REPORT

The Canada Saver's Credit

A proposal to build financial security for lower- and modest-income Canadians

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Acknowledgments

This proposal grew out of the Common Good Retirement Initiative (www.commongoodplan.org), a cross-sectoral, collaborative effort to strengthen retirement security within Canada's not-for-profit sector. Part of Common Good's mandate is to explore public policy ideas that would help build long-term financial security for lower- and moderate-income Canadians, including those working in Canada's voluntary sector. The authors of this report are André Côté, an independent public policy consultant, and Alex Mazer and Jonathan Weisstub, cofounders of Common Wealth, one of the partners on the Common Good project. This work was made possible through the generous financial support of Common Good's funders, including Maytree, Vancity, the Metcalf Foundation, the Atkinson Foundation, the Hamilton Community Foundation, and the Lawson Foundation. Maytree also provided generous in-kind support in producing the report.

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Subject matter experts consulted

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- Bob Baldwin, independent pensions consultant, advisor, and board member
- Timothy Flacke, Executive Director, Commonwealth (formerly D2D Fund)
- Brian Gilmore, Senior Innovation Manager, Commonwealth (formerly D2D Fund)
- J. Mark Iwry, Nonresident Senior Fellow, Brookings Institution; former Senior Advisor to the US Secretary of the Treasury, and a principal architect of the Saver's Credit

- David John, Deputy Director of the Retirement Security Project, Brookings Institution
- Elizabeth Mulholland, Chief Executive Officer, Prosper Canada
- Jennifer Robson, Associate Professor, Kroeger College, Carleton University
- Richard Shillington, statistician
- John Stapleton, Innovation Fellow, Metcalf Foundation

About Maytree

Maytree is committed to advancing systemic solutions to poverty and strengthening civic communities. It believes the most enduring way to fix the systems that create poverty is to have economic and social rights safeguarded for all people living in Canada. Maytree's work supports leaders, organizations, and civic communities by developing and sharing knowledge; strengthening learning and leading; and mobilizing action to further social and economic rights.

About Common Wealth

Common Wealth is a mission-driven business focused on expanding access to retirement security. Based in Toronto, Common Wealth designs and manages collective retirement plans for groups of workers who are uncovered or underserved by traditional workplace retirement plans. Recently, the company helped create the first retirement plan in Canada for lower- and moderate-income earners, and is currently working with a group of foundations and employers to create Common Good, a national, portable retirement plan for Canada's not-for-profit sector. Common Wealth also advises and partners with a wide range of institutions in both Canada and the United States on initiatives that will materially strengthen retirement security, including governments, unions, associations, and pension funds, with collective assets under management exceeding $800 billion.

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Executive summary

This paper proposes a targeted policy intervention to help boost savings and build assets among modest-income Canadians: the Canada Saver's Credit (CSC). The CSC would provide lower- and moderate-income Canadians with a refundable, dollar-for-dollar match of up to $1,000 per year for contributions into a Tax-Free Savings Account (TFSA). We offer the CSC proposal as a starting point to inform debate among policy-makers and stakeholders about how to improve savings outcomes among modest-income Canadians.

The CSC is not an entirely new idea. It builds on, and attempts to improve on the shortcomings of a US program called the Saver's Credit which was enacted in 2001. In a Canadian context, it is a more detailed version of an idea first proposed by two social policy experts who were among the original proponents of the TFSA as a savings instrument for modest-income Canadians: John Stapleton and Richard Shillington.

Modest-income Canadians face challenges when it comes to building asset wealth. Studies estimate that one third of Canadians are "asset poor" – meaning they lack savings to live for three months above the poverty threshold. Sixty per cent of Canadians with incomes below $50,000 do not contribute to a tax-advantaged savings account, whether a TFSA, a Registered Retirement Savings Plan (RRSP), or a workplace pension plan. Canadians with lower incomes are considerably less likely to have access to a workplace pension, and the median retirement savings of Canadians age 55-64 without pensions is a meagre $3,000. Given the changing nature of work and constrained household budgets, these outcomes are unlikely to improve in the future absent some intervention, posing a challenge for the equality of Canadian society.

Canada's tax system could do more to help modest-income Canadians build savings. Although the federal government reports $45 billion dollars in tax expenditures to confer advantages on RRSPs and pension plans, most of this spending benefits middle- and upper-income Canadians. The savings incentives embedded within our tax system are effectively "upside down." Lower-income Canadians saving in RRSPs receive little in the way of tax deductions for their contributions, and risk being subject to a punitive Guaranteed Income Supplement (GIS) "clawback" of 50 per cent or more when they use these savings for retirement income. Although TFSAs are widely considered a better

savings vehicle for modest-income Canadians, there is no up-front incentive for these modest-earners to open or save in a TFSA account.

The CSC would be a simple, flexible way to help Canadians with low and modest incomes increase their savings – for improved day-to-day financial security, major purchases, or retirement. Its design features would include:

- **Refundable tax credit aimed at households on low and modest incomes,** offering a dollar-for-dollar match up to 100 per cent of an eligible saver's TFSA contributions (or an employer's contributions made on behalf of an eligible employee) during the calendar year to a cap of $1,000 annually (thereby increasing the TFSA account balance by up to $2,000 annually).
- **Eligibility would mirror the GST/HST credit**, with the full matching amount available to savers with family net income of about $36,000, with a smoothed phase-out.
- Like the GST/HST credit, the **Canada Revenue Agency (CRA) would administer the credit and automatically determine eligibility** through the annual tax-filing process. Savers would be notified of their Saver's Credit entitlement through the annual Notice of Assessment.
- The credit would be **deposited directly into the saver's TFSA account,** with funds flowing from the Government of Canada to the financial institution that maintains the TFSA. This would discourage immediate consumption, while offering the saver flexibility in accessing their funds.
- **Both individual and group TFSA accounts would be eligible for the credit.** Given evidence of the effectiveness of workplace-based plans, efforts should made to **encourage employers to offer group plans** to employees with automatic payroll contributions and the option of offering additional employer contributions.
- The design should **limit negative interactions with income-tested or retirement benefits** (e.g., GIS, family responsibility), and help reduce barriers to accessing financial services.

- **The roll-out of the CSC** should be complemented by consumer awareness programs and initiatives (e.g., financial literacy, tax filing, behavioural "nudges" that can encourage uptake) engaging employers, financial institutions, tax preparers, and the range of civil society and social services entities that support greater savings and financial security.
- The costing and fiscal impacts of the proposal would require more detailed and dynamic modeling but, based on the proposed design, a **simple, static estimate suggests a cost range of approximately $550 million –** or just above 1 per cent of the $45 billion in current Government of Canada tax expenditures on RRSPs and pension plans.[1]

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1 The estimate assumes take-up of 10 per cent (double the US Saver's Credit rate) on an eligible population base of about 11 million, with average credit value of 50 per cent of the maximum ($500 per year). Further details are provided later in the paper.

Foreword

By Mark Iwry

The people of Canada and the United States share a number of common challenges. Prominent among these is a lack of financial readiness for retirement and a lack of savings among lower- and modest-income households. Too many Canadians and too many US citizens are at risk of retiring without the ability to maintain an adequate standard of living. In addition, too few have even enough savings to sustain them through short-term emergencies. Moreover, both countries' tax incentives for retirement savings generally are structured in a way that tends to benefit those in high tax brackets more than modest- or lower-income households. Too often, as a result, those who need the help the most receive the least.

Accordingly, nearly two decades ago, we in the United States developed a simple, 50 per cent, refundable retirement savings tax credit targeted to modest- and lower-income savers. Designed in the US Treasury Department as a kind of government matching incentive to help "level the playing field" for working families and encourage them to engage in tax-favored retirement saving, we called it the "Saver's Credit."

Congress enacted the Saver's Credit in 2001, but only after drastically cutting back our proposed design to a version that was almost unrecognizable – not refundable, the credit cut in nearly all cases from 50 per cent to only 10 or 20 per cent, and not deposited to the account in which the individual saved. Under political and industry pressure, Congress diverted resources from what would arguably be the single most progressive element in the US private pension system in order to further raise maximum tax-favored retirement plan saving limits used mostly by upper-income individuals. Nevertheless, even in its truncated form, the Saver's Credit is claimed each year by some 8 million modest-income US taxpayers.

In the thoughtful and important paper that follows, Common Wealth and its dynamic founders, Jonathan Weisstub and Alex Mazer, along with co-author André Côté, propose a similar solution for Canadian savers, growing out of the Common Good Retirement Initiative. And they propose to get it right the first time: a targeted, refundable, dollar-for-dollar credit in the form of a

match. Meanwhile, in the United States, we are embarked on a similar project, proposing legislation in Congress to improve and enlarge the US Saver's Credit by restoring it more closely to its original proposed design before it reaches its 20th anniversary. As our two nations pursue these parallel paths, we have much work ahead of us, much to learn from one another, and much to hope for in expanding saving and retirement security for all of our citizens.

J. Mark Iwry, Washington, DC, January 2019

J. Mark Iwry, a nonresident Senior Fellow at the Brookings Institution in Washington, DC, and a Visiting Scholar at the University of Pennsylvania's Wharton School, was one of the main architects of the Saver's Credit nearly 20 years ago and has been a continuing proponent of expanding it. He served as Senior Advisor to the US Secretary of the Treasury from 2009 to early 2017 as well as in other posts at the US Treasury Department (1992-2001), where he initiated and led numerous reforms of the private pension system. He previously served as a partner in the law firm of Covington & Burling and as Of Counsel to the law firm of Sullivan & Cromwell.

Introduction

It is an important moment for social policy in Canada. Accelerating changes in the economy and labour market are highlighting skills gaps, wealth stratification, and levels of financial and socio-economic insecurity for low- and modest-income Canadians. Many governments, civil society leaders, businesses, and public institutions are signaling a firm commitment to update Canada's social and employment policy architecture to address these issues.

In recent years, a number of ambitious and forward-looking federal, provincial, and local initiatives have been introduced, aimed at addressing cross-cutting issues such as poverty, employment and income security, housing affordability, Indigenous reconciliation, and retirement savings adequacy. At the national level, major initiatives have included the expansion of the Canada Child Benefit, the introduction of a National Housing Strategy, the renewal of the Labour Market Transfer Agreements, and enhancements to the Guaranteed Income Supplement and the Canada Pension Plan.

These types of broad, pan-Canadian reforms represent an essential starting point. Their success, however, will be dependent upon their design, delivery, and alignment, as well as the complementary interventions that can target more specific challenges and population groups with greater precision. One such area is financial security, where the persistent challenges faced by low- and modest-income Canadians suggest that further policy innovations are urgently needed.[2]

This proposal will focus on the issue of savings, asset accumulation, and retirement security for low- and modest-income Canadians. It will begin by reviewing the evidence regarding general and retirement savings rates, identifying gaps in savings policy architecture as well as practical barriers that savers are facing. It will then propose a targeted intervention for policy-makers, civil society leaders and other stakeholders to consider – a "Canada Saver's Credit" that builds on a model that has existed for nearly two decades in the United States.

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2 In using the terms "low-income" and "modest-income," this proposal applies the categories in the "Summary Report on Retirement Income Adequacy Research", prepared for the Department of Finance Canada by Jack Mintz (2009). They are:
Low: $0-25,000 for singles / one-parent families; or $0-40,000 for couples / two-parent families
Modest: $25,000-60,000 or $40,000-100,000
Middle: $60,000-100,000 or $100,000-167,000
High: $100,000+ or $167,000+

A persistent savings and wealth gap for modest-income Canadians

Introduction

This section examines trends in savings, as well as the multiple factors that appear to be driving them now or in the future.

A scan of recent research and evidence identifies a number of important trends:

1. A sizeable segment of low- and modest-income households across generational groups continue to face a persistent savings and asset wealth shortfall, financial exclusion, or gaps in retirement readiness.
2. Workplace pension coverage, an important determinant of financial security, has fallen since the 1970s and is generally lower among workers who are younger, lower-income, and less educated.
3. Lower- and modest-income households are much less likely to contribute to registered, tax-preferred savings accounts (RPPs, RRSPs, TFSAs).
4. A number of behavioural barriers continue to limit modest-income savers, including less access to employer pensions and lower take-up of targeted tax-preferred benefits and programs.
5. Financial incentives for savings, including matching programs, have proven effective in encouraging savings among lower-income groups.
6. Yet, there is an “upside down” distribution of financial incentives for savers, with over $45 billion in federal tax expenditures going disproportionately to householders with higher incomes.
7. While the expanded CPP will make a material difference in the retirement security of middle-income Canadians, there are opportunities to build on this important reform with targeted initiatives for “at-risk” populations on modest incomes.

8. Canada arguably lags behind other developed countries in helping lower- and modest-income households to save. Countries such as the United Kingdom, New Zealand, and the United States have taken creative, targeted steps to help low- and modest-income savers.

In addition to these macro trends, this section will also explore some of the market, policy, and behavioural factors underpinning these trends. The section will conclude with a focus on recent policy initiatives aimed at increasing savings, offering early analysis of the impacts of retirement income system (RIS) reforms such as CPP expansion and the gaps that are left to address, and highlighting some innovative new models in other countries that Canada could follow.

Trends in Canadians' savings

Over the past two decades, there has been a spirited debate about the savings rates, debt levels, and retirement preparedness of Canadians, and what governments should do in response to these issues of financial (in)security. While methodologies, data sources, and perspectives vary, a scan of recent evidence and analysis points to some alarming trends for low- and modest-income Canadian households.

Falling household savings rates, troubling levels of asset poverty

Since the early 1980s, the household savings rate in Canada fell from a peak of 20 per cent to a trough of below 1 per cent in the mid-2000s before climbing back to about 5 per cent today. Household debt levels have also spiked through this period, rising from 85 per cent of disposable income in the early 1990s to around 170 per cent today.[3] Recent surveys have suggested that more than half of Canadians have less than $10,000 in savings, and that a quarter would deplete their emergency savings in a month or sooner.[4] While these trends are linked to factors such as low interest rates and large increases in housing-related debt, they have nonetheless prompted concerns at the Bank of Canada and among economists, and calls for increased household savings.

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3 *Trading Economics* website, accessed July 3, 2018. https://tradingeconomics.com/canada/

4 Jamie Sturgeon, "More Canadians Report Less 'Rainy Day' Savings in the Bank," *Global News*, September 8, 2014. https://globalnews.ca/news/1550642/more-canadians-report-less-rainy-day-savings-in-the-bank/

An important caveat is that household savings and debt figures obscure homeownership impacts, with substantial unrealized capital gains on housing assets. Recent research has taken account of asset ownership in considering economic vulnerability and poverty, identifying assets housing as well as automobiles, bank accounts, and investment and retirement accounts. In the first national-level estimate of asset poverty for Canada, Rothwell and Robson found that, as of the most recent data in 2012, roughly one third of Canadians are asset-poor – meaning they lack savings to live for three months above the poverty threshold. Robson finds that this asset-poverty rate remains unchanged in 2016. What's more, half of all Canadians living in income poverty are also asset-poor.[5] This is troubling, as studies in Canada and abroad have suggested that asset ownership has many positive effects, allowing households to cover unexpected expenses, acting as a stabilizer in the event of temporary income shocks, and increasing levels of social and civic engagement. The OECD has also adopted asset poverty as a measure of financial vulnerability, noting that it may help policy-makers to identify those whose incomes are currently above the poverty line but may be at greater risk of falling into poverty in the future.[6]

Financial exclusion of "unbanked" Canadians

Access and use of financial services such as bank accounts and digital payments can be an important factor in financial inclusion, helping people escape poverty by securely and cost-effectively accumulating their savings, and enabling investments in things like education and businesses. World Bank survey data from 2017 suggests Canadians are among the most "banked" populations globally. Almost 100 per cent of people over the age of 15 report holding an account at a financial institution. Nearly all Canadians made or received digital payments and used a debit or credit card, with four in five using the internet to pay bills or make online purchases. Fewer, however, reported saving at a financial institution (67 per cent) than borrowing from one (82 per cent).[7]

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5 The study used Statistics Canada's Survey of Financial Security. The net worth poverty line included financial assets as well as home equity and other real estate, minus total debts. David Rothwell and Jennifer Robson, "The Prevalence and Composition of Asset Poverty in Canada: 1999, 2005 and 2012," International Journal of Social Welfare, Issue 27 (2018): 17-27.

6 See, for example, OECD, *How's Life? 2017: Measuring Well-Being* (2017).

7 The World Bank, "The Global Findex Database 2017," accessed October 29, 2018. https://globalfindex.worldbank.org/

Other analyses paint a less rosy picture. Low income advocacy group ACORN Canada suggests the number of unbanked Canadians is closer to 3 per cent overall – one million people – and cite research suggesting it is as high as 15 per cent among Indigenous peoples. In addition, they note that 13 per cent of Canadians can be described as "underbanked, with zero-balance accounts and very limited engagement with financial institutions.[8] Reflecting similar trends, a study by Bank of Canada economists of the "unbanked" in the euro area and United States reports that low-income, unemployed and poorly educated populations are most likely to be affected, and have substantially lower net wealth.[9] In addition, looking at bank accounts is only one measure of financial inclusion. Another important metric is access to workplace retirement plans, where lower- and modest-income households face significant barriers, and which we will discuss further on.

Retirement readiness gaps, generational inequities

Canadians' financial retirement readiness continues to be a subject of uncertainty and debate among policy-makers and researchers. A review by Bob Baldwin of five recent retirement income adequacy studies finds that "headline" findings differ dramatically, from 17 per cent of future retirees expected to suffer a decline in living standard to 50 per cent of such future retirees. Baldwin notes that this wide range can be attributed to differing methodologies, data sources, and assumptions, and that conclusions feed into often fractious debates on public policy reform where "analysis and political philosophy are simultaneously at play."[10]

The retirement readiness debate has also tended to focus on middle- and upper-middle-income Canadians, rather than the modest-income earner. The conventional wisdom has held that lower-income Canadians are not willing or able to save for retirement; and that, regardless, they do not need to save for retirement because they will be supported through the public pillars of CPP, OAS/GIS, and other income-tested benefits.

8 ACORN Canada, "Submission to the Finance Canada Financial Sector Review," November 15, 2016. https://www.fin.gc.ca/consultresp/pdf-ssge-sefc/ssge-sefc-01.pdf

9 Miguel Ampudia and Michael Ehrmann, "Financial Inclusion - What's it Worth?" Bank of Canada Staff Working Paper 2016-30, July 2016. https://www.bankofcanada.ca/2016/07/staff-working-paper-2016-30/

10 Bob Baldwin, "Assessing the Retirement Income Prospects of Canada's Future Elderly: A Review of Five Studies," *C.D. Howe Commentary* N. 456, September 2016.

A recent survey calls the first premise into question, finding that the desire to save is virtually unchanged for all households up to $100,000 in income.[11] Regarding the second premise, it may be true for the lowest-income Canadians but does not appear to be for those on modest incomes. Whether analysis is at the population-level, of individual cases, or of savers' perceptions, modest-income households are facing – *and perceive they will face* – a retirement income shortfall.[12]

Viewed through a generational lens, empirical analysis presented by Andrew Heisz of Statistics Canada concludes that younger workers are disadvantaged, but that there is also inequality within generational cohorts. Millennials (aged 25-34) have accumulated little net worth or savings, and are investing primarily in education while slowly entering the housing market. Among Generation Xers (aged 40-49), pension assets vary significantly by income level, educational attainment, and family type, with substantial savings among the highest income households but no pension assets for fully one quarter of households. The Boomers (aged 55-64) have an *inter*-generational advantage in accumulated wealth, but also substantial *intra*-generational inequity – with nearly one in five Boomers having no pension assets, and a particularly acute challenge for singles.[13] The inequality within generations appears to be growing. A recent study by Jennifer Robson and Andrée Loucks found that, compared to Generation Xers of the same age, Millennials were both more likely to have a pension and more likely to have no retirement savings at all.[14]

Decline in workplace savings coverage

The long-term decline in workplace pension coverage is a critical factor. The overall share of employees with a registered pension plan (RPP) – either defined

11 Bob Baldwin for CAAT Pension Plan, "Designing retirement schemes Canadians want: observations from a Modern DB Pension Plan," prepared for CPPLC Pension Forum: A National Discussion on Public Pension Issues, April 13, 2017.

12 See Alex Mazer, "Retirement Security for Modest Earners: Rethinking the Issue," *The Aspen Institute Financial Security Program blog*, June 16, 2017. https://www.aspeninstitute.org/blog-posts/retirement-security-modest-earners-rethinking-issue/

13 Andrew Heisz, "Canada's Household Balance Sheet," Presentation to the Prosper Canada Policy Research Symposium, March 9, 2018.

14 Jennifer Robson and Andrée Loucks, "Millennial Money: Financial Independence and Well-being for the Next Generation, Part 2: Research and Recommendations," Public Policy Forum, 2018. https://ppforum.ca/wp-content/uploads/2018/11/MillennialMoney-Part2-ResearchRecommendations-PPF-NOV2018-EN-1.pdf

benefit (DB) or defined contribution / hybrid (DC/H) – has fallen from over 45 per cent in 1977 to below 40 per cent by 2011. The modest decline masks a larger drop in DB coverage, partly offset by an increase in DC/H coverage. In the private sector, DB pension coverage has fallen from above 30 per cent in the late 1970s to 10 per cent in 2015.[15] Across population groups, the trendlines have seen that RPP coverage rates for women exceed those for men,[16] and that they are substantially lower among younger workers, those with only high school education, employees of small employers, and people on low incomes.[17]

For the group of modest-income Canadians approaching retirement, a recent study by Shillington highlights the gap among those with workplace savings plans and those without. He finds that only a small minority (15-20 per cent) of people retiring *without a workplace pension plan* will have saved enough. Among those aged 55 to 64 with incomes between $25,000 and $100,000, this group with no workplace pension plan represents roughly half (47 per cent) of the population. The overall median value of retirement assets for this group is just $3,000. Shillington's analysis suggests that only one in five of them will have enough savings to avoid a significant fall in income in retirement.[18] As younger workers participate less in workplace savings plans, the importance of individual savings will only increase over time.

Lower use of tax-advantaged savings vehicles

Modest-income Canadians are less likely to use tax-advantaged savings vehicles. As of the 2016 census, two in three Canadian households (65 per cent) contributed to one of the most common registered savings vehicles: a registered pension plan (RPP), registered retirement savings plan (RRSP), or

15 See Statistics Canada, "Pension Plans in Canada" for the relevant years. https://www150.statcan.gc.ca/n1/daily-quotidien/180627/dq180627e-eng.htm

16 This is in large part because women represent a higher share of workers in industries with higher coverage rates (e.g., public administration, education, health care), though, among lower-income groups, pension coverage among women is lower than it is among men. See Statistics Canada, "Longitudinal and International Study of Adults" (2012).

17 Coverage rates decline across the income spectrum, with the lowest income decile more than five times less likely to have pension coverage than the highest decile. See Marie Drolet and René Morissette, "New facts on pension coverage in Canada," *Insights on Canadian Society*, Statistics Canada, 18 December 2014.

18 Richard Shillington, "An Analysis of the Economic Circumstances of Canadian Seniors," The Broadbent Institute, February 2016. https://www.broadbentinstitute.ca/an_analysis_of_the_economic_circumstances_of_canadian_seniors

tax-free savings account (TFSA).[19] Yet, lower-income households, and those with younger major breadwinners, are significantly less likely to use one of these savings vehicles. Over 90 per cent of households with after-tax income of $100,000 or more contribute to at least one of the three savings vehicles, and a large share use multiple registered savings vehicles. By contrast, for people in households earning under $50,000, fewer than 40 per cent contributed to a tax-advantaged savings account.[20] The 2016 census data also illustrates that TFSAs have been the preferred savings account option among lower-income households and younger earners (under 35). Since the introduction of the TFSA in 2009, many lower-income people have opened a TFSA as a first tax-advantaged savings account. There have also been gradual declines in both the number of RRSP contributors and funds contributed, and an increase in pre-retirement RRSP withdrawals, with withdrawals correlated to indicators of financial hardship such as lower earnings and receipt of employment insurance income. There appeared to be little substitution to TFSAs among those who were already using RRSPs.[21]

The lower uptake of the RRSP among modest-income earners, or other trends like the increasing amount of unused RRSP contribution room since the late 2000s, likely results at least in part from the unsuitability of RRSPs for modest-income workers. Income tax deductibility yields little benefit for low-income earners. Lock-in provisions limit the liquidity of money for people on tight budgets or facing financial emergencies, and income drawn from RRSPs results in the reduction of GIS benefits in retirement.

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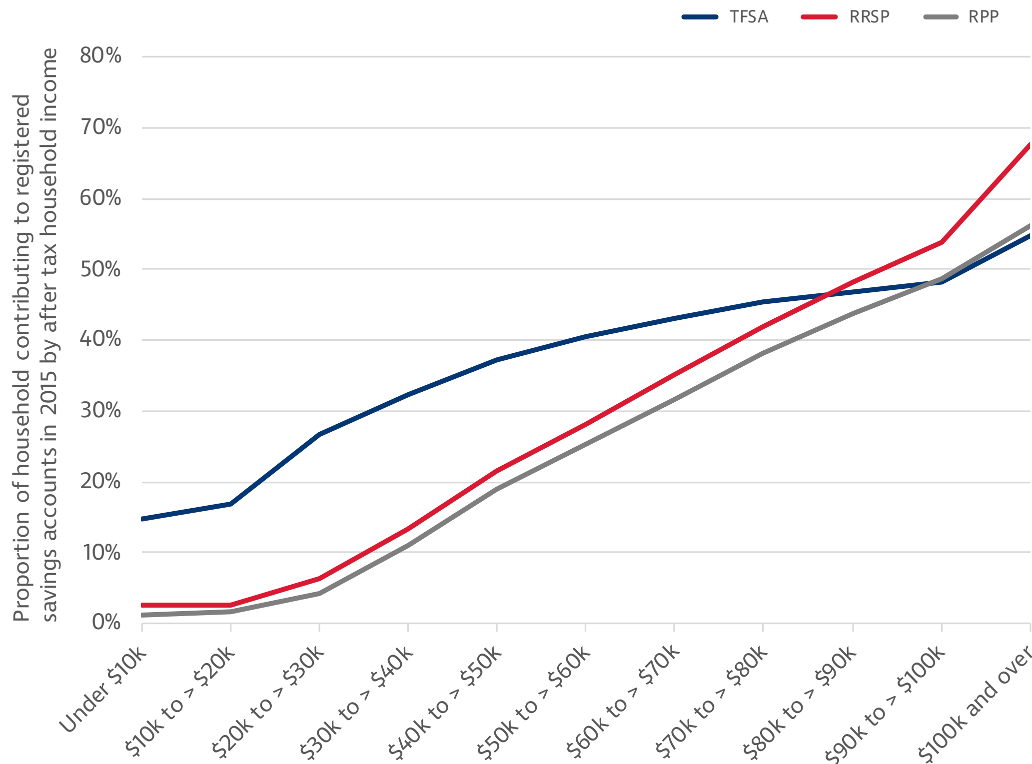
19 On average, 40 per cent of households contributed to TFSAs, 35 per cent to RRSPs, and 30 per cent to RPPs – and 9 per cent contributed to all three.

20 For households earning under $20,000, just 20 per cent use registered accounts. See Statistics Canada, "Household Contributions Rates for Selected Registered Savings Accounts," *Census in Brief*, September 2017. RRSP contribution rates are in single digits for households with income under $30,000.

21 The total increase in the number of RRSP withdrawers, however, has been modest, and often tied to use of the Home Buyers Plan. The analysis utilized data from StatsCan's Longitudinal Administrative Databank for Canadian taxfilers aged 25 to 54. See Statistics Canada, "Trends in RRSP Contributions and Pre-retirement Withdrawals, 2000 to 2013," *Economic Insights*, February 13, 2017.

Lower-income households are less likely to contribute to a registered savings account



Source: Statistics Canada, 2016 Census of Population, Statistics Canada Catalogue no. 98-400-X2016103

Key drivers of trends

Consumer financial decision-making that limits capacity to save

Many modest-income Canadians face challenges in saving and building asset wealth, often resulting from their financial circumstances. For instance, many are missing out on income-tested benefits because they do not file taxes. Many pay punitively high interest rates to payday lenders. Recent surveys have revealed that many consumers are unaware of the high costs of payday lenders, and are often using them for expected expenses such as monthly bills.[22] Others are dissuaded from saving by "right of offset" rules, under which financial firms and governments can recover money directly from a

22 Financial Consumer Agency of Canada, "Payday Loans: Market Trends," October 25, 2016. https://www.canada.ca/en/financial-consumer-agency/programs/research/payday-loans-market-trends.html

depositor's account to cover unpaid debts, whether for credit cards and loans, or student aid and child support payments.[23]

Governments, financial institutions, and civil society organizations are making efforts to address these issues, through financial literacy campaigns, payday lending regulations, or initiatives like CRA's new File My Return service aimed at low- and fixed-income Canadians that allows them to file quickly and easily over the phone.[24] But consumers could benefit from further efforts to inform, assist, and incentivize sound financial decision-making. For those on modest incomes, tax preparation time is an important moment for savings decisions, such as designating a portion of a tax refund to a savings account. In this context, tax preparation companies and non-profits that offer free tax clinics can be important influencers in enabling saving by promoting tax credits or encouraging tax filers to save their tax refund rather than spend it.

Workplace savings plans as a critical "nudge" factor

The decline in workplace pension coverage presents not only financial and equity challenges, but also behavioural ones. Studies suggest that savings rates are influenced more by access enhanced by effective saving arrangements and behavioural strategies than by income levels.[25] Savings behaviour is positively influenced by participation in a workplace savings plan, particularly where the default or "nudge" is towards participation, and contributions are automatic through payroll.[26] For low-income individuals, workplace plans can also encourage opening a savings account with a bank, where many would not feel comfortable doing so otherwise.

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23 See Government of Canada website for description of how right of offset works. https://www.canada.ca/en/financial-consumer-agency/services/banking/right-of-offset.html

24 See here: https://www.canada.ca/en/revenue-agency/campaigns/file-my-return.html

25 US Government Accountability Office (GAO), "Automatic IRAs: Lower-Earning Households Could Realize Increases in Retirement Income," GAO-13-699, August 2013. Behavioural approaches are reflected in the US "Auto IRA" proposal to automatically enroll uncovered workers in individual retirement accounts (IRAs – similar in some respects to TFSAs) which is being implemented in California, Oregon, Illinois, and other US states. For more information, see J. Mark Iwry and David John, "Pursuing Universal Retirement Security Through Automatic IRAs," Nº 2009-3, The Retirement Security Project, Brookings Institution, 2009. https://www.brookings.edu/wp-content/uploads/2016/06/07_automatic_ira_iwry.pdf

26 See, for example, Gale, Iwry, John, and Walker, *Automatic: Changing the Way America Saves* (Brookings Institution Press, 2009).

One effort to stem this decline in workplace pension coverage was the introduction of the Pooled Registered Pension Plan (PRPP). Announced by the federal government in 2012, PRPPs have only recently been made available to federally regulated employers and in some of the provinces. It is too early to tell if they will have a meaningful impact, but early indications are that uptake has been very low and other opportunities should be considered.

Matching incentives and subsidies to encourage saving

Evidence from the United States has demonstrated that matching financial incentives can significantly improve modest-income earners' uptake rates if designed and offered properly. A randomized control trial of low-income tax filers in St. Louis, supported by tax preparers, found that retirement contributions were up to seven times greater for those receiving a 50 per cent matching contribution than for the control group. The authors found that a clear and understandable matching program, an easily accessible savings vehicle, and professional guidance were all factors that increased contributions savings accounts.[27] Matching incentives or subsidies could have longer-term behavioural impacts as well, given that saving has been found to be habit forming.[28]

In Canada, the Registered Education Savings Plan (RESP) offers an interesting example. To incentivize RESP use to save for a child's post-secondary education, government offers both a low-income subsidy to kick-start family contributions into an account (Canada Learning Bond, or CLB), and an income-tested matching grant to encourage ongoing contributions (the Accelerated Canada Education Savings Grant, or A-CESG) on top of a universal matching grant (the Canada Education Savings Grant) for all families using an RESP for a child.[29] In spite of the financial incentives, low-income

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27 Esther Duflo, Jeffrey Liebman, Emmanuel Saez, William Gale, Peter Orszag, "Savings Incentives for Low- and Middle-Income Families: Evidence from a Field Experiment with H&R Block," NBER Working Paper 11680, 2005.

28 See, for example, Cazilia Loibl, David S. Kraybill and Sara Wackler Demay, "Accounting for the role of habit in regular saving," *Journal of Economic Psychology* 32.4 (August 2011): 581-592.

29 The CLB is an educational savings subsidy targeted to low-income families totaling up to $2,000 for beneficiaries under 18, with eligibility tied to Canada Child Benefit income thresholds. The CESG offers a tiered matching grant of 20, 30 or 40 per cent tied to family income thresholds, to a yearly maximum of $600.

households uptake rates remain persistently lower than those of middle- and higher-income families. As of 2016, 35 per cent of eligible low-income beneficiaries had received the CLB.[30] The SmartSAVER program, designed to increase CLB uptake and RESP use through information sharing and "nudging," is an exciting innovation in collaborative social policy launched by the Government of Canada and a coalition of financial institutions, community agencies, and foundations.[31] It should offer valuable lessons for encouraging saving in other forms as well.

Financial services as key influencers of savings behaviour

The financial services sector plays a central role in influencing savings behaviour and enabling financial inclusion. Canada's largest six banks, representing over 90 per cent of all Canadian banking assets, are critical actors. At the same time, Canada's financial services landscape includes nearly 50 small and medium-sized and foreign banks, as well as large and small insurance companies, mortgage lenders, credit unions, and a range of other players.[32] There is extensive engagement with governments around public policy issues, such as recent engagements with the Government of Canada to modernize the Bank Act, focused in areas such as improving financial security and enhancing financial consumer protection.

ACORN and others have identified a number of barriers people on low incomes and in vulnerable groups face in trying to access financial services. These include inadequate identification to open accounts; poor language, literacy or numeracy skills; lack of access to computers or digital banking channels; high fees, penalties and borrowing costs; little physical access to branches in rural or poorer communities; and the growing complexity of financial products and services, with inadequate information about them. Some have criticized financial institutions for avoiding low-income consumers, whether through benign neglect or exclusionary policies like minimum balance requirements, overdraft rules, and unnecessary holds on cheques. Yet, as

30 Employment and Social Development Canada, "2016 Canada Education Savings Program Annual Statistical Review," 2017, p.30. https://www.canada.ca/en/employment-social-development/services/student-financial-aid/education-savings/reports/statistical-review-2016.html

31 See http://www.smartsaver.org/resp-about.shtml

32 Finance Canada, "Supporting a Strong and Growing Economy: Positioning Canada's Financial Sector for the Future," A Consultation Document for the Review of the Federal Financial Sector Framework, August 26, 2016.

SmartSAVER illustrates, financial institutions, governments, and civil society organizations can partner effectively to develop solutions to help savers and improve financial security.

"Upside down" distribution of government incentives for savings

Each year, the Government of Canada spends over $45 billion on tax expenditures to encourage people to save through RPPs, RRSPs, and TFSAs.[33] At 34 per cent of all federal tax expenditures in 2015, this represents the largest category of tax expenditures, far in excess of other personal and corporate tax incentives.[34] Provincial tax expenditures off the same tax base are also substantial for RPPs and RRSPs, totaling nearly $4 billion in Ontario alone in 2017.[35] Federal and provincial governments are directing well over $50 billion in tax expenditures every year to help people save – roughly equivalent to the entire budget of the government of British Columbia.

Because Canadians in the upper income quintiles are more likely to use tax-preferred savings accounts and have greater RPP coverage, contribute larger absolute amounts to tax-advantaged vehicles, and receive more marginal tax benefit, it can be safely assumed that a disproportionate amount of these tax expenditures accrue to upper-middle and upper-income Canadians. To offer a specific example of the distributional impact, for the same RRSP contribution, an Ontarian in the highest tax bracket (with income over $220,000) would receive an RRSP deduction worth nearly 54 per cent, whereas an Ontarian in the lowest bracket (below about $42,000) would receive a deduction worth only 20 per cent.

Even for the TFSA, which has been more popular among younger and lower-income households, modest-income households have received less benefit. Introduced ten years ago, one of the stated objectives of the TFSA was

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33 Department of Finance Canada, "Report on Federal Tax Expenditures - Concepts, Estimates and Evaluations 2017," February 23, 2017. While this represents a very rudimentary estimate based on recent federal figures, Robson (2013) has undertaken a much more robust analysis to estimate public expenditures on tax-preferred savings. She and other reviewers noted that factors like benefit interactions and the behavioural impacts make estimating the true cost tricky.

34 For instance, capital gains exemptions, GST/HST credits, or small business and scientific research deductions.

35 Ontario Ministry of Finance, "Transparency in Taxation, 2017," addendum to *2017 Fall Economic Statement*, November 14, 2017.

“improved savings opportunities for low- and modest-income Canadians,”[36] with many of the program’s original advocates envisioning it primarily as a more attractive way for lower- and moderate-income earners to save without being subject to the GIS clawback.[37] A decade on, the benefits have still largely gone to higher income groups.[38]

Jennifer Robson has highlighted the regressive nature of Canada tax-preferred savings instruments, and has also suggested that policy-makers’ consideration of Canada’s welfare state programs should take account of household distributional impacts from these costly tax-preferred savings incentives.[39] A recent study by Murphy, Veall, and Wolfson estimates that the top one per cent of income earners get 15 per cent of the benefit from the RRSP tax deduction.[40] Given the magnitude of government expenditures on them and the inequitable distribution of benefits, there is a significant opportunity to better target investments to low- and modest-income Canadians as well as increasing their use of existing tax-preferred savings accounts.

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36 Government of Canada, “The Budget Plan 2008,” February 26, 2008, p. 80.

37 See, e.g., Jonathan Kesselman and Finn Poschmann, “A New Option for Retirement Savings: Tax-Prepaid Savings Plans,” *C.D. Howe Commentary* N. 149, 2001; John Stapleton and Richard Shillington, “No Strings Attached: How the Tax-Free Savings Account Can Help Lower-Income Canadians Get Ahead,” *e-Brief*, C.D. Howe Institute, 2008.

38 See Rhys Kesselman, “Who benefits most from tax-free saving? Hint: it’s not the poor, says public finance expert Rhys Kesselman,” *Maclean’s*, June 29, 2015.

39 Jennifer Robson, “Does Canada have a hidden ‘wealthfare’ system?: The policy history and household use of tax-preferred savings instruments in Canada,” Thesis submitted to the Faculty of Graduate and Postdoctoral Affairs, Carleton University, 2013.

40 Brian Murphy, Mike Veall, and Michael Wolfson, “Top-End Progressivity and Federal Tax Preferences in Canada: Estimates from Personal Income Tax Data,” Canadian Tax Journal 63.3 (2015): 661-88.

Recent public policies aimed at increasing savings

Analysis of Canadian reforms for modest-income savers

The most significant recent policy reform to increase Canadians' savings is the CPP expansion, to be phased in beginning in 2019. Early analysis suggests the CPP expansion will deliver on its broad objectives of strengthening retirement security for the middle class, but will be less beneficial for low-income earners. Milligan and Schirle concluded that CPP reform should meet its objective of substantially raising expected retirement benefits for most younger workers over the coming decades. Yet, for those on low incomes, it will require additional contributions even though existing public benefits in retirement already offer higher incomes than in pre-retirement, and extra CPP benefits could actually result in the clawback of existing income-tested benefits, such as the Guaranteed Income Supplement (GIS) that around one-third of Canadian seniors currently receive.[41] Baldwin and Shillington reach similar conclusions in examining the broader suite of retirement income system reforms, finding that they do not reflect major trends in the labour market and could result in significant tax-back rates for the lowest-income Canadians.[42]

Another recent study of Canadian retirement savings rates by Malcolm Hamilton suggests that broad trends are positive, but that targeted interventions are still needed. According to Hamilton, most Canadians actually save more than the 5 per cent household savings rate, and most will be able to comfortably retire on less than 70 per cent income replacement, a commonly-used target. Reforms to CPP/QPP are effective in their reach and should broadly support these trends. However, the reforms will be less effective in addressing hard-to-identify "at risk" savers with divergent personal

41 Kevin Milligan and Tammy Schirle, "The Pressing Question: Does CPP Expansion Help Low Earners?", *e-Brief*, C.D. Howe Institute, 2016. "Low earners" are defined as individuals below the current YMPE cap of $54,900.

42 Baldwin and Shillington find that while recent reforms to CPP, Old Age Security (OAS) age of eligibility, and GIS benefit top-ups all support the objectives of an enhanced system, they do not reflect that the workforce is older, people are working longer, and labour force growth is slowing. They estimate that tax-back rates on CPP benefit increases will approach 100 per cent for Canadians earning below $10,000, and will be be over 10 per cent for those earning about $50,000. See Bob Baldwin and Richard Shillington, "Unfinished Business: Pension Reform in Canada," *IRPP Study* N. 64, June 2017.

circumstances and priorities. Hamilton concludes that "we need better-targeted programs – programs that are better able to recognize and address our individual needs."[43]

Initiatives in other countries to help modest-income savers

The conditions in Canada are not unique, with many other countries experiencing similar trends and challenges that contribute to rising financial insecurity. People on modest incomes are not saving enough in general and for retirement. They are less likely to use private savings plans, while workplace pension coverage is in continual decline. There is generally a lack of awareness of savings opportunities, as well as market, policy, and behavioural barriers that act as a disincentive to saving. In this context, other countries have taken action, introducing innovative, targeted policies to help low- and modest-income savers and address many of the challenges identified in this section.

In 2008, the United Kingdom introduced the National Employment Savings Trust (NEST) defined-contribution pension scheme, linked to pension reforms that required employers to automatically enroll their employees in a workplace retirement plans. NEST is free for employers to use, offers auto-enrolment, simplicity and ease of use for members, and the scale that allows for more sophisticated asset management and lower cost.[44] As of 2018, workplace pension coverage had increased significantly in the UK, especially for younger savers.[45] NEST is also piloting a new "sidecar" savings model for the self-employed, a hybrid model that allows for both rainy-day and retirement savings.[46]

In 2018, the UK government also launched a "Help to Save" program. Low-income persons (based on receipt of the Universal Credit and labour force participation) can receive up to a 50 per cent match on modest savings into

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43 Malcolm Hamilton, "Do Canadians Save too Little?", *C.D. Howe Commentary* N. 428, June 2015.

44 United Kingdom Department for Work and Pensions, "Pensions Bill - Impact Assessment," December 5, 2007. See also NEST website: www.nestpensions.org.uk/schemeweb/nest/aboutnest.html.

45 UK Office for National Statistics, "Annual Survey of Hours and Earnings pension tables, UK: 2017 provisional and 2016 revised results," *Statistical Bulletin*, March 26, 2018.

46 Will Sandbrook, "Five potential benefits of the sidecar savings model," *NEST Insight*, May 21, 2018. http://www.nestinsight.org.uk/five-potential-benefits-sidecar-savings-model/.

a tax-prepaid account, very similar to TFSAs in Canada. Within a four-year window, the credit could be worth as much as GBP 1,200. The policy was designed with the idea of helping lower- and modest-income UK residents to build small nest eggs that could help them handle emergencies, improve their financial security, and reduce reliance on payday loans and other high-cost credit. As of January 2019, 80,000 "Help to Save" accounts had been opened, one year after the launch. However, this represents a fraction of the 3.5 million people eligible for the benefit. At least one stakeholder has called for reforms to the program, to simplify eligibility and make the program design more attractive to low income savers.[47]

In 2007, the New Zealand government launched KiwiSaver, a voluntary long-term savings plan. KiwiSaver includes many innovative features, including auto-enrolment of new employees with the ability to opt out, mandating employer contributions, supplementing savings with an initial grant and a tax credit, and a partial lock-in model that allows for pre-retirement withdrawals for major purchases like housing or for significant financial hardship.[48]

In the early 2000s, the United States also introduced a new retirement savings policy called the Saver's Credit that will be described in the next section.

47 See Money Advice Trust, "Help to Save scheme 'should go further'," http://www.moneyadvicetrust.org/media/news/Pages/Help-to-Save-scheme-should-go-further.aspx.

48 See KiwiSaver website: http://www.kiwisaver.govt.nz/new/about/

The Canada Saver's Credit

Introduction

This second section presents a targeted proposal to address the issues discussed in section one for the consideration of Canadian policy-makers, civil society leaders, the financial services community, and other stakeholders, building on the Saver's Credit model established in the United States. It was further inspired by evaluation and insight from south of the border on how to improve the Saver's Credit, and by a Canadian proposal that first introduced the idea of supplementing lower-income earners' savings through a government match of TFSA contributions.[49]

The US Saver's Credit

- In 2001, the United States Congress created the Saver's Credit to assist low- and modest-income people with access to retirement savings vehicles. The approach was simple and practical: apply targeted financial incentives to encourage greater use of existing retirement savings vehicles.
- The Saver's Credit was created as an income-tested non-refundable tax credit, claimed by contributors to a qualified retirement savings account (IRA, 401(k), etc) who file a tax return and have income tax liability. The credit is up to $1,000, phasing out from 50 per cent of the saver's contribution to 0 per cent at the higher modest-income levels.
- Since its introduction, the Saver's Credit has had a positive impact in improving retirement savings among its target populations. Still, evaluations have identified a number of aspects of structure and administration that could be improved.
- The US Saver's Credit offers a compelling model to consider in the Canadian context as a targeted intervention to support many of the hard-to-reach modest-income households that face persistent savings difficulties.

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49 See John Stapleton and Richard Shillington, "No Strings Attached: How the Tax Free Savings Account Can Help Lower Income Canadians Get Ahead," *e-Brief*, C.D. Howe Institute, September 30, 2008.

The Canada Saver's Credit proposal

The proposed model would help those on low and modest incomes with saving – whether for improved day-to-day financial security, to make major purchases, or to help prepare for retirement. It would take the form of an income-tested refundable tax credit, matching a portion of an individual's contributions to a TFSA account, which can be accessed as a group plan through employers and other plan sponsors, or individually.

The US Saver's Credit: an overview of the model and analysis of effectiveness

In 2001, the United States Congress created the Saver's Credit to encourage saving by low- and moderate-income taxpayers with access to retirement savings vehicles. There were many similarities to the challenges described in section one that precipitated the creation of the Saver's Credit.

In the early 2000s, US policy-makers were concerned about income adequacy in retirement for modest-income savers. As in Canada, utilization of existing tax-advantaged savings accounts in the United States is highly concentrated among higher income households. Only half of American households earning $50,000 or less have retirement accounts, with the share falling to 20 per cent of households at or below $20,000. The United States also has a regressive distribution of financial assistance for retirement savings through the tax system. In 2013, two thirds of the financial benefits from tax-preferred retirement savings accounts went to the top income quintile.[50]

The approach in designing the Saver's Credit was intended to reduce this gap and take a step to "level the playing field" with respect to saving tax incentives for lower- and modest-income households. Using existing tax and qualified retirement savings instruments, it applied targeted financial incentives to encourage greater use of these instruments by low- and modest-income populations. Therefore, as originally proposed, the US Saver's Credit was a 50

50 See William Gale, Mark Iwry, and Peter Orszag, "The Saver's Credit: Expanding Retirement Savings for Middle- and Lower-Income Americans," The Retirement Security Project Policy Brief No. 2005-2 (March 2005); Orszag, Gale, and Iwry, *Aging Gracefully* (Century Foundation Press, 2006), chapter 5, pp. 77-98; Jennifer Erin Brown and David C. John, "Improving the Saver's Credit for Low- and Moderate-Income Workers," *AARP Public Policy Institute*, Issue 132, September 2017.

per cent refundable tax credit,[51] income-tested to be available to lower- and modest-income workers, that could be claimed by contributors to a qualified retirement savings account (IRA, 401(k), 403(b), or 457) who file a tax return. The value of the credit was up to $1,000 (for single individuals, $2,000 for couples), phasing out over a range of income above the maximum dollar eligibility thresholds.[52]

However, during the legislative process leading up to the June 2001 enactment of the major tax cut legislation proposed by President George W. Bush (which included the Saver's Credit among many other tax and retirement-related provisions),[53] the proposed Saver's Credit provisions were severely truncated, reducing their cost in order to shift budgetary resources to other retirement savings proposals – notably greater increases in the maximum tax-favored contributions permitted under pension plans and individual retirement accounts – that were of higher priority to higher- and middle-income taxpayers, corporations, the financial services industry, and many members of Congress.[54]

As a result, the Saver's Credit, as enacted, was made non-refundable, and was converted from a 50 per cent credit to a three-tiered credit (10 per cent for most eligible taxpayers, 20 per cent for some others, and 50 per cent for a very few). The credit would only reduce federal income tax liability, rather than being deposited to the retirement plan account (including IRA) to which the saver had contributed. To save further revenue cost, the provision was made temporary and the income eligibility ceilings were set at $25,000 for single filers and $50,000 for married taxpayers filing jointly (lower than originally proposed).[55]

Notwithstanding its curtailment by Congress between proposal and enactment, the Saver's Credit has had a positive impact in improving retirement savings among its target populations. About 10 per cent of all US tax filers are eligible to claim the credit in a given year. Between 2006 and 2014, uptake of the

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51 Non-refundable credits reduce taxable income, whereas refundable tax credits offer a direct cash transfer, even to those without tax liability.

52 Interview with J. Mark Iwry (Jan. 21, 2019).

53 Economic Growth and Tax Relief Reconciliation Act of 2001, Public Law 107-16, section 618, adding new section 25B to the Internal Revenue Code of 1986, as amended.

54 Interview with J. Mark Iwry (Jan. 21, 2019).

55 See note 51.

credit grew from 3 to 5 per cent of these tax filers, representing nearly 8 million Americans by 2014. The average value of the credit per year also grew from $156 in 2006 to $174 in 2014.[56]

In later years, Congress amended the provision to make it permanent and make a few other limited changes: the income eligibility thresholds were indexed to inflation (in 2019, they are $32,000 and $64,000 for single and married filing jointly, respectively), and provisions were added to suspend eligibility for the credit if the saver makes certain retirement plan withdrawals corresponding to previous contributions that had given rise to the credit.[57]

Because the architects of the credit had designed a significantly more robust proposal, and had hoped for a higher utilization rate, they and US think tanks and policy-makers have continually proposed that the credit be expanded to reflect its original proposed design:

- Making it refundable in order to reach tens of millions of additional low-income households that have no tax liability and therefore cannot benefit from a non-refundable credit.
- As an alternative to straightforward refundability, providing for the credit to be deposited to the account in which the individual saved (in effect transforming the credit to a government matching contribution).
- Restoring the proposed simple, single 50 per cent credit rate (which would help avoid the three-tier structure with income eligibility cliffs that can substantially reduce benefits for an additional dollar of income).
- Increasing the income eligibility ceilings to extend the credit to millions of additional modest-income households.[58]

These are all addressable issues, and they will be reflected in the following section that provides analysis of how the basic Saver's Credit model proposed and implemented in the United States could be effectively translated into the

56 Jennifer Erin Brown and David C. John, "Improving the Saver's Credit for Low- and Moderate-Income Workers," *AARP Public Policy Institute*, Issue 132, September 2017.

57 Internal Revenue Code section 25B.

58 See William Gale, Mark Iwry, and Peter Orszag, "The Saver's Credit: Expanding Retirement Savings for Middle- and Lower-Income Americans," The Retirement Security Project Policy Brief No. 2005-2 (March 2005); Orszag, Gale, and Iwry, Aging Gracefully (Century Foundation Press, 2006), chapter 5, pp. 77-98.

Canadian context. It is important to recall, however, that the architects of the US Saver's Credit initially proposed the fully refundable model at a 50 per cent credit rate, before the design was curtailed, as described, in the 2000-2001 legislative process.

Translating the US model into a Canadian context

Despite its shortcomings as enacted, the US Saver's Credit (especially as initially conceived and proposed) offers a compelling model to consider in the Canadian context as a targeted intervention to support many low- and modest-income households that struggle to save. As illustrated in the table below, the proposed Canada Saver's Credit incorporates some of the features of the US Saver's Credit that work well, while also addressing the key shortcomings of the US version as enacted.

The Canada Saver's Credit: Building and improving upon the US experience	
Design elements of the US Saver's Credit to follow	Recommended improvements upon the US Saver's Credit design
• Target the credit at lower- and modest-income earners • Use an existing account type (TFSAs), rather than creating new vehicles • Deliver the credit through the tax system • Allow eligibility for both individual and workplace-based accounts	• Make the credit refundable (so that savers with minimal or no tax liability can receive the benefit) • Deposit the credit directly into a saver's account • Link eligibility to an existing tax credit (the GST/HST tax credit) • Smooth the phase-out of the credit to eliminate the perverse impact of "cliffs"[59] • Provide a dollar-for-dollar (or 100%) match, rather than a 50% match, to encourage greater uptake

59 Income or benefit "cliffs" describe what happens when public benefits programs phase down or out quickly, leading to an abrupt reduction or loss of benefits for families as household earnings increase. The effect on household behaviour can be similar to that of a high marginal tax rate on earnings.

Proposal architecture and design considerations

A Canada Saver's Credit would adopt core elements of the American model, but be calibrated to reflect the Canadian context, address the shortcomings of the US Saver's Credit, and borrow from other innovations at home and abroad. In summary, our proposed Canada Saver's Credit would be a simple, flexible model with the aim of helping those on low and modest incomes increase their savings – whether to improve short-term financial security, to make major purchases, or to help prepare for retirement. The basic idea underlying the Canada Saver's Credit – an income-tested matching program for TFSA contributions – is not new. In fact, it was first proposed over a decade ago by John Stapleton and Richard Shillington in a C.D. Howe Institute paper on the TFSA as a valuable instrument for low-income savers.[60]

Why TFSAs and not RRSPs?

Unlike the US Saver's Credit, which can be used for a variety of account types, the proposed Canada Saver's Credit would be applicable to contribution to TFSAs, but not to RRSPs. Before outlining the other elements of the proposed design, it is worth reviewing the rationale for this approach.

A Canada Saver's Credit that more closely mirrored the US approach might include RRSPs as eligible accounts. The RRSP has more in common with the US 401(k) model and other comparable, qualified retirement savings accounts. As a program designed for retirement, it could more directly address retirement savings issues. Further, the tax penalty for pre-retirement withdrawals from RRSPs may encourage people to apply a longer time horizon to their savings. However, the tax-deferral structure potentially offers fewer benefits for low- and modest-income savers, and the withholding tax applied on withdrawal could be a disincentive for households with tight cash flow and worries about needing emergency withdrawals. Perhaps most importantly, post-retirement withdrawals from RRSPs are likely to result in the aggressive reduction of GIS benefits, which is why many advocates

60 John Stapleton and Richard Shillington, "No Strings Attached: How the Tax-Free Savings Account Can Help Lower-Income Canadians Get Ahead," *e-Brief*, C.D. Howe Institute, 2008.

have discouraged the use of RRSPs as a savings vehicle for lower-income households.[61]

The TFSA is a general savings account. It can be used for short-term, medium-term, or long-term savings goals, including retirement. Many of the TFSA's original proponents intended it to help lower- and modest-income earners build assets without being subject to punitive GIS clawbacks of government benefits.[62] The TFSA has been more appealing to modest-income families and younger Canadians than the RRSP. Because our objective is to encourage both short- and long-term savings, the flexibility and lack of penalty on withdrawals is attractive, enabling savings for big purchases but also for financial emergencies or retirement. The TFSA offers a lot of potential for making the tax-advantaged savings system more friendly to low- and modest-income savers. On the whole, then, the TFSA is a better savings vehicle for lower- and modest-income Canadians than the RRSP, and is therefore the appropriate vehicle to which to apply a Canadian Saver's Credit.

Proposed design

The proposed design of the Canada Saver's Credit can be summarized as follows:

- The Canada Saver's Credit would be a **refundable tax credit aimed at households on low and modest incomes**. It would offer a "dollar-for-dollar" match up to 100 per cent of TFSA contributions during the calendar year to a cap of $1,000 annually (thereby increasing the TFSA account balance by up to $2,000 annually).
- **Eligibility would mirror the GST/HST credit**, with the full matching amount available to savers with family net income[63] of about $36,000

61 See, for example, John Stapleton, "Low Income Retirement Planning," *Open Policy Ontario*, 2014. https://openpolicyontario.s3.amazonaws.com/uploads/2017/04/LowIncome-GIS-booklet-Final_web.pdf

62 See, for example, Jonathan Kesselman and Finn Poschmann, "A New Option for Retirement Savings: Tax-Prepaid Savings Plans," *C.D. Howe Commentary* N. 149, 2001.

63 Reported on line 236 of the income tax return, the individual's net income plus the net income of a spouse or common law partner. The Canada Child Benefit and registered disability savings plan are not included as part of family net income for the calculation.

and a smoothed phase-out as income increases.[64] Indexation of the thresholds would see them rise in future years in line with the thresholds for the GST/HST credit.

- Like the GST/HST credit, the **CRA would administer the credit and automatically determine eligibility** through the annual tax filing process. Savers would be notified of their Saver's Credit entitlement through the annual Notice of Assessment.
- The credit would be **deposited directly into the saver's TFSA account,** with funds flowing from the Government of Canada to the financial institution or plan administrator.[65] This would discourage immediate consumption (as with some other refundable credits), while still offering the saver full liquidity and access to their funds.
- The rules governing TFSA accounts eligible for the Canada Saver's Credit would be the same as those governing all other individual and group TFSAs. This would avoid the complexity – for regulators, tax authorities, and providers – of creating a new type of TFSA, with its own rules about withdrawals and transfers, qualifying investments, and regulatory reporting.
- Any individual with a TFSA account would be eligible, though efforts would be made to encourage employers and other groups to offer workplace-based group TFSAs. Workplace plans can help improve outcomes by using payroll deduction, by enrolling members on an automatic or mandatory basis, and by generally offering lower fees than retail arrangements.
- There would be no minimum deposit and monthly contributions required to access the credit.
- The design should aim to limit negative interactions or clawbacks with other income-tested or retirement benefits (e.g., GIS, family responsibility), as well with provincial social assistance programs.

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64 For 2018, the maximum GST/HST credit is reduced by 5 per cent starting at a family net income threshold in excess of $36,429.

65 This approach could parallel the delivery model of the Registered Disability Savings Plan (RDSP), whereby Canada Disability Savings Grant and Bond payments are deposited directly into the beneficiary's account.

- **The roll-out of the new Saver's Credit** should be complemented by programs and supports to promote awareness and uptake among the target group. This could include financial literacy or education initiatives focused on the Credit, incorporation of the Credit into tax preparation or tax clinics for lower-income workers, and the use of behaviourally-informed "nudges" to help boost utilization. Government should endeavour to engage a wide range of stakeholders in these efforts, including employers, financial institutions, group plan providers, tax preparers, and the range of civil society and social services entities that support greater savings and financial security.
- Based on the design proposed above, a **simple, static estimate suggests a cost range of about $275 to $550 million**. This assumes uptake ranging from 5 per cent (the 2014 uptake rate of the US Saver's Credit) to 10 per cent (two times the US Saver's Credit rate) on an eligible population base of about 11 million (40 per cent of about 28 million tax filers, representing the bottom two income quintiles), with average credit value of 50 per cent of the maximum ($500 per year). At the high end, this estimate represents just over 1 per cent of the $45 billion in current Government of Canada tax expenditures on retirement savings. The costing and fiscal impacts of the proposal would require more detailed and dynamic modeling, subject to policy-makers' decisions about the design and structure of the credit and available fiscal capacity or offset opportunities.

What this proposal does not cover

The aim of this paper is to present evidence and analysis to demonstrate a savings challenge faced by many lower- and moderate-income Canadians, and to offer a simple and flexible solution with some level of policy design and delivery detail for the consideration of policy-makers, members of the financial services community, civil society leaders, and other interested Canadians.

Because the proposal is preliminary and high-level, there are inevitably certain topics this paper does not cover that will require further analysis by policy-makers, academics, members of the financial services community, and others. They include:

- Detailed and dynamic financial and fiscal modelling of costs, uptake of the credit, or substitution effects across savings and benefits programs.
- Mechanisms in policy design and delivery to safeguard against tax-planning and "gaming" of higher income groups to access the credit.
- Detailed implementation considerations across government departments and agencies, financial institutions, and other key stakeholders.

Summary of proposal design elements and alternative approaches

The core elements of the proposed model are summarized in the table below.

There are, however, a number of alternative approaches that could be taken in designing a Canada Saver's Credit, as policy-makers weigh factors such as program eligibility, implementation and administration, interactions and substitution effects with services and benefit programs, or costing and government fiscal capacity and offset options. For example, if policy-makers wanted to lower the cost of the program, or extend the program's eligibility to more Canadians without increasing its cost, they could consider using a 50 per cent "match" rate, the approach used in the United States and in the United Kingdom's recently introduced "Help to Save" program. These alternatives, presented simply for illustrative purposes, suggest that there are many different and dynamic potential configurations to consider.

Design parameter	Proposed approach	Alternative approaches
Vehicle	Refundable tax credit – administered by CRA	• Grant – similar to Canada Learning Bond, administered by ESDC
Eligibility	Parallels eligibility rules for the GST / HST credit (phase-out begins at about $36,000 in 2018)	• Establish unique eligibility rules (e.g., set higher phase-out thresholds)
Size of credit	Maximum of $1,000 per year	• Maximum of $1,000 one time (could be paid out over time – e.g., $250 per year over four years)
Credit or "match" rate	100%	• 50% (mirroring the US Saver's Credit and the UK's "Help to Save" program)
Degree of locking in / liquidity	No locking in – same as current TFSA, with full liquidity	• Partial locking in – similar to models in other countries like KiwiSaver or UK NEST Sidecar pilot • Full locking in – same as Registered Pension Plan • Penalty for early withdrawal • No locking in, but do not make credit available until the account has been open for a certain period of time

Design parameter	Proposed approach	Alternative approaches
Fiscal impact	Technical modeling is required, but estimated annual cost at 10% uptake of about $500 million	• Can increase or decrease program cost depending on maximum credit value, eligibility rules, and other design elements • Many potential options to fully offset cost of program (e.g., reducing RRSP contribution room)