

**ELIMINATING POVERTY AMONG WORKING
FAMILIES: FUNDING SCENARIOS**

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INTRODUCTION

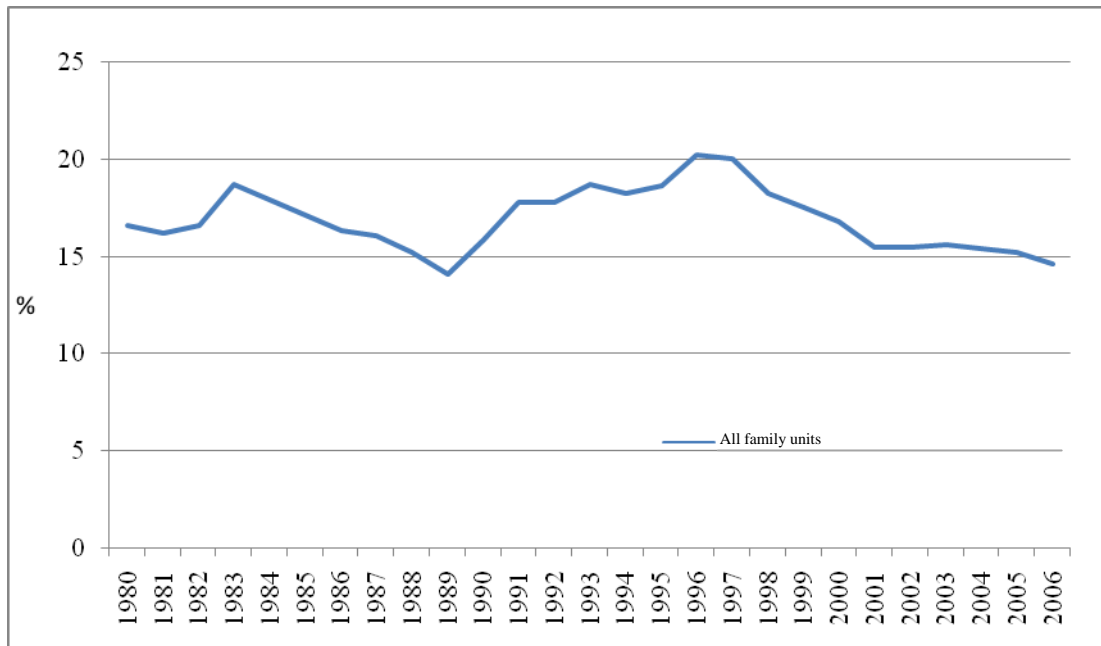
Stamping out poverty is a priority for all governments in the industrialized world, and they dedicate a significant portion of their budget resources to reaching that goal. However, despite their efforts, poverty still affects many Canadians. In fact, the poverty rate in Canada, measured using the low income cut-off (LICO),⁽¹⁾ is barely lower today than it was in 1980 (see Figure 1).

Internationally, countries like Sweden, Finland, Norway and Germany are doing better. According to the UN Human Poverty Index, Canada ranked midway among the 19 richest countries in 2007–2008.⁽²⁾ There is room for improvement, and a number of observers believe that current social and fiscal programs have reached their limits⁽³⁾ and that new solutions must be found.

This paper presents one such solution. The proposal targets a particular segment of the population – families in which at least one member works but whose incomes are below the appropriate LICO – and it examines the impact of implementing a three-year increase to the Working Income Tax Benefit to bring the income of these families up to their appropriate LICOs.

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- (1) Defining poverty and the poverty line is a matter of ongoing debate among policy-makers around the world. Many different poverty indicators are used in Canada, but none has been formally approved by the federal government. (For more information, see Chantal Collin, *Measuring Poverty: A Challenge for Canada*, PRB 08-65E, Parliamentary Information and Research Service, Library of Parliament, Ottawa, 17 October 2008.) For the purposes of this document, the poverty rate is associated with Statistics Canada's low income rate and corresponds to the percentage of families whose income is below the low income cut-off (LICO). The LICO is a statistical measurement of income thresholds below which Canadians will likely spend a larger-than-average share of their income on basic necessities, namely, food, shelter and clothing.
 - (2) United Nations, "Human Development Report 2007/2008," United Nations Development Programme, 2007, <http://hdrstats.undp.org/indicators/28.html>.
 - (3) The Collective for a Poverty-Free Québec, "Un Québec sans pauvreté: la théorie, la réalité et un chemin," http://www.pauvrete.qc.ca/article.php3?id_article=36.

Figure 1 – Low-income Families in Canada as a Percentage of the Total Number of Families, 1980–2006*



* After-tax LICOs (1992 base in 2006 constant dollars) were established by analyzing data from the 1992 Survey of Family Expenditures. Families with an income below these thresholds usually spent 63.6% or more of their income or more on food, shelter and clothing. The LICO varies according to the size of the area of residence and family size.

Source: Statistics Canada, Table 202-0804.

INCREASE TO MEET THE LOW INCOME CUT-OFF

A. The Principle

In industrialized countries, people generally maintain a reasonable standard of living through employment. However, employment does not necessarily safeguard some Canadians against poverty: their employment income is too low to pay for a household's basic needs. Some, such as seasonal workers, simply cannot work enough hours.

In February 2007, the federal government established the Working Income Tax Benefit (WITB),⁽⁴⁾ a refundable tax credit intended to provide tax relief for low-income workers

(4) The WITB is based on business and employment income earned in one year, without considering any losses claimed that year. The WITB provides a refundable tax credit equal to 20% of earned income up to \$510 for individuals and \$1,020 for families in 2008. To ensure that assistance goes to those with the greatest need, the credit is reduced by an amount equivalent to 15% of net income for individuals earning more than \$9,500 and for families earning more than \$14,500. The WITB also provides a supplement for eligible people with disabilities.

and their families. A study by Human Resources Development Canada (now Human Resources and Skills Development Canada) shows that the likelihood of re-entering poverty decreases significantly once a family has been out of poverty for three years.⁽⁵⁾ These findings indicate that temporarily increasing the WITB for three years could help low-income working families to raise their incomes to the level of their LICOs and to try in this way to break free of poverty permanently.⁽⁶⁾

B. The Numbers

According to the estimates shown in Table 1, low-income families with employment income – more than one million families – account for about half of all low-income families in Canada (working and non-working) and approximately 8% of all families across the country.

Table 1 also shows, for each type of economic family,⁽⁷⁾ the gap that must be filled so that low-income families with an employment income can reach the LICO as defined by Statistics Canada. In 2008, the average gap was approximately \$7,000.⁽⁸⁾ The total cost to bridge the gap between disposable income and the LICO is estimated to be \$7.9 billion for 2008, that is, a total of \$23.7 billion over three years until 2010–2011. This is the investment that would be needed to bring all low-income families with an employment income in 2008 out of poverty.

(5) Ross Finnie, *Low Income (Poverty) Dynamics in Canada: Entry, Exit, Spell Durations, and Total Time*, “6. The Hazard Models: Duration Effects,” Document W-00-7E, Human Resources Development Canada, June 2009, <http://www.hrsdc.gc.ca/eng/cs/sp/sdc/pkrf/publications/research/2000-000167/SP-315-02-01E.pdf>. According to this study, the probability of re-entering poverty decreases significantly as the number of years spent out of poverty increases. After three years, the re-entry rate (people who become poor again) varies between 9.3% and 14.6%, depending on the type of family. We used a hypothetical but realistic re-entry rate of 12% for our calculations for low-income families with an employment income.

(6) Similar programs exist in other countries, including the United States and England. The American model, the “U.S. Earned Income Tax Credit,” is often held up as the standard for this type of program. While it does not aim to completely eliminate the gap between a low-income family’s disposable income and the LICO, it is still the most significant poverty reduction program in the United States.

(7) “Economic family refers to a group of two or more persons who live in the same dwelling and are related to each other by blood, marriage, common-law or adoption. A couple may be of opposite or same sex. Foster children are included.” (Statistics Canada, *Standard Statistical Units – Economic Family*, <http://www.statcan.gc.ca/concepts/definitions/fam-econ-eng.htm>).

(8) Statistics Canada, 2004 data, updated and adjusted for inflation.

Table 1 – Low-income Families in Canada and the Working Income Tax Benefits Required to Raise Their Income to the Low Income Cut-off, 2008

	One adult with child(ren)	Couple with child(ren)	Single person 65 years and older	Couple 65 years and older	Single person	Childless couple	Total
Total number of EFs* (thousands)	529.20	3,216.60	1,599.80	1,762.30	3,516.60	3,689.90	14,284.40
Number of EFs with employment income (thousands)	401.80	3,059.30	143.50	742.80	2,629.10	3,321.50	10,298.00
Number of low-income EFs, after taxes and transfers (thousands)	187.20	300.60	383.70	61.10	1,266.00	321.10	2,519.60
<i>Number of low-income EFs with employment income after taxes and transfers (thousands)</i>	<i>89.50</i>	<i>218.00</i>	<i>8.30</i>	<i>10.00</i>	<i>641.20</i>	<i>187.50</i>	<i>1,154.50</i>
Low-income EFs with employment income, after taxes and transfers, as a proportion of the total number of EFs (%)	16.90	6.70	0.50	0.60	18.20	5.00	8.00
<i>Total gap between the income of low-income EFs and the LICO, after taxes and transfers (millions of \$)</i>	<i>-508.70</i>	<i>-1,723.20</i>	<i>-20.20</i>	<i>-72.8</i>	<i>-4,246.80</i>	<i>-1,415.86</i>	<i>-7,987.30</i>
Average gap between income of low-income EFs and the LICO, after taxes and transfers (\$)	-5,685.00	-7,906.00	-2,432.00	-7,528.00	-6,623.00	-7,551.00	-6,919.00

* EF = Economic family

Source: Social Policy Simulation Database and Model (SPSD/M), Statistics Canada. The SPSSD/M is a micro-simulation model used by various Canadian organizations to analyze changes to the federal tax and tax transfer system. It cannot simulate the impact of policy changes on individual behaviours. (Calculations and estimates are author's own.)

In order to increase the incomes of low-income families with employment incomes to levels that reach their respective LICOs, the reimbursable portion of the WITB must be calculated and adjusted based on the LICO for each family type. Table 2 gives an example of the calculation for a hypothetical family of four living in an urban area:

Table 2 – Sample Working Income Tax Benefit Calculation to Bring a Low-income Family’s Income Up to the Low Income Cut-off

Steps	Sample amounts
Calculate the after-tax LICO for the family type*	\$33,000
Determine the net income	\$30,000
Determine the basic deduction	\$9,111
Calculate the taxable income (Net income <i>minus</i> basic deduction)	\$20,889
Calculate the tax payable (Tax rate of 15.5%)	\$3,238
Calculate the disposable income (Net income <i>minus</i> tax payable)	\$26,762
Calculate the WITB (LICO <i>minus</i> the disposable income)	\$6,238

*Statistics Canada, 2004 data, updated and adjusted for inflation.

FUNDING THE INITIATIVE

An income supplement program such as the one outlined above can be funded in different ways, mainly through methods that rely on tax adjustments. Table 3 gives two scenarios, in strictly economic terms, for temporarily adjusting the current tax system to generate tax revenues of \$7.9 billion annually until 2010–2011, by increasing either personal income tax rates or the Goods and Services Tax (GST).

According to tax simulations, funding such an initiative would mean increasing the GST to between 7% and 8%, or significantly increasing personal income tax rates for those in the highest tax bracket.

Table 3 – Working Income Tax Benefit Funding Scenarios, 2008–2011

Scenario 1 – Increasing personal tax rates				
	Tax bracket	2008 tax rate	Suggested tax rate	Revenue generated
		%		
2008–2009	\$0–\$37,934	15.50	15.50	\$7.9 billion
	\$37,935–\$75,869	22.00	23.00	
	\$75,870–\$123,345	26.00	28.00	
	\$123,346+	29.00	36.42	
2009–2010	\$0–\$38,718	15.50	15.50	\$7.9 billion
	\$38,719–\$77,437	22.00	23.00	
	\$77,438–\$125,894	26.00	27.00	
	125,895+	29.00	36.42	
2010–2011	\$0–\$39,502	15.50	15.50	\$7.9 billion
	\$39,503–\$79,005	22.00	22.70	
	\$79,006–\$128,443	26.00	26.50	
	\$128,444+	29.00	35.50	

Scenario 2 – Increasing the Goods and Services Tax (GST)				
		Current GST	Suggested GST	Revenue generated
		%		
2008–2009		5.00	7.72	\$7.9 billion
2009–2010		5.00	7.40	\$7.9 billion
2010–2011		5.00	7.58	\$7.9 billion

Source: Social Policy Simulation Database and Model (SPSD/M), Statistics Canada. (Calculations and estimates are author's own.)

CONCLUSION

A study shows that once families break free of poverty, they are less likely to return. Therefore, a possible strategy in the fight against poverty in Canada would be to offer temporary support to families that have an employment income but remain below the low income cut-off – a measurement used to define poverty. The federal government would need to bridge the gap between the disposable income of these families and the LICO, which would involve a one-time cost of up to \$23.7 billion over three years. Various tax adjustments could absorb the cost, by increasing either personal income tax or the GST.

By helping these families emerge from poverty, and with all other things being equal, Canada could significantly reduce its poverty rate. The rate would fall from an estimated 17.6% in 2008 to 10.5% over three years, and Canada would lead the 19 richest countries listed in the UN Human Poverty Index.

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