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Delivery of Social Benefits through the Personal Income Tax*

I would like to thank the organizers for inviting me to participate in this symposium. Our panel has been asked to address the role of the personal income tax in achieving social objectives.

There is no single or simple answer to this question. The personal income tax is an ideal system for certain social purposes and a less-than-effective mechanism for other social objectives.

The problem is that the personal income tax currently is used as a blunt instrument for meeting various social purposes. We need to explore whether there are better ways of achieving these diverse objectives.

Now I know that there are few Canadians who would readily agree with me on the following point. But I happen to love the personal income tax system. Why?

Because it is *elegant*. After today's discussion about the need for simplifying the personal income tax, *elegant* is probably the last word one would use to describe this system. But as a mechanism for a specific social purpose – the delivery of income security benefits – it doesn't get much better.

The personal income tax is the national railway of social policy. It provides the most effective method for determining eligibility for and paying income security benefits throughout the country. We see this in the delivery of the Canada Child Tax Benefit.

As a pan-Canadian railway, the personal income tax respects the principle of equity. Eligible Canadians receive the same federal benefit whether they live in Inverness or Iqaluit, Charlottetown or the Queen Charlotte Islands (Haida Qwaii), Ottawa or the Outaouais.

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The personal income tax also enables portability throughout Canada. You can move from sea to sea to sea without worrying about losing benefits or having to requalify for the program.

There is no intrusive administration. Canadians are eligible if their net incomes fall below a designated level. Households need not strip themselves of their assets in order to qualify as is the case for welfare.

The delivery of benefits does become more complex when it comes to income payments in respect of disability. The presence of severe and prolonged disability must be established. This second layer of screening – in addition to level of net income – is required.

But for the delivery of income security benefits on the basis of *readily identifiable* factors, such as age or presence of children, you simply can't beat the personal income tax.

What about use of the personal income tax for other social purposes, such as supporting participation in the arts or recreation, or the provision of child care, caregiving or disability supports? Right now, provinces/territories and voluntary organizations deliver these goods and services, and charge a sliding fee based on household income.

The main federal role has been to help offset the costs of these 'social purpose' goods and services through tax breaks for the individuals who purchase them. We need to ask whether the personal income tax is the best way to deliver these important social benefits. I would answer "not necessarily" to this question on three main grounds: design, policy considerations and philosophical arguments.

With respect to ***design***, most of the tax credits introduced for social purposes take the form of non-refundable credits. Individuals must owe income tax in order to gain any benefit. As a result, non-refundable tax credits leave out households that are too poor to pay tax or that pay relatively little tax. Ironically, these are precisely the people who would benefit most from this financial assistance.

In the 2011 taxation year, for example, 1.5 million Canadians claimed the Children's Fitness Tax Credit. Relatively few of them had low incomes, while the opposite is the case for upper-income claimants. The percentage of taxpayers who claimed the Children's Fitness Tax Credit ranged from less than one percent (.89) of taxpayers with incomes under $10,000 to 22 percent for households with incomes of $250,000 or more [Battle and Torjman 2014].

This skewed distribution is precisely why Caledon has argued that non-refundable credits with a social purpose should, at the very least, be turned into refundable credits. They need to reach the people who require the most assistance paying for these social goods. In fact, the federal government did announce the refundability of the Children's Fitness Tax Credit effective 2015.

Yet another example is caregiver tax credits. Twenty-five percent of Canadians are caregivers of children or spouses with severe disabilities or of aging parents. This percentage is expected to grow substantially with the rapid aging of Canada's population [Torjman 2015b].

Caregivers typically incur costs for this care – sometimes substantial. The federal government provides some relief through several tax measures – notably, the Caregiver Tax Credit and Infirm Dependent Tax Credit. The Family Caregiver Tax Credit is rolled into these other credits.

We have argued that turning non-refundable tax credits into refundable tax credits would ensure that all households, including the very poor, receive some money to offset their caregiving costs. Both Québec and Manitoba currently provide refundable tax credits for caregivers. The Primary Caregiver Tax Credit in Manitoba, for example, is worth a maximum annual $1,275 per care recipient.

Better still, financial assistance for designated social purposes should be delivered as an allowance or direct payment. Nova Scotia pays eligible caregivers a maximum $400 monthly benefit. This type of design helps with the problem of cash flow as the benefit is delivered monthly rather than in one lump sum after reconciliation at the end of the tax year.

But even with refundability, other design problems remain. Households must first pay for specific goods and services in order to qualify for the credit. Even the Children's Fitness Tax Credit, which was introduced in 2007 and then doubled and made refundable in 2015, still means you need to pay to play. The up-front payment is a problem for low-income households.

There are serious ***policy considerations*** when it comes to delivering social benefits through the personal income tax. We need to have a fulsome discussion in this country about the policy purpose of non-refundable tax credits.

In 2004, I co-chaired a Technical Advisory Committee on Tax Measures for Persons with Disabilities that reported to the Minister of Finance and Minister of National Revenue. Our mandate derived from the findings of a Parliamentary Committee, which had identified problems with various disability-related tax measures [Technical Advisory Committee 2004].

Most persons with severe disabilities incur additional costs. In some cases, these extra costs may be partially claimed under the Medical Expense Tax Credit. But households must be able to afford and pay for these expenses in the first place. There is a deductible amount as well. Persons with severe and prolonged disabilities may also qualify for the Disability Tax Credit.

Once again, these tax provisions are of little or no value to persons with disabilities who are too poor to pay income tax. Because the current tax measures are not reaching the people who most require this assistance, our Committee had long discussions about the possible refundability of the Disability Tax Credit. But we were always halted in our tracks.

The Committee was reminded repeatedly by the Department of Finance that the purpose of non-refundable tax credits is to enable Canadians' ability to pay income tax. Finance officials made clear that their scope of concern was the *universe of taxpayers*. The needs of the rest of the population were deemed to be the responsibility of other departments.

I don't believe that the spate of boutique tax measures introduced in recent years can pass this policy test. If the major purpose of non-refundable credits is to enable the ability to pay income tax, I am not sure how measures, such as the Children's Arts Tax Credit, Children's Fitness Tax Credit, Search and Rescue Volunteers Tax Credit or Adoption Expenses Tax Credit, fit that bill.

There appears to be a contradiction between the policy theory and actual practice. There are certainly some policy apples and oranges that are making for a strange conceptual mix. Many 'social purpose' tax measures that have come on board appear quite inconsistent with the Department's earlier stated policy purpose.

Finally, there are ***philosophical questions*** regarding the provision of non-refundable tax credits for social purposes. For one thing, adequate income security transfers and a progressive income tax system are the major policy levers for reducing inequalities in market incomes. But as the income tax system delivers more benefits to higher-income Canadians, it has exacerbated – rather than offset – income inequality.

Another philosophical issue has to do with whether we incentivize and reward the behaviour of selected families or whether we invest in social goods that can be used by the entire population.

A burgeoning literature is pointing to the value of recreation for all ages for both physical and mental well-being. It documents the vital role of exercise in helping to remediate and prevent cardiovascular illnesses, neurological conditions and even dementia. Canada is facing an astoundingly high and rising incidence of chronic disease.

Given what we know about the value of active living and recreation, we have argued the need to invest in recreational programs and amenities that are available to Canadians of all ages and income levels. An evidence-based approach to policy-making would call for investment in the social infrastructure of communities and not in the pocketbooks of individuals [Torjman 2012].

Private households cannot possibly build and maintain through their individual contributions the facilities and programs that communities require. The $115 million annual expenditure on the Children's Fitness Tax Credit could be spent instead on national parks, walking trails, community fitness and retrofit of facilities. Year over year, the same money could be used to far better purpose.

The Children's Arts Tax Credit is another example. There is a large body of evidence of the value of arts and cultural programs for positive social and psychological development for all children. Why would we confer the advantages of this participation only to well-off children whose families would enroll them in these activities with or without a tax break?

If we are really talking about social purpose measures, then benefits should go not only to those with the greatest ability to pay – who would probably engage in the activity in any case. We have recommended using scarce public resources to provide opportunities for all children, the poor in particular rather directing limited resources toward families that can afford to purchase these social amenities.

The basic challenge has to do with relative investments in supply and demand. Should we support the demand side of the equation (i.e., the ability to pay) in which a small percentage of the population get tax breaks? Or should we invest as a society in the supply side of the equation in the form of fitness programs, community arts programs, respite for caregivers, disability supports – the actual social amenities and services that are available to the population?

The current federal government prefers to support the demand side of the equation. Sometimes this approach is a good thing. In certain areas of social policy, we are moving toward the demand side of the equation by finding new ways to help people offset costs.

Some provinces, like Alberta, provide individualized funding as a way of meeting the unique needs of persons with disabilities. They receive dollars directly from the government to enable them to purchase precisely the goods and services they require.

Work is also under way in several provinces to deliver housing assistance through a housing supplement rather than building the supply of affordable homes. It is a more expeditious way to meet the pressing demand for this assistance and is portable across housing types and communities.

Unlike current tax measures, these types of demand-side funding are made available to households at the low end of the income scale. But demand-side funding cannot meet all social purposes.

With the rapid aging of the population, growing numbers of Canadians will require assistance with the activities of daily living. Given the current limitations of the income tax system in assisting persons with disabilities and addressing the needs of an aging population, it is preferable to invest in the supply of the required goods and services.

An expanded focus on accommodation is one way to proceed. Funds currently spent on selected tax measures could be redirected toward schools, training centres, post-secondary educational institutions, small and medium-sized enterprises, and municipalities to enable them to introduce various forms of accommodation.

Another crucial action that the federal government can take is to invest in the supply of disability supports, which include technical aids and equipment and various services provided at home. There are many ways to do this: a Disability Supports Fund, federal income benefit for persons with several disabilities with an associated provincial/territorial investment in disability supports or National Disability Supports Insurance. We have been exploring these options [Torjman 2015a].

The federal government may prefer to use the personal income tax for social purposes because it can move expeditiously to implement its own agenda. It does not need permission from the provinces and territories. It need not engage in antagonistic bilateral or multilateral negotiations.

A one-size-fits-all tax formula may be politically expeditious. But it is not the most effective solution when it comes to complex social issues like the participation of persons with disabilities, Canada's aging population and the rising incidence of chronic disease.

Effective policy should trump expedient politics if we are truly concerned about the well-being of Canadians.

Sherri Torjman

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1354 Wellington Street West, 3rd Floor
Ottawa, ON K1Y 3C3
CANADA

Tel./Fax: (613) 729-3340

E-mail: caledon@caledoninst.org
Website: *www.caledoninst.org*
Twitter: @CaledonINST