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Canada has made important progress in reducing poverty, particularly for seniors, children and single parents. The common and critical element in each of these cases has been the introduction and maturation of income transfers tied to our federal income tax system.

However, poverty remains disturbingly widespread among Canada's Aboriginal Peoples and for persons with disabilities. Furthermore, we are now seeing increases in rates of low-income (after-tax) for working-age Canadians, particularly singles and newcomers to Canada. Poverty in Canada is, for the vast majority who experience it, thankfully transitory. Yet the numbers of "persistently" poor seem to be rising compared to just a decade earlier.

Despite progress on some aspects of low-income, income inequality has been rising. Studies find that income inequality grew during the 1990's, although the estimates of the magnitude and speed of the increase vary. Furthermore the patterns of inequality are quite different from region to region across the country. Inequality, more than absolute poverty, has been connected to a wide range of economic, social and political challenges from obesity to violent crime. On an individual level, behavioral economics tells us that people are more sensitive to their personal gains and losses relative to others than they are to the absolute dollars involved.

In other words, **poverty in Canada isn't fixed.** We haven't addressed poverty among many vulnerable groups. What's more, growing inequalities between the rich and the rest of us mean that surest pathways towards opportunity and prosperity risk becoming concentrated in the hands of fewer and fewer Canadians.

The Key Tools in the Federal Tool-Kit: Taxes and transfers

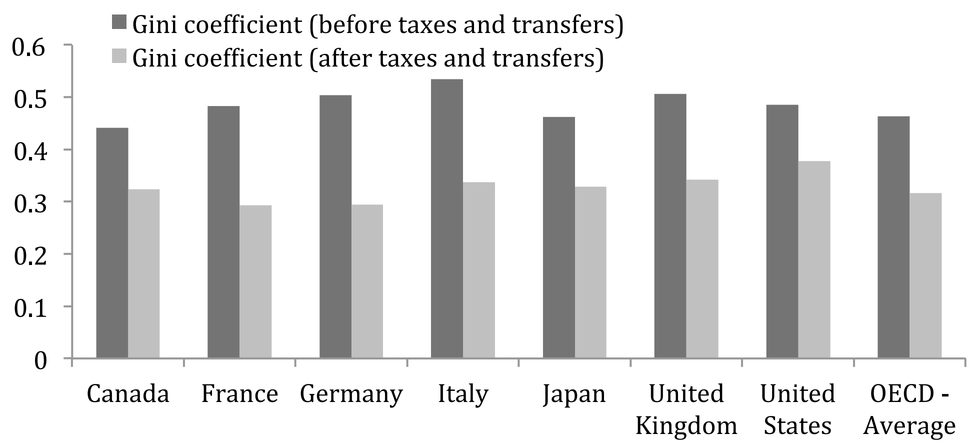
Even working full-time, Canadians make very different levels of income for a large number of sound reasons including local labour conditions, employer demand and individual skills or education. Traditionally, our income tax system and income transfers to individuals have been a way to make sure the least well-off have enough to get by and that the wealthiest are paying their fair share. These personal income tax and individual transfers have been the most critical tools in making gains on absolute poverty for many groups and on inequalities among all Canadians.

Starting in the mid-1990s, the redistributive effects from our tax and transfer system began to slow – in other words, something happened in our tax and transfer system so it became less effective in offsetting the inequalities that come from different wages in the labour market and earnings in capital markets.

As a share of all government transfers to all Canadians, the poorest 20% are getting less today than in 1989, while the middle 60% of Canadians saw their shares rise or stay the same. Although the richest 20% of Canadians also saw their shares of government transfers decline, the decline was greatest for the poor.[1]

Comparing measures of inequality of 'before tax and transfer income' to measures of inequality of 'after tax and transfer income' gives us some estimate of the impacts of the key tool in softening market inequalities for families and individuals. **By international standards, Canada now does less to reduce inequality through taxes and transfers than the OECD average and less than any G-7 country except the US.**

Fig.1: Current Gini index, income before and after taxes and transfers
(OECD.Stat)



Recommendation #1: In addition to examining the effects of tax and transfer systems on income inequality in Canada, **the Committee has an important opportunity to call attention to inequalities in wealth and the effects of certain tax measures on inequalities in the financial resources that Canadians own as well as earn.**

Quite apart from inequalities in income, wealth inequality in Canada has been rising more and faster, due in part to large increases in the net worth of the very wealthiest Canadians and in part to declines in the net worth of the poorest Canadians. Savings and assets play an important role in the well-being of individuals and households, enabling them to take productive risks and to be more resilient to financial strains. Financial well-being, for all of us, means not just the income flows we live on day-to-day, but also the pools of savings and assets that we build and use over the longer-term.

We cannot solve polarization of economic resources if we look at income alone. Low-income Canadians do have some assets and, like middle-income earners, many of

[1] Statistics Canada CANSIM Table 202-0708.

them work hard to build some modest savings. Wealthier Canadians have more assets and tend to hold their wealth in the range of preferential tax instruments (for example Registered Retirement Savings Plans) now available. Using data from the Survey of Financial Security, I estimate that half or more of the net worth of wealthier households is receiving some form of tax benefit. **At the same time that Canada's tax and transfer system has stopped doing as much to reduce inequalities in income, it may have started to accelerate inequalities in wealth.**

Our federal income tax system is more complicated than ever before. We have seen the introduction of many new deductions, non-refundable credits and refundable credits, creating a more complex and less transparent system where distributive effects by income and wealth are harder to keep track of. There are good questions to be asked about the effectiveness of a series of visible but small and largely token credits. Similarly, the annual contribution limits for RRSPs have accelerated out of all proportion to the actual contributions by average Canadians for the last decade or longer. Each credit, each increase in the value of an annual deduction, costs something to our fiscal framework.

Recommendation #2: That the Committee propose a comprehensive and public review of the federal income tax code to simplify targeted credits and deductions with a view to balancing clarity and transparency against equitable taxation, with attention to effects on household income as well as wealth.

It has been 50 years since the Government of Canada last launched such a substantial review. We were then and are now "a pragmatic and practical people," more inclined towards "the devil we know than the devil unknown"[2] and yet it is clear that the current system is cumbersome, confusing and more costly than it needs to be.

Cost-savings from eliminating loopholes was identified as an important part of the Government's plan to balance the budget. A more comprehensive review, perhaps even approaching the scale of the Carter Commission, could generate substantial reductions in tax expenditures. Such savings could be directed towards enhancements to the income transfers that have already been shown to make a difference in the economic security of vulnerable Canadians, namely the Guaranteed Income Supplement, the Canada Child Tax Benefit and the Working Income Tax Benefit.

Recommendation #3: As part of its current study, the Committee might explore avenues to make savings instruments more progressive while preserving their essential universal quality.

All Canadians who want to save and build assets should have equitable access to the federal instruments designed to make that easier. A fairer system would see, proportionally, greater public support flow to those who need more support. The exemption of Tax Free Savings Account amounts from the Guarantee Income Supplement is an important step in the right direction. In the US, policy-makers have

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[2] Duncan Gordon Blair, M.P. (Grenville-Carleton), House of Commons, June 23, 1971.

explored, for example, refundable tax-credits for small savers. The changes to the matching grants and income-tested bonds have made the Canada Education Savings Grant (for Registered Education Savings Plans) and Registered Disability Savings Plans somewhat more progressive than other tax-preferred instruments. Improving the accessibility of these instruments is another important avenue worth exploring.

Programs and services

Recommendation #4: Accelerate federal investments in financial literacy.

There is no simplification of the tax code, incentive for saving or enhancement of income transfers that can fully eliminate the need for Canadians to maintain their financial capability. As the terms of reference for this study by the Committee have made clear, Canadians want a system that enables individual opportunity. Every change in one's financial circumstance or to the private and public systems we navigate requires that we each make some decisions about our own self-interest. Without adequate access to help (including information and advice), it is far more difficult to keep track, to make ends meet, to chose products, to plan ahead or to stay informed. Canadians at the bottom end of our income distribution are better than most Canadians at budgeting and finding ways to economize. But, just as there are inequalities in our tax and transfer system, there are inequalities in the supply of personal financial help in Canada.

Budget 2013 reiterated the Government's commitment to financial literacy and announced a further increase in the annual funding for the financial education program of the Financial Consumer Agency of Canada. The FCAC has established a strong role in the development and delivery of information resources to Canadian consumers and intermediaries and as a valued partner with organizations at provincial and community levels. As a complement to its current investments in financial literacy, the federal government could do more to:

- **Foster evaluation and dissemination of good practice in financial literacy programs.**
- **Integrate relevant, personalized financial information and guidance into the front-line delivery of more federal programs**, from Canada Student Loans, to Seniors' Benefits, to Employment Insurance**.**
- **Explore, in partnership with the private and voluntary sectors, the development of a cross-country network of not-for-profit service centres for financial capability.** Informed by the network of Citizen's Advice Bureaus in the United Kingdom and the network of Financial Empowerment Centers in the United States, these local centres could provide accessible, unbiased and relevant information, guidance and assistance tailored to local needs. In the UK and US, the networks deliver a range of supports from financial problem-solving, to tax clinics, personalized financial learning and help with applications to programs and benefits. There are already several experienced providers of financial literacy programs across the country that might serve as the starting point for such a network.

Recommendation #5: Improve access and portability of non-wage benefits for more Canadians.

Inequalities in income flows and pools of wealth are happening alongside a polarization the non-wage benefits of work that improve financial security – benefits such as extended health and dental care, paid parental leave, disability insurance and retirement savings. Rates of pension coverage have declined in Canada over the past decades, though not as dramatically as many have claimed. In 2006, 32% of Canadian workers had a workplace pension, down just slightly from 37% in 1976.[3] The Pooled Registered Pension Plans were introduced by the Government as one way to try to promote pension coverage for the growing numbers of workers in more mobile fields, working multiple jobs or in self-employment. Parental EI benefits have been extended to interested self-employed Canadians. It remains to be seen whether these voluntary, opt-in mechanisms will have the desired impact.

In cooperation with provincial governments, the federal government can explore avenues to find sustainable and portable options for Canadians without workplace-related benefits. A supplemental Canada Pension Plan program might provide better access to secure retirement savings as well as a basic insurance in case of disability. Removing parental leave from the EI system could create avenues for a more flexible, portable and inclusive system that ensures that all parents have an adequate income in the first and critical year of their child's life. Finally, we need solutions for the growing numbers of Canadians without extended health or dental benefits – by one estimate, half of all workers making an average hourly wage and nearly 90% of workers making half the average hourly wage do not have any health, dental or disability insurance from their employer.[4] The same provincial programs that, in many parts of the country, have improved the well-being of low-income children and seniors or those on social assistance, could, with federal-provincial cooperation, be extended to include vulnerable workers as well.

Conclusion

The challenges of poverty and inequality in Canada are not insurmountable. Left unchecked, they pose a risk to our common prosperity and cohesion. In our favour, we have a heritage of Canadian values of fairness and progressive universalism. We already have many of the instruments and options before us. What we need now is political courage and policy creativity.

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[3] Author's calculations from CANSIM Tables 282-0002 and 280-0008.

[4] Marshall, K. (2003) "Benefits of the job", Statistics Canada, Ottawa.