CALEDON INSTITUTE OF SOCIAL POLICY

The Déjà Vu All Over Again Budget

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The 2010 federal Budget arrived with less drama than usual. Why? Because we have seen echoes of it before – notably last year in 2009, four years ago in 2006 and 15 years ago in 1995.

2009 revisited

The 2010 Budget is effectively the second year of the stimulus package introduced in last year's Budget. The purpose of the stimulus package is to prop up a moribund economy, stave off rising unemployment and prevent further decline. Downward slides may be good Olympic sport, but they make for poor economic prospects and even worse social conditions – not to mention political suicide.

The stimulus package is Canada's response to the economic recession, which scathed the entire world. While the downturn was not a made-in-Canada problem, it did require a made-in-Canada response.

The fiscal shot in the arm, though necessary, was a shot in the dark. The impact of stimulus spending in the board rooms, on factory floors and in the pocket books of the nation will be known only after the economy is clearly out of recession and the economists do their analyses.

The jury is still out on whether the stimulus was enough. The measures have undoubtedly helped keep the lid on rising unemployment – though at 8.3 percent in 2009, up from 6.2 percent in 2008 – it is still unacceptably high and projected to rise further to 8.5 percent in 2010 before it gradually eases in future. Thousands of jobs lost in the past two years, including well-paid full-time employment, have not been recovered and may never come back.

Other signs are more positive. The latest figures on economic growth found that GDP surged 5 percent on an annualized basis in the last quarter of 2009.

Despite mixed reviews of the stimulus package, the government stayed the course. Budget 2010 is basically a restatement of 2009. Virtually all its spending measures represent the second installment of a two-year package.

Caledon had assessed the 2009 Budget on the basis of the following assumptions.

Spending injections for stimulus purposes ideally should be delivered through income programs, such as the Canada Child Tax Benefit and Working Income Tax Benefit targeted to low- and modest-income Canadians. Employment Insurance is in need of major repair because of its drastically inadequate coverage. These income programs put cash directly into the hands of families and individuals who are more likely to spend it right away and thus help stimulate the economy.

Income tax cuts, by contrast, are more apt to be saved or used to pay down personal debt, especially if the largest tax savings are enjoyed by those with high incomes. We also called for investment in infrastructure that creates jobs in the short term and helps build prosperous, strong and healthy communities in the long term.

Last year's *Red-Ink Budget* was a mixed bag. On the plus side: The Working Income Tax Benefit was increased and extended to assist more working poor Canadians.

Employment Insurance, which should be a bulwark during recession, saw some useful but limited changes in Budget 2009. But these changes were restricted to two years and were not intended to become a permanent feature of the EI program. Only 48 percent of Canada's unemployed received regular EI benefits in 2009.

The maximum duration of Employment Insurance benefits was lengthened by an extra five weeks, up to a maximum of 50 weeks. After last year's Budget and under pressure from the NDP, the federal government made another important change. It extended – by up to 20 weeks – the duration of EI regular benefits for unemployed persons who, prior to the 2008-09 recession, had been gainfully employed for a long period and had previously made limited use of the program.

Training measures for the unemployed were enhanced in the 2009 Budget for some workers who do not qualify for EI. Ottawa also extended EI benefits for persons participating in longer-term training, the target being individuals who have lost their job after working many years in one industry or for one employer.

The 2010 Budget at least should have extended EI benefits for several more months to the many thousands of workers who have been exhausting their EI entitlements over the last year. Many have no recourse but welfare. Just in the month of January 2010, there were more than 10,000 new social assistance beneficiaries in Ontario alone.

Instead, all we got were a couple of worthy but relatively small improvements to sickness and parental benefits – which will do nothing to close the glaring gap between the large number of unemployed Canadians and the fraction that manage to qualify for Employment Insurance. But at least these two changes will be permanent.

Ottawa will provide $6.6 million over two years to strengthen support for victims of crime, including facilitating access to EI sickness benefits for eligible workers who have lost a family member as a result of crime.

Employment Insurance offers parental benefits to eligible parents who are adopting a child or caring for a newborn. Parental benefits for biological parents and their partners are payable from the child's birth date, and for adoptive parents and their partners from the date the child is placed with them. Parental benefits are available only within the 52 weeks following the child's birth, or for adoptive parents, within the 52 weeks from the date the child is placed with them. To help members of the Canadian Forces whose parental leave is deferred or interrupted because of military requirements, EI will extend by another 52 weeks the period in which they are eligible for parental leave.

The 2009 Budget enhanced work-sharing agreements, intended to avoid layoffs by providing EI benefits to qualified employees willing to work a reduced work-week. The agreements were extended at that time from 38 weeks to 52 weeks. Budget 2010 builds on that advance by stretching these provisions for a further 26 weeks, to a maximum 78 weeks, until March 2011. This measure has helped keep some 30,000 workers from being laid off.

Financing Employment Insurance is a dicey issue. According to the existing rules for EI financing, premiums are to be set by an independent board each year at a rate sufficient to pay for the forecast costs of EI, though the change in premiums in any one year is limited to 15 percent. In addition, Cabinet may override the rules by edict. As we anticipated in our 2009 Budget commentary, Cabinet is once again exercising its powers. The EI premium rate is being frozen for another year, to the end of 2010. So far the EI financing rules are batting zero for five. After being created in 2005, the independent rate setting Board has never been allowed to set the rate.

We remain skeptical that the financing regime will finally be implemented in 2011 and even more doubtful that it *should* be implemented. If the rules were implemented, premiums would rise by 15 percent a year (compounded) for the foreseeable future. It is entirely appropriate that EI premiums eventually go up – when unemployment is significantly down – but not before.

The current EI financing rules are, in reality, unenforceable because they are pro-cyclical when they should be counter-cyclical. Were the rules applied, premiums would go up when unemployment increases and down when it declines. There is no chance of this happening in the next few years because the EI fund has built up a solid deficit. So we can anticipate a spate of increases whenever Cabinet takes the lid off, regardless of economic conditions. Nonetheless, it is clear that the EI financing rules in place are non-functional and – dare we say it so bluntly – dumb. The government needs to initiate a serious and careful review of EI financing involving both labour and business, so we can have clear, stated rules and accounting for EI financing that is both operable and sensible.

Budget 2010 continues the 2009 investments in infrastructure in community hardware such as roads, sewers and water mains. Federally owned buildings, bridges and airports were slated for upgrading. There was money for housing construction and repair, including the popular Home Renovation Tax Credit. Infrastructure funds for First Nations' communities were directed toward schools, water supply, health and police.

Caledon supported last year's announcements because of the potentially positive impact of infrastructure investment on economic, social and environmental well-being. We had expressed concern, as did others, about Ottawa's ability to get the money out the door quickly – especially because much of it requires matching by provincial and local governments. Stimulus money spent too late could heat up the economy when the fire is no longer required.

Budget 2010 reminds us of these investments – and of the fact that they will all be ending this fiscal year. It is clear that there is no intention on the part of the government to take seriously the need for ongoing infrastructure support for social housing in particular. At the end of the stimulus spending, it has no future plans to give this policy orphan a home.

There was a thin sprinkling of new initiatives in Budget 2010 worth noting.

Several measures for youth were announced. The Canadian Youth Business Foundation will receive $10 million to assist young entrepreneurs. A further $20 million was allocated to Pathways to Education for its work in promoting literacy and school completion for disadvantaged youth. The Skills Link component of the federal Youth Employment Strategy will be increased by $30 million to assist young persons with disabilities, Aboriginal youth, recent immigrants and students who have not completed high school. The Career Focus component of the Youth Employment Strategy will also be increased by $30 million to help more graduates obtain training in their field.

Two key announcements affect persons with disabilities. The Enabling Accessibility Fund to assist persons with physical disabilities will be extended for three years with an additional $45 million over that period.

Changes were also introduced to the Registered Disability Savings Plan, launched in 2007 to help parents ensure the financial security of their child with a severe disability. The federal government assists lower- and modest-income households through Canada Disability Savings Grants and Canada Disability Savings Bonds. Budget 2010 allows a 10-year carry forward of the latter measures to help families that may not be able to contribute regularly to their disability savings plans. The Budget also permits a deceased person's RRSP or RRIF proceeds to be transferred tax-free to the RSDP of a financially dependent infirm child or grandchild.

In the area of Aboriginal education, the Budget announced new funding of "$30 million over two years to support an implementation-ready tripartite K-12 education agreement." The odd wording of this announcement suggests that this funding is for a single, specific K-12 agreement. The most likely candidate is the BC First Nations Education Authority, which was to be set up under the *First Nations Jurisdiction over Education in British Columbia Act*. The *Act* and a complementary statute in BC were passed in 2006 to reflect a tripartite agreement among a group of BC First Nations, Ottawa and the provincial government. While the agreement was greeted with great fanfare in Ottawa and Victoria, it turned out that there was insufficient funding for implementation.

If this additional $30 million is indeed funding for the BC agreement, this is welcome news – with a few caveats. First, most or all of the funding will need to be ongoing, not just for two years. Second, during the last four years of hiatus many of the First Nations that were part of the original consensus have become frustrated and reportedly have gone their own way. Despite these concerns, this announcement is good news, but Ottawa must be prepared to exercise patience and time to reconstruct the implementation process.

In another announcement, which may have been more suitable to a Throne Speech than a Budget, the government stated that it is ready to "work with First Nations groups and other willing partners to develop options, including new legislation, to improve the governance framework and clarify accountability for First Nations elementary and secondary education."

The Caledon Institute of Social Policy has long called for the development of such a framework. This somewhat understated and slightly cryptic Budget statement may indicate Ottawa's concurrence that such a framework is needed. If so, it is a significant advance in policy and holds real hope for systemic improvements in First Nations outcomes. The Budget statement should be seen as a positive invitation to the Assembly of First Nations and to regional First Nations organizations to step forward and open discussions. We hope the Minister of Indian and Northern Affairs will take advantage of a later opportunity to clarify and expand upon the intent of this announcement.

More ominously, there have been rumours circulating among First Nations educators about planned changes in the Post-Secondary Student Support Program, the main vehicle through which First Nations are financed to provide assistance to their students attending post-secondary institutions. Over the last decade, the number of students assisted has fallen from about 30,000 to 20,000 due to the crunch between rising tuition and living costs, and constrained increases in the Support Program. At the same time, more First Nations students are qualifying for post-secondary schooling, which should be unabashedly good news and not a problem.

It appears that the rumours were correct. The Budget announced that the government will introduce a new approach to post-secondary support for First Nations students. The Budget language is ominously unilateral, with use of the word 'will' and no mention of negotiations with First Nations.

While the Post-Secondary Support Program could benefit from reform, the biggest problem seems to be that it has been held to 2 percent annual increases while tuition has spiralled upwards. Even if the new program does provide better support to more students, unilateral implementation will put a huge damper on what should otherwise be a positive development. Our prediction is that the federal government may in the end find that unilateral change is even more difficult and costly to implement than the admittedly long, drawn-out process of negotiation.

There was also less in Budget 2010 than might have been anticipated from the Speech from the Throne. The Speech, read the day prior to the Budget, recognized a significant social innovation in the country in which citizens, businesses and charitable groups join forces to tackle local problems. The Speech noted that the government would take steps to support communities in their efforts to resolve local challenges, but gave no indication as to what those actions would be. This promising methodology of place-based initiatives was notably absent from Budget 2010.

Last year's income tax cuts, in our view, were both unnecessary and damaging. They left a fiscal cavity that will be painful to fill.

Corporate tax cuts are especially pointless right now, as corporate taxes are paid only by companies making a profit. These reductions in corporate income tax will do nothing to help struggling small – and large – businesses get through the recession. The cuts will, moreover, further erode Canada's fiscal position by lowering taxes on precisely those companies that can best afford to pay – namely those with taxable profits.

In short, the 2010 Budget follows the route previously charted. Unfortunately, it does not seek to tackle some tough problems that the country now faces in terms of protecting income for the unemployed, providing relief for caregivers and ensuring adequate independent living supports for an aging population. The only initiative for seniors comes in the form of $10 million over two years to enhance the New Horizons program that supports volunteering. The need for a discussion of how to ensure a "strong and efficient retirement income system" was flagged in the Budget and is scheduled for the upcoming meeting of Finance Ministers in May.

2006 revisited

Budget 2010 focuses our attention on the government's new interest in innovation. Perhaps "renewed" is the more appropriate word. The last foray into the innovation field was in 2006 when Canada's New Government introduced a manifesto called *Advantage Canada*. The document was billed as a long-term plan to help create conditions for economic success. It set out five areas in which Canada should gain global competitive advantage.

Tax advantage involved tax reductions for households and business. *Fiscal advantage* called for eliminating government net debt. *Entrepreneurial advantage* would reduce unnecessary red tape and increase market competition. *Knowledge advantage* would create the best educated and most skilled workforce in the world. *Infrastructure advantage* would build the modern underpinnings of innovation.

Actions in the 2010 Budget concerning corporate tax cuts, supports for entrepreneurs, investment in human capital and a more competitive business environment draw from this earlier blueprint. We certainly have seen these measures before, even though they are now being touted as recalibrated new think. *Déjà vu.*

Another flashback from that year: The 2006 Budget brought the Universal Child Care Benefit, one of the Conservatives' key election platform promises. The program pays $100 a month to all families with children age 5 and under.

Budget 2010 announced a significant change in the Universal Child Care Benefit, one of the federal government's three child benefit programs – the Canada Child Tax Benefit and the nonrefundable child tax credit being the other two. Unfortunately, the new measure will simply trade one inequity for another and leave the Universal Child Care Benefit just as complicated and inequitable as before.

The Universal Child Care Benefit (UCCB) is subject to federal and provincial/territorial income taxes. In two-income couples, the parent with the lesser income pays income tax on the UCCB. In one-income couples, the parent with the income pays tax on the UCCB, and ditto for single-parent families.

This feature of the program creates unfairness because families of different types (i.e., one-income couples, two-income couples and single-parent families) with the same net income can end up with differing after-tax UCCB benefits. To confuse matters even more, families with the same net income but living in different jurisdictions may receive different after-tax benefits because their UCCB payments are also subject to variable provincial/territorial income tax regimes.

The Budget notes that a single-parent family can end up paying more income tax on their Universal Child Care Benefit than a one-earner couple with the same income. To remedy this problem, single parents will be allowed to choose to include their UCCB payments in the income of the dependant for whom an Eligible Dependent Credit is claimed, thus providing treatment comparable to one-earner two-parent families. In most cases, the dependant child would not be subject to tax and so the family would keep the maximum $1,200 UCCB annual payment. Or the parent can continue to include the UCCB in their own income, as is the current practice. This change will cost Ottawa an estimated $5 million in 2010-11 and $5 million in 2011-12.

But the change will create new inequities. If we read the Budget correctly, then virtually all single-parent families which opt to include their UCCB payments in the income of the dependant (which surely most will do) will pay no federal income tax on their UCCB – whatever their income. Yet one-earner and two-earner couples will continue to pay income tax on their UCCB (with the exception of very poor families below the tax threshold) and so will end up with smaller benefits than single-parent families with the same net income. This is patently unfair.

So the UCCB will remain a complicated and virtually incomprehensible social program in terms of its real as opposed to apparent value to families – i.e., its after-tax rather than pre-tax value. Its name is also deceptive: The Universal Child Care Benefit is not tied to use of child care and, even if used for this purpose, covers but a fraction of the cost of child care for most families.

Oddly, the Universal Child Care Benefit is the only federal income program that is not indexed. The much-touted $100 monthly payment when the UCCB was introduced in 2006 is now worth only $92 and will continue to erode each year by the amount of inflation – a classic case of social policy by stealth.

There is a simple solution to the failings of the Universal Child Care Benefit: Get rid of it and use the $2 billion in savings to bolster the geared-to-income Canada Child Tax Benefit, a fair and transparent social program that pays the same non-taxable amount to all types of family with the same income everywhere across the country.

1995 revisited

There is yet another section of the 2010 Budget that hearkens back to an earlier time: its theme of deficit reduction. This is not the first time that Canada has wrestled with the deficit dragon. Ottawa's last round of major deficit reduction took place 15 years ago in the 1995 Budget.

That previous effort to reduce the federal deficit and debt burden landed squarely on the back of provincial social programs. One of the major building blocks of the social safety net – the Canada Assistance Plan, which shared with the provinces the costs of their social assistance programs and social services – was dismantled and replaced by a new form of financing called the Canada Health and Social Transfer, a block fund which arrived with a massive cut. It subsequently evolved into the Canada Health Transfer and the Canada Social Transfer.

Ottawa's cuts to social transfer payments to the provinces led to reduced benefits and services mainly at the expense of low-income Canadians, who ended up carrying much of the burden of deficit reduction. Canada became a more unequal and harsh society as a result.

In retrospect, it is now clear that not all of the deep cuts in public programs were necessary, as proven by the later huge reductions in taxes – suddenly affordable – over the last decade. Moreover, all of the money removed from health transfers subsequently was replaced, and then some.

We also learned, in the transition from cost sharing to block funding, that a dollar is not a dollar. The way in which funds are transferred between governments makes a big difference in their capacity to intervene in problems – especially those exacerbated by the uncertainties of economic cycles.

The dismantling of the Canada Assistance Plan meant the loss of built-in cyclical protection. When provincial costs rise with higher welfare caseloads resulting from recessions, the federal government no longer picks up 50 percent of the tab. The loss of federal cost-sharing put serious pressures on the last-resort income safety net, which was already tattered.

It is likely that Canada would have been in a better position to protect those bearing the brunt of the current recession had we not destabilized the social underpinnings formerly in place.

As noted, the Canada Assistance Plan provided for investment in more than income security. It also shared the cost of a range of social services furnished by the provincial and territorial governments, many of which will be required in future by an aging population and to prevent that population from becoming more dependent more rapidly. With the benefit of hindsight, it appears that the cuts in social services may have been shortsighted as well.

But the 2010 Budget made a clear pledge that this time will be different. The government attests it will not cut federal transfers to individuals – i.e., major programs such as Old Age Security and the Guaranteed Income Supplement for seniors and child benefits such as the Canada Child Tax Benefit. Nor will it reduce social transfers to the provinces and territories.

In contrast to 1995 when the tough cuts were simply announced with no warning, Budget 2010 at least opens up the deficit-cutting conversation. It promises explicitly *not* to revisit the mistakes of the past.

the medium term

Caledon welcomes a national conversation on deficit slaying. In our response to the spending hikes in last year's Budget, we called for a sensible strategy when payback time comes due. We are examining in greater depth possible options for deficit reduction. The following speak to just some of our concerns.

The Harper government's decision to reduce the GST rate from 7 to 6 and then 5 percent permanently punched a big hole in federal revenue capacity – some $11.5 billion in 2009-10. The Finance Minister had argued at the time that the cut in GST was made in anticipation of the need for stimulus in a recession. If true, the government should be open to restoring the GST in the recovery.

Another wrong-headed move in our view was the introduction of $2.2 billion worth of income tax cuts in last year's Budget, which further eroded the federal revenue base on a permanent basis. The largest tax breaks went, not surprisingly, to Canadians with higher incomes and not to those with low and moderate incomes as last year's Budget had claimed.

These kinds of tax cuts are relatively ineffective as fiscal stimulus because higher-income taxpayers tend not to spend tax cuts but rather bank them or pay down debt. By contrast, doubling the GST credit would have had a greater stimulative impact and could have easily been reversed in the recovery.

Canada is limping out of recession, but unemployment has yet to recede. So in the near term, expenditures on Employment Insurance will continue to be high.

But even when the recession is over and the jobless picture improves, the aging of the population will exert relentless and growing demands on federal and provincial/territorial coffers – on elderly benefits for Ottawa and on health care for the provinces and territories – as the baby boomers bloom in their older years.

These swelling areas of public spending threaten to crowd out other important social programs that require investment such as child care, child benefits, income supplementation for the working poor, supports to persons with disabilities, help for caregivers and services for Aboriginal people and new Canadians.

To help deal with these pressures, the federal government should plug the major tax leak in the GST and scrutinize its programs to ensure they are sound and effective. Governments at all levels must look carefully at their programs to make sure they are efficient, effective and equitable.

Several federal measures fail to measure up including the Universal Child Care Benefit, nonrefundable child tax credit, splitting of pension income and flaws in the design of elderly benefits. These programs deliver substantial benefits to high-income Canadians – money that would be better spent on assisting low- and modest-income households hit especially hard in the recession.

This is not the first time that Caledon has called for a review of program design and associated expenditures. There is a small fortune currently being spent on the fortunate. It is time to replay that message and to revisit that practice. *Déjà vu*.

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