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INVESTING IN OUR CHILDREN: A NOT SO RADICAL PROPOSAL

*Donald B. Tobin**

I. INTRODUCTION

The United States is currently under-investing in the human capital of its children. This significant investment deficit threatens both our children's vitality and the nation's ability to compete in a knowledge-based economy. At all income levels, investment in children—in education, housing, training, and nutrition—has significant long-term beneficial returns for both the recipients of the investment and for society as a whole. This Article proposes that the nation shift the focus of its current fiscal policies towards human capital investment in children. This Article advocates a self-sustaining investment program that delivers resources directly to children and that children are required to repay when they start working. It relies on the economic literature on human capital, the educational literature on the impact of money on childhood attainments, and the political theory literature on civic responsibility to help justify the self-sustaining investment program implemented through the tax code. This Article seeks to promote new ways of evaluating our current programs and policies and to facilitate further discussion about a child-centered investment strategy.

Politicians generally agree that helping our children is an important national priority. While some policies and reforms have proved beneficial, the path policymakers are currently taking to improve the lives of children is inadequate. Over one fifth of the population of children is poor or near poor, yet Congress continues to under-fund programs that invest in children and to reduce funding for many of the safety net programs specifically designed to ensure that children remain out of poverty.¹

* Assistant Professor of Law, Michael E. Moritz College of Law, The Ohio State University. I would like to thank James Brudney, Marc Spindelman, Douglas Berman, Steven Huefner, Dale Oesterle, Allan Samansky, Paul Caron, the participants in the Ohio Legal Scholarship Workshop, and the faculty workshop of the University of Dayton School of Law for their helpful comments and advice, and my research assistants, Jason Job, Elizabeth Willoughby, Steve Toth, and Jessica Carvey.

1. Over 16.2 million children, 22.3% of the total population of children, live in poverty or near poverty, and of that 22.3%, 6.9% live in severe poverty. BERNADETTE D. PROCTOR & JOSEPH DALAKER, *POVERTY IN THE UNITED STATES: 2002*, at 12 (U.S. Census Bureau, Pub. No. P60-222, 2003), available at <http://www.census.gov/prod/2003pubs/p60-222.pdf>. Near poverty is defined as people with incomes under 125% of the poverty threshold. *See id.* at 9. Severe poverty is defined as families with incomes below

The decision about how heavily to invest in children affects far more than simply those children who live in poverty. At all income levels, investment in children—in education, housing, training, and nutrition—has significant beneficial returns for both the recipients of the investment and society as a whole.² Children in low, moderate, and upper-income families all benefit from increased investment in their human capital. With the exception of families with extremely high incomes, families from a broad range of socioeconomic classes struggle to provide their children with adequate child care, health care, housing, and education.³

Despite fairly strong evidence that investing in human capital will produce beneficial results, the United States has failed to invest adequately in children. During the past 20 years, and especially in the last 10 years, the United States has relied heavily on tax cuts and market mechanisms to create economic incentives for families with children. Because many of the children most in need of investment live in low- or moderate-income families, tax cuts and market mechanisms often leave them behind. Tax cuts for education, which are designed to increase

half of the poverty threshold. *Id.* at 9. In 2002, the severe poverty rate for a head of household with two children would be \$7,247. *See id.* at 4. The poverty rate is not adjusted geographically, so families in high cost areas may be significantly worse off than the statistics indicate. Some scholars have argued that the poverty rate is not the right measure of poverty and that it underestimates poverty. *See* Robert Greenstein et al., Center on Budget and Policy Priorities, *Bearing Most of the Burden: How Deficit Reduction During the 104th Congress Concentrated on Programs for the Poor* (Nov. 26, 1996), available at <http://www.cbpp.org/104TH.HTM>; Donald J. Hernandez, *Poverty Trends*, in CONSEQUENCES OF GROWING UP POOR 18 (Greg J. Duncan & Jeanne Brooks-Gunn eds., 1997). This level of poverty is not an inevitable result of the capitalist system. The poverty rate in the United States is significantly higher than Canada, the United Kingdom, or Germany. *See* MICHAEL J. GRAETZ & JERRY L. MASHAW, TRUE SECURITY: RETHINKING AMERICAN SOCIAL INSURANCE 117-18 (1999). For a study of poverty rates among various industrialized countries see UNICEF: INNOCENTI RESEARCH CENTRE, A LEAGUE TABLE OF CHILD POVERTY IN RICH NATIONS 17 (2000) (finding the United States was one of the worst performing countries with the second to highest poverty rate of the 23 countries surveyed).

2. *See* GARY S. BECKER, HUMAN CAPITAL: A THEORETICAL AND EMPIRICAL ANALYSIS, WITH SPECIAL REFERENCE TO EDUCATION 109 (3d ed. 1997); SUSAN E. MAYER, WHAT MONEY CAN'T BUY: FAMILY INCOME AND CHILDREN'S LIFE CHANCES 110 (1997) ("increasing housing environment index by a standard deviation increases four- and five-year-olds' PPVT [Peabody Picture Vocabulary Test] scores by 2.16 points"); THEODORE W. SCHULTZ, THE ECONOMIC VALUE OF EDUCATION 53, 65 (1963) [hereinafter SCHULTZ, VALUE OF EDUCATION] (human capital investment through education); Theodore W. Schultz, *Investment in Human Capital*, 51 AM. ECON. REV. 1, 1-17 (1961) [hereinafter Schultz, *Human Capital*] (discussing health, job training, and education as forms of human capital investment); *see also infra* note 17.

3. *See* ROBERT J. MILLS & SHAILESH BHANDARI, HEALTH INSURANCE COVERAGE IN THE UNITED STATES: 2002, at 2 (U.S. Census Bureau, Pub. No. P60-223, 2003) (indicating that 7 million people with income over \$75,000, almost 7 million with incomes between \$50,000 and \$75,000, and over 14.5 million with incomes between \$25,000 and \$50,000 were without health insurance in 2002), available at <http://www.census.gov/prod/2003pubs/p60-223.pdf>. For a look at middle-class families with no health insurance, *see* Stephanie Strom, *For Middle Class, Health Insurance Becomes a Luxury*, N.Y. TIMES, Nov. 16, 2003, § 1, at 33.

investment in children, barely help middle-income families and are of no help to poor families who pay little or no income tax.

Furthermore, although there is a significant economic benefit both for individuals and society in investing in children, the market will not, and cannot, supply the needed investment. Children are too much of an investment risk. Banks have little or no certainty of repayment and cannot take a security interest in a child's future.⁴ But if investing in children now will produce positive returns in the future, then some type of mechanism should exist to provide the needed investment. In many ways, children are like start-up companies seeking venture capital. They are a risky investment, but the potential rewards from success are very great. A venture capitalist knows that many of his investments will not succeed, but also knows (or at least hopes) that some will hit the jackpot. He is willing to take on a risky investment because the potential returns from the investment are great.

In this Article, I propose a program designed to shift the focus of our current fiscal policies towards investment in children.⁵ I advocate a federal investment program that delivers resources directly to children and that children are required to repay when they start working.⁶ The program will create Child Investment Funds to provide every child under the age of 15 with a yearly cash payment of approximately \$2,000.

I focus on investment payments directly to children for two main reasons. First, if the payment is made directly to children, and the payment belongs to the children, there is a greater chance that the funds will be invested in the child.⁷ Second, recent programs providing

4. BECKER, *supra* note 2, at 291 ("poor families often have difficulty financing investments in children because loans to supplement their limited resources are not readily available when human capital is the collateral."); DANIEL SHAVIRO, DO DEFICITS MATTER? 154-57 (1997) (discussing argument that parents might increase investment in child's education if parent could share in the benefits).

5. See Aletha C. Huston, *Children in Poverty: Developmental and Policy Issues*, in CHILDREN IN POVERTY: CHILD DEVELOPMENT AND PUBLIC POLICY 1, 4 (Aletha C. Huston ed., 1991) (noting that most discussions regarding possible solutions to children's poverty center on influencing adults).

6. The basic payback, which is discussed in more detail in Part IV.A *infra*, requires children (as a group) to pay back the amount they received plus interest. Because I assume that general tax revenues will increase because of wage growth, I use an interest rate tied to the inflation rate. Thus, children need to pay back what they received in inflation-adjusted dollars, but they are not required to pay market rate interest. See EDWARD F. DENISON, TRENDS IN AMERICAN ECONOMIC GROWTH 1929-1982, at 15 (1985) (finding that education per worker accounted for 16% of growth in output in nonresidential business); KJELL A. CHRISTOPHERSEN & M. HENRY ROBISON, STATE OF ILLINOIS, THE SOCIOECONOMIC BENEFITS GENERATED BY 39 COMMUNITY COLLEGE DISTRICTS IN ILLINOIS I (2002) (finding that taxpayers receive 13.8% return on their annual investments in community colleges), available at <http://www.iccb.state.il.us/HTML/pdf/econimpact/92002IllinoisAggFinalES.pdf>.

7. There is, for example, no requirement that parents invest the Child Tax Credit, the Earned Income Credit, or amounts saved from the Dependency Exemption on their child. See I.R.C. § 24 (West

assistance to families with children often include significant restraints on parental behavior, and families can lose essential benefits when parents run afoul of these controls. This loss of benefits significantly impacts a family's ability to invest in its children. This child-centered program reorients attention away from punishing parental behavior and towards investing in children.⁸

At first, a program that provides cash payments directly to children may seem like a radical proposal. However, it will become clear that this approach is not so radical after examining the program in light of the economic literature on human capital theory and the educational literature on childhood attainments. Moreover, the nation's current policies to provide subsidies to children or families, and other proposals to provide such assistance, also allow the reader to evaluate the feasibility of this proposal. Additionally, examining current policies through the lens of human capital theory and investment in children will shed new light on those policies.

The model I propose is at least partially based on the rational economic choice a child would make in the marketplace if he or she were able. Rational lower-income or middle-income children would often choose to borrow money now to invest in their own human capital. Poor children clearly would borrow money now to ensure that they had adequate food and shelter. As we have seen with student loans, middle-class children routinely borrow money to invest in their education. The problem here is that without intervention the market will not make many of these loans. The risk of default is simply too great absent an extremely large pool of borrowers and an easy systematic way of collecting.⁹

This Article presents a road map for creating a permanent self-sustaining program to close the investment gap facing our children. No

2002 & Supp. 2004) (Child Tax Credit); *id.* § 32 (Earned Income Credit); *id.* § 152 (dependency exemption).

8. Since the purpose of this proposal is to provide human capital investment to all children, the program is not means tested and is available to all children. In addition, the benefit is available to the child regardless of a guardian's behavior or actions. Even if one concludes that punitive measures are appropriate to encourage welfare recipients to get off welfare or to discourage drug use, punitive measures towards children of those recipients are not appropriate. The three-year-old child of a welfare mother did nothing to deserve his or her poverty and certainly did nothing to warrant the removal of benefits, but it is the child who likely will suffer the most from the elimination of welfare benefits. As discussed in Part IV.A.2 *infra*, my proposal contains safeguards to ensure that unfit parents have no control over the child's payment. In this regard, the proposal helps shift our current focus away from normative judgments about parental behavior.

9. See BECKER, *supra* note 2, at 291; GARY BECKER, A TREATISE ON THE FAMILY 247-48 (1991) [hereinafter BECKER, FAMILY]; Lynn A. Stout, *Some Thoughts on Poverty and Failure in the Market for Children's Human Capital*, 81 GEO. L.J. 1945, 1947 (1993) (finding that the market for "children's human capital may be rife with imperfections" that encourage under-investment in children).

initial project can, or should, address all the technical questions, concerns, or objections that a program of this magnitude necessarily raises, and no author can create a perfect plan. I hope that this project will encourage people to examine our current programs and policies in a new way and will open a dialogue for further discussion about a self-sustaining child-centered investment program.

Part II examines the economic problems facing children in the United States and explains why the proposed program is necessary. In presenting the basic theory behind the program, Part II relates my proposal to the economic literature on human capital, the educational literature on the impact of money on childhood attainments, and the political theory literature on civic responsibility. Part III consists of a brief description of existing subsidies to children or families with children and presents programs and policy ideas that can be drawn upon for guidance in creating a self-sustaining investment program for children. It also examines current policies and programs through a lens of investment in children. In Part IV, I detail my proposal for investment assistance to children—a universal cash assistance program with a commensurate payback. This Part also addresses alternative models including a voluntary program with more risk-based financing and a direct loan approach that allows each person to take out a government-backed human capital loan. Part IV also responds to some of the concerns and criticisms that will be raised regarding my proposal.

II. ECONOMIC, EDUCATIONAL, AND POLITICAL THEORY ARGUMENTS FOR INVESTING IN CHILDREN

The country is failing its children. The current political and economic climate in the United States has left millions of children behind, with substandard child care, health care, housing, education, and training.¹⁰ The problem of under-investment in children is not, however, just a problem for poor children. As education, health care, housing, and child care costs rise, more families are finding it harder to make ends meet and to provide adequately for their children.¹¹ A recent report by

10. See MILLS, *supra* note 3, at 2 (8.5 million children have no health insurance); FED. INTER-AGENCY FORUM ON CHILD AND FAMILY STATISTICS, AMERICA'S CHILDREN: KEY NATIONAL INDICATORS OF WELL-BEING 2003, at 19, 92 (2003) (finding that, in 2001, 36% of U.S. households with children had one or more indicators of housing problems—physically inadequate housing, crowded housing, or housing that cost more than 30% of household income), available at <http://www.childstats.gov/ac2003/pdf/ac2003.pdf>; *id.* at 49, 115 (44% of children age 3 to 5 do not participate in early childhood care and educational programs).

11. See MARK LINO, U.S. DEP'T OF AGRIC., EXPENDITURES ON CHILDREN BY FAMILIES, 2002, at ii (2003) (discussing the costs of raising children), available at <http://www.usda.gov/cnpp/crc/>

the U.S. Department of Agriculture indicates that a middle-income family with two children and a household income of \$52,900 will spend almost \$20,000 per year on their children.¹²

The problem of inadequate investment in children impacts the child, his or her family, and society as a whole. Children cannot learn if they are hungry, malnourished, or in unstable environments.¹³ A child's potential is not recognized if he must forgo further education because it is too expensive or inaccessible.

This Part considers the theoretical and policy justifications for a self-sustaining child investment program. First, it discusses the economic theory and principles that indicate investing in the human capital of children is an economically wise proposition. It is not only essential for the child to succeed in an ever transforming knowledge-based economy, but it is also necessary for society to continue to grow and prosper as the economic climate in the United States is transformed from a manufacturing economy to a skills-based economy. Second, this Part addresses some of the societal justifications and theories for an investment program, and third, it examines political theories that should encourage investment programs aimed at children.

A. Economic Justifications for Investing in Children

The consequence of under-funding investment in children is that the human capital of the next generation suffers. In their groundbreaking work starting in the 1960s, Gary Becker and Theodore Schultz, working separately in a series of articles, formalized the human capital theory in economics.¹⁴ This theory provides the basis for understanding why

crc2002.pdf; CARNEGIE CORPORATION OF NEW YORK, *STARTING POINTS: MEETING THE NEEDS OF OUR YOUNGEST CHILDREN* (1994) (discussing high cost of quality child care); *see also* COLLEGE BOARD, *TRENDS IN COLLEGE PRICING 2004* (n.d.) (discussing the increase in college pricing and its affordability), available at <http://www.collegeboard.com/research/home/>; TERESA A. SULLIVAN ET AL., *THE FRAGILE MIDDLE CLASS: AMERICANS IN DEBT* (2000) (discussing the economic stress facing middle class families); ELIZABETH A. WARREN & AMELIA WARREN TYAGI, *THE TWO-INCOME TRAP: WHY MIDDLE-CLASS MOTHERS AND FATHERS ARE GOING BROKE* (2003) (noting two-income families are barely meeting their basic expenses).

12. MARK LINO, *supra* note 11, at ii (families with incomes less than \$39,700 spend approximately \$7,080 per child, families with incomes between \$39,700 and \$66,900 spend approximately \$9,660 per child, and families with incomes over \$66,900 spend approximately \$14,133 per child).

13. Shahin Yaqub, *Poor Children Grow into Poor Adults: Harmful Mechanisms or Over-Deterministic Theory?*, 14 J. INT'L. DEV. 1081, 1084 (2002) (reviewing findings of other scholars and concluding that poor nutrition impacts attention spans, motivation, memory, and school attendance).

14. BECKER, *supra* note 2; SCHULTZ, *VALUE OF EDUCATION*, *supra* note 2; Schultz, *Human Capital*, *supra* note 2.

investment in children is necessary and why such investment is beneficial to people throughout the socioeconomic scale.

1. Overview of Human Capital Theory and Investing in Children

Human capital theory recognizes that people are themselves capital. Just like plant and equipment, personal attributes and skills create value-added capital that is used to increase personal output. In a series of lectures and articles, Becker and Schultz developed and analyzed the different types of investments that increase human capital. Principally, Becker and Schultz recognized that education and training provide significant increases in human capital and significant increases in income.¹⁵ On a simple level, this can be seen by analyzing the median wage by educational attainment. In the United States in 2002, the median wage for someone who had not completed high school was \$19,205, for high school graduates was \$26,795, for college graduates it was \$50,623, and for people with professional degrees it was \$101,375.¹⁶ Although estimates vary, it has generally been found that the return on a person's investment in education exceeds ten percent.¹⁷

Similar conclusions regarding the benefits of investment in human capital were reached with regard to training and health care.¹⁸ Obviously, someone who is sick and cannot work or someone who is trained only for menial work will have difficulty earning a decent wage. A similar problem exists for children in poverty, whose human capital is being destroyed by inadequate nutrition, housing, education, and health care.

15. SCHULTZ, VALUE OF EDUCATION, *supra* note 2, at 46, 53, 65; Theodore W. Schultz, *Reflections on Investment in Man*, 70 J. POL. ECON. 1 (1962); see also Orley Ashenfelter & Cecilia Rouse, *Schooling, Intelligence, and Income in America*, in MERITOCRACY AND ECONOMIC INEQUALITY 89 (Kenneth Arrow et al. eds., 2000) (recognizing and rejecting the argument that "[e]ducation does not generate higher incomes; instead, individuals with higher ability receive more education and more income").

16. BUREAU OF LABOR STATISTICS AND BUREAU OF THE CENSUS, CURRENT POPULATION SURVEY: ANNUAL DEMOGRAPHIC SURVEY (March Supp. 2002), available at http://ferret.bls.census.gov/macro/032002/perinc/new04_001.htm.

17. Orley Ashenfelter & Alan Krueger, *Estimates of the Economic Return to Schooling from a New Sample of Twins*, 84 AM. ECON. REV. 1157, 1157 (1994) (finding that "an additional year of schooling increases wages by 12-16 percent"); Ashenfelter & Rouse, *supra* note 15, at 92 (estimating a 10% return on investing in education); see also BECKER, HUMAN CAPITAL, *supra* note 2, at 7; SCHULTZ, VALUE OF EDUCATION, *supra* note 2, at 62; CHRISTOPHERSEN & ROBISON, *supra* note 6 (students have a 26.1% rate of return on their investment in college). See generally GEORGE PSACHAROPOULOS & HARRY ANTHONY PATRINOS, RETURNS TO INVESTMENT IN EDUCATION: A FURTHER UPDATE (World Bank Policy Research, Working Paper No. 2881, 2002) (discussing the issue of and reviewing the return to investment in education in various countries); OECD, EDUCATION AT A GLANCE: OECD INDICATORS 2002, at 124-25 (2002) (There is a strong positive correlation between educational attainment and earnings.).

18. Schultz, *Human Capital*, *supra* note 2, at 9-10.

What human capital theory indicates is that people with less investment in human capital generally will make less money and be less successful. Greater investment in human capital should lead to a better trained and educated work force that is more productive and better able to earn a liveable wage. In the current economic environment, however, there is an investment gap. Poor and middle-class parents often need to spend most of their money on current consumption and thus have less money to invest in their children's human capital.¹⁹ So even though investment in human capital will pay long-term dividends (at least for their children), parents may not be making the investment because their economic survival takes precedence over investing in their children.

In some cases, there is an under-investment in a child's human capital because a parent needs the money for economic survival. In other cases, there may be under-investment due to current consumption preferences by the parent. In light of the above, a rational child, or at least a rational child with advice from a rational adult, would choose as much investment in education, training, food, and health as was possible based on his economic situation.²⁰ We see that today as students attempt to obtain higher education even as the cost of education rises. Students consistently borrow large sums of money betting on the human capital theory of economics. They are betting that the large debt they are taking on is worth it, because their future wages will be sufficient to cover the debt burden. In most cases, this is a sound decision by students.

It also would be rational for a young child to borrow money to ensure he was adequately clothed, fed, and housed. He could predict that by investing in himself now he would be better able to learn in school, have less chance of dropping out, and have a higher chance of success. Of course, there are not student loans for young children,²¹ but as I propose

19. Mary Corcoran & Terry Adams, *Race, Sex, and the Intergenerational Transmission of Poverty, in CONSEQUENCES OF GROWING UP POOR*, *supra* note 1, at 462; see BECKER, FAMILY, *supra* note 9, at 5, 244-47, 302 (Parents must allocate between children's human capital and current consumption.).

20. BECKER, FAMILY, *supra* note 9, at 244 (discussing human capital investment for children, Becker argues that the proper level of investment would assume that parents can maximize the welfare of their children by borrowing whatever is necessary to maximize the net income of their children).

21. We do, of course, have public education. As a society, we recognize the importance of investing in the human capital of children by publicly financing public schools. Although the system of financing public education has its own serious problems, public education is designed to ensure that all children have at least a basic level of education. Public schools also highlight the problem of inadequate investment in children, as the quality of public education varies dramatically by the economic demographics of a particular area. Children in poorer demographic areas often receive lower-quality education, further stratifying the different levels of human capital investment.

here, it might be appropriate to provide human capital loans for young children.²²

2. Empirical Evidence Supporting Human Capital Investment in Children

Empirical evidence supports Becker and Schultz's hypothesis that investment in human capital will pay dividends,²³ but the focus of most of that research has been on adults.²⁴ Scholars in education, however, have examined the impact that income and poverty have on a child's ability to achieve. Combining human capital theory with their research, it is clear that increased income allows families to invest more in their children and results in higher educational attainment and a lessening of other risk factors.

For example, recent studies indicate that poverty in childhood adversely impacts a child's ability to achieve and that persistent poverty is particularly harmful.²⁵ Poor children are more likely to have to repeat a grade, to drop out of high school, and to have out of wedlock births.²⁶ In addition, children living in poverty are more likely to experience

22. BECKER, HUMAN CAPITAL, *supra* note 2, at 291 ("poor families often have difficulty financing investments in children because loans to supplement their limited resources are not readily available when human capital is the collateral. Such capital market restrictions lower investments in children from poorer families.")

23. BECKER, HUMAN CAPITAL, *supra* note 2, at 161-251. *See generally* Jacob Mincer, *On the Job Training: Costs, Returns, and Some Implications*, 70 J. POL. ECON. 50 (1962) (job training and human capital); Burton A. Weisbrod, *Education and Investment in Human Capital*, 70 J. POL. ECON. 106 (1962) (discussing human capital investment in education); Selma J. Mushkin, *Health as an Investment*, 70 J. POL. ECON. 129 (1962) (argues that investing in health is an investment in human capital).

24. *See supra* note 23; *see also* Huston, *supra* note 5, at 4-6.

25. *See* Thomas L. Hanson et al., *Economic Resources, Parental Practices, and Children's Well-Being, in CONSEQUENCES OF GROWING UP POOR, supra* note 1, at 190 (reviewing the literature and finding that children from "economically disadvantaged families exhibit lower levels of physical development, cognitive functioning, academic achievement, self-esteem, social development, and self control than do children from more advantaged families"); *see also* Greg J. Duncan & Jeanne Brooks-Gunn, *Family Poverty, Welfare Reform, and Child Development*, 71 CHILD DEV. 188, 188 (2000) [hereinafter Duncan & Brooks-Gunn, *Family Poverty*] (concluding that "deep or persistent poverty early in childhood affects adversely the ability and achievement of children"); Greg J. Duncan et al., *Economic Deprivation and Early Childhood Development*, 65 CHILD DEV. 296, 296 (1994) (even accounting for other differences between low and high-income families, family income and poverty strongly correlate with cognitive development); Glen H. Elder, Jr. et al., *Linking Family Hardship to Children's Lives*, 56 CHILD DEV. 361 (1985); Greg J. Duncan, *The Economic Environment of Childhood, in CHILDREN IN POVERTY: CHILD DEVELOPMENT AND PUBLIC POLICY, supra* note 5, at 40-46 (finding that poverty has a negative impact on child attainments); CRAIG T. RAMEY & FRANCES A. CAMPBELL, *Poverty, Early Childhood Education, and Academic Competence: The Abecedarian Experiment, in CHILDREN IN POVERTY: CHILD DEVELOPMENT AND PUBLIC POLICY, supra* note 5, at 190, 218-19 (finding that early childhood interventions significantly increase child attainments).

26. Duncan & Brooks-Gunn, *Family Poverty, supra* note 25, at 188.

abuse, neglect, and violent crime.²⁷ Alternatively, studies indicate that there is a correlation between increasing income and increasing childhood attainments.²⁸

Some have argued that the culture of poverty, not income per se, creates these poor outcomes.²⁹ But in recent work, Greg Duncan and Jeanne Brooks-Gunn have attempted to isolate income from other factors. They found that family income has a significant effect on children's attainments.³⁰ Importantly, they found that family income has a strong impact on verbal ability and achievement and less of an impact on behavior or physical health. Moreover, they found that "being poor in all of the first four years of life is associated with about a nine point difference in Wechsler Preschool and Primary Scale of Intelligence (WPSSI) IQ test scores at age 5, compared with not being poor in those years."³¹ They also found that the depth of poverty was important and that children below the poverty line had test scores significantly lower

27. *Id.*

28. H. Elizabeth Peters & Natalie C. Mullis, *The Role of Family Income and Sources of Income in Adolescent Achievement*, in CONSEQUENCES OF GROWING UP POOR, *supra* note 1, at 340, 365-66, 376 ("increases in income at all levels of socioeconomic status improves outcomes").

29. See, e.g., CHARLES MURRAY, *LOSING GROUND* 9 (1984); Mayer, *supra* note 2, at 14-17 (concluding that once basic necessities are met, increased income does not significantly benefit children); LAWRENCE M. MEAD, *THE NEW POLITICS OF POVERTY: THE NON-WORKING POOR IN AMERICA* 5, 15 (1992) (arguing that non work by the poor is the greatest social problem); LAWRENCE M. MEAD, *BEYOND ENTITLEMENT: THE SOCIAL OBLIGATIONS OF CITIZENSHIP* 37-41 (1986) (arguing that the impact of generous social benefits was to generate dependency on government).

30. Duncan & Brooks-Gunn, *Family Poverty*, *supra* note 25, at 188-89 (poverty adversely impacts the ability and achievement of children); Hanson, *supra* note 25, at 190 (finding that income generally increases children's welfare); Peters & Mullis, *supra* note 28, at 376 (1997) (higher level of family income positively associated with outcomes for teens); see also Robert Haveman & Barbara Wolfe, *The Determinants of Children's Attainments: A Review of Methods and Findings*, 33 J. ECON. LIT. VOL. 1829 (1995) (discussing the benefits to children from increased human capital investment); Corcoran & Adams, *supra* note 19, at 461 (noting that "[c]onsiderable research . . . has documented an association between fathers' incomes and sons' earnings"); WILLIAM H. SEWELL & ROBERT M. HAUSER, *EDUCATION, OCCUPATION AND EARNINGS: ACHIEVEMENT IN THE EARLY CAREER* 108 (1975) ("parents' average income . . . has the largest effect on earnings . . . of all the variables in the model"); OECD, *supra* note 17, at 99 (differences in socio-economic status are associated with large differences in reading literacy). But see David M. Blau, *The Effect of Income on Child Development*, 81 REV. ECON. & STAT. 261 (1999) (finding that the effect of temporary increases in income on cognitive development is small, and the effect of permanent increases is larger, but still small); Yaqub, *supra* note 13, at 1081, 1086 (2002) (noting that there is a correlation between a parent's income and the ultimate income of the child, and that the earnings advantage of well-off parents is similar to the advantages gained through higher education); David J. Zimmerman, *Regression Toward Mediocrity in Economic Stature*, 82 AM. ECON. REV. 409, 410 (1992) (finding strong correlation between father's earnings and son's future income); Gary Solon, *Intergenerational Income Mobility in the United States*, 82 AM. ECON. REV. 393 (1992) (finding the same correlation); D. O'NEILL & O. SWEETMAN, *THE PERSISTENCE OF POVERTY IN BRITAIN: EVIDENCE FROM PATTERNS OF INTERGENERATIONAL MOBILITY* 2, (Nat'l U. of Ir., Econ. Dep't, Working Paper N61/10/95, 1995) (finding that in the United Kingdom a "1% increase in fathers' earnings increases sons' earnings by .6%").

31. Duncan & Brooks-Gunn, *Family Poverty*, *supra* note 25, at 189.

than children who had family incomes above the poverty line.³² In addition, Duncan and Brooks-Gunn found that young children's outcomes were particularly sensitive to family income.³³ Greater family income during a child's younger years significantly increased the child's chances of graduating from high school.³⁴

A recent study by Eric Turkheimer found that almost 60 percent of the variance in IQ for low-income individuals is the result of their environment and almost none of the variance is due to heredity.³⁵ This means that intervening in a low-income child's life can have a significant positive impact on IQ. Increasing a child's IQ increases the chances that the child will succeed economically and decreases the chances that the child will end up in poverty.³⁶

3. Money Matters

What emerges from an examination of the economic literature on human capital theory and the education literature on childhood attainments is the conclusion that money matters. Children in families with

32. *Id.*

33. It is for this reason that I advocate giving money directly to children during their early childhood. Other proposals, like the Stakeholder Society or Human Capital Accounts, discussed *infra* Part III.B.1., provide benefits to children only after they reach adulthood. In my view, this assistance reaches them too late.

34. Duncan & Brooks-Gunn, *Family Poverty*, *supra* note 25, at 189.

35. Eric Turkheimer et al., *Socioeconomic Status Modifies Heritability of IQ in Young Children*, 14 PSYCHOL. SCI. 623 (2003); *see also* Peters & Mullis, *supra* note 28, at 376 (finding that "[f]or most outcomes the income effect was close to linear, so poverty is not a special case: increases in income at all levels of socioeconomic status will improve outcomes"). *But see* MAYER, *supra* note 2 (finding that increased income is only beneficial for extremely low-income families); RICHARD J. HERRNSTEIN & CHARLES MURRAY, *THE BELL CURVE: INTELLIGENCE AND CLASS STRUCTURE IN AMERICAN LIFE* 10-11 (1994) (arguing that IQ is mostly hereditary); CLAUDE S. FISCHER ET AL., *INEQUALITY BY DESIGN: CRACKING THE BELL CURVE MYTH* 22-69 (1996) (disputing Herrnstein and Murray's findings and concluding that intelligence is not fixed at birth).

36. There is significant disagreement regarding the impact IQ has on job performance and economic success and a thorough review of this literature is outside the scope of this Article. I only argue that increasing a child's IQ is one factor that will increase the child's ability to succeed. For a discussion of the impact IQ has on job performance, *see* HERRNSTEIN & MURRAY, *supra* note 35, at 70-79, 165 (arguing that there is a link between higher IQ and job performance and employment); Frank L. Schmidt et al., *Personnel Selection*, 43 ANN. REV. PSYCHOL. 627, 654-60 (1992). *But see* Fischer, *supra* note 35, at 97-101 (criticizing Herrnstein and Murray's analysis and concluding that intelligence explains approximately 10% of the variance in incomes); Joop Hartog, *On Human Capital and Individual Capabilities*, 47 REV. OF INCOME & WEALTH, 515, 535 (2001) (ability has a significant correlation with earnings, but IQ is a bad measure of ability); John Crawley et al., *Three Observations on Wages and Measured Cognitive Ability*, 8 LAB. ECON. 419, 433 (2001) (cognitive ability accounts for small variance in wages); *see also* Griggs v. Duke Power Co., 401 U.S. 424, 433 (1971) ("The facts of this case demonstrate the inadequacy of broad and general testing devices as well as the infirmity of using diplomas or degrees as fixed measures of capability.").

higher incomes do better.³⁷ They have higher graduation rates, higher incomes, and fewer behavioral problems. One explanation for these better outcomes is that people with higher incomes have greater resources available to invest in their children's human capital. Higher income people can afford to purchase higher quality day care, to provide better nutrition for their children, and to live in better neighborhoods.³⁸

The education literature indicates that a child's performance and IQ can suffer due to consistent poverty and that childhood educational attainments are affected by the quality of the child's neighborhood, education, and health care. The economic literature indicates that children in general benefit from increased human capital investment.³⁹ As the knowledge-based economy becomes more dependent on skilled workers, human capital investment in the next generation becomes essential for fulfilling the goal of having an educated and skilled workforce.

B. Civic Responsibility and Benefits

Although a self-sustaining investment program in children can be justified purely on economic theory, it also finds strong support in social welfare theory. This section examines social welfare justifications for supporting a child investment program. The first part of this section examines the theories based on the justification that assistance to children increases societal well-being, the second part examines individualistic justifications for investment in children, and the third section examines theories of justice and fairness. The first two sections primarily rely on Michael Graetz and Jerry Mashaw's recent work examining justifications for a social safety net. The third section

37. See *supra* note 30.

38. Duncan & Brooks-Gunn, *Family Poverty*, *supra* note 25, at 190; 1 JAMES BROOKS-GUNN ET AL., NEIGHBORHOOD POVERTY: CONTEXT AND CONSEQUENCES FOR CHILDREN (1997). But see HERRNSTEIN & MURRAY, *supra* note 35, at 127-42 (arguing that IQ is a greater indicator of future poverty than economic status); O'NEILL, *supra* note 30, at 18 (finding that even adjusting for ability "has little impact on the persistence of poverty across generations").

39. Duncan & Brooks-Gunn, *Family Poverty*, *supra* note 25, at 188-89; see SCHULTZ, VALUE OF EDUCATION, *supra* note 2, at 53 ("differences in the amounts invested in human capital in workers may be the single most important factor accounting for differences in wages"). See generally BECKER, *supra* note 2. Although in developing the argument here I rely on studies and literature involving human capital investment, this Article is not attempting to prove that increased investment in the human capital of children is beneficial. I leave that to others far more qualified in the field. Instead, this Article assumes that increased human capital investment is beneficial and is designed to discuss a creative way of increasing the current level of investment.

examines the implications of Rawls's theory of social justice for a self-sustaining investment program for children.

Graetz and Mashaw's and Rawls's arguments are particularly persuasive when applied to children.⁴⁰ Children are not in a position to help themselves. They cannot lift themselves up by their own bootstraps.

1. Societal Maximization Justification

In their recent book, *True Security, Rethinking American Social Insurance*, Graetz and Mashaw use the story of the three pigs to set out several reasons why society should provide a social safety net.⁴¹ These arguments basically break down into two groups. The first is social maximization or charitable justification, and the second is the individual maximization. Under the social maximization theory, society itself benefits from the social program. For example, when there is a market failure, the government may step in to correct for inequities or to provide support that reduces the harsh consequences that may result when the market is unwilling or unable to provide the necessary insurance.⁴² Under this approach, Graetz and Mashaw argue that government has an obligation to correct for inequities in the market or at least reduce the harsh consequences that may result from market failure.

In the context of investing in children, one can see a type of market failure. Children are not able to enter into market transactions or obtain human capital loans even though investing in human capital is a wise investment. As a society, it is reasonable to attempt to create social programs to correct for this market failure. This is especially true when considering investments for children because it appears that the market failure is creating an aggregate reduction in societal wealth. Thus, by correcting for the market failure society is actually better off.

Society also may recognize that inefficiencies in the market cause an unequal distribution of income, or that some members of society are not well-equipped to operate in a competitive arena. In this regard, society may wish to provide food to the poor, subsistence-level income assistance, or economic assistance to people who are disabled. Society meets this obligation for charitable reasons, but also because society receives

40. As Graetz and Mashaw explain, "[t]he core difficulty in delivering adequate social insurance protection to children is that the virtually universal desire to help these children is accompanied by suspicion of, and sometimes even antipathy toward, their parents." GRAETZ & MASHAW, *supra* note 1, at 114.

41. *Id.* at 15-23.

42. *Id.* at 17-19.

benefits from its benevolence.⁴³ Because society will likely not make this contribution absent a societal benefit, the aggregate benefits to society—including the goodwill that society feels by being charitable—must outweigh other costs to society. Thus, a social safety net may increase society's well-being and wealth.⁴⁴

2. Individualistic Maximization

The second group of justifications for a social safety net involves individualistic maximization. An individual may realize that providing a social safety net is necessary for his own benefit. Graetz and Mashaw refer to this as self-regard.⁴⁵ Absent a safety net, the poor may want something from me; family members may want to stay in my house; poor people may ask me directly for charity. Instead of being accosted by homeless on the street, one might prefer to fund homeless shelters. Under this justification, society creates a safety net because doing so is in the best interests of its individual members.

In addition, some scholars argue that societal stability depends on those at the bottom having sufficient economic well-being that they choose to at least accept the status quo.⁴⁶ In this regard, an individual may prefer to "subsidize" poor people to ensure that they accept current societal norms that benefit the particular individual. Chaos or public unrest by those with no economic stake in society poses a direct threat for those individuals who benefit from the current social structure.

43. *Id.* at 17-21.

44. For a general discussion of social insurance, see GEORGE E. REJDA, *SOCIAL INSURANCE AND ECONOMIC SECURITY* (1988).

45. GRAETZ & MASHAW, *supra* note 1, at 19.

46. *Id.* at 18-19 (discussing reasons for social insurance including fairness, obligation and self-regard); see Colin Wringe, *Children's Welfare Rights are Entitlements*, in *VISIONS OF ENTITLEMENT, THE CARE AND EDUCATION OF AMERICA'S CHILDREN* 31, 41 (Mary A. Jensen & Stacie G. Goffin eds., 1993) (A rational actor would not enter society and give up his or her freedoms to be worse off than he would be outside society. We, therefore, must assume that members of society make a trade-off and surrender part of their freedom and accept obedience to the law in exchange for some benefit. If no benefits result, the individual would be better off living outside society and not in accordance with its rules.) Wringe further argues that requiring the poorest in society to obey the law comes with a concurrent societal obligation to protect them from extreme poverty. *Id.*; see also Peter Edelman, *The Next Century of Our Constitution: Rethinking Our Duty to the Poor*, 39 *HASTINGS L.J.* 1, 2, 23 (1987) (arguing that there should be a constitutional right to some form of minimum income or subsistence level assistance).

3. Justice and Fairness Rationale

In *Theory of Justice*, John Rawls outlines an additional reason for providing a social safety net⁴⁷ and urges society to create and impose a system that is just and fair.⁴⁸ He argues that such a system must be determined in the "original position,"⁴⁹ which assumes that people do not know their ultimate place in society and are forced to make decisions behind a "veil of ignorance."⁵⁰ They do not know their social class, economic status, education, or intelligence. They could be born rich or poor, intelligent or not-intelligent. Because of the uncertainty as to one's position in society, Rawls argues that a rational actor would choose a social safety net that at least provided minimal economic protection for the poor. After all, under Rawls's theory, that person could end up poor without the mental acumen to succeed.⁵¹

4. Impact of Analyses of Civic Responsibility on Investment in Children

Investment in the human capital of children has both individualistic and societal benefits. Society benefits from a more educated, trained, and self-sufficient citizenry.⁵² It would therefore be unfair and inefficient to require all social welfare policies to pay for themselves, or for all programs that invest in children to be paid for by the recipients. The dual benefits derived from investing in children indicate that there should be a dual role in funding these investments. Because I endorse this justification, I do not suggest that society should reduce existing funding for

47. JOHN RAWLS, *A THEORY OF JUSTICE* 17 (1971). For a discussion of Rawls's theory of social justice, see generally WILL KYMLICKA, *CONTEMPORARY POLITICAL PHILOSOPHY: AN INTRODUCTION* (1990).

48. RAWLS, *supra* note 47, at 17. For a discussion of Rawls' theory in the context of child welfare assistance, see Edward B. Foley, *Social Justice and Child Poverty*, 57 OHIO ST. L.J. 485, 490-93 (1996). See also Linda Sugin, *Theories of Distributive Justice and Limitations on Taxation: What Rawls Demands from Tax Systems*, 72 FORDHAM L. REV. 1991 (2004) (discussing Rawls's theory as applied to taxation).

49. RAWLS, *supra* note 47.

50. *Id.* at 17-19.

51. For an argument that economic welfare and security are a component of citizenship, see T. H. MARSHALL, *CITIZENSHIP AND SOCIAL CLASS* 10-11 (1950). See also Martha T. McCluskey, *Efficiency and Social Citizenship: Challenging the Neoliberal Attack on the Welfare State*, 78 IND. L.J. 783, 790-97 (2003) (analyzing Marshall and arguing that society cannot be just unless all its citizens have economic and political security); CITIZENSHIP TODAY: THE CONTEMPORARY RELEVANCE OF T. H. MARSHALL (Martin Bulmer & Anthony M. Rees eds., 1996) (discussing Marshall's theory in light of contemporary welfare questions).

52. Providing assistance to children, either through income assistance or other programs helps stop poverty and can be justified by the human capital theory of economic growth. Yaqub, *supra* note 13; OECD, *supra* note 17, at 136-37 (Human capital investment significantly contributes to strong economic growth and has both social and individual returns.).

children's programs. Nothing I advocate here suggests that government should stop funding day care, Head Start, or food stamps in exchange for the Child Investment Funds. In fact, if anything, this discussion makes clear that government is not doing enough. Similarly, I do not advocate elimination of tax benefits that indirectly help children, including the child tax credit, the Earned Income Credit, or the dependency exemption.

Investing in children, however, provides a specific benefit to the child as well as to society as a whole. If a child is better educated and earns a higher income, the child is a direct beneficiary of that investment. It is therefore appropriate to require that child, or at least the aggregate of all children who receive a benefit, to contribute or pay back some of the money he received for investment.

Recently, Amy Wax has argued that current trends in social policy are centered on helping those who are willing to help themselves and that what she terms "social reciprocity" is an essential component of government assistance programs.⁵³ Work requirements in recent welfare legislation are just one example. Although a child investment program can be justified on civic responsibility grounds alone, the Child Investment Fund program I propose attempts to bridge the gap between those who support pure subsidy programs and those who advocate social reciprocity or market mechanisms for increasing investment in children. As discussed and developed in Part IV, I advocate a cash assistance program for children with a commensurate payback by the child once the child is employed.

C. Public Choice Theory and Correcting the Funding Bias Against Children

Another justification for a self-sustaining investment program in children is that children are powerless to influence the legislative process and are under-represented in the political arena. Children cannot lobby, do not contribute to political campaigns,⁵⁴ and cannot represent themselves

53. See, e.g., Amy L. Wax, *A Reciprocal Welfare Program*, 8 VA. J. SOC. POL'Y & L. 477 (2001) (arguing that "social reciprocity" is an important ingredient in government assistance programs); Amy L. Wax, *Something for Nothing: Liberal Justice and Welfare Work Requirements*, 52 EMORY L.J. 1, 2-3 (2003) ("conditional reciprocity" requires individuals, if they are able, to contribute to society in some way as a quid pro quo for assistance); Peter B. Edelman, *Promoting Family by Promoting Work: The Hole in Martha Fineman's Doughnut*, 8 AM. U.J. GENDER SOC. POL'Y & L. 85, 88-89 (2000) (arguing that work outside the home is important but those jobs must be available and pay a livable wage).

54. The Bipartisan Campaign Reform Act of 2002 (BCRA), prohibited children under 17 from making political contributions. 2 U.S.C.A. § 441k (West 2003 & Supp 2004). In *McConnell v. FEC*, the Supreme Court overturned this restriction. 540 U.S. 93, 231-32 (2003). Major contributions from children, increase the parent's influence in the political process, not the child's. See *McConnell v. FEC*, 251

in the political process. Interested adults have formed organizations to lobby for children, and parents often represent their children's interests, but these organizations cannot adequately represent children's interests.

The political incentive to under-invest in children and over-spend on adults is supported by public choice theory.⁵⁵ Public choice theory examines the legislative process and government decision making through the lens of economic theory and models.⁵⁶ The premise is that government spending is an economic good and that interest groups will compete to obtain the good for themselves. Thus, groups with greater influence will be able to obtain a bigger piece of the pie.⁵⁷

Although the public choice approach has been rejected by some scholars,⁵⁸ it is generally because the theory does not fully explain legislators' actions, not because it is wholly irrelevant.⁵⁹ Public choice theory tends to minimize a legislator's own political agenda, views, and morals. It treats our public officials as indifferent actors ready to be bought and sold. Although this may be public perception, it is certainly questionable based on the literature.⁶⁰

The public choice model, however, does provide some insight into the legislative process. People who vote, organize, and are wealthy have greater ability to influence legislation. The public choice model requires society to recognize, or at least examine, whether the political process is biased against children. As the population ages and fewer families

F. Supp. 2d 176, 588 (D.D.C. 2003) (discussing concerns by the FEC and others that parents were giving contributions in their children's names, and noting that large donations have been made by 4 year olds).

55. See Stout, *supra* note 9, at 1956 ("A primary obstacle to optimal social investment in children is the fact that the principal beneficiaries of such investment are disenfranchised.")

56. For a discussion of Public Choice Theory, see WILLIAM N. ESKRIDGE, JR. ET AL. & PHILLIP P. FRICKEY, CASES AND MATERIALS ON LEGISLATION: STATUTES AND THE CREATION OF PUBLIC POLICY 54-60 (2001). See also MANCUR OLSON, THE LOGIC OF COLLECTIVE ACTION: PUBLIC GOODS AND THE THEORY OF GROUPS (1965); WILLIAM H. RIKER, LIBERALISM AGAINST POPULISM: A CONFRONTATION BETWEEN THE THEORY OF DEMOCRACY AND THE THEORY OF SOCIAL CHOICE (1988); Gary S. Becker, *A Theory of Competition Among Pressure Groups for Political Influence*, 98 Q.J. ECON. 371, 371 (1983).

57. See Susan A. MacManus, *Taxing and Spending Politics: A Generational Perspective*, 57 J. POL. 607, 619 (1995) (finding less support among older people than younger people for increased funding in public education).

58. Daniel Shaviro, *Beyond Public Choice and Public Interest: A Study of the Legislative Process as Illustrated by Tax Legislation in the 1980s*, 139 U. PA. L. REV. 1, 6-9 (1990) (arguing that public choice theory fails to adequately explain the legislative process); see also Daniel A. Farber & Phillip P. Frickey, *The Jurisprudence of Public Choice*, 65 TEX. L. REV. 873-74 (1987) (noting public choice theories are insufficient to explain the legislative process); Joseph P. Kalt & Mark A. Zupan, *Capture and Ideology in the Economic Theory of Politics*, 74 AM. ECON. REV. 279 (1984) (economic justification of legislative action is not a good predictor of legislative outcomes).

59. Shaviro, *supra* note 58, at 76 ("[O]ne should not conclude from the theory's failure here that it lacks significant explanatory power. It needs to be supplemented, not abandoned."); see also *id.* at 75-106 (discussing problems with public choice theory and the ways it can be improved).

60. Kalt & Zupan, *supra* note 58.

have children, public choice theory indicates that children will receive a smaller and smaller piece of the pie.⁶¹ Not only will children get a smaller portion, but the federal deficit incurred through other people's success in obtaining the pie will be borne disproportionately by them.⁶² A self-sustaining investment program ensures that children will at least receive a basic level of investment in their human capital.

III. LESSONS FROM CURRENT AND PROPOSED PROGRAMS FOR CREATING A SELF-SUSTAINING CHILD INVESTMENT PROGRAM

At first, the idea of providing cash assistance directly to children may seem outlandish. Nevertheless, current programs indicate that creating a self-sustaining investment program in children is not so radical a proposal. Subsection A examines existing programs and policies that provide subsidies to families with children and discusses how these existing programs confirm the plausibility of a self-sustaining child investment program. Subsection B reviews other policy proposals designed to increase assistance to families with children, or to increase investment in children, and explains how the program I suggest incorporates or benefits from these prior policy initiatives.

61. The number of families with children has dropped from 55.9% in 1970, to 52% in 1980, to 48.9% in 1990, to 48.1% in 2000. Author's calculations based on U.S. Department of Education, National Center for Education Statistics, Digest of Education Statistics 2001, at 25 (2002), available at <http://nces/ed/gov/programs/digest/do2/tables/dto.18.asp>. See MacManus, *supra* note 57, at 619 (finding spending preferences are closely linked to the "expected priorities of people at that point in the life cycle").

62. For a thorough discussion of budget deficits and intergenerational transfers, see SHAVIRO, *supra* note 4, at 140-44; Laurence J. Kotlikoff, *From Deficit Delusion to the Fiscal Balance Rule: Looking for an Economically Meaningful Way to Assess Fiscal Policy*, in GENERATIONAL ACCOUNTING AROUND THE WORLD 9 (Alan J. Auerbach et al. eds., 1999). In his most recent discussion on the topic, Daniel Shaviro notes that the George W. Bush Administration's policy of cutting taxes and increasing spending further exacerbates problems of inter-generational transfers. See DANIEL N. SHAVIRO, RECKLESS DISREGARD: THE BUSH ADMINISTRATION'S POLICY OF CUTTING TAXES IN THE FACE OF AN ENORMOUS FISCAL GAP (Center for Law and Business Working Paper Series, Working Paper No. CLB 03-19, 2003). This large increase in the budget deficit obviously impacts the ability of the government to fund the program I suggest in the short term. It also highlights the importance of the program I propose. The current tax cuts and spending increases benefit this generation at the expense of the next. If we are going to saddle future generations with more and more debt, we should at least provide those generations with sufficient human capital investment to pay those debts.

A. Current Programs and Subsidies Indicate that a Self-Sustaining Child Investment Program is Workable

1. Social Security

a. Social Security Retirement Benefits

In many ways, the funding for the Child Investment Fund program works like Social Security but in reverse. Under Social Security, current workers pay a wage tax, and the proceeds from the tax are credited to the Social Security trust fund.⁶³ Current retirees, who presumably contributed to the fund while they were working, receive a Social Security benefit from the fund. The working population funds the benefits paid to the retired population. It does so with the hope that the next generation will work and pay into the system to honor promises made to it. Thus, each generation funds the previous generation's benefits. Social Security beneficiaries receive cash benefits, and except in extreme cases, the recipients are free to spend the money as they choose.⁶⁴ In large part because of Social Security, the poverty rate among the elderly has dropped dramatically.⁶⁵ If we are willing to provide a safety net for adults who presumably had a lifetime to plan for retirement, why not have a similar program for children?

As discussed in more detail in Part IV, I propose a program for children that is funded in a manner similar to Social Security, with one substantial difference—a payback requirement. Social Security provides benefits to one generation and expects the next generation to fund these benefits. There is a disconnect between the beneficiaries and the contributors. Under my proposal, each generation receives a benefit and then is required to pay back that benefit during its working life. The entire cohort will receive a certain benefit, and that cohort must pay back the amount received. There is no attempt to shift the burden of the payback on other generations. Just as under the Social Security system, some will receive more and some less than they ultimately will have to pay back, but the cohort as a whole will pay back what was received.

63. I.R.C. § 3101 (West 2002 & Supp. 2004).

64. 42 U.S.C.A. §§ 301-1397j (West 2003 & Supp. 2004).

65. The poverty rate for people over 65 has dropped from approximately 35.2% in 1959 to 10.4% in 2002. See PROCTOR & DALAKER, *supra* note 1, at 28; see also Robert B. Hudson, *The History and Place of Age-Based Public Policy*, in THE FUTURE OF AGE-BASED PUBLIC POLICY 2 (Robert B. Hudson ed., 1997); Eric R. Kingson & James H. Schulz, *Should Social Security Be Means-Tested?*, in SOCIAL SECURITY IN THE 21ST CENTURY 52 (Eric R. Kingson & James H. Schulz eds., 1997).

b. Social Security Survivor Benefits

The Social Security system is a model for the suggested program in a second way. Social Security includes a program that provides cash benefits directly to children. Children whose parents are deceased, retired, or disabled are entitled to Social Security benefits.⁶⁶ These benefits belong to the child. The Social Security Administration (SSA) reports that it distributes approximately \$1.6 billion each month to almost 3.8 million children.⁶⁷

Because the child is not able to make financial decisions for herself, the Social Security Administration appoints a "representative payee" who controls the money on the child's behalf.⁶⁸ The representative payee is usually a parent or guardian who has custody of the beneficiary, and the SSA has specific regulations for determining who should be appointed as the representative payee⁶⁹ if such a parent is not available or appropriate.⁷⁰ The representative payee receives the money on behalf of the child and must use the payments for the benefit of the child.⁷¹

The representative payee is required to submit a statement to the SSA explaining how the money was spent.⁷² The SSA has authority to investigate abuse by representative payees, but the SSA does not exercise direct oversight regarding how the money is spent.⁷³ The SSA may re-

66. 42 U.S.C. § 402(d)(1) (2000).

67. Social Security Administration, *Benefits for Children*, SSA Pub. No. 05-10085 I (March 2001), available at <http://www.ssa.gov/pubs>.

68. 42 U.S.C.A. § 1383(a) (2003 & Supp. 2004); 20 C.F.R. § 416.610 (2004) ("When payment will be made to a representative payee.").

69. See 20 C.F.R. § 416.620 (indicating the factors the SSA uses to choose a representative payee, including the relationship to the beneficiary, the amount of interest the person shows in the beneficiary, legal authority the person or entity has to act on child's behalf, whether the person has custody over the child, whether the payee is in a position to know and look after the beneficiary); *id.* § 416.621(b) (indicating order of preference for selecting a representative payee for beneficiaries under age eighteen).

70. *Id.* § 416.621(b) provides that SSA's preference in choosing a representative payee are as follows: (1) parent who has custody, (2) parent who does not have custody but provides support, (3) parent who does not have custody and does not provide support but has demonstrated "strong concern" for the beneficiary, (4) a relative or stepparent who has custody of the beneficiary, (5) a relative who does not have custody but who contributes towards the beneficiary's support, (6) a relative or close friend who does not have custody but who demonstrates concern for the beneficiary's well being, and (7) an authorized agency or institution.

71. *Id.* § 416.635(a).

72. *Id.* § 416.635(c).

73. Social Security recommends that the benefits should first be used to pay for the day-to-day needs of food and shelter for the beneficiary, and then may be used for the beneficiary's personal needs. The benefits may also be used to pay for medical needs not covered by insurance. See SOCIAL SECURITY ADMINISTRATION, PUB. NO. 05-10076, *SOCIAL SECURITY: A GUIDE FOR REPRESENTATIVE PAYEES 3* (2001), available at <http://www.ssa.gov/pubs/10076.pdf>.

move a representative payee who abuses her position,⁷⁴ and a representative payee may be liable to the beneficiary for misspent funds.⁷⁵

2. Alaska's Permanent Fund

Another program that provides an example of cash assistance to children is Alaska's "dividend" program.⁷⁶ Alaska currently provides a dividend from its oil revenues to all qualifying residents.⁷⁷ Children as well as adults qualify for the dividend,⁷⁸ and over the last five years dividend payments per person have averaged almost \$1,650 per year.⁷⁹ Alaska distributes the dividend through the Alaska Department of Revenue.⁸⁰

What is instructive about the Alaska system is that Alaska routinely pays a cash dividend to children in an amount and form similar to what I propose here. The Alaska program provides support for the notion that a Child Investment Fund could be both feasible administratively

74. 20 C.F.R. § 416.650.

75. See *id.* § 416.641; SOCIAL SECURITY ADMINISTRATION, *supra* note 73, at 2.

76. Alaska's constitution provides that 25% of the royalties Alaska receives from oil and mineral leases be placed in a permanent fund. ALASKA CONST. art. IX, § 15. By statute, Alaska has increased the 25% contribution to 50%. 2003 ALASKA SESS. LAWS ch. 22 (amending ALASKA STAT. § 37.13.010(a)(2) (Michie 1997)). The permanent fund is designed to be a savings account for the state, and the funds may not be spent absent a constitutional amendment. *Id.* Alaska statutes also provide for inflation protection for the fund. ALASKA STAT. § 37.13.145(c) (Michie 1997). The idea of the permanent fund is that Alaska can save for the future so that when its natural resources dwindle it will have self-sustaining financial reserves. The investment returns from the fund may be appropriated by the legislature. The legislature has determined that a portion of those returns should be distributed to the citizenry as a "dividend." The amount of the dividend is provided by a statutory formula. See *id.* § 43.23.025.

77. Alaska Statutes § 43.23.005 provides that a person is eligible for a dividend if he is a state resident, applies to the department, was a state resident during the entire qualifying year, was in the state for at least 72 consecutive hours, and is a citizen of the United States or an alien meeting certain specific criteria. An individual is not entitled to a dividend even if the person meets the above criteria if, during the relevant year, the person was incarcerated due to 1) a felony conviction, or 2) a misdemeanor conviction and had been previously convicted of either a misdemeanor or a felony. See ALASKA STAT. § 43.23.005(d).

78. Alaska Statutes § 43.23.005(a) provides that any person who applies for a dividend, is a state resident, and was a state resident during the entire qualifying year is entitled to a dividend. Alaska Statutes § 43.23.005(c) provides that a parent or guardian may claim a permanent fund dividend on behalf of a minor, and that minors who do not meet the residency requirement are eligible for a dividend if "during the two calendar years immediately preceding the current dividend year, the minor was born to or adopted by an individual who is eligible for a dividend for the current dividend year." The statutory framework ensures that all children who are residents of Alaska, or who were recently adopted by or born to, residents of Alaska qualify for the dividend.

79. 2002 PERMANENT FUND DIVIDEND ANN. REP. 6, available at <http://www.pfd.state.ak.us>.

80. For further information on the Alaska Permanent Fund and the dividend program, see RÖGNGVALDUR HANNESSON, INVESTING FOR SUSTAINABILITY: THE MANAGEMENT OF MINERAL WEALTH 57 (2001); William S. Brown & Clive S. Thomas, *The Alaska Permanent Fund: Good Sense or Political Expediency?*, 37 CHALLENGE 38 (1994); J. Patrick J. O'Brien & Dennis Olson, *The Alaska Permanent Fund and Dividend Distribution Program*, 189 PUB. FIN. Q. 139 (1990); see also Alaska Permanent Fund Corporation Web site, available at <http://www.apfc.org>.

and successful programmatically. For example, there appears to be no evidence of a huge upsurge in fertility in Alaska, nor does the dividend payment appear to discourage work or encourage alcoholism or drugs.

Alaska's cash dividend payment program provides an interesting example of a statutory framework for how a national program might deliver cash assistance to children. Under Alaska law, a parent may claim a permanent fund dividend on behalf of a minor by submitting an application to the Department of Revenue.⁸¹ The dividend, however, is the child's and the parent's right to receive the dividend is based on whether the child qualifies for the dividend. Surprisingly, there are no statutory rules regarding a parent's duty to the child recipient with regard to the dividend payment.⁸² Alaska law gives the parent tremendous leeway to use the child's dividend payment as the parent chooses. In fact, relying on general common law principles, the Alaska Supreme Court indicated that one of the "'parental rights' protected by the constitution [is] 'the right to control and manage' a minor child's earnings and property."⁸³ Although the court has held that a parent has a right to control a child's dividend, it is unclear whether such control allows the parent to take ownership of the dividend, or whether the parent has some duty to the child with regard to the dividend. Concluding that a parent has "'the right to control and manage' a minor child's earnings and property" is not the same as holding that the parent may use the child's money for the parent's own benefit. It may be that the parent has control over the money but still has some duty to ensure that the child receives the benefit of the dividend.

Despite the fact that the parent has control over the dividend, the dividend clearly belongs to the child. A parent who fails to make an application for an eligible child may not make one retroactively.⁸⁴ The child, however, is allowed to make an application on her own behalf when she reaches age 18, and is entitled to any dividends not previously paid to her due to the parent's failure to make an application.⁸⁵ Moreover, the United States treats the dividend payment as taxable income to the child.⁸⁶ If parents had complete control over the child's per-

81. ALASKA STAT. §§ 43.23.005, 43.23.015.

82. *See Lawson v. Reynolds*, No. S-10053, 2002 WL 1486484, at *9 (Alaska, July 10, 2002) (indicating that "[i]n Alaska the law is silent regarding a parent's responsibilities once a child's PFD is distributed").

83. *See id.*; *Lee v. Cox*, 790 P.2d 1359, 1363 (Alaska 1990) (quoting *L.A.M. v. State*, 547 P.2d 827, 832-33 n.13 (Alaska 1976)).

84. *See* ALASKA ADMIN. CODE tit. 15, § 23.133.

85. ALASKA ADMIN. CODE tit. 15, § 23.133(b).

86. *See* INTERNAL REVENUE SERV., DEP'T OF TREASURY, PUB. 3328, CAT. NO. 26988N, HOW TO FILE YOUR CHILD'S 2001 TAX RETURN: INFORMATION FOR PARENTS OF ALASKAN CHILDREN 1 (2002), available at <http://www.unclefed.com/IRS-Forms/2002/p3328.pdf>.

manent fund dividend, including the right to spend the child's dividend on themselves, the parent, not the child, would be subject to federal tax on the dividend.⁸⁷ Finally, even Alaska recognizes that the child's permanent fund dividend is not the parent's property because the dividend is not included in the custodial parent's income when calculating that income for purposes of child support and alimony.⁸⁸

There are no Alaska cases reporting disputes between parents and children regarding ownership or custodianship of the dividend.⁸⁹ Most legal disputes concerning a minor's dividend payment involve parents fighting over which parent should receive the child's dividend or arguing that the other parent has misspent the child's dividend.⁹⁰ The Alaska program therefore places complete trust in parents that they will use the dividend for the child's benefit. Although this provides for administrative simplicity, it fails to place any control on parental behavior.

The Alaska model gives parents too much control over the dividend payment and treats the dividend as income support for the family. The parents may have control over the child's funds, but if Alaska intends for the funds to be the child's property, the parents should have some duty to manage and control the child's funds for the child's benefit. In Part IV, I propose that parents must have a fiduciary duty to the child with regard to the funds, similar to the duties of a "representative payee" in the Social Security context.

87. See *Lucas v. Earl*, 281 U.S. 111 (1930) (assignment of income case); *Helvering v. Horst*, 311 U.S. 112, 116 (1940) (taxation may occur when taxpayer has use or control over the income).

88. See *Fernau v. Rowdon*, 42 P.2d 1047, 1052 n.9 (Alaska 2002) (calculating monthly income of mother by including alimony, part-time work, and the mother's permanent fund dividend. The court did not include the children's permanent fund dividend in this calculation).

89. See *Lawson v. Reynolds*, No. S-10053, 2002 WL 1486484, at *9 (Alaska July 10, 2002) ("In Alaska, the law is silent regarding a parent's responsibilities once a child's PFD [Permanent Fund Dividend] is distributed."); *Lee v. Cox*, 790 P.2d 1359, 1363 (Alaska 1990). But see *Chizmar v. Mackie*, 896 P.2d 196, 211 n.13 (Alaska 1995) (As part of a lawsuit against a doctor for false disclosure of an HIV test, children of divorced couple claimed that due to the divorce they lost their permanent fund dividend. Prior to the divorce the dividend was placed in the children's accounts for future education. The children did not attempt to sue their parents for misuse of the dividend, but instead chose to sue the doctor.).

90. See *Hayes v. Hayes*, 922 P.2d 896, 897-901 (Alaska 1996) (Mother "borrowed" \$4,000 from children's dividend with an oral promise to pay the funds back. Father argued that this was an abuse and that as part of the divorce proceeds the mother should be required to pay back the borrowed funds. The court indicated that the transaction was between the mother and the children and that only they could enforce the agreement. From a contract perspective, "borrowing" \$4,000 from your children hardly seems valid since the child lacks the legal capacity to contract.); *Lee*, 790 P.2d at 1363 (dispute over custody and dividend); *R.I. v. C.C.*, 9 P.3d 274, 278 (Alaska 2000) (custody dispute where court ordered that child's dividend to be held until custody issues were resolved); *Teseniar v. Spicer*, 74 P.3d 910, 916-17 (Alaska 2003) (parent could use the money to support herself and the child when husband failed to make full child support payments despite agreement with former husband that she would deposit the money into an educational account).

3. Dependency Exemption and the Child Tax Credit

The federal tax system delivers the equivalent of cash benefits to families with children through the Dependency Exemption and the Child Tax Credit. This subpart discusses why the Dependency Exemption and the Child Tax Credit are subsidies to families with children. It also discusses that, as subsidies, these benefits are misdirected toward middle- and upper-income families and thus are inefficient mechanisms for increasing human capital investment in children.

a. Dependency Exemption

Although the federal tax system does not provide cash assistance directly to children, it does provide economic benefits to families with children. First, taxpayers are entitled to a deduction of \$3,100 for each dependent.⁹¹ While the definition of a dependent is very expansive, it generally includes children who are living with the taxpayer and who receive more than one-half of their support from the taxpayer.⁹² Since this benefit is provided as an exemption from income, it is only available to people who have income subject to tax. Moreover, the exemption is phased out for high-income earners, so married couples with incomes over \$336,550 do not receive the benefits of the exemption.⁹³ The Dependency Exemption formula thus delivers the equivalent of cash assistance to taxpayers with annual incomes from around \$20,000 to \$325,000, with the greatest benefit going to taxpayers with incomes around \$200,000. Those higher-income individuals whose income is not quite great enough to be subject to the phase out, however, receive the greatest benefit.⁹⁴ The Dependency Exemption thus provides the equivalent of a cash benefit to taxpayers, but it does so in a way that provides the greatest assistance to those who may need it the least—middle and upper-class taxpayers. It provides assistance to middle and upper-income families because they have children, but it does not

91. I.R.C. §§ 151, 152 (West 2002 & Supp. 2004). The dependency deduction is adjusted for inflation. See Revenue Procedure 2003-85, 2003-49 I.R.B. 1184, for the inflation adjusted figures for 2004.

92. I.R.C. § 152(a).

93. I.R.C. § 151(d)(3). See Revenue Procedure 2003-85, 2003-49 I.R.B. 1184, for inflation adjusted figures.

94. Since the income tax system is progressive, people with higher incomes have higher marginal tax rates. A \$3,000 deduction or exemption is worth \$900 to a taxpayer with a marginal rate of 30%, because that is the amount of tax he would have had to pay on the \$3,000 had he not been entitled to the exemption. A \$3,000 exemption is worth only \$450 to a taxpayer with a marginal rate of 15%. The Dependency Exemption provides a greater subsidy to taxpayers in higher brackets. Once a taxpayer's income reaches a certain amount, however, the Dependency Exemption is phased out and that taxpayer receives little or no benefit from the exemption. See I.R.C. § 151(d)(3).

provide assistance directly to children. It is a deduction available to parents, and there is no requirement that the parents must spend that money on their children.

b. Child Tax Credit

In part because of the distributional problems associated with the Dependency Exemption, in 1993 Congress passed a Child Tax Credit.⁹⁵ A tax credit is credited against the amount of tax owed, providing a taxpayer who qualifies for the credit a dollar for dollar decrease in her tax bill.⁹⁶ So a taxpayer with a \$3,000 tax liability and a \$1,000 tax credit pays a tax of \$2,000. Currently, taxpayers with incomes between \$20,000 and \$110,000 receive a tax credit of \$1,000 per child.⁹⁷

Unlike the Dependency Exemption, the tax credit does not generally become more valuable as income rises. All taxpayers who qualify for the full amount of the credit receive the same benefit regardless of their income. But once again, since the tax credit is a credit against one's tax liability, absent a specific provision to the contrary, a taxpayer generally must have a tax liability to receive the credit.

During the Child Tax Credit debate, there was significant discussion whether some of the tax credit should be available to people who had no income tax liability.⁹⁸ Congress ultimately created a partially refundable Child Tax Credit, so that some low-income individuals receive part of the tax credit even if they pay no federal income tax.⁹⁹

95. The Taxpayer Relief Act of 1997, Pub. L. No. 105-34, 111 Stat. 788, (codified at 26 U.S.C.A. § 24(a)(2) (West 2002 & Supp. 2004)).

96. For a discussion of tax credits generally see DANIEL Q. POSIN & DONALD B. TOBIN, *PRINCIPLES OF FEDERAL INCOME TAXATION* 633-34 (6th ed. 2003).

97. People with incomes below \$20,000 and above \$110,000 are subject to complicated transition rules. People with incomes below \$20,000 often have no federal income tax liability. The credit is partially refundable to the extent of 10% of the taxpayer's income that exceeds \$10,000. So a person with \$11,000 in income will receive a refundable child tax credit of \$100 (10% of \$1,000-\$10,000). Taxpayers with incomes over \$110,000 are subject to a phase out of the tax credit. They receive a \$50 reduction in their tax credit for every \$1,000 that their adjusted gross income exceeds \$110,000. For a more detailed explanation of the transition rules surrounding the child tax credit, see POSIN & TOBIN, *supra* note 96, at 641-43, and Martin J. MacMahon Jr., *The New Child Credits: Explainable Mechanics and Unfathomable Policy*, 76 TAX NOTES 1625 (1997).

98. This is referred to as a refundable credit. It means that the credit is not just against tax. If a credit is fully refundable, any amount of the credit not used to offset an income tax liability is still sent to the recipient in the form of a positive payment.

99. See *supra* note 93. The argument by some members in Congress was that the tax credit should be refundable because low-income people still had sizeable employment tax obligations, and thus still have significant tax liability. The refundability amount of the Child Tax Credit for a person with three or more children takes into account social security taxes paid. See I.R.C. § 24(d)(1)(B)(i) (West 2002 & 2004); see also 143 CONG. REC. 14,796 (1997) (statement of Rep. Stupak) (indicating that many low-income individuals

c. The Dependency Exemption and the Child Tax Credit as Mechanisms for Investing in Children

The Dependency Exemption and the Child Tax Credit in many ways provide the exact type of assistance I advocate in this Article. They both provide a cash equivalent to families based on the number of children in the family, but both the Dependency Exemption and the tax credit provide assistance to mainly middle-class families, and both payments reduce the parents' tax liability. Neither payment belongs to the child or is justified on the basis that the parents will use the money to invest in their children. Because it delivers the benefit to parents and not children, and mainly to middle-class families, the Dependency Exemption and the Child Tax Credit are inefficient and ineffective methods of promoting human capital investment in children.

To the extent that the goal is to deliver cash subsidies to families with children, instead of directly to children as I advocate, the nation should at least deliver such assistance to people who need it most. It makes no sense to have a cash assistance program designed primarily for the middle class. In the recent debates in Congress regarding President Bush's proposal to accelerate the phase-in of the Child Tax Credit,¹⁰⁰ some have argued that expanding the tax credit to low-income people is welfare, as if calling it welfare clearly indicates that the payment is improper.¹⁰¹ This fails to recognize that the current tax system provides welfare as well—it is just welfare to the middle class.

Others in Congress argue that a tax credit or a Dependency Exemption is not welfare to the middle class as long as it is provided to people who are already paying tax.¹⁰² But the fact that we provide a benefit through the tax code in no way changes the character of the payment.¹⁰³

pay significant social security and state and local taxes); *id.* at 11,987-88 (statement of Rep. Jackson-Lee) (people paying social security taxes deserve to receive the \$500 Child Tax Credit).

100. The child tax credit was increased from \$500 to \$1,000, and the refundable amount of the tax credit was scheduled to increase from 10% of that amount of income over \$10,500 to 15% of the amount over \$10,500. The Bush proposal accelerated the amount of the tax credit but not the percentage of the tax credit that was refundable. This meant that most low-income families received no benefit from the acceleration of the child tax credit. See ANDREW LEE & ROBERT GREENSTEIN, CENTER ON BUDGET AND POLICY PRIORITIES, HOW THE NEW TAX LAW ALTERS THE CHILD TAX CREDIT AND HOW LOW-INCOME FAMILIES ARE AFFECTED (2003), available at <http://www.cbpp.org/5-28-03tax3.pdf>.

101. 149 CONG. REC. H5321 (daily ed. June 12, 2003) (statement of Rep. Bachus) (arguing that a refundable tax credit is welfare); *id.* at H4963 (daily ed. June 4, 2003) (statement of Rep. Kingston) (same).

102. *Id.* at H5321 (statement of Rep. Bachus) (stating that if you get money back that you paid, it is not welfare).

103. See Anthony Infanti, *A Credit to Their Brackets*, PITTSBURGH POST-GAZETTE, June 29, 2003, at B2 (arguing that the recent cut in the taxable rate for dividends is equivalent to a check by the government to corporate shareholders).

Presumably, a tax credit or deduction that reduces revenue from the standard tax baseline is a subsidy to the person receiving it and can thus be termed welfare.¹⁰⁴ Welfare is simply a subsidy to the recipient for their benefit. A subsidy to middle class or wealthy individuals for their benefit is as much welfare as a subsidy to the poor. The question is whether the tax credit and the Dependency Exemption are such a payment. If they are, is there any justification for providing welfare solely to the middle class? If we were designing from scratch a system to provide cash assistance to families with children, we would never design one that provided almost all the benefits to families with incomes between \$20,000 and \$325,000.

d. The Dependency Exemption and Child Tax Credit Operate as Subsidies to Families with Children and are Similar to Welfare Payments

There are several theoretical reasons why Congress might want to provide a tax deduction or credit to families with children. First, such a deduction might be necessary to clearly reflect a taxpayer's income. Second, Congress might decide that the deduction is necessary based on "ability to pay" principles. Third, Congress might want to provide a subsidy for people with children and decide that a tax benefit is the simplest way to reach that goal.

The first justification to clearly reflect income is the only one that does not have a "welfare purpose." When Congress justifies a deduction on this rationale, it has determined that the party's income will not be properly stated unless such a deduction is granted. A classic example of such a deduction is section 162 of the Internal Revenue Code, which provides a deduction for ordinary and necessary business expenses.¹⁰⁵ It would not clearly reflect a business's income to tax it on its gross receipts, and for many businesses with small profit margins, such a tax system would appear unfair. Allowing a business to deduct its costs ensures that the business pays tax only on its profits. The ordinary and necessary business deduction is therefore necessary to clearly reflect the taxpayer's income. From this perspective, it is not welfare or a subsidy, but instead is designed so that the entity is taxed on what is considered to be the proper amount.

104. See *Leathers v. Medlock*, 499 U.S. 439, 451 (1991); *Regan v. Taxation with Representation of Washington*, 461 U.S. 540, 547 (1983). For a discussion of the tax baseline and tax deductions and credits acting as a subsidy, see Donald B. Tobin, *Anonymous Speech and Section 527 of the Internal Revenue Code*, 37 GA. L. REV. 611, 643 (2003).

105. See I.R.C. § 162 (West 2002 & Supp. 2004).

The second justification—to properly reflect a taxpayer's ability to pay—as applied in the Dependency Exemption context is a decision by the government to subsidize one type of activity over another. Generally, the U.S. tax system is based on an ability to pay principle.¹⁰⁶ This principle holds that people should pay taxes with some adjustment or accommodation for their ability to pay. This idea forms the basis for many of the elements of our income tax. For example, progressive taxation, which is designed to increase a person's tax burden as income rises, and the standard deduction, which ensures that people have a subsistence level of income prior to subjecting them to tax, are both based on ability to pay principles.

The Dependency Exemption also is justified by the ability to pay principle: if the goal is to ensure that a family is not taxed unless its income exceeds subsistence, then some adjustment must be made for family size. A family with four children will obviously require a higher subsistence level than a family with no children. The Dependency Exemption accounts for this differential and ensures that the larger family does not pay tax until its income exceeds a higher threshold.

But the decision to include family size in the measurement of ability to pay is a decision by the government to favor one cost over another. It is, in a sense, a decision to subsidize a particular behavior. Recognizing this, Henry Simons, in his famous work on personal income taxation, indicated that parents made a voluntary decision to have children and that expenses in caring for those children were consumption decisions made by the parent.¹⁰⁷

A decision by Congress to include the number of children in the calculation of ability to pay is a decision to subsidize families with child-

106. William J. Turner, *Personal Deductions and Tax Reform: The High Road and the Low Road*, 31 VILL. L. REV. 1703, 1711-13 (1986); EDWIN R. A. SELIGMAN, *THE INCOME TAX: A STUDY OF THE HISTORY, THEORY, AND PRACTICE OF INCOME TAXATION AT HOME AND ABROAD* 5-15 (1911).

107. HENRY C. SIMONS, *PERSONAL INCOME TAXATION: THE DEFINITION OF INCOME AS A PROBLEM OF FISCAL POLICY* 140 (1938); see Allan J. Samansky, *Tax Policy and the Obligation to Support Children*, 57 OHIO ST. L.J. 329, 372 (1996). But see Lawrence Zelenak, *Children and the Income Tax*, 49 TAX L. REV. 349, 359 (1994) ("From this, it would seem to follow that money spent on children should have no more relevance to parental ability to pay income tax than money spent on vacations or sports cars."); Boris I. Bittker, *Federal Income Taxation and the Family*, 27 STAN. L. REV. 1389, 1448 (1975) (only a tax theorist would argue that spending on children was the same as spending on a yacht); Anne L. Alstott, *Comments on Samansky, "Tax Policy and the Obligation to Support Children"*, 57 OHIO ST. L.J. 381, 381-82 (1996). But Zelenak concedes that "Simons himself was not quite that doctrinaire," Zelenak, *supra*, at 359 n.49, and that Simons stated raising children is a "form of consumption on the part of parents—whether one believes in the subsidizing of such consumption or not." SIMONS, *supra*, at 140. In this Article, I am not arguing against a Dependency Exemption, but instead argue that such an exemption should be viewed as a choice by the government to subsidize a particular behavior—child rearing. This is a choice I wholeheartedly support, but if the Dependency Exemption and Child Tax Credit are subsidies to families, then there can be no justification for denying that subsidy to low-income taxpayers.

ren. A taxpayer that makes \$100,000 with no children has more money and can afford to pay more tax than a taxpayer who makes \$100,000 with 10 children. Congress has simply recognized that children are expensive and has chosen to reduce the taxpayer's taxable income because of that expense. But the decision to reduce taxable income based on the number of children is a decision by Congress that children are worthy. Congress has decided that the cost of children should be taken into account before we determine someone's tax liability.¹⁰⁸

Why do I argue this is a welfare or subsidy concept? There are many other expenses that impact one's ability to pay, and a decision by Congress to favor one over another is in fact a subsidy to the recipient of the amount saved by the deduction or credit.¹⁰⁹ For example, Congress has not provided an extra exemption to parents with a disabled or special-needs child. Obviously, it is often more expensive to care for a special-needs child than a child who does not have special-needs, so providing an increased deduction for a special needs child could be seen as necessary based on ability to pay principles. Moreover, there is no deduction for people who live in expensive cities or states, even though a person making \$100,000 per year has lower expenses in Gary, Indiana than he does for the same items in San Francisco, California.¹¹⁰ Congress has been selective, deciding that some expenses warrant a deduction and some do not. The decision by Congress that a specific expense is deductible because it impacts on ability to pay is identical to a decision by Congress that the expense is one that Congress believes is worth subsidizing. By providing the subsidy, Congress is providing a specific benefit to a specific group of people. It is just as much welfare to provide a deduction that is only warranted because a family has children as it is to provide a check to everyone who has children.¹¹¹

108. Zelenak argues that the Dependency Exemption is not a subsidy because it is based on the ability to pay principle. Zelenak, *supra* note 107, at 362. He also notes that the Joint Committee on Taxation does not consider the Dependency Exemption a tax expenditure. *Id.* at 364 n.69. Congress, however, implicitly recognized that the Dependency Exemption was a type of tax preference when it determined that the Dependency Exemption was added back into income for purposes of calculating the alternative minimum tax. See I.R.C. § 56(d) (West 2002 & Supp. 2004).

109. See Turnier, *supra* note 106, at 1711-13 (discussing how various deductions are consistent or inconsistent with the ability to pay principle).

110. For a discussion of cost of living differences and the ability to pay principle see Michael S. Knoll & Thomas D. Griffith, *Taxing Sunny Days: Adjusting Taxes for Regional Living Costs and Amenities*, 116 HARV. L. REV. 937 (2003) (concluding that ability to pay is not the best justification for adjusting tax rates by jurisdiction); Jeffrey H. Kahn, *Personal Deductions—A Tax “Ideal” or Just Another “Deal”?*, 2002 L. REV. MICH. ST. U.-DET. C.L. 1, 50 n.162.

111. I do not take issue with Zelenak's argument that “there is no political or popular support in the United States today for an income tax generally treating children as just another consumption choice.” Zelenak, *supra* note 107, at 361. I agree that some deduction or credit for children is warranted, but my preference reflects my belief that subsidizing families with children is positive. Regardless of our personal

The third rationale is to provide a deduction or credit to taxpayers because Congress wants to reward or encourage a particular type of behavior.¹¹² Under this rationale, Congress has decided to use the tax code as a means of reaching a particular policy goal. For example, Congress attempts to encourage home ownership through the mortgage interest deduction and retirement savings through individual retirement accounts. These deductions provide a direct subsidy to the taxpayer and often are referred to as tax expenditures. Tax expenditures are the cost to the government of providing specific tax benefits that reduce the general tax base.¹¹³ If the Child Tax Credit and the Dependency Exemption are merely decisions to reward families then there is really no justification for providing the subsidy only to families who have tax liability. It is tax preferences in this third category that most resemble welfare.

preferences, however, a decision by Congress to provide a dependency exemption within the framework of a person's ability to pay, is a decision by Congress to subsidize the raising of children. See also Lucy A. Williams, *The Ideology of Division: Behavior Modification Welfare Reform Proposals*, 102 YALE L.J. 719, 734 (1992) (noting that we punish AFDC parents whose children are truant, but would never think of conditioning the Dependency Exemption on a child's school attendance); Dorothy A. Brown, *The Tax Treatment of Children: Separate but Unequal*, 54 EMORY L.J. ____ (forthcoming 2005) (discussing the term welfare in the context of the Child Tax Credit and the Earned Income Tax Credit).

112. Zelenak notes two other arguments in favor of a tax subsidies to children. Zelenak, *supra* note 107, at 388. First, that we should consider the well-being of the child. *Id.* He rejects this argument because there is no connection between entitlement to the deduction and of any actual parental expenditures on the child. *Id.* at 389. The child would clearly benefit from the increase in family income, but there is no clear correlation between the increase in family income and the welfare of the child. *Id.* Second, he recognizes a human capital investment rationale (he terms an externalities rationale). *Id.* at 388. The argument is that "investment in children produces important positive externalities for society at large. . . ." *Id.* at 388. He notes that the weak link here is that the credit is not premised on proof of spending on the child. *Id.* at 389.

113. A deviation from the tax baseline causes a reduction in revenue. This reduction in revenue has a "cost" to the government. The cost to the Treasury due to a tax deduction, exemption, or credit is known as a tax expenditure. The theory is that movements away from the tax baseline are really equivalent to expenditures, because in both cases the government is giving up money. In the spending context, it is actually providing money directly to taxpayers, and in the tax context, it is foregoing revenue it would otherwise be entitled to receive. See 1 JOINT COMM. ON TAXATION, 81ST CONG., STUDY OF THE OVERALL STATE OF THE FEDERAL TAX SYSTEM AND RECOMMENDATIONS FOR SIMPLIFICATION, PURSUANT TO SECTION 8022(3)(B) OF THE INTERNAL REVENUE CODE OF 1986, at 68-69 (2001) ("[T]ax expenditures can be viewed as government spending programs that are embedded in the tax laws."); see also STANLEY S. SURREY & PAUL R. MCDANIEL, TAX EXPENDITURES 2-4 (1985) (discussing tax expenditure concept); RICHARD A. WESTIN, WG&L TAX DICTIONARY 776 (2004) (defining tax expenditure as "a diminution in government tax revenues that results from tax benefits granted for policy reasons and that diminish a comprehensive tax base"); STANLEY S. SURREY, PATHWAYS TO TAX REFORM: THE CONCEPT OF TAX EXPENDITURES 179-80 (1973) (discussing tax expenditure concept); Victor Thuronyi, *Tax Expenditures: A Reassessment*, 1988 DUKE L.J. 1155, 1155 ("The concept of 'tax expenditures' holds that certain provisions of the tax laws are not really tax provisions, but are actually government spending programs disguised in tax language." (citing SURREY, *supra*, at vii)); Julie Roin, *Truth in Government: Beyond the Tax Expenditure Budget*, 54 HASTINGS L.J. 603 (2003) (discussing the tax expenditure concept in the context of regulations); Daniel N. Shaviro, *Rethinking Tax Expenditures and Fiscal Language*, 57 TAX L. REV. 187 (2004).

Neither the Child Tax Credit nor the Dependency Exemption can be justified solely to clearly reflect a taxpayer's income. Children are not a cost of doing business, and the number of children one has does not impact what the taxpayer actually earns. It certainly impacts how far a taxpayer can stretch his income, but the deduction or credit is not necessary to clearly reflect a taxpayer's income.¹¹⁴

Congress justified the Child Tax Credit on the second and third rationale. The House Budget Committee Report states that the reason for the Child Tax Credit was that the current Dependency Exemption did not sufficiently reflect a family's ability to pay.¹¹⁵ It further noted that the Child Tax Credit would "better recognize the financial responsibilities of raising dependent children, and will promote family values."¹¹⁶ Congressional debate on the subject further indicates that Congress was trying to provide a subsidy to families with children.¹¹⁷ While there is some indication that Congress wanted to provide the benefit to "working" families, work itself was not a criterion. All that was necessary was to have sufficient income to offset the credit. A person who receives \$30,000 from a trust fund would receive the full credit, while a minimum wage worker earning \$10,000 per year would receive no credit at all.

The federal tax system therefore provides a subsidy to families with children in a somewhat bizarre and unequal fashion. Families with tax-

114. On a theoretical level it might actually decrease income because a taxpayer may shift his or her preferences away from earning money and towards her children.

115. H.R. REP. NO. 105-148, at 309-10 (1997).

116. *Id.* at 310.

117. See 143 CONG. REC. 17,108 (1997) (statement of Sen. DeWine) ("child tax credit . . . will help ease the burden of working families who need to hold down two or more jobs to make ends meet"); *id.* (statement of Sen. Dorgan) (child tax credit "will be a significant benefit to American families"); *id.* at 17,110-11 (statement of Sen. Grams) (working families "just want to go to work to make a good living, have a decent place to call home, and to have the opportunity to provide for their children. . . . child tax credit is a great victory for families"); *id.* at 17,113 (statement of Sen. Hutchinson) ("[i]t is the mothers and fathers who will get help raising their children"); *id.* at 17,124-25 (statement by Sen. Hatch) ("The child tax credit is especially important for America's working families. Raising children in today's world becomes more expensive each year. This family tax credit will put the tax relief where it is needed most, in the pockets of parents with small children."); *id.* at 16,975 (statement by Rep. Solomon) ("[t]his will better enable all American families to care for their children"); *id.* at 16,976-77 (statement by Rep. Goss) ("For families trying to pay bills . . . we have provided a . . . child tax credit. That is \$500 more that you can use for things like school clothes or taking the kids for a summer vacation . . ."); *id.* at 16,978 (statement by Rep. Pryce) ("[t]o ease the financial burden on families with children"); *id.* at 16,999 (statement by Rep. Sanchez) ("This budget gives a \$500 per child tax credit to every family in America."); *id.* at 17,007 (statement of Rep. Boehlert) ("helping working families make ends meet"); *id.* at 17,013 (statement of Rep. Arney) ("It is time for Mr. and Mrs. America, as they struggle with the needs of their family which they desire and hope and must put first, that they would have a \$500-per-child tax credit so that they can do things for their children that they know must be done . . . buying the diapers . . . paying for some kindergarten, some preschooling . . . for their braces.").

able incomes of approximately \$60,000 to \$110,000 receive the largest benefit—a tax credit of \$1,000 per child and a Dependency Exemption worth approximately \$775 per child.¹¹⁸ Poor families and families with incomes below \$10,000 receive no benefit from either the tax credit or the Dependency Exemption. Families with incomes greater than \$110,000 do not receive the tax credit, but receive up to \$1,000 due to the Dependency Exemption.¹¹⁹

The U.S. currently has a program to provide per child cash assistance, however it ignores the people who need the assistance the most and is not designed to maximize investment in children. Since the Child Tax Credit and Dependency Exemption are tax preferences to parents, there is no requirement or incentive to invest the cash assistance in the child's human capital.

4. Earned Income Credit

The Earned Income Credit (EIC) is designed to provide the equivalent of cash assistance to low-income working people.¹²⁰ The EIC provides a credit to eligible taxpayers against taxes owed. If the taxpayer is entitled to a credit that exceeds the amount owed, the taxpayer receives the remainder as income. The amount of the EIC first increases as income increases to a certain level,¹²¹ then flattens out, and then decreases.

While this program provides cash assistance to families without children, working families with children receive the greatest benefit. A taxpayer with two children earning \$10,500 in 2002 received an EIC of \$4,140, while a taxpayer with no children received a credit of \$45.¹²² At lower income levels, the EIC provides over a \$2,000 subsidy per child. The program has been justified in part as a means of compensating for

118. In 2004, taxpayers with taxable incomes from \$60,000 to \$110,000 have a marginal rate of 25% and receive the full \$1,000 tax credit. The Dependency Exemption is \$3,100. Taxpayer's benefit from a \$3,100 Dependency Exemption is \$775.

119. Families with incomes over \$336,550 receive no benefit from the Dependency Exemption because it is fully phased out. *See* Rev. Proc. 2003-85, 2003-49 I.R.B. 1184.

120. *See* I.R.C. § 32 (West 2002 & Supp. 2004). For a more detailed explanation of the Earned Income Tax Credit see POSIN & TOBIN, *supra* note 96, at 639-40.

121. In 2002, the credit for a taxpayer with two children increased as the taxpayer's income rose to \$10,350. At that point, the taxpayer received a maximum credit of \$4,140. The subsidy was then held constant until the taxpayer's income reached \$14,550. As the taxpayer's income exceeded \$14,550, the credit diminished, ultimately becoming zero when earnings reached \$34,178. *See* POSIN & TOBIN, *supra* note 96, at 640; *see also* INTERNAL REVENUE SERVICE, PUB. 596, CAT. NO. 15173A 40-44, Earned Income Credit (EIC): Are You Eligible? (2003), available at <http://www.irs.gov/pub/irs-pdf/p596.pdf>.

122. INTERNAL REVENUE SERVICE, *supra* note 121, at 29-44.

the regressive payroll tax,¹²³ but the main point of the program is as a wage support for low-income workers.¹²⁴ It is another method of providing cash assistance, through the tax code, to families with children. Once again, however, it is cash assistance to families and there is no requirement that the money received be spent on the recipient's children.

5. Temporary Assistance to Needy Families

In 1935, Congress established Aid to Families with Dependent Children (AFDC), which provided cash assistance to needy families with children.¹²⁵ In 1996, as part of the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (PRWORA), Congress significantly modified the program and Temporary Assistance to Needy Families (TANF) replaced AFDC as the main financial support to poor families with children.¹²⁶ In actuality, when Americans discuss "welfare," they are usually talking about TANF, and to a lesser extent food stamps.¹²⁷ Unlike AFDC, however, TANF is not an entitlement program, so qualifying recipients are not guaranteed assistance. Instead, TANF provides block grants to the states, which are charged with creating and operating assistance programs in accordance with federal regulations.¹²⁸ Benefit levels vary depending on the state and on family size, but generally average around \$163 per month per person or \$428 per month per family.¹²⁹

123. S. REP. NO. 94-36, at 11 (1975) (noting families who currently pay little or no income tax have been hurt by rising food and energy costs and this credit provides help for those who have to pay payroll taxes).

124. *Id.*

125. Social Security Act, Pub. L. No. 74-271, ch. 531, §§ 401-406, 49 Stat. 620, 627-29 (1935) (codified as amended at 42 U.S.C. §§ 601-06 (2000)). For a complete history of aid to the poor in the United States, see MICHAEL B. KATZ, *IN THE SHADOW OF THE POOR HOUSE* (1986).

126. The Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (PRWORA), Pub. L. No. 104-193, 110 Stat. 2260 (codified at 8 U.S.C. §§ 1601-02) (2000).

127. For a discussion of TANF and welfare reform, see, for example, PETER EDELMAN, *SEARCHING FOR AMERICA'S HEART: RFK AND THE RENEWAL OF HOPE* 119-43 (2001), R. KENT WEAVER, *ENDING WELFARE AS WE KNOW IT* 328-35 (2000), and MICHAEL B. KATZ, *THE PRICE OF CITIZENSHIP: REDEFINING THE AMERICAN WELFARE STATE* 322-27 (2001). For a discussion of the "single minded" focus of cash assistance as "welfare," see David A. Super, *The Quiet "Welfare" Revolution: Resurrecting the Food Stamp Program in the Wake of the 1996 Welfare Law*, 79 N.Y.U.L. REV. 1271 (2004), and Brown, *supra* note 111.

128. 42 U.S.C. §§ 601-17 (2000).

129. U.S. DEP'T OF HEALTH AND HUMAN SERVICES, *INDICATORS OF WELFARE DEPENDENCE: ANNUAL REPORT TO CONGRESS*, app. A, at A-13, available at <http://aspe.hhs.gov/hsp/indicators02/>; see also Thomas L. Gais & Cathy M. Johnson, *Welfare Reform, Management Systems, and Their Implication for Children*, 60 OHIO ST. L.J. 1327, 1350-51 (1999) (examining state TANF benefits by quintile of caseload changes and finding a maximum benefit at the bottom of \$309 and a maximum benefit at the top of \$564).

In addition to creating a block grant program, PRWORA also set limits on the number of years a family can receive cash assistance. Under PRWORA, a recipient is allowed 24 consecutive months at a time to find employment before her benefits stop, and she may not receive benefits for more than a total of five years.¹³⁰

TANF was a shift in welfare policy to a more punitive form of assistance. TANF provides for significant sanctions against recipients who do not comply with certain behavioral norms. For example, states are permitted to deny benefits to teenage mothers, to children of recipients born after a family started collecting TANF, and to recipients whose children are truant.¹³¹ Moreover, states may not use grant money provided under TANF to provide benefits to people who have been convicted of a drug felony.¹³²

The idea is that if a welfare recipient is faced with living "right" or starving, she will choose the former. But a recent study of Iowa mothers found that only about one-half of the mothers who lost their welfare benefits then found jobs.¹³³ Thus, thousand of families, and thousands of children, found themselves without income and without government support. Furthermore, the termination or decrease in TANF benefits is associated with higher odds that children will experience hunger and hospitalization.¹³⁴

Even if society rightly determines that parents who engage in the above behavior are unworthy of public support, their children also are hurt by these punitive measures. The two-year-old child did nothing wrong, but is penalized simply for being born to parents who do not obey the law.¹³⁵ Unless society decides to put children in the above

130. 42 U.S.C. §§ 602(a)(1)(A)(ii), 608(a)(7) (2002). Up to 20% of the state's caseload may include mothers who have exceeded the cap due to economic hardship. *See id.* § 608(a)(7)(C).

131. AFDC provided fairly strict requirements regarding eligibility rules and benefits and states were required to receive waivers from the government in order to deviate from those specific rules. *Id.* § 615. States were thus required to apply for waivers to implement family caps or to deny benefits to teen mothers. As part of TANF, states must comply with certain requirements, but have considerably wider latitude to design and implement their assistance programs. *See id.* § 602 (basic requirements for plans). There is no prohibition under TANF for states to impose family caps or restrictions on teenage beneficiaries, and the lack of prohibition means that states can implement such programs if they so choose. Moreover, 42 U.S.C. § 602(a)(7)(A)(iii) requires states' plans to include provisions that allow for waiver of requirements, including a family cap, if those requirements unfairly penalize individuals who are at risk of, or victims of domestic violence. *See also id.* § 604(i) (state may sanction for truancy).

132. 21 U.S.C. § 862a(b) (2000) (felony drug convictions).

133. Duncan & Brooks-Gunn, *Family Poverty*, *supra* note 25, at 191-92.

134. John Cook et al., *Welfare Reform and the Health of Young Children: A Sentinel Survey in 6 U.S. Cities*, 156 *ARCHIVES PEDIATRICS & ADOLESCENT MED.* 678, 681 (2002).

135. *See* Cynthia Godsoe, *The Ban on Welfare for Felony Drug Offenders: Giving a New Meaning to Life Sentence*, 13 *BERKELEY WOMEN'S L.J.* 257 (1998) (discussing the impact on children of denying welfare benefits to drug offenders).

categories in foster care or orphanages because of their parents' poverty or bad behavior, it must come up with some mechanism of ensuring that young children are not victimized due to the actions of their parents.¹³⁶

TANF thus operates as a short-term cash assistance program to qualifying families with children. It is designed to help families survive while they are facing dire economic consequences. It is only available to the very poorest in society and serves a social purpose. Families that receive TANF have little opportunity to use the funds as an investment.¹³⁷ Moreover, like the Dependency Exemption and the Child Tax Credit, TANF provides cash assistance to the family, not the child. It is not designed to provide specific benefits to the child. In fact, TANF benefits are disseminated and terminated based on the parent's actions.

B. Previous Policy Proposals Designed to Increase Assistance to Families with Children or to Increase Investment in Children

This section discusses various proposals to increase child well being that have been suggested over the last 40 years. The literature is rich with examples of programs and proposals to support human capital investment and family incomes. Some of these proposals are briefly described here because they provide an excellent background for the proposal I suggest in Part IV of this Article. These proposals are grouped into two categories—programs designed (1) to increase human capital investment and (2) to provide minimum income assistance.

1. Human Capital Investment

In the late 1960s, James Tobin proposed a "National Youth Endowment,"¹³⁸ to attempt to equalize investment in human capital for the nation's youth. Under this program, upon graduation from high school or the attainment of age 19, every child would receive an endowment of \$5,000. The child could use the endowment to pay for higher education, vocational training, apprenticeships, and other forms of on-the-job

136. Michael Wines, *Team in Place, Gingrich Comes Out Slugging*, N.Y. TIMES, Dec. 7, 1994, at B11 (discussing Newt Gingrich's proposal that orphanages may be preferable to the arrangement the current welfare system makes for some children).

137. In fact, as Creola Johnson notes in her recent work on welfare, although TANF provides incentives for recipients to accumulate assets to purchase a home or to fund education, it does not allow asset accumulation for basic human capital needs. For a discussion of welfare reform and asset accumulation see Creola Johnson, *Welfare Reform and Asset Accumulation: First We Need a Bed and a Car*, 2000 WIS. L. REV. 1221.

138. James Tobin, *Raising the Incomes of the Poor*, in AGENDA FOR THE NATION: PAPERS ON DOMESTIC AND FOREIGN POLICY ISSUES 77, 92 (Kermit Gordon ed., 1968).

training. Tobin did not describe an in-depth payback plan, but indicated that the recipient would be required to pay back the endowment through higher income taxes after age 28. Tobin's proposal, however, was not mandatory, and young adults were not required to use their endowments.

Around the same time, William Klein advocated that every child who graduates from high school or reaches age 18, receive a set of capital accounts from the government.¹³⁹ The individual could withdraw funds from the account for education or health expenses. As part of this proposal, Klein assumed the existence of a basic income support system in addition to the capital accounts, so he proposed that the capital accounts should be drawn down only for education or health expenses. Some 20 years later, as part of a major project dealing with poverty, Robert Haveman proposed personal capital accounts for youth, which could be used to purchase education, training, and health care services.¹⁴⁰ Neither Klein nor Haveman envisioned a direct payback by the recipients of the fund.

Other scholars have examined and proposed assistance to children on income distribution grounds.¹⁴¹ Roberto Unger advocates "social endowment accounts" to affect the inequities created by inter-generational transfers. People may receive such transfers through private inheritance and/or the advantages of education and social status. Unger believes that these inter-generational transfers make it very difficult for the underclass to move up the economic ladder. He argues that social endowment accounts paid for by the government should replace private inheritance.¹⁴²

Similarly, Bruce Ackerman and Anne Alstott have proposed that every citizen receive an \$80,000 "stake" upon reaching the age of 18.¹⁴³

139. William A. Klein, *A Proposal for a Universal Capital Account*, in INSTITUTE FOR RESEARCH ON POVERTY: DISCUSSION PAPERS 109 (1972).

140. ROBERT HAVEMAN, *THE TWENTIETH CENTURY FUND, STARTING EVEN: AN EQUAL OPPORTUNITY PROGRAM TO COMBAT THE NATION'S NEW POVERTY* (1988).

141. Roberto Mangabeira Unger, *The Practical Promise of Democratic Experimentalism: From the Existing Policy Debate to the Missing Programmatic Conversation*, in WHAT SHOULD LEGAL ANALYSIS BECOME? 11, 14-15 (1996); ROBERTO MANGABEIRA UNGER, *DEMOCRACY REALIZED: THE PROGRESSIVE ALTERNATIVE* 51, 209 (1998); ROBERTO MANGABEIRA UNGER & CORNEL WEST, *THE FUTURE OF AMERICAN PROGRESSIVISM: AN INITIATIVE FOR POLITICAL AND ECONOMIC REFORM* 62 (1998) (advocating social-endowment accounts as a tool for self-reliance).

142. Unger, *The Practical Promise*, *supra* note 141, at 14-15.

143. See BRUCE ACKERMAN & ANNE ALSTOTT, *THE STAKEHOLDER SOCIETY* 38 (1999). If a qualifying individual fails to graduate from high school, the interest of the stake is provided in smaller increments over a number of years. *Id.* In her new book, Anne Alstott proposes a caretaker allowance, which would provide parents or legal guardians of children under age 13 with a \$5,000 payment that could be used for child care while the adult works, the adult's education, or to set up a retirement fund. See ANNE L. ALSTOTT, *NO EXIT: WHAT PARENTS OWE THEIR CHILDREN AND WHAT SOCIETY OWES PARENTS*

Their proposal is very similar to the National Endowment Accounts suggested by Tobin. The main difference is that the stake can be used for any purpose. Although Ackerman and Alstott recognize the benefits of human capital investment that may occur due to the "stake," it is not their justification for the proposal. Their proposal rests more on egalitarian grounds. They argue that by providing each American with \$80,000, all Americans will have a chance at the American dream.¹⁴⁴ Some will use the stake for education, others for investment in a small business, and others will spend the money in foolish ways, but under Ackerman and Alstott's proposal every American has a similar opportunity to manage his stake.¹⁴⁵

Ackerman and Alstott's plan requires that the stake be paid back at death, if sufficient funds exist in the estate.¹⁴⁶ But, since most 18 year olds will not die for over 50 years, Ackerman and Alstott recognize the need for a current financing mechanism. They propose that for the near future the stake should be paid for with a two percent tax on wealth.¹⁴⁷

Although these plans are designed to provide the equivalent of cash assistance, and in many cases to encourage human capital investment, the programs are aimed at the wrong age group and are implemented in the wrong way. First, all the proposals provide assistance to individuals once they reach the age of 18. For purposes of human capital investment, this is too late. While Ackerman and Alstott want to even the playing field and ensure that each citizen "is free to shape her outcomes," providing the stake at 18 does not serve this purpose.¹⁴⁸ A child with poor education, poor health, or poor nutrition does not start in the same place as children without such problems. The children who suffer from lower human capital investment will not be in the same position to take advantage of the stake. The investment must take place well before age 18. Tobin, Klein, and Haveman's proposals suffer from the same limitation.¹⁴⁹

Second, all the proposals except Ackerman and Alstott's require that the capital investment come from general funds, and there is no requirement that the funds be paid back. Although I have no problem with assistance to children being paid from the general fund, there is clearly

(2004). This program differs significantly from the one proposed in this Article because the money is provided to the caretaker, not the child, and is not designed to increase the child's human capital.

144. ACKERMAN & ALSTOTT, *supra* note 143, at 24.

145. *Id.* at 9. As Ackerman and Alstott recognize, some Americans will have their "stake" and more. Since everyone receives a stake, those with more economic resources will receive a "stake" plus.

146. *Id.* at 90-93.

147. *Id.* at 102.

148. *Id.* at 24.

149. Tobin, *supra* note 138, at 92; HAVEMAN, *supra* note 140, at 155; Klein, *supra* note 139, at 4.

no national support for such a proposal. Moreover, to the extent the proposal is not funded, it is open to the same criticisms that have been levied against AFDC and TANF. Finally, if the benefit is seen as welfare, Congress will be more willing to place controls or constraints on the beneficiaries. Congress could deny funds to felons, drug users, or children who have been suspended from school. It may be that these children are the ones most in need of human capital investment. In this political climate, a program must have a strong payback component to have any chance of success. Moreover, the payback plan must be tied to the needs of the population that receives the benefit.

Third, many of the proposals do not allow the accounts to be used broadly enough. To the extent the accounts can only be used for education or health, they fail to provide a sufficiently broad base for human capital investment. A family with food insecurity or poor housing should be able to use the funds to purchase food or pay the rent. Families should also be able to use the funds for child care, preschool, or other educational programs.

Finally, to the extent possible, a broad-based mandatory program is preferable to an optional one. For economic, administrative, and societal reasons, the program will be stronger if all children receive the benefit. On economic grounds, the greater diversity in the pool of recipients, the greater chances that a payback plan will work. If the plan is optional, there is a greater chance that only the "risky" investors will participate.

A mandatory plan will provide better stability for the program and will be easier to administer. All children will be considered to have participated and will be required to participate in paying the funds back. These attributes ensure that the program will not be seen as a welfare program for the poor. Just as Social Security recipients are not viewed as "on welfare," there will be no stigma attached to receiving benefits as part of a broad-based child human capital investment program.¹⁵⁰

150. See Martha B. Coven, *The Freedom to Spend: The Case for Cash-Based Public Assistance*, 86 MINN. L. REV. 847, 891 (2002).

2. Minimum Income Assistance

Several prominent scholars, including Milton Friedman¹⁵¹ and Anne Alstott,¹⁵² have advocated a basic income support system.¹⁵³ One popular mechanism for providing a basic level of income is the negative income tax. The negative income tax generally provides for a tax credit designed to reflect the basic needs of an individual in society. To the extent an individual has no tax liability because his income is too low, the tax credit is fully refundable. Thus, if the tax credit for subsistence was set at \$10,000, a person with no income would receive a tax credit of \$10,000. A person with \$100,000 of income and \$30,000 of tax liability would receive a \$10,000 credit and therefore have a tax liability of only \$20,000.

Because the credit is integrated into the progressive nature of the tax code, the benefit of the credit gradually decreases as a person earns more income. The person is always better off, however, by working. For example, a person with no income would receive a negative income tax payment of \$10,000. If a person's income rose from zero to \$5,000, the \$5,000 would be taxable at the prevailing marginal rate, say 15 percent. The individual would thus have an initial tax of \$750. The \$10,000 credit would then be applied and he would receive a negative income tax payment of \$9,250. By earning an additional \$5,000, the individual would be able to raise his total from \$10,000 to \$14,250 (\$9,250 negative income tax + \$5,000 of income). Although there is obviously some cost to earning money, the negative income tax is designed so that a person will have an economic incentive to increase his earnings.¹⁵⁴

The negative income tax is not premised on human capital theory. Friedman argued that, through various social welfare programs, the

151. Milton Friedman, *The Case for the Negative Income Tax*, in *REPUBLICAN PAPERS* 202 (Melvin R. Laird ed., 1968); MILTON FRIEDMAN, *CAPITALISM AND FREEDOM* 190-94 (1962) [hereinafter *FRIEDMAN, CAPITALISM*].

152. Anne Alstott, *Work vs. Freedom: A Liberal Challenge to Employment Subsidies*, 108 *YALE L.J.* 967 (1999).

153. The idea of providing a basic minimum income for all has enjoyed bi-partisan support. In addition to Friedman's negative income tax proposal, President Nixon also proposed a minimum family income benefit for all citizens. See Family Assistance Act of 1969, H.R. 14,173, 91st Cong. (1st Sess.); VINCENT J. BURKE & VEE BURKE, *NIXON'S GOOD DEED: WELFARE REFORM* (1974) (discussing the history of Nixon's proposal); see also James Tobin, *The Case for an Income Guarantee*, 4 *PUB. INT.* 31, 36-38 (1966) (promoting the idea of an income guarantee); James Tobin et al., *Is a Negative Income Tax Practical?*, 77 *YALE L.J.* 1, 1-4 (1967); Daniel Shaviro, *The Minimum Wage, the Earned Income Tax Credit, and Optimal Subsidy Policy*, 64 *U. CHI. L. REV.* 405, 469 (1997); Alstott, *supra* note 152; Robert J. Lampman, *Approaches to the Reduction of Poverty*, 55 *AM. ECON. REV.* 521, 526-27 (1965).

154. See Friedman, *Negative*, *supra* note 151, at 208; *FRIEDMAN, CAPITALISM*, *supra* note 151, at 192-95.

government already provided a minimum annual income.¹⁵⁵ He argued that a negative income tax was a more efficient method of distributing such aid because the existing programs were not well targeted for those in need.¹⁵⁶ He further argued that his proposal, unlike current welfare programs, "treat[ed] indigents as responsible individuals, not incompetent wards of the state."¹⁵⁷ He argued that a negative income tax would give the poor responsibility over their own welfare, thus increasing their self-esteem and independence.¹⁵⁸

Friedman's proposal is based on different grounds than the one presented here. He sought to provide minimum income to all. My proposal is far more limited and less monumental. I advocate a method for increasing investment in children and thus increasing their welfare. Friedman's proposal would do that as well, since some of the tax credit obviously would trickle down to children. Although Friedman's proposal received strong support for a period of years, it has been more than 30 years since he first advocated the negative income tax. Smaller steps must be taken.

The proposal I advocate is designed to incorporate policies and theories that can be supported by liberals and conservatives. It is interesting that both Friedman (traditionally thought of as conservative) and Ackerman and Alstott (traditionally thought of as liberal) have coalesced around the idea of personal empowerment. Both proposals advocate giving people power over their financial decisions and limiting government interference in the way funds are expended. My proposal embraces this personal empowerment theory and attempts to provide a mechanism whereby individuals, and not government, make decisions regarding how the funds should be invested.

IV. INVESTING IN CHILDREN THROUGH A SELF-SUSTAINING CHILD INVESTMENT PLAN

This Part proposes an investment program for children. After briefly summarizing the proposal, subpart B discusses the program components and addresses some of the potential criticisms of the proposal. Subpart C examines other more limited options for investing in children and considers two types of non-mandatory proposals to increase investment in children.

155. Friedman, *Negative*, *supra* note 151, at 202.

156. *Id.* at 214.

157. *Id.* at 211.

158. *Id.*

A. A Summary of the Proposal

In order to increase investment in children and provide a minimum subsistence level of benefits to children, I propose that every child under age 15 receive a payment of around \$2,000 per year. The money belongs to the child, and a parent or another responsible adult acts as a fiduciary over the money.¹⁵⁹ The money may be used for any purpose consistent with that fiduciary duty.¹⁶⁰

For example, if families are in extreme poverty—income at less than one-half of the poverty level—the parent could use the payment for food, clothing, or housing for the child. Parents slightly above poverty might choose to save it for college, use it to provide better day care for their child, send their child to private school, or move to a better neighborhood. Middle-income families might save it for the child's higher education, send their child to private school, or provide the child with a "nest egg" when she leaves home. At all levels of income, the payment might serve as money of last resort when a child becomes seriously ill.

The point is that adults, acting as fiduciaries for the child, decide how the payment should be spent. The goal is for the parents to use the money to increase human capital investment in their children. The plan recognizes that parents, not the government, are generally the best judge of what particular investment best serves the child's needs. Just as the government exercises very little oversight regarding how Social Security payments are spent, it should exercise very limited oversight here.

But since this money is designed as a public investment, not a subsidy, the child is responsible for paying back the amount she receives. Once the program is in full effect, every person who received the payment would pay in taxes an extra two percent of adjusted gross income. The child thus will pay back the amount invested over his or her working life.¹⁶¹ As with Social Security, some children will pay back more and

159. Under common law, some states recognize that parents, in exchange for their support, have a right to their child's earnings. See *Hines v. Cheshire*, 219 P.2d 100 (Wash. 1950) (parent has the right to the child's earnings); *Raney v. Barnes Lumber Corp.*, 81 S.E.2d 578 (Va. 1954); *Reyna v. Vowell*, 470 F.2d 494 (5th Cir. 1972) (Texas law); *Mitchell v. Mosher*, 362 S.W.2d 532 (Mo. 1962); *Immel v. Richards*, 93 N.E.2d 474 (Ohio 1950).

160. Depending on state law, parents do not necessarily have a fiduciary duty to their child. Compare *Murphy v. Murphy*, 694 A.2d 932 (Me. 1997); *In re The Marriage of William T. Glover v. Torrence*, 723 N.E.2d 924 (Ind. 2000); *State v. Crystal D. Gould*, 23 P.3d 801 (Kan. 2001) (finding a fiduciary duty between parent and child) with *Estate of John A. Kieras v. Kieras*, 521 N.E.2d 263, 266 (Ill. 1988) ("the relationship between parent and child is not fiduciary as a matter of law"); *Curtis v. Freden*, 585 P.2d 993, 998 (Kan. 1978) ("The mere relationship of parent and child does not raise a presumption of a confidential and fiduciary relationship.").

161. Because the payback is tied to gross income, a person starts paying back the amount received

some less, but every recipient who works will make some payment in return for the investment.¹⁶²

B. Program Components—How the Proposal Would Work

1. Child Investment Fund

The assistance to children under this program will be cash assistance. I have specifically rejected using vouchers or other types of cash equivalents. The child investment funds need to be used in ways that are the most beneficial to the child. For some children, the best use of the funds might be to hire a nanny; in other cases, the money might best be used to provide better housing or to purchase food. If vouchers or other cash equivalents were used, children would have fewer options regarding the use of the investment funds, and the funds might not be used in the most efficient manner.¹⁶³

Moreover, using non-cash equivalents will most likely hurt poor and low-income individuals. Children in upper-middle and higher-income households will not necessarily consume the benefit immediately. They will likely save the money for their child's education or some other future expenditure because they are meeting the current consumption and investment needs of their children. Any voucher they received would be placed in an appropriate savings mechanism for the child's future.¹⁶⁴ Lower-income families, however, will need to make investments now, and the types of human capital investments they may need to make will be those least accommodated by vouchers.¹⁶⁵

For example, a lower-income person may want to use the child benefit to put her child in better home day care. It would be a significant administrative burden to require all home day care operators to accept payment through the voucher system. Similarly, the family might want to use the money for food or clothes at local stores or to pay rent or other housing costs. Forcing the providers of these items to

once they have gross income. The payback, therefore, may start at any age. Similarly, the payback stops once a person has no gross income.

162. Throughout the course of the program, interest rates and risk factors will change. The payback tax and payment amount may need to be adjusted to ensure that the program remains fiscally neutral.

163. For an excellent discussion defending the use of cash assistance see Coven, *supra* note 150.

164. This is a perfectly appropriate use for the money. Most families in the United States struggle to finance their children's education. To the extent middle- and upper-income families are already providing sufficient current capital investment for the future, it makes sense for them to save the amount received for future human capital investment.

165. For a discussion of how cash transfers increase human dignity and reduce social stigma see Coven, *supra* note 150, at 890.

accept vouchers could be onerous. Cash payments, however, are flexible and thus essential to maximize human capital investment in children. To the extent that one designs a voucher or other non-cash assistance program flexibly enough to accommodate these concerns, then the voucher is really no different than cash.

2. Child Fiduciary

The benefits will be distributed to children through a government agency, most likely the IRS or the SSA, in a manner similar to that used by Alaska. Parents, guardians, or other responsible adults will apply for the benefit on the child's behalf upon the birth of the child.¹⁶⁶ These responsible parties will be considered the Child's Fiduciary (CF) and will be charged with making decisions regarding how the Child Investment Funds should be spent.¹⁶⁷ There is, however, a serious question regarding how much leeway or control the CF should have over the child's money.

One option, following the Alaska model, would be to impose almost no regulation or oversight on the CF's investment decisions. The government would distribute the benefit and the CF would be required to spend the funds for the child's benefit, but there would be no accounting for how the money was spent. This is similar to the way in which Social Security benefits are paid to adults.

The Alaska model is inappropriate in this context because it fails to properly direct the payment to the child and is ripe for abuse. Such a system would make the Child Investment Fund a family benefit almost undistinguishable from the Child Tax Credit. This is particularly improper in the context of this program because the child is going to have to pay back the amount received when he starts working.

A second option would be to have fairly strict government control over the payment. The government would mandate that a CF could use

166. If someone fails to apply for the child benefit on behalf of the child, the money will accrue in a "child investment account." The amount in the account will earn interest. Once a CF is appointed, the CF will be able to draw down the funds in the investment account. If no CF is ever appointed for the child, the child will be able to apply for the funds in the account when he or she reaches the age of 18.

167. The CF would be chosen through a set of default rules similar to those used by the SSA in selecting a representative payee. Default rules would provide that in cases where the child lives with his parents, the parents jointly would be the CF. If the parents were not married, then the CF would be the parent who has custody of the child. If the parents were incompetent, under age 18, or otherwise not capable of carrying out the responsibilities of a CF, the CF for the child would have to be appointed by a relevant government agency.

the funds only for a qualified purchase.¹⁶⁸ As previously discussed in the voucher context, a program that significantly limits a CF's flexibility to make investments in the child may inhibit people from making the exact kinds of investments that are most needed for their particular child.

Another option would be to have a social worker system in which each child would have a social worker assigned to monitor how the child's investment benefit was spent. For example, France has a very complex system of benefits to families with children.¹⁶⁹ Raising children is considered both an individual and a communal responsibility, and a state social worker is assigned to aid each family. The U.S. could design a similar system, however, it would be administratively burdensome and extremely expensive. It would also be very intrusive and propel the government into intimate family decisions.

My proposal employs a middle ground among these options: a CF will have a statutorily imposed fiduciary duty to spend the child benefit in a way that aids investment in the child's human capital.¹⁷⁰ It would be necessary for the federal government to mandate the CF's duty because state common law is in conflict regarding whether a parent has a fiduciary duty to the child.¹⁷¹ In some states, like Alaska, the parent is deemed to have control, and in some cases, ownership, over the child's money.¹⁷²

Elizabeth Scott and Robert Scott have developed a theory of examining and treating the parent-child relationship as a fiduciary one.¹⁷³ Although I do not need to adopt their theory for the entire parent-child relationship, it does provide a nice basis for establishing a fiduciary duty under this proposal. A fiduciary duty is generally defined as the duty to act for another's benefit.¹⁷⁴ In business, it encompasses the duties of care and of loyalty. The duty of care requires a CF to use reasonable diligence in managing the child's money and deciding how to expend

168. For example, James Tobin, in his proposal for human capital accounts, would allow the payment to be used for "higher education, vocational training, apprenticeship, and other forms of on-the-job-training." Tobin, *supra* note 138, at 92. For the program to qualify, he would require that the recipient be approved by a government agency.

169. See BARBARA R. BERGMANN, *SAVING OUR CHILDREN FROM POVERTY: WHAT THE UNITED STATES CAN LEARN FROM FRANCE* (1996).

170. For example, the Uniform Transfer to Minors Act a custodian must exercise "the standard of care that would be observed by a prudent person dealing with property of another." UNIF. TRANSFERS TO MINORS ACT § 12(b) (1983).

171. See *supra* note 160 and accompanying text.

172. See *supra* note 159.

173. Elizabeth S. Scott & Robert E. Scott, *Parent as Fiduciaries*, 81 VA. L. REV. 2401, 2419 (1995) (fiduciary relationship captures the essence of a parental obligation to serve the child's interests).

174. BLACK'S LAW DICTIONARY 410 (7th ed. 1999).

the funds. The duty of loyalty requires the CF to put the interests of the child first when considering how to spend the benefit.

The standard for judging whether the CF is acting properly will be whether the CF is investing the funds in a reasonable manner for the child's benefit. The relevant government agency could promulgate rules that would provide a safe harbor for expenditures made by the CF. For example, the regulations could indicate that educational expenses, day care, food, housing, and tutoring are permissible expenditures. In order to ensure flexibility, the regulation should be designed to create such a safe harbor without restricting the CF's discretion.

Granting the CF broader discretion, however, increases the chance that a CF will abuse that discretion and misallocate funds. But as Scott and Scott recognize in their discussion of a parent's fiduciary duty, "[t]he affective bond provides powerful grounding for a parental precommitment to care for the welfare of one's child."¹⁷⁵ Social norms will act as informal rules to ensure that parents act in a way that is in the best interest of the child. In other words, most CFs will properly invest the funds in their child's human capital.

Finally, the misuse of a child's investment benefit is an abuse of the child's trust. There is no question that some parents currently abuse their children's trust, but in most cases the state attempts to take action against parents for such abuses. Nothing is more precious than a child's health and safety. If a parent can be trusted with custody of the child, it is reasonable to trust that same parent with the duty to manage the Child Investment Fund.

It is inevitable, however, that some CFs will abuse their positions as fiduciaries. An administrative system would have to be created to adjudicate complaints without overburdening the legal system. There appears to be no great answer to this problem, but there are two existing models that provide examples of how fiduciary relationships between parents and children are enforced. Under the Uniform Transfer to Minors Act, the custodian, usually the child's parent, is required to act as a "prudent person" dealing with another's property.¹⁷⁶ The custodian is also required to keep records of all transactions and make them available to the parent or the minor if the minor is at least 14 years old.¹⁷⁷ If a custodian breaches his duty to the child, the child may bring an action against the custodian to recover the lost funds.¹⁷⁸

175. Scott & Scott, *supra* note 173, at 2434.

176. *See supra* note 170.

177. UNIF. TRANSFERS TO MINORS ACT § 12(d) (1986).

178. *See In re the Marriage of Beverly Robin Rosenfeld*, 668 N.W.2d 840, 845 (Iowa 2003) (father misappropriate daughters UTMA funds and was required to repay); *Buder v. Sartore*, 774 P.2d 1383

There are very few reported cases involving a child suing a parent for mismanagement of UTMA accounts and almost all the conflicts arise in divorce cases.¹⁷⁹ UTMA funds, however, have a natural check against abuse because a family member usually gave the child the funds in the first place. The Child Investment Fund, however, will be a government benefit that the child will have to pay back, and it will be paid to every child regardless of circumstance. There is a significant risk that providing children with an action against their parents will be unworkable in the Child Investment Fund situation.

The SSA deals with this problem by requiring an accounting by the representative payee, by reserving the right to revoke the right to be a representative payee, and by requiring the representative payee to pay back funds that were not spent on the child's behalf. These same tools can be used to sanction CFs who abuse their fiduciary responsibilities.

A CF would be required to file (with his income tax return) a one-page form indicating how the child benefit was spent. The agency in charge of implementing the program would have the authority to question a CF regarding the form and take action to ensure that the CF was not abusing his position of trust. The agency also could question the CF based on a referral from a social service agency or an individual complaint. In fact, the child benefit might provide a mechanism for social services to provide real help to a struggling family, by providing early intervention when a problem arises. In addition, if the supervising agency found a violation by the child fiduciary, the agency could order that the funds be repaid to the child.

3. Who Receives the Benefit?

As previously discussed, the child investment benefit is provided directly to the child. Unlike the Child Tax Credit or TANF, this investment benefit is specifically designed to increase investment in the child. In a study on family spending patterns, Lazear and Michael found that a family spends approximately \$38 per child for every \$100 spent per adult.¹⁸⁰ Thus, two adults with two children can be expected to spend

(Colo. 1989) (father breached fiduciary duty to children when he failed to prudently invest certain of their funds and used the funds for his own personal use. The father was required to pay back the funds with interest.); *In re Levy*, 412 N.Y.S.2d 285 (N.Y. Sur. Ct. 1978) (recognizing an action by children against their mother, the custodian of UTMA accounts, for commingling funds and using the children's funds to pay the debts of husband's estate).

179. See cases cited *supra* note 178.

180. EDWARD P. LAZEAR & ROBERT T. MICHAEL, ALLOCATION OF INCOME WITHIN THE HOUSEHOLD 6-7, 77-114 (1988) (thus 27.5% of expenditures are spent on the child); see also LINO, *supra* note 11, at 12 (indicating that a one child family spends from 26% to 33% of its income on its child).

\$55 on their children for every \$200 they spend on themselves. If the hypothetical four-person family was entitled to a Child Tax Credit of \$2,000, approximately \$550 of that would be spent on the child and presumably some fraction of the amount spent on the child would be spent investing in the child's human capital.

If the benefit is delivered directly to the child, the entire amount of the benefit should be spent on the child. A direct child investment benefit increases the chances that the money will actually be invested in the child's human capital. Such an investment is particularly important in this program because the child, not the parents, is responsible for paying back the funds received.

In addition, the benefit is designed to ensure that children in our society are cared for and have the ability to realize their potential. The goal would be to support a broad-based program that was available to everyone living in the United States. Realistically, however, since this program is designed to provide an investment in children with a commensurate payback, the program needs to be targeted to those children who will likely be in the United States during their working years. I would therefore require that recipients be United States citizens or resident aliens to receive the benefits under this program.

The Child Investment Fund program is also available only to children under 15 years of age. The program is limited for several reasons. First, it appears that the greatest deficit in childhood investment is in the early years.¹⁸¹ By age 15, certain investments, like child care and pre-kindergarten education, are no longer necessary. Second, in most states, children at age 15 may engage in part-time employment and the teen's own initiative can make up for the lost benefit. Third, the program proposed here is expensive and is designed to be fully paid for with only a minor drain on the recipient's future resources. Stopping the payment after age 14 is simply more affordable than continuing the program through age 17.¹⁸²

4. Costs of the Program

This program provides a vision for the future and is designed to ensure that each child in America receives at least a minimum level of human capital investment.¹⁸³ The exact budget implications of the

181. See, e.g., Duncan & Brooks-Gunn, *Family Poverty*, *supra* note 25, at 188.

182. In fact, a less grandiose version could be implemented that provides the benefit only to children up to age six. This would significantly limit the amount of investment in children, but would be far more affordable and would provide cash assistance to children when they need it the most.

183. The idea is to provide a set amount of capital investment each year. Absent a prohibition, the potential income stream could be sold on the market for a set fee based on a discount rate. For example,

program are immensely complicated and vary greatly depending on interest rates, inflation, and other economic assumptions relied upon in the calculations. Moreover, the costs of the program also depend on whether one expects children to pay back the amount received plus the costs of inflation (thus each child is paying back what he received), or whether one expects them to pay back the amount received plus interest (thus providing for a market rate payback of the amount received). Finally, one's view of the cost of the program also depends on whether the government makes an up-front investment in the program, ameliorating the significant start-up costs.

One way of examining the cost of the program without complicated economic models is to determine whether the program is self-sufficient once it is fully phased in. There are approximately 60 million children under the age of 15, and this population demographic has held relatively constant over the last several years.¹⁸⁴ Under these assumptions, in any given year the government would be required to distribute approximately \$120 billion to children. In 2000, the total adjusted gross income for taxpayers was \$6.42 trillion.¹⁸⁵ A two percent payback tax tied to gross income would raise approximately \$128.5 billion. Thus, if the program had existed in 2000, the amount paid in would exceed the amount paid out by approximately \$8.5 billion.¹⁸⁶ This does not take into account any increase in wages or economic growth that may occur due to the increase in investment in human capital.

Another way of examining the fiscal consequences of this proposal is to examine what would happen to the hypothetical "median person." This calculation is far more complex and is highly influenced by decisions one makes regarding interest rates, wage growth, and inflation. In addition, the investment in children should increase productivity and wage growth. The two percent payback tax only accounts for part of

a \$2,000 payment over 15 years would be worth \$20,759 at a discount rate of 5%. Allowing the CF to sell the discount stream for a set payment might allow the CF to make one very large capital investment or to determine that the CF could invest the money more profitably than relying on the discount rate. Since the proposal is designed to help ensure a set amount of capital investment, it is imperative to protect against the potential loss or squandering of the entire child benefit. I would, therefore, prohibit a CF from entering into such a contract. For a discussion of this issue in the context of the "Stakeholder Society," see ACKERMAN & ALSTOTT, *supra* note 143, at 57.

184. POPULATION PROJECTIONS PROGRAM, U.S. CENSUS BUREAU, POPULATION PROJECTIONS OF THE UNITED STATES BY AGE, SEX, RACE, HISPANIC ORIGIN, AND NATIVITY: 1999 TO 2100 (2000), available at <http://www.census.gov/population/www/projections/natsum-T3.html>.

185. INTERNAL REVENUE SERVICE, STATISTICS OF INCOME, TABLE I.1: INDIVIDUAL INCOME TAX RETURNS: SELECTED INCOME AND TAX ITEMS, BY SIZE AND ACCUMULATED SIZE OF ADJUSTED GROSS INCOME (2000), available at <http://www.irs.gov/pub/irs-soi/00in11si.xls>.

186. In order to avoid the situation where currently unused tax deductions could be taken against the payback tax, the payback tax must be added after the tax due is established. Thus, if a person had a tax liability of \$2,000, and a payback tax of \$1,000, the total tax bill would be \$3,000.

the revenue the government will receive from this program. In addition to the payback tax, general tax revenue will increase due to higher wage growth. Because of this benefit to the government, one can assume that the person paying back the Child Investment Fund only needs to pay back the funds received accounting for inflation. The opportunity costs for the government for not having the ability to invest the child investment payment in another activity are borne by the government and are covered by the increased general revenue to the government. Under these assumptions, the median person will pay back the amount received by her fifties or early sixties. If the median person was expected to payback the amount received plus market rate interest, the payback would have to be increased or the payout decreased for the program to completely pay for itself.¹⁸⁷

In any event, the point of this project is not to set the exact amount of the payment and the payback. There is some point where a reasonable equilibrium can be reached between the payout and the payback. Whether that point is a payout of \$2,000 through age ten, or a payout of \$2,000 through age 14, or whether the payback should be one and one-half percent or two percent is a debate for another time. What is clear is that the program I suggest can provide a significant payout that should increase investment in children, with a commensurate payback and without breaking the federal budget.

For administrative convenience, the payback would be collected along with the taxpayer's federal income taxes. This could be done in several ways. First, the payback could be collected by age. The payment would be made to all children of a particular age group, making it clear what cohort received the payout. The payback tax would then apply only to people within the age range that received benefits. That age would increase as more and more of the population consisted of people who received the payout. This has the disadvantage of taxing all people within this age group, even people within the age group who did not receive the benefit. This means that people who immigrate to this country will be subject to the payback tax even though they never received the Child Investment Fund.

The system could also be set up so that only children who received the child investment benefit were subject to the payback tax. The child benefit could be tied to the child's social security number, so it would be relatively easy to design a tax form and system that only required children who received the benefit to pay the payback amount.¹⁸⁸

187. See Appendix *infra* for description of the calculations.

188. The program would have to be phased in. You could design a system whereby children who received less of a benefit during the phase-in years have a lower payback. For example, a child who was

5. Ensuring Continued Investment in Children—Promises Kept

The point of this proposal is to increase human capital investment in children. I justify a payback because the benefits to children under this program will be worth the cost. In this discussion, however, I assume that current investments in children remain at least constant. If the child benefit becomes an excuse for cutting existing programs, investment in children will not increase, and the proposal will be a serious failure.

As previously discussed, investing in children is both necessary for a productive society and for productive children, and the current investment is clearly insufficient. One concern with this proposal is that Congress will cut funding for other investment programs because children would now have their own funds that they could spend in lieu of such programs. Cutting Head Start, for example, because children now have a \$2,000 child benefit that they could use to pay for Head Start will only hurt children. The promise to them of increased investment will be illusory while the cost to them will increase.¹⁸⁹

I recommend that the adoption of this program also include an escalation clause providing that the amount of child benefit is automatically increased by any commensurate decrease in general federal funding for children. Funding for children should at least remain constant, including adjustments for inflation. If funding for children decreases, the amount of the child benefit should be increased pro rata by that amount. This will ensure that the program actually provides increased investment in our children.

6. Response to Potential Criticisms of the Proposal

Although there are endless criticisms that could be leveled against a program of this magnitude, there are two criticisms that warrant particular attention. Opponents of government programs often argue that they are inefficient or that government intervention distorts the marketplace causing negative outcomes. This subpart addresses the concerns that the Child Investment Funds might be wasted, or might encourage harmful behavior.

14 when the program started, and thus only received one \$2,000 payment might only be required to pay a payback tax of 0.1%, a 13-year old might be required to pay 0.2% and so on.

189. Similarly, the Child Tax Credit or the Earned Income Tax Credit should not be reduced as a means of funding this program.

a. Efficiency

One criticism of this proposal is that CFs will waste the Child Investment Fund. Critics of social welfare programs often claim that recipients are wasting funds on drugs or alcohol or luxuries.¹⁹⁰

The administrative process of choosing a CF, discussed above, is one structural component of the Child Investment Fund program designed to lessen these efficiency concerns. Presumably, the CF must use the Child Investment Funds for investment in the child recipient. But even with these controls, some may be concerned that the CF will waste the funds, or use them for drugs or alcohol. Although any program or policy will have some waste, many of the concerns about waste in the social welfare context are based on negative and untrue stereotypes about the poor that are often asserted without any empirical evidence.¹⁹¹ The scholarship surrounding these issues provides very little evidence that benefit recipients waste government funds.¹⁹²

In her work on cash transfers, Martha Coven concludes that low-income people are usually more careful with their money than middle- or upper-class individuals.¹⁹³ She explains that the marginal utility for

190. See Daniel M. Weintraub, *Advocates for Poor Protest Wilson's Welfare Remark; Budget: Governor is Called Insensitive After Saying AFDC Cut Would Leave Recipients Less to Spend on Beer*, L.A. TIMES, Jan. 12, 1991, at A1 (Gov. Pete Wilson defending cuts in AFDC saying that it will just mean that welfare recipients will not be able to buy a six-pack of beer); Kevin Sack, *The 1992 Campaign: Issues; The New, Volatile Politics of Welfare*, N.Y. TIMES, Mar. 15, 1992, § 1, at 24 (Democratic state senator Creedon states that people on general relief are just "[taking the money] and go[ing] to the nearest bar and spend it."); Thomas O'Brien, *Rethinking America's Safety Net*, WORLD & I, May 1, 2003, available at 2003 WL 11504883 (asserting without any indications of actual knowledge that "[i]t is a withering injustice for lower-income working parents who buy generic items and wait in the checkout line with carts full of off-brand foods when the customer in front of them uses food stamps to purchase expensive, brand-name junk food items that the working parents feel they cannot afford for their own families."). President Reagan promoted this idea by talking about a "welfare queen" who was driving a Cadillac. The woman in question, Linda Taylor, was actually committing welfare fraud, and was claiming government benefits under a number of different aliases. Welfare payments were clearly not enough for her to buy a Cadillac. Ultimately, the Cadillac was repossessed by the state because it was "believed [to be] used in the commission of a crime." *"Welfare Queen" Loses Her Cadillac Limousine*, N.Y. TIMES, February 29, 1976, at 42.

191. See DAVID ZUCCHINO, MYTH OF THE WELFARE QUEEN: A PULITZER PRIZE-WINNING JOURNALIST'S PORTRAIT OF WOMEN ON THE LINE 117 (1997). See also MARK ROBERT RANK, LIVING ON THE EDGE: THE REALITIES OF WELFARE IN AMERICA 2-3 (1994) (discussing welfare myths and egregious political statements, including "People are saying these breeding factories have got to stop," and politicians suggesting selling the organs of dead welfare recipients without consent). See generally Williams, *supra* note 111 (discussing and refuting arguments against AFDC that are based on racial or class stereotypes). See also Weintraub, *supra* note 190; Sack, *supra* note 190 (Creedon also stated that "[g]eneral [r]elief goes to people who are urinating on the floor in the bus station. . . . They take that \$338 and go to the nearest bar and spend it."); O'Brien, *supra* note 190 (asserting without support that food stamp recipients waste their food stamps on non-nutritional items).

192. For a discussion about how the moral hazard doctrine has been used improperly to limit social responsibility, see Tom Baker, *On the Genealogy of Moral Hazard*, 75 TEX. L. REV. 237 (1996).

193. Coven, *supra* note 150, at 898; see also Jan M. Newton, *Economic Rationality of the Poor*, 36 HUM.

money declines as income increases. Thus money, or spending it wisely, is worth more to people with lower-incomes than higher ones.¹⁹⁴ The simple reason for this is that poor people have more to lose when they waste funds. A poor person's failure to spend money wisely can be the difference between whether or not she has food or clothing for her children.

In a recent study examining the spending patterns of people on public assistance, Lucilla Tan found that families on public assistance spend almost all of their income on necessities.¹⁹⁵ Over 70 percent of assisted families' incomes went to food, housing, or transportation, with another ten percent going to clothing, health, or education.¹⁹⁶ Assisted families spent a little over four percent for entertainment and a little over seven percent for "other expenditures."¹⁹⁷ Thus the prevailing picture is not one of poor people wasting money on drugs and alcohol, but is instead one of people working hard to make ends meet.¹⁹⁸

Moreover, contrary to public perception, there appears to be very little evidence that there is a large problem with drug-addicted mothers spending all the family resources for drugs. In a recent study, James Swartz and colleagues concluded that providing Supplemental Social Security Income (SSI) to people with drug addictions did not increase the level of drug use.¹⁹⁹ In other words, the level of the government benefit had no significant impact on drug use. Other studies have found that while drug abusers will increase their drug use as income rises,

ORG. 50, 58 (1977); Stephen J. Hoch et al., *Determinants of Store-Level Price Elasticity*, 32 J. MARKETING RES. 17, 28 (1995) (people with more expensive homes and people who are more educated are less price sensitive); R. P. Bagozzi, *Marketing as Exchange*, J. MARKETING, Oct. 1975 at 32 (poor persons use limited resources wisely).

194. Coven, *supra* note 150, at 898.

195. Lucilla Tan, *Spending Patterns of Public-Assisted Families*, MONTHLY LAB. REV., May 2000, at 29, 33-34.

196. *Id.*

197. *Id.*

198. See KATHRYN EDIN & LAURA LEIN, MAKING ENDS MEET: HOW SINGLE MOTHERS SURVIVE WELFARE AND LOW-WAGE WORK 280 (1997) (finding that a third of low-income families spent nothing on entertainment in the last year, two-thirds did not eat out, and approximately half spent nothing on cigarettes or alcohol).

199. James A. Swartz et al., *Disability Payments, Drug Use and Representative Payees: An Analysis of the Relationships*, 98 ADDICTION 965, 965-75 (2003) (finding that supplemental security income (SSI) disability payments to people addicted to drugs do not increase the level of drug use); see also Robert Rosenheck & Linda Frisman, *Do Public Support Payments Encourage Substance Abuse?*, 15 HEALTH AFF. 192, 194-95 (1996) (finding that people who received high levels of public support had no greater tendency to use or purchase drugs than people with lower levels of public support); Dru Stevenson, *Should Addicts Get Welfare? Addiction & SSI/SSDI*, 68 BROOK. L. REV. 185, 198-200, 221 (2002) (finding little correlation between SSI payments and drug use).

increases in income have no impact on drug use among non-drug users.²⁰⁰

To the extent that there is a concern about low-income people on drugs wasting family resources, the problem is not limited to this program and needs to be addressed on a broader scale. The problem exists whether or not there is a Child Investment Fund. In fact, the problems facing a child due to a parent or guardian's heavy drug use are far more serious than the concern that the child's CF might spend the money on drugs. If parents are unfit to care for their children, action should be taken to protect the children regardless of the financial situation in the family.

There is, however, the possibility that unfit or irresponsible parents would not, absent controls, spend the Child Investment Fund wisely. The design of the Fund, however, should alleviate many of these concerns. If a parent has a drug or alcohol problem, or is otherwise unfit to be a CF, the relevant agency can appoint an alternate CF for the child. Since the cash assistance is the child's, the drug addicted parent or guardian has no right to the payment. The alternative CF could ensure that the child's money is actually spent on the child. This is particularly important if one believes that the family's other resources are being spent on drugs. If that is the case, the child is obviously suffering from low human capital investment. Allowing an independent CF to control the money will at least ensure that the child receives a minimum level of human capital investment.

In addition, the child benefit also might help identify children in households with drug abusers and help the child's parent or guardian find treatment. For example, a teacher might realize that a child was not receiving sufficient food or clothing. The teacher could report this to a social service representative or other counselor. The counselor could then investigate why the child was not receiving at least subsistence support. The CF would have to explain why the child was not receiving ample support from the Child Investment Fund payment. The excuse that there wasn't sufficient money, on its own, would no longer be convincing. But the important point here is that if on a wide spread basis, parents are using the Child Investment Fund to buy drugs at the expense of their children's health and safety, we have a far larger problem than the management of the cash assistance received. To the extent an abuse exists regarding the Child Investment Funds in a relationship where the parent or guardian is otherwise a suitable guar-

200. Nancy M. Petry, *Effects of Increasing Income on Polydrug Use: A Comparison of Heroin, Cocaine and Alcohol Abusers*, 95 ADDICTION 705, 705-17 (2000).

dian,²⁰¹ then either another CF would have to be chosen or the current CF would have to receive the child benefit in voucher form.

b. Moral Hazard Dilemma

The second major criticism of this proposal is that the Child Investment Fund will impact the recipient's behavior in a socially inefficient way. This is often referred to as a "moral hazard."

Moral hazard is a doctrine developed by the insurance industry to define the potential changes in behavior when a person receives insurance. For example, if a person has health insurance he may be more willing to see a doctor even if he is not really sick. Health insurance makes visiting the doctor less expensive, and a person may do so even if the visit is inefficient in economic terms. Life insurance is another classic example. A person with a very unhealthy lifestyle, or a person thinking of suicide has a strong incentive to buy life insurance. The insurance industry thus takes steps to minimize these "moral hazards" by creating co-pays for health insurance or disallowing life insurance in the case of suicide.²⁰²

In this context, some will raise the moral hazard rationale and claim that providing investment in children will negatively impact parent's behavior. It will encourage people to have children to receive the benefit and will discourage work.²⁰³

On policy grounds, it is debatable whether in fact having children is a moral hazard. The United States is currently below replacement level fertility,²⁰⁴ and there is some evidence that the lack of population growth

201. For example, a parent with a gambling addiction might not be trustworthy with regard to the child investment payment but might be a reasonable caregiver to the child.

202. For a discussion of the moral hazard doctrine and welfare, see McCluskey, *supra* note 51, at 807.

203. See LAWRENCE M. MEAD, BEYOND ENTITLEMENT: THE SOCIAL OBLIGATIONS OF CITIZENSHIP 41 (1986) (arguing that welfare makes recipients dependent upon government); CHARLES MURRAY, LOSING GROUND: AMERICAN SOCIAL POLICY, 1950-1980, at 147-66, 178-91 (1984) (arguing that welfare hurts poor people by discouraging work, decreasing self-esteem and providing economic incentives for failure); RANK, *supra* note 191, at 3 (discussing statements by politicians indicating that welfare encourages children and referring to welfare recipients as "breeding factories."); CHARLES NOBLE, WELFARE AS WE KNEW IT: A POLITICAL HISTORY OF THE AMERICAN WELFARE STATE 126-27 (1997) (discussing argument that welfare encourages people to have children). Since the payment here belongs to the child not the parent, it should not provide a significant incentive for CFs to quit work. In addition, any work disincentives created by the Child Investment Funds might create social benefits, not harms. The Child Investment Fund might make it more affordable for one parent to stay home.

204. The birth rate in 2002, 4,019,280 or approximately 13.9 per 1,000 of population, was the lowest rate ever since national data has been available. Brady E. Hamilton et al., *Births: Preliminary Data for 2002*, NAT'L VITAL STATISTICS REP. (Nat'l Ctr. for Health Statistics, U.S. Dep't of Health & Human Serv., Hyattsville, Md.) June 25, 2003, at 1, available at http://www.cdc.gov/nchs/data/nvsr/nvsr51/nvsr51_11.pdf. The Total Fertility Rate (TFR) for 2002 was 2012.5 per 1,000, meaning that women over their

can have economic consequences.²⁰⁵ In fact, one problem with the financial stability of the Social Security system is that there are not enough workers to support the growing number of retirees. A growing well-trained and well-educated workforce would likely benefit society, not harm it.

But even if population growth is a moral hazard, there is little likelihood that the program I propose will actually increase population growth.²⁰⁶ The \$2,000 payment is significantly less than the cost to raise a child, and it is very unlikely that someone will have a child just to receive the benefit.²⁰⁷ In economic terms, it is only those people whose marginal cost for having children exceeds their marginal benefit by \$2,000 or less. Thus there are obviously some people who want to have children, but believe that they cannot afford to do so. If the \$2,000 payment is sufficient to make the next child affordable to them then that couple's decision to have children may be impacted by the payment. But from a societal perspective, there is really nothing wrong with

lifetime are currently having 2.01 children. *Id.* at 3. The TFR has fallen 3% since 1990. *Id.* The United Nations Population Division estimates that the average TFR will fall to 1,850 per 2,000 over the years 2045-2050. UNITED NATIONS, DEPARTMENT OF ECONOMIC AND SOCIAL AFFAIRS, POPULATION DIVISION, WORLD POPULATION PROSPECTS: THE 2002 REVISION: HIGHLIGHTS, U.N. Doc. ESA/P/WP.180, at 4, available at <http://www.un.org/esa/population/publications/wpp2002/WPP2002-HIGHLIGHTSrev1.PDF>. The Replacement Level Fertility (RLF), defined as the rate necessary for a woman to replace herself and her partner, is set at 2.1 for industrialized societies. *Id.* at 1. This number is greater than two because of infant mortality. Thus, the current TFR in the United States is below replacement level and long-term trends indicate that the rate is declining. *Id.*

205. See Geoffrey McNicoll, *Economic Growth with Below-Replacement Fertility*, 12 POPULATION AND DEVELOPMENT REV. 217 (Supp. 1986) (recognizing that low fertility has only a slight impact on labor supply, technological change, investment or consumption, but finding that low fertility potentially may have a serious negative economic consequence due to distributional changes that will result from low fertility). But see U.S. COMMISSION ON POPULATION GROWTH AND THE AMERICAN FUTURE, POPULATION AND THE AMERICAN FUTURE: THE REPORT (1972); Thomas J. Espenshade, *Zero Population Growth and the Economies of Developing Nations*, 4 POPULATION & DEV. REV. 645 (1972).

206. See, e.g., RANK, *supra* note 191, at 73-77 (finding no correlation between receipt of welfare benefits and childbearing, and finding a negative correlation between long-term welfare receipt and childbearing); BECKER, *supra* note 2, at 23 (economic growth and higher income does not appear to increase birth rates). But see BECKER, FAMILY, *supra* note 9, at 139-40 (arguing that AFDC increased birth rates).

207. The Department of Health and Human Services estimates that it costs \$3,930 per year to provide the basic necessities for a child. Annual Update of the HHS Poverty Guidelines, 68 Fed. Reg. 6456 (February 7, 2003). The Department of Agriculture estimates that, on average, families with incomes below \$39,700 and two children spend at least \$6,620 per year per child. See LINO, *supra* note 11, at ii. For this and other reasons, I strongly reject the notion that the payment should decrease if parents have more than a certain number of children. As stressed throughout this Article, the child benefit here is the child's. The child is in no way responsible for her own birth, and there is no basis for punishing the child for its existence. In addition, such a policy makes no sense in this context because ultimately it is the child who will be responsible for paying back the amount received. But see Foley, *supra* note 48, at 486 (proposing a "personal allowance" for adults with children but capping the benefit at two per married couple).

making it more affordable for this small group of parents to raise a family.²⁰⁸

Moreover, there is no evidence that other policy initiatives providing benefits to families or children have increased fertility rates.²⁰⁹ Recently, there have been very large increases in the Earned Income Tax Credit, the Child Tax Credit, the Childcare Tax Credit, and the Dependency Exemption, and there is no evidence that these policy initiatives have had any impact on population growth.²¹⁰ In addition, other industrialized countries have family allowances and other benefits for families that are far more generous than those in the United States and these policies appear to have very little impact on fertility.²¹¹ Moreover, pronatalist policies in Europe, which provide economic incentives to families with children, have been found to have very little, if any, impact on fertility.²¹²

C. *Is There Another Way?*

I have presented my vision for a comprehensive program to increase investment in children. Many people, however, are troubled by the compulsory nature of the program. Upper-middle and upper-class

208. Since the payment at issue here is the child's, not the parent's, the payment may have less impact on a parent's decision to have a child. But, if for example, parents were concerned about paying for day care or college, the child benefit might lessen their concerns. Thus, the benefit might make raising children more affordable and thus more attractive to some people on the margins.

209. In *The Ideology of Division*, Lucy Williams refutes the common myth that welfare payments encourage people to have children. Williams, *supra* note 111, at 737-41. She notes that the amount of additional welfare benefits received by a parent for having an additional child is small, that a large majority of welfare mothers have fewer than two children, and that differing welfare benefits among states do not correlate to family size. *Id.* For example, Mississippi has the highest rate of families with four or more children, yet the lowest AFDC payment. Maine and Vermont have very low percentages of families with four or more children and have AFDC levels well above the national average. *See id.* (citing U.S. DEPARTMENT OF HEALTH & HUMAN SERVICES, FAMILY SUPPORT ADMINISTRATION, 1989 AFDC RECIPIENT CHARACTERISTICS STUDY 24 (Table 6) (1991)); *see also* Kristin A. Moore & Steven B. Caldwell, *The Effect of Government Policies on Out-of-Wedlock Sex and Pregnancy*, 9 FAMILY PLANNING PERSPECTIVES 164, 164-69 (1977) (finding that AFDC was not an incentive for teens to have children).

210. *See supra* note 204 and accompanying text. In addition, the crude birth rate, defined as the number of births per year per 1,000 people, has been declining 17% since 1990. *Id.* at 2; *see also* 1 NAT'L CTR. FOR HEALTH STATISTICS, U.S. DEPT. OF HEALTH & HUMAN SERV., VITAL STATISTICS OF THE UNITED STATES, 1999, NATALITY, Table 1-1 (2001), <http://www.cdc.gov/nchs/datawh/statab/unpubd/natality/natab99.htm>.

211. C. ALISON MCINTOSH, RECENT PRONATALIST POLICIES IN WESTERN EUROPE, 12 POPULATION AND DEVELOPMENT REVIEW: BELOW-REPLACEMENT FERTILITY IN INDUSTRIAL SOCIETIES: CAUSES, CONSEQUENCES, POLICIES 323 (Supp. 1986).

212. Paul Demeny, *Pronatalist Policies in Low-Fertility Countries: Patterns, Performance, and Prospects*, in BELOW-REPLACEMENT FERTILITY IN INDUSTRIAL SOCIETIES: CAUSES, CONSEQUENCES, POLICIES 335, 350 (Kingsley Davis et al. eds., 1987) (indicating that the modal finding is that the effects of pronatalist policies are nil or negligible).

children may not be helped by this proposal. Children within these socio-economic groups are already receiving sufficient investment in their human capital.²¹³ In their situation, the child benefit becomes a forced loan that the child must pay back. In addition, since higher-income individuals usually invest heavily in their children, children from higher income families often have higher incomes themselves.²¹⁴ A pay-back that is based on income will likely require higher-income individuals to pay back more than "their share."

Despite the fact that some higher-income individuals may not receive a dramatic benefit from the program, the benefits of a mandatory program outweigh the fact that some higher-income individuals will receive only a small benefit. Just as with Social Security, there is no guarantee what will happen to any child, and no guarantee which children will pay more and which less. Furthermore, as discussed earlier, a broad-based program in which all children participate is simpler to administer and less stigmatizing. There is, however, a way of implementing this program on a voluntary basis.

First, the child's parent or guardian would elect before the child's first birthday whether or not the child would participate in the program. At the time, no parent or child knows how successful the child will be in life. The parent or guardian would file a form, a CF would be appointed for the child, and the child would start receiving benefits. Just as under the mandatory model, the child would be required to pay back the funds as a percentage of income.

The program would work in the following manner. First, the government would have to set a payback rate for participants. This payback rate would have to be set based on the amount of benefit received, the interest rate necessary for the payout and payback to reach equilibrium, and a calculation of the risk that some participants will default. Since the collection method here is through the Internal Revenue Code, it is likely that there will be less risk of default than if this were a commercial transaction. It is therefore likely that the risk premium and the interest rate could be kept at a reasonable level. Once the payback rate was set for a particular year, it would remain constant throughout the recipient's life. The payback rate would have to be re-adjusted at reasonable intervals. All children (through their parents) that chose to participate would know the amount received and the payback rate at the time they chose to receive the payment. Since collection of the payback is through the Internal Revenue Code, it would be easy to adjust the payback on

213. See *supra* note 35.

214. See *supra* Part III.B for a discussion of alternative proposals.

a yearly basis. All people born from 2005-2006 could have a payback rate of two percent, while people born from 2007-2008 might have a payback rate of 1.8 percent. The payback rate would all depend on the interest rates and risk factors that existed at the time participants joined the program.

A second type of voluntary option would be a human capital loan. This program would operate in a manner similar to the student loan program. Parents could take out loans on behalf of their children for human capital investment. Just as in the student loan program, the government could guarantee private loans up to \$2,000 a year for human capital investment. The child would then be responsible for paying back the loan once he or she started working. Unlike the other investment proposals, in this proposal, the child would only be required to pay back the amount he received plus interest. A successful child's obligation would stop once the loan was retired. Conversely, an unsuccessful child would continue to owe money regardless of his ability to repay. Those that could not pay would default on the loan with the commensurate consequences from default.

The loan option has several problems. First, if the government is guaranteeing the loan, the program itself is not completely self-supported. If the government does not guarantee the loans, the loan rates will be very high and paying the loan back might be very onerous. Unlike in either the mandatory or voluntary program discussed above, in the loan program children are on their own. Each child is only responsible for paying back his particular loan. Since each child is only paying back his or her loan, those who succeed will not be subsidizing those who fail.²¹⁵ Moreover, absent a government subsidy, it is likely that only low-income people will seek investment dollars through this program since middle- and upper-income people will probably have better methods of obtaining funds to invest in human capital. The result is that the lower-income people seeking human capital loans will have to pay high rates of interest, which may compound their already difficult financial situation.

A government subsidized loan program might provide a sufficiently attractive rate to make it a viable option. This, however, would require a move away from the principle of revenue neutrality and towards one of requiring at least a partial government subsidy. This in itself may be appropriate if one believes that our allocation of resources needs to shift to children away from other priorities.

215. Except to the extent they pay higher interest rates because of the risk of default. This could be reduced by a guarantee on the part of the government, but that would require government subsidy of the program.

V. CONCLUSION

The Child Investment Fund proposal creates a self-sustaining investment program in our children's human capital, and accomplishes this task in a fiscally responsible way. A second goal of this proposal, however, is to shift the focus away from punitive welfare policies designed to punish parents who receive government assistance, to a system that recognizes that children are the true beneficiaries of these policies. A system that provides benefits directly to children helps accomplish this task.

In a country with over 12 million children living in poverty, and with middle-class families finding it harder to invest in their children, we need to do more. To the extent we promote a social system where people are required to sink or swim, we need to provide children with the tools and resources to become great swimmers. It is simply too late to throw them in the pool as adults and see what happens.

A system of human capital grants to children will help all children learn to swim. The small cash allocation I propose may not be enough to make all children Olympic swimmers, but it should provide a basis to ensure that all of our children receive basic human capital investment that is necessary for them to be self-supporting adults.

This proposal is not, in my view, the ideal way of addressing this issue, and others have proposed far more grandiose programs,²¹⁶ but this is a program that, at this point in time, is both politically and economically feasible. We have been willing to place too much of a burden on our children while spending resources on ourselves. It is time to reverse that trend, and to make sure that all children can recognize their potential.

216. See *supra* Part III.B for a discussion of alternative proposals.

APPENDIX

The following calculations are designed to provide general information regarding the cost of this program. These figures represent when a worker earning the median wage will pay back the amount he received.

Payout	Payback tax	Inflation	Interest	Wage Growth	Payback Age
2,000	2%	3%	0%	1%	50
2,000	2%	3%	1%	1%	59
2,000	2%	3%	2%	1%	Insufficient
2,000	2%	3%	0%	2%	48
2,000	2%	3%	1%	2%	55
2,000	2%	3%	2%	2%	Insufficient

Since everyone who participates in the program will not necessarily be in the payback pool, I adjust the payback for labor force participation. Some will die, and others will chose not to work. In this regard, I multiply the median wage by labor force participation rates by age minus the unemployment rate.²¹⁷ In calculating the median wage, I use the median wage by age provided by the Census Bureau. I then adjust these figures to create a linear curve between age cohorts to create a baseline median income. I then apply the wage growth figure in the above table to that baseline.

These calculations are based on a very simplistic model and are merely designed to show that an investment program similar to the one I propose is financially responsible. The above calculations do not take into account the fact that if this program is successful general revenues to the Treasury will also rise.

217. The labor force participation rate measures the number of people working or looking for work. To determine the percentage of the labor force actually working, I subtract from the labor force participation rate the percent of the labor force that is unemployed. The resulting number gives a ballpark figure regarding how many people will be in the payback pool.