by the views of others onthe Committee, but it was actually a perfectly reasonable question: there was indeed more that he could have done for them.

Instead, though, the Federal Reserve kept credit tight for the economy as a whole, while treating the symptoms of that tight credit individually with bespoke rescue packages for financial institutions. This inconsistent state of affairs persisted for about nine months until December 2008, when the Fed finally caved on policy rates and set them to zero.

### *2009-2014: Overly-Hawkish Communications*

Over the 2009-2014 period, the Federal Reserve's actions were constrained to some degree by the zero lower bound: it had little or no ability to reduce interest rates further. This zero interest rate policy was appropriate, as the output gap was huge. The Federal Reserve also used some additional policy tools to further spur spending.[39] One of these was communicating more about the future of Federal Reserve policy ("forward guidance").

The addition of forward guidance to the Federal Reserve's policy toolkit was an extraordinarily important development—and forward guidance can be extraordinarily effective. After all, almost every asset in the economy, from equities to corporate bonds to mortgages, is affected by future Federal Reserve decisions—or even, the entire universe of possible Federal Reserve decisions. Economists sometimes call this universe the "reaction function."

But there was a problem with forward guidance in the 2010s: Federal Reserve communications often described a hawkish reaction function—an inclination to run monetary policy relatively tightly.

Consider the Federal Reserve Board's projections from January 2012[40], when interest rate predictions (often known as "dot plots," for the way they were frequently charted) had just been issued for the first time. The projections told us that the median participant in the exercise believed that 2014 was theappropriate year for interest rates to rise. They also told us some other thingsabout 2014: that participants believed Core PCE inflation would be below- target in the range of 1.6 to 2.0 percent, and that participants believed the unemployment rate would be in the range of 6.7 to 7.6 percent.

Put together, these predictions paint a clear picture of extraordinarily tight monetary policy. They told us that a Federal Reserve faced with an economy with elevated unemployment and below-target inflation would act to curb spending by tightening credit.

In a world of forward-looking economic actors, a strong signal of future tight monetary policy has a direct transmission mechanism into spending decisions today. When people expect future nominal incomes to be lower, that result is capitalized into every bond and equity price. For example, firms will get lower valuations from venture capitalists, private equity, and public stock markets, curbing their ability to raise cash to spend on new projects. Ironically, the predictions of too-early "liftoff" likely helped delay the actual liftoff, by keeping asset prices and investment depressed.

Caveats abound about the dot plots. They are not a rigid policy plan. They are a collection of several different people's views, some of whom are not voting members. They are prone to misinterpretation. But communication in January 2012 (and in many future meetings) was actually quite clear: it predicted that the Federal Reserve would begin tightening even with below-target inflation and above-target unemployment. And it predicted correctly: the Federal Reservesoon would raise rates in 2015 under precisely those conditions.

There was one other clear problem with the Federal Reserve's communications strategy: it published predictions about the sustainable long-run rate of unemployment, and actually raised that estimate all the way to 5.6 percent at the peak of the output gap, even though unemployment below five percent had recently been experienced before the crisis. This signaled that it would consider such an unemployment rate desirable, or even, difficult to improve upon without creating inflation. It was neither. One can also see this as a form of "forward guidance," broadly defined. It was a strong hint that the Federal Reserve would begin hiking rates and constricting credit again, even if unemployment was still relatively far from pre-crisis levels. This prediction also proved to be true.

While forward guidance was too hawkish throughout this period, it became less so over time—eventually tying interest rate guidance to fairly-specific inflation and employment outcomes. By the end of the period, guidance policy had improved substantially.

*2015-2019: Premature Rate Hikes*

When the Federal Reserve achieved "liftoff" in 2015 by raising interest rates, the economy was still a moderate distance away from the pre-crisis level of employment. A flurry of rate hikes followed in 2017-2018, stalling the prime-age employment-to-population ratio below its prior peaks, and preceding the kind of wage growth one would expect of a full-employment economy.

In a 2018 analysis, Moody's economists Adam Ozimek and Michael Ferlez argue persuasively that the Federal Reserve hiked interest rates too quickly. It believed at the time that the economy was closer to full employment than it actually was.[41] At the time, the unemployment rate was just above five percent: worse than the best pre-crisis months, but somewhat close to them. However, subsequent data has shown—for reasons that are not fully understood—that the unemployment rate measure can go much lower than it did in previous expansions.[42]

In 2019, the Federal Reserve ended up reversing some of its 2018 rate hikes, in part to mitigate the error described by Ozimek and Ferlez; the current Chairman of the Federal Reserve, Jerome Powell, has stated that the long-run sustainable rate of unemployment is lower than previously thought.[43] This error was the final error of the cycle, but perhaps the simplest: there was no zero-lower-boundissue to contend with, there were no fast-moving financial collapses to react to, and there were no commodity shocks going on at the same time. The Federal Reserve simply misread the labor market and slowed the pace of its recovery using conventional policy tools.

## MONETARY POLICY CAN USE BETTER MEASURES

The Federal Reserve made mistakes in the most recent recession, but it also was creative and thoughtful in response to a new situation, making policy innovations in areas such as forward guidance that will be valuable for decades to come. Central banking—and especially, central banking close to the zero lower bound—is a relatively young science with a small sample size of experiences to learn from. The 2007-2019 output gap was an extraordinarily valuable learning experience, and the insights gleaned from it can be put to good use.

One lesson from the most recent output gap is that the Federal Reserve often had trouble gauging the state of the economy. It has access to many indicators, but some are more valuable and reliable than others—and which indicators are best depends on what portion of a business cycle the economy is in.

*Use Employment Measures as Early Warning Signs*

The earliest warning signs of the financial crisis were employment-related indicators. While the conventional wisdom usually dates the beginning of the crisis to March 2008 and Bear Stearns, or September 2008 and Lehman Brothers, there were troubling signs from employment indicators before then.

There are good practical and theoretical reasons to believe that drops in employment will continue to be the fastest warning signs of demand-side trouble. The practical reason is that employment is relatively simple to measure, while GDP or PCE inflation are a great deal more complex and require the collection of many more data points. Over the long run, these indicators are quiteuseful—but given constraints on the speed of data collection, jobs numbers simply get into decisionmakers' hands faster.

The theoretical reason to favor employment measures is that drops in employment will accelerate other stressors. For example, if people are losing their jobs, they are more likely to spend less and further slow the economy, or default on their debts and contribute to financial instability.

Recent work by the Federal Reserve has affirmed this view of employment measures. Economist Claudia Sahm devised an algorithm colloquially known as the "Sahm Rule," which treats sudden rises in the unemployment rate as reliable early warning signs of a contraction.[44] While the Sahm Rule is based on the official unemployment rate for simplicity's sake and to facilitate comparability across time, it is likely that other employment measures, such as payroll surveys or unemployment claims, could be used as additional data points to scan for early signs of recession.

*Understand the Limitations of the Headline Unemployment Rate*

While the official unemployment rate is very useful at predicting the start of recessions, and is generally directionally correct for measuring the state of the economy over the short run, it has proven less useful as output gaps wear on. In contrast, the prime-age employment-to-population ratio seems to have held up better and allows for more sensible comparisons between pre-crisis and post-crisis perceptions of full employment.

There is a reason for this: the unemployment rate implicitly divides the populace into three groups—the employed, the unemployed seeking work, and those notin the labor force. However, it simply discards the final category, and it turns out that final category includes useful information.

Many jobless individuals identify as retired, as students, as homemakers, or as disabled. These are understandable reasons not to work, and many individuals in these categories would not work under any realistic circumstances. Yet some of the people who place themselves in these categories during output gaps can and do find jobs when the economy improves. This empirical fact suggests that for some, nonemployment is not an immutable feature of demographic characteristics, but rather, at least partly contingent on the state of the labor market.

The reason that the unemployment rate becomes less useful as output gaps drag on is that the unemployed find substitute activities to occupy their time,like going back to school, or at least find personal reasons for why they do not have a job—such as being retired. We begrudge no one their retirementor

their ability to go back to school, but if they would have instead taken a job in a healthier labor market, that is useful information to know. The prime-age employment-to-population ratio gets at this distinction, while the unemployment rate does not.

### *Choose Inflation Indicators Wisely*

As described above, the inflation component of the dual mandate led the Federal Reserve astray in 2008. While one aspect of the mistake—the attentionto oil—seems apparent and widely-accepted in retrospect, it is worth thinking about the inflation component in a little bit more detail.

The purpose of the inflation component of the dual mandate is not to protect Americans from all possible price increases, even if they reflect real fundamentals, or prices of foreign goods or global commodities. The purpose is more like preventing the central bank from a particular failure mode, where it fruitlessly throws money at the economy in a bid to bring output above the maximum possible or maximum sustainable amount. Such an effort will bid upall factors of production--land, capital, and wages—as more and more money chases the same capacity.

If we understand the inflation component of the dual mandate in this way, it makes sense for the Federal Reserve to put very little weight on commodity prices from its analyses, and make use of Core PCE.

It is also worth paying particularly close attention to the nominal growth in domestic worker compensation, which is a good measure of the extent to which factors of production are being bid up (or, from the consumer's perspective, the extent to which the price of services are being bid up).

The employment cost index (ECI) collected by the Bureau of Labor Statistics (BLS) is a good measure here, especially the ECI for wages and salaries. It is stable for an inflation measure, and—while it has a shorter history than many other economic indicators, it may be expected to continue to show less random noise than other inflation measures and come close to approximating the platonic demand-side inflation that central banks should avoid bringing to excess.

The ECI tends to run higher than other inflation measures like the PCE index, because increased productivity does not dampen growth in the ECI. This is mostly a feature, not a bug: it would not make much sense to loosen monetary policy in response to a positive productivity shock that was passed on to consumers in the form of lower prices, or to tighten it in response to a year of weak productivity growth that was passed on into higher prices.

### *Beware Updated Estimates of Potential GDP or Employment in Timesof Cyclical Disruption*

One problem worsening the 2008-2019 output gap was that the Federal Reserve increased its estimates of the "natural rate of unemployment" (the lowest

sustainable rate) as more people lost jobs, lowering potential GDP inaccurately and underestimating the output gap. This strategy has the obvious problem of mistaking cyclical movements for structural ones. The Federal Reserve has since revised its estimates of the natural rate back downward, as jobs were added once again. While updating one's beliefs in response to new data is good, one should be wary of updating beliefs about long-run capacity based on data collected under unusual short-run conditions.

### *Beware of Using Interest Rates as a Measure of the Stance of Monetary Policy*

One particularly technical point about measurement concerns the stance of monetary policy. FOMC statements have frequently identified low interest ratesas a sign of accommodative policy.
This is not always and everywhere correct. Neither is the converse: that high interest rates are a sign of tight policy. As Milton Friedman observed in his famous American Economic Association presidential address:

> As an empirical matter, low interest rates are a sign that monetary policy has been tight-in the sense that the quantity of money has grownslowly; high interest rates are a sign that monetary policy has been easy-in the sense that the quantity of money has grown rapidly.[45]

This observation—made in 1968—has largely held up, and in fact predicted to some degree both the late 1970s (when, despite high interest rates, inflation soared to record levels) and the early 2010s (when, despite low interest rates, inflation remained persistently below target and unemployment remained elevated.)
The key to the observation is that easy money gives ample credit, allowing spending to increase at an accelerating pace, raising nominal GDP growth expectations and inflation expectations, pushing the equilibrium interest rate (at least in nominal terms) upward. Tight money does the opposite: it causes spending to slow and lowers nominal growth expectations and inflation expectations, which pushes the equilibrium rate of interest down.

Only one amendment needs to be made to Friedman's telling: he focused on growth in the quantity of money. At the time, interest rates were always positive, and people only held money if they intended to spend it shortly. At the zero lower bound, this is no longer true; velocity of money—the extent to which it switches hands—can fall sharply. Instead of looking to quantity of money, one must look to quantity times velocity (which happens to be equivalent to nominal GDP, or NGDP).
Scott Sumner phrases it in an improved and more modern formulation.[46]

> Interest rates are not a reliable indicator of the stance of monetary policy. On any given day, an unexpected reduction in the fed funds target is usually an easing of policy. However, an extended period of time when interest rates are declining usually represents a tightening ofmonetary policy. That's because during periods when interest rates are falling, the natural rate of interest is usually falling even faster (due to slowing NGDP growth), and vice versa.

The natural rate of interest is another economic abstraction that is hard to pin down precisely, but Sumner can be loosely translated as follows: during periods where the central bank is cutting interest rates, the risk-adjusted attractiveness of private-sector investments is falling even faster, so savers are still crowding into government bonds even at the lower rates.

Sumner considers the growth rate of NGDP a better guide to the stance of monetary policy. A policy that enables an acceleration in spending—however it is implemented—is loose, and one that forces a deceleration or contraction—however it is implemented—is tight. This formulation—based on effects—seems more appropriate than a measure based on interest rates alone.

Why are the semantics here important? First, because effects matter. Monetary policy stances are named after their intended effects; loose or accommodative or expansionary monetary policy should presumably be loosening, accommodating, or expanding something. Tight or contractionary policy should presumably be tightening or contracting something.

Second, semantics are important because names have an effect on the policy's politics. The Federal Reserve in 2015 had essentially achieved some relatively-normal results for years: steady improvement in the employment rate, steady (though below-target) core inflation, and steady four percent growth in NGDP, which is also a normal result. However, it labeled these policies "accommodative." This lent credibility to the plausible-sounding-but-wrong critique that the low interest rates at the time were "artificial" in a way that higher interest rates would not have been. It put the FOMC under pressure to "normalize" policy by tightening, which it did by the end of the year.

Third, a results-based measure of the stance of monetary policy, such as NGDP growth, appropriately captures the effects of policies that do not involve the setting of short-term interest rates: for example, quantitative easing or forward guidance.

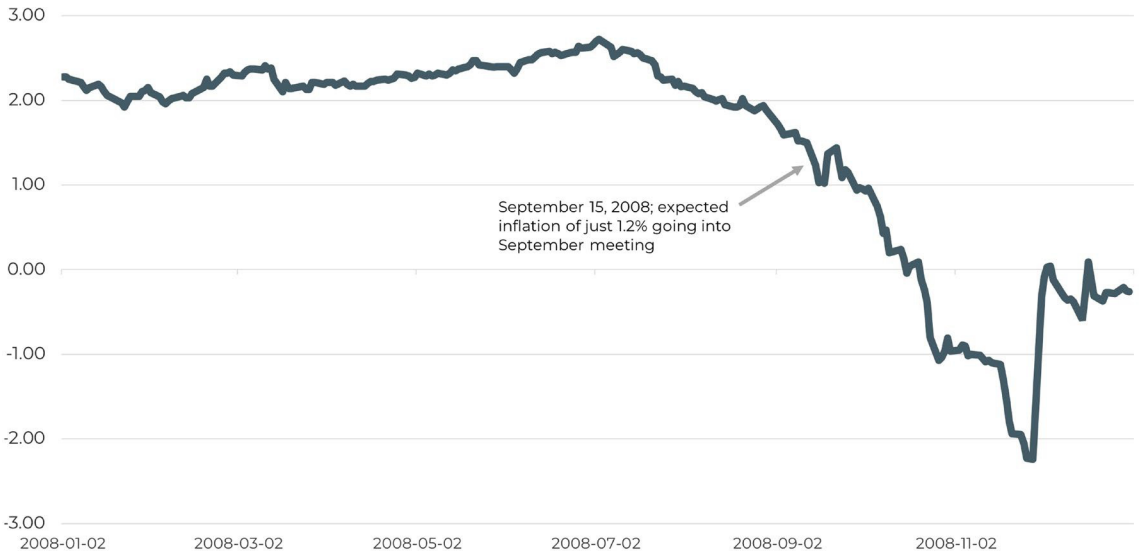
### *Use Market Indicators More Frequently*

A number of market indicators can help the Federal Reserve make good predictions about the future. Mechanically tying Federal Reserve actions to market data is largely not a reasonable policy option, but markets can help the Federal Reserve predict the consequences of policy.

Treasury inflation-protected security (TIPS) spreads, or the difference in yield between inflation-protected bonds and ordinary bonds, have been underusedin the Fed's decision-making process in the past. These can tell the Federal Reserve what market expectations of inflation are. While the Fed's inflation projections are typically good, TIPS spreads are extraordinarily quick to updatein critical moments—as they were in 2008. By the September 2008 meeting, where the FOMC statement considered downside growth risks and upside inflation risks to be about equal, TIPS markets were pricing in far-below-targetinflation of just one percent.

The Federal Reserve updated its beliefs towards low inflation soon after the TIPS market did—however, there was at least one FOMC-meeting window where policy could have been better informed by using the TIPS spread.

Figure 12. Inflation Rate Expected Over the Next Five Years, as Indicated by the TIPS Spread




Source: Federal Reserve Bank of St. Louis, 5-Year Breakeven Inflation Rate [T5YIE], retrieved from FRED, Federal ReserveBank of St. Louis; https://fred.stlouisfed.org/series/T5YIE

## ADOPT BETTER POLICY FRAMEWORKS

There are several changes to the policy framework that could help monetary policy tackle output gaps with more vigor. Several have been discussed by current and former Federal Reserve officials.

We will begin with policies intended to be helpful at the beginning of output gaps—or at catching them before they start. Then we will move to policies intended to be helpful at the zero lower bound, to be used after conventional interest rate cuts are no longer possible.

### *Reject Interest Rate Smoothing, Especially When Conditions are Worsening*

The Federal Reserve tends to move interest rates in increments—often by quarter points, sometimes by half points, and very rarely by three quarters of a point or more. In many circumstances, this is welcome, creating an impression ofa captain with a steady hand on the tiller.

However, when one needs to change course quickly, this steadiness—the slow, deliberate movement, as if turning a battleship—is no longer the right move. The experience in 2008 showed that conditions can often deteriorate quickly, and in such cases, a central bank interested in slow course change can end up falling behind the curve; conditions change so rapidly and feedback loops are so strongin the private sector that the natural rate of interest falls faster than the central bank

cuts rates. It therefore ends up failing to provide the desired stabilization. Economists Miles Kimball and Scott Sumner are among those wary of this particular practice. Sumner writes "The Fed needs to be much more aggressive when the business cycle is impacted by a dramatic shock."[47]

A potentially dangerous phrase in the monetary policy vocabulary is "cutting cycle." It suggests that the central bank will cut rates, but then, finding the previous cut too weak or less responsive than private capital markets, will have to cut rates again, and potentially repeat this process several times. It is plausiblethat "cutting cycles" do have some place in optimal monetary policy, but in practice most cutting cycles—like that of 2008—have had unhappy results. Credibility may be improved more by a single forceful action than several tentative ones.

### *Integrate the Two Components of the Dual Mandate into a Single Mandate*

The dual mandate leaves much room for ambiguity in terms of how to weight unemployment and inflation concerns; however, it is possible to integrate inflation and unemployment data into a single mandate that implicitly contains both components. The most promising methods for this begin with the observation that inflation is a price, and employment is a quantity. Therefore, theylook to measures of price multiplied by quantity.

Fortunately, many such metrics exist. One of the most obvious of these is nominal GDP. The idea of targeting nominal GDP originated with monetary economist Bennett McCallum,[48] but also has been advocated by other economists such as Scott Sumner, Christina Romer,[49] Jan Hatzius,[50] and Joshua Hendrickson.[51] While there are some technical issues implementing a nominal GDP target in real time, economist David Beckworth, another advocate, proposes methods to predict nominal GDP more quickly, including the use of new data sources or futures markets.[52] At a minimum, stable nominal GDP growth is an excellent medium- and longer-run measure of central bank performance.

One way of thinking about monetary policy is in terms of a "nominal anchor." The idea is that the central bank can choose to hit exactly one nominal target, no more. It sets one price, and all other prices are determined by their relationship with that anchor price. NGDP targeting advocates propose anchoring the price of all things combined. This has the very simple virtue of making sure that policymakers stay focused on the big picture, rather than becoming too heavily invested in specific and idiosyncratic measures or markets.

For example, any regime that directly targets employment will be required to define how it measures employment, and then define what constitutes full employment under that measure. (This has sometimes been known as the non-accelerating inflation rate of unemployment.) However, with many measures anda changing economy, this rate is hard to find or define.

Similarly, any regime that targets inflation will be required to define its inflation measure: what basket of goods counts, how that basket of goods changes over

time as tastes or technologies change, and how the measure accounts for quality improvements in newer goods. This is quite technical and sensitive to assumptions.

NGDP targeting has fewer of these details to account for. There are no assumptions embedded in it about the natural rate of unemployment or the right basket of goods. Only the growth in overall currency usage is stabilized, and everything else is left to markets.

### *Make Clear, Specific Forward Guidance*

A brilliant innovation of the mid-2010s Federal Reserve was state-specific forward guidance, a policy tool that remains highly effective at the zero lower bound. Guidance was "state-specific" in that the FOMC described theconditions or "states" under which it would commit to decisions. (In that particular case, raising rates above zero.) As forward guidance becomes
clearer and more specific, it begins to resemble rule-based policy rather than discretionary policy, creating a predictable guide to how monetary policy would work in a variety of scenarios.

Ben Bernanke described the evolution of this policy in his presidential address to the American Economic Association:

> Over time, the FOMC pushed back against the excessively hawkish expectations of market participants with more precise and aggressive forward guidance. In August 2011, the FOMC for the first time explicitly tied its guidance to a date, indicating that it would keep the fed funds rate near zero "at least through mid-2013." In January 2012 it extended that commitment "at least through late 2014," and in September 2012 it extended the commitment yet again to "at least through mid-2015." In December 2012, the FOMC switched from guidance specifying a date for policy action (calendar guidance) to a description of theconditions that would have to be met for rates to be raised (state-contingent guidance). Specifically, policymakers promised not even toconsider raising the policy rate until unemployment had fallen at leastto 6.5 percent, as long as inflation and inflation expectations remainedmoderate. A year later, this statement was strengthened further, with the FOMC indicating that no rate increase would occur until "well pastthe time" that unemployment declined below 6.5 percent. In principle,state-contingent guidance, which ties future policy rates to economic conditions, is preferable to calendar guidance because it permits the market's rate expectations to adjust endogenously to incominginformation bearing on the outlook.[53]

This policy was highly effective because it could influence market participants' expectations about the future. Bernanke further documents a variety of quantitative and anecdotal evidence that the policies had the desired effects and loosened monetary policy—not by changing the interest rate people were experiencing at that very moment, but instead, by informing them about the path of interest rates under a variety of hypothetical moments. In other words: by describing the reaction function.

While the specific numbers used in the forward guidance were ultimately not nearly aggressive enough (6.5 percent unemployment turned out to be an unambitious goal) the framework for forward guidance was exactly right, and

monetary policy should make ample use of it during slowdowns.

*Adopt a Level Target*

Level targeting is perhaps the single most effective zero lower bound policy, and likely has benefits even outside of the zero lower bound. The idea of "level targeting" is to have a consistent long-run growth path in mind for the target variable, not just growth rate to target anew each period.

There are two strong reasons to believe a level target would be effective. The first is that level targets would do a better job of anchoring expectations for long-term contracts, such as mortgages. For example, it is considerably easier for a mortgage lender to operate if she has at least a general sense of what nominal incomes in America will look like in the 30th year of the loan. Will theydouble? Will they triple? A nominal income level targeting regime can actuallyprovide an answer to that question, making long-term contracts considerably easier to write. Similarly, if a pension plan were interested in implementing a cost-of-living adjustment to benefits based on inflation, it would be easy to make long-run projections under an inflation level targeting regime.

The second reason for believing in the effectiveness of a level target is that a level target constitutes a kind of forward guidance, which—through its impacton expectations, can actually work backwards in time. In promising a steady long-run path, it encourages people to invest more steadily in the present, knowing that over the long run, rough patches will be smoothed out.

Nominal GDP level targeting, or NGDPLT, is one of the most popular uses of the level targeting idea. Level targeting dovetails particularly well with NGDP targeting because it turns the target into a long-run goal. In a level-targeting regime, short-run blips like revisions to GDP data are understood to be less consequential; instead the central bank maintains focus on keeping the long-run path steady.

The Federal Reserve recently moved towards understanding its inflation targetas a longer-run average, rather than a short-run point to target each period.[54] This is similar to level targeting in its focus on stabilizing long-run expectations, and also improves predictability for private-sector contracts.[55]

*Use Market Signals to Help Find Full Employment*

As covered above, the Federal Reserve from 2015 to 2018 raised interest rates because it believed the economy was approaching full employment and that a rate hike would help stave off inflation. Had its belief been correct, this movewould have made sense: generating unnecessary inflation by attempting andfailing to bring employment above its natural level would have been a costly mistake worth avoiding.

However, this prediction turned out not to be quite right; the economy was ableto sustain, without inflation, unemployment levels significantly lower than the FOMC had estimated, and significantly lower than those of the recent past.

That revelation required some epistemological modesty—which the Federal Reserve has embraced—but it also requires a rethinking of how we close out recoveries and achieve a "soft landing."

It may be best to rely on an automatic process derived from the private sector's price signaling, and wait until market prices show evidence that the output gaphas been closed.

This approach would be especially valuable when paired with the use of wage growth measures such as the ECI.

## CORONAVIRUS DISEASE 2019 AND MONETARY POLICY

U.S. economic activity peaked in February 2020.56 In the ensuing months, economic activity declined dramatically as individuals and institutions responded to Coronavirus Disease 2019 (COVID-19.) For many economic indicators, the changes in response to COVID-19 are the fastest or largest changes on record.

Monetary policy cannot mitigate the direct harms of COVID-19. However, it is still worthwhile to consider how to implement monetary policy appropriately in 2020 in light of the pandemic. Maintaining stability is unusually challenging because of the large size and the peculiar nature of the disruption.

Some of the general advice for monetary policy in the previous sections will applyto the COVID-19 pandemic. Some of it will not. Furthermore, some new points unique to this particular crisis will apply, even though they do not apply normally.

### *Monetary Policy Adjusted Quickly in March 2020*

Above, this report criticized past monetary policy for slow reaction times, and discussed the use of early indicators, such as unemployment claims, to head off collapses in spending. These criticisms do not apply to 2020 economic contraction.

The Federal Reserve reduced interest rates to near-zero levels in March 2020, the first month of the contraction. This was an appropriate recognition of market conditions: the expected return on private sector investments had fallen, so it was necessary for government-issued assets to trade at reduced yields as well, rather than setting an impossibly-high hurdle rate for private lending.

Additional policies with macroeconomic impact came from Congress: particularly, the Families First Coronavirus Response Act and the Coronavirus Aid, Relief, and Economic Security (CARES) Act, both signed into law that same month. These were not monetary policy, and their merits will not be discussed here, but they are relevant to monetary policy in that they increased nominal incomes to individuals, offsetting losses in income from business closures or layoffs.

These responses actually pre-dated most unemployment indicators; while unemployment numbers are usually the quickest indicator of a collapse in spending, faster indications, such as prominent business closures, were availablein this unusual case.

*Increases in Short-Run Spending are Not Always Desirable or Feasible*

Under usual conditions where nominal spending falls sharply, the development is unwanted and a sound monetary policy regime would typically reduce interest rates to counteract that. This reduces the opportunity cost of spending, inducing the private sector to hire, consume, and invest, until the path of nominal spending is once again stabilized.

This prescription is less useful under current circumstances than under the typical conditions where spending falls. Some ways of spending increase the risks of COVID-19 infection and spread; those kinds of spending have decreased, in some cases, dramatically. Some spending has been expressly prohibited by state or local laws, and other spending has simply been reduced by ordinary consumer choice. These drops in spending are not the products of monetary policy, and unlikely to be shifted by anything in the monetary policy toolkit. Another way to put this idea is that potential output simply will be lower for as long as COVID-19 remains a relevant concern.

It is important to recognize the limits of short-run monetary policy underthese circumstances. Some economists, such as Narayana Kocherlakota, a former president of the Federal Reserve Bank of Minneapolis, suggest reducing short-term interest rates into negative territory in an attempt to stimulate the economy.[57] Setting aside potential unintended legal or administrative consequences of this move, the prescription is likely to have limited effectiveness while COVID-19 is circulating.

Rate cuts work primarily through a substitution effect; they change for individuals the tradeoff between current spending and future spending, and make current spending relatively more attractive. (While this is a tradeoff at the individual level, it is not a tradeoff for the economy as a whole. The spending of the first individual increases the income of another.) While the substitution effect is normally powerful, it is limited for a cautious individual or firm during the COVID-19 pandemic, as many forms of spending would increase transmission. The usual substitution effect that makes rate cuts expansionary is less effective than usual.

There are also other effects, such as income effects: rate cuts effectively mean that banks or savers will have less money in the future than they would absent the rate cut. This can curb lending or spending. Under most circumstances, the substitution effect dominates the income effects, and rate cuts are expansionary. However, after a certain point, rate cuts may be contractionary. This point is known as the reversal rate.[58] Under circumstances where the substitution effect is less potent than usual, it follows that the reversal rate should be higher than usual. Central banks have historically not worried about the reversal rate—and they should not worry about it under current policy—but driving interest rates negative in an attempt to marginally increase spending during a pandemic would

certainly risk reaching the point where rate cuts are counterproductive. Short-run monetary policy is of limited use until consumers and firms are comfortable with the health consequences of spending more freely.

### *Employment Data Requires Substantial Adjustments to Be Understood*

Another issue unique to the year 2020 is that data series in employment and inflation are less helpful in the short run than they would usually be in guiding monetary policy.

Employment series have some unusual problems that must be considered and adjusted for.

First, many workers are in unusual states somewhere between employment and unemployment. (For example, unemployed on temporary layoff.) Some such workers categorize themselves incorrectly when taking the household survey (for example, by marking themselves as employed but absent from work.) The BLS has been forthcoming and transparent on how to think about this issue, andprovided information on how to adjust for these likely-incorrect responses.[59]

Furthermore, it may be difficult—among those workers in limbo—to understand which ones really will have a job to go back to, and which ones will not. Just because a layoff is reported as temporary in the household survey doesnot mean it will ultimately be temporary.

Finally, labor force participation declined dramatically as the pandemic took hold, from 63.4 percent in February to 60.8 percent in May.[60] This suggests that some unemployed workers are not looking for jobs—but presumably, only temporarily so, because they are waiting for COVID-19 to abate to begin their search. Their removal from the labor force—and therefore, the unemployment rate calculations—results in a measured unemployment rate that does not reflect their joblessness.

Some of the best work in understanding the employment situation comesfrom Jason Furman and Wilson Powell, who adjust for both the labor force participation issue and the misclassification of those marked as employed but absent. They find that the unemployment situation is worse than one would typically infer from the unemployment rate.[61]

Furman and Powell further suggest a measure of “full recall unemployment rate,” of what the unemployment rate would be if all the workers who report themselves as temporarily laid off were immediately able to return to work. This is an optimistic measure, they note, as some who report temporary layoffs will end up permanently laid off. However, it puts a lower bound on the number of Americans without jobs of any kind. Their full recall unemployment rate for May was 7.1 percent, suggesting a substantial number of Americans neither had a job nor expected to have one to return to.[62] By September, it had fallen to 6.6 percent, which is better but still millions of jobs short of full employment.[63]

The unemployment data are difficult to read, and likely less precise than they usually are; however, clear lessons can be drawn from them. First, that unemployment is historically high. Second, much of it is reported to be temporary, but some of it is not; even a full reopening and a successful suppression of COVID-19 could leave the U.S. with some people unemployedwho should not be, and were not unemployed prior to the pandemic.

### *Inflation Data Will Not Be Easily-Usable until Suspended Economic Activities Return*

Inflation data is likely to be extremely incommensurate with past experience, so much so that the headline numbers may not be useful, and even individual components may need contextualization.

A large number of products have become temporarily unavailable. While this is an ordinary problem for the BLS, and they have procedures for imputing the prices of temporarily-unavailable items by finding prices of comparable items from elsewhere, this problem is happening at an extraordinarily scale in 2020 as millions of businesses are paused. There are also changes in how the data is collected; in-person data collection has ceased, and respondents may bechanging their behavior in ways unknown to survey takers.[64]

Finally, there is an important conceptual point about what the large number of product absences means for the dollar—and what returning those products to market would restore. The dollar's purchasing power has fallen, in a certain sense, in that it can no longer safely get people a product that was previously available to them. It will rise substantially if COVID-19 is effectively suppressed or burns itself out. The absence or availability of products is, for the time being, a much more interesting component of the purchasing power of the dollar than the price levels of the goods that are available.

In the long run, after COVID-19 is at bay, stable inflation will once again be a meaningful indicator of the state of the economy. However, for the short run, it is likely inadvisable to treat 2020's inflation figures as comparable with those of the recent past, or assume that inflation works the same way as it has in the recent past.

### *Although GDP is Falling, Nominal Personal Income Has Remained High*

This paper has thus far treated nominal income and nominal spending as synonymous goals. As one person's spending is another person's income, these two indicators move together (and, under certain formulations, they are identical.)

However, under the specific circumstances of the COVID-19 recession, GDP has fallen even as personal income has risen, an unusual combination. The contours of the COVID-19 recession can best be seen in the BEA's advance GDP estimates for the second quarter of 2020.

For that quarter, nominal GDP declined by $1.805 trillion—a huge disruption that would concern any analyst. However, disposable personal income grew by a total

of $1.53 trillion (annualized). Most forms of market income declined precipitously; in annualized terms, employee compensation fell $794 billion, and proprietors' income by $224 billion. However, personal income ultimately rose, because government transfers and lower taxes contributed $2.419 trillion and $148 billion to annualized personal income, respectively.[65]

GDP and personal income are typically correlated; however, in 2020 nominal personal income has been sustained through increases in government transfers and decreases in taxes—some automatic, and some as consequences of acts of Congress.Government deficits have increased sharply, which is not a sustainable long-run solution, and some individuals have lost income even after transfers, but on averagepersonal income has been shielded from the consequences of the recession.

The final notable item from the BEA report is that personal saving has increased sharply, to a $4.694 trillion annualized rate, up from just $1.594 trillion in the first quarter. This suggests that on average—if not in every individual case—households are accumulating money that they expect to spend later.
Although nominal GDP is usually an excellent measure of whether policy has been too loose or too tight, nominal personal income may temporarily be better for understanding the state of the economy. Under ordinary circumstances, a drop in nominal GDP usually comes with low disposable income and weak household balance sheets, and therefore, a limited ability for households to spend in the future and return nominal GDP back to trend. However, in this particular case—since nominal household income was preserved by Congress, and since households have potential savings to deploy as the virus recedes, the prospects for returning nominal GDP to its pre-COVID path are much more realistic than the Q2 nominal GDP numbers would suggest.

### *Level Targeting and Long-Run Guidance Can Build Expectations of a Strong Recovery*

The principal instrument of monetary policy—short term interest rates—is already at zero and likely to remain there. Furthermore, attempts to increase spending in the very short run may not be welcome, as many forms of business are closed and many forms of spending are unsafe.

However, despite this, monetary policy can still be improved, and this can be done primarily through clarifying expectations about the future—about the period where COVID-19 is successfully and permanently suppressed. As mentioned previously, forward guidance is an extraordinarily powerful tool for currency issuers, especially when it is detailed and state-specific.

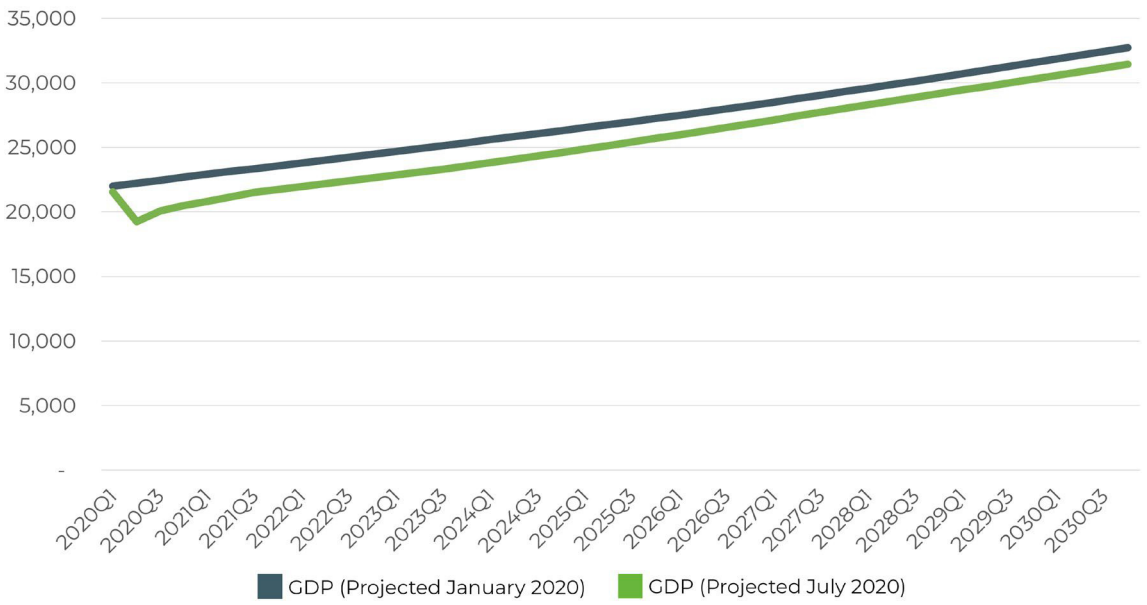
The most important directive for monetary policy is to allow the surge of spending to come once COVID-19 clears. It should explicitly avoid hiking interest rates, which would encourage dollar users to park money with the government rather than useit for hiring new workers, until the economy has returned to its original path.

The second most important directive for monetary policy is to clarify—now, in the present—that monetary policy will not be tightened too early. For example, in the very recent past, prior to COVID-19, more than eighty percent of Americans age 25-54 were employed. In the very recent past, there were consensus expectations about nominal GDP for the years 2021, 2022, and beyond. Describing a "level target" policy—in which monetary policy is not tightened until the economy returns to that trend, with specific markers for what would constitute a return to normalcy—would help build confidence that a strong recovery is coming.

It is important to build that confidence now; while many types of spending are currently being avoided for health reasons, it is still possible for some firms to raise capital, hire, and invest in some long-run projects. They will do both more freely and more easily if a strong recovery is expected.

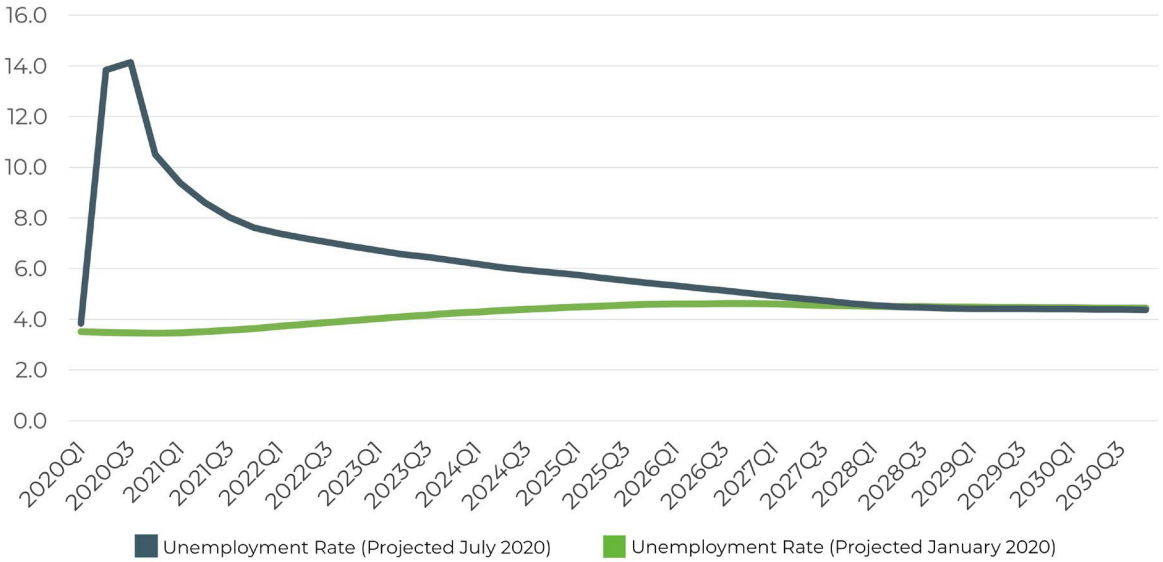
It is important to note that CBO projections show a slow, decade-long slog towards the prior trend. When its July economic projections are compared to its January 2020 baseline, developed prior to the COVID-19 outbreak in the United States, one can see a large and enduring difference on both nominal GDP and employment.[66] [67]

Figure 13. Projections of Nominal GDP, Pre- and Post-COVID-19 (billions of dollars, annualized)




Sources: Congressional Budget Office, The Budget and Economic Outlook: 2020 to 2030, January 28, 2020, https://www. cbo.gov/publication/56020; Congressional Budget Office, An Update to the Economic Outlook: 2020 to 2030, July 2, 2020,https://www.cbo.gov/publication/56442

Figure 14. Projections of Unemployment, Pre- and Post-COVID-19

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These projections, if they became reality, would be disheartening: a decade of economic progress wiped out, and a decade more to earn it back once again. But there are reasons to expect or hope that a better path for the economy is possible. CBO projections cannot assume the impact of new policies that have not yet been enacted, and some promising employment data has been released since the projections were made.

Finally, monetary policy could communicate that such an outcome would be unacceptable, using state-specific forward guidance. Under the CBO's forecast, for example, rate hikes are projected even at times when unemployment exceeds 5 percent. While this may be consistent with past experience, and with the rate hikes described by Ozimek and Ferlez as a mistake, it need not be true of the future. Monetary policymakers could state that if nominal GDP was still below its expected trend, and unemployment was still elevated relative to the recent past, that there would be no tightening under such circumstances.

The temporary COVID-19 economy was not meant to endure for the long run. Once the virus has waned, policy should clear the runway for spending to pick up again as fast as possible. From a monetary policy perspective, this means forgoing rate hikes or other tightening actions until normalcy is restored.

## CONCLUSION

Output gaps, generating periods of mass unemployment similar to that of thelast decade, are among the most important problems in developed economies.Recent experience and research have helped us understand the nature of the problem, and to devise progressively-better strategies to alleviate it.

Devising these strategies is a project deeply worth undertaking. Output gaps like that of the last decade come with tremendous losses. The losses are most easily denominated in dollars and jobs, but they can also be denominated in other units: mental wellbeing, work friendships, and children who were never born because young couples did not feel financially secure enough for parenthood.

These losses are terrible, but at least some of them are preventable. Some past losses were simply mistakes by currency issuers in understanding the complex and fragile systems built atop their currency. In the future, currency issuers could achieve better outcomes by stabilizing nominal income. More generally, we can use what we have learned from the experiences of 2007-2019 to help mitigate the present COVID-19 recession, and prevent or mitigate future recessions as well.

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## ENDNOTES


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# A Time to Build: Unleashing the Construction Industry to Support American Families

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The construction industry in the United States plays a critical role for workers, consumers, and savers. It is a robust source of well-paying jobs, especially for workers who otherwise might struggle for opportunity. It also creates a product that end users value highly and genuinely need more of. Finally, it provides an outlet for savings in the economy: savers can fund construction projects, directly or indirectly, and earn a return on their saving.

In short, construction projects often result in large gains from trade. Left to their own devices, free people should pursue such projects often and enthusiastically. Unfortunately, though, the construction industry has been prevented from reaching its true potential by its regulatory and financial environment. U.S. construction output is lower than it should be. This shortfall does not come from issues with the underlying physical world, where workers want jobs and people want structures. Rather, it comes from policy choices in areas like zoning, regulation, taxes, and macroeconomic stabilization.

In all cases, these policy choices err on the side of slowing the construction industry down. The result is fewer jobs, fewer and lower-quality structures, and fewer places to earn a return on saving. The following report will discuss some of the unique benefits of the construction industry, some of the hurdles created for it by public policy, and some fixes to remove those hurdles.

## THE CONSTRUCTION INDUSTRY HAS A UNIQUE EMPLOYMENT PROFILE

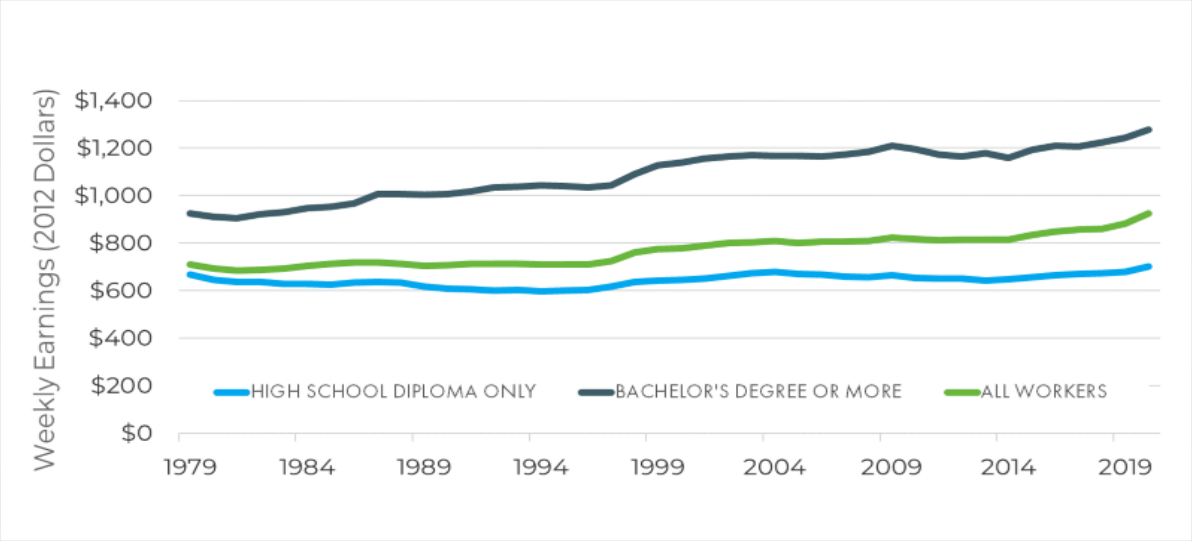
Formal employment provides people with a variety of economic, social, and psychological benefits. While jobs are sought out primarily to earn wages and finance consumption, they are also structured environments that can help forge social bonds, develop personal virtues, and create communities.[1] Jobs are not merely transactions that generate economic surplus through gains from trade. They are a valuable part of the American social fabric.

The construction industry has a particularly strong role to play in employing Americans and strengthening the social fabric, employing more than seven million Americans.[2] This is valuable in its own right, but perhaps especially valuable given the industry's unique demographic profile. It is disproportionately less-educated, disproportionately Hispanic, and disproportionately male. Each of these demographics is either disadvantaged on key measures, or losing ground on them, or both. With high wages for its education level, the construction industry is a much-needed lifeline.

Of all industry sectors in the North American Industry Classification System (NAICS), construction has perhaps the lowest overall educational demands. Just 13 percent of workers have a bachelor's degree, and 58 percent have no schooling beyond high school.[3]

This is important because Americans with relatively less schooling have fallen far behind their more-educated counterparts in the labor market, and the gap is growing with time. In fact, adjusted for the PCE chain-type index, median usual weekly earnings for Americans with only a high school diploma are barely higher than weekly earnings for those with only a high school diploma in 1979. By contrast, earnings for their college-educated peers have risen substantially.

Figure 1. Real Weekly Earnings Are More Favorable For Those With Higher Education




Source: U.S. Bureau of Labor Statistics, Weekly and Hourly Earnings from the Current Population Survey; Bureau of Economic Analysis Personal Consumption Expenditures Chain-Type Price Index

There is an additional mitigating factor to consider; wages for workers as a whole have risen through composition effects. More Americans are earning bachelor's degrees than before, so the workforce is shifting from the less favorable earnings track to the more favorable one.[4]

However, for Americans who have not completed any postsecondary education, the problem of low swages remains. The construction industry provides opportunities that alleviate that problem, in that it pays relatively high wages for workers at lower education levels.

Table 1. Common Construction Jobs and Wages

| Title | Number Employed | Percent without Secondary Education | Wage |
|---|---|---|---|
| Carpenter | 734,170 | 68% | $23.24 |
| Electrician | 688,620 | 44% | $27.01 |
| Construction Laborer | 1,020,350 | 72% | $17.72 |
| Operating Engineers and Other Construction Equipment Operators | 405,750 | 74% | $23.55 |
| First Line Supervisor | 626,180 | 57% | $31.83 |
| Construction Manager | 293,380 | 32% | $45.80 |
| **National Average for All Jobs** | | **32%** | **$19.14** |

Source: U.S. Bureau of Labor Statistics, Educational Attainment for Workers 25 Years and Older by Detailed Occupation, https://www.bls.gov/emp/tables/educational-attainment.htm; May 2019 National Occupational Employment and Wage Estimates, https://www.bls.gov/oes/current/oes_nat.htm

Consider, for example, the role of the first-line supervisor in construction. Such workers are less educated than the national average; 57 percent of them have no schooling beyond high school, compared to an average of 32 percent across all occupations.[5] Nonetheless, first-line construction supervisors are paid a median wage of $31.83 per hour, 66 percent higher than the national average wage of $19.14.[6]

This is almost a uniquely high wage for its education level. There are only six jobs in the U.S. where the median worker has never attended college but earns $30 an hour. Most of them are niche jobs in the operation of specialized equipment.[7] However, while these jobs employ a few thousand people at a time, there are more than six hundred thousand first-line construction supervisors in the United States.[8] The job is arguably the most robust path to high wages for the non-college-educated.

Construction's relatively high wages for its education level also extend to other positions. There are also a variety of specialist trades, such as electrical work, that pay well. Even the median construction laborer, overwhelmingly high-school-educated or less, is paid close to the national average wage.

Construction also disproportionately employs another group that is relatively disadvantaged in the labor market: Hispanics or Latinos. According to the Current Population Survey, they comprise about 18 percent of all workers, but 30 percent of those in the construction industry.[9]

In general, Hispanics and Latinos earn about 79 percent of the national average. This puts them about even with Black Americans, and well-behind White or Asian Americans.[10] Relatively-high wages in the construction industry help offer this group some advantages.

Finally construction is about 90 percent male.[11] Unlike the previously-described demographics, men in the aggregate do earn more than the national average. However, male workers are a large and diverse group, especially with respect to education levels, and there are reasons to worry about some subsets of the male workforce.

For example, in 2018, 71.4% of recent female high school graduates had enrolled in college, but only 66.9% of recent male high school graduates had done the same. As discussed above, the relationship between worker wages and education includes a "composition effect;" while high-school-only workers have not seen much real wage growth, the population of workers as a whole has seen wage growth through increasing education. These gains have been helpful for millions, but there is still a substantial group of people without post-secondary education—and over time, that group is becoming more and more male. It will remain important to provide that group with opportunity, and the construction industry can play a big role in doing so.

There are some additional reasons to be concerned about men. The share of prime-age men that is neither working nor looking for work has been rising for decades. A lack of employment for men is associated with much worse measures, both subjective and objective, of well-being.[12] While causation is never straightforward in such situations, there is plenty of reason to believe that additional employment opportunities may relieve some of the problems these men face, such as having fewer friends. The downside risk for men is also unusually high; for example, men in general are more likely to commit crimes than women are, and non-employed men are particularly at-risk.

One measure that illustrates the construction labor market well is the sector's unemployment rate. The unemployment rate for construction professionals tends to be higher than that of the rest of the economy. This fact is best understood to mean that people would like more construction jobs than are currently available to them. The lives of workers or would-be workers could therefore be improved by creating more construction jobs.

Figure 2. Unemployment Rates are Higher in Construction

Source: U.S. Bureau of Labor Statistics, Employment Situation

Overall, the construction industry creates many well-paying jobs, often with opportunities available for groups that are otherwise short on opportunities. From a worker's perspective, though, it would be good if there were even more of those jobs. Construction already contributes a great deal to our labor market, and it has the potential to help counteract some worrying trends in struggling demographics.

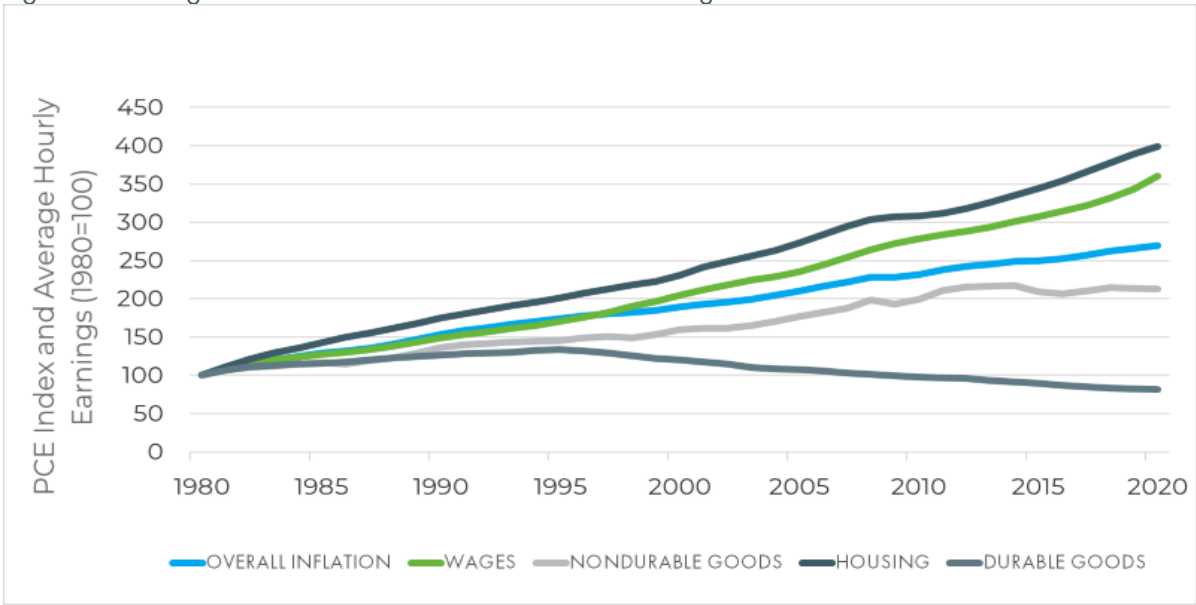
Its benefits may not be limited to just the workers directly employed in the industry. In a tight labor market, the comparatively high wages in construction may be helpful not just to the workers directly employed by construction; they also increase bargaining power for workers with similar skillsets across the board.

## ROBUST CONSUMER DEMAND GIVES CONSTRUCTION ROOM TO PAY HIGH WAGES

The construction industry's ability to pay relatively-high wages comes in part from an environment of robust demand. Buildings and houses in the United States are valuable to their inhabitants. In recent years, the combination of high demand and comparatively-scarce supply have resulted in high prices. While the high prices can be unfortunate for end users, they do generate ample revenues for those who build new structures. The more revenue an enterprise brings in, the easier it is for that enterprise to pay high wages.

This lens of analysis is especially useful for comparing construction to its blue-collar peer, manufacturing. Many policy analysts in recent years have focused on the subject of employing men without college degrees, and many have looked to manufacturing as a good way of doing so. While manufacturing can be a path to high wages for men without college degrees, price data suggest that construction may be more fruitful. The chart below shows overall inflation and wages, as well as the inflation for three end products that might be built or manufactured by blue-collar workers: housing, durable goods, and nondurable goods.

Figure 3. Housing Has Faster Price Growth Than Goods or Wages




Source: U.S. Bureau of Economic Analysis, Personal Consumption Expenditures Chain-Type Index; U.S. Bureau of Labor Statistics, Average Hourly Earnings of Production and Nonsupervisory Employees

In housing, prices have risen faster than overall inflation, and faster even than wages. In a market with this kind of rapid price growth, a firm might in principle be able to deliver roughly the same products as it had in the past and still come out ahead, even after allowing for higher worker pay.

In contrast, nondurable goods (quickly-used items like dish soap or paper towels) have risen only slowly in price, and durable goods (longer-lived items like appliances or computers) have declined in price. Firms in these industries may face a much more difficult calculus. With wages growing faster than revenues, firms cannot run the same playbook forever. They must innovate; either by increasing output per worker and shedding jobs (which would run contrary to the popular goal of increasing blue-collar employment) or by creating new, improved, complex products that can command a price premium, at least for some time.

While these are broad sketches drawn from a handful of data series and inferences, there is enough information above to indicate what kind of blue-collar jobs can generally support high wages: construction and cutting-edge manufacturing. By contrast, low-tech manufacturing of cheap, plentiful commodity goods is unlikely to support many jobs at high wages.

It is good to be a producer when prices are high, and prices for housing and other structures are indeed high; this gives the construction industry a lot of room to offer good wages, especially for men without college degrees. An expansion of this industry, overall, would benefit workers. This potential improvement has its limits; expanding construction substantially could eventually make the market more competitive, reducing prices, and attenuating this ability to pay high wages. However, overall, a move from lower-wage industries to construction, with its higher wages, would benefit many people.

## THE CONSTRUCTION INDUSTRY COULD SATISFY ROBUST CONSUMER DEMAND

A robust construction industry would also benefit people on the other end of the transaction—the end consumers of homes, business structures, or infrastructure. All of these can, at times, be expensive and scarce. More construction can make them more available and cheaper.

This is most significant, and most observable, in residential housing. Americans spend about $2.8 trillion a year on housing and utilities, more than they spend on healthcare ($2.4 trillion) or food ($2 trillion.)[13] Rent or mortgage is the biggest line item in most family budgets. In addition to being the largest consumer expense, housing is also among the fastest-growing. As shown above, the price of housing has increased faster than wages or other components of inflation. A greater supply of housing could put some downward pressure on prices, making it more affordable. Furthermore, ideally, consumers would like to do more than keep up with inflation. When possible, consumers prefer better and larger houses than they had in the past. Construction is necessary to achieve this goal as well.

In some cases, this simply happens all by itself. After all, what has been described above is a situation with substantial surplus—or gains from trade—to keep both producers and consumers happy. In a normal free market, absent other constraints, people should keep making this trade until there are no more people left who stand to gain from trading.

At least in some cases, this is more or less what has happened. Some metropolitan areas, particularly in the Southwest, have built ample new housing to meet consumer demand. Furthermore, overall Americans have succeeded in improving their housing: for example, the median square footage of a house has increased from 1,525 to 2,301 since 1973; the mean has increased from 1,660 to 2,509 over the same period.[14] In addition to improvement in square footage, it is likely that houses have also generally improved on quality. For example, in the 1970s just 65% of homes had central air conditioning, while by the 2000s, 89% did.[15]

For areas where supply meets demand—where workers get jobs and people get newer, better, or larger houses—the industry is working as it should, and there is no policy issue to address. This is true of much of the United States. However, in some places, the available housing has not kept up with consumer desires. For example, in San Jose, many people are buying the same homes that always existed, but at much higher prices than previous generations bought them for. A typical 1,525 square foot home built in 1973 in San Jose might easily command a price of over $1 million today. The San Jose real estate market is frequently characterized by intense bidding wars over houses that appear on their surface to be fairly average and fairly easy to construct.

Furthermore, even within some cities where overall price levels are reasonable, there are still areas that command a premium. For example, a resident of Richmond might note that prices in the Fan District, a desirable area close to the Virginia Commonwealth University campus, are substantially higher than prices for similar-sized homes outside of it.

At the extremes, when housing is particularly expensive or scarce in an otherwise-worthwhile area, there is a clear loss in standard of living. RentCafé, an apartment listing service, estimates that the average renter in Fremont or Santa Ana lives in less than half the square footage of the average renter in Louisville.[16] This fact may seem shocking, but it is consistent with other attempts to understand the California housing market. The Urban Institute's Claudia Solari also argues that crowding is a growing problem, and it is most acute in California, where renter households are almost four times more likely to have multiple occupants per room than renter households in Kentucky.[17] Households in California would undoubtedly prefer more living space if it were affordable and available. A more active construction industry in the state would help them.

Housing affordability is especially important to the Joint Economic Committee Social Capital Project (SCP) because it is the largest component of family affordability, and increasing family affordability is one of the five main objectives of the Project. Larger families—families with children—are likely to need more livable space, and livable space costs money. Places with higher costs per square foot are less hospitable to families, and this is a problem worth addressing.

There is an additional human cost to expensive housing in the form of long commutes. Typically, housing closer to work is more expensive per square foot than housing in exurbs. Workers who live in exurbs not by preference but because closer-in housing is too expensive, pay a price in time, rather than in dollars. Commutes are generally more onerous in cities that have problems with housing costs.[18]

In many housing markets, residents could clearly be made better-off in the long run through either a reduction in prices, an increase in square footage, or housing closer to work. A stronger construction industry could help with all three of these problems.

Commercial real estate has some of the same basic issues as residential real estate; firms would prefer high-quality spacious offices in central locations, but—much like in housing—office space is becoming increasingly expensive, often in the most desirable places. Much like in housing, construction could help alleviate the problem, by making office space more plentiful, cheaper, higher-quality, and more centrally located.

Finally, public investments like transportation infrastructure or parks or schools also can be extremely valuable. Of course, not all are—they are not necessarily disciplined by the need to satisfy paying customers—but at least some of them are extraordinarily valuable, and measurably so. The George Washington Bridge, for example, connects Manhattan to New Jersey and generates hundreds of millions of dollars in profit from paying users every year, even after paying for its own maintenance.

While it is more challenging to assess the costs and benefits of public investments than private homes, they are noted here to illustrate that robust demand for construction extends beyond the residential real estate market.

## A STRONG CONSTRUCTION INDUSTRY HELPS SAVERS PUT THEIR MONEY TO USE

This report has so far discussed the construction industry as a match between producers and consumers, builders and residents. However, there is an additional activity involved in the process, beyond producing and consuming: housing is a long-lasting investment, and therefore has an impact on saving.

Long lasting investment, or production that is not immediately and fully consumed at the time it is created, is critical for saving. It is in fact one of the few ways that society as a whole can save for the future.

The distinction between individuals saving and the economy at-large saving is crucial here. A single American can save by holding dollars or treasury bonds. However, this saving of government-issued financial assets is perfectly matched by dissaving of a sort from the Federal government. The dollars are a liability on the government's balance sheet because it is charged with holding the dollar's value relatively steady. More obviously, treasury bonds are also a liability for the government as well. An American could also save by lending to some entity other than the Federal government—but that too would result in dissaving of an equal amount by the borrower. At least in these areas, one person's asset is another's liability.

However, not all saving is canceled out with dissaving. The greatest exception is in new investments. For example, consider a typical residential mortgage. By the homeowner's account, they have an asset (the home) and a liability (the mortgage.) From the lender's perspective, they have an asset (the mortgage). On net, the two parties have saved.

In general, a rule of thumb for understanding this is that all paper transactions cancel out in the aggregate; they may redistribute wealth between people, but they cannot create new wealth. Aggregate wealth is only what exists in the real world, and one of the most obvious, tangible, and valuable forms of wealth is in buildings.

Finding outlets for aggregate investment is important because there is a lot of demand for investable opportunities. The 21st century has largely seen plentiful private saving for demographic reasons: aging and wealthy populations in developed markets expect to live a long time in retirement, and therefore like to hold large amounts of wealth in reserve.

Ideally savers would help fund new investments and earn a positive return. However, saving is so plentiful that it has been difficult to find sufficient new investments to spend on. The risk-free interest rates in many developed markets have been driven to zero, or close to zero, multiple times in the 21st century. These low interest rates were not artificial interventions by a specific government, but instead an accurate reflection of global supply-and-demand dynamics imposed by demographics.

This has made deficit-financing cheap for currency-issuing countries, which has some advantages and disadvantages. Debt is more manageable under low natural interest rates, but they also make recessions more likely because of dynamics known as "liquidity traps," where it becomes difficult to hold the pace of spending steady. When debt is lower-interest and output is underutilized, it can be easier for governments to justify inefficient spending or practices that would not be optimal at full employment.

Overall, most economists would prefer avoiding liquidity traps, and one way to do that is to find more outlets for private-sector saving besides additional government debt. The construction of additional housing helps achieve this objective. Additionally, it makes the savers themselves happy, because they have a way to make a yield-bearing secured loan. From the perspective of savers, just as for workers and residents, construction is a helpful activity.

## HOUSING IS HELD BACK BY ZONING

Described above is a situation where there should be gains from trade on all sides: people are eager to work in construction, people are eager to use new structures, and people are eager to provide financing for new structures. In at least some cases, there seems to be a massive amount of surplus available: end user willingness to pay seems to greatly exceed the combined costs of labor and capital, leaving plenty of gains from trade to distribute. This raises the natural question of why the construction projects don't go forward in these cases. The most typical reason is that laws and political customs err too far on the side of hampering the construction industry.

The most important barrier to the construction industry is in residential land use laws: most precisely, in municipal or local governments drastically limiting the amount of livable indoor space per unit of land.

Recent academic work by Edward Glaeser and Joseph Gyourko can help quantify and identify this effect—the gains from trade foregone. In a 2018 paper, they construct a measure of "minimum profitable production cost" for housing, which includes cost of land, cost of construction, and a rate of entrepreneurial profit to compensate the builder. Then they note how cities' actual housing costs compare to the minimum profitable production cost. They find that cities fall into three rough categories. In some places, such as Detroit, houses are actually cheaper than the minimum profitable production cost. This suggests that demand for housing was greater in the past than it is now, and houses can therefore be purchased at a discount. In a second category of places, such as Atlanta, home prices are about on par with construction costs, suggesting that builders are capable of responding to new demand. In the final category of places, though, such as San Francisco, home prices exceed the minimum profitable production cost. This suggests that San Francisco is constrained by something other than demand or building costs.[19]

While San Francisco is one of the most dramatic examples of the phenomenon—and one where an entire metropolitan area struggles—the phenomenon can also be seen in other cities, or at least, parts of other cities. It is common for some parts of a city to be noticeably more expensive than other parts, even for roughly identical structures. Glaeser and Gyourko's research concerns metropolitan areas, but the framework is sound for more granular analysis as well, and quantifies the gains from trade left on the table in places where prices exceed construction costs.

The most likely causes of the phenomenon are high demand coupled with limitations on constructing more livable space. This is a narrow and particular subset of housing regulations; many housing regulations have other objectives and effects. Building codes might promote home safety, for example, by limiting vulnerability to earthquakes or fires. Building codes also come at a cost in terms of additional work, which does raise home prices (and create more paid work for builders.) However, many of these effects are limited in scope since the codes do not explicitly restrict housing supply.[20]

The strongest effects come when new construction is blocked almost entirely. Consider two metropolitan areas of similar size: North Port-Sarasota-Bradenton, FL, and Oxnard-Thousand Oaks-Ventura, CA. Both areas have a population of about 800,000, and both are relatively desirable places to live. However, the Floridian metropolitan area built about 10,000 housing units a year in both 2018 and 2019. In contrast, the Californian metropolitan area built just 1,146 units in 2019 and 1,204 in 2018.[21]

The effects of these choices are very straightforward. North Port-Sarasota-Bradenton makes new housing available for the growing population that wants to live there. As a result, it has reasonable prices. In contrast, Oxnard-Thousand Oaks-Ventura keeps housing supply restricted, and forces people to bid competitively against each other—not to pay construction workers, but to grab limited admissions to the area. Unsurprisingly, Glaeser and Gyourko identify it as one of the areas with the highest ratios of price to minimum profitable production cost.[22] This identification is further reinforced by the U.S. Census's estimates of regional price parities: rent in North Port-Sarasota-Bradenton is 20% above the national average, while rent in Oxnard-Thousand Oaks-Ventura is 75% above the national average.[23] It leaves potential jobs, potential homes, and potential gains from trade on the table.

This raises the question: why landowners and homeowners in the area do not simply attempt to build more homes on their lots, or sell to someone who will? This happens because there are rules that prevent people from doing so. For example, in much of the land in these cities, multifamily designs such as duplexes or apartment buildings are simply illegal. Additionally, even the multi-family residences are very small; only a handful of buildings in the whole area are more than five floors. One reply to this critique might be that places like Oxnard-Thousand Oaks-Ventura are too "full" to build new housing. But it is hard to imagine why this would be the case without begging the question; the "fullness" is only evident if one already assumes that current land use must persist, and in fact, must be enshrined into law.

The same broad issues that are present in Oxnard-Thousand Oaks-Ventura are also present in many other areas, including some large ones: San Francisco, San Jose, Los Angeles, Washington, and New York. While the precise mechanisms differ, all have fewer and more expensive homes than an unrestricted market would generate. This is not just true of expensive cities, but also certain areas within smaller cities.

There are many ways that land use policy can effectively stop housing supply entirely. The most damaging policies either limit the number of families that can live in a unit of land area, or limit the amount of buildable indoor space per unit of land area, or both.

For example, single-family zoning prevents a property-owner from building any type of housing other than a detached single-family home, even if a location is very desirable and many families would like to live there. Minimum lot sizes force residents to buy larger yards than they might prefer. Maximum floor area ratios (FAR) place a cap on a building's total floor area (all levels, not just ground floor) as a percentage of the lot size. A related measure, building coverage ratio, looks only at the footprint size. Minimum setbacks establish a necessary distance between a building and a street or neighboring lot. When too onerous, these force residents to have smaller houses or larger yards than they would prefer. Height limits block the creation of livable space by adding stories. Finally, parking minimums, which require off-street parking spaces, preclude builders from using that space for livable area.

While there are sometimes justifications for individual regulations, many of them restrict what property owners can do with their space, and they err consistently on the side of making less space available for people to live in.

The result is that housing is limited by a sort of collusive trust, similar to how oil-producing countries used to agree to limit production. It might be individually rational or profitable for people to add housing, but collective rules prevent them from doing so. The restricted supply results in higher prices, making it more difficult to join the neighborhood and more difficult to be able to afford to start a family.

Plenty has been written about these policies and their potential drawbacks individually, but it is best to address them with a single thesis that gets to the heart of the underlying concept: as Nolan Gray puts it, density is how the working poor outbid the rich for urban land.[24] In a competitive market, few individual families with single-family homes could outbid the combined efforts of two families who would split a plot in half and pay for housing on each half. Fewer still could outbid four families paying for a pair of duplexes, and almost no one could outbid a dozen families or a hundred families in a larger building. The way that single-family homeowners win the bidding war for urban land is to preclude those options through the legal system—to make it illegal for larger-scale arrangements to even exist.

This behavior curbs the construction industry and the jobs it creates, as well as making it harder for many Americans to afford housing and start a family.

## LEVELS OF GOVERNANCE AFFECT HOUSING REGULATION

Despite the efficiency and affordability case for building more housing, rules such as those described above are rather common at local levels of government. There are some fairly simple reasons for this: many of these choices are rational to the people choosing them, even though they produce outcomes that are socially suboptimal. The difficulty of bargaining over unclear property rights is another source of inefficiency. Below is an exploration of some of the political economy issues in housing: an examination of why suboptimal policies end up being created in the first place.

Several of these political economy issues have to do with the size and scope of different layers of government. The United States Constitution explicitly provides for a federal government while reserving many powers, both enumerated and otherwise, to states. A variety of local or municipal governments also exist. It is up to states to determine what authorities, if any, to delegate to the local level.

States should consider this question carefully: by definition, the smaller levels of government in states do not represent all residents of the state. For example, in Oregon, the mayor of Portland does not represent people from Salem. This is in general a useful feature for accountability, experimentation, and choice; Portland can try one thing, Salem can try another. If one of the cities' policies fails, it can look to a more successful city as a model, or risk losing those who vote with their feet. Alternatively, both cities might succeed but in different ways, allowing each set of people to live as they prefer without imposing those preferences on others.

A drawback of this model is that would-be movers or would-be residents may not have representation at the local level, creating a Catch 22 for those who would like to pay for new housing and move into a neighborhood: in order to do so, they must petition the local government to allow housing development, but in order to petition the local government, they must already live there.

This is a problem for state governments to consider. The Oregon state government does represent people who would like to move from Salem to Portland or vice versa, even if the cities do not. In fact, it has an interest in the free movement between the cities: the "voting with their feet" component of accountability for local governments is useful only if people can actually do it.

For these reasons, state governments should consider carefully how much power they would actually like to delegate. The right to enter into contracts, or homeowner associations, or, most formally, local governments, is a useful one. In fact, states enable these legal structures by providing them with use of the court system for enforcement. In effect, the state creates a limited power to write additional rules beyond the state's own laws.

However, states need not enforce absolutely every kind of contract imaginable. For example, California does not enforce a kind of labor contract known as a non-compete agreement, which would restrict an ex-employee of a firm from working at a competitor. California judged that allowing such an agreement in order to

restrict commerce is not actually in the interest of the public at large. States could make similar considerations for housing restrictions.

Another issue to consider is the design of elections within cities. Cities sometimes divide themselves into wards, a smaller jurisdiction within the city that has its own representation within the city government. They also have at-large offices, elected by the city as a whole. Recent research by Evan Mast shows that cities that switch from at-large representation to ward-level representation tend to have more restrictive housing supply.[25] This is in effect a microcosm of the larger issue in local representation. While it may be in a city's interest to allow more housing overall, an individual neighborhood may find it advantageous to restrict supply. Elected representatives follow through on the interests of their constituencies. Given these considerations, cities with housing affordability issues may be better off using more at-large seats and fewer ward-level seats.

Notions of efficiency, representation, and self-interest depend a great deal on the level of granularity: the size of the group of people or the jurisdiction. For example, it might be individually rational or profitable to turn a property into a multi-family home, yet unpopular at the neighborhood level because of parking concerns, and still yet efficient at higher levels of analysis because of a citywide housing affordability crisis. Depending on the unit of analysis and the legal or political structure, different outcomes may look optimal and different outcomes may be reached. In general, though, large jurisdictions should be wary of delegating commerce-restricting powers.

## FORMALIZING INFORMAL RIGHTS CAN IMPROVE EFFICIENCY

Another way to analyze the problem is to understand and address some of the reasons why voters are so interested in using government to curb housing development. Often, there are material reasons: preserving access to amenities. Particularly, their concerns are about amenities that economists would call "rivalrous:" that is, where one person's use may crowd out someone else's use. Some examples of these include roads, parks, transit systems, and street parking. While they have no explicit ownership of these amenities, they have an implicit share by living nearby, and that share would be diluted with more residents. They therefore support regulation that curbs housing development, not because they dislike housing per se, but because they would like to preserve their fractional share of rivalrous amenities.

For certain kinds of shares in amenities—parking, in particular—a better system may be available that could prevent concerns of share dilution while allocating parking more efficiently in the future. Counterintuitively, this involves giving people more control, not less, over their neighborhoods. Such a system would make formal the rights that were previously only implicit.

For example, a neighborhood with relatively-available street parking might be inclined to fight to keep that street parking by attacking new developments that might dilute residents' share of the street parking. The best solution may be to formalize their right: give them ownership over the parking spaces, and make that ownership tradeable or alienable. In doing this, a government can allow people

to hold onto their space, if that is indeed important to them, or sell that space and reallocate it to someone else if it is not.

This same principle of formalizing rights and making them alienable is useful in other areas of urban land use, such as setback rules. Rather than making a hard rule that applies to a whole neighborhood, it would be better to formally distribute, and make alienable, the veto rights over some kinds of building. Consider, for example, setbacks to the side: these rules are designed to protect neighbors to the side. Those protectees should have a choice to waive those protections under whatever terms they see fit: for example, for a side payment or some other concession. Then they can choose how much they value a buffer zone between their property and the next, rather than having that choice made for them.[26]

This idea of formalizing rights and making them tradeable or waivable comes from the most famous insight of Ronald Coase: if formal rights are made clear, and trading them is sufficiently possible and the costs of making the transaction is low, then an efficient outcome will ultimately be achieved, regardless of the initial allocation. Cities can take advantage of this insight by distributing formal rights where informal rights were previously understood to have existed. This is not a perfect solution: in practice, even with formal rights, there can be disputes and inefficiencies, especially if there are many of them and putting together a negotiation is difficult. But it can help, especially for relatively simple rights such as street parking, to allow finer and more efficient solutions than blanket rules.

## DISCRETIONARY REVIEW SHOULD BE AVOIDED FOR SMALLER PROJECTS

If formal rights to property can increase efficiency and allow for speedy and consistent resolution, discretionary review tends to do the opposite. In some cities, almost any residential construction project—even ones that are fully within the law—can still be open to a politicized review process. Under such a system, would-be builders must do things like take part in hearings, conduct studies, and attend meetings, in order to get a project started.

A discretionary process has some merits for structures like airports or stadiums, which may have unusual or undesirable effects on neighbors, often known as externalities. The purpose of discretionary review is, at least in theory, to address those externalities. However, it is overkill for ordinary apartments, shops, and offices. Cities need large numbers of these basic building blocks, and a review of each one is a costly solution relative to general rules. Furthermore, the asymmetries of discretionary review can be too easily gamed by opponents.

For example, delays to acquire more information—even lengthy ones—are treated as a neutral choice, when in fact they contain, de facto, the same policy prescription as a decision against the project. Furthermore, the epistemological standards are often asymmetric. Casual claims against a project are effectively treated as true until rigorously refuted. Opponents may assert, proponents must prove. In effect, projects are presumed guilty until proven innocent. Finally, there is asymmetry in terms of the material risks taken by each side. A would-be builder

has money tied up in the project, and suffers financial hardship from delays, while opponents often have no such material stake.

One particularly strong example of how all of these items fit together lies in the Mission District of San Francisco, with a case sometimes known as the "historic laundromat," a five-year story of a laundromat owner, Robert Tillman, who attempted to redevelop his building into mixed-use housing. He began seeking authorization to do this in 2014. Local activists, some of whom wanted to purchase the property at below-market cost for a different purpose, attempted to stop or delay this redevelopment.[27] The proposal was within all of the explicit laws, but nonetheless was subject to discretionary review by local government officials.

The case first became notorious when Tillman was forced to determine whether or not the laundromat was of historical significance, and provide a report on that matter. This drew some scoffs at the notion that a laundromat could be historic.

After Tillman proved the laundromat had no historic value, activists argued that the proposed development might cast new partial shadows on a nearby school.[28] The school was to the south of the site, and San Francisco is in the northern hemisphere, so any shadows cast would be relatively minimal. However, shadows were investigated nonetheless. Tillman eventually won approval after five years and after suing the city, but many economic resources—by Tillman's estimates, close to a million dollars—were spent investigating largely-unimportant claims.

While this is usually given as a single anecdote of the barriers to construction in San Francisco, it is instructive; it shows flaws in the process that could easily repeat themselves in another case.

First, discretionary policy is wasted on a simple building remodel. San Francisco is a large city with many laundromats. Rather than governing each laundromat individually through meetings, it should have broad and consistent rules about how they can be modified, saving time.

Second is the issue of standing—nobody had come forward to say that the site had historical value to them, personally, as a laundromat in particular, and that the historical significance would be lost if the laundromat were turned into something else. Furthermore, those who raised the shadow complaints were not among those who might be affected by the shadows. A well-functioning legal system should generally address only the interests of real people who come forward; it should not shop around for hypothetical interests of people who may not want to bring legal opposition, and may not even exist at all.

Third is the asymmetry in burden of proof. It was Tillman's responsibility—not his opponents' responsibility—to provide a 137-page report on the historic value of the laundromat. The opponents were permitted to casually claim something, while Tillman was required to rigorously refute it.

Fourth is the asymmetry in terms of the default action taken (or, more pointedly, not taken) as the dispute was being resolved: while the dispute was in process,

Tillman was not allowed to move forward. In effect, just by creating a dispute—any dispute—the opponents were immediately awarded the outcome they desired.

Fifth is the lack of a time limit on bringing claims. Opponents could raise concerns serially, rather than in parallel, lengthening the conflict. This interacts strongly with the previous flaw—that the policy default while an argument was ongoing was identical to the outcome that the opponents wanted. They were therefore incentivized to lengthen the process by raising complaints one at a time, even if the complaints were relatively weak.

Sixth is the style of analysis—a lengthy breadth-first search for all possible arguments pertaining to the issue, no matter how ancillary. This is generally not an effective way to do cost-benefit analysis. Well-considered decisions are typically driven by a few key ideas—by weighing the primary costs against the primary benefits and evaluating the magnitude of those costs and benefits correctly. In the case of the Mission Street laundromat, all parties were clearly far more concerned with how the property would be used, not what kind of shadow it would cast. The decision should have been made on the important issues, with the unimportant claims ignored.

Discretionary review simply has too many pratfalls to be used for ordinary residential, commercial, or office buildings. For these, governments should instead elect a more streamlined approach. For example, the smallest externalities can be ignored, on the grounds that litigating them is more expensive than simply allowing them to continue. For larger externalities, there are a few options. Following the insights of Ronald Coase, a government can give people protection from certain nuisances by default, but also give them the option to waive that right on terms of their choosing—for example, in exchange for some kind of concession. Government could also charge fines or fees for inconveniencing behaviors. Finally, the largest externalities can be banned entirely. These approaches may not be better than discretionary review in all cases, but enforcement is relatively quick, consistent, and accountable.

## DECISIONS SHOULD BE EXPEDITED FOR LARGER PROJECTS

Even much larger entities with far more political clout suffer problems like Robert Tillman's. For example, the University of California San Francisco (UCSF) is currently interested in expanding the hospital and medical research facilities at its Parnassus Heights campus, and has been met with opposition by neighboring property-owners, and even lawsuits.[29] Hospitals are of course much more important and much less numerous than individual apartments or shops, so a discretionary and unique decision-making process for them makes some sense. However, if discretionary choices must be made, they still should be made with speed and clarity.

Unfortunately, in many jurisdictions, speed and clarity are not particularly forthcoming. UCSF, much like Tillman, has been met with complaints about shadows. UCSF, much like Tillman, has been met with requests for delay.[30] While UCSF has greater political clout, and some protections from its status as a state institution, the same pattern of mistakes is present. Delaying to assess the

situation delivers a default victory to the proponents of the status quo, and they are therefore incentivized to create such delays.

As with the laundromat, prominent opponents raised trivial issues, ones unlikely to change the final verdict, but likely to delay building and create a chilling effect on future builders. Prominent arguments against the expansion include issues such as obstructed views and bird strikes.[31] It is unlikely that—during the worst year for public health in living memory, in which three million Californians caught a potentially deadly disease—bird strikes would ultimately move the needle and cause the government to reject the need for a hospital. However, a decision-making structure that rewards any argument at all, no matter how trivial, results in the increased production of trivial arguments.

A key component in this decision-making structure is the California Environmental Quality Act (CEQA), which forces a drawn-out process of analysis and public disclosure for all projects. Critically, even if a concern is relatively unimportant, virtually anyone is able to sue by alleging that the concern was not sufficiently analyzed. The lawsuit against the UCSF Parnassus campus takes this approach.

The CEQA process contains many of the same pratfalls as those of the historic laundromat case. As with the laundromat, much higher burdens of proof are placed on the new plan rather than the status quo. For example, the aging current campus is not fully in compliance with modern seismic codes. The renovation would rectify this issue. Each day of delay is, in effect, a day of replacing a modern building with a non-compliant building for one more day. However, those who wished to delay and retain the current structure, rather than start construction, had no obligation to assess the environmental impact of reduced seismic compliance, even though that would be an outcome of fulfilling their request.

There are, of course, more consequential impacts to the expansion plans—ones worthy of some degree of consideration. However, even the more serious issues are plagued by a lack of formal principles of standing or specific rights.

For example, one objection of the opponents is that the hospital did not make sufficient plans on where new employees might live. This objection was not made by the prospective new employees themselves, but rather, other people not affiliated with the hospital. Their claim relied on a long chain of causality: that because the hospital was planning to pay new employees, those employees would have income that they might then use to buy or rent housing on the open market, and that they might outbid other unnamed people for those homes. While this is generally valid economic logic, there is no clear indication of which rights are violated, and who has the standing to challenge. Generally speaking, one does not have the right to object to other people's jobs, and certainly not on the grounds that those other people make purchases with their income.

Traffic is another commonly-raised objection, and one of the components of the legal effort to stop the hospital; hospital workers and patients would use the roads nearby. This proposition is undoubtedly true. However, the homeowners do not

own roads, and certainly not major roads like Parnassus Avenue. They own only their homes. The question before the city is whether the incumbent homeowners have a kind of ownership right to the road that is so broad and so far-reaching that it extends not just to the roadway, but even to parcels of land nearby that do not belong to them.

Considering a formalization of the rights is often a clarifying exercise: it can help make explicit what is being demanded, and help one decide whether or not it is desirable. In many cases, such claims will then sound unreasonable, and they can be rejected. But formalization can also serve a practical purpose when the claims are relatively modest and paired with the principle of alienability: that is, make it possible for people to trade their formal rights to the things they have claims over.

There are many potential ways that construction can be held back by local governance. However, when considered carefully, they often can be reduced to the same abstract issue: people have some limited rights to ask neighbors to address externalities, but those limited rights are poorly-defined. Reforms that define those limited rights better—whether affirming or denying them—ultimately make for a quicker, less acrimonious, and more efficient process.

## THE FEDERAL GOVERNMENT CAN GET OUT OF THE WAY

Although the sections above have largely concerned state and local laws, the federal government also hinders the construction industry. Sometimes it engages in costly delaying processes similar to the ones found in states. It also restricts the autonomy of growing western cities through an overly-zealous and inflexible program of federal land management.

The National Environmental Policy Act (NEPA) requires assessments of the environmental impacts of federal projects, or projects that would require a federal permit. While principled cost-benefit analysis is a useful way to make decisions, the process has become distorted over time through legal abuse. Whatever its original intentions, it is now one of the greatest obstacles to project development, and it should be reformed.

NEPA is not a binding environmental law in the way a layman might think. It does not prohibit specific actions, or demand that builders avoid specific environmental impacts. Instead, it requires review of federal actions that affect the quality of the environment. These reviews are typically called environmental assessments (EA) or, for more expansive reports, environmental impact statements (EIS). Included in these federal actions is the issuance of permitting to private projects, so NEPA also affects private projects.

As with local deliberation processes, the law has resulted in increasingly-long evaluation time and a persistent bias against building—even in cases where the new building would be more environmentally friendly. For example, the Federal Highway Administration completed 114 EIS from 2010-2017, with a mean time to completion of 7.30 years and a median of 6.85 years each. The Army Corps of Engineers completed 89, with a mean time of 6.13 years and a median of 5.16.[32]

To understand what is wrong with NEPA, it is first worth outlining the key tradeoff it makes. The tradeoff is not one at the object-level: it is not about, for example, how much to prioritize animal welfare over human welfare, or how much to prioritize industrial production over pollution. Those tradeoffs are up to policymakers, regardless of what the analysis shows; a NEPA review could conclude that a project harms the environment, and a federal agency could nonetheless approve it. This is not merely an academic point. NEPA regularly slows down environmentally-friendly construction, such as wind farms, or even the New York City plan for congestion pricing in Manhattan. NEPA is not a direct, substantive environmental protection.

Instead, NEPA is more like an environment-agnostic tradeoff at the abstract level: it is about the value of having additional information against the cost of acquiring that information. Spending time to write reports can help clarify the stakes of an issue, but that clarity comes at the cost of effort and time. To the extent that NEPA cheaply provides valuable information, it could be considered successful. However, to the extent that it expensively provides unimportant information, it fails.

Unfortunately, NEPA errs too far towards the latter. This is especially true at the margin. It is obviously helpful for the Federal Highway Administration to take some time and acquire some information before doing something or approving something. But at the margin, the question is not one of some information gathering against none. It is instead a question of six years' worth against five. The relevant tradeoff is whether additional years of study are worth it. This seems unlikely. If something is so obscure and so difficult to notice that one can only uncover it in a six-year process, not a five-year one, then it is also probably not important enough to be worth delaying decisions an additional year just to learn about it.

If the process is indeed too long—if it spends too much time in analysis paralysis—then one should ask why it hasn't been made shorter. The best answer is that its current structure creates incentives to delay. Specifically, proponents of the status quo, whatever that might be, can keep the status quo for longer if they push for more and more expansive acquisition of information. Even if the information is not actually important enough to be material to the decision, simply creating a new question to be answered can slow the process down, and get status quo proponents—temporarily—what they want. Reforms are difficult; those with expertise in navigating the process are paid handsomely to navigate it, and therefore benefit from its complexity.

The ultimate result of NEPA is substantially higher infrastructure costs and substantial delays to projects. Beyond the direct legal costs and the costs of delay, there are some more subtle costs. NEPA and other "citizen voice" measures tend to increase the cost of infrastructure substantially on average through demands for extremely costly improvements.[33]

Many of these demands would fail a cost-benefit analysis on an individual basis. However, because they are attached to an otherwise-worthwhile infrastructure

project, and because those making the demands have so much leverage, it is better for the builders to pay the ransom in order to move forward.

In the longer run, this process creates a chilling effect on construction. While some projects power through, many more are deterred by the uncertainty and cost of the process.

One of the best reforms to NEPA available is a suite of policy proposals from Senators Mike Lee, Ted Cruz, and Kevin Cramer.[34] These reforms include many elements that would speed or clarify the process, including a requirement that plaintiffs bringing NEPA-related suits demonstrate tangible harm, require clear and convincing evidence for injunctions, a "shot clock" for review, and permission for agencies to reuse relevant previous EIS work. This style of reform would make the NEPA process more flexible and nimble, and substantially reduce its status quo bias.

Another way the federal government gets in the way of the construction industry is with an out-of-control federal land management program that strangles development of cities in western states. While Americans from the east half of the country typically think of federal lands as uninhabited wilderness, this is not the case for growing western states. Frequently, federal land ownership in states like Utah goes right up to the edges of, or even into, suburban areas.

According to the real estate company Geomancer, 650,000 acres of land are within one mile of city boundaries.[35] These lands have been valued as part of a tax dispute; Utah could earn hundreds of millions of dollars in additional property tax revenue if lands were in private hands. The Department of the Interior offers an offset (though an insufficient one) for this lost property tax revenue, called "Payment in Lieu of Taxes," or PILT. The value of federal lands near fast-growing western cities therefore is a subject of considerable debate.

This tax debate can be informative, though, on what is being given up by the overreaching federal lands program: valuable housing construction. The federal government should return autonomy to Utah and other western states by relinquishing some portions of federal land—particularly areas nearest to growing populations and that contain no historical landmarks or hold cultural significance—for use by private citizens, who are more likely to employ that land in efficient valuable ways.

## THE CONSTRUCTION INDUSTRY BENEFITS FROM MACROECONOMIC STABILIZATION AND NEUTRAL TAX AND TRADE POLICY

Most policy issues in construction are regulatory: policies that either delay or prevent building. However, additionally, there are a few macroeconomic or financial issues worth considering, where better policy could help make the construction industry more robust.

The first of these is in macroeconomic stabilization, which is especially important for investor confidence in long-lived assets such as buildings, or for lender confidence in the mortgages that help finance residential home construction. When investors fund the construction of a large building, or lenders issue a mortgage, they are exchanging a large amount of present money, or principal, in exchange for cash flows at a future date: for example, rent from tenants, or mortgage payments from the borrower. The structure of this arrangement—where people trade future cash for present cash—is heavily dependent on the discount rate. The higher the discount rate, the less likely it is for an investment in a new building to be worthwhile.

The most common model of cost of capital—one that is both simple and approximately true—is that investors choose a discount rate based on a combination of two factors: the risk-free nominal interest rate for the country as a whole, and a risk premium based on the systemic or market risk of the asset—that is, risk that cannot be diversified away because it is determined by the economy as a whole. This model is known as the Capital Asset Pricing Model (CAPM) and while it is not strictly true in all cases, it is a solid first approximation of investment returns.

The key insight of the CAPM is that in a deep and efficient market where diversification is possible, idiosyncratic risk does not matter, and instead only market risk—the risk that income throughout the economy all falls at once—creates the premium.

For example, in construction, an idiosyncratic risk might be the idea that a particular building, or particular kind of building, would be less popular than the builder had hoped. While this is a problem, it also has a solution: simply invest in a diversity of structures, so that one individual mistake is not particularly costly.

However, the market risk, or "beta," is that people everywhere will have lower incomes, all at the same time, and therefore be less willing to spend on rent. This risk cannot be diversified, so it still commands a premium from investors, raising the discount rate. The higher discount rate then causes some construction to be foregone.

It would be possible to lower or even eliminate the market risk premium by successfully stabilizing nominal income in the economy.[36] This would prevent the source of market risk for construction—if nominal income is expected to grow at a stable rate, there will always be willing renters for construction in the aggregate, and rent levels will be more predictable. Stable nominal income growth, and the reduction of market risk, could reduce the cost of capital for all sorts of assets, and increase investment generally, including in construction.

A second financial consideration for the construction industry is the tax code. Business-level taxes are biased against new construction because they do not allow businesses to immediately deduct construction expenses, as they would for almost all other expenses. Instead, they deduct the value of those expenses over several years—up to 39 years for nonresidential buildings.

From an investor's perspective, this asymmetric treatment biases businesses against construction, relative to other expenses that might bring in revenue. This is misaligned with the motives of investors, who are taught to care about free cash flow, not income, when evaluating business ventures.

Under most circumstances, these two concepts are closely related. However, they differ when it comes to longer-lived assets owned by the business. If a business builds a new factory, for example, it has a major cash outflow but not a loss of income because it traded away cash for an equally-valued factory.

The investment in a structure compares unfavorably to other kinds of investment—for example, hiring a management consultant to improve the process at an existing factory. This is written off as an immediate expense: a "loss" on the business's income statement.

One could note that these are actually identical from an investor's perspective: both are ways of spending cash now to earn better returns later. And one could note that the income statement treatment is mostly an artifact of subjective accounting principles. The consultant's contract was an exchange of cash for hopefully-long-lived advice that presumably is worth what was paid for it. The fact that the factory goes on the balance sheet and the income statement, but the consultant advice is written off, is mostly a concession to practicality and simplicity, not a real distinction with economic merit.

However, an even better concession to practicality and simplicity would be to equalize the treatment of all expenses by moving entirely to a cash flow treatment and allowing the full expensing of structures. This would align the tax code more fully with investor incentives, and not create a bias against construction.[37]

One of the seminal attempts to quantify the effect of taxes on investment behavior came from Robert Hall and Dale Jorgenson (1967), who derived an expression for the cost of capital.[38] An extension of the Jorgensen-Hall framework can actually show that tax rates do not distort time preferences if capital costs are deductible.[39] This is not to say that taxes do not matter at all—they do take money from the private sector, they do disincentivize some productive behaviors, and they do impose administrative costs for payers and collectors. However, under full expensing, taxes no longer bias the private sector against long-term assets relative to other kinds of production.

Finally, trade policy in recent years has been a contributor to extraordinarily high lumber prices. In a long-running political dispute, U.S. lumber producers have accused their Canadian counterparts of gaining an unfair advantage through the use of Canadian public lands, and sought retaliatory tariffs. These tariffs have, in turn, been passed onto U.S. homebuilders, making it more expensive to build a home.[40] And finally, those expenses have been passed onto American families, making homes less affordable. It should be a high priority to find a way to reduce or remove these tariffs.

## CONCLUSION

Construction has a great role to play in two of the most important aspects of economic life: connecting people to work, and making family life more affordable. It provides a great deal of opportunity and fairly high wages to workers who otherwise have weaker opportunities in the job market: particularly, men without college educations and Latinos. Furthermore, the high and growing demand for structures makes it a much more sustainable source of blue-collar jobs than many manufacturing industries.

Construction also helps make it more affordable to raise a family. It is often said that housing, health, and education are three of the largest and fastest-growing costs for raising a family. Housing in urban areas, particularly, has become especially expensive—a problem that disproportionately impacts households with more people to house.

Construction is also often important for public or quasi-public infrastructure in sectors like transportation, defense, and energy.

Given its substantial benefits to both users and builders, it is a puzzle that Americans do not build things more often. Above are some of the answers to that puzzle—some of the impediments to the construction industry that keeps it from reaching its full potential. Clarity in regulatory frameworks, reforms at the local level, an improved tax code, reduced tariffs, and stable monetary policy would all help the construction industry reach its full potential.

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# Improving the Effectiveness of Investments in Youth and Young Adults

# Multiple Choice:

## Increasing Pluralism in the American Education System

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Three decades after the debut of the nation's first voucher system, educationreform discussions have grown repetitive. Instead of continuously retreating to dueling impact evaluations, policymakers interested in education should return to first principles.[2] Debates over choice in schooling should focus on what, fundamentally, the role of education ought to be and what underlying principles public policy ought to reflect.

The Social Capital Project has adopted improving the effectiveness of youth investment, and particularly strengthening parents' ability to invest in their children, as one of its core goals.[3] "Investment" should not be construed narrowly, concerned only with improving test scores and educational attainment. It should also encompass parents' ability to bring their children up in the values and traditions they hold dear, and to surround those children with an environment that supports their formation as burgeoning young adults.

Investing in children relies on social capital — the value embedded in relationships, interpersonal networks, and connection to institutions. Children spend more formative hours in schools than in any other institution save the family. Ideally, schools formalize community relationships, embody the values and traditions of the community, and teach children not just factual knowledge, but also the expectations of life in a liberal democracy.

However, the American education system makes it difficult for parents—unless they have sufficiently high incomes—to individually tailor their children's educational experience. Most families are defaulted into a one-size-fits-all model, designed in the age of assembly lines, and no longer fit for era of technological disruption.

To expand the ability of all parents, regardless of income, to better invest in their child's educational experience and development, we must increase the role of civil society in education, ensure a diversity of educational paths, providers, and philosophies, and hold providers to clear standards.

This approach, defined by Johns Hopkins University scholar Ashley Rogers Berner as "educational pluralism," is common in education systems across the globe.[4] As Berner points out in her definitive exploration of the topic, ***Pluralism and American Education: No One Way to School***, educational pluralism recognizes the value of having distinctive school cultures and couples choice with accountability.[5] American families would benefit from an education system that cherishes cultural distinctiveness, and embeds students in a broader context of intergenerational support. This paper will explore the case for an explicitly pluralistic conception of education, and highlight policy options that could increase the degree of pluralism within our educational system.

## A BRIEF HISTORY OF EDUCATION IN AMERICA

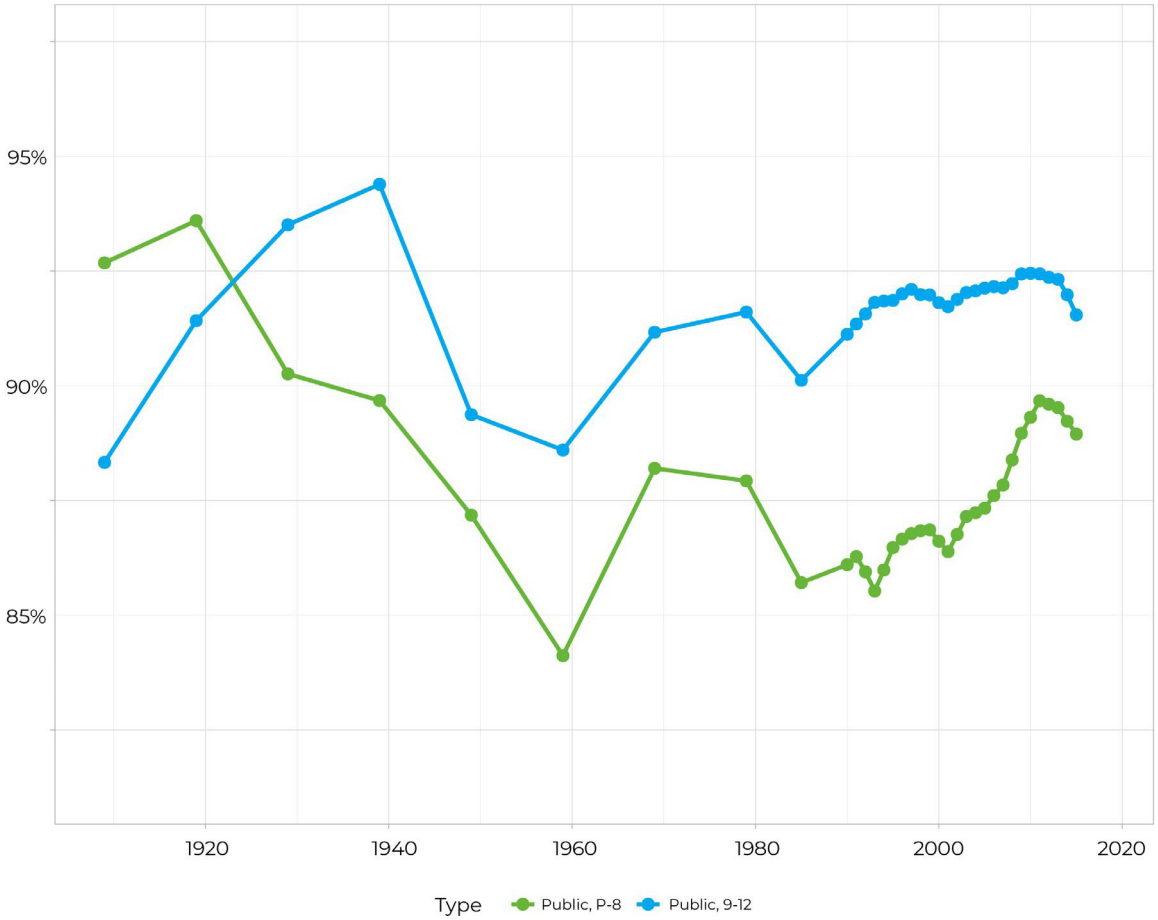
From its beginnings, American education was situated within a context of moral formation. In the colonial era, schooling was handled by groups of families banding together to hire a schoolteacher, usually from a specific religious tradition, to offer instruction in reading, writing, and morals.[6] The first legislative step towards public education came when the Massachusetts Bay Colony passed the General School Act of 1647, better known as the Old Deluder Satan Act. It required cities of fifty families or more to hire a schoolteacher so that "ye ould [sic] deluder, Satan" might not take advantage of illiteracy to "keepe [sic] men from the knowledge of ye Scriptures."[7]

In the 19th century, perhaps due to increasing immigration from southern Europe and Ireland, American intellectuals pushed for the development of "common schools." They sought to strip schooling of all "sectarian" content and instead provide a "universalist" (non-sectarian Protestant) style of education to all students.[8] The inventor Samuel Morse complained that "Popery [Roman Catholicism] is the natural enemy of ***general*** education," arguing that sectarian schools were "***prisons*** of the youthful intellect of the country."[9] In 1875, President Grant called on his countrymen to

> "resolve that not one dollar of money…shall be appropriated to the support of any sectarian school. Resolve that neither the state nor nation, nor both combined, shall support institutions of learning other than thosesufficient to afford every child growing up in the land the opportunity of a good common school education, unmixed with sectarian, Pagan, orAtheistical tenets.[10]

This approach was nearly enshrined in our Constitution. A proposed amendment, referred to by the name of its sponsor, Congressman James G. Blaine, would have barred any "money raised by taxation" from going to any religious or sectarian schools, and precluded any "peculiar doctrines, tenets, belief, ceremonials, or observances [being] taught or inculcated in the free public schools."[11] The federal Blaine Amendment passed the House in 1875, but failed by four votes in the Senate.[12] But the spirit of the amendment was taken up by states and made a condition of admission to the union for western territories. By 1913, 33 states had constitutional provisions barring state funds going toward sectarian education; notably, non-sectarian (meaning, Christian universalist) prayer and reading of the Bible in public schools was generally exempted under this regime.[13]
Over the past century and a half, delivery of educational services has been predominately state-funded and state-operated. State provision of education has proved remarkably stable. In 1909, 92.1 percent of students in prekindergarten through eighth grade attended public schools. A century later, fully 89 percent of students in prekindergarten through eighth grade, and 91 percent of high school students, attended public schools.[14] Religious and cultural factors made Catholic schools the largest meaningful exception to the public education system.[15] In 1960, at their twentieth-century peak, Catholic schools were educating roughly one out of every eight school-age children.[16]

Figure 1: Fraction of Enrolled School-age Children in Public School, by Grades P-8 and 9-12, 1909-2015




Source: Digest of Education Statistics, Table 105.30

Public education became more centralized and more professionalized — the number of school districts fell from over 100,000 in 1940 to fewer than 14,000 today.[17] It also ceded its aspirations towards moral formation. A 1951 publication of the National Education Association encouraged schools to teach "consensus" common values and set aside particular moral and religious teachings.[18] Supreme Court cases stripped away explicitly religious elements in public education.[19] Education, intended to resist the depravities of the "Old Deluder" or to induct youth into the creed of democracy, came to be re-conceptualized as a method of training productive workers, building human capital, and encouraging industriousness. As far back as the 1920s, a school board president in Muncie, Indiana, lamented that "For a long time, all boys were trained to be President...Now we are training boys to get jobs."[20]

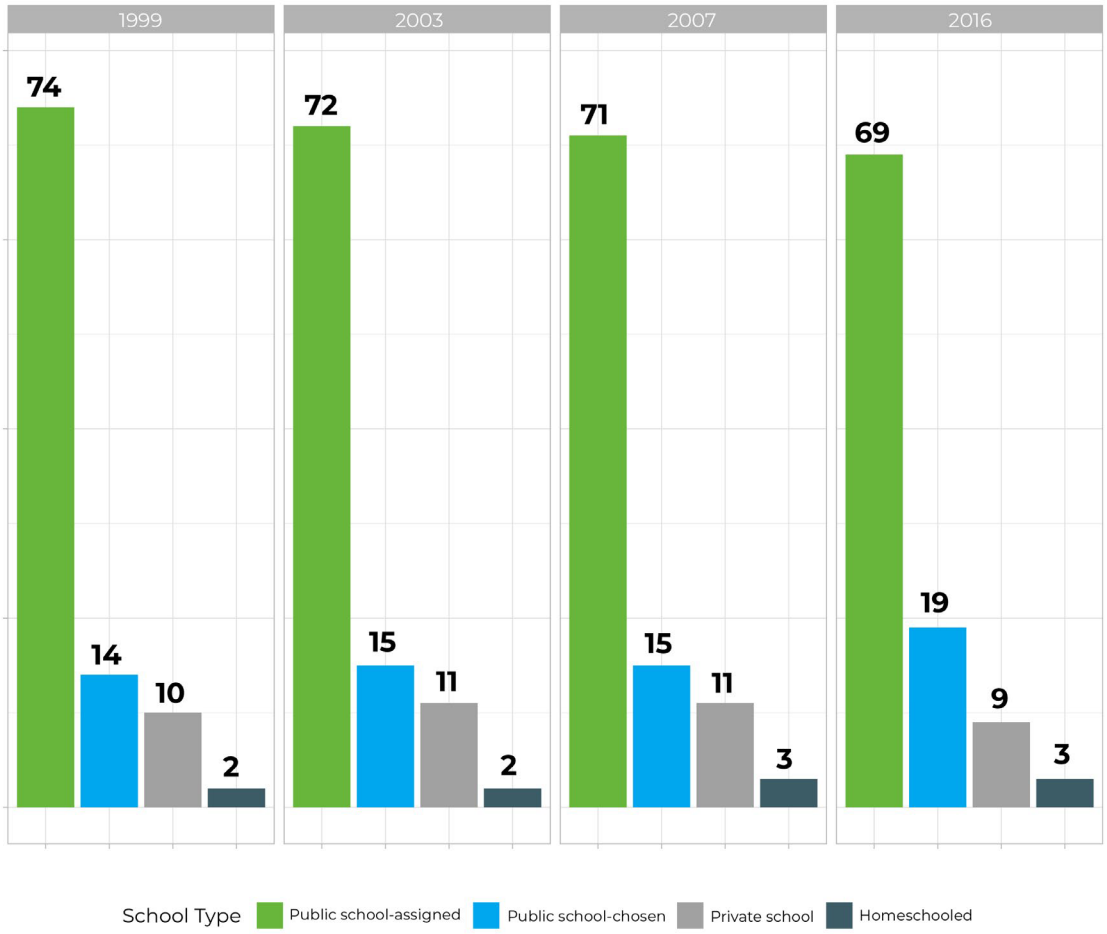
In 1983, a landmark study from President Ronald Reagan's National Commission on Excellence in Education found that America's schools were leaving "a nationat risk," with too many children left unprepared for the rigors of a competitive global economy.[21] The report helped provide an impetus for reformers interested in introducing meaningful change to American education through greater choice in schooling.

Nobel laureate Milton Friedman had laid out a theoretical case for greater latitude in school choice, arguing that in education, "as in other fields, competitive enterprise is likely to be far more efficient in meeting consumer demand."[22] This theoretical approach influenced a generation of reformers, who promised to unleash the creative destruction of market forces on a public sector accused, fairly or not, of underperforming. In 1989, Milwaukee introduced the nation's first voucher program, paying private school tuition for low-income students; two years later, Minnesota became the first state to pass a charter school law, authorizing non-traditional schools to provide education with state funding.

The No Child Left Behind era ushered in an intense (some would say myopic) focus on test scores and accountability, with the unintended consequence of marginalizing education's role of forming children into adults able to participate in a democratic society.[23] Questions about civic education and character formation required the difficult work of reaching societal consensus; an easier task was to focus on the meritocratic side of schooling, stressing economically-remunerative technical skills. Yet gaps by socioeconomic status did not close — Stanford University sociologist Sean Reardon estimated that "The achievement gap between children from high- and low-income families is roughly 30 to 40 percent larger among children born in 2001 than among those born twenty-five years earlier," while a more recent examination of the evidence posited gaps in achievement that "are very large [but] have remained essentially unchanged."[24]

A focus on choice dominated the education policy landscape for most of the 1990s and early 2000s, with an equilibrium that favored limited choice within the public school system, through open enrollment and charter schools. The fraction of public school students attending chosen public schools, rather than assigned, grew by roughly a third from 1999 to 2016 (Figure 2).[25]

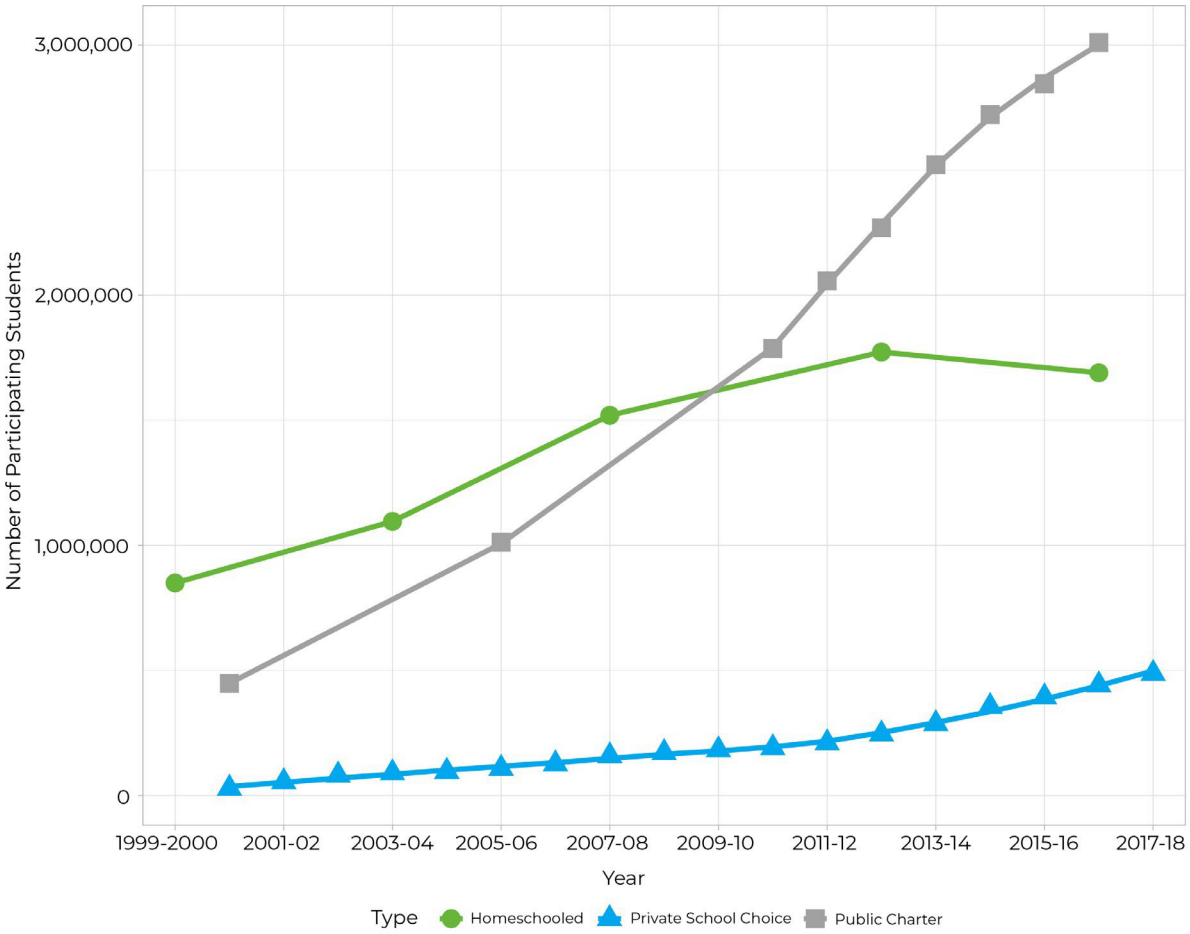
Figure 2: Percentage of Students Attending by School Type, Selected Years from 1999 to 2016




Source: School Choice in the United States: 2019 (NCES)

From 2000 to 2018, the number of students participating in a private school choice program increased 16 times over, while participation in public charter programs increased nearly seven-fold.[26] Today, 56.5 million students attend a public or private elementary or secondary school in the United States, 89 percent of whom attend an assigned or chosen public school.[27] Fully 5.5 million students attend private school, three million attend public charter schools, and just under two million are homeschooled. Half a million students now participate in a privateschool choice program.[28]

Figure 3: Students Participating in Choice Programs or Homeschooling, 1999-2018.




Source: National Center for Education Statistics; American Federation for Children.

Confidence in public education has been declining. In 1975, 62 percent of parents expressed having a "great deal" or "quite a lot" of confidence in the public schools, with only 35 percent responding "very little" or "no" confidence. By 2019, the fraction expressing quite a lot or a great deal of confidence, 29 percent of respondents, was exactly equal to those with little or none.[29] At the same time, parents tend to be satisfied with the quality of their own child's education, while being dissatisfied with the quality of K-12 education in the U.S. at large.[30]

Parents who send their child to private school tend, unsurprisingly, to be part of more-advantaged families. The proportion of private school students from two-parent households (81 percent) is far higher than those attending public school, and their parents disproportionately tend to have at least a bachelor's degree. And, as a previous Social Capital Project report has shown, there is a strong relationship between house prices and school quality, particularly in localities with rigid school or residential zoning.[31] In a recent survey, a majority of all household income groups, and all racial groups except for Asians, said that they would prefer to send their child to private, rather than public, school, if costs were the same. Parents that attend religious services more frequently were especially likely to express a preference for private over public school.[32]

## FOUR CONCEPTS FOR UNDERSTANDING PLURALISM

To many Americans, private education is a deviation from an unquestioned status quo. But compared to many other industrialized nations, the American system of predominantly state-provided education is an outlier. Berner writes:

> The Netherlands, Sweden, Denmark, the UK, Hong Kong, Israel, most of Canada's provinces, Australia, and France — to name a few — support a wide variety of schools that are pedagogically, philosophically, and religiously diverse.[33]

As Berner details, parental choice among a diversity of publicly-funded school systems is a constitutional right in Belgium and the Netherlands.[34] In Sweden, a child's per-capita share of funding can be used at a public or private school.[35] In Australia, even with its U.S.-style federalist model of education, the central government is now the primary funder of non-public schools, which offer a variety of educational philosophies.[36] Schooling in Hong Kong is funded by the government, but largely provided by non-profit organizations.[37] Many of these systems empower distinctive school cultures while also requiring rigorous assessment of academic knowledge across all schools, intentionally cultivatingthe conditions for a well-educated citizenry.

Even within the American public education system, some policymakers have recognized the limits of a one-size-fits-all approach. Miami-Dade County Public Schools, the fifth-biggest public school district in the country, has improved quality by incorporating models beyond the traditional neighborhood school.[38] The adoption of magnet schools, gifted programs, English as a Second Language classes, and other tailored approaches reflect a recognition that even within the contemporary public education system, students are better served by an individualized approach, surrounded by peers with similar goals and challenges.

John Dewey, one of the intellectual godfathers of the modern education movement, wrote that "what the best and wisest parent wants for his own child, that must the community want for all of its children."[39] Dewey's aphorism elides the fact that what is best for each child may differ from family to family and from child to child. What each community should want for all of its children is the education that is best for each individual child, respecting his or her particular strengths, needs, interests, and passions. A state-designed and -delivered educational experience can too frequently be divorced from family traditions, community bonds, and civic associations. (This monopolistic approach can, of course, also generate higher levels of community engagement in certain circumstances, as any given Friday night at a rural high school's football stadiumin autumn can demonstrate.)

A pluralist approach recognizes the importance of social capital in education, appreciates the value of authentic diversity, acknowledges the importance of meaningful civic engagement, and encourages excellence across school types and sectors. Four concepts are helpful in understanding the distinctive value of a pluralist approach to education:

- Embedding schools in a broader community of intergenerational relationships;
- Pursuing a more honest diversity;
- Ensuring a baseline commonality of values, and;
- Recognizing the importance of accountability.

## EMBEDDED SCHOOLS: THE RELATIONSHIP BETWEEN EDUCATION AND SOCIAL CAPITAL

Acknowledging the importance of civic norms and virtues means reframing education as both an input to, as well as a product of, a flourishing civil society. As we have seen, countries around the world recognize the importance of engaging religious and civic groups in building a supportive superstructure around education. In examining American education in a comparative context, Notre Dame Law School professor Richard Garnett notes,

> [O]ne sees a striking willingness to employ state power and processes in the production of civic virtues through education, rather than rely on the norm-generating capacities of families, associations, and civil society.[40]

Emphasizing social capital helps distinguish the pluralist perspective from the libertarian-infused "choice" rhetoric that often influences education reform debates in the United States. Education offers tremendous private returns to investment, but it is not a ***strictly*** private good, like a sandwich or a car. Educated, engaged graduates go on to participate in our democracy, form stable families, lead neighborhood groups, and participate in activities that provide immeasurable social benefits. In economic terms, the externalities of having active, engaged citizens provide a social return that may exceed each individual's private return to their increased human capital. This positive externality may indeed be worthy of public subsidy.

In a 1982 study, the preeminent sociologist James Coleman and his coauthors discovered the "paradoxical" finding that "Catholic schools function[ed] much closer to the American ideal of the 'common school,' educating children from different backgrounds alike, than [did] the public schools."[41] In a follow-up study six years later, Coleman attributed the success of Catholic schools to their existence as "functional communities with intergenerational closure."[42] Functional communities are ones that are necessary, that draw on the social capital among the adults in the surrounding community to "make possible the achievement of certain ends that [without them] would not be possible."[43]

In these communities, interactions among parents created norms and a structure to monitor behavior, set expectations, and built relationships across age groups and social classes. Coleman found that

> Parents knew who their children's friends were and knew their parents. The norms that pervaded the school were in part those dictated by the needs of youth themselves…but in part those established by the adult community and enforced by the intergenerational contact that this closure brought about.[44]

Coleman found that embedding youth in a context of behavioral norms and expectations led to lower dropout rates, and his work has been extended throughout the years by studies finding beneficial effects of Catholic schools on educational attainment, particularly for minority students.[45]

In some respects, new incarnations of the community-based school model,like the Harlem Children's Zone, are attempts to re-create this sense of "embeddedness" around children, particularly those at risk. Engaging the whole community increases the network of adult role models and mentors available to a child. Research from Harvard University's Opportunity Insights has found that neighborhoods with stable families and engaged communities tend to have greater economic mobility.[46]

A whole-community approach to expanding educational opportunity wouldddirectly leverage the resources of adults and elders, affording at-risk youth exposure to a wider array of potential role models and mentors. Such an approach could help to combat what Coleman identified as the "absence of intergenerational closure that prevents the human capital that exists among theadults from playing any role in the lives of the youth."[47]

Bryk, Lee and Holland's landmark 1993 book, *Catholic Schools and the Common Good*, stressed the importance of trust for the effectiveness of Catholic schools, particularly in urban settings. They underlined the importance of community and a decentralized governance structure in encouraging localized decision-making.[48] They argued that parents, as the primary educators of their children, depended on teachers' explicit

> moral obligation to do what was best to advance the education and welfare of each child. A structure of moral commitments and mutual obligations had a profound impact on teachers' work efforts and satisfaction, and strengthened students' engagement with the school.[49]

Teachers saw themselves not just as instructors, but as role models. High levelsof intra-community trust were also tied to less contentious decision-making processes and a more cohesive atmosphere around school operations. In effect, a space where normative questions could be raised allowed for greater community involvement around what those norms should be.

There may be broader spillovers from grounding schools in a broader community context as well. Notre Dame Law School's Margaret Brining and Nicole Garnett found suggestive evidence from Chicago that the presence of Catholic schools across police beats may be associated with a decrease in the crime rate, and that Catholic school closures may have triggered local increases in serious crimes. In weighing the evidence, they wrote, "We suspect that there are feedback effects between the social capital generated within a Catholic school and the level of social capital in a community surrounding it."[50]

## A RICHER DIVERSITY: MOVING BEYOND THE MYTH OF NEUTRALITY

In a society with different conceptions of the good and competing traditions and comprehensive worldviews, Berner argues, a pluralist approach to education is

> more honest than the current model, because it acknowledges that education always rests upon particular views about what education is for, who the child is, what role the teacher and school play, and how the atmosphere of the school reflects those beliefs.[51]

The basic structure of American education has remained fundamentally unchanged from its mid-19th century roots, reflecting, in part, concerns over rapid demographic change. Charles Glenn, former director of urban education and equity efforts for the Massachusetts Department of Education, notes that "absent a national church, a monarchy, [or] an external threat, there seemed little to holdthe new nation together… [the common school] would be above religious and political divisions."[52]

It is no slur against the common school reformers to say that our current regime of near-monopolistic state provision of education has not elevated debates over curriculum or school practices above religious and political divisions. These issues are understandably combustible, most famously in the 1962 *Engel v. Vitale*decision that struck down nondenominational prayer in school, as well as cases over flag salutes, religious "release time," free speech, and other ways our schoolsinculcate habits of the heart or mind.[53]

The hair-trigger combustibility of these issues illustrates the impossibility of a "value-neutral" approach to education. The aspirational rhetoric of Justice Brennan, asserting that "the public schools serve a uniquely public function: the training of American citizens in an atmosphere free of parochial, divisive, or separatist influences of any sort" may have described the America of 1963 (and even that is debatable).[54] It seems exceptionally misguided in describing classrooms in the United States in 2019.

The lack of an explicit moral framework in the classroom does not, of course, mean that there is no moral framework in the classroom. As Glenn forthrightly put it, "No aspect of schooling can be truly neutral."[55] Even in an avowedly-neutral setting, a school's ethos defaults to the comprehensive worldview favoring ends identified by administrators and codified in school mission statements and curricula.[56] Any method of understanding the world is influenced just as much by what is included on syllabi or lesson plans as what is left out.[57]

Our contemporary focus on education as primarily being about skills formation is no less a comprehensive philosophy than the more morally-influenced one it replaced. Circumscribing questions of ethics, faith, and personal values from the neutrality imposed by a state-operated public space contributes to a compartmentalization of private life in which questions about theology, philosophy, or personal morality are ruled beyond the scope of appropriate public discussion.[58]

Relying on bureaucrats and state standards to engender an academic environment that forms the full student is likely asking too much of a state apparatus. As James Hunter of the University of Virginia points out, public schools have "resolved" issues of disagreement around moral questions by largely avoiding the enduring questions of human existence ( "why should we begood?") unless they can be grounded in self-interest ("because it will lead you tobe successful").[59] Recent efforts to rechristen questions of character and morality as "socioemotional learning" (SEL) have likewise been called into question — "SELstripped of its moral and religious roots is neither possible nor desirable," writes the University of Arkansas' Jay P. Greene.[60] A 2019 poll found that 68 percent of parents indicated that classes in Bible studies should be offered or required in public schools, and 76 percent said public schools should offer or require classes incomparative religion.[61]

A pluralistic approach to education does not and should not mean exclusively focusing on religious schools. Howard Fuller, as superintendent of Milwaukee Public Schools from 1991-1995, was a leading advocate for school vouchers in the belief that parental choice in education would allow for the flourishing of a path of self-determination for the black community.[62] Instead of needing to effectively ask for special permission to exist, as under the current framework, schools representing minority traditions would be welcomed as equally-valid options in a pluralist approach.

The rise of no-excuses charter schools, schools with curricula grounded in specific cultural identities, "classical" academies that stress ancient languages and learning, and other identity-focused schools demonstrate the search for authentic diversity along many dimensions. These experiments should be encouraged, paired with a baseline expectation of civic inculcation and assessments of content-specific knowledge.

Coleman pointed out that, in a time of greater ethnic and religious homogeneity,it would be expected that the culture of the local school would be permeated by the values held by a largely white and Protestant majority. In many respects, this was an active policy choice, as in the decision to permit non-sectarian (that is, non-denominational Protestant) prayers and Bible readings in public schools. For minority groups during this period, however, Coleman noted that "the larger society was not an extension of the family for them, either religiously or culturally."[63] In an increasingly heterogeneous America, recognizing the costs imposed by a false uniformity should encourage steps to increase the ability of ethnic, cultural, and religious minorities to participate in an educational experience that respects, not obviates, meaningful differences.

## A COMMUNITY OF COMMUNITIES: ADDRESSING FEARS OF BALKANIZATION

Precisely because of America's racial, ethnic, and religious diversity, critics fear embracing pluralism will lead to self-segregating groups that isolate themselves into balkanized communities or exclude members of minority communities. Rutgers University's Benjamin Justice and the University of Victoria's Colin MacLeod have argued that American exceptionalism points us in the direction of

an educational system that is more self-consciously state-operated than other Western nations:

> A distinctly American combination of social and political factors has led to the system we currently have. Not only has there always been significant religious diversity in the United States; there has also been a strong constitutional tradition of protecting rights to religious liberty and sharply limiting state promotion of particular religious creeds.[64]

In her seminal book ***Democratic Education***, Amy Gutmann, now president of the University of Pennsylvania, argues education should operate within the electoral process, such as through traditional school board elections. Otherwise, she worries, it could be prohibitively difficult to ensure they are promoting the values the general public intends them to promote, rather than "sectarian" beliefs. "Just as we need a more democratic politics to further democratic education, so we need a more democratic education to further democratic politics," she writes, arguing that "in recognizing that children are future citizens, the democratic state resists the view...that children are creatures of their parents."[65]

Likewise, in his 2002 *Zelman* dissent, Justice John Paul Stevens worried that "[w]henever we remove a brick from the wall that was designed to separate religion and government, we increase the risk of religious strife and weaken the foundation of our democracy."[66] More dramatically, opponents of greater diversity in publicly-funded schooling have warned of government-funded extremism, with television advertisements against state ballot initiatives raising the specter of classrooms taught by skinheads, cultists, and members of the Ku Klux Klan.[67]

One objection would be that it is by no means clear the current status quo has successfully avoided balkanization and segregation. Researchers disagree over whether racial segregation in traditional public schools is increasing or stagnant, but our relatively high levels reflect an underlying intense residential segregation along race and class lines.[68] A recent Urban Institute study found charter schools may have led to a slight increase in racial segregation in certain schools, but also led to decreased segregation between districts in the same metropolitan area.[69] And claims that private and religious schools lead to higher levels of intolerance are not supported by evidence; if anything, a major study found "students in private secular and Catholic schools appear to have higher levels of tolerance than students in public schools."[70]

Constitutional minefields await as well. The bonds of civil society are, to some degree, pre-political, and education in the context of civic association or religion should be recognized as enjoying appropriate protections against undue state coercion.[71] The Supreme Court precedent of ***Meyer v. Nebraska***, which struck down a Nebraska law mandating all education be conducted in English, offers some precedent for the idea that civic unity may be a legitimate, but not overriding, interest in regulating the character and curriculum of a school.[72]

Schools, of course, would not be able to violate pupils' constitutional rights by discriminating against protected categories. For example, no private school is allowed to discriminate on the basis of race. Religious schools are currently

exempted from Title IX sex discrimination regulations only "to the extent that… [they] would be inconsistent with the religious tenets of the organization."[73] But compelling (or restricting) certain speech in the classroom as a condition of participating in a school funding program would seem to be unconstitutional.[74]

Some baseline foundation of shared civic virtues is essential. "A democratic political community can no more perpetuate itself without attending carefully to the dispositions of its citizens than a religious community that does not evangelize each new generation can hope to thrive and survive," Garnett writes.[75] But, he continues, "The question remains: does the perceived fragility of democratic values require, or even justify, restrictions on school choice or intrusive regulation of private and religious schools?"[76] More pointedly, Glenn asks, "Is our national unity really so fragile that it depends upon the indoctrination of the young?"[77]

Relying on professional bureaucrats to manage the transmission of American values suggests a lack of faith in the promise of American pluralism and a robust civil society. The vision of American associational life, of a nation comprised of strong communities, will always engender tension between local identities and national values. Pluralism requires a deeper form of tolerance than the false promise of state-imposed conformity, but also suggests a longer-lasting vision that stresses both the *pluribus* and the *unum* of our unofficial national motto.

## PURSUING EDUCATIONAL EXCELLENCE: MARRYING CHOICE WITH ACCOUNTABILITY

The understanding that education should involve whole communities suggests the related insight that education involves more than just a purely private decision. As such, using taxpayer dollars to fund poor-quality education is not only a disservice to the children receiving it, but makes our society worse off by leaving those students unprepared to fully participate in civil society upon reaching adulthood. When public dollars are involved, there is an inarguable state interest in ensuring education funds do not reward bad actors. The natural experiment in greater school choice following Hurricane Katrina succeeded, in large part, due to the city of New Orleans' willingness to shut down poor-performing charter schools — not based on educational ideology or philosophy, but on their inability to provide basic instruction to their students.[78] Ohio's charter reforms, including tougher accountability policies, seem to have reduced the number of underperforming schools in the state.[79]

Michael Petrilli, president of the Fordham Institute, an education policy think tank, acknowledges the fine line that authorizers and regulators must walk, but argues that "allowing schools to operate without regard to performance may harm students — and the charter sector as a whole."[80] A major analysis of 41 regions with charter schools found that the systems with the strongest rules around authorization and accountability tended to have the strongest academic results, while states with laxer regimes have not seen charters outperform traditional public schools.[81]

A pluralist approach also sidesteps the morass of trying to compare voucher and charter programs to traditional public schools. As international examples indicate, comparing across sectors becomes largely irrelevant in a pluralistic model; what matters is ensuring all schools, regardless of whether operated by the state or by a civic or religious entity, are providing a decent education.
Parents are then empowered to choose which school best fits their conceptionof what education is for.

One prominent school of thought holds that a functioning market for educational services will, over the long run, weed out underperforming schoolsand bad actors. A recent study argued "costly regulations tend to reduce the quantity and quality of private schools that elect to participate in school choiceprograms."[82] Yet when public dollars are involved, pluralism — recognizing that the choice is more than a private one — entails a necessary role for public accountability. If taxpayers are funding students' access to many types of school,they have a stake in ensuring that the educational experience provided there helps children grow, socially, emotionally, and academically.

Advocates also worry, fairly, that promoting "accountability" could be a covert step towards undermining pluralism by placing educational philosophies and practices under the aegis of the state. "The power to regulate cannot be a backdoor strategy for obliterating all meaningful differences between public and private schools," notes William Galston, senior fellow at the Brookings Institution and a former dean at the University of Maryland's School of Public Policy.[83]
The appropriate level of accountability will have to be found on a continuum between content-specific knowledge and regulating the means and method of instruction.

The charter system in Indiana, for example, demands accountability while permitting a selective admissions process, leading to higher school participation rates than in other states.[84] In many countries, accountability concerns are addressed by having students sit for comprehensive and content-specific exit exams at the end of high school. Berner suggests that in these countries:

> The tight coupling of content-rich curriculum and exit exams narrowsthe achievement gap...It also incentivizes students, who must take primary responsibility for their learning and results. This scenario is vastly different from the accountability standards in the United Statesthat reward or penalize teachers maximally, but students minimally.[85]

Turning a blind eye towards predatory practices or poorly-operated charter schools is not the market at work, but negligence. Petrilli has criticized those he calls "choice purists" for abstracting away from the real difficulties in designing a system that does not reward academic malpractice.[86] The goal, as Glenn puts it, should be a framework that allows for schools that have both the cohesiveness necessary to develop character and civic virtue, as well as the rudiments of instructional ability to be educationally effective.[87] Ensuring schools meet some kind of baseline performance, while allowing them to innovate on other dimensions of their instructional context and content, can achieve that goal.

## POLICY APPROACHES

Pluralism is best described as a way of thinking about education, rather than a prescriptive policy agenda. But there are steps policymakers can take towards increasing the degree of civil society's engagement in the education system. Education policy should strive for what Nicole Garnett calls a "sector agnostic" approach, where public policy offers equitable, portable funding formulae, withrules that support experimentation and appropriate accountability.[88] As Berner writes:

> "Americans in the nineteenth and early twentieth centuries lost the experience of, and therefore the capacity to imagine, the benefits of diversepublic education. This lack of imagination is still with us, and we have too readily believed that our schools are somehow ideologically neutral and democratically beneficial."[89]

The example from other industrialized nations should inspire confidence that encouraging a diversity of educational perspective and philosophies is compatible with, and indeed, helpful for, a healthy and robust democratic society.

## POLICY LEVERS TO INCREASE PLURALISTIC OPTIONS

In the United States, education has traditionally been understood as a matter of state, not federal, jurisdiction. (A 1973 Supreme Court case found that there is no federal right to an education.[90]) Most policies to move toward more diversity in education will, therefore, involve state innovation.

Pluralism-inspired reforms at the state level should broaden the definition of public education to mean "publicly-funded," not just "publicly-provided," education. Because of the strictures of school choice jurisprudence, a more pluralist approach to education will likely involve allowing families more options in choosing their educational provider, rather than explicitly asking religious or civic groups to take on responsibility for public education. This could take the form of tax credits or vouchers for parents to use toward their child's schooling. As will be covered later, a pending Supreme Court case, *Espinoza v. Montana Department of Revenue* (18-1195), may open a new realm for state experimentation with public funding ofeducation going towards non-state actors.
Policymakers can increase the degree of community embeddedness surrounding children by streamlining the charter process for community groups, including through legislation that proactively affirms the role of religious institutions in the system. In the Netherlands, for example,

> groups of parents who want their children to attend a school that has a distinctive educational philosophy have a constitutional right to have the government establish and fund such a school if one does not exist nearby or if the ones that do exist are full.[91]

Offering religious, cultural, or ethnic groups targeted assistance through the charter application or operation process, with sufficient safeguards to protect their authentic identity, could meaningfully increase the options available to parents and students.

A more individualist approach would have education funding follow the child — parents would receive the value of their children's public education dollars to use at the school of their choice. In 2011, Arizona became the first state to introduce "empowerment scholarship accounts," allowing certain categories of families to apply 90 percent of the funding they would have otherwise received to other qualified educational opportunities.[92] Eligibility for the program was limited to specific categories, including children with special needs or those with an active-duty military parent.

Another policy proposal to increase families' options would be broadening access to education savings accounts. Currently a benefit that accrues primarily to high-earning families, tax-advantaged 529 savings accounts were expanded in the 2017 Tax Cuts and Jobs Act to cover up to $10,000 in qualified expenses for K-12 education, including private school tuition.[93] 529 savings plans could be seeded at the state or federal level (Following the model of the tax credit scholarship program operated in Pennsylvania, the amount should be preferably adjusted to account for income and family size.)[94]

To maximize the options families would have in a system with more choice, states could explore property tax reform that breaks the link between residence and school quality. In Indiana, for example, property tax relief for homeowners was paired with fiscal equalization grants, which boosted state aid for poorer districts.[95] By supplanting school funding via local property taxes with state dollars, Indiana's reforms leveled the playing field between districts, easing the process for families to transfer across district lines. Districts began to compete for student transfers, and the number of transfer students rose from below 3,000 before the reform to over 11,300 following it.[96] A system in which the quality of schools is less directly tied to local property taxes could be more accommodating to a pluralist approach, by lessening some of the pressure that couples neighborhood desirability and school quality. This could also have the effect of reducing levels of socioeconomic segregation.
While the federal scope for education policy is limited, Congress could explore steps to assist state efforts. Title I of the Elementary and Secondary Education Act, which currently provides financial assistance to local education agencies and schools serving high percentages of low-income students, could be reformed to increase the availability of those funds to schools outside the traditional district model.[97]

Choice is not choice unless it is realizable, so transportation policy could promote more flexible transportation options available to families outside of the public school system. Denver Public Schools, for example, launched the Success Express shuttle bus service to increase access to both public and private schools. (Charter schools were assessed a per-pupil cost to help cover the expense of the additional service.)[98] Efforts to increase the availability of ride-sharing, carpooling, and point-to-point shuttles could increase families' options.[99]

## EMPOWERING TRULY LOCAL CONTROL

Even under a system that respects genuine pluralism, many parents will still prefer to enroll their children in traditional district schools. Even in the most pluralist examples abroad, for example, many students still attend public schools. For sparsely-populated rural school districts, expanding the availability of options facing parents may actually reduce their community's store of social capital, undermining the public school as locus of social life and source of identity. Can a pluralist approach — even in the absence of broader policy change — better engage civil society in traditional public schools as well?

Putting local control of schools into practice requires devolving more authority to the lowest appropriate level.The families of students who attend traditional public schools are too frequently treated as recipients of services, often ones dictated and mandated by federal or state bureaucrats, rather than fully-participating members of a community. Glenn, among others, laments that public schools "do not belong to the communities that they serve."[100] Parents will be most invested — and their investment will often be most effective — in an institution that invites stakeholders into decision-making, makes them feel part of a broader community, gives them channels of input into the direction and ethos of the school, and empowers them to be part of building a collective project.

Breaking up bureaucratic calcification means proactively and intentionally soliciting parent input. State boards of education could consider introducing "sunset" provisions into certain regulations, forcing their applicability and necessity to be re-examined at regular intervals. Education officials could intentionally leave room for civil society groups to be involved in curriculum decisions. They could deliberately decide not to hand down a certain policy, instead placing the onus on parent-teacher associations or parent groups toenact their own school-specific guideline.
For example, a recently-passed Florida law requires each school district to adopt a policy regarding objections to textbooks or instructional materials that parents do not believe are grade level- or age-appropriate.[101] Without mandating specific content guidelines or a rigid bureaucratic framework, the state legislature made it clear that school districts should engage with parents on appropriateness of curriculum, allowing latitude for local solutions to present themselves.

Other examples of localized policies that federal and state officials could charge local schools and parents to develop could include school start times, nutrition in lunches, discipline policies, and other practical matters of school culture. Charter school authorizers and state education regulatory bodies should also re-examine relevant regulations. A light-touch approach, focused on core competencies, allows for the greatest diversity of approaches that respect local practices and preferences while ensuring appropriate safeguards.

Throughout the education system, policymakers should focus on making it easier for schools to be truly locally controlled. The Social Capital Project has drawn on the seminal work of Alexis de Tocqueville's *Democracy in America* and his emphasis on associational life in ensuring the health of our democracy.[102] Making public

school more Tocquevillian means cultivating active, not passive, participation. Drawing on his experience in Massachusetts, Glenn comments that

> [S]urely it is wise public policy to create conditions that would permit more parents to become involved in the schools their children attend, not as passive participants in periodic open houses, but as creators, sustainers, and participants in important decisions, just as many of them are in their churches.[103]

When it comes to questions of character, democratic habits, or ethical decision-making, the best way to teach those concepts is to demonstrate them, not lecture on them. Communities that can speak openly about normative questions will have a greater ability to model them as well. Glenn notes, "the crucial policy issue in civic education is how parents and teachers can be motivated and empowered to behave in ways that serve as examples of civic virtue to the children and youth under their care."[104] A school environment enmeshed in a broader community of shared values and commitment can catalyze those conversations and provide a template for the students of today to be the community leaders of tomorrow.

## REVIVING CIVICS EDUCATION IN A DIVERSE NATION

Tying pluralism to content-based accountability may also help rescue the sorry state of civics education. There is seemingly nowhere to go but up; in 2010, only 23 percent of public school seniors scored "proficient" or above on the National Assessment of Educational Progress (NAEP) civics exam.[105]

Large majorities of Americans express support for teaching honesty, civility, respect for authority, patriotism, and acceptance of differences — one poll found 97 percent of Americans say public schools should be teaching civics.[106] But in a nation with rich diversity, finding majority support for even the barest-bones definition of civic values may be challenging. "The level of support for teaching [civic] values exceeds the number who say it would be possible to get people in their community to agree on a basic set of values that should be taught," a national poll found, notingthat 61 percent of adults agree that this kind of agreement would be possible, downfrom 69 percent in 1993.[107]

Gutmann typifies the reliance on professionalization of education, claiming that teachers' unions and educational bureaucracies can "pressure democratic communities to create the conditions under which teachers can cultivate the capacity among students for critical reflection on democratic culture."[108] But critically reflecting on a culture requires being formed in that culture to begin with. The state of American civic education raises the question of whether students truly understand the culture they are being taught to critique.

A pluralistic approach to civics education would allow localities to move beyonda lowest-common denominator approach to these questions. "Patriotism" will mean something very different in San Francisco than in San Diego, to say nothing of Salinas. Putting pluralism into practice is a more intellectually honest way to deal with differences of opinion on patriotism, activism, and other civic

values. Civic engagement will likely mean one thing at an Afrocentric school and another at a Montessori school or classical Christian academy. But if nothing else, students should graduate with a basic understanding of the nuts and bolts of our democracy. In Alberta, for example, private schools that receive provincial funding are required to ensure students meet basic civic competencies, but are allowed to have different frameworks for talking about the context in which they operate.[109]

A content-based framework of accountability, rather than a state-imposed orthodoxy, appreciates America's tradition of associational life and robust civic engagement. Requiring that students are able to graduate with specific knowledge about the form and function of our democracy, while allowing schools to present that knowledge in a culturally-appropriate and philosophically-honest manner, would allow for creative local approaches while retaining a common body of knowledge.

## SAFEGUARDING THE DISTINCT IDENTITIES OF RELIGIOUS SCHOOLS

The parent-child relationship — the foundational unit of society — has traditionally received tremendous deference in American jurisprudence. In striking down a voter-passed 1923 Oregon law that would have effectively outlawed private schools, the Court ruled that

> The fundamental theory of liberty...excludes any general power of the State to standardize its children by forcing them to accept instruction from public teachers only. The child is not the mere creature of the State; those who nurture him and direct his destiny have the right, coupled with the high duty, to recognize and prepare him for additional obligations.[110]

As has been noted, parents with means enjoy tremendous latitude to construct an education that best fits the needs, interests, and appropriate developmental context for their children. Efforts to make the same range of options available to all families, however, have been rife with legal controversy. Currently, three-quarters of private school students attend a religious school, necessitating that any discussion of diversity in education address questions of church-state separation.[111] Could a state fund religious schools as part of a pluralist approach to education without running afoul of First Amendment concerns?

For decades, educational jurisprudence has been shaped by the 1947 case of *Everson v. Board of Education*. It found that a New Jersey program that reimbursed parents' use of public transportation to bring their children to a religious school did not violate the "wall of separation between church and state" (a phrase that does not appear in the Constitution).[112] But in so doing, the majority incorporated the Establishment Clause of the First Amendment — "Congress shall make no law respecting an establishment of religion" — into state constitutions, effectively prohibiting them from providing direct aid to religious schools. Payments offered to parents, instead of religious institutions, and to all students, regardless of religious tradition, have been deemed constitutional under the framework developed under Everson and subsequent cases.[113]

The most rigorous doctrine evaluating the permissibility of aid to schools was laid out in the 1971 case of ***Lemon v. Kurtzman***, in which a three-prong test — the program must be secular in purpose, must have the effect of neither advancing nor inhibiting religion, and must not result in an "excessive government entanglement" with religion — was instituted to strike down a Pennsylvania law that reimbursed private schools for the cost of teachers' salaries.[114] Since then, the Court has shown signs of being less bound by the so-called "Lemon test." In the 2002 ***Zelman v. Simmons-Harris*** decision, the Court held that school vouchers, even when used for religious schools, did not run afoul of the Establishment clause. Public support for sectarian schools that was ***de facto***, as a result of parents' private choices in a religiously neutral program, not ***de jure***, as a result of direct appropriations, was deemed constitutional.

However, in states with bans on funding for religious schools ("Blaine amendments"), programs that provide parents with the choice to use their vouchers at religious schools are often found unconstitutional. As of this writing, "thirty-seven state constitutions contain provisions that prohibit the public funding of private 'sectarian' schools."[115] Depending on how case law has been interpreted, some states have been prohibited from creating voucher programs, while other states allow families to use aid at religious schools.[116]
***Espinoza v. Montana Department of Revenue*** (18-1195), scheduled to be heard by the Supreme Court in January 2020, could have major ramifications for the permissibility of these structures. In 2018, the Montana Supreme Court ruled that the state's Blaine amendment would render a newly-passed tax credit scholarship program unconstitutional if it did not include language barring religious schools from participation.[117] The Court's upcoming decision may provide greater clarity on the ground rules facing states wishing to explore alternatives to the state-monopoly model of education.

In other nations with pluralistic approaches to education, some non-public schools have lost their distinctiveness. In England, Berner notes, a large study of Anglican schools found they "were not particularly Anglican: very few principals could articulate what made their schools different." How did this happen? Berner suggests "It could have been a consequence of teacher preparation programs that de-emphasized philosophical differences. It could have been the pursuit of other goals, such as prestige, that urged leaders to chase trends that inadvertently subverted the school mission."[118]

While drift in mission and identity can happen organically, as a result of broader societal trends, policymakers should avoid state enticements or requirements to abandon long-held practices or beliefs as a condition of increasing public support of non-public institutions. "It is precisely the concern that school choice programs might require or induce religious schools to water down their religious character that leads many devout religious believers to oppose vouchers," Richard Garnett says. "Similarly, some have contended that vouchers should be supported precisely in order to enable increased secularizing regulation of religious schools." Citing ***Meyer v. Nebraska***, Garnett believes that appropriate policy safeguards could be conceived. "Efforts to require private and religious schools to compromise their

distinct ethos, or religious mission, as a condition of participating in an otherwise neutral school choice program would likely be unconstitutional."[119]

Indeed, some measures of pluralism may involve defensive legislation and protections. Religious schools, in particular, already face pressure to acclimate themselves to state-imposed guidelines on matters of morals and values. Already, the state of Maryland has attempted to force a Christian school out of a state-run voucher program, and make them reimburse prior tuition payments, for not abiding by sexual orientation non-discrimination language. The school has filed suit, arguing that it asks all students, not just a particular group, to refrain from sexual activity outside marriage.[120] Successful lawsuits were filed against Muslim- and Jewish-operated charter schools in Minnesota and Florida, respectively, alleging that their culturally-specific curricula contained religious overtones.[121] A commitment to pluralism in education entails a robust commitment to defending schools against encroachments on their distinctive philosophies and identities.

Battles over religious accommodation on hot-button cultural issues will be unavoidable; but so will they be under the current status quo, in forms ranging from Blaine Amendments to "Dear Colleague" letters. A more pluralistic philosophy in education policy will acknowledge the existence of difference, ratherthan trying to centralize resolutions in a top-down fashion.

## HOMESCHOOLING

There is another choice outside the traditional education system of which parents can avail themselves. The legal landscape facing homeschooling has shifted dramatically. As late as the 1980s, Vanderbilt University scholar Joseph Murphy has written, "It was only clearly legal to homeschool in a few states." By the mid-1990s, in a "nothing short of remarkable" shift, 27 states passed laws clarifying the legal status of or decriminalizing homeschooling, which now enjoyslegal status in all 50 states.[122]

Since 1999, the Department of Education recently estimated, the number of children homeschooled in the United States has doubled, rising from 1.7 percent to 3.3 percent of school-age children across the nation. These children predominantly live in middle-class families — 54 percent of homeschooling families have a household income between $20,000 and $75,000 — and often have one parent out of the labor force. (Among all households with one parent working and one parent at home, 7 percent homeschool.) The families' reasons to homeschool vary widely — a plurality of parents, 34 percent, do so due to concerns about the school environment, such as the prevalence of drugs or the threat of negative peer pressure, while others are dissatisfied with academic instruction (17 percent) or have religious reasons for homeschooling (16 percent).[123]

A pluralist approach to education policy could offer financial support for homeschooling parents, particularly since their property taxes are going to fund schools and districts their children do not utilize. Even in lieu of direct support, states could build on experimentation around homeschooling. In Utah,for example, private providers are enrolling homeschooled students as full- time virtual charter

students with specific curricula, including field trips and entrepreneurship and tech coursework.[124] Some states affirmatively protect the right of homeschooled students to access district school classes or extra-curricular activities, while others have considered such a change.[125] The state of Washington has created programs within public school districts to specifically offer enrichmentprograms for homeschooled children.[126] Legislation that would expand eligible expenses under 529 savings accounts to books and materials purchased by homeschooling parents has been introduced in the Senate, co-sponsored by Joint Economic Committee Chairman Mike Lee.[127]

## CONCLUSION

Schools today are asked to do a lot of the heavy lifting that was once done by civil society and family. Teachers are asked to be instructors, advisors, life coaches, guidance counselors, discipline enforcers, moral leaders, and therapists. They are called on to redress imbalances in youth investment, close the achievement gap, and make sure every student succeeds and no child gets left behind. Rebalancing the amount of responsibility schools have, by leveraging the resources and support of broader communities, will make it easier for teachers to teach, for students to learn, and for communities to thrive.

Respect for the ambitious promise of the common school model should not prevent us from recognizing its flaws or the ability of civil society to extend opportunity and belonging. Public education aspired to be the common ground onwhich sectarianism could be put aside to focus on values we all share. This model is increasingly breaking down, evidenced by court cases, public opinion polling, and parents frustrated at their inability to influence the content or context of their child's educational experience.

Additionally, despite decades of rising investment in public education, it is unclear that the traditional neighborhood school has succeeded as a meritocratic vehicle for increasing opportunity. Public expenditures per pupil have more than doubled since the 1960s.[128] Yet a recent working paper found that the relationship between socioeconomic status (SES) and educational achievement is as strong today as it was fifty years ago. "The long-term failure of major educational policies to alter SES gaps suggests a need to reconsider standard approaches to mitigating disparities."[129] The track record of the status quo deserves merits not deference, but critical examination.

Public opinion on proposed voucher programs suggests that increasing the availability of non-public schools may be politically popular. Surveys by EducationNext suggest support for efforts to use public funds to pay for private school tuition may have ticked up in recent years. Fully 55 percent of American adults support vouchers available to all families, whereas only 37 percent oppose such programs. If vouchers were available only to low-income families, support drops to 49 percent of adults, with 41 percent opposing. Large majorities of racial minority groups support targeted as well as universal vouchers.[130]

The rhetoric of "choice" has been injected into the bloodstream of education discussions, but individual choice is insufficient as a pathway forward. Instead, the next generation of education reform should focus on enlivening the role of authentic communities in schools, both to expand opportunity to low-income students and to invigorate the role of civil society in creating norms and a sense of belonging.

Recall Coleman's focus on the importance of communities with an intentional purpose. "To describe functional communities with intergenerational closure as a resource for parents in raising their children is more than a figure of speech," he wrote:

> The extraordinary social mobility that children from lower-class backgrounds, both rural and urban, have had in previous generations in America was accomplished by families with meager tangible resources... Where did the resources come from to develop and nurture [them]? These children were surrounded by functional communities, either in rural areas or in ethnic neighborhoods of urban areas.[131]

Having conversations around values, building up norms and behaviors, tapping into moral wisdom and intergenerational relationships, and authentically appreciating the contributions of different cultures and approaches are more easily accomplished in an educational system that prioritizes pluralism.

Civil society, as philosopher Michael Walzer has written, is a "project of projects," that needs to be granted "space [for] uncoerced human association and also [for] the set of relational networks — formed for the sake of family, faith, interest, and ideology — that fill this space."[132] Strengthening civil society sometimes means reducing state activity or thinking about it in a different way. A framework of genuine pluralism in education "reflects an understanding of civil society that views the state as the guarantor of a rich social ecology, not its chief actor," writes Berner.[133]

American public education is failing too many children, and schools alone cannotbe expected to remedy differences stemming from family, neighborhood, and social environments. The ways in which we have prioritized state-delivered education should spur reflection on the ability of civil society to offer all children broader communities of support and opportunity. Fostering authentic pluralism within our educational system will increase the ability of parents to invest in their children as students, future citizens, and full members of a broader community.

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## ENDNOTES


1. See, e.g., Greene, Jay P. 2011. *Why America Needs School Choice*. New York: Encounter Books.

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8. Glenn, Charles L. 1988. The Myth of the Common School. Amherst: University of Massachusetts Press, p. 4, inter alia.

9. Quoted in Glenn, 1988, p. 69. Emphasis in the original.

10. Grant, Ulysses S. 1875. "Speech at the Annual Reunion of the Society of the Army of Tennessee at Des Moines, Iowa." In *Words of Our Hero, Ulysses S. Grant*, Chaplin, J. [ed.] Boston: Lothrop &Co. https://archive.org/details/wordsofourheroul00gran/page/n9

11. In his majority opinion in *Mitchell v. Helms*, 530 U.S. 793 (2000), Justice Thomas wrote that in the 1870s, consideration of the Blaine Amendment, and its state-level counterparts, "arose at a time of pervasive hostility to the Catholic Church and to Catholics in general, and it was an open secret that 'sectarian' was code for 'Catholic.'"

12. United States Senate, Committee on Education and Labor. 1889. "Religion and Schools: Notes on Hearings before the Committee on Education and Labor, United States Senate, Feb. 15 and 22, 1889, on the Joint Resolution (S.R. 86) Proposing an Amendment to the Constitution of the United States Respecting Establishments of Religion and Free Public Schools." Washington: Government Printing Office. https://ia800202.us.archive.org/34/items/cu31924070708551/ cu31924070708551.pdf

13. Schultz, Jeffrey D., John G. West, and Iain S. MacLean. 1999. ***Encyclopedia of Religion in American Politics***. Phoenix, Ariz.: Oryx Press, p. 29.

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19. As will be discussed later, these cases included ***McCollum v. Board of Education***, 333 U.S. 203 (1948), which held that "release time," class periods set aside for religious instruction, was unconstitutional; ***Engel v. Vitale***, 370 U.S. 421 (1962), which ruled that prayer in public schools was unconstitutional; ***Abington School District v. Schempp***, 374 U.S. 203 (1963), which declared school-sponsored Bible readings in school to be unconstitutional; ***Lemon v. Kurtzman***, 403 U.S. 602 (1971), which found that a private school reimbursement program was unconstitutional; and ***Stone v. Graham***, 449 U.S. 39 (1980), which struck down the practice of posting the Ten Commandments in public classrooms.

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# Zoned Out:

## How School and Residential Zoning Limit Educational Opportunity

SCP REPORT NO. 6-19 | NOVEMBER 2019

The primary community a child belongs to outside of her family is her school community. Under the best circumstances the school community positively contributes to a child's socialization, academic outcomes,[1] skill development,[2] and social mobility. Schools can provide a platform for students and their families to build bonding and bridging social capital, and they act as stabilizing institutions that provide supportive social networks for families.[3]

About 90 percent of American students are educated at public schools, and 9 percent at private schools.[4] Public education has traditionally been tied directly to housing through residential assignment policies that assign homes to schools via school attendance zones. School zones are typically designed so that students attend schools near home, and despite growing opportunities to opt out or choose another school via charters, magnets, and public school open enrollment policies, 71 percent of students attend their assigned public school.[5]

Families with children predictably take housing selection seriously, as housing often determines children's access to educational opportunities. A nationally representative survey of homebuyers found half of households with children consider school district quality when selecting a neighborhood during home buying[6] and a recent study found low-income families with Section 8 housing vouchers cited "better schools" as their primary motive for moving neighborhoods.[7] However, many Americans say they are prevented from moving to a better neighborhood due to high housing costs.[8]

This paper explores the relationship between housing and public education and finds the average U.S. ZIP code associated with the highest quality (A+) public elementary school has a 4-fold ($486,104) higher median home price than the average neighborhood associated with the lowest quality (D or less) public elementary schools ($122,061).

In a cross-city comparison, major cities with more restrictive residential zoning are less effective at providing high quality public education at a low, affordable price. Portland, Oregon features traditional residential assignment policies, restrictive residential zoning, and high, climbing average home values across increasing school quality levels.

In contrast, Houston and Chicago, two major cities with less restrictive residential zoning, do a better job delivering access to high quality public schools than comparison cities with restrictive residential zoning, keeping home prices low and affordability high across school quality levels. As anticipated, cities with open enrollment or districtwide lotteries exhibit flatter relationships between home values and school quality.

Since housing is the traditional gateway to public education, this paper suggests policymakers consider improving access to educational opportunity by minimizing residential zoning while expanding public school choice policies. Reforming residential zoning supports public school choice efforts by permitting a variety of housing throughout school zones, reducing prices, and improving affordability at every school quality level.

## BACKGROUND

Housing and education policy are frequently treated separately by policy makers, although they are practically enmeshed. Part of the relationship between housing and schools exists de facto, as students will naturally attend schools that are within commuting distance of their homes and research suggests school quality is partly capitalized into home prices.[9]

However, housing's relationship to schools is also a policy choice: districts have traditionally drawn school boundaries by neighborhood and assigned students to schools by home address, even when other options are more convenient or appealing to families. Meanwhile, residential zoning regulations control the type, size, and amount of homes built in different school zones and segregate cities by income within and across metropolitan areas.[10] Research finds housing characteristics vary systematically across school zones, with larger houses and single family homes more common within high performing school boundaries,[11] and larger housing cost gaps exist across high and low quality schools in areas with more restrictive residential zoning.[12]

Education reform efforts have worked to address disparities in opportunity and untether housing from schools in a variety of ways. Charter schools, magnet schools, and districtwide lotteries decouple housing from schools within a specified area. More limited transfer opportunities including attendance waivers are available within districts or between districts in some places.[13] Educational savings accounts (ESAs) and school vouchers provide private school opportunities outside the traditional public education system.[14]

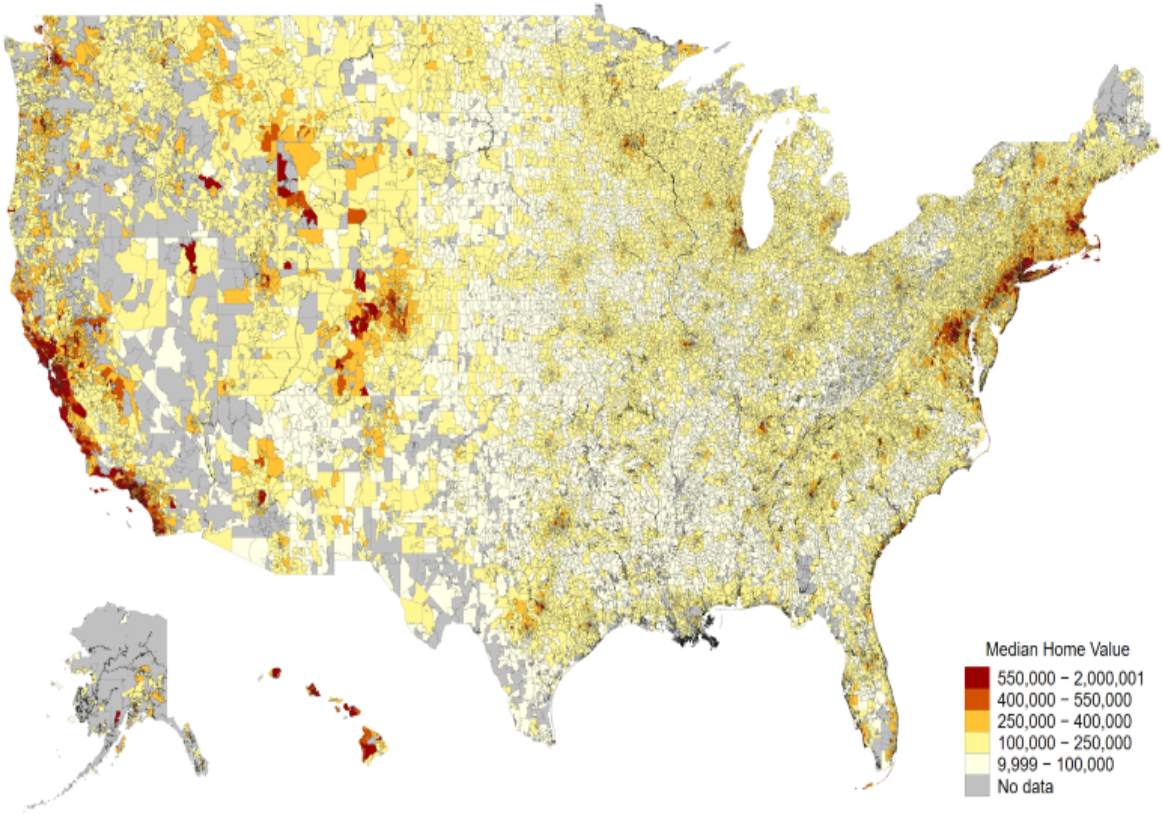
Many of these strategies reduce the link between housing and public education on the margin, but the traditional relationship persists: although 9 percent of K-12 students attend a private school, and 20 percent attend a chosen public school, 71 percent of students still attend their assigned public school.[15] Housing still effectively acts as a gateway to educational opportunity for a majority of K-12 students.

## NEW EVIDENCE ON THE RELATIONSHIP BETWEEN HOUSING AND SCHOOLS

This study relies on housing and school data compiled from a variety of public and private data sources.[16] Housing and school data are linked by ZIP code or neighborhood. ZIP codes or neighborhoods that intersect school boundaries constitute unique observations.[17] Letter grades were assigned to schools by Niche.com (an online publisher of school and residential data) and represent various dimensions of each school's quality (Appendix A).

Elementary schools tend to be associated with smaller attendance zones than middle and high schools, and public elementary schools are the sole focus of this analysis.[18] Median home values vary widely across ZIP codes in the United States (Figure 1) and the average ZIP code associated with a high quality public school has a significantly higher median home value than the average ZIP code associatedwith a low quality public school (Figure 2 and Table 1), even when regional differences are accounted for.[19]

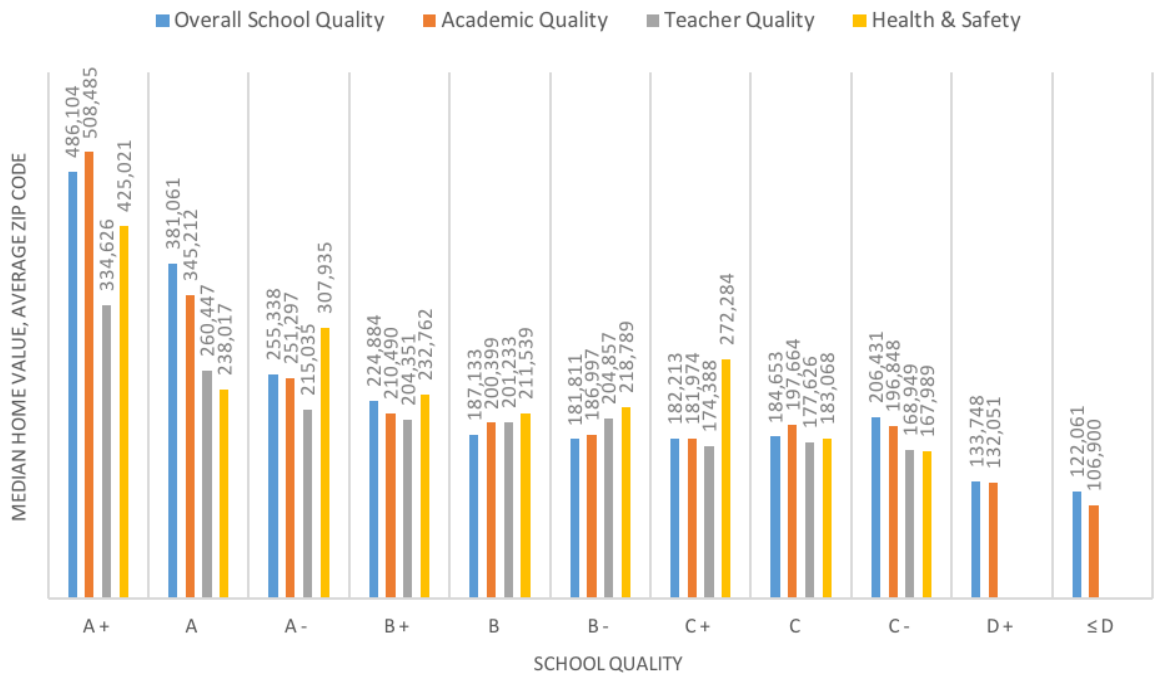
Figure 1. Median home value by ZIP code / ZIP code data coverage




Note: Colored ZIP codes contain one or more ZIP code-school observations and grayed ZIP codes represent areas without ZIP code-school observations.
Data Source: Niche, "K-12 and Place to Live Data." Licensed exclusively for the Joint Economic Committee. 2019.

For example, the average ZIP code associated with an A+ public elementary school has a median home value of $486,104, which is roughly four times higher than a D or lower public elementary school ($122,061).[20] This relationship between home values and school quality suggests many American households would find B+ or higher quality public schools out of reach; the median home value in the United States is $200,000.[21] Median home values follow a similar pattern across continuous measures of overall school quality (Appendix C).[22]

Figure 2: School quality varies by home value across U.S. public elementary schools




Note: Home values represent the mean ZIP code within a school-quality category. Note that certain districts with open enrollment policies contain non-binding school attendance zones and these relationships are reflected in this figure andthroughout the paper, except in Appendix H. School grade assignment by Niche.com is intended to follow a roughly bell-shaped distribution and the number of zip-school observations in each school-grade category varies by quality measure,see Appendix B for details. Median home values are based on 2017 American Community Survey (ACS) estimates.

Data Source: Niche, "K-12 and Place to Live Data." Licensed exclusively for the Joint Economic Committee. 2019.

Table 1. School quality varies by home value across U.S. public elementary schools

| | Overall School Quality | Academic Quality | Teacher Quality | Health & Safety |
|---|---|---|---|---|
| A+ | 486,104 | 508,485 | 334,626 | 425,021 |
| A | 381,061 | 345,212 | 260,447 | 238,017 |
| A- | 255,338 | 251,297 | 215,035 | 307,935 |
| B+ | 224,884 | 210,490 | 204,351 | 232,762 |
| B | 187,133 | 200,399 | 201,233 | 211,539 |
| B- | 181,811 | 186,997 | 204,857 | 218,789 |
| C+ | 182,213 | 181,974 | 174,388 | 272,284 |
| C | 184,653 | 197,664 | 177,626 | 183,068 |
| C- | 206,431 | 196,848 | 168,949 | 167,989 |
| D+ | 133,748 | 132,051 | | |
| ≤D | 122,061 | 106,900 | | |

Data Source: Niche, "K-12 and Place to Live Data." Licensed exclusively for the Joint Economic Committee. 2019.

The relationship between median home value and academic and teacher quality follows roughly the same pattern. The average ZIP code's median home value is $106,900 for schools at the lowest academic quality level, and $508,485 for schools at the highest.

Median home value doubles across teacher quality. The average ZIP code associated with C- teacher quality has a median home value of $168,949, while an average ZIP code associated with a school with A+ teacher quality has a median home value of $334,626.[23]

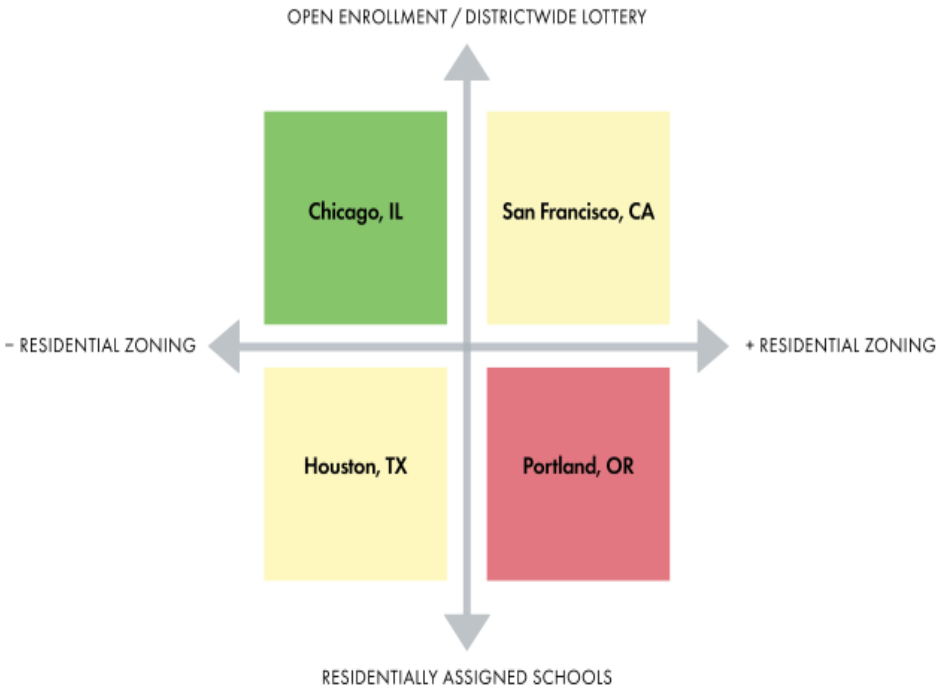
Finally, median home value is flatter across health and safety ratings but with more disparity between the tails. The average ZIP code intersecting a school with the lowest health and safety rating has a median home value of $167,989, while an average ZIP code intersecting a school with an A+ health and safety has a median home value of $425,021.

## CITY CASE STUDIES

The trend in home values across school quality levels may simply reflect individual choices about where to live, how households value educational amenities, or what type of households' children excel at school. However, past and present

school zoning and comprehensive residential zoning suggests it isunlikely the relationship between homes and schools reflects a natural productof free choice. To test the idea that public policy affects the relationship between home values and school quality, the following case studies exploit differences between cities that vary substantially across two policy dimensions (Figure 3). Cities vary from restrictively zoned to minimally regulated and from traditional residential assignment to districtwide lottery assignment (Appendices D and E).[24]

Figure 3. Two dimensions of public school access

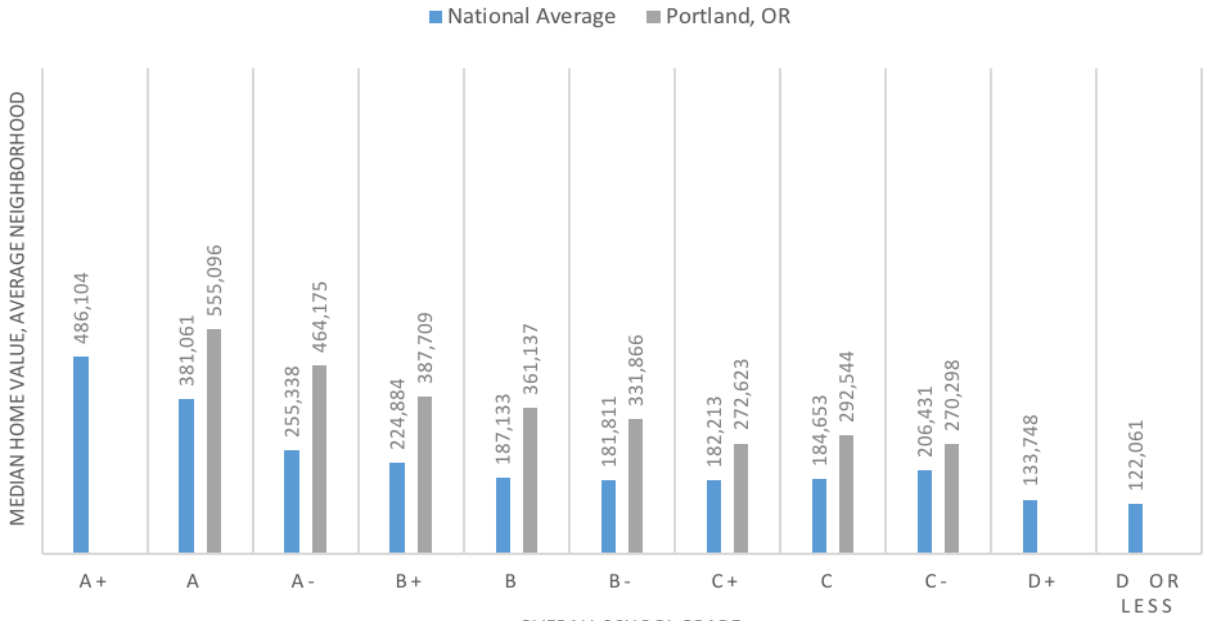



## PORTLAND, OREGON: RESIDENTIAL SCHOOL ASSIGNMENT WITH RESTRICTIVE ZONING

Portland, Oregon pairs traditional school assignment policies and limited transfer opportunities with restrictive residential zoning.[25] Over three quarters (77 percent) of residential land is zoned for detached single-family homes in Portland and Portland's urban growth boundary also artificially limits available land.[26] Meanwhile, Portland's population grew almost 12 percent between 2010 and 2018, increasing demand for housing over time.[27]

Portland should theoretically exhibit greater housing price disparities across low and high quality schools and fare poorly at providing high quality schools at low or affordable prices. In fact, Portland home prices are significantly above national averages at every school quality level (Figure 4), and the average neighborhood median home value associated with an A quality school is $555,096.

Figure 4. Portland home values are high and increase across school quality levels




Notes: Averages are for neighborhoods within Portland and ZIP codes nationally. Public elementary schools only.
*Data Source*: Niche, "K-12 and Place to Live Data." Licensed exclusively for the Joint Economic Committee. 2019.

Portland features increasing average home values across increasing school quality levels, with around $285,000 difference between home values associated with its highest and lowest quality schools. For policymakers that care about access to high-quality education, Portland arguably represents the worst of both worlds: restrictive zoning which segregates housing by income and pushes home prices up at every quality level plus residentially assigned public schools that partition neighborhoodsinto school zones less-accessible to families at different income levels.

This policy pairing likely drives inter-district segregation as well, as would-be residents are excluded or deterred from moving to Portland based on high home values associated with even Portland's low quality public schools.[28] Portland's recently slowing population and job growth may marginally ease price pressuresin the future but do not constitute a solution to the problem.

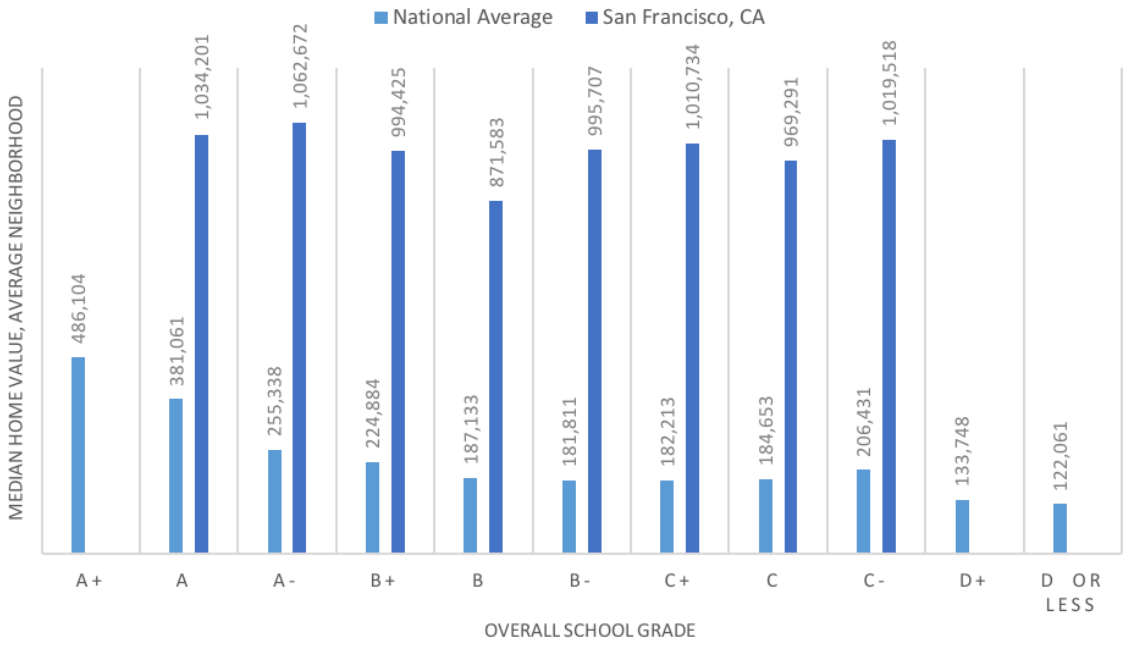
## SAN FRANCISCO, CALIFORNIA: DISTRICTWIDE LOTTERY WITH RESTRICTIVE ZONING

San Francisco has a districtwide lottery system that assigns students to schools using an open enrollment application that uses "tiebreakers" to place students at schools when schools are over capacity. It pairs this policy with highly restrictive residential zoning, and strong and growing demand for housing.

Restrictive zoning creates artificial scarcity which creates upward pressure on home prices at every quality level; estimates from past research suggest residential zoning increases the cost of housing by 53 percent in San Francisco.[29]

San Francisco exhibits a flatter relationship between housing and school quality (Figure 5) and effectively charges one average home price across all quality levels.[30] However, the price is so high that public education opportunities are inaccessible to many existing and would-be residents.

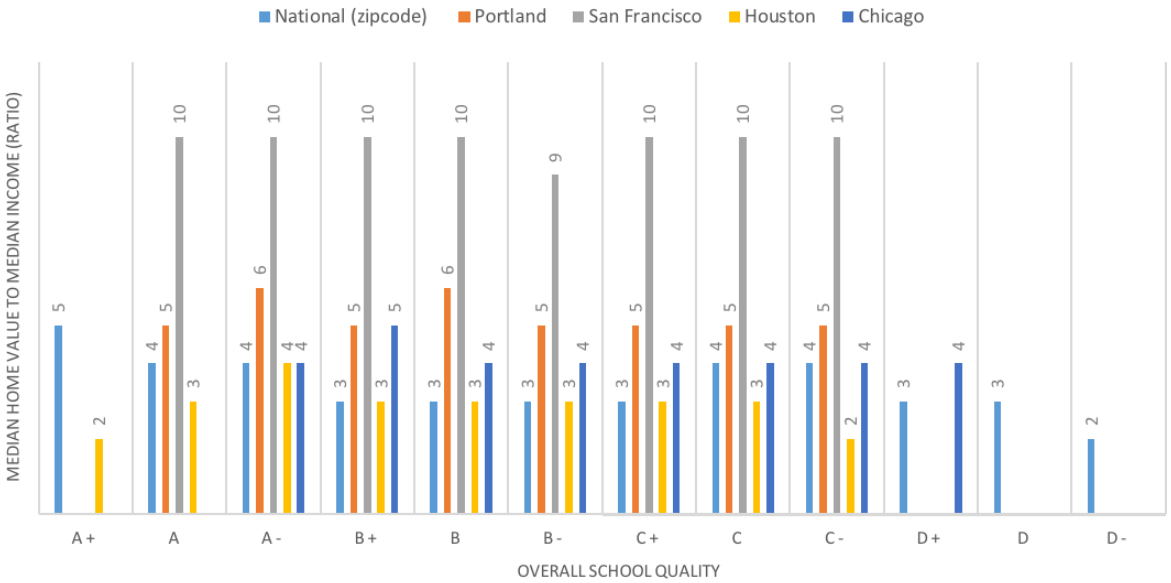
Figure 5. San Francisco home values are high and relatively flat across school quality levels




Note: In this figure San Francisco's neighborhood-school relationships are based on the city's school attendance areas.However, as a consequence of San Francisco's districtwide lottery, these attendance zones are non-binding and the functional relationship between schools and neighborhoods in San Francisco may be more accurately represented by Appendix H, Figure 1.
*Averages are for neighborhoods within San Francisco and ZIP codes nationally. Public elementary schools only.*
*Data Source*: Niche, "K-12 and Place to Live Data." Licensed exclusively for the Joint Economic Committee. 2019.

San Francisco's districtwide lottery would likely be more effective at improving access if city residential zoning policies supported housing affordability, but the average neighborhood's median home value in San Francisco is approximately $1 million at every school quality level. The home-value-to-income ratio is much higher in San Francisco at every school quality level than nationally or within any comparison city (Figure 6), which likely makes living in San Francisco unappealing to families. Prices are so high that research suggests minorities and low-income residents have led out-migration from San Francisco, and families with children have led out-migration from the state generally.[31]

Figure 6. Housing affordability varies by city and school quality




Note: Ratios are for neighborhoods within each city and ZIP codes nationally. Ratios are rounded to the nearest whole number.Data Source: Niche, "K-12 and Place to Live Data." Licensed exclusively for the Joint Economic Committee. 2019.

San Francisco is wavering on its commitment to a districtwide lottery, and the district is poised to adopt a new enrollment system likely to include stronger elements of residential assignment in coming years.[32] Criticisms of the current districtwide lottery include that the lottery is creating more demographically patterned enrollment due to information and transportation limitations, despite efforts to address these issues by non-profits and through city bus routes.[33]

Even in cities with a wide degree of public school choice, students face barriers in exercising it due to practical considerations like commute time, transportation costs, and social challenges associated with attending a school outside of their neighborhood.

Transportation demands unique to public school choice have strained school budgets in some places. For example, in recent years Boston Public Schools spent a substantial portion of the district's budget on transportation. Costs are high partly because a lottery system necessitates moving children to schools across the city in an inefficient fashion. In Boston, older children receive a public transportation pass, but children up to sixth grade use yellow buses which cost the district up to $10,000 to $20,000 per student per year.

Moreover, administrators have observed that low-income, late-comer, and immigrant families are less likely than other students to effectively access public school choice options, and are more likely to attend their local neighborhood school irrespective of quality.34 Reforming residential zoning policies could theoretically mitigate some of the challenges associated with open enrollment in San Francisco and Boston by allowing families to not only choose their school,but choose to live closer to their school.

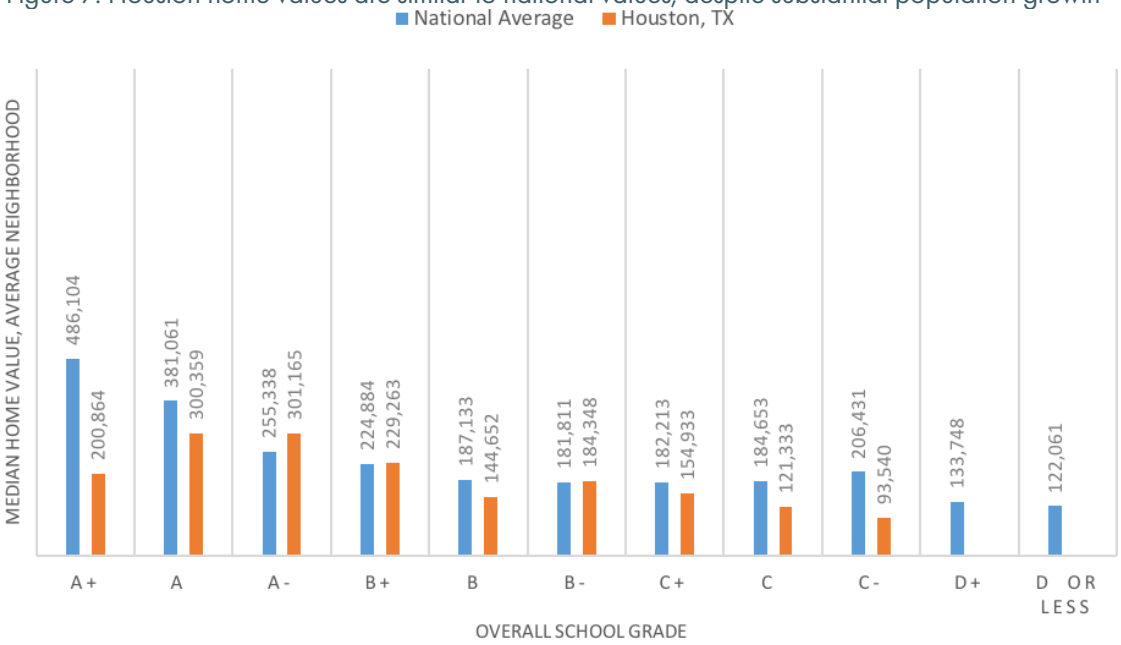
## HOUSTON, TEXAS: RESIDENTIAL SCHOOL ASSIGNMENT WITH LIBERAL RESIDENTIAL ZONING

Texas is a lightly zoned state, ranked 49th-most-restrictive,[35] and Houston is theonly major city without a traditional zoning code. Houston is not regulation-free, and does have minimum lot size regulations, front setbacks, street design regulations, and parking requirements.[36] Still, zoning was previously estimatedto account for 0 percent of the cost of housing in Houston as a result of its lax regulatory environment, and this makes the city unique in this cross-city comparison.[37]

Like Portland, schools are traditionally assigned in Houston and limited transfer options are available. Houston also has some charter and magnet schools which provide a lesser degree of public school choice not captured in this analysis.

The Houston metro area has seen remarkable in-migration in recent years, adding more people between 2010 and 2018 than all other metro areas in the US except Dallas.[38] In spite of increasing demand, the city has successfully kepthome prices low both generally and across its highest school quality levels (Figure 7).

Figure 7. Houston home values are similar to national values, despite substantial population growth

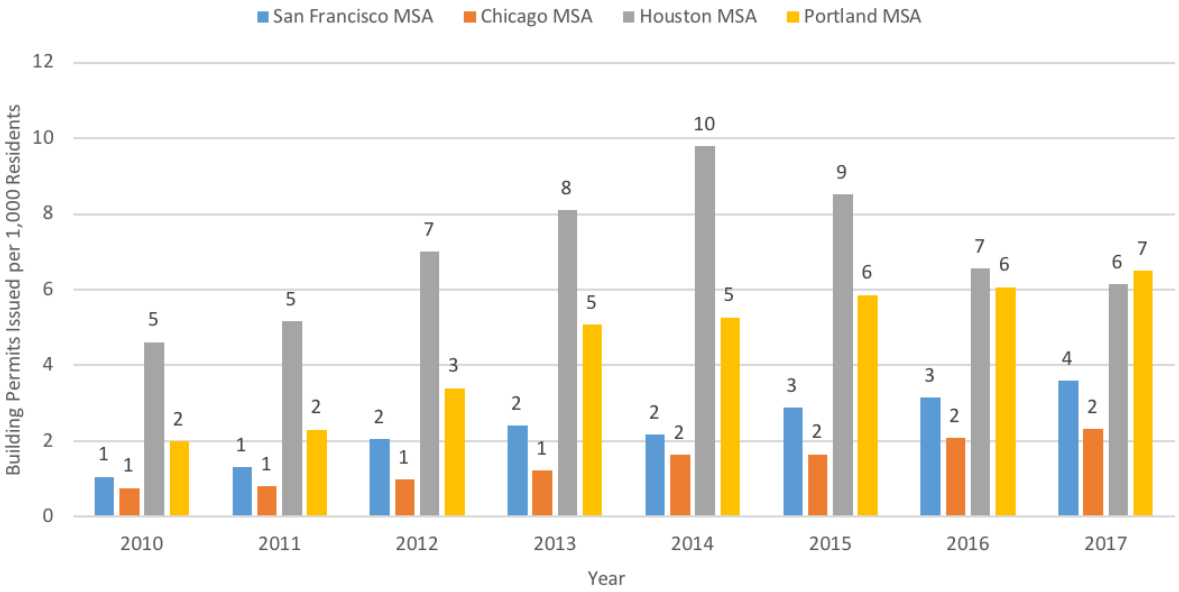



Note: Averages are for neighborhoods within Houston and ZIP codes nationally. Public elementary schools only. There isonly one A+ observation. The combined, weighted average of observations in A and A+ categories is $298,515.
Data Source: Niche, "K-12 and Place to Live Data." Licensed exclusively for the Joint Economic Committee. 2019.

In Houston, the average neighborhood associated with an A quality school has a median home value of $300,359, around $81,000 less than the national average at that school quality level. At every school quality level, Houston has lower home prices than the other major cities in the analysis, except that Chicago's median home value at the A- level is $8,000 less.

Houston's success likely hinges on its elastic housing supply which translates to more homes being permitted in the Houston metropolitan area on an annual basis (Figure 8). Economic theory predicts that inelastic supply in the face of growing demand will cause price escalations, and the housing and zoning literature supports this idea.

Figure 8. Houston MSA issues more building permits annually per capita




Note: Hurricane Harvey caused catastrophic damage to the Houston MSA in 2017, likely resulting in fewer housing starts in the Houston MSA the same year.
Data Source(s): ***Building Permits, Annual New Privately Owned Housing Units Authorized in Permit-Issuing Places.2019. Distributed by Haver Analytics, Inc.***
Metropolitan and Micropolitan Statistical Area Totals Dataset: Population and Estimated Components of Change: April 1, 2010 to July 1, 2018. 2019. Distributed by U.S. Census Bureau. https://www2.census.gov/programs-surveys/ popest/datasets/2010-2018/metro/totals/cbsa-est2018-alldata.csv

Houston also likely benefits from the unusual land use pattern resulting from its lack of traditional Euclidean zoning, which separates development by type or use. Unlike most cities, Houston's organic land use pattern intersperses multi-family housing throughout school zones in the Houston metro area.[39]

Despite huge immigration inflows over previous decades, Houston is arguably more inclusive and accessible at most school quality levels than San Francisco, Portland, and even Chicago. Houston provides access to highly rated public schools for a much wider range of economic backgrounds, in spite of its choice-limiting residential assignment policies.

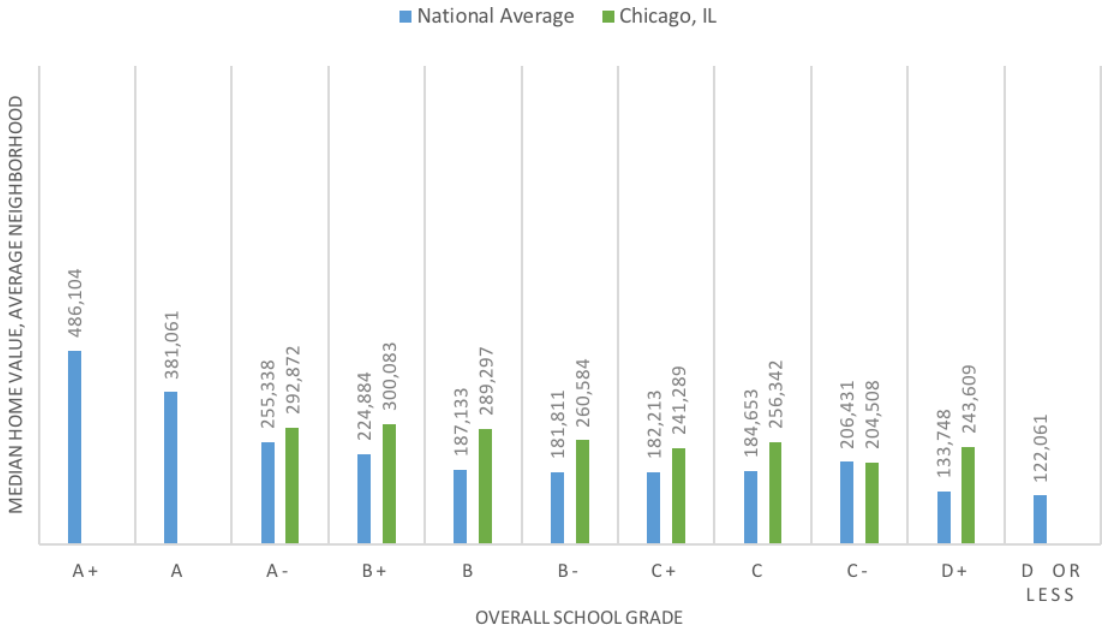
## CHICAGO, ILLINOIS: OPEN ENROLLMENT WITH MODERATE ZONING

Chicago pairs inclusive open enrollment policies which allow students to applyto non-neighborhood schools through a computerized lottery[40] with moderate residential zoning supported by historically pro-growth leadership.[41] Chicago's zoning tax, or the gap between the marginal cost of new construction and

the market price of an apartment, was previously estimated at 5.7 percent. For comparison, Chicago's zoning tax is around one-tenth of the zoning tax in San Francisco.[42]

This policy pairing seems to improve access across school quality compared to other cities. For example, the relationship between housing prices and school quality in Chicago is flatter than nationally or in comparison cities with traditional residential assignment policies.[43] Perhaps the premium to home ownership in neighborhoods with better schools is smaller when all residents have access to all schools, or residential sorting is less likely to take place along school boundaries under open enrollment as a result of school boundaries' reduced significance.

Figure 9. Chicago home values are moderate and mostly flat across school quality




Notes: In this figure Chicago's neighborhood-school relationships are based on the city's school attendance zones. However, as a consequence of Chicago's open enrollment policy, these attendance zones are non-binding and the functional relationship between schools and neighborhoods in Chicago may be more accurately represented by Appendix H, Figure 2.
*Averages are for neighborhoods within Chicago and ZIP codes nationally. Public elementary schools only.*
Data Source: Niche, "K-12 and Place to Live Data." Licensed exclusively for the Joint Economic Committee. 2019.

Chicago's moderate residential zoning likely helps contain prices overall. The average neighborhood associated with an A- quality school has a median home value of $292,872, substantially less than Portland or San Francisco and around $8,000 less than Houston.

Although some of Chicago's affordability across quality levels is due to good policy, some is likely due to poor fiscal health and population outflows. For example, Chicago's pension system is largely thought to be unsustainable and property taxes are growing to support public obligations. Current and future taxesare likely priced into home values, suppressing home values in Chicago overall.[44]

Chicago's affordability is also arguably less impressive than Houston's because Houston has experienced significant and sustained population increases while Chicago has experienced a population decline in recent years.[45] The city is also less successful in allowing a diversity of housing options across geography than Houston, which may practically reduce access to high performing schools.[46]

However, the city is still a seller's market and Chicago's general pro-growth outlook has arguably kept prices in check historically, and continues to temper home prices today.[47] As a result, Chicago's open enrollment and moderate zoning policies provide a useful model for cities that want to increase access and inclusivity.

## POLICY IMPLICATIONS

Despite public education's promise of being a free, inclusive, and equalizing force, families are faced with the reality that attending a high-performing public school often requires paying more for housing, and many students' educational opportunities are limited as a result. School zoning and residential zoning regulation directly impact the type and price of homes associated with schools, and as a result can positively or negatively impact access to opportunity.

Education policy often highlights the relationship between school zoning and access to opportunity. In this study, residential assignment policies are associated with climbing home values across increasing school quality in Portland and Houston, and open enrollment policies are associated with flatter relationships between home value and school quality in Chicago and San Francisco.

Although open enrollment policies have often been favored by policymakers interested in expanding opportunity, San Francisco's districtwide lottery experience provides a cautionary tale that open enrollment policies are not a panacea. While public school choice is helpful in creating new educational opportunities for students, students are likely to attend schools that are close to home, particularly when they are young, and are unable to attend schools in a district where home prices are too high.[48]

Residential zoning reform could be a powerful tool to make high quality schools and districts more accessible. In this study, cities with less restrictive residential zoning exhibit lower home prices and improved affordability at nearly every school quality level.

Previous research finds that cities with less restrictive zoning produce more varied and affordable housing than restrictively zoned cities. Local reforms including eliminating single family-only zoning, increasing height limits, and reducing minimum lot sizes could increase housing diversity and reduce homeprices in districts, whether or not residential assignment policies are in place. Momentum for residential zoning reform is growing, with places including Minneapolis, Minnesota, Salt Lake City, Utah, and Oregon passing related

legislation this past year. Whether these reforms will be effective rests partly on government's ability to meaningfully change the process and incentives that generated restrictive regulation to begin with.[49]

Increasing states' roles is likely necessary to produce effective reform. States should revisit their State Zoning Enabling Acts (SZEA), which provide local municipalities with nearly unlimited latitude in producing residential zoning regulation. At the federal level, attaching zoning liberalization requirements to housing, transportation, or educational grant money may send an important message to jurisdictions.

Whatever methods are used, this paper suggests that the merits of zoning liberalization may extend well beyond affordability. Paired with comprehensive open enrollment policies, residential zoning reform may improve educational access and opportunities for students within and between school districts. These changes would build and strengthen communities as greater numbers of families and students are able to participate in the school community they desire and access educational opportunities necessary to succeed long-term.

## APPENDIX A. FACTORS CONSIDERED IN NICHE.COM SCHOOL GRADING

Table 1. Overall Quality Grade

| Factor | Description | Source | Weight |
|---|---|---|---|
| Academics Grade (See below) | Based on state assessment proficiency, SAT/ACT scores, and survey responses on academics from students and parents. | Multiple Sources | 50.0% |
| Teacher Quality Grade (See below) | Based on teacher salary, teacher absenteeism, state test results, and survey responses on teachers from students and parents. | Multiple Sources | 15.0% |
| Culture & Diversity Grade | Based on racial and economic diversity and survey responses on school culture and diversity from students and parents. | Multiple Sources | 10.0% |
| Parent/Student Surveys on Overall Experience | Niche survey responses scored on a 1-5 scale regarding the overall experience of students and parents in the district. | Self-reported by Niche users | 10.0% |
| Health & Safety Grade (See below) | Based on chronic student absenteeism, suspensions/expulsions, and survey responses on the school environment from students and parents. | Multiple Sources | 5.0% |
| Resources & Facilities Grade | Based on expenses per student, staffing, and survey responses on facilities from students and parents. | Multiple Sources | 5.0% |
| Clubs & Activities Grade | Based on expenses per student and survey responses on clubs and activities from students and parents. | Multiple Sources | 2.5% |
| Sports Grade | Based on the number of sports, participation, and survey responses on athletics and athletic facilities from students and parents. | Multiple Sources | 2.5% |

Table 2. Academics Grade

| Factor | Description | Source | Weight |
|---|---|---|---|
| State Assessment Proficiency | Percentage of students at or above proficiency levels on state assessments. For comparison across states, percentiles within each state were calculated, then compared. | U.S. Department of Education | 30.0% |
| Composite SAT/ACT Score | Average SAT/ACT composite score (normalized to the same scale), as reported by Niche users from this district. | Self-reported by Niche users | 15.0% |
| Top Colleges Score | Average score of colleges that students are most interested in or go on to attend, based on Niche Best Colleges ranking. | Self-reported by Niche users | 15.0% |
| Graduation Rate | Percentage of 12th grade students who graduate. | U.S. Department of Education | 10.0% |
| Parent/Student Surveys on Academics | Niche survey responses scored on a 1-5 scale regarding the academics in the district. | Self-reported by Niche users | 10.0% |
| Student-Teacher Ratio | Ratio of students to full-time teachers. Please note: Student-teacher ratio is not a representation of average class size. | National Center for Education Statistics | 10.0% |
| AP Enrollment | Percentage of students enrolled in at least one AP course. | Civil Rights Data Collection | 5.0% |
| AP Test Pass Rate | Percentage of AP students who pass at least one AP exam. | Civil Rights Data Collection | 5.0% |

Table 3. Teacher Quality Grade

| Factor | Description | Source | Weight |
|---|---|---|---|
| Academics Grade (See above) | Based on state assessment proficiency, SAT/ACT scores, and survey responses on academics from students and parents. | Multiple Sources | 30.0% |
| Parent/Student Surveys on Teachers | Niche survey responses scored on a 1-5 scale regarding teachers in the district. | Self-reported by Niche users | 25.0% |
| Teacher Absenteeism | Percentage of teachers missing 10 or more days for sick or personal leave per school year. | Civil Rights Data Collection | 15.0% |
| Teacher Salary Index | Average teacher salary normalized by Median Household Income by county. | U.S. Department of Education | 10.0% |
| Teachers in First/Second Year | Percentage of teachers in their first or second year of teaching. | Civil Rights Data Collection | 10.0% |
| Average Teacher Salary | Average teacher salary in the district. | National Center for Education Statistics | 5.0% |
| Student-Teacher Ratio | Ratio of students to full-time teachers. Please note: Student-teacher ratio is not a representation of average class size. | National Center for Education Statistics | 5.0% |

Table 4. Health and Safety Grade

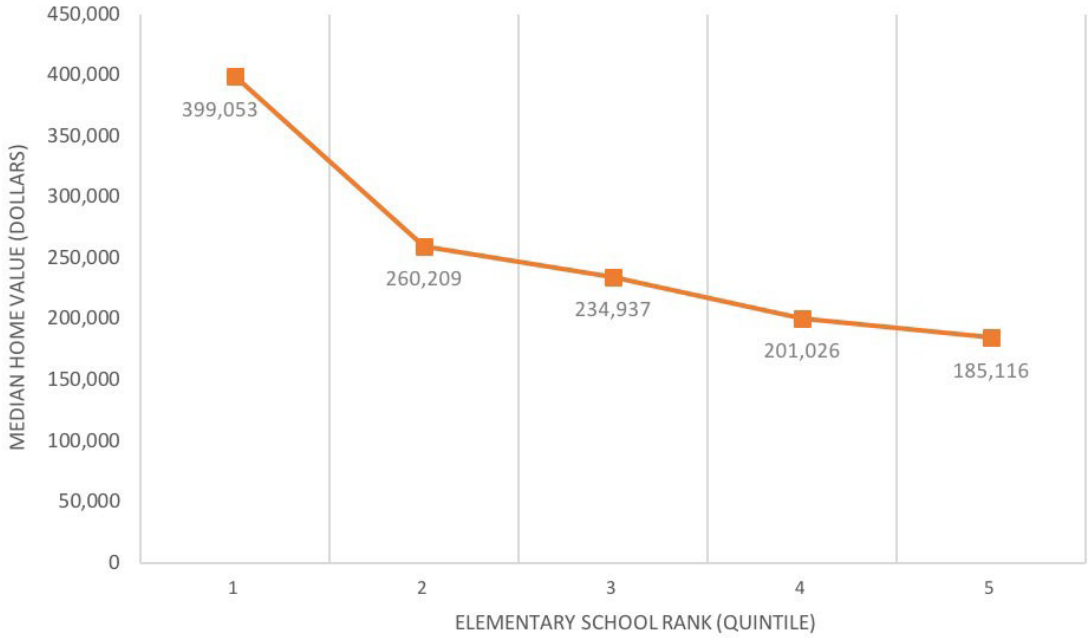
| Factor | Description | Source | Weight |
|---|---|---|---|
| Parent/Student Surveys on Health & Safety | Niche survey responses scored on a 1-5 scale regarding safety in the district. | Self-reported by Niche users | 50.0% |
| Expenses per Student | Total expenses divided by the total number of students. | National Center for Education Statistics | 10.0% |
| Student Absenteeism | Percentage of students missing 15 or more days per school year. | Civil Rights Data Collection | 10.0% |
| In-School Suspensions | Percentage of students receiving at least one in-school suspension. | Civil Rights Data Collection | 7.5% |
| Out-of-School Suspensions | Percentage of students receiving at least one out-of-school suspension. | Civil Rights Data Collection | 7.5% |
| Expulsions | Percentage of students expelled from the district. | Civil Rights Data Collection | 5.0% |
| Law Enforcement Referrals | Percentage of students referred to law enforcement. | Civil Rights Data Collection | 5.0% |
| School-Related Arrests | Percentage of students arrested for a school-related incident. | Civil Rights Data Collection | 5.0% |

Note: for more information on letter grade assignment and methodology see: https://www.niche.com/about/methodology/best-school-districts/

## APPENDIX B. PERCENT OF ZIP CODE-SCHOOL OBSERVATIONS BY QUALITY LEVEL, U.S. PUBLIC ELEMENTARY SCHOOLS

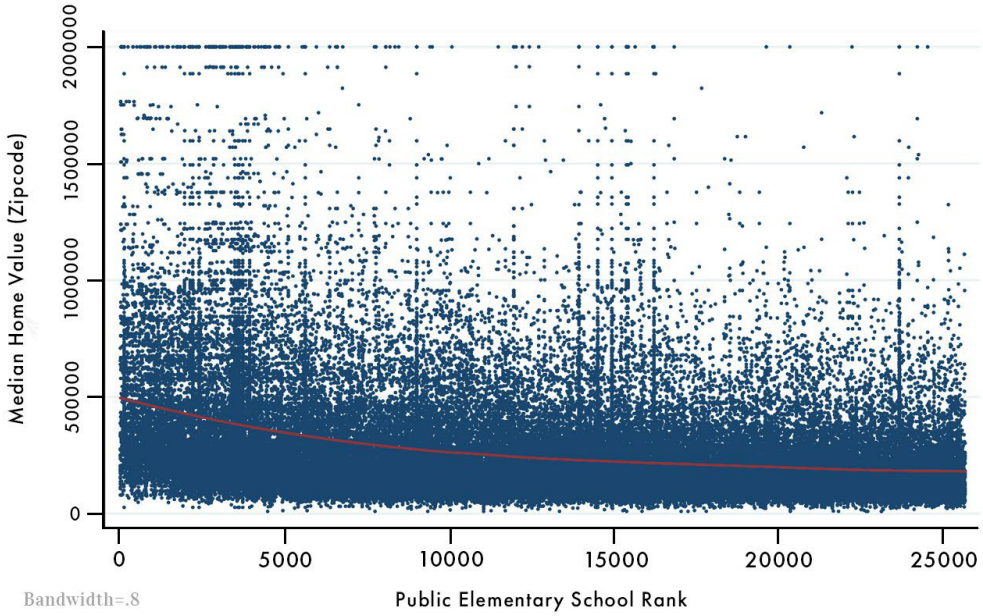
| | Overall | Academic | Teacher | Health & Safety |
|---|---|---|---|---|
| A+ | 1.4 | 0.8 | 8.2 | 5.3 |
| A | 8.4 | 10.7 | 17.3 | 36.5 |
| A- | 10.8 | 12.1 | 16.7 | 28.3 |
| B+ | 13.0 | 12.2 | 15.2 | 13.8 |
| B | 16.4 | 14.4 | 15.1 | 5.8 |
| B- | 15.7 | 14.3 | 11.9 | 5.9 |
| C+ | 12.8 | 11.8 | 7.1 | 2.4 |
| C | 10.0 | 11.6 | 4.7 | 1.0 |
| C- | 9.2 | 11.8 | 3.8 | 0.9 |
| D+ | 1.9 | 0.2 | - | - |
| D or less | 0.3 | - | 0.3 | - |
| Total | 100.0 | 100.0 | 100.0 | 100.0 |

## APPENDIX C. FIGURE 1. MEDIAN HOME VALUE VARIES BY PUBLIC SCHOOL RANK




Note: Home values represent the mean ZIP code within a school-quality quintile. Note that certain districts with open enrollment policies contain non-binding school attendance areas and these relationships are reflected in this figure and others in the paper. Factors considered in Niche.com school ranking are described in Appendix A. Median home values are based on 2017 American Community Survey (ACS) estimates.

## APPENDIX C. FIGURE 2. MEDIAN HOME VALUE VARIES NON-LINEARLY WITH SCHOOL RANK




Note: This figure was generated using lowess smoother, a locally weighted regression of median home value on public elementary school rank. Each data point represents a zip-school observation, with Y axis values indicating the median home value for a zip codeassociated with a school with X axis value rank.

## APPENDIX D. SELECTED CITIES' MEASURES OF ZONING REGULATION

| | Zoning Tax[2] (Glaeser) | Metro Rank (of 47, Gyuorko) | State Rank, Land Use (of 50, Calder) | State Rank, Zoning (of 50, Calder) |
|---|---|---|---|---|
| Portland, OR | N/A | 24[1] | 7 | 15 |
| San Francisco, CA | 53.1% | 6 | 22 | 38 |
| Houston, TX | 0% | 38 | 49 | 49 |
| Chicago, IL | 5.7% | 29 | 48 | 46 |

[1] The metropolitan area is Portland-Vancouver, OR-WA, which may bias the measure downward.
[2] The zoning tax is the gap between the marginal cost of new construction and the market price of an apartment.
*Source(s)*: Glaeser, Edward L., Gyourko, Joseph and Saks, Raven. "Why is Manhattan so expensive? Regulation and the rise in housingprices." The Journal of Law and Economics 48, no. 2 (2005): 331-369. https://www.nber.org/papers/w10124.pdf Gyourko, Joseph, Albert Saiz, and Anita Summers. "A New Measure of the Local Regulatory Environment for Housing Markets: TheWharton Residential Land Use Regulatory Index," December 13, 2006. https://doi.org/10.18411/d-2016-154 Brown Calder, Vanessa. "Zoning, Land-Use Planning, and Housing Affordability." *Cato Institute* Policy Analysis 823 (2017). https://www. cato.org/publications/policy-analysis/zoning-land-use-planning-housing-affordability

## APPENDIX E. SELECTED CITIES' ENROLLMENT POLICIES

| | Enrollment Policies | School Enrollment Policies, (rated 0-4) |
|---|---|---|
| Portland, OR | Residential assignment with limited transfers | 1 |
| San Francisco, CA | Districtwide lottery | 4 |
| Houston, TX | Attendance waivers | 1 |
| Chicago, IL | Open enrollment | 4 |

Note: Districts are assigned values from 0-4, with limited transfers/attendance waivers awarded 1 point and districtwide lottery or open enrollment awarded 4 points.
Portland scored by author, all other values provided by source.
*Source:* Wohlstetter, Priscilla, and Zeehandelaar, Dara. "America's Best (and Worst) Cities for School Choice." *Fordham Institute*. (December 2015). https://fordhaminstitute.org/sites/default/files/publication/pdfs/1209-americas-best-and-worst-cities-school-choice.pdf

## APPENDIX F. SCHOOL QUALITY BY HOME VALUE COMPARISON (OVERVIEW)

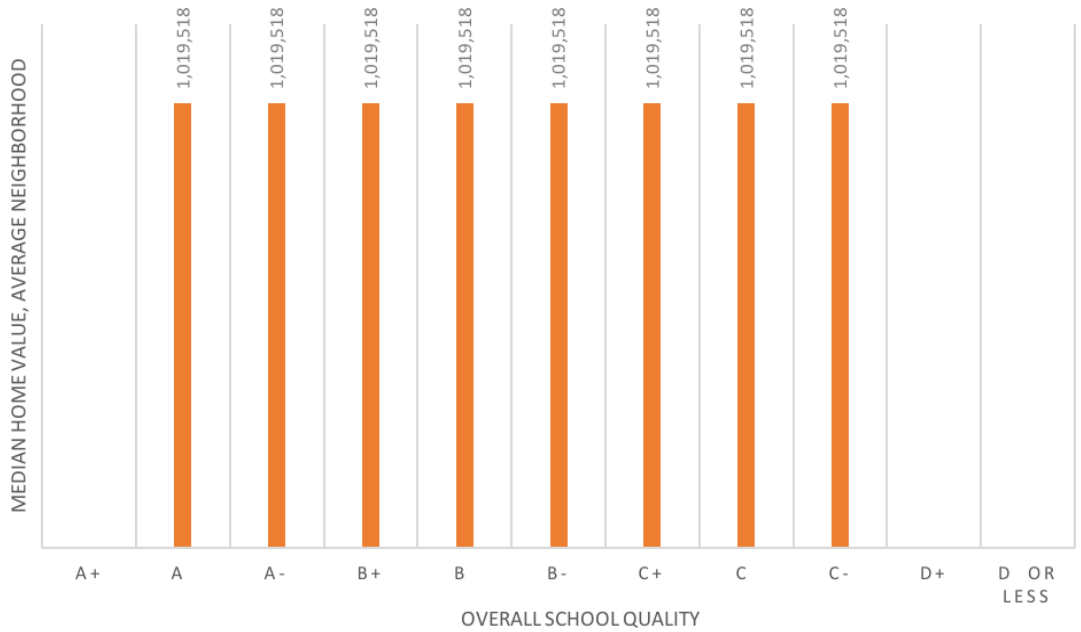
| | Home Value, Highest Quality School | Home Value, Lowest Quality School | Home Value Difference, % (A to C school unless noted) | Home Value Difference, $ (A to C school unless noted) | School Enrollment Policies (rated 0-4) | Zoning Policy Description (Restrictive, Moderate, Liberal) |
|---|---|---|---|---|---|---|
| National[1] | $486,104 | $122,061 | 106% | $196,408 | n/a | n/a |
| Portland, OR | $555,096 | $270,298 | 90% | $262,552 | 1 | R |
| San Francisco, CA | $1,034,201 | $1,019,518 | 7% | $64,910 | 4 | R |
| Houston, TX | $200,864 | $93,540 | 148% | $179,026 | 1 | L |
| Chicago, IL | $292,872 | $243,609 | 14%[2] | $36,530[2] | 4 | M |

Note: Home value represents the average neighborhood median home value associated with a given school quality level. Zoning policydescription by author.
[1] National trend is driven by both intra and inter-district differences, whereas city trends are intra-district only.
[2] A- to C difference only (no A observations available).

## APPENDIX G. SCHOOL QUALITY BY HOME VALUE COMPARISON (DETAIL)

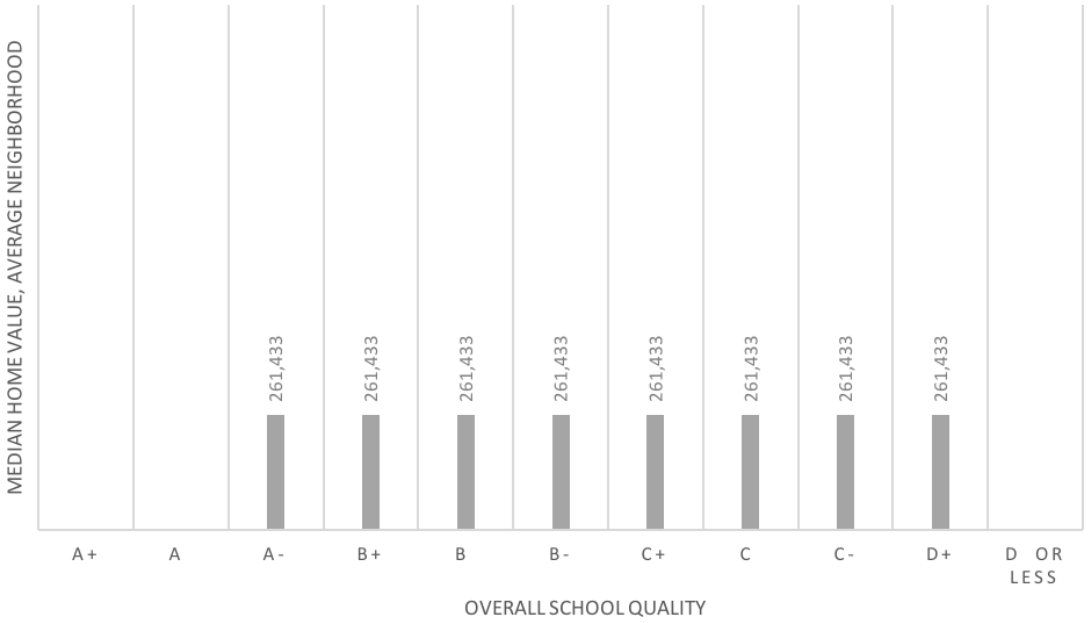
| | National | Portland | San Francisco | Houston | Houston |
|---|---|---|---|---|---|
| A+ | 486,104 | - | - | 200,864 | - |
| A | 381,061 | 555,096 | 1,034,201 | 300,359 | - |
| A- | 255,338 | 464,175 | 1,062,672 | 301,165 | 292,872 |
| B+ | 224,884 | 387,709 | 994,425 | 229,263 | 300,083 |
| B | 187,133 | 361,137 | 871,583 | 144,652 | 289,297 |
| B- | 181,811 | 331,866 | 995,707 | 184,348 | 260,584 |
| C+ | 182,213 | 272,623 | 1,010,734 | 154,933 | 241,289 |
| C | 184,653 | 292,544 | 969,291 | 121,333 | 256,342 |
| C- | 206,431 | 270,298 | 1,019,518 | 93,540 | 204,508 |
| D+ | 133,748 | - | - | - | 243,609 |
| ≤ D | 122,061 | - | - | - | - |

## APPENDIX H. FIGURE 1. SAN FRANCISCO HOME VALUES ARE HIGH AND FLAT ACROSS SCHOOL QUALITY LEVELS




Note: This figure is produced using a single average of all unique neighborhoods associated with a San Francisco public school. It does not rely exclusively on San Francisco's smaller, non-binding attendance areas to determine neighborhood-school relationships, but instead assumes that all neighborhoods intersecting San Francisco public school boundaries are functionally connected with all public schools in San Francisco.

## APPENDIX H. FIGURE 2. CHICAGO HOME VALUES ARE MODERATE AND FLAT ACROSS SCHOOL QUALITY




Note: This figure is produced using a single average of all unique neighborhoods associated with a Chicago public school. It does not rely exclusively on Chicago's smaller, non-binding attendance zones to determine neighborhood-school relationships, but instead assumes that all neighborhoods intersecting Chicago public school boundaries are functionally connected with all publicschools in Chicago.

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3. Bonding social capital develops within social groups, whereas bridging social capital develops between social groups. Social groups include groups defined by religious, class, or racial/ ethnic associations.
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Chiodo, Abbigail, Rubén Hernández-Murillo, and Michael T. Owyang. "Nonlinear effects of school quality on house prices." ***Federal Reserve Bank of St. Louis Review*** 92, no. May/June 2010 (2010). https://files.stlouisfed.org/files/htdocs/publications/review/10/05/Chiodo.pdf Recent research suggests high income parents are more likely to invest in their children at home, and this home investment is more important than school investment in a child's early development. This may help explain why higher home values are often associated with higher quality public school outcomes (high home values are correlated with high incomes and therefore higher home investment). Still, educational quality has an impact on skill formation and can vary outside of home investment, thereby exacerbating or reducing home-based gaps. See: Agostinelli, Francesco, Saharkhiz, Morteza, Wiswall, Matthew J. "Home and School Investment in the Development of Children." ***National Bureau of Economic Research Working Paper Series*** No. 26037. (July 2019). https://www.nber.org/papers/w26037

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Property taxes typically fund 2/3 of school budgets, with most of the remaining funding provided by the state. Property taxes may also encourage restrictive residential zoning in order to control the tax base and ensure higher per capita revenue. Fischel, William A. Zoning ***Rules?: the Economics of Land Use Regulation*** Cambridge, Massachusetts: Lincoln Institute of Land Policy, 2015.

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17. ZIP codes are used for national estimates, and neighborhoods are used for cross-city comparisons. ZIP codes provide more comprehensive data coverage for national estimates (Figure 1) and neighborhoods provide a more granular unit of analysis for most comparison cities.
Niche's neighborhood data includes approximately 69 million residents located in 59 U.S. metro areas. Ninety-nine percent of 326,865 neighborhood-school observations are located in one of these metro areas. Neighborhoods vary in size from 60 residents to 60,000 and run the spectrum from well-defined and locally-understood boundaries to boundaries subjectively created by third parties.

18. Charter and magnet schools, which receive public funding but lack traditional school zones, are excluded.

19. A model regressing logged median home value on school quality grade dummies and state fixed effects with 185,027 zip-elementary school observations finds an overall $R^2$ = 0.51, F-stat = 3215.00, p-value = 0.00, adjusted $R^2$ = 0.51, root MSE = 0.49.

20. Relationships presented in Figure 2 are intended to provide descriptive information about the housing-school choice landscape families face. There are many variables that may influence the relationship between home values and school quality.

21. Median home values are based on the 2017 American Community Survey (ACS). The median home value in the United States in 2017 was approximately $200,000, or less than the median home value in an average ZIP code associated with a B+ quality school. US Census Bureau "2017 American Housing Survey" Table Creator tool "Nation – Value, Purchase Price, and Source of Down payment – Owner-occupied Units" Accessed October 23rd, 2019.
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22. Note that not all school quality measures vary with home prices in the same way. For instance, school resources and facilities grades generally decline as average neighborhood median home value rise, and some other measures don't follow an obvious pattern. The former relationship may be a consequence of redistributive federal or local programs.

23. Niche.com restricts the range of grade values for teacher quality between A+ and C- for display purposes.

24. Only major U.S. cities with historically strong housing demand are selected for comparison. In some cases selected cities do not provide widespread public school choice through a districtwide lottery, but provide other types of public school choice including magnet schools, charter schools, and attendance waivers. These alternatives can provide opportunities for circumventing the local housing and public school choice set, and are noted in some places though not reflected in estimates.

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# What's Next for Schools

## Balancing the Costs of School Closures Against COVID-19 Health Risks

SCP REPORT NO. 1-21 | FEBRUARY 2021

The COVID-19 pandemic altered the lives of every family in America and particularly affected American families with school-aged children. In March 2020, every school district in the country closed and transitioned to remote learning, and this posed new challenges for parents, teachers, and students. The virus persisted throughout the fall and winter, and so have the associated challenges for families and children.

Some schools began the process of reopening in the spring, while others either remained closed or canceled their reopening plans amidst rising infection rates. As of spring 2021, 24 percent of schools remain fully remote, and 18 percent are teaching fully in person.[1] The majority of schools (51 percent) are operating under some type of hybrid model, offering in-person instruction on limited days of the week or for select grade levels, with no option for full-time in-person instruction.[2]

The evidence suggests that this disruption to children's education harms their learning, as well as the mental health of parents, students, and teachers. Parents are facing additional stress as a result of overseeing their children's at-home education, teachers must adapt to a new method of instruction, and children have entered the uncharted territory of at-home learning, separated from their teachers and friends. While the costs are concerning, decision makers have the unenviable task of balancing the costs of school closures against the health risksof in-person instruction.

This paper surveys the research on the costs of school closures and the health risks of reopening in order to help inform local decision-making. School closures have negative, predictable ramifications for parents and students, with the greatest harm concentrated among the youngest students. At the same time, research also indicates that young children are less likely to contract and spread COVID-19, and this suggests that local leaders should prioritize young children's return to school.

The circumstances that American families find themselves in during the pandemic are unusual. Families' diverse needs during the COVID-19 pandemic underscore the drawbacks of a traditional one-size-fits-all approach to education and highlight the need for innovative alternatives to traditional options, now and in the future.

## THE ACADEMIC IMPACT OF SCHOOL CLOSURES

For a variety of reasons, extended school closures have harmful implications for children's academic and developmental progress. First, early childhood education is dependent on sensory and social experiences that are not easily replaced at a

distance. Additionally, recent research estimates that remote learning will result in considerable learning losses among older students, and these losses will have long-term effects.

*Developmental Losses*

It is unlikely that distance learning can serve as a suitable replacement for the classroom for young children. To begin with, closing schools separates children from important learning tools used in the classroom. To the extent these tools are not adequately replaced at home, this separation may hinder children's education and development.

For instance, a primary method used in the instruction of young children is sensory play—hands-on activities that aid learning by engaging the five senses. Sensory play has been referred to as "the foundation of all the skills children will use in school learning to read, write and solve math and science problems."[3] For example, young children's use of blocks as learning tools can help build the foundation for math skills by aiding the development of spatial awareness and pattern recognition. Research also suggests that sensory play-based experiences in preschool and kindergarten result in better social and academic outcomes than direct instruction.[4]

Another consequence of remote learning is that it can lead to reduced social development. As many adults have learned, even the best online experiences can hardly replicate in-person interactions. Children are less likely to learn how to interact with peers and adults without in-person schooling or extracurricular activities such as sports. In a Pew Research Center survey conducted in fall 2020, 47 percent of parents with young children said they were more concerned about their children falling behind in social skills than they were before the pandemic, compared to just seven percent who were less concerned.[5]

By decreasing the amount of time children spend learning and socializing in school, school closures have also led children to increase their use of digital media, exacerbating parents pre-existing concerns about their children's screen time. In a Pew Research survey conducted in early March, just before pandemic restrictions went into effect, 71 percent of parents with children under 12 reported being at least somewhat concerned that their children were using screens too often.[6] Prior to the pandemic, children ages five to eight were already using screen media for more than three hours per day, with the large majority of that time spent watching television or online videos.[7] Since then, Nielsen ratings data show that television and video viewing among children has only increased.[8] Similarly, survey data indicate that parents' concerns have grown as screen use among their young kids has increased.[9]

Unfortunately, research suggests that higher levels of television watching can have negative effects on young children's development. For example, higher levels of television viewing is linked to poorer attention issues among young children.[10] Although the bulk of the literature connecting television watching and developmental outcomes focuses on children who are not yet school age, more frequent television viewing among school-aged children has been associated

with lower physical health, less pro-social behavior, and decreased academic achievement,[11] and some of these adverse outcomes seem to persist into young adulthood.[12]

Beyond television watching, there may be additional reason for pause with regard to children's increased screen use. For instance, preliminary results from a ten-year longitudinal study of 11,000 U.S. nine- and ten-year-olds indicate a relationship between increased screen use and lower scores on cognitive and language tests.[13] Overall, the available evidence suggests that remote learning is suboptimal for younger students' development.

*Learning Losses*

School closures threaten to disrupt children's education, leading to poorer academic outcomes and potentially worse economic outcomes later in life. Just as students experience a "summer slide," and forget much of what they learned over the past year during summer vacation,[14] so students today are experiencinga "COVID slide."

Using past research on summer learning loss, as well as work on human capital investment and other interruptions to students' education, several studies have attempted to estimate the learning loss resulting from COVID-19 school closures. These studies predicted that severe learning losses would dramatically set children back in the fall semester.[15]

Later in the year, researchers were able to use real-world data to quantify the magnitude of the COVID learning slide. According to one study of grades 1-8, students in many grades were reading close to expectations in the fall semester, though others were several weeks behind. Furthermore, every grade was behindin math, in some cases up to 12 or more weeks behind.[16] Another study of grades3-8 similarly found that students had made some progress in math and learningsince the pandemic began, with reading ability similar to past years but math ability roughly 5 to 10 percentage points below normal.[17]

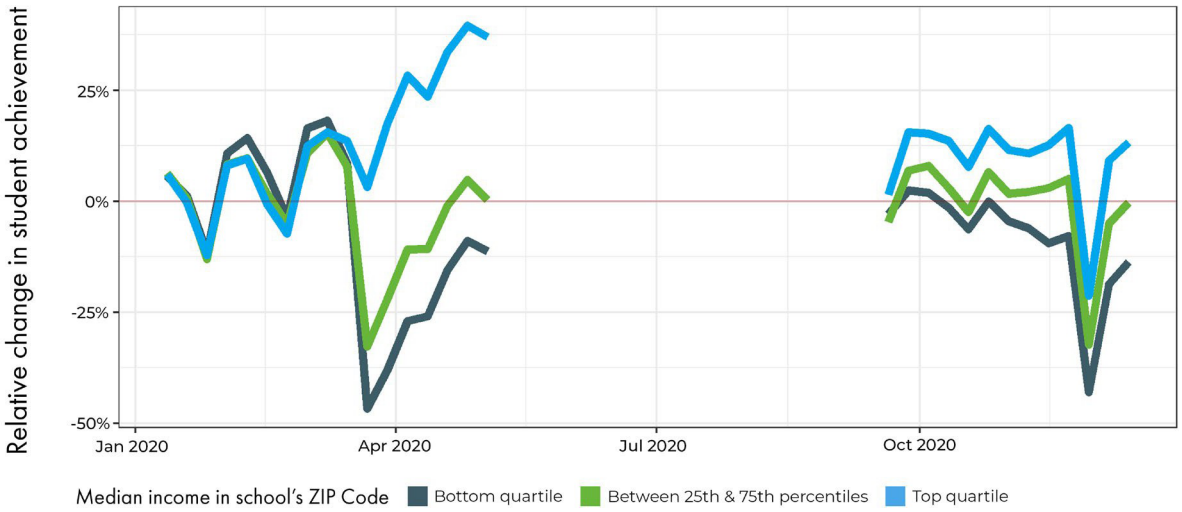
Nevertheless, teachers and parents seem more skeptical of students' abilities than study results suggest. In an October 2020 survey, 66 percent of teachers said that most students were less prepared for grade-level work compared to lastyear, and 27 percent reported that a majority of their students were significantly less prepared. Only 19 percent of teachers reported that they had covered all or nearly all of the material they would have covered by this point a year ago, while 56 percent said that they had covered half or less of last year's material.[18] Similarly, only 40 percent of parents believe that their children have learned as much at home as in the classroom.[19]

The COVID slide may be particularly harmful to low-income students, partly due to differences in home environments and access to the technology necessary for online learning.[20] Assuming a complete return to in-person instruction in January 2021, McKinsey estimated that low-income students will lose 12.4 months of learning compared to the overall average loss of 6.8 months.[21] The disparity is due to a variety of factors; low-income students are less likely to have

a high-quality learning environment at home free of distractions, less likely to have access to their own devices dedicated to remote instruction, and less likelyto engage in online school with the same consistency as students from higher-income families.[22] Indeed, in an October 2020 survey, 33 percent of teachers in the highest-poverty schools reported that students were significantly less prepared than the year prior, versus 16 percent of teachers in low-poverty schools.[23]

Data from Harvard University's Opportunity Insights highlights these disparities (Figure 1).[24] Prior to the pandemic, rates of student progress were relatively similar across schools aggregated by their respective ZIP codes' median incomes.Since then, students in ZIP codes in the top quartile by median income have progressed further in online math courses than those from ZIP codes in the bottom quartile.[25] They have also participated far more consistently in online math than those from areas in the three lower quartiles.[26]

Figure 1: Online Math Learning Achievement by School ZIP Code's Median Income(as of December 13, 2020)




Source: Opportunity Insights Economic Tracker

In addition to learning loss varying by income, learning loss also appears to vary with age. Younger children are likely to face the greatest setbacks because they are supposed to be learning foundational skills. For example, numerous studies have projected pronounced reading losses among U.S. kindergarteners due to school closures.[27] Researchers from Illuminate Education recommend that schools "[s]pend more time focused on reading and math in K-3 classrooms. The risk of learning loss is greater in these grades, so it is even more critical to spend time helping students make up for the lack of instruction in these foundational subjects."[28] Additional research has concluded that "there may be a need to think about providing more resources at early grades to help students catch upin their learning or to prioritize what skills are taught in these grades."[29]

*Economic Costs of Learning Loss*

Learning loss will bring with it long-term economic costs, even if schools return to full in-person instruction immediately. McKinsey estimated that, assuming in-school instruction resumes in January 2021, the average K-12 U.S. student could lose $61,000 to $82,000 (constant 2020 dollars) in lifetime earnings.[30] For the aggregate K-12 cohort, this amounts to an estimated $110 billion in annual earnings lost—$98.8 billion from learning loss, and $11.2 billion from an increase in high-school dropouts. Of course, any delays past January 2021 would increase losses further.

The Penn Wharton Budget Model similarly estimated that, as of October 1, 2020, school closures had already cost students in grades 1-12 between $43,000and $57,000 each.[31] Each additional month of school closures is estimated to cost current students $12,000 to $15,000 in future earnings.[32]

As with learning loss, young children will likely face the greatest economic harm from today's school closures. One study estimates that children aged six—those just starting primary school when the pandemic struck—will suffer earning losses 60 percent higher than children aged 14.[33] All told, the BrookingsInstitution estimated that the aggregate cost of four months of lost education in the United States is $2.5 trillion, or 12.7 percent of annual GDP.[34]

## THE EFFECT OF SCHOOL CLOSURES ON AMERICANS' MENTAL HEALTH

In addition to children's developmental and academic losses, American familiesare experiencing declines in their mental health. Children are suffering from a loss of routine, isolation from their peers, and the stress of remote learning. Parents, especially those with young children, face the added stress of overseeing schooling in addition to their other responsibilities.

*Harm to Children's Mental Health*

Disruptions to normal school activity have caused many children to struggle with their mental health. In May, nearly 30 percent of parents surveyed by Gallup reported that their child was experiencing emotional or mental harm due to social distancing and school closures. Nearly half believed that their child's separation from classmates and teachers posed a major challenge, and of those, only 12 percent thought that their child could continue with remote learning indefinitely.[35] Parental concerns grew considerably as schools remained closed. A Pew Research Center survey from October revealed that 59 percent of parents with children in grades K-12 were concerned about their child's emotional well-being,and that 60 percent were concerned about their children not maintaining socialconnections and friendships. Parents were significantly more concerned about each of these issues if their child was only receiving online instruction versus in- person instruction.[36]

In addition to causing feelings of isolation, school closures are contributing to families' stress more generally. When higher levels of stress translate to a stressful home life, they further harm children's mental health: research shows that high-stress environments can exacerbate pre-existing psychological issues in children, such as behavioral problems and psychological disorders.[37] Indeed, in a national survey of parents, nearly one-fifth reported that their child's behavioral health had worsened from March to June after schools had closed – findings that were similar across racial and economic groups.[38] Reports did differ, however, depending on the age of their child. Parents with children ages 6 to 12 were more likely to report worsening behavioral health than parents with children older than 13.[39]

Increasing stress in family life may also worsen some children's treatment at home. Parents' stress levels are undoubtedly rising as they are being asked to be work, teach, and care for their children at the same time, especially while some children exhibit greater behavioral problems. These stressors may lead to parental burnout, defined as "a prolonged response to chronic and overwhelming parental stress.[40] Research shows that parents with higher levels of parental burnout engage in greater levels of child abuse and neglect.[41] At the same time, school closures are separating children from teachers, school psychologists, nurses, and other staff trained to identify and report child mistreatment. One analysis of child abuse hotline allegations in Florida found that reported allegations of abuse, neglect or abandonment in March and April were 27 percent lower thanexpected, and the reduction was driven by decreased calls from school staff.[42]

The potential for mistreatment is increasing at a time when mental health services are less accessible to children. A nationally representative survey conducted in 2014 found that 13 percent of children aged 12 to 17 received mental health services from a school setting.[43] These services can include talking to counselors or participating in programs for students with emotional or behavioral problems, and younger adolescents were more likely than older adolescents to receive these services. An analysis of the same survey from 2012 to 2015 found that, of the adolescents that received any mental health services, 35 percent received their services exclusively from school settings and 57 percent received at least some services in a school setting.[44]

Finally, school shutdowns have been particularly difficult for students with learning disabilities. Schools are required to provide these students with specialized services to help them succeed, yet these services are harder to deliver while schools are closed. For example, some students may require one-on-one assistance in the classroom from a personal aid, and others require modified equipment or a different method of instruction. According to a survey conducted in May by ParentsTogether, 80 percent of parents with children in special education said that their children were not receiving all of the specializedservices they require, as mandated by law.[45] Additionally, parents of special needschildren were twice as likely as other parents to say that their child was doing little to no remote learning (35 percent vs. 17 percent).[46]

### *Harm to Parents' Mental Health*

In 2019, there were over 50 million working parents with children under 18 years old, 42 percent of which had children under the age of six.[47] As children have suffered from the disruption of routine, these parents have also struggled with taking on the new responsibility of schooling their children. The added stress is even greater for the parents of younger children, who require more attention throughout the day.

In an April survey of parents with children ages 12 and younger, 45 percent did not feel prepared to educate their children at home, and 50 percent felt overwhelmed by their new responsibilities, citing behavioral problems and the difficulty of balancing their work with their children's schooling.[48] Similarly, in a Pew Research Center survey conducted in May, 72 percent of working parents said that balancing a job with helping kids with school was a challenge, and over 40 percent reported it was a major challenge.[49]

Not surprisingly, this added stress has worsened parents' well-being. A national survey from June 2020 revealed that over one quarter of parents experienced declining mental health since March, and parents of young children saw even more widespread declines.[50] Furthermore, using survey data collected from February to April, researchers have estimated that the increased caregiving burdens caused by school closures are significantly associated with negative parental mood, even after controlling for the mood effects of COVID-related job and income loss.[51] More recently, the U.S. Census Household Pulse Survey from early December revealed that adults in households with children under 18 report higher rates of anxiety and depression than adults in households with no children.[52]

### *Economic Implications*

Productivity is a key component to economic growth. By harming working parents' mental health, school closures have negative ramifications for the labor force and the economy.

In 2019, nearly one third of workers in the United States had children under the age of 18.[53] Therefore, school closures threaten to reduce a large proportion of thelabor market's productivity. For instance, one study of dual-income households found that, during the COVID-19 lockdowns, mothers reported lower workbproductivity and job satisfaction than fathers. Prior to the lockdowns, however, there were no differences between reported productivity and satisfaction, suggesting that mothers took on a greater role in childcare once schools closed.[54] Additional research found that mothers of school age children in states with early closures worked longer hours than mothers in states with laterclosures, and this indicates a decrease in work productivity among mothers that work from home.[55] As long as school closures require working parents to be responsible for overseeing their children's schooling, it seems safe to assume U.S. productivity will suffer.

## HOW REOPENING SCHOOLS AFFECTS THE SPREAD OF COVID-19

Closing schools harms children and parents—developmentally, academically, and psychologically. Yet, teachers, parents, and policymakers have worried sincethe beginning of the pandemic that reopening schools will increase the spread of COVID-19.

It is important that decision makers balance the benefits of school reopening against associated health risks; however, evidence on the relationship between school reopening and health risks is more mixed than commonly recognized. One interesting area of consensus is that younger children are at much lower risk of contracting and transmitting the virus than older children.

### *Health Risks for the Overall Population*

Reopening schools brings with it the fear that in-person contact will increase the spread of COVID-19 and threaten at-risk teachers and relatives. In line with that concern, one analysis estimated that 42 percent of school employees are high-risk due to confounding factors like obesity and high blood pressure, and additionally that 59 percent of school-aged children live with at least one adult who meets the definition of increased risk.[56] Given this information, it is important to determine to what extent school reopenings might increase COVID-19 transmission.

Many researchers have attempted to quantify how school reopenings influence infection rates, both in domestically and around the world. In the United States, preliminary evidence suggests that school reopenings do not significantly contribute to the spread of COVID-19. For example, researchers from the Center for Disease Control and Prevention (CDC) recently concluded there is little evidence that school attendance increases community transmission.[57] They cite studies of schools offering in-person instruction in North Carolina, Wisconsin, and Mississippi, in each case finding that COVID-19 transmission is rare between students and faculty and amongst students themselves. Because of the low rates of infection at schools, the researchers argue that reducing community-based transmission is more important to slow the spread of COVID-19 than reducing school-based transmission.

Additional evidence from two new studies seem to echo these findings, but with caveats for schools in communities with high infection rates. The first, an examination of Michigan and Washington schools in fall 2020, used multivariate regressions to find that interventions like mandatory mask wearing effectively eliminate the relationship between in-person instruction and COVID case counts.[58] Yet, the researchers caution that in-person schooling is predicted to increase community spread in areas with very high pre-existing infection rates. The second study was a nationwide analysis of schools in nearly every county in the United States from January to October.[59] Using difference-in-difference analysis, the researchers found that in-person instruction had no effect on

infection rates in counties with fewer than 36 to 44 new COVID-19 hospitalizations per 100,000 people per week. Roughly 75 percent of the schools examined fell beneath this threshold.

Using data from 47 states, economist Emily Oster found similar results: in schools that reopened, infection rates were only equal to 0.13 percent amongschool students and 0.24 percent among staff. These rates equate to "about 1.3 infections over two weeks in a school of 1,000 kids, or 2.2 infections over two weeks in a group of 1,000 staff,"[60] and they suggest that school reopenings do not pose a significant threat for COVID-19 spread. Oster later analyzed October and November infection rates in New York and found that 80 percent of schools offering in-person instruction reported zero COVID-19 cases.[61] She noted that "of those schools that did detect covid, nearly 90 percent had only one or two cases across all students and staff."[62]

The international evidence is less clear. For instance, one study analyzed interventions in 79 countries and found that school closures were among the most effective at reducing infection rates.[63] Another study came to a similar conclusion after evaluating interventions in 131 countries, finding that school closures had the largest impact on reducing infection rates.[64] It is worth noting, however, that the researchers were unable to evaluate the effectiveness of school safety protocols – such as desk dividers, physical distancing, and enhanced hygiene – which scientists argue reduce the spread of COVID-19.

Other international studies have been unable to draw causal relationships between school reopenings and infection rates. For example, one study found that closing schools in Norway and Denmark led to a decline in infections, yet reopening schools did not lead to a corresponding increase due to low rates of community transmission.[65] Similarly, in Germany, school reopenings increased transmission among students, but not school staff.[66] In Spain, reopening schools led to cases rising in one region but falling in another.[67] And after Sweden chose to keep its schools open and Finland chose to close its schools, students under the age of 20 in both countries experienced nearly identical infection rates.[68]

Perhaps the non-profit group Insights for Education summarizes the research best. After studying the experience of 191 countries, Insights for Education concluded that "no consistency can be observed between school status and infection levels."[69] Yet, at least domestically, the evidence seems to suggest that school reopenings are safe for areas with lower rates of community transmission.

*Health Risks across Age Groups*

Though the evidence on the relationship between school reopenings and overall infection rates is somewhat mixed, the research is united on one point: the risk of transmission increases with age.

First, a review of worldwide outbreaks by researchers at the University of Vermont found that young children are hardly ever the primary sources of infection. The authors posit that, because children are more likely to be asymptomatic than adults, they are less likely to cough or otherwise release infectious particles that

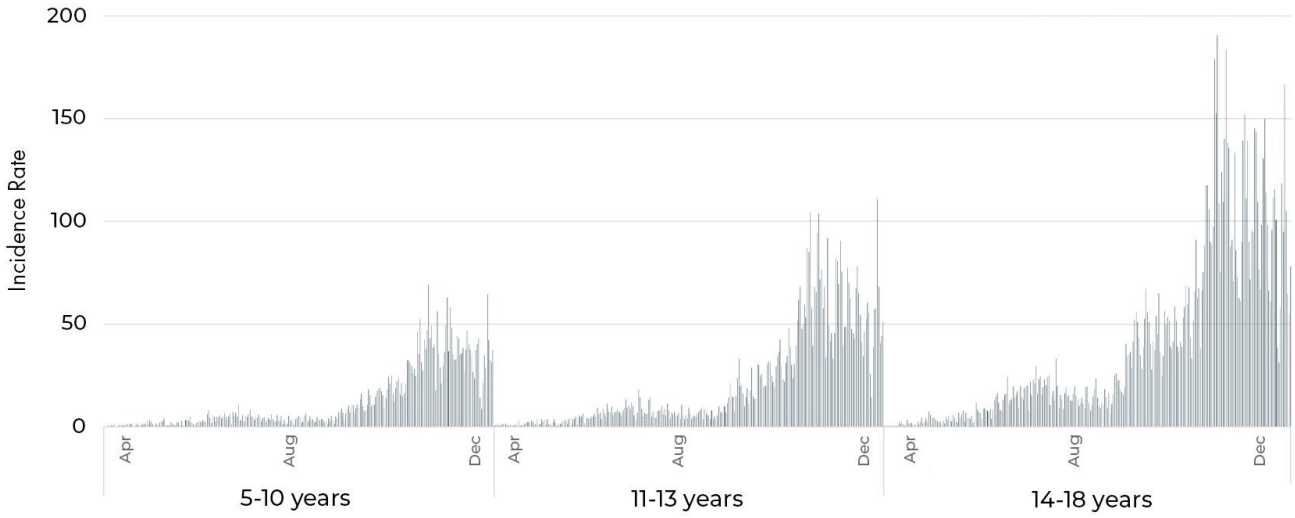
spread the virus.[70] Similarly, a study from South Korea showed that children under age 10 transmit the virus at one quarter of the rate of children ages 10 to 19.[71]

Other research confirms that infection rates are consistently lower in younger populations. One study of German schools found that children ages 6 to 10 were less likely to have COVID-19 than adults and older children at the same schools.[72] Another study of Italy, Japan, and four other nations found that individuals under age 20 were only half as susceptible to infection as adults over the age of 20, and that nearly 80 percent of infected students did not show symptoms.[73]

The same patterns are observable in the United States. In New York, high school students and staff have similar infection rates to the overall population, yet the rates for elementary and middle school students are consistently lower.[74]

These trends can be visualized using data from Utah, which keeps detailed records of school-associated COVID-19 cases. Figure 2 displays Utah infection rates by age from April to December, and it shows that high school-aged children are much more likely than elementary school-aged children to be infected over the entire time period. According to data from December, the daily infection rate was 177 percent higher among high school-aged children than elementary school-aged children, and 70 percent higher among high school-aged children than middle school-aged children.[75]

Figure 2. School-Age Group Specific Case Rates per 100,000 Population in Utah, by Report Date




Source: Utah Department of Health COVID-19 Surveillance

This evidence confirms that younger children face only modest health risks from returning to school, and this suggests that their return to school should be prioritized. Across all ages, a flexible approach to education is critical; this approach should include an option to return to school or utilize other educational options based on students' and families' educational needs, risk factors, and risk tolerance.

## THE RESPONSE FROM PARENTS AND COMMUNITIES

While teachers and policymakers consider whether, when, and how to reopen schools, parents face the more personal question of how to continue their children's education in a way that fits their family's needs, priorities, and risk tolerance. Many parents appear to be treating the pandemic as an opportunity to reevaluate their children's educational options. For example, in October 2020, 64 percent of parents said that schools should focus on "rethinking how we educate students, coming up with new ways to teach children moving forward as a result of the COVID-19 crisis," rather than prioritizing a return to pre-pandemic conditions.[76] Similarly, a July surveyfound that 69 percent of parents believed that schools should provide multiple learning options in fall 2020.[77]

Parents' interest in new educational approaches is apparent in their willingness to experiment with new ways of meeting their children's educational needs. For instance, homeschooling has seen a dramatic increase. One recent survey reported an increase in homeschooling from 5 percent in fall 2019 to 10 percent in fall 2020,[78] while another reported an increase from 7 to 16 percent.[79] As the Social Capital Project has documented, results from the nationwide American Family Survey conducted this summer show that roughly 40 percent of parents say the pandemichas made them more likely to consider homeschooling in the future.[80] Overall, 67 percent of parents have a more favorable opinion of homeschooling since the pandemic began in March, compared to 19 percent whose opinion is less favorable.[81]

Although parents' views on charter schools are roughly the same as in March,[82] thereare some indications that parents have been especially satisfied with charter schools this year. For example, 45 percent of charter school parents reported in May being "very satisfied" with their school's response to COVID-19, versus 26 percent of public school parents. Compared to parents of public school students, parents of charter school students also report that their students' schools devote a greater share of remote instruction to learning new material and they report more one-on-one teacher-student interaction.[83]

Perhaps the most notable, recent educational innovation has been the rise of "learning pods"—small groups of students that function as schools in miniature. Students generally meet in person at one family's house or elsewhere and receive instruction from a parent or outside tutor. A recent survey of Americans shows widespread support for policies that would reduce the regulatory obstacles to parents creating pods, and this suggests further public support for a more pluralistic approach to education. For example, 50 percent of respondents agreed that policymakers should consider aligning pods with current laws for homeschooling and private schools so that pod families do not face heavier regulatory burdens, while only 15 percent disagreed. Similarly, 41 percent of respondents agreed that states should avoid putting in place new pupil-staff ratios for pods and further supported permanent waivers to childcare regulations for pods, compared to just 20 percent who disagreed.[84]

## CONCLUSION

As policymakers contemplate reopening schools, it is important that they balance the often-ignored costs of continued school closures with the critical health risks of school reopenings. This paper aims to aid decision-makers by surveying existing research on each of these topics.

First, research confirms that school closures constitute a difficult disruption to students' development. The harm is especially concentrated among very young children, whose separation from teachers and classroom tools may hinder their progress. Furthermore, these children are the most at risk of developing cognitive issues from excessive screen time, a feature of remote learning.

Disruptions to in-person education also harm older children academically. Students with learning disabilities may be disproportionately harmed by not having access to the specialized services they depend on at school. Because of differences in home environments and technology access and use, continued remote learning may also exacerbate current gaps in educational achievement across the socioeconomic spectrum. These COVID-19 learning losses may reduce all students' expected future earnings, however children at the beginning of their school career will likely suffer to the greatest extent.

Second, school closures significantly increase stress for American families with school-aged children. Surveys show that parents are worried about their children's emotional wellbeing while they are isolated from their teachers and friends, and that their children are experiencing greater behavioral issues while they engage in remote learning. Furthermore, separating children from school also separates them from many mental health services, which can be particularly damaging during this time of increased stress and isolation. Reported harm is even worse among younger children, who are experiencing greater issues with their behavioral health and normally take greater advantage of school-provided mental health services.

Parents are also experiencing greater stress as they are confronted with the new responsibility of schooling their children at home. This stress is bleeding into their work life, requiring them to work longer hours and reducing their work productivity. Parents with young children are especially impacted as they must devote more time and attention to caring for their children throughout the day.

All of this evidence suggests that young children should be prioritized for going back to school. Although the research is quite conclusive regarding the harms of school closures, the obvious concern about reopening schools is that it would exacerbate the spread of COVID-19. In this area, the connection between school reopenings and COVID-19 infection rates is less than clear. What the research does agree on is that young children are at lower risk of getting and transmitting COVID-19 than older children and adults.

As important as the immediate matter of school reopening is, however, the pandemic also provides an opportunity to think more broadly about how to improve the American education system and better enable parents to select the education that best fits their preferences and their children's needs. As the Social Capital Project's paper "Multiple Choice" argued, policymakers should promote "educational pluralism," which "recognizes the value of having distinctive school cultures and couples choice with accountability."[85] Educational pluralism recognizes that the challenges and competing priorities of reopening schools cannot be solved by a one-size-fits-all approach.

The pandemic in particular calls for a response that recognizes the variation in parental and student needs. Indeed, the range of efforts from parents to continue their children's education today suggests that many are already well aware of the benefits of flexibility to adapt each child's education to his or her particular needs. Though the pandemic will pass, the need for policymakers and educatorsto accommodate those needs will remain. As policymakers weigh the costs and benefits of reopening schools with the appropriate safety measures, they should recognize the growing popularity of alternative schooling methods and work to improve parents' ability to organize educational approaches that best meet the needs of students and parents alike.

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# Examining the Relationship Between Higher Education and Family Formation

SCP REPORT NO. 6-21 | OCTOBER 2021

## INTRODUCTION

As educational attainment continues rising, the presumed price of admission to the middle class increasingly seems to require a college degree. In the United States, more young adults than ever attend college, and more young adults than ever rely on student loans. The percentage of all households with any outstanding student loan debt rose from 8.9 percent in 1989 to 21.4 percent in 2019.[1] And from 2006 to 2020, the average amount of outstanding student loan debt per working-age American grew from under $4,000 to over $13,000.[2]

At the same time, a growing cultural emphasis on "individual financial and personal responsibility as a necessary precursor for marriage" has led to a profound shift in attitudes towards family formation.[3] Marriage has become more of a "capstone," signaling a full transition into adulthood, and less of a "cornerstone," on which young couples begin to build a life together.[4]

These two facts have led many to associate rising student loan burdens with delayed marriage and parenthood.[5] A study by a private student loan lender found that roughly one-third of adults who attended college "might" consider delaying marriage due to education-related debt.[6] "How could I consider having children if I can barely support myself?" asked one Chicago woman who graduated from a for-profit interior design school with six figures of debt.[7]

But declining marriage and fertility rates are happening across the board, while student loan burdens are less widespread. According to the Federal Reserve, 70 percent of all U.S. adults, including 57 percent of those who attended college, have never incurred education-related debt.[8] A full two-thirds of the Millennial generation, who came of age during the rapid run-up in education-related debt, hold no student loan debt.[9]

Additionally, education-related debt is an investment as well as an obligation. Paying for higher education through student loans is one way of increasing human capital, and this makes it both a liability and an asset.

The Social Capital Project has identified "making it more affordable to raise a family" as one of the core goals of our work. [10] Proposals to reduce or eliminate student debt on a large scale are often proposed in the spirit of lifting barriers to family formation, allowing young adults to marry or become parents.[11] But

understanding what role student debt plays in the lives of young Americans is important before adopting widespread policy prescriptions.

Careful consideration of the research suggests that some individuals with exceptionally high loan burdens, particularly women, are more likely to delay marriage. There is less evidence that student loans are associated with lower fertility. And on balance, large debt burdens are largely shouldered by a largely self-selected subset of households, many with higher educational attainment and higher earning potential.

Still, no one wants young adults to be overly burdened by student loans. Income-based repayment can be improved, particularly for individuals who did not finish college or who are underemployed. Supporting community college, trade schools, and non-traditional pathways to the workforce, and encouraging more competition in higher education, would help more young people increase their options without overreliance on debt.

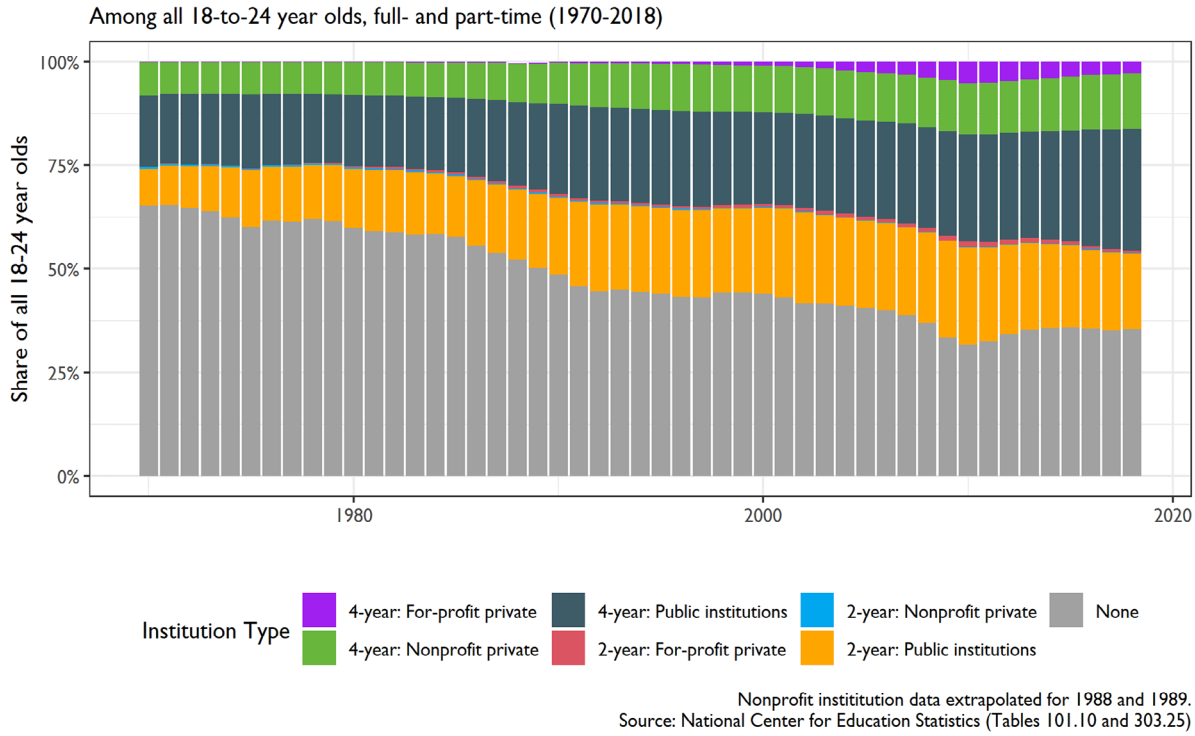
This paper will weigh the extent to which student loan debt may be interfering with young adults' desire to get married and start a family, before concluding with a brief exploration of related public policy options.

## THE EVOLUTION OF STUDENT DEBT

### *Increasing Attendance, Rising Costs*

Some form of college education has become the norm for a majority of young adults. Ever since 1988, more young adults than not have been enrolled full- or part-time in an institution of higher education, with the share of young adults enrolled in college plateauing somewhat in the early 2010s.

Figure 1: Enrollment in degree-granting post-secondary institutions, by type




Nonprofit institution data extrapolated for 1988 and 1989.
Source: National Center for Education Statistics (Tables 101.10 and 303.25)

College has also become more expensive. The average sticker price for tuition, fees, room, and board (TFRB) facing a full-time student at a four-year, public university doubled from 1992 to 2018.[12] The reason for the increasing costs are multifaceted. For one, amenities have improved – room and board costs at a four-year university have more than doubled, in constant dollars, since 1980.[13] Additionally, new administrative positions, some tied to regulatory compliance, have pushed up colleges' operating costs; the number of administrative and managerial staff at private four-year universities doubled from 1991 to 2011.[14] Finally, colleges may also have gotten better at price discrimination, the economic term for charging according to a consumer's ability to pay; among full-time undergraduates, the rise in prevalence and average size of student loans is most notable among families in the top income quartile, as seen in Figure 2.[15]

Another explanation for rising tuition is that increases in federal education loans are responsible for subsequent rises in tuition. This idea is known as the Bennett Hypothesis, after President Reagan's Secretary of Education William Bennett, who first proposed it in 1987.[16] Ever since, researchers have sought to empirically isolate the effect of increasing federal aid on tuition, with different papers reaching varying results.

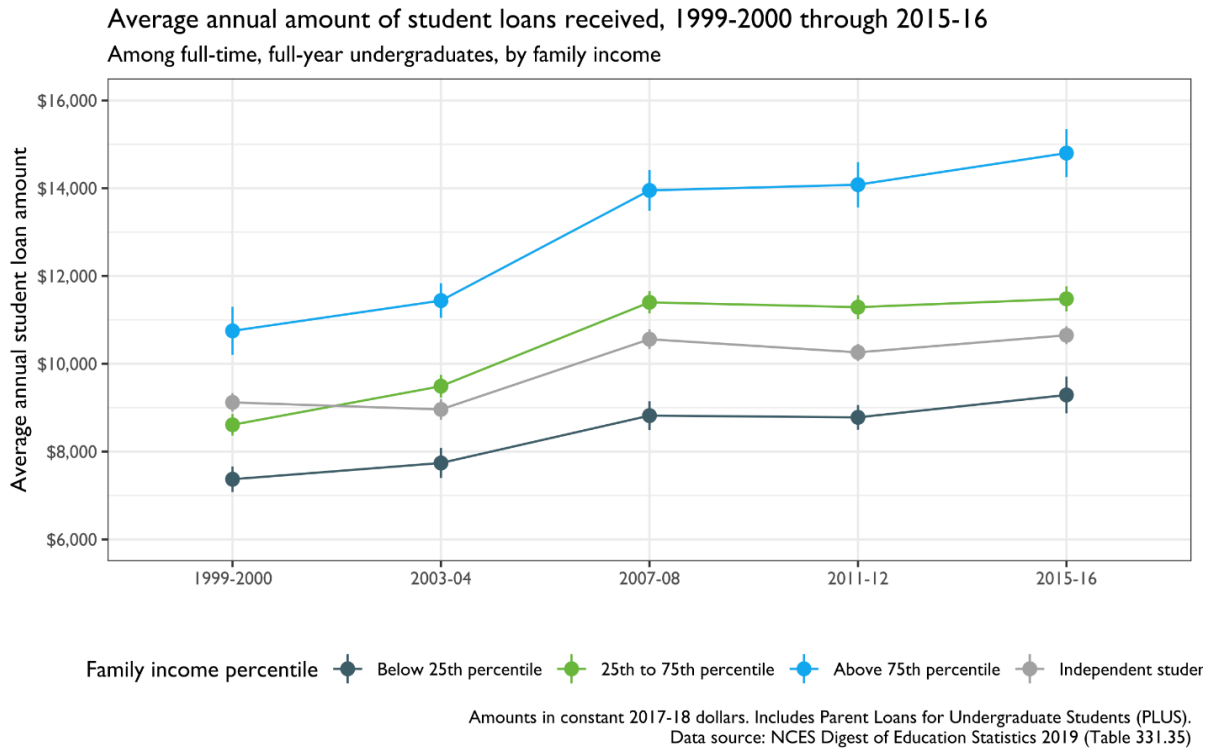
As Texas Public Policy Foundation scholar Andrew Gillen has written, "'Is the Bennett Hypothesis true?' is the wrong question as it has no consistent answer. The better question is, 'When does the Bennett Hypothesis hold or not hold, and why?'"[17] One paper found distinct evidence for the Bennett hypothesis in

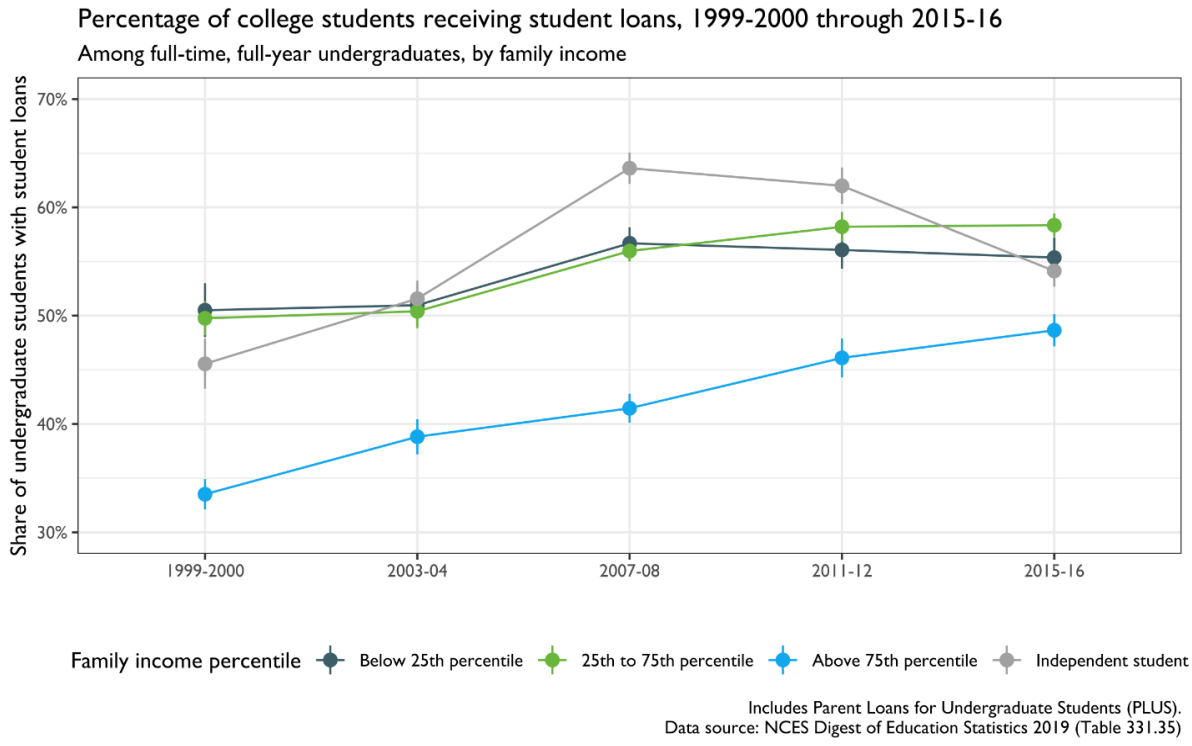
for-profit programs offering certificate programs; institutions that participated in federal student aid programs charged tuition that was 78 percent higher than comparable programs in institutions that did not participate.[18] Another paper found evidence to suggest an effect on "more expensive degrees, those offered by private institutions, and for two-year or vocational programs."[19]

Another form of federal subsidy for higher education comes in the form of parent PLUS loans. These loans are only available to parents of undergraduate students, and unlike undergraduate loans, there is no set maximum loan. As such, parents can borrow up to the full cost of attendance, with even less cost discipline in this form of loan than in other programs. According to a Brookings Institution paper, "the average annual borrowing amount for parent borrowers has more than tripled over the last 25 years, from $5,200 per year in 1990 (adjusted for inflation) to $16,100 in 2014." The paper suggests these uncapped loans increased access to credit for institutions and programs that may otherwise have had to lower tuition or take other measures to appeal to students.[20]

Although the sticker price for undergraduate education has increased, actual out-of-pocket costs for families have risen at a much slower pace. This helps explain why over the past two decades, room and board expenses have risen steadily for all students, but families making below the median income have seen out-of-pocket spending on tuition and fees remain largely stable.[21] Meanwhile, the share of students who received student loans rose from 45.6 to 54.7 percent from 2000 to 2015, with the average annual loan amount rising from $8,840 to $11,610 (in 2017-18 dollars.)[22]

Figure 2: Percentage of college students receiving student loans, 1999-2016

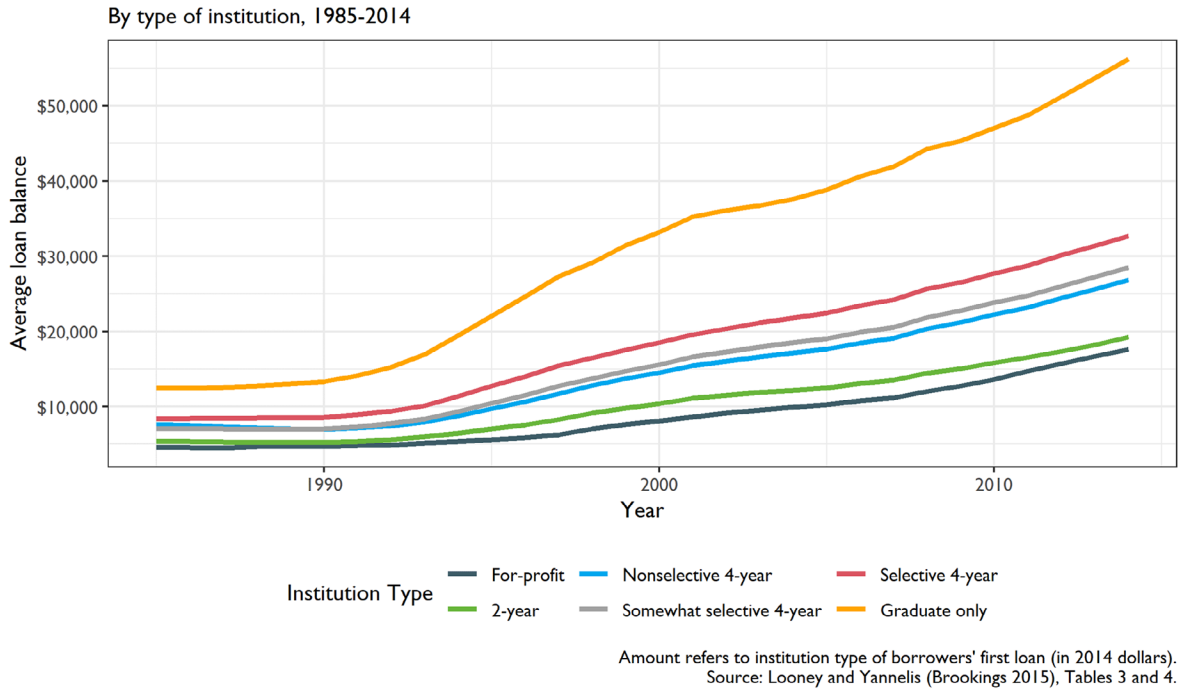



A 2015 Brookings paper provides a closer look at student debt burdens. Using tax data, it finds that median annual borrowing for education-related debt

has gradually risen for undergraduate borrowing since the 1980s, especially for students who attended selective four-year institutions.[23]

Figure 3: Average outstanding federal loan balances upon repayment




As Figure 3 indicates, the bulk of the increase in student debt is driven by graduate loans, on both the intensive and extensive margin. More people are attending graduate school, and taking out more loans to do so. Full-time enrollment in graduate programs increased nearly two-thirds from 2000 to 2018,[24] and the average amount of cumulative borrowing (including undergraduate debt) for those who borrowed for graduate school rose from $62,720 in 2000 to $85,830 in 2016.[25]

### *Repayments and Defaults*

For many people, taking on student loan debt can be a rational decision to smooth consumption over the lifecycle and achieve greater educational attainment with an assumed wage premium.[26] In this sense, education-related debt is a long-term investment, and thus a kind of asset. However, because the rewards to a college degree are uncertain, it is a somewhat-riskier asset with a deferred and variable payoff.[27]

Rising balances may be cause for concern, but less so if increased earnings make it possible to pay the amount owed. However, many students do not graduate, or are

underemployed after graduation. Student loans are generally not dischargeable in bankruptcy and often require payments regardless of income, with some exceptions noted below. “Reflecting this uncertainty, over two-thirds of college students carrying debt report being either very or extremely anxious about their college debts,” found one study.[28]

Meanwhile, default rates are most strongly associated with the earnings profile of the borrower and the institution they attended, not the size of the loan balance.[29] Borrowers with the most debt, often from post-baccalaureate studies or highly selective colleges, are statistically the least likely to default.[30] The Federal Reserve found that adults who attended a for-profit college are nearly three times more likely to be behind in repayment relative to those who attended a public college or university.[31] In short, a Brookings paper notes, if “there is a crisis, it is concentrated among borrowers who attended for-profit schools and, to a lesser extent, 2-year institutions and certain other nonselective institutions”—not the six-figure loan balances from elite programs that receive media attention.[32]

Additionally, as the Urban Institute’s Sandy Baum notes, “Federal student loans are probably the only category of debt for which there is already a system in place to suspend payments when borrowers’ incomes will not support them.”[33] Income-driven repayment (IDR) plans limit monthly payments to a set percentage of income (often 10 percent of income above 150 percent of the federal poverty level) with any unpaid balance forgiven after 20 to 25 years. About one-third of student loan borrowers in repayment are enrolled in an IDR plan, though the current federal structure of these programs is fragmented and often bureaucratically onerous for borrowers.[34] IDR plans offer policymakers a way to target relief to low- and middle-income borrowers in a way that proposals for blanket loan forgiveness proposals do not.

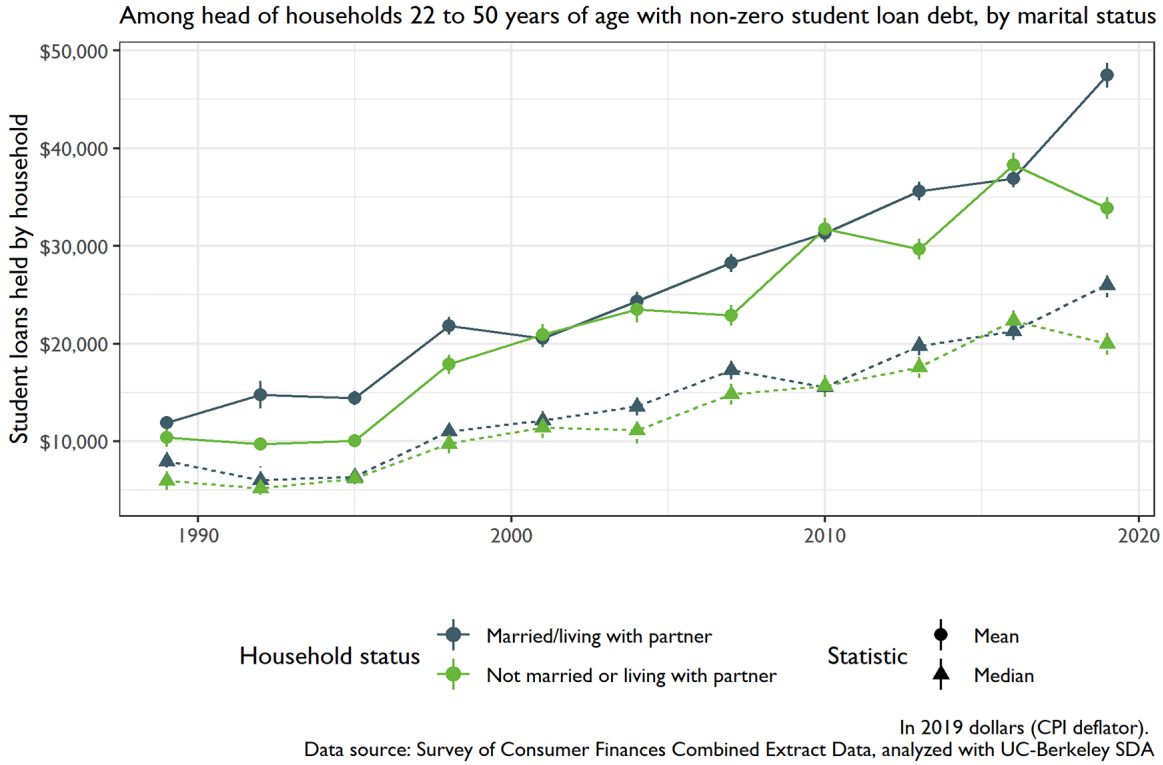
## EVALUATING THE EVIDENCE

Although debt and default rates may not be at crisis levels, the timing of student debt in the lifecycle may merit special consideration. Student loans require repayment in the years after an individual leaves college, which coincides with the prime years for family formation, so debt burdens may be holding young adults back and preventing them from forming families. More young adults than ever before are taking on education-related debt, which could directly affect household formation, delaying marriage and reducing fertility.[35]

Nevertheless, certain facts complicate the story as an explanation for declines in family formation overall: for example, declining marriage and fertility rates predate the large growth in student loans, and occur across all levels of educational attainment.[36] Moreover, whereas in prior generations more-educated women would marry later, the average age at first marriage has increased and converged across all groups by educational attainment.[37]

The Survey of Consumer Finances (SCF) provides relevant descriptive information, and shows the rise in student debt over the past three decades by family type.[38] For households headed by someone aged 22-50, the percentage of households reporting any student loan debt increased from 13.2 to 35.7 percent over the last three decades. [39] In 2019, the average loan balance for married or cohabiting couples (with a head of household below age 50) with any outstanding loans approached $50,000, and this tended to exceed non-married/non-cohabiting households' average loan balance slightly (Figure 4).

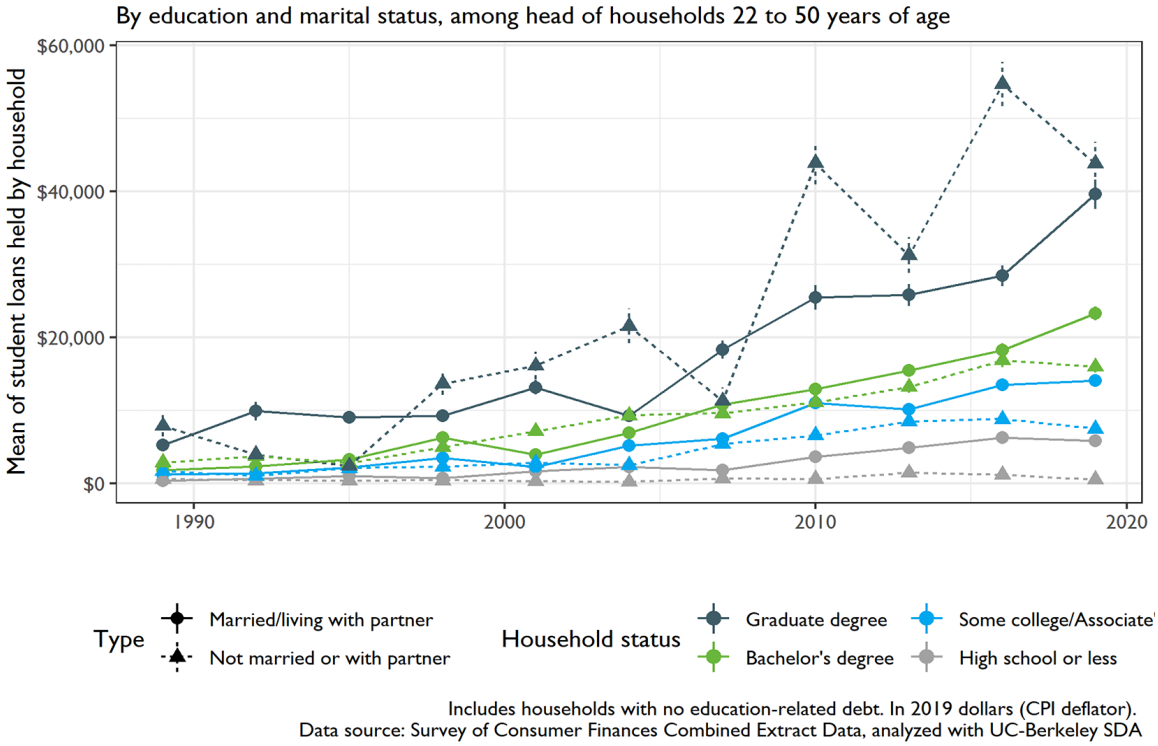
Figure 4: Average value of outstanding student loan balance held by households, 1989-2019




Note: Figure 4 demonstrates how large values in the distribution's tail can pull the average student loan balance upward. In this figure, the mathematical average (mean), is plotted alongside the statistical midpoint of the data (median). The median suggests a much flatter rise in outstanding loan debt than the mean.

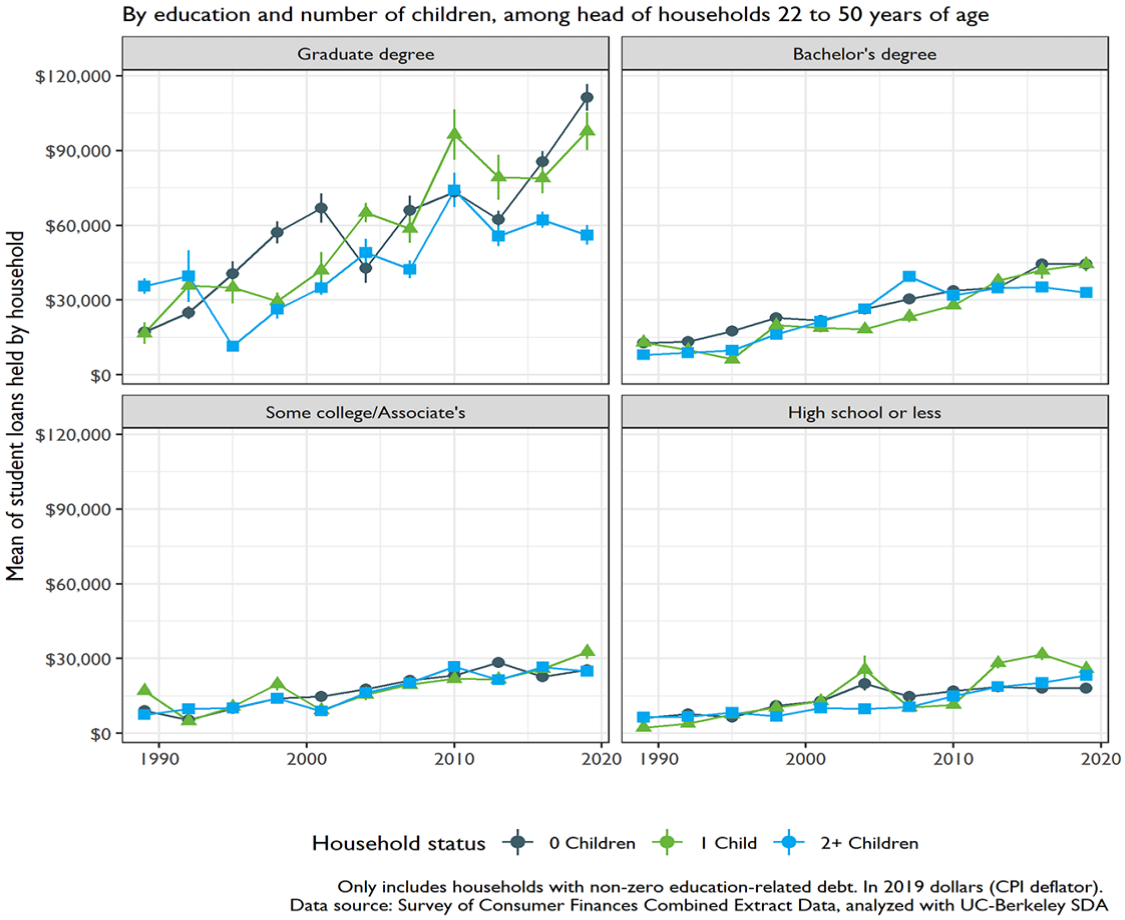
Some individuals may have higher earnings profiles and may pay their loans back more quickly, so Figure 5 includes all households to account for this. Even including all households, married households tend to have slightly more student loan debt than unmarried ones overall. Households headed by a graduate degree holder are the exception to the rule and tend to have lower debt levels if they are married, which is what we would expect to see if graduate degree holders with high loan balances are less likely to marry.

Figure 5: Average value of education loans held by household, 1989-2019




Data sorted by number of children and highest education level attained shows the dramatic increase in student loan debt among graduate degree-holding households, and the highest loan balances are found among childless households (Figure 6). This corresponds to what we would expect to see if high cumulative debt loads had a negative impact on fertility. On the other hand, there appears to be no difference in debt levels across number of children in the household for households with less than a Bachelor's degree. And among households headed by an adult with a bachelor's degree, there may be an emerging differential in debt for families with two or more children compared to families with zero or one child since 2013, but the association between more children and less debt is far from clear-cut.

Figure 6: Average outstanding loan balance among households with student debt, 1989-2019



In summary, descriptive information suggests that graduate degree holders hold the highest average cumulative student loan debt, and graduate degree holders with the highest cumulative debt are less likely to have children or be married. However, disentangling whether those who are more career or self-oriented may be more likely to pursue advanced degrees, avoid marriage, and have fewer kids is a question that simple descriptive analysis cannot answer. And for households with other educational attainment levels, a link between debt and family formation outcomes is far from clear-cut.

The growth in student loan debt may or may not be grounds for a policy response in and of itself, but growing student loan debt would be a more compelling reason for action if researchers understood the relationship between debt and reductions in marriage or fertility more comprehensively. While the previous analysis relied on descriptive analysis, the following sections explore the academic literature on these topics in more detail.

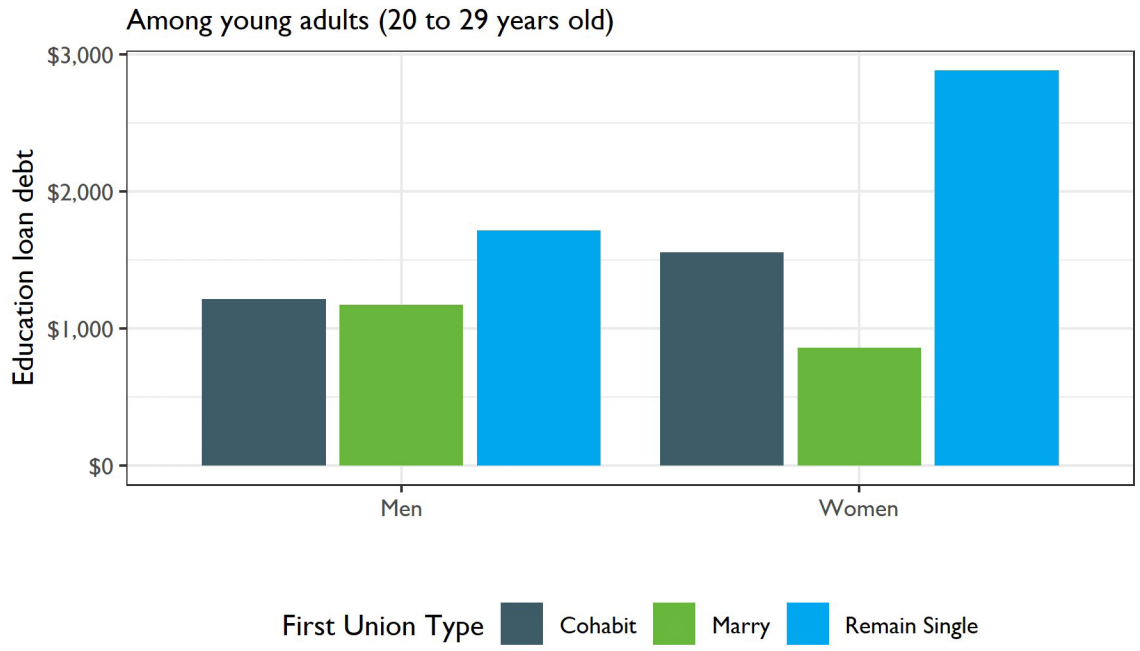
### *Student loan debt and delayed marriage*

The first question is to what degree student loan debt influences marriage rates and timing. Different studies have found suggestive evidence, to varying degrees, that student loans affect marriage. One frequently cited paper found that "controlling for age and education, both men and women are less likely to marry if they hold student loans." However, that study examined the marital choices of college graduates taking the GMAT as a precursor to a graduate business degree, which may reflect some degree of self-selection.[40] Another paper found that female law school graduates with high debt burdens—again, a select group—were more likely to postpone marriage than those with low amounts of debt.[41] An older study found no relationship between debt and marital status, among undergraduates graduating in the early 1990s.[42]

These papers, however, pre-date the Great Recession, during which 14 percent of college students said that they had delayed marriage or a committed relationship because of their student loan burden.[43] A more recent study of undergraduates who entered the job market in the middle of the Great Recession found that each additional $5,000 in student loans was associated with a 7.8 percentage point lower likelihood of having married, which could reflect the credit-constrained, adverse job market graduates faced.[44]

A similar study found student loan debt is linked to delayed marriage, especially for women, those majoring in health care, residents of areas with higher unemployment rates, and for graduates with more educated parents.[45] While these studies face some methodological questions, they suggest that student loans did not negatively affect marriage decisions in prior generations, but may do so now.[46]

Fig. 7 Mean educational loan debt held by first union type, by sex




From NLSY97 (updated to 2020 dollars (CPI).) Source: F. Addo, Demography (Oct. 2014) 51(5), Table 1.

Ethnographic work suggests that debt could be considered a barrier to marriage but not cohabitation.[47] Drawing on Andrew Cherlin's work on the "deinstitutionalization of marriage,"[48] University of Wisconsin sociologist Fernanda Addo notes that in marriage, individual debts brought into a union become the responsibility of both members, whereas in less-formal relationships, like cohabitation, the debt remains the responsibility of the individual who incurred it. "If young adults prefer to be financially established prior to marriage, cohabitation will be more likely if debt is high, and marriage will be more likely if debt is low or nonexistent."[49]

Using the National Longitudinal Survey of Youth (NLSY), Addo finds that young women who cohabited before marriage were most likely to have student debt, while young women who married without cohabitation had the lowest average student debt load. She estimates that each additional 1 percent in student loan debt is associated with a 2 percent reduction in the likelihood of being married for women. However, no similar pattern existed for men.[50]

Another paper found a similar estimate, with each additional $1,000 in debt tied to a one percent decline in likelihood of marriage, but again "the negative relationship between remaining debt and the odds of first marriage held for women only." The authors note that "there are fewer college-educated men in the population, and so their demand in the marriage market may trump their earnings or debt as signals of marriageable mates."[51]

Different logic could be at work for young men and young women.[52] For instance, some couples contemplating starting a family may believe that the woman is more likely to withdraw from the labor force after childbirth, at least temporarily, which could lead men to have a preference for relatively debt-free spouses. This could lead to a preference for cohabitation while there is debt outstanding, as financially-independent individuals progress towards marriage without taking on the joint burden of assuming each other's debts in marriage.

Importantly, Addo finds that marriage rates following a period of cohabitation remain unrelated to student debt. Instead, she finds suggestive evidence that increasing debt balances have only reduced "direct marriage (and not marriage preceded by cohabitation)" for young women.[53]

It may be that student loan debt is not leading young women to opt for cohabitation over marriage, but student loan debt is introducing premarital cohabitation as an extra stop on the pathway to marriage. This could contribute to the increasing average age at first marriage and reduce the number of years available to couples who wish to have children in wedlock, as cohabitation is a less-stable type of union.[54]

*Student loan debt and reduced fertility*

In addition to student loan debt's relationship with marriage, the relationship between student loan debt and fertility is an important question for family affordability. However, in this area research has struggled to find a consistent story, with multiple scholars failing to reach consensus on the direction or magnitude of any impact. A 2019 working paper found student loan balances were not statistically significantly associated with fertility in the first four years after graduation.[55] Another paper, resting on controvertible assumptions, found each additional $5,000 in student loan debt was associated with graduates being 5 percentage points less likely to have a child, though the finding was only statistically significant for females.[56]

One of the more reliable papers to examine the question uses the NLSY, and finds each additional $1,000 in student loans is associated with a 1.2 percent decrease in the annual likelihood of having a child. Women with $60,000 in student loan debt were 42 percent less likely to have a child in any given year compared to women with no debt (2.5 percent likelihood, compared to 4.3 percent.)[57] "Student loans may not have noticeable effects on fertility at moderate levels," the paper notes, but "these effects can be quite substantial at high levels." But most student loan balances do not approach that magnitude—only 9 percent of women at age 25 had outstanding loans that large in their sample.

The authors note the importance of self-selection, and the fact that women who choose to pursue advanced degrees may be "qualitatively different, and that the career payoff compensating for this level of debt may take even longer than for more moderate debt levels." Women with high levels of debt, often

due to graduate school, may be making an intentional tradeoff between early career advancement and fertility. In sum, the authors find, it is "unlikely that indebtedness would be sufficiently large (for most) to significantly change the decision to have children at all, but may affect the timing of fertility."[58]

There may be another factor contributing to the limited relationship between student loan debt and fertility—especially as compared to the intentionality behind a decision to get married, "the transition to parenthood can occur even in cases where individuals have not planned to become parents, and thus material readiness may not always be the most salient factor predicting the transition. This potential for accidental transitions may in effect diminish the role of financial security."[59]

Other factors beyond a person's control can also impact the decision to become a parent as well—when Robb and Schreiber control both for household income and macroeconomic conditions, "student loans are not significantly associated with the transition to parenthood."[60]

## POTENTIAL AVENUES FOR POLICYMAKERS

The evidence suggests that the decision to marry may be impacted by our ongoing shift to a debt-financed model of human capital formation, with a more tenuous case that student debt may impact parenthood, as well. The reasons behind this shift, which could include greater emphasis on professional fulfillment over marriage and higher opportunity costs to parenthood, may be beyond the ability of policy to affect directly.

But opportunities exist to shift existing policies on the margins to make it less difficult for individuals who want to form families to do so. Policymakers could make it easier for individuals to weigh the trade-offs associated with higher education, promote competition in higher education, and reform payment options to make it more affordable for individuals to have a family and pursue their education.

One potential option is to double the student debt interest deduction in the tax code from $2,500 to $5,000 for married filers, ensuring that couples do not face an implicit penalty in choosing to marry.[61] The Lifetime Learning Credit, which allows taxpayers to deduct qualified education-related expenses such as tuition and textbooks, is currently capped at $2,000 per return; it could also be doubled for married filers to minimize associated marriage penalties.[62] However, if policymakers are interested in rectifying the root of the issue, then they should eliminate marriage penalties and check tuition costs through removing the tax structures that create these issues in the first place.

Streamlining income-driven repayment (IDR) could be an easier way to direct assistance to those in difficult financial circumstances.[63] IDR, which sets monthly student loan payment at an amount deemed "affordable" based on income

and family size, can be improved for newly-married households and those with children. Repayment plans tied to income have been implemented in Australia, New Zealand and the United Kingdom,[64] and have been supported conceptually by economists from Milton Friedman to James Tobin, two Nobel laureates who occupied opposing ends of the political spectrum.[65]

Multiple pieces of legislation that would streamline the current mix of four IDR options into one, simplified program have been introduced on both sides of the aisle and included in the President's budget in FY2018, FY2019, and FY2020.[66] Importantly for the purposes of this paper, income-driven repayment programs often penalize couples upon marriage. Under current law, married couples that file jointly would have a higher adjusted gross income (AGI), and therefore a higher amount owed, than if they hadn't married, and could possibly become ineligible for IDR (couples can still file separately, but would lose out on other benefits of joint filing). Any reform of IDR programs should find ways to soften marriage penalties for couples filing jointly, such as introducing a set-aside of some spousal income in calculating joint AGI, doubling the IDR eligibility cutoff for newly-combined incomes, or otherwise adjusting the expected contribution for families in IDR programs.

More broadly, eliminating marriage penalties in the tax code or further increasing the Child Tax Credit would be a way to provide benefits to all families, regardless of student loan balance.[67] Not all of the steps to address any effects of student debt on family formation need come from Washington, D.C. Given the balance of evidence shows student loan burdens associated with declines in marriage, philanthropic organizations and private industry could focus some efforts on providing interest rate reduction or balance forgiveness following a marriage. University administrations, especially in graduate programs, could ensure that stipend or financial aid calculations are adjusted for household size, and expand the generosity of financial supports and services for families to better support students that choose to marry or have children in school.[68]

While this paper focuses specifically on student debt as it relates to family formation, multiple proposals have been introduced to make higher education more affordable across the board. Notably, the *Higher Education Reform Opportunity* (HERO) Act introduced by JEC Chairman Sen. Mike Lee, proposes a number of policy mechanisms to lower college costs through increased competition and transparency.

The HERO Act would lower barriers to entry for new educational models by encouraging accreditation reform to allow for innovative, non-traditional approaches to credentialing; building on ongoing efforts to make transparent scorecards available on earnings by major and by institution, making it easier for students and their parents to "comparison shop" across competing programs; consolidating and capping existing student loan programs; and introducing a "skin-in-the-game" measure for universities and colleges.[69]

Capping or eliminating PLUS loans, including Parent-PLUS loans for post-baccalaureate students and Grad-PLUS loans, could also instill more discipline in graduate school debt.[70] Congress could restrict or eliminate Parent-PLUS loans, which encourage families with undergraduates to take on debt and serve as "a no-strings-attached revenue source for colleges and universities, with the risk shared only by parents and the government."[71] A bolder step would be to introduce per-student, per-year caps into federal student loan programs; the Heritage Foundation estimates such a plan could reduce total federal student lending by one-third.[72] Introducing more price discipline to higher education could take the form of ensuring that career and technical education pathways, such as registered apprenticeships, are available to young adults who want to pursue careers that do not require degrees.[73]

Another alternative could include broadening access to income-share agreements (ISA), which offer an alternative pathway to financing higher education, particularly for students studying majors in high demand.[74] As opposed to IDR, ISAs do not entail taking on a balance or paying interest; instead, a student promises to pay a certain percentage of their future income to an investor. Some institutions, notably Purdue University, have begun to offer ISAs for certain fields of study.[75] Congress could clarify that it is acceptable for schools to provide ISAs, as proposed last Congress by Senator Young.[76]

## CONCLUSION

Our current model of human capital formation has the potential to subtly nudge young adults to put off pursuing meaningful relationships, marrying, and becoming a parent. We should be creative in exploring alternatives, whether it be income-driven repayment, making marginal changes in the tax code, increasing options both inside and out of traditional higher education, and providing more social support for parents.

But a problem can be a problem without being a crisis. Relying on outlier-inflated means as an excuse for forgiving large amounts of student debt paints a misleading picture. The decisions of individuals to put off marriage or parenthood while pursuing a medical, business, law, or graduate degree is important to distinguish from a popular narrative that paints a rising tide of red ink preventing the modal young adult from starting a family.[77]

Policymakers should keep the goal of broadening the choice set available to individuals in mind. The steps suggested in this paper could make it easier for all young adults to pursue appropriate education without being burdened by debt and having to sacrifice other, invaluable, parts of life in the process.

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