caledon commentary

November 1998 ISBN #1-894159-24-1

The Don't-Make-Sense Welfare Rules

The policy talk is all about reducing welfare caseloads. The policy action falls well behind.

Moving off welfare is easier said than done. Many of the rules create disincentives to work. Welfare recipients face a range of barriers in trying to get off the program.

The Caledon Institute identified these barriers in research on the interaction of the welfare and tax systems [Battle and Torjman 1993a; b]. Our findings showed that welfare recipients faced a veritable 'welfare wall' in attempting to move from welfare into the paid labour market.

Welfare is an income program of last resort. Households may apply for welfare when they have no other source of income or when their needs exceed the resources available to them through employment, government benefits and private sources.

Applicants are expected to deplete most of their 'liquid' and 'fixed' assets before they are considered eligible for welfare. Liquid assets refer to cash or cash-convertible assets (e.g., bonds or monies held in a trust fund). Fixed assets include property, equipment and household effects. Each province has a complex set of rules defining the maximum amounts of liquid and fixed assets that applicants can retain and still qualify for financial assistance.

The rules with respect to cash assets are known as 'liquid asset exemption guidelines.' Households with cash or cash-convertible assets are expected to use them for personal support. The level of allowable assets typically is so low that the guidelines could be more appropriately named the 'must-be-in-dire-poverty-to-qualify' rules.

In addition to being stringent, these rules on assets can be a blunt instrument and can skew

appropriate decision-making. The following examples illustrate the problem.

Most provinces encourage – if not require – 'employable' welfare recipients to seek work. Self-employment is being promoted actively as a viable option.

The problem is that it takes money to start a business – lots of spare cash that welfare recipients simply do not have. Most can barely feed their children properly or buy them warm boots in winter, let alone invest in work tools or incorporation papers.

Neither do low-income households have access to credit through traditional banking institutions. Welfare recipients, in particular, do not rank high on banks' list of preferred clients.

Various communities have responded to this access-to-capital problem through creative initiatives such as peer lending, community loan funds or individual development accounts [Lewis 1998; Evoy 1997]. These initiatives raise capital from individual donors, companies, private foundations and credit unions. The effort that goes into organizing, financing and managing these arrangements is nothing short of monumental.

These sources have provided many prospective entrepreneurs with funds for business start-up – only to come smack up against unbending welfare rules. Loans made through these community efforts represent assets that exceed the permitted guidelines. Prospective entrepreneurs find themselves tangled in the Catch-22 welfare web.

A related problem is that some welfare authorities consider work tools and equipment as assets for personal support (most jurisdictions exempt the value of farm tools and equipment). But in selling these assets, recipients cannot return to their trade. Ironically, their need for immediate cash strips them of their primary means to leave welfare.

Provinces should ensure that both their written rules and actual practice exempt the value of loans intended for employment purposes. The exemptions also should apply to work tools and equipment.

Another concern is that provincial policies with respect to assets are virtually incomprehensible. It is impossible for any single human being to know, let alone understand, all the welfare rules on assets. Their complexity is compounded by the fact that these rules vary widely throughout the country.

There are still more rules that create problems. Welfare recipients are permitted to earn a certain amount of income per month before they start losing part of their welfare benefits. This amount is set out in regulations known as 'earnings exemption guidelines.'

Typically, the earnings exemptions are so low that they barely cover the additional costs associated with work, such as child care, clothing or transportation. Welfare recipients have argued that their work efforts should not be penalized so stringently because it is often difficult to get started or re-engaged in the labour market.

Those who try to set up businesses find the earnings exemption rules to be particularly rigid. The amount that they earn may exceed the allowable levels – but their earnings often must be invested back into the business in order to build it up. Instead, these earnings are 'taxed back' by the province in the form of lower welfare benefits. The rules discourage – sometimes outright prevent – essential business capitalization [Loewen 1998].

The other difficulty is that it takes time to get a business off the ground and make it run successfully. But welfare administrators generally are so anxious to reduce their caseloads that prospective entrepreneurs are cut off too soon.

This practice is a sure-fire recipe for failure. Many would-be business people end up back on welfare because they were not given enough time to get the enterprise off the ground. Neither do they have access to Employment Insurance (EI); the self-employed are not allowed to contribute to EI and are therefore not eligible for this program if the business fails.

Another problem is that some jurisdictions calculate the value of earned income on a gross, rather than net, basis. They do not take into account reasonable business costs before reducing welfare payments. All income is deemed available to offset living expenses even though recipients actually are spending their earned income on business-related costs.

Welfare rules need to change to allow recipients to reinvest more of their profits in the business. Earned income should be calculated on the basis of net income – i.e., income after, not before, work-related costs are deducted. And welfare recipients who try to start their own businesses should be given a reasonable grace period to allow successful start-up and continuity.

In short, welfare rules should permit greater discretion for the disregard of work-related costs in both initial application for welfare and the ongoing calculation of benefits. Provinces may want to build in peer review or second-stage screening for cases involving self-employment to ensure appropriate discretionary decisions.

At the very least, all jurisdictions – including those that have made or think they have made progressive changes – should ask welfare recipients themselves about the impact of these rules upon their lives. Provinces also should meet with groups engaged in community economic development, such as the newly-formed national Digby Network, to learn how certain welfare rules create obstacles to labour force participation and business start-up.

Provinces need to hear first-hand how welfare policies that may appear efficient on paper can have perverse effects in practice. An active ear-to-the-ground approach is required to rectify this problem.

The pace of welfare 'reform' has been moving quickly throughout the country. Before placing further expectations – or restrictions – upon 'employable' recipients, all jurisdictions should examine their own welfare systems. Provinces need to listen carefully and take concrete steps to produce the conditions for success. They can start by changing their don't-make-sense welfare rules.

Sherri Torjman

References

Battle, Ken and Sherri Torjman. (1993a). *The Welfare Wall: Reforming the Welfare and Tax Systems*. Ottawa: Caledon Institute of Social Policy, Summer.

Battle, Ken and Sherri Torjman. (1993b). *The Welfare Wall: The Interaction of the Welfare and Tax Systems.* Ottawa: Caledon Institute of Social Policy, Summer.

Evoy, Lance. (1997). *The Montreal Community Loan Association and Social Partnerships*. Ottawa: Caledon Institute of Social Policy, February.

Lewis, Mike. (1998). "Community Economic Development." Chapter for book on employment policy options. Ottawa: Caledon Institute of Social Policy, forthcoming.

Loewen, Garry. (1998). *Removing Welfare Barriers in Manitoba*. Ottawa: Caledon Institute of Social Policy, May.

National Council of Welfare. (1997). *Welfare Incomes 1996*. Ottawa: Minister of Public Works and Government Services Canada, Winter.

Torjman, Sherri. (1998). *Community-Based Poverty Reduction*. Ottawa: Caledon Institute of Social Policy, February.

Copyright © 1998 by the Caledon Institute of Social Policy.

The Caledon Institute of Social Policy publications are available from:

Renouf Publishing Company Limited
5369 Canotek Road
Ottawa, Ontario
Canada K1J 9J3
PH: (613) 745-2665
FX: (613) 745-7660

and from Renouf stores at:
71 1/2 Sparks Street, Ottawa (613) 238-8985
12 Adelaide St. West, Toronto (416) 363-3171