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Options for a Refundable Disability Tax Credit for ‘working age’ persons

by

Michael Mendelson

June 2015

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Council of Canadians with Disabilities
A VOICE OF OUR OWN

Conseil des Canadiens avec déficiences
CETTE VOIX QUI EST LA NOTRE

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Caledon Institute of Social Policy
1354 Wellington Street West, 3rd Floor
Ottawa, ON K1Y 3C3
CANADA
Tel.: (613) 729-3340
E-mail: caledon@caledoninst.org
Website: *www.caledoninst.org*
Twitter: @CaledonINST

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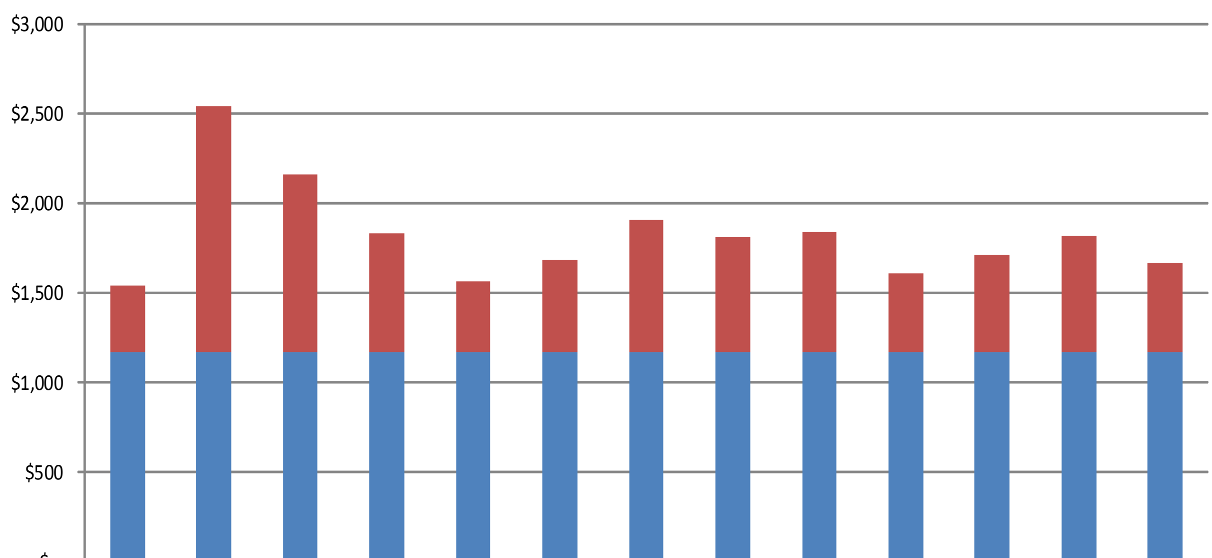
What is the Disability Tax Credit?

The federal government offers a Disability Tax Credit to those who meet certain criteria: broadly, a severe and prolonged impairment in physical or mental functions that restricts activities of daily living. The Disability Tax Credit is established as an ‘amount,’ which is then multiplied by the tax rate for the lowest income tax bracket to arrive at an actual value. In 2014, the ‘amount’ of the federal Disability Tax Credit was $7,766. The tax rate of the lowest tax bracket was 15 percent, so the value of the Disability Tax Credit was $1,165 (15 percent of $7,766) in 2014.

This value is then subtracted from federal income tax owing. If the value is more than the tax owing, the excess value may be transferred to a life partner (a spouse or common-law partner). But if this is not possible for the tax filer, he or she forgoes some or all of the value of the Disability Tax Credit. In short, for those who would otherwise be eligible for the Disability Tax Credit but who owe little or no tax, the Credit is worth little or, in most cases, nothing at all.

In addition to the federal government, the provinces and territories also offer a Disability Tax Credit. A tax filer is eligible for the provincial or territorial Credit if he or she is eligible for the federal credit. Both the amounts and the tax rates for the provincial and territorial Disability Tax Credits vary enormously. Figure 1 shows the actual value (in tax savings) in 2014 of the federal, provincial and territorial Disability Tax Credits. The value varied from a high of $1,372 in Alberta to a low of $375 in BC, with a mean (population adjusted) value of $563 for the provincial and territorial Disability Tax Credits.

Figure 1 Maximum value of federal (Canada), provincial and territorial Disability Tax Credit, 2014



	BC	AB	SK	MB	ON	QC	NB	NS	PE	NL	YK	NT	NU
Prov & Terr	$375	$1,372	$997	$667	$395	$514	$742	$645	$675	$446	$547	$654	$503
Canada	$1,165	$1,165	$1,165	$1,165	$1,165	$1,165	$1,165	$1,165	$1,165	$1,165	$1,165	$1,165	$1,165

The purpose of the Disability Tax Credit

The Disability Tax Credit is not a traditional redistributive transfer meant to reduce poverty and decrease inequality – sometimes called 'vertical equity.' Rather, the Disability Tax Credit is meant to promote 'horizontal equity' between those with disabilities and those without. All persons with severe disabilities have added costs that are difficult to itemize. These costs include, for example, "higher utility costs for heat or air conditioning, additional transportation costs and higher prices for goods because of fewer shopping choices" [Torjman 2002]. The Disability Tax Credit is meant to roughly 'equalize' income between those with the same income, with and without disabilities, after these types of hidden costs have been taken into account.

In our 2010 paper proposing a basic income plan for persons of working age with severe disabilities, we set out the case for a broad conception of this form of 'horizontal equity' that would include not only those paying income tax, but everyone with a severe disability:

> The Report of the Technical Advisory Committee on Tax Measures for Persons with Disabilities discussed the purpose and design of the Disability Tax Credit. According to the Report, the federal Department of Finance sees the purpose of the Disability Tax Credit as promoting 'horizontal equity' [Technical Advisory Committee on Tax Measures for Persons with Disabilities 2004]. In the tax system, 'horizontal equity' is usually considered to mean that taxpayers of similar ability to pay should pay similar amounts of tax. The Disability Tax Credit allows a rough average of non-itemizable disability costs to be taken into account when computing income taxes owed, so that a taxpayer with a disability ends up paying about the same tax on his or her 'after disability costs' disposable income as does a taxpayer without a disability, assuming no other non-deductible disability-related expenses.
>
> From our perspective, the Finance Department view reflects only one aspect of 'horizontal equity' – as it is confined to the income tax system and those who pay income tax. A broader social conception of horizontal equity argues that the added cost of disability should be recognized for everyone with a disability, so that their 'after disability costs' are at least roughly compensated for the additional non-itemizable expenses related to disability, whether or not they pay any income tax. In this social conception, horizontal equity requires that everyone with a disability – not just those with taxable income above a certain amount – should benefit from the Disability Tax Credit. This disability tax break should be related to the fact of having a disability, and not to the person's income" [Mendelson et al. 2010].

How many with severe disabilities do not benefit from the Disability Tax Credit?

In this paper, we develop estimates only with respect to the 'working age' population, from ages 18 to 64, as different programs and policies may be appropriate for children and seniors. This is also consistent with our previous proposal for a basic income for persons with disabilities. We can use the Canadian Survey of Disability to make an educated estimate of the number of people who do not apply for a Disability Tax Credit because they do not have taxable income but who would otherwise meet the criteria and be eligible.

According to the Survey, among the population ages 18 to 64, there were 2,283,300 Canadians with disabilities in 2012. Among these, 49.4 percent reported severe or very severe disability. Taking ‘severe or very severe’ disability as a proxy, albeit inexact, for eligibility for the Disability Tax Credit, there were about 1,130,000 Canadians of working age potentially eligible for the Credit.

According to the Statistics Canada Longitudinal Administrative Databank, there were about 375,000 tax filers ages 18 to 64 claiming the Disability Tax Credit either for themselves or a life partner, but not on behalf of a dependent. At a rough approximation, we surmise therefore that there were likely about 755,000 (1,130,000 minus 375,000) working-age Canadian residents who may qualify under the Disability Tax Credit criteria but who do not benefit from it because they do not have sufficient income.[1]

755,000 may appear at first to be a startlingly large number. However, in Ontario alone, there were 300,000 cases on the Ontario Disability Support Program (social assistance for persons with disabilities). Only a handful of these people would have had any taxable income, but most would otherwise likely be eligible for the Disability Tax Credit. In addition, many people on private disability, Workers Compensation and other programs would likely meet eligibility criteria but have insufficient taxable income to make applying for the Credit worthwhile. Therefore 755,000 eligible persons of working age in Canada as a whole, but unable to take advantage of the Disability Tax Credit due to lack of taxable income, is likely a reasonable ‘ball park’ estimate.

A Refundable Disability Tax Credit

A tax credit that pays its full value to a tax filer, regardless of the amount of income tax the tax filer owes, is called a ‘refundable’ tax credit. A federal Refundable Disability Tax Credit at 2014 values would pay $1,165 to all eligible tax filers, whether or not they owe income tax.

Based on the number of people ages 18 to 64 reporting severe and very severe disabilities in the Canadian Survey of Disability, as discussed above, and increasing that number by 1.7 percent to reflect population growth among those ages 18 to 64 from 2012 to 2014, we find that approximately 1,150,000 people of working age could have been eligible for a Refundable Disability Tax Credit in 2014.

For this disability population estimate, the approximate cost of a federal Refundable Disability Tax Credit in Canada in 2014 would be about $1,336 million. However, this Refundable Credit would completely replace the current Disability Tax Credit, so we need to subtract the cost for working age people of the current Disability Tax Credit to find the incremental federal cost of the proposed Refundable Credit.

As noted, using the Statistics Canada Longitudinal Administrative Databank, we found about 375,000 tax filers ages 18 to 64 claiming the Disability Tax Credit either for themselves or a life partner in 2012. Increasing this estimate to include two years of population growth, we found the approximate cost of the 2014 Disability Tax Credit for the working age population in 2014 was $442 million. So the incremental net cost of a federal Refundable Disability Tax Credit at the 2014 value would be $894 million. This is a very large amount of money, but it is in the mid-range and perhaps even modest compared to the cost of many other tax changes made not only in the last few years, but in the last few decades.

The estimation for federal costs in each province and territory and the total for Canada is set out in Table 1 below.

The provinces and territories and the Disability Tax Credit

Table 1
Net federal cost of a Refundable Disability Tax Credit (RDTC) in 2014 for ages 18-64

	Gross cost of federal RDCT	2014 cost of Disability Tax Credit	Net new cost of federal RDTC
NL	$22,073,560	$11,766,375	$10,307,184
PE	$5,352,796	$3,318,946	$2,033,850
NS	$45,878,013	$20,160,284	$25,717,729
NB	$36,447,229	$13,856,311	$22,590,919
QC	$214,670,919	$64,149,226	$150,521,693
ON	$620,304,014	$186,347,906	$433,956,108
MB	$46,343,949	$28,044,082	$18,299,867
SK	$35,144,766	$11,555,459	$23,589,307
AB	$126,953,672	$43,401,227	$83,552,446
BC	$179,901,451	$58,296,838	$121,604,613
YK	$1,231,247	$261,054	$970,193
NT	$979,762	$-	$979,762
NU	$382,653	$-	$382,653
CANADA	**$1,336,286,324**	**$442,303,054**	**$893,983,271**

If the provinces and territories saw the introduction of a Refundable Disability Tax Credit as an opportunity simply to cancel their non-refundable Disability Tax Credits, there would be large losses for all those persons who now get the full value of the Disability Tax Credit. The loss would be equal to the value of the current provincial and territorial Credits, as seen in Figure 1. Of course, the majority of those with disabilities who were previously getting nothing from the Disability Tax Credit would still be $1,165 better off, but about 375,000 persons with disabilities would be worse off. There are several possible alternatives to avoid this result.

First, and simplest, the provinces and territories could just continue to offer their current non-refundable Disability Tax Credits. There is nothing in the existing federal-provincial tax arrangement that makes this alternative impossible. A second more substantive problem with this solution is that the 700,000+ persons with disabilities who do not benefit from the current Disability Tax Credit would continue to not benefit from the provincial and territorial credits. Nevertheless, this is the least expensive alternative available; it ensures that there are no losers and those who pay little or no tax are still substantially better off. It is, in short, much better than nothing.

A second alternative would be for the provinces to parallel the federal move and convert their Disability Tax Credits to refundable credits. Using the estimating methodology reviewed above, Table 2 shows the gross and net cost to the provinces of introducing their own Refundable Credits at 2014 values. As may be seen, the net additional cost to the provinces would be about $420 million.

A third alternative would be for the federal government to take up part of the value of the current provincial and territorial credits by increasing its Refundable Disability Tax Credit by the mean value of the provincial and territorial credits – $563 – for a federal Refundable Disability Tax Credit of $1,728. This would get the federal Credit closer to the estimated average cost of non-itemizable items for persons with severe disabilities of about $2,000 [see discussion in Mendelson et al. 2010]. This would bring the gross cost of the federal Refundable Disability Tax Credit to almost $2 billion and the net incremental cost to a little more than $1.5 billion.

Assuming that those provinces and territories whose Credit was above the mean would then follow through with converting the value of their Credit above the mean to a refundable

Table 2
Net cost of converting provincial and territorial Disability Tax Credits (DTC) to Refundable Disability Tax Credits (RDTC) at 2014 maximum amounts for ages 18-64

	Gross cost of prov./terr. RDTC	2014 prov./terr. cost of DTC for 18-64	Net new cost of federal RDTC
NL	$8,445,065	$4,501,666	$3,943,398
PE	$3,102,682	$1,923,786	$1,178,896
NS	$25,41,241	$11,167,400	$14,245,840
NB	$23,223,803	$8,829,100	$14,394,703
QC	$94,721,309	$28,305,178	$66,416,130
ON	$210,072,672	$63,108,736	$146,963,935
MB	$26,553,185	$16,068,111	$10,485,074
SK	$30,067,193	$9,885,973	$20,181,220
AB	$149,523,941	$51,117,249	$98,406,692
BC	$57,842,309	$18,743,727	$39,098,582
YK	$577,869	$122,521	$455,348
NT	$550,022	$ -	$550,022
NU	$165,123	$ -	$165,123
CANADA	**$630,258,413**	**$213,773,448**	**$416,484,965**

credit, the net savings to the provinces and territories as a whole would be about $100 million. However, Alberta, Saskatchewan and the Northwest Territories would all have incremental costs as their current Disability Tax Credit is above the provincial/territorial mean. Of these, Alberta would have relatively high incremental costs because of the large amount by which its current Credit exceeds the provincial/territorial mean. Table 3 below shows the overall estimates for this option for the federal government and the provinces and territories.

A final option would be for the federal government to consider an alternative to the current tax credit formula and instead convert the Disability Tax Credit to a federal transfer

Table 3
Federal RDTC equal to the maximum federal DTC plus the mean provincial/territorial DTC, and provinces and territories above the mean implement a RDTC for ages 18 to 64

	Current value of prov./terr. DTC	Prov./terr. DTC over mean value	Gross cost of federal RDTC at max of DTC plus mean of prov./ terr. DTC	Gross cost of prov./terr. RDTC of amount above mean	Net cost of federal RDTC at max of DTC plus mean of prov./terr. DTC	Net cost/(saving) for a prov./terr. RDTC above mean equal to prov./terr. max DTC
NL	$446	$0	$32,742,129	$0	$20,975,754	-$4,501,666
PE	$675	$112	$7,939,903	$515,575	$4,620,958	-$1,408,211
NS	$645	$82	$68,051,726	$3,239,528	$47,891,442	-$7,927,873
NB	$742	$179	$54,062,866	$5,608,166	$40,206,555	-$3,220,934
QC	$514	$0	$318,425,443	$0	$254,276,217	-$28,305,178
ON	$395	$0	$920,108,699	$0	$733,760,794	-$63,108,736
MB	$667	$104	$68,742,858	$4,154,276	$40,698,776	-$11,913,834
SK	$997	$434	$52,130,897	$13,081,062	$40,575,438	$3,195,089
AB	$1,372	$809	$188,312,788	$88,164,825	$144,911,561	$37,047,576
BC	$375	$0	$266,851,232	$0	$208,554,394	-$18,743,727
YK	$547	$0	$1,826,332	$0	$1,565,278	-$122,521
NT	$654	$91	$1,453,299	$76,485	$1,453,299	$76,485
NU	$503	$0	$567,596	$0	$567,596	$0
CANADA			**$1,982,138,830**	**$114,839,917**	**$1,540,058,063**	**-$98,933,532**

payment (i.e., an income program). In the recent changes to federal child benefits, the federal government abolished the previous non-refundable Child Tax Credit, worth approximately $338 per child, and used the resultant savings to boost the Universal Child Care Benefit (from $1,200 to $1,920 for children ages 5 and under), and extend it to children ages 6 to 17 at the amount of $720 a year. The Universal Child Care Benefit is paid as a non-income-tested but taxed transfer payment (though single parent families are excluded from taxation on their benefit). A similar program innovation could be considered for the Disability Tax Credit.

If the federal government introduced a flat-rate taxable transfer payment of, say, $1,165 for each person who meets the eligibility criteria for the Disability Tax Credit, the effect and the cost would be the same as a Refundable Disability Tax Credit for those who paid no income tax, while those who did pay income tax would have a reduced benefit. However if the payment were taxable, there would be considerable net savings compared to a Refundable Disability Tax Credit, although this would sacrifice much of the horizontal equity objective and result in all those paying tax losing some net benefits. At least with this option, the reduced Credit would go to those with the highest income rather than those with the lowest income and everyone eligible would still get some benefit.

While we cannot estimate the savings without better data on incomes of persons with disabilities, the additional tax revenue could reduce net federal costs by a substantial amount. If, say 10 percent of the gross payment were taxed back, then the added cost of converting the non-refundable disability credit to a taxable direct payment would be about $750 million, which is a modest cost compared to most other tax changes. At that level of taxation, the provinces and territories would collect about $70 million more in tax. They could use this sum to reduce the cost of any of the options discussed above, assuming that they would not want to follow the federal lead.

Conclusion

This paper outlines the methods and costs of converting the current Disability Tax Credit to a refundable format. What it does not discuss is the substantial impact such a change would have on the lives of persons with disabilities who, as a group, are among the poorest in Canada. For many, such a change would result in a meaningful increase in income. The paper also does not discuss the interaction with other programs, especially social assistance. As noted, many of those who would benefit from the Refundable Disability Tax Credit are on social assistance of some form. Arrangements would have to be negotiated with provinces and territories to make sure that the federal increases benefited assistance recipients and were not just negated by changes on the provincial and territorial side.

Endnote

1. This may be somewhat of an overestimate because there were also about 220,000 claims made on behalf of dependents and a small percentage of those dependents may be of working age. However, even if say, 10 percent, of those claims were on behalf of working age dependents, this would decrease the 'missing' Disability Tax Credit claims by only 22,000 and would not make a material difference in the estimates.

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