

Ending Poverty through Child Benefits: Hitting the Wall?

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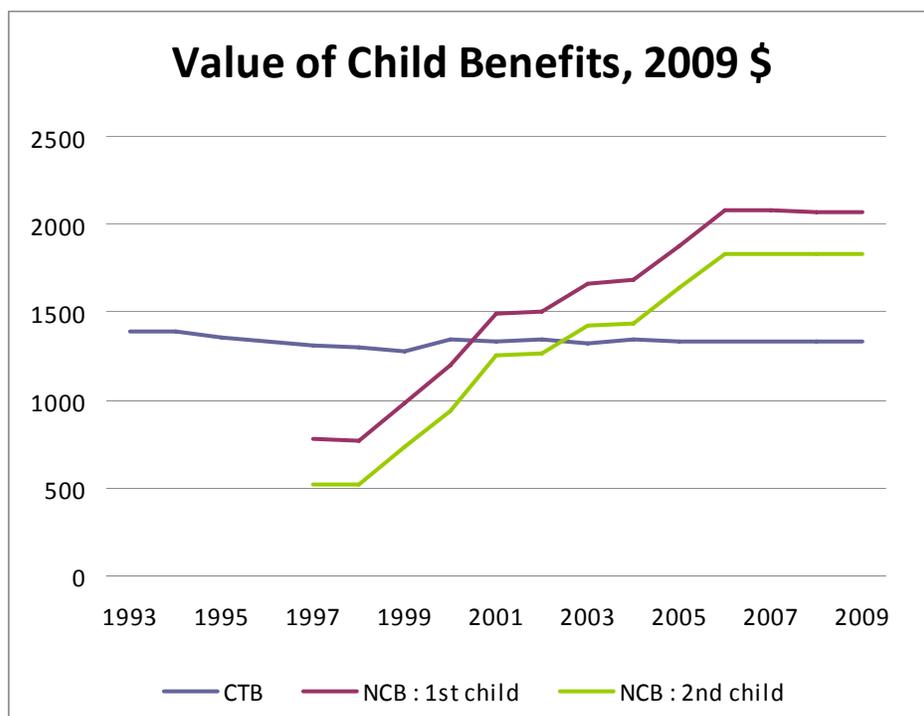
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Ending Poverty through Child Benefits: Hitting the Wall

The cornerstone of Liberal policy to fight child poverty was the National Child Benefit program. Figure 0 shows the real value of the maximum federal Child Tax Benefits and the National Child Benefit Supplement entitlements since the introduction of the programs.¹ Contrary to what might (or might not) be one's preconceptions, the value of the basic federal child tax benefit has hardly budged in real terms since it was first introduced. The National Child Benefit Supplement, however, was enriched substantially throughout the 1990s and early 2000s. When the present Conservative government was elected in 2006, however, it took a different approach to poverty relief. Since 2006, the maximum amount available to families through the NCB supplement and CCTB has remained constant. Instead, the government has begun separating support for families with children and poverty relief strategies. In this essay, I discuss how and why.



¹ (adjusted for inflation using CPI (until 2006) and the federal indexing factor (after 2006)).

There a number of inherent problems with the use of child benefits to fight poverty. One is timeliness: child benefits received from July 2009 to June 2010 will be based on income in the 2008 taxation year. When an economy is growing and incomes are rising, this lack of responsiveness may not be a problem. When the economy contracts – as is happening at present – and families see large reductions in incomes, the child benefit's lack of responsiveness may become an issue. Another issue is the lack of sensitivity to local labour market conditions and living costs. Child benefits are reduced once a family's net income reaches, as of this budget, \$23,713 – yet the standard of living implied by that income is very different for, say, a rural Maritime two-parent family and an urban Toronto one-parent family. A (Malthusian?) might be concerned that the use of child benefits as a poverty reduction strategy could, conceivably, cause more people – especially poor people – to conceive. All of this is old, stale and familiar to people immersed in child benefit policy. But the point is: this government is allowing child benefits to stagnate, and it is interesting to understand why.

One of the founding principles of the Conservative Party is:

A belief that it is the responsibility of individuals to provide for themselves, their families and their dependents, while recognizing that government must respond to those who require assistance and compassion

[\(http://www.conservative.ca/EN/4679/\)](http://www.conservative.ca/EN/4679/)

The philosophical basis for the Liberal child benefit strategy was that government should provide basic income support for children – and, by taking children of welfare, reduce the welfare wall. The philosophical basis for Conservative strategies is that individuals

should support themselves and their children out of their own earnings – unless they are unable to do so. If there is a welfare wall, build a ramp and get over it!

Policies reflect philosophies: they also reflect efficiency concerns and practical, get-the-vote politics. The new system for child benefits and income support reflects a fundamental change in philosophy: it is more universal, it involves more benefits for men, it is relatively more generous to single-earner families – especially those with an at-home parent -- and less generous to dual-earner couples.

A more universal system.

A number of years ago, Nick Rowe and I wrote a paper entitled “The Efficiency Case for Universality”. In this paper, we made a straightforward argument for universal benefits. If, say, child benefits are targeted towards low- and middle-income families, they must at some point be taxed back. The tax back of benefits means that people with children face higher marginal tax rates than people without children. Unless there is some reason to believe that parents have particularly inelastic labour supplies, efficiency can be increased by universalizing benefits.

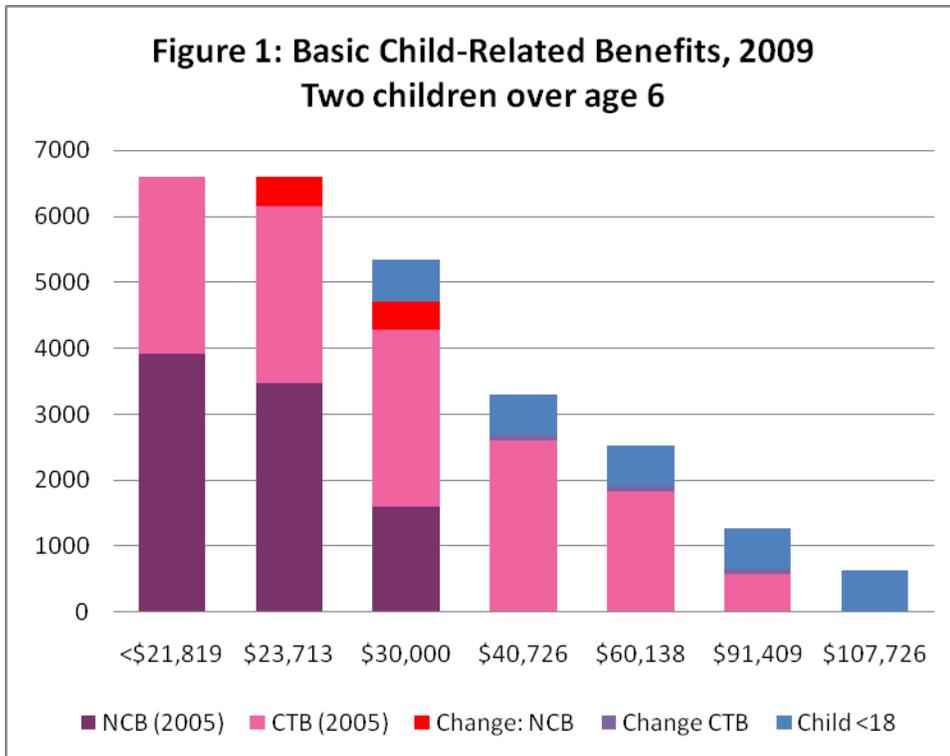
The net effect of various tax changes for families with children over the past four budgets has been to create a system of tax credits and child benefits that is, at least in part, universal. Today every family with children in Canada receives some child-related tax credit. There would have been a simple way of achieving this end: reduce the rate at which the existing Canada Child Tax Benefit is taxed back. The government chose not to pursue this option until the most recent (2009) budget. Instead a variety of new credits and benefits were introduced, including two universal benefits: the Amount for Dependent Children and the Universal Child Care Benefit.

Prior to the election of the Harper government in 2006, the only broad-based recognition of children in the income tax system was the income-tested Canada Child Tax Benefit. Because, for example, a mean income two-earner family in Toronto has an income close to the upper limit for CCTB receipt, it was possible for a family with children to face the same tax burden as a family without children at the same income level.

Figure 1 shows how the last four budgets have shaped basic child-related benefits. The 2005 benefit structure, indexed to 2009 levels, is shown in purple (National Child Benefit) and pink (Canada Child Tax Benefit). The 2007 budget introduced the Amount for Children non-refundable credit in 2007 (shown in blue). The 2009 budget increased in the income threshold at which National Child Benefit (red) and Child Tax Benefit (lilac) begin to be taxed back. (The non-refundable credit is not applied to families with income below \$23,713 because, given the other credits available to these households (personal, eligible dependant, employment, CPP/EI, public transit, etc) families would be able to claim).

The net effect of these changes is to tilt the basic child-related benefits towards a more universal system. For an average two earner family – with a market income in the \$90,000 range² - the changes mean that non-refundable credits are a more important source of tax recognition for family responsibilities than refundable credits. Yes, the amounts involved are small. But what is interesting is the philosophy behind the changes – what it says about how our tax system chooses to recognize the cost of children.

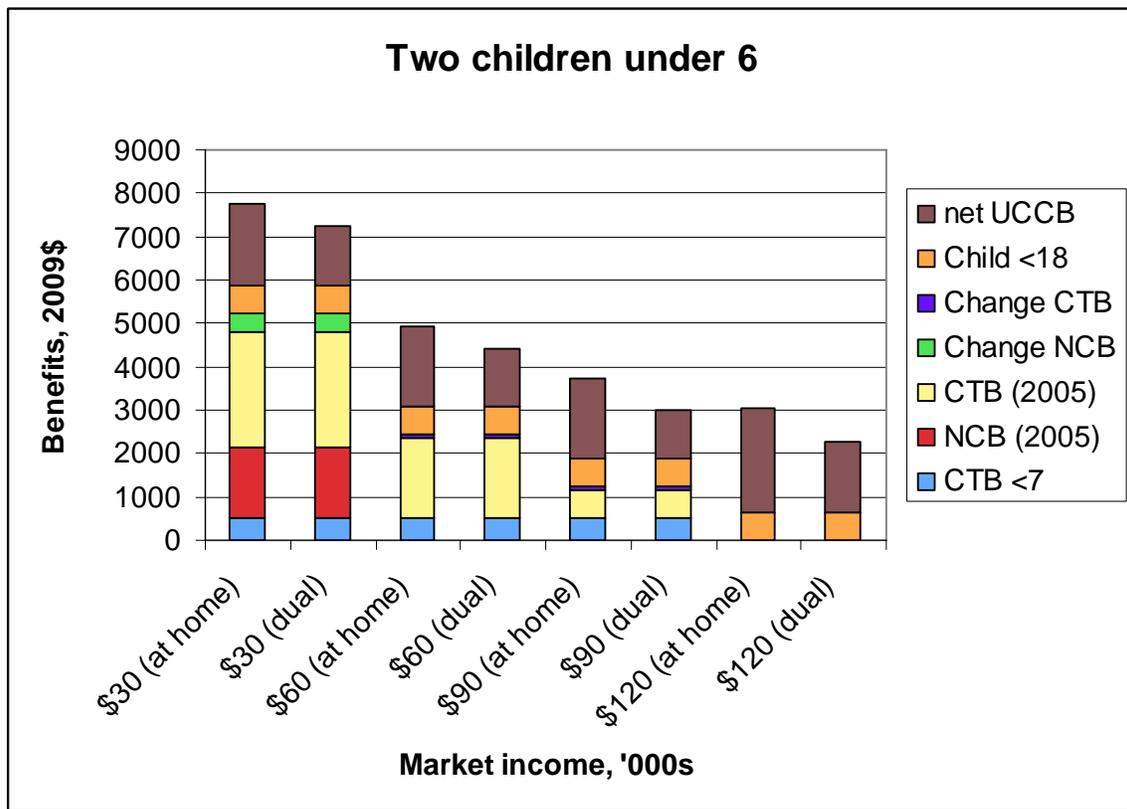
² (Note: mean income=2006 average market income (economic families) taken from Statistics Canada, adjusted for inflation using the CPI)



While for families with children over the age of six, the new Conservative benefits are relatively small, this is not true for families with children under the age of six. Figure 2 shows the new Universal Child Care Benefit (\$1200 per child under the age of six, taxable in the hands of the lower income earner), as well as the benefits in Figure 1. The first three bars (blue, red, yellow) represent the 2005, Liberal benefit structure, the remaining bars represent the changes since 2006.

What is immediately apparent is that the UCCB universalizes benefits for children. For a two-parent family anywhere above the median income, the UCCB represents a major change in the financial recognition of the cost of children. If it is, in the words of Scott Reid, ‘beer and popcorn’ money, where does that leave the pre-UCCB set of benefits? A second point is that the UCCB is worth more to a family with an at-home parent. How much less will depend upon the lower earner’s marginal tax rate, as UCCB is taxed as income in the hands of the lower earner – or in the hands of the single

parent, for single parent families. In Figure 1, I took a ‘almost-worst case scenario’ approach and considered dual earner families where the income would be equally split between the two spouses (the absolute worst-case scenario is a single-parent family, where the UCCB is taxed at the single/highest earner’s marginal tax rate). At income levels around that of a mean income two earner family, the taxability of UCCB reduces the value of the benefit by a third relative to that received by a family with an at-home parent. Another point to note: the UCCB replaced the previous child under 7 CTB supplement, hence the gain was tilted even more strongly towards higher income families as these families were not receiving the CTB.



Refundable credits for mom, tax credits for dad?

The NCB and CTB are shown in pink in Figure 1. The reason is that, while these are paid (so as not to seem sexist) to the person “primarily responsible for the care and upbringing

of a child” (www.cra-arc.gc.ca/E/pbg/tf/rc66/rc66-08e.pdf), this parent is assumed to be the mother: “If there is a female parent who lives with the child, we usually consider her to be this person. However, it could be the father, a grandparent, or a guardian.” For families with older children, only this budget’s increase in the threshold at which the NCB supplement is taxed back has a significant positive impact for women. (The change in the CTB, while it also goes into women’s purses, has an effect so small that it is not actually visible in Figure 1). For families with younger children, however, the UCCB tilts the balance in favour of moms – for median and above income two-parent families with small children, the UCCB is the now the major source of income.

The “Amount for Children” non-refundable credit could, in theory, be claimed by either parent, as long as the parent has some amount of tax payable. As a credit (as opposed to a deduction) its value is independent of the parent’s income. Given that the majority of mothers of children are in the labour force, surely it makes sense to view the Amount for Children as a gender-neutral tax credit.

Here, however, we enter the realm of economic psychology. Most people do not understand exactly how their taxes are calculated. In terms of taxes, it is not true that a dollar is a dollar. The principle of loss aversion, for example, refers to the psychological phenomenon that people experience more harm from losing a dollar than they do benefit from gaining a dollar. People decide how to allocate credits between spouses – and we don’t know how or why. Unfortunately, the income tax statistics that would allow us to know who claims the Amount for Children are not yet available. Yet we can discover some interesting patterns from considering the information that is available in the 2006 income taxation statistics (interim statistics, taken from the CRA web site).

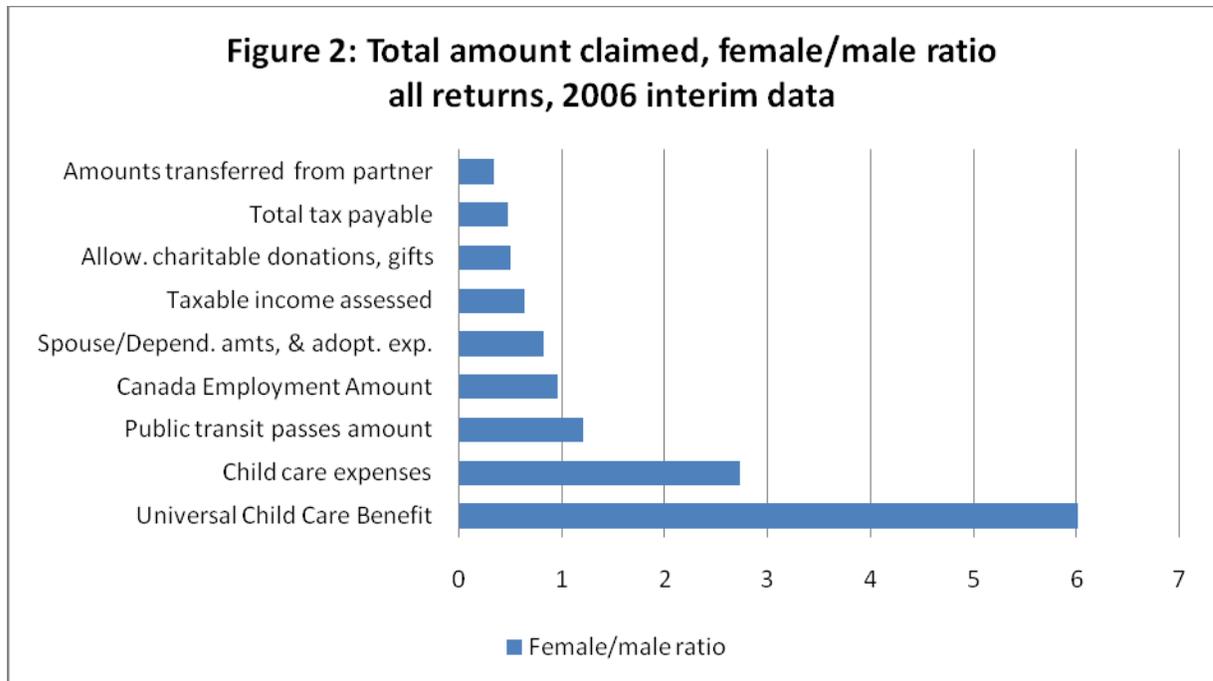


Figure 2 simply takes information from the CRA’s Taxation Statistics on, for example, the total tax payable for all female taxfiles in Canada and all male taxfilers in Canada, and divides the first number by the second to find a female/male ratio. Men have higher incomes than women: the female/male ratio of taxable income assessed is 0.63 – an amount very close to the female/male income ratio. Because Canada has a progressive tax system, and because men earn more on average than women do, men pay about two-thirds of the taxes in Canada: the female/male ratio of taxes paid is 0.47. None of this is very surprising. What is interesting is how different tax credits have (sometimes surprisingly different) gendered effects. The spousal amount/amount for eligible dependants tax credit is – because of the number of single parents who are able to claim it – claimed by a large number of female taxfilers (a female/male ratio of 0.81). The Canada Employment Amount, that can be claimed by anyone with employment income, is essentially gender neutral. Public transit is pro-female. But the amounts that are claimed disproportionately by women are those that must be claimed by the lower

income earner: the Child Care Expense Deduction and the Universal Child Care Benefit. (I have no idea why the CCED is so much less pro-female than the UCCB – use of the CCED is heavily concentrated in the higher income groups, hence there may be an element of tax planning going on here). This will be important later.

What I want to focus on now is the amounts claimed for the charitable donations. Because of the graduated structure of the charitable donations tax credit (a 15 percent credit on the first \$200 or so claimed, a 29 percent credit on amounts over and above \$200), it is always advantageous, from a tax minimization point of view, to concentrate the charitable donations claim on one tax return – but it doesn't matter which one. We have independent information on the gender breakdown of charitable donations.

According to the National Survey of Giving, Volunteering and Participating, 51 percent of total donations are made by men, 49 percent by women – men who give, give more, but women give more often (2004 data reported in <http://www.statcan.gc.ca/pub/71-542-x/71-542-x2006001-eng.pdf>). That equality in giving is certainly not reflected in the amounts claimed, however.

Hockey Dads and Soccer Moms

A Ramp Over the Welfare Wall

If child benefits are no longer being used as a way of getting families out of poverty, what is being used instead? The Conservative government's policy innovation is the Working Income Tax Benefit. There are a number of critical differences between the WITB and the National Child Benefit Supplement

- Payments are independent of the number of children one has. Any adult is eligible, except for students.

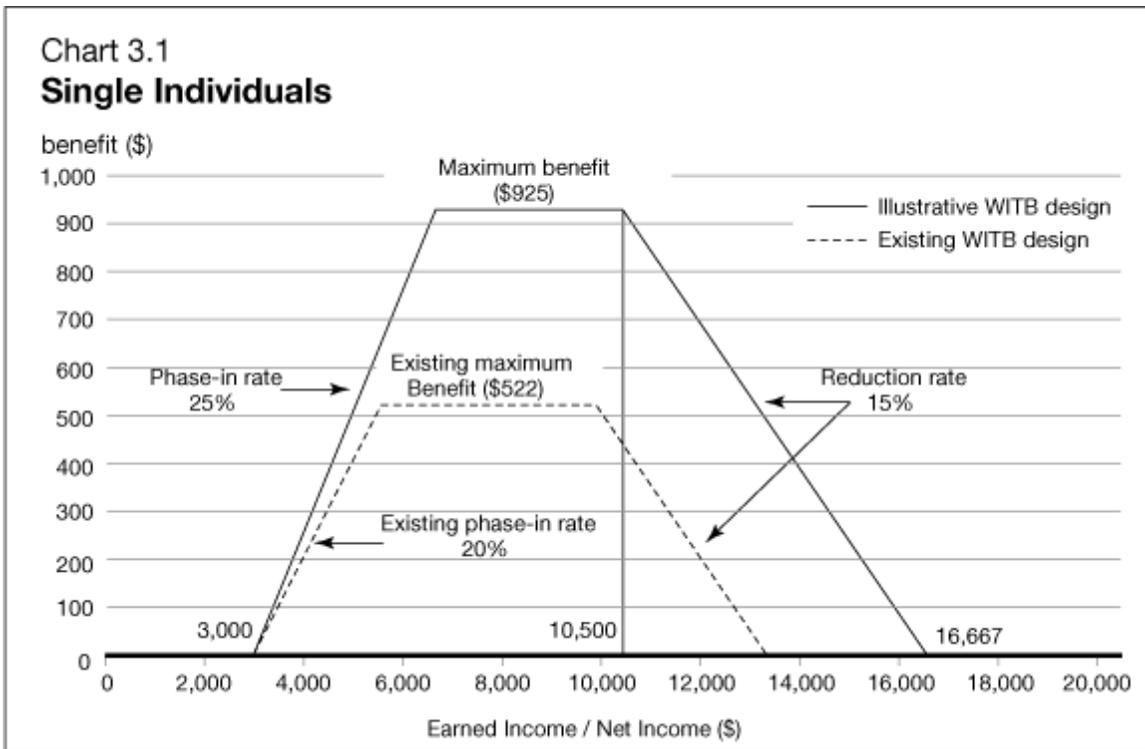
- Unlike child benefits (but like the GST credit), it can be claimed by either adult. Unfortunately, there is no published information on who claims the GST credit in couple families, so we have no idea of the likely gender breakdown of WITB claims. However available evidence (Lundberg, Pollak and Wales; Burton, Phipps and Woolley, 2008; and, to some extent, Milligan and ...) finds that payments made to women have a different effect on family spending than payments made to men, so this matters.
- WITB (potentially) provides a ramp over the welfare wall, by subsidizing entry into the labour market.

It is interesting to interpret these differences between WITB and the NCB in light of the founding Conservative principles mentioned earlier in this paper – as well as the issues I mentioned that are (perhaps?) not on the policy agenda. Personal responsibility for provisioning is emphasized through the incentives for labour force participation. This was the stated motivation for the WITB in the 2006 federal budget: “Reducing barriers to paid employment is essential to fostering opportunities and economic growth. In this context, the Government of Canada will identify, in consultation with provinces and territories, potential measures to improve incentives to work for low-income Canadians, including through an earned income tax credit such as a WITB.”

“Family values” have not, as far as I am aware, ever been mentioned as a motivation for WITB. However it is interesting that WITB removes the incentive to have more children that is present in child benefit programs. And because WITB can be claimed by fathers, it potentially reinforces paternal contributions to the family – the message is ‘Dad contributes’ rather than ‘I have enough income to go it alone’.

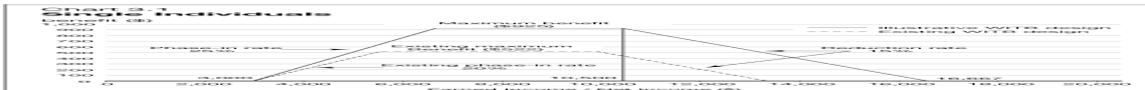
All of this is all very well and good in theory, but how does the program actually work?

If we ignore the interactions between the WITB and other income support programs (EI, CPP disability, provincial income assistance programs) the structure of the program is simple. The budget shows how it works – however the graphical representation is somewhat misleading because the scale on the vertical axis is about 1/10th of the scale on the horizontal axis.

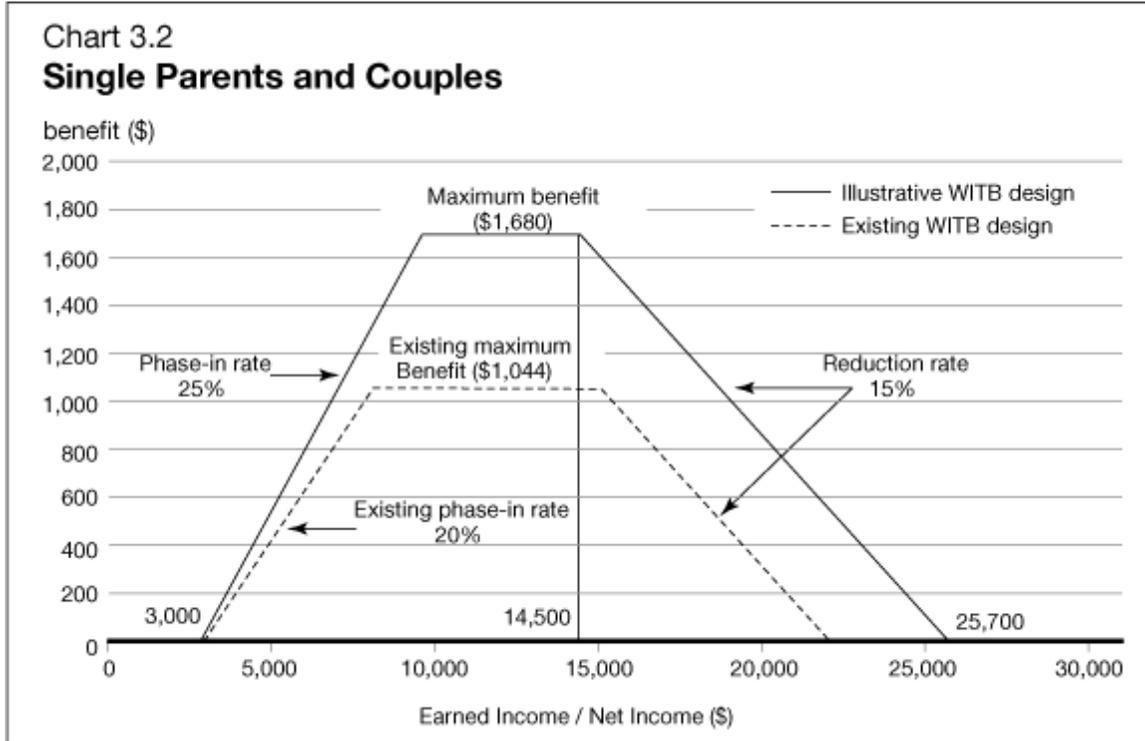


Source: Budget: 2009

If we rescale the chart so that the horizontal and vertical axis are on more or less the same scale, it looks something like that:



The picture for single parent and couples suffers from much the same phenomenon.



Source: Budget 2009

All of this begs the question – so what? Whose labour supply will be positively effected by the WITB, and whose will be negatively effected? To work this out, I did some illustrative calculations. As in the Budget diagrams above, I assumed that the individual received no employment insurance, CPP disability or other benefits that would add to net income but not earned income.

For a single person to face positive work incentives as a result of the WITB, they would have to be working full-time between nine and nineteen weeks per year, and receive no other source of income. Any other source of income, such as EI, would reduce the range in which incentives would be effective. For a couple, the range in which work incentives are binding are smaller – subsidies begin to end at 25-30 weeks of full-time

work. The only group that I can see facing significant incentives to work as a result of these changes are single earner families – so single parents and couples with an at-home parent. To get some sense of the numbers affected it is, of course, essential to crunch the numbers – which I’m not going to do. But my sense of this program is that the rhetoric – the sense that it’s important to build ramps to help people climb the welfare wall – is more important than the reality. It’s a blueprint, a step towards implementing the ultimate goal of personal responsibility, rather than a finished program.

	Min wage	Subsidy starts: earnings \$3000			Subsidy ends - single: net income \$6700		
		Min annual hours	Weeks FT	Weekly hrs PT	Max annual hours	Weeks FT	Weekly hrs PT
Alberta	8.8	341	9	7	761	19	15
British Columbia	8	375	9	8	838	21	17
Manitoba	8.75	343	9	7	766	19	15
New Brunswick	8	375	9	8	838	21	17
Newfoundland and Labrador	8.5	353	9	7	788	20	16
Northwest Territories	8.25	364	9	7	812	20	16
Nova Scotia	8.6	349	9	7	779	19	16
Nunavut	10	300	8	6	670	17	13
Ontario	9.5	316	8	6	705	18	14
Prince Edward Island	8	375	9	8	838	21	17
Québec	9	333	8	7	744	19	15
Saskatchewan	9.25	324	8	6	724	18	14
Yukon	8.89	337	8	7	754	19	15

	Min wage \$/hr	Subsidy starts: earnings \$3000			Subsidy ends - net income \$9720		
		Min annual hours	Weeks FT	Weekly hrs PT	Max annual hours	Weeks FT	Weekly hrs PT
Alberta	8.8	341	9	7	1105	28	22
British Columbia	8	375	9	8	1215	30	24
Manitoba	8.75	343	9	7	1111	28	22
New Brunswick	8	375	9	8	1215	30	24
Newfoundland and Labrador	8.5	353	9	7	1144	29	23
Northwest Territories	8.25	364	9	7	1178	29	24
Nova Scotia	8.6	349	9	7	1130	28	23
Nunavut	10	300	8	6	972	24	19
Ontario	9.5	316	8	6	1023	26	20
Prince Edward Island	8	375	9	8	1215	30	24
Québec	9	333	8	7	1080	27	22
Saskatchewan	9.25	324	8	6	1051	26	21
Yukon	8.89	337	8	7	1093	27	22

Source: Wikipedia (the shame!)