



**RENEWING CANADA'S
SOCIAL ARCHITECTURE**

CHILD BENEFITS IN CANADA POLITICS VERSUS POLICY

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CONTENTS

PROBLEM STATEMENT	1
POLICY OBJECTIVE	1
CURRENT STATUS	1
DRIVERS OF CHANGE	14
RECOMMENDATIONS	17
CONCLUSION	22
REFERENCES	23

PROBLEM STATEMENT

Child benefits are social programs that can be powerful tools to combat poverty and inequality. They not only help low-income families but also the middle class. The federal and provincial/territorial governments over the years have achieved considerable progress in strengthening the architecture of child benefits in Canada.

Unfortunately, the current federal government took an about-face on child benefits when it came to power in 2006. It imposed a series of programs intended to help not only low- and middle-income families — the traditional target of child benefits — but also affluent households that do not need help from government.

POLICY OBJECTIVE

The policy objective for child benefits in our social architecture is to build a single, streamlined and progressive support with a strong poverty reduction impact and improved income security for modest- and middle-income families.

CURRENT STATUS

CORE OBJECTIVES

To properly understand the current debate over federal child benefits, we first must explain what their core purposes are. In Canada, child benefits — meaning income payments on behalf of children, delivered either in the form of cheques or income tax reductions — have historically pursued two fundamental and related purposes: poverty reduction and parental recognition.

Under the poverty reduction objective, child benefits help fill the gap between the earnings of low- and modest-wage parents and their families' income needs, based on the long-recognized reality that a market economy does not vary wages

and salaries to take into account the number of family members dependant on that income. The parental recognition objective views child benefits as an important way for society to provide some financial recompense for the fact that parents bear expenses that childless households, at the same income level, do not.

These dual objectives are interrelated. Both assume that society has an interest and obligation to help parents with their child-rearing costs. Children grow up to become workers and taxpayers and so it is in the interest of everyone — including those without children — that the value of this work is recognized and parents are supported in the child rearing work that they perform.

Old as they are, the twin aims of child benefits are as relevant today as they were when instituted decades earlier. Profound social, economic and demographic changes challenge the capacity of our social architecture to help Canadians [Mowat Centre 2015, Caledon Institute of Social Policy 2006]. Many families struggle to raise their children in a Canada of persistent poverty, stagnating incomes, precarious employment and widening inequality. Fortunately, child benefits play a crucial role in supplementing incomes for lower- and middle-income households.

Important social programs such as child benefits need to be modernized. Child benefits are a major but unappreciated element of federal income security policy. Not surprisingly, child benefits architecture has changed significantly over the years though the evolution has not been smooth and steady.

HISTORY AND EVOLUTION

Child benefits are one of this country's oldest income security programs. The personal income tax system, created as a 'temporary' measure to help finance Canada's contribution to the First World War, introduced the children's tax exemption in 1918 — the first use of the income tax at the federal level to deliver a social program. The children's tax exemption paid its benefit in the form of federal income tax savings that increased in value as taxable income increased and excluded lower-income families that did not owe income tax — the majority at a time of widespread poverty and modest average incomes. So Canada's first child benefit lined up with the parental recognition objective and made little or no contribution to poverty reduction.

Other child benefits followed, namely universal Family Allowances (1945), the refundable Child Tax Credit (1978) and the non-refundable Child Tax Credit (1988). The evolution of federal child benefits architecture over the years saw changes in design, cost and relationship among programs that are too complex to discuss here [see especially the numerous publications by the Caledon Institute of Social Policy, including Battle (2008), Battle and Mendelson (2007), Battle and Torjman (1993), Battle and Torjman (2014) and Battle, Torjman and Mendelson (2014)]. However, several trends stand out.

There has been a long-term trend towards progressive income testing of child benefits [i.e., gearing the payment amount to need (as measured by family income), so that poor families get the most and the amount of benefits declines as incomes increase]. Spending on federal child benefits rose substantially and steadily between 1997 and 2006, as Ottawa boosted the Canada Child Tax Benefit under its commitment to the federal-provincial/territorial National Child Benefit reform. By 2007, Ottawa was spending \$13.1 billion on its three core child benefit programs (Canada Child Tax Benefit, Universal Child Care Benefit and non-refundable Child Tax Credit) — \$5.6 billion or 74 per cent over its 1984 expenditure of \$7.5 billion (in constant 2007 dollars). Combined spending on the Canada Child Tax Benefit and Universal Child Care Benefit for one child under age 6, in constant 2015 dollars, climbed from \$2,575 in 1993 to \$5,681 in 2015 — a large increase of \$3,106 or more than double.

Non-poor families, on the other hand, experienced a loss in their child benefits. Since the late-1970s, the poverty reduction objective generally has been given higher priority than the parental recognition objective, with a substantial boost in child benefits to the poor and decline in payments to non-poor families. However, recent changes have begun to reverse this trend by increasing benefits for non-poor families.

INTEGRATED CHILD BENEFIT

Canadian social policy had a watershed year in 1993. It launched a major structural reform of federal child benefits that replaced Family Allowances and the refundable and non-refundable Child Tax Credits with a single, geared-to-income Child Tax Benefit. The provinces and territories joined in by reforming their welfare-embedded child benefits. Finally, Ottawa, and the provinces and territories had a sound architecture of child benefits to better tackle poverty and inequality.

The new Child Tax Benefit replaced three programs that differed in purpose, design and distributional impact:

1. Family Allowances that were roughly progressive and universal (though with an income test in the last few years that effectively ended their universality).
2. A refundable Child Tax Credit that was very progressive and geared to poor families.
3. A non-refundable Child Tax Credit (which had replaced the regressive Children's Tax Exemption during the income tax reforms of 1988), which was a quasi-universal demogrant that delivered the same federal and provincial/territorial income tax savings to all non-poor families. Because the credit was non-refundable, poor families without taxable income got nothing.

This mismatched troika of child benefits was inequitable, complicated and surely incomprehensible to most parents and probably most politicians. The combined distribution of benefits bore no logical or defensible relationship to need as measured by level of family income. Families with the same income received different amounts of benefit depending on each parent's share of family income. The core aims of child benefits — reducing poverty and helping parents with their childrearing costs — were in tension.

By contrast, the new Child Tax Benefit introduced in their place in 1993 offered several major advantages. As a non-stigmatizing, inclusive program it delivered its benefits to the large majority of Canadian families through the same vehicle. It was portable, providing a stable and assured supplement to income no matter where families lived or moved. It was progressive, meaning benefits declined as incomes rose. What you saw is what you got because benefits were not subject to income tax. The program paid the same amount to all families with the same income, regardless of the sources of that income, where they lived or their family type. [Note that the Canada Child Tax Benefit that succeeded the Child Tax Benefit in 1998 and remains the largest child benefit today has all these features].

The provinces and territories also delivered child benefits, targeted to families on welfare. This resulted in the inequitable situation where families on welfare received twice as much child benefits as the working poor. Welfare-embedded child benefits formed part of what Sherri Torjman coined the 'welfare wall' when the Caledon Institute did a project on the interaction of the tax and welfare systems for the Ontario Tax Reform Commission.

The term welfare wall refers to the fact that it might be more rational in financial terms for a poor family to get, and stay, on welfare because they receive cash benefits for spouses and children and might receive a variety of other cash and in-kind benefits, such as supplementary health, dental and drug care; subsidized housing; and access to supports for recipients with disabilities. If families left welfare and worked for low wages, they would not only forfeit welfare-provided income and services but also see their incomes reduced by income taxes and payroll taxes, and work-related expenses such as clothing, transportation and child care.

In a rare act of cooperative federalism, Ottawa and the provinces and territories launched the National Child Benefit initiative in 1998. The main engine of reform was the 1998 Canada Child Tax Benefit (CCTB), a restructured version of the 1993 Child Tax Benefit that built on the same strengths as the latter program. The CCTB had two layers: a basic benefit serving both poor and most non-poor families and the National Child Benefit Supplement (NCBS) that targeted low-income families and sat on top. [Note that when we use the term Canada Child

Tax Benefit we normally include the National Child Benefit Supplement since it is a major part of the program's architecture].

As Ottawa incrementally increased payments under the NCBS portion of the Canada Child Tax Benefit, the provinces and territories were expected to reduce their welfare-embedded child benefits by the amount of the federal increases. The provincial and territorial governments agreed to 'reinvest' the resulting savings in other programs and services for low-income families with children, such as early learning and child care services, supplementary health care, income-tested child benefits (now offered by all jurisdictions except PEI) and earnings supplements. While Quebec did not formally participate in the National Child Benefit reform, in practice it did.

The goal was to raise the federal Canada Child Tax Benefit to the point where it alone, or in combination with provincial/territorial income-tested child benefits, displaced basic welfare-embedded child benefits — estimated at about \$2,500 per child in 1998 or \$3,500 in 2015 dollars. That amount would achieve the goal of an 'integrated child benefit': All low-income families, regardless of their major source(s) of income, would receive the same amount of federal child benefits. By displacing welfare-provided child benefits, the distinction between child benefits for the working poor and the non-working poor would be eliminated.

The National Child Benefit architecture succeeded because it made both good politics and good policy — an all too rare combination. All provinces and territories endorsed the reform. Both the federal and provincial/territorial orders of government made joint structural changes to their respective child benefit systems that they could not have accomplished on their own.

Empirical evidence from government, think tank and academic research indicates that the National Child Benefit has had positive income and behavioural effects — reducing poverty, improving school test scores, decreasing aggression and maternal depression, and reducing hunger [Milligan and Stabile 2009] — as well as helping lower the welfare wall as recipients move from welfare to work [Milligan and Stabile 2006].

But social policy reform can be fragile and fleeting. Although both Progressive Conservative and Liberal governments had contributed to the long evolution of child benefits over the years, the current government wanted to put its own stamp on the system by boosting child payments for middle- and high-income voters and offering families cash instead of services for their child care. Although Ottawa did increase child benefits for low-income families, it placed greater weight on the parental recognition objective for non-poor households.

BACK TO THE FUTURE: THE UNIVERSAL CHILD CARE BENEFIT

While the federal government left the Canada Child Tax Benefit alone (except for eliminating the program's young person supplement), it reached into the past and resurrected two social policy zombies: the Universal Child Care Benefit (similar to the archaic Family Allowances) and the non-refundable Child Tax Credit (the same as its 1980s' name). These schemes delivered benefits to upper-income families and reintroduced inequities into the child benefits system.

The Universal Child Care Benefit is a classic case of social policy by stealth. Launched in 2006, the program targets children under age 6 (recently extended to age 17). Benefits are subject to federal and provincial/territorial income taxes, so most families do not end up with the full \$1,200 annual per child amount. To confuse matters, Ottawa later decided to exempt Universal Child Care Benefits from taxation in single parent households, though in two parent households, benefits remain taxable. As a result, families of different types (i.e., single parents, one-earner and two-earner couples with children) with the same income get different amounts of after-tax benefits (for most of the income range, one-earner couples and single parents end up with larger benefits than two-earner couples with the same total income). Since their tax rates differ, families with the same income also receive different amounts of after-tax payments depending on the province or territory they live and pay taxes in.

Despite its title, the Universal Child Care Benefit is not tied to use of child care; families can spend the money however they wish. Even if used for child care, the \$1,200 per year (less after taxes) buys little in the way of decent care. Because the Universal Child Care Benefit is not indexed to inflation, it loses value each year equal to the rate of inflation. The \$1,200 payment in 2006 is now worth only \$1,029 in constant 2006 dollars (a loss of \$171 or 14 per cent). A recent study by the Parliamentary Budget Officer estimated that the Universal Child Care Benefit as a share of household spending on child care declined from 47 per cent in 2007-08 to 41 per cent in 2013-14 due to non-indexation [Malanik 2015: 5].

Ottawa recently announced that the Universal Child Care Benefit maximum payment will increase in 2015 from \$1,200 to \$1,920 a year for children age 5 and younger (as it is paid monthly, from \$100 to \$160). The program will expand to pay \$720 a year (\$60 per month) for children ages 6 to 17. But the benefit remains poorly designed and those changes will not fix its weaknesses: It remains un-indexed and thus is reduced annually by erosion; taxable so is worth less than its face value; and pays an inadequate benefit if touted as a program of child care.

There is more sleight-of-hand going on. The federal government has eliminated the non-refundable Child Tax Credit (a little-known child benefit discussed next) to help pay for the enhancements to the Universal Child Care Benefit. Once we take into account the demise of the non-refundable Child Tax Credit, worth an estimated \$345 per taxpayer in 2015, things are not so rosy.

Take the example of a single-parent family with one child under age 6. Their Universal Child Care Benefit currently pays \$1,200 and will rise to \$1,920, for an increase of \$720. But this family will also lose its \$345 Child Tax Credit as part of the UCCB boost. So they will gain only \$375, not \$720, from the enhanced Universal Child Care Benefit and related loss of the non-refundable Child Tax Credit.

Unlike single parents, couples have to pay income tax on their UCCB. As an example, assume a two-parent family's lesser earning parent has a marginal tax rate of 22 per cent (for taxable income between \$43,953 and \$87,907). They would pay federal income tax of \$264 on their current UCCB, reducing it from \$1,200 to \$936. Factor in the \$345 non-refundable Child Tax Credit, and the family saw an actual advance of just \$1,281.

The enhanced Universal Child Care Benefit will be \$1,920 in gross terms. Federal income tax on this amount is \$422, lowering the after-tax benefit to \$1,498. But the non-refundable Child Tax Credit is gone, so the family's after-tax UCCB remains \$1,498 — a mere \$217 more than the current \$1,281. Meaning that instead of coming \$720 ahead under the boosted program, this family will see an actual advance of just \$217. To further complicate things, the provinces and territories also tax the Universal Child Care Benefit, which further reduces the actual value.

BACK TO THE FUTURE: THE NON-REFUNDABLE CHILD TAX CREDIT

The 2007 federal Budget continued the government's back-to-the-future changes to child benefits by announcing a "new \$2,000 child tax credit" payable on behalf of children under 18. Unlike the Family Allowances-modelled Universal Child Care Benefit, the non-refundable Child Tax Credit did not even bother getting dressed up with a new name, as it is the same program, with the same name, that operated between 1988 and 1992.

The "new \$2,000 child tax credit" was neither new nor worth \$2,000 — its maximum actual value, in federal income tax savings, was \$300 per child or the \$2,000 amount multiplied by the lowest income tax rate of 15 per cent. All non-poor families received \$300 per child, including the rich. Some lower-income families with a small tax liability (between \$1 and \$299) received a smaller

amount, while the poorest got nothing at all because they did not owe income tax. The non-refundable Child Tax Credit — which also reduced provincial and territorial income taxes — made inequality worse.

As part of their recently-announced family policy package, the federal government cancelled the non-refundable Child Tax Credit and instead will use the resulting savings of \$1.8 billion in 2015-16 to help pay for the enriched Universal Child Care Benefit.

FAMILY INCOME SPLITTING

The newest child benefit is a tax break in the form of family income splitting (named the Family Tax Cut), inspired by the pension income splitting provision launched in 2006 [Tamagno and Battle 2006].

Family income splitting is intended to correct an alleged inequity in the tax system: A family with children and one earner in a higher tax bracket can pay more income tax than a family with the same total income earned by both parents in a lower tax bracket. The one-earner family is often the traditional 1950s-style mom at home caring for the kids with dad in the workforce. The same problem can hold for two-earner couples in which one parent makes substantially less than the other.

Take, for example, the amount of income tax paid by two types of family: two-earner families and one-earner families. Each spouse in the two-earner family earns \$40,000, for a total income of \$80,000. They each pay \$6,000 in federal income tax, for a total of \$12,000. In the one-earner family, one spouse earns all the income — \$80,000 — and pays \$14,523 in income tax. The one-earner family pays \$2,523 more in federal income tax than the two-earner couple.

The reason for the tax gap between these households is that the one-earner family pays income tax at two rates: 15 per cent on taxable income up to \$43,953 and 22 per cent on taxable income between \$43,954 and \$80,000. But the two-earner family pays tax at only one rate — the lowest 15 per cent.

Family income splitting aims to reduce income taxes for one-earner families with children under age 18. Under the current version, called the Family Tax Cut and effective as of the 2014 tax year, family income splitting will shift taxable income up to a limit of \$50,000 from the spouse in a higher tax bracket to the spouse in a lower bracket (who traditionally is not in the labour force or works part time). So the higher-income earning spouse pays less tax while the lower-income spouse pays more tax (for eligible families, income tax will be less).

The amount of income tax savings is calculated as the product of the amount shifted between spouses and the difference between their two marginal tax rates. Tax savings from splitting will arise only if the spouses' taxable incomes are in a

different tax bracket. The Family Tax Cut will “allow the higher-income spouse to, in effect, transfer up to \$50,000 of taxable income to a spouse in a lower income tax bracket for federal tax purposes, up to a maximum benefit of \$2,000” [Department of Finance Canada 2014].

Family income splitting has been criticized by experts and commentators. Here are some key criticisms:

COMPLEX

The family income splitting scheme is the most complicated child benefit program. Economist Jonathan Rhys Kesselman, who wrote a trenchant critique of family income splitting, noted that the use of a non-refundable credit “adds considerable complexity to the operation of the provision (taking four pages to explain in the Notice to Amend the Income Tax Act)” [Kesselman 2014: 2]. The Department of Finance made a valiant but likely futile attempt to explain family income splitting to ordinary Canadians:

Pat and Chris are a two-earner couple with two children. Pat earns \$60,000 of taxable income and Chris earns \$12,000, for a combined taxable income of \$72,000.

Pat faces a marginal federal tax rate of 22 per cent. Chris is in the first tax bracket, where income is taxed at 15 per cent. Since the value of his non-refundable tax credits is greater than the tax on taxable income, Chris does not pay federal tax.

For federal tax purposes, under the proposed Family Tax Cut, Pat would be able to, in effect, transfer \$24,000 of taxable income to Chris. This would bring their taxable incomes for the purposes of calculating the credit to \$36,000 each, which puts both of them in the 15 per cent tax bracket. In addition, Chris would be able to use up his unused non-refundable tax credits with the notional transfer of income. As one person in the couple may claim the Family Tax Cut, they decide that Pat would do so. The Family Tax Cut would reduce Pat’s tax payable by about \$1,260 in 2014, taking into account both the reduced tax on their taxable incomes, and the additional value of the non-refundable credits that Chris is able to use [Department of Finance Canada 2014].

ONE-INCOME VERSUS TWO-INCOME FAMILIES

Proponents of income splitting contend that families with similar total income should pay similar amounts of tax, according to the principle that equals should be taxed equally.

Analysis supports the argument that many one-income families with children pay more income tax than two-income families with children. The average tax burden of families with children is higher when most of their income comes from one spouse. Comparing families in which the lower-income parent earns less than 15 per cent of income with families where the lesser earner makes more than 35 per cent of family income, the tax burden on one-earner couples is heavier between family incomes of \$50,000 and \$80,000 by \$500-\$1,500. The same holds for incomes above \$100,000 [Laurin and Kesselman 2013: 3].

Critics of family income splitting argue that concentrating on cash income leads to a narrow view of income [Laurin and Kesselman 2013: 2]. A broader conceptualization of families' total economic resources is required that takes into account the value of in-kind home-produced services (e.g., housework, cooking and child care). Such home-produced services are generally worth more if one spouse spends less time, or no time, in the paid labour force. For their part, two-earner families face work-related costs such as transportation, clothing and purchased child care. So the actual income gap between one- and two-earner families with children is much smaller, if at all, once in-kind services and work-related expenses are taken into account.

Fans of family income splitting contend that it will help parents spend more time caring for their children in the home. This argument fails to acknowledge that income splitting favours upper-income one-earner families that are already most able to reduce one parent's paid work, and helps least those lower- and modest-income couples with less ability to do so [Laurin and Kesselman 2013: 16]. Moreover, income splitting does nothing at all for single parents.

Another criticism of the Family Tax Cut is that it includes children up to age 17 — the age of eligibility for child benefits such as the Canada Child Tax Benefit. Families most need assistance in caring for their children at home when they are infants or preschoolers. But Ottawa's income splitting plan will extend throughout the school years [Laurin and Kesselman 2013: 16].

A TIGHTLY TARGETED PROGRAM

Family income splitting is a tightly targeted program. It will reach only 13 per cent of all Canadian households or 1.7 million families [Kesselman 2014: 30]. It is intended to favour one-income couples with children and two-income families in which one parent has significantly more income than the other parent. The Family Tax Cut will be expensive — a hefty \$1.9 billion in 2015-16.

The family income splitting measure will pay nothing to single adults (who make up a large 46 per cent of households), single parents (6 per cent of households), childless couples (31 per cent) and couples with children and low incomes (5 per cent) that are below the taxpaying threshold. The scheme will

exclude low- and modest-income families where neither parent earns more than the bottom tax bracket (\$44,793 in 2015), or if both spouses have earnings that place them in the same tax bracket.

WHO GAINS FROM FAMILY INCOME SPLITTING?

Income splitting targets two-parent single-earner families with children. This is a small group as only 22 per cent of women with school-age children and 34 per cent with preschoolers are not in the paid labour force [Jackson 2014].

Family income splitting is a regressive and elitist program, favouring high-income one-earner couples who need government assistance least. The higher their income, the more likely they are to receive the Family Tax Cut and the larger their benefit will be.

A recent study from the Parliamentary Budget Officer found that the family income splitting program will distribute most of its benefits to medium- and upper-income households [Scholz and Shaw 2015: 3]. The Family Tax Cut is supposed to support parents who choose to stay out of the workforce and care for young children, but the scheme favours high-income families whose incomes already allow for this choice [McInturff and Macdonald 2015: 26-27].

FIGURE 1: AVERAGE INCOME SAVINGS FROM INCOME SPLITTING, BY FAMILY INCOME AND PERCENTAGE OF INCOME EARNED BY LOWER-INCOME PARENT, 2015

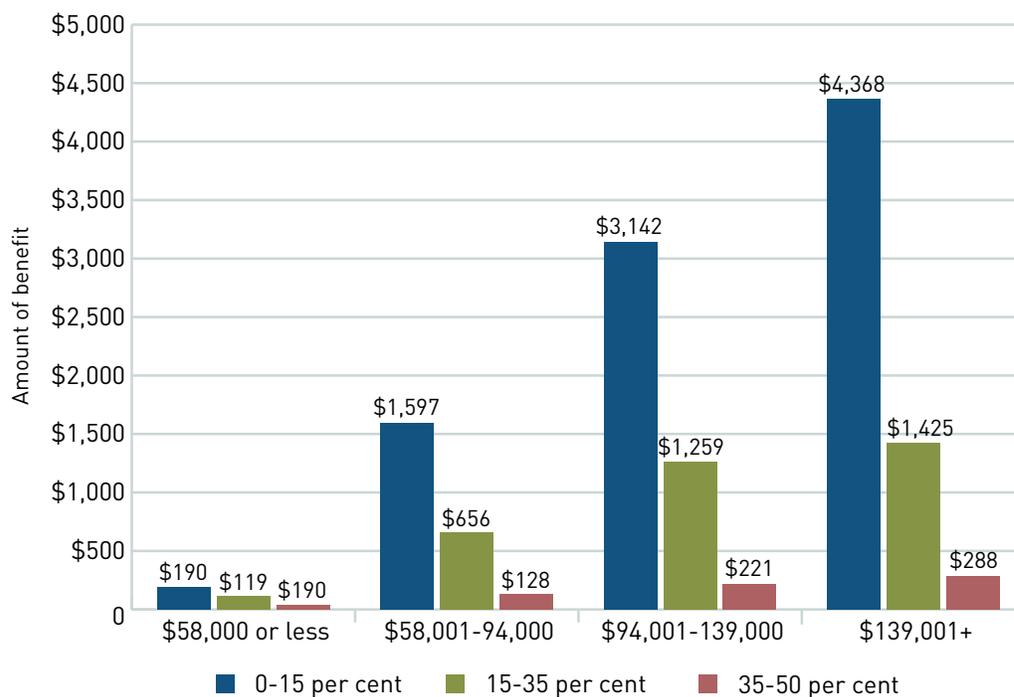


Figure 1 shows average federal tax savings from income splitting for three types of families according to the lesser earning spouse's share of family income: 0-15 per cent (shown in blue bars), 15-35 per cent (green bars) and 35-50 per cent (red bars). Average federal income tax savings for families in which the lower-income spouse earns less than 15 per cent of family income range from \$190 for families with incomes of \$58,000 or less to \$1,597 for families between \$58,001 and \$94,000, \$3,142 for those between \$94,001 and \$139,000, and \$4,368 for families with incomes of \$139,001 or more [Kesselman 2014: 31]. While the numbers are smaller for the other sets of bars (the 15-35 per cent green and 35-50 per cent red), the regressive pattern is the same for all.

In short, the greatest tax savings from income splitting arise for one-earner couples, particularly at the highest levels for the working parents [Kesselman 2014: 4]. Dividing families into three groups according to the lower-income parent's share of family income, average federal tax savings are \$1,771 for those in the 0-15 per cent group, \$929 for those in the 15-35 per cent groups and \$192 for those in the 35-50 per cent group [Kesselman 2014: 31].

The Canadian Centre for Policy Alternatives underscored a key failing of family income splitting:

The federal government's income splitting policy is intended to support parents who choose to stay out of the work force and care for young children. However, the benefits of income splitting are highly concentrated among high-income families — whose incomes already allow for this choice. The small or non-existent benefit to low and middle income families and single parents mean that the families whose choices are most constrained will not see a benefit sufficient to allow them to forgo further hours of earned income in order to spend more time with young children [McInturff and Macdonald 2015: 26-27].

The Family Tax Cut is projected to cost a hefty \$1.9 billion in 2015-16. Expenditures could be even larger over time to the extent that family income splitting affects work incentives. Income splitting can raise the 'marginal effective tax rate' (i.e., the rate of tax increases and decreases in income-tested programs for every dollar of earnings) on the lower-earning parent:

Income splitting would induce some married spouses — mostly women — to reduce their hours of work, others to withdraw from the labour force, and still others to choose not to re-enter the labour force after withdrawing to mind infants or young children. All of these responses would reduce that spouse's taxable earnings and taxes paid [Laurin and Kesselman 2013: 13-14].

SUMMARY: CURRENT CHILD BENEFITS

With the federal government’s various changes, the child benefits system has become complicated all over again. Here are the three core benefits that we have discussed, shown in Table 1. Cost estimates are for fiscal year 2016-17.

The biggest program is the Canada Child Tax Benefit (CCTB/NCBS), which will cost an estimated \$10.7 billion. The maximum payment for one child is \$3,750, payable to families with net incomes of \$26,021 or less. The program is progressive, paying the largest amount to low-income families and the least to upper-income families. Once net family income reaches \$118,251, eligibility for benefits ends. Benefits go to families with children under age 18.

The Universal Child Care Benefit (UCCB) will cost a net (after-federal tax) \$7.0 billion. The maximum benefit is \$1,920 for each child age 5 and under, and \$720 for every child 6 to 17. The program pays a flat rate benefit to all recipients, but is roughly progressive because it is taxable (except for single parents, who pay no income tax on their benefits).

Family income splitting (a.k.a., the Family Tax Cut) costs \$1.9 billion. It will allow eligible families up to \$2,000 in tax relief and is regressive, giving the most to families who already have the most.

The total price tag for the three programs is \$19.6 billion.

TABLE 1: FEDERAL CHILD BENEFITS

PROGRAM	COST (\$ BILLION) 2016-2017	MAXIMUM PAYMENT	AGE OF CHILD	DISTRIBUTION OF BENEFITS
CCTB	\$10.7	\$3,750	Under 18	Progressive
UCCB	\$7.0	\$1,920 \$720	5 and under 6-17	Roughly Progressive
Income Splitting	\$1.9	\$2,000	Under 18	Regressive
Total	\$19.6			

DRIVERS OF CHANGE

The evolution of child benefits in Canada has been driven by two opposing forces: policy and politics.

POLICY DRIVES REFORM

Over time the vision of an ‘integrated child benefit’ has driven reform. An integrated child benefit has the following key elements:

- single large program, replacing multiple benefits that conflict in design and impact
- progressive income testing, gearing the amount of benefits to need as measured by family income. Low-income families get the most and payments decline as incomes increase
- pays the same amount to all families with the same income, regardless of the sources of that income, where they live or what their family type
- benefits are not taxed, so what you see is what you get
- portable and indexed, providing a stable and assured supplement to income no matter where families live or move
- transparent, understandable and non-stigmatizing
- can piggyback other child-related benefits, such as the Child Disability Benefit and the Canada Learning Bond
- includes provincial/territorial as well as federal programs
- seeks to strengthen both anti-poverty and parental recognition core aims of child benefits system.

The National Child Benefit reform succeeded because it was founded on sound income security architecture that gained the support and buy-in of both orders of government.

POLITICS DRIVES REFORM

While Ottawa and the provincial/territorial governments made progress over the years in building an integrated child benefit, the arrival of the current government in 2006 changed all that. Social programs now had to play their part in the government's benefits-for-the-middle class (and upper class) political imperative.

The federal government was determined to put its stamp on child benefits, and looked to the past for inspiration. We have already discussed their various changes to child benefits aimed at winning middle class votes. Their most recent child benefit, family income splitting, is intended to appeal to the (shrinking) demographic of well-off one-earner families. The expansion of the Universal Child Care Benefit and introduction of family income splitting are products of a majority government, which didn't have to worry about any real political opposition.

The federal government has expended a lot of energy and effort into advertising its happy-family offerings. One TV ad, "Helping Families Prosper", depicts a smiling couple on a stroll with two children (girl and boy) and a baby plus the family dog.

The recent changes to child benefits are being timed for maximum political effect. The family income splitting scheme is now in place for its inaugural 2014 taxation year — ensuring that it will be within voters' memory during the October 2015 federal election. Families will receive their Universal Child Care Benefit increases in July 2015 with payments retroactive to January.

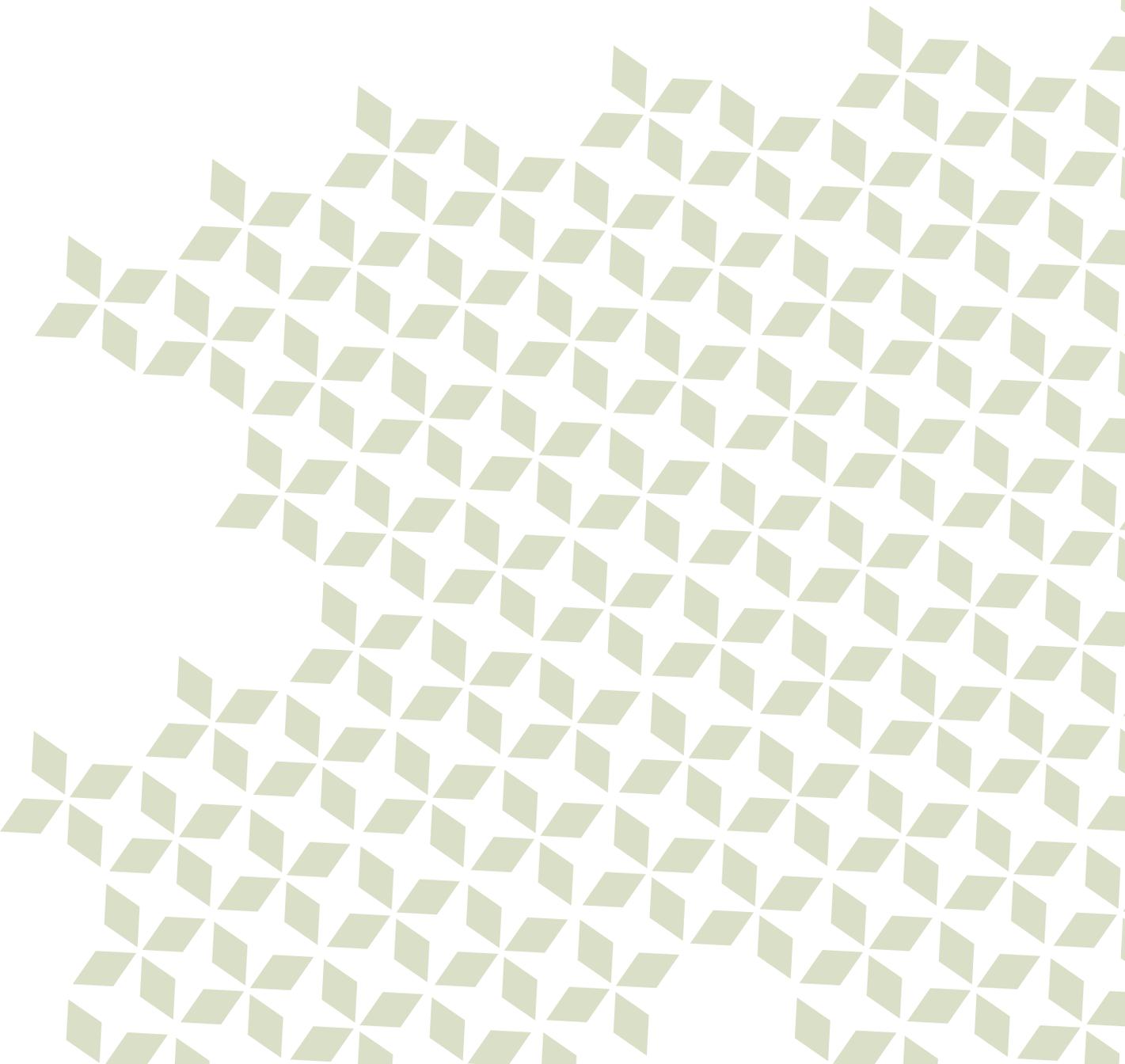
Some of the government's politically-motivated changes to child benefits are head-scratchers. The Universal Child Care Benefit is not indexed, so it loses value every year. Exempting single parents from paying income tax on their Universal Child Care Benefit is unfair to couples whose benefit is taxed. Presumably, the government's reason for this unfair move is to favour single parents, another demographic they might want to appeal to.

The government's changes to child benefits do seek to strengthen the important parental recognition aim. The enhanced Universal Child Care Benefit, the (soon-to-end) non-refundable Child Tax Credit and the advent of family income splitting all serve non-poor families and bolster the parental recognition purpose of child benefits. Boosting the Canada Child Tax Benefit also can beef up the parental recognition aim and improve financial support for non-poor families without the failings of those other schemes.

GOOD NEWS

We have been critical of the Universal Child Care Benefit because of its many design flaws. However, the recent increases in UCCB benefits, when added to the Canada Child Tax Benefit, achieve a social policy milestone — maximum child benefits should be set at the cost of raising a child in a low-income family, which is an estimated \$5,700 in 2015.

The maximum Canada Child Tax Benefit (\$3,750 for a first child) plus the Universal Child Care Benefit (\$1,920 for a child age 5 and under) together amount to \$5,670 for children 5 and under and \$4,470 for children 6 to 17, so Canada will reach the integrated child benefit target of \$5,700 in 2015 for younger children. However, the Universal Child Care Benefit is not the best way to achieve the \$5,700 target. The best way is by investing in the superior Canada Child Tax Benefit.



RECOMMENDATIONS

Canada should put its child benefits system back on the path of progressive reform through the architecture of an integrated child benefit. The federal government should dismantle the current hodgepodge of child benefits in favour of one big program in the form of an enhanced Canada Child Tax Benefit.

The challenge is to improve the Canada Child Tax Benefit for middle-income families, while also increasing benefits for low-income households. This approach would strengthen both the poverty reduction and parental recognition aim of the child benefits system.

An integrated child benefit should set its maximum payment at the cost of raising a child in a low-income family. That amount is an estimated maximum \$5,700, so we have reached it already for young children (the UCCB and CCTB together are \$5,670). Further increases to the Canada Child Tax Benefit are needed (above the current \$3,750) to bring us to the target \$5,700 since we strongly recommend a single program – the Canada Child Tax Benefit. This increase is \$1,950 (\$5,700 minus \$3,750).

The \$5,700 target was decided many years ago, at the Caledon Institute, so it would be prudent to update it, based on the cost of raising a child in a low-income family. Note that a \$5,700 maximum amount should not be set in stone or that might preclude further improvements in benefits. One suggestion would be to adjust the maximum benefit annually by inflation plus 1 percentage point.

To improve benefits for modest- and middle-income families, we would increase the base benefit (which goes to the large majority of families) rather than the National Child Benefit Supplement (targeted to those with low income). Despite the necessary emphasis on child benefits as a stronger poverty reduction instrument, their parental recognition performance also is important and must be enhanced for families with modest and middle incomes.

Table 2 compares Caledon's integrated child benefit proposal with the current system according to their major characteristics. The contrast between the two approaches is clear.

One of the more objectionable features of the government's approach to child benefits is its complex and opaque nature. Politics trumps policy. A strengthened Canada Child Tax Benefit would put policy ahead of politics and explain its workings clearly to families, social groups, researchers and the media. Public education should replace vacuous advertising.

Canadians need to see alternatives to current child benefits. Such options should come from the opposition parties as well as NGOs, think tanks and universities. Ideally, the federal finance department would undertake costed analyses of various options, including those from the non-governmental sector. But that is not going to happen. Perhaps the Library of Parliament or the Parliamentary Budget Officer could do the job. The opposition parties could usefully make public their child benefit options.

A PROMISING POLICY OPTION

In May 2015, the Liberal Party released a comprehensive reform of child benefits as part of its policy platform for the next election. The Canada Child Benefit, as it is called, would replace the existing programs — the Universal Child Care Benefit, the Family Tax Cut, the Canada Child Tax Benefit and the National Child Benefit Supplement.

The proposed Canada Child Benefit is effectively an option for the boosted Canada Child Tax Benefit that Caledon has been advocating for years — an integrated child benefit.

The structure of the proposed Canada Child Benefit is based on the current Canada Child Tax Benefit/National Child Benefit Supplement. It is family income tested and delivers its payments in a progressive fashion, with decreasing benefits as incomes rise. Benefits are tax-free and vary according to two age groups — children 5 and under, children 6-17. The new program will be indexed, like the Canada Child Tax Benefit that is its inspiration.

Maximum benefits under the new Canada Child Benefit are \$6,400 per year for each child 5 and under and will extend to net family income of \$30,000, then decline slowly as incomes increase to end at \$195,000. For children 6-17, maximum payments are \$5,400 per child up to family income of \$30,000 and then decrease as family income rises, ending at \$160,000.

It is noteworthy that the maximum proposed Canada Child Benefit — \$6,400 for children 5 and under — is \$700 more than the \$5,700 target. The maximum amount for children 6 to 17 is \$5,400 or just \$300 below the target.

TABLE 3: CURRENT CHILD BENEFITS SYSTEM VERSUS CALEDON REFORM

CHARACTERISTIC	CURRENT SYSTEM	CALEDON PROPOSAL
SIMPLE OR COMPLEX	<ul style="list-style-type: none"> ↪ Complex ↪ Three programs (UCCB, income splitting, CCTB) with different designs 	<ul style="list-style-type: none"> ↪ Sole program (boosted CCTB) ↪ Easy to understand its income-tested delivery
TRANSPARENT OR STEALTHY	<ul style="list-style-type: none"> ↪ What you get is not what you keep: most families must repay in income taxes part of their UCCB to federal, provincial and territorial governments ↪ UCCB for single parents not taxed ↪ UCCB not indexed ↪ Income splitting is complex ↪ CCTB not taxed, is indexed 	<ul style="list-style-type: none"> ↪ Families keep what they get: <ul style="list-style-type: none"> ↪ CCTB not taxed ↪ Only one program ↪ Indexed
DISTRIBUTION OF BENEFITS	<ul style="list-style-type: none"> ↪ UCCB is roughly progressive ↪ Income splitting is regressive ↪ CCTB is progressive 	<ul style="list-style-type: none"> ↪ Progressive
TREATMENT OF FAMILY TYPES	<ul style="list-style-type: none"> ↪ UCCB favours single parents and one-earner couples over two-earner couples ↪ Income splitting targets one-income couples ↪ CCTB treats all types the same 	<ul style="list-style-type: none"> ↪ Treats all family types the same
COVERAGE	<ul style="list-style-type: none"> ↪ UCCB covers all families ↪ Income splitting helps minority of well-off one-earner families 	<ul style="list-style-type: none"> ↪ Covers all but high-income families

Figure 2 illustrates the distribution of child benefits under the current system and the proposed Canada Child Benefit. The current system is made up of the Canada Child Tax Benefit, the National Child Benefit Supplement and the Universal Child Care Benefit. The current system begins at a maximum benefit of \$5,670 and declines to \$1,363 at \$137,000 of net family income, after

which it remains at that level. The proposed Canada Child Benefit begins with a maximum benefit of \$6,400 and decreases as family income increases until it reaches zero at \$195,000 of net family income.

The Canada Child Benefit pays more than the current system for families with net income as high as \$150,000, then disappears by the time net family income reaches \$195,000. The current system is not as progressive as the Canada Child Benefit, since the former becomes a flat-rate payment after \$150,000 and the latter ends at \$195,000.

The space between the blue and red lines, on the left side of the graph, indicates the gains under the Canada Child Benefit. Low-, moderate and middle-income families would come out significantly ahead.

Table 3 compares child benefits for one child under the current system and the proposed Canada Child Benefit. The table looks at several income levels.

FIGURE 2: CANADA CHILD BENEFIT AND CURRENT CHILD BENEFIT SYSTEM, ONE CHILD UNDER AGE 6, 2015

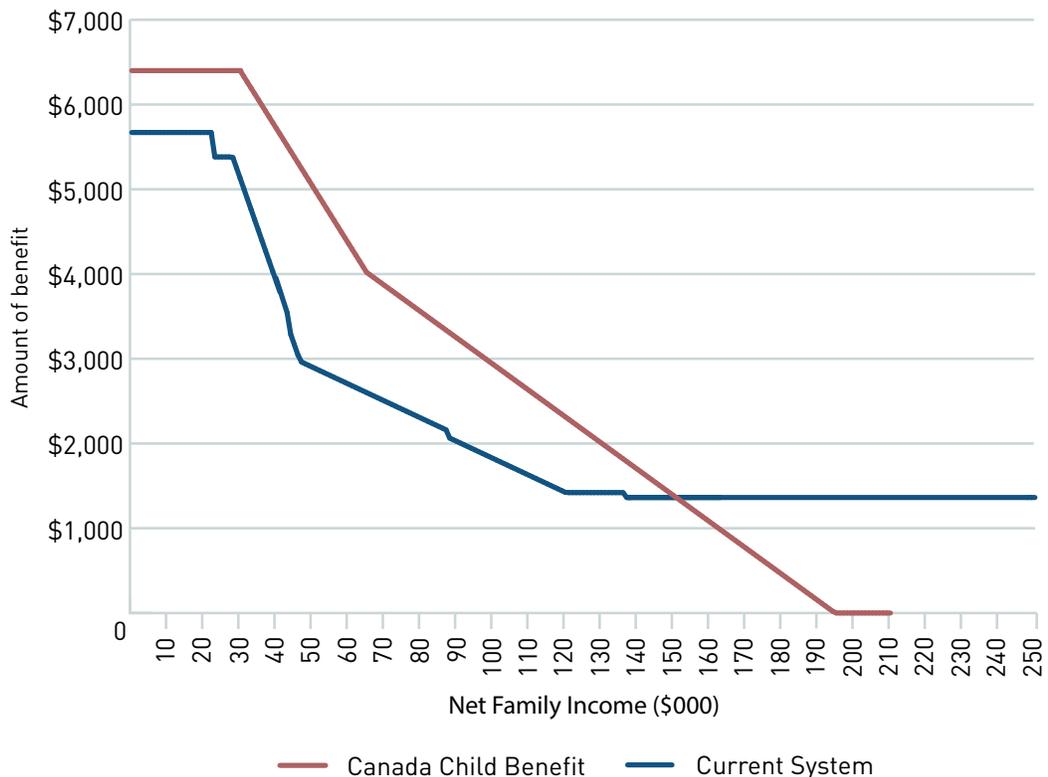


TABLE 3: CHILD BENEFITS, ONE CHILD, BY FAMILY INCOME, CURRENT SYSTEM AND PROPOSED CANADA CHILD BENEFIT

FAMILY INCOME	CURRENT SYSTEM	CANADA CHILD BENEFIT	\$ INCREASE
\$15,000	\$5,825	\$6,400	\$575
\$45,000	\$3,350	\$5,380	\$2,030
\$90,000	\$2,125	\$3,245	\$1,120
\$140,000	\$1,500	\$1,695	\$195
\$200,000	\$1,425	\$0	\$0

A low-income family with household income of \$15,000 currently gets \$5,825 in child benefits. It would receive \$6,400 from the Canada Child Benefit, for a not insignificant increase of \$575. A modest-income family with income of \$45,000 receives \$3,350 now but would get \$5,380 under the Canada Child Benefit — a sizeable gain of \$2,030. While a middle-income family with income of \$90,000 gets \$2,125 now, it would get \$3,245 under the Canada Child Benefit, or \$1,120 more. An upper-middle family with income of \$140,000 gets \$1,500 from the current system but would get \$1,695 from the Canada Child Benefit — a small increase of \$195. A high-income family with \$200,000 currently receives \$1,425 but would get nothing from the Canada Child Benefit.

CONCLUSION

Few Canadian families likely have a clear idea what they actually get from current child benefits and how these various programs operate. The names of the multiple benefits and their accompanying acronyms make for a confusing jumble. Confusion reigns — and perhaps not by accident: Social policy by stealth is alive and well in Ottawa.

An astonishing omission from the current debate over child benefits is the Canada Child Tax Benefit, which was rarely mentioned — with the exception of one journalist who said Child Tax Benefit when he meant Universal Child Care Benefit.

The Canada Child Tax Benefit displays superior social architecture — powerful, poverty-fighting, progressive, fair, inclusive, indexed, non-stigmatizing, transparent and efficient. The Liberals' recently proposed Canada Child Benefit builds firmly on the architecture of the Canada Child Tax Benefit. The Canada Child Benefit stands to be a major step forward in the history of child benefits in Canada — hopefully one that will prevail.

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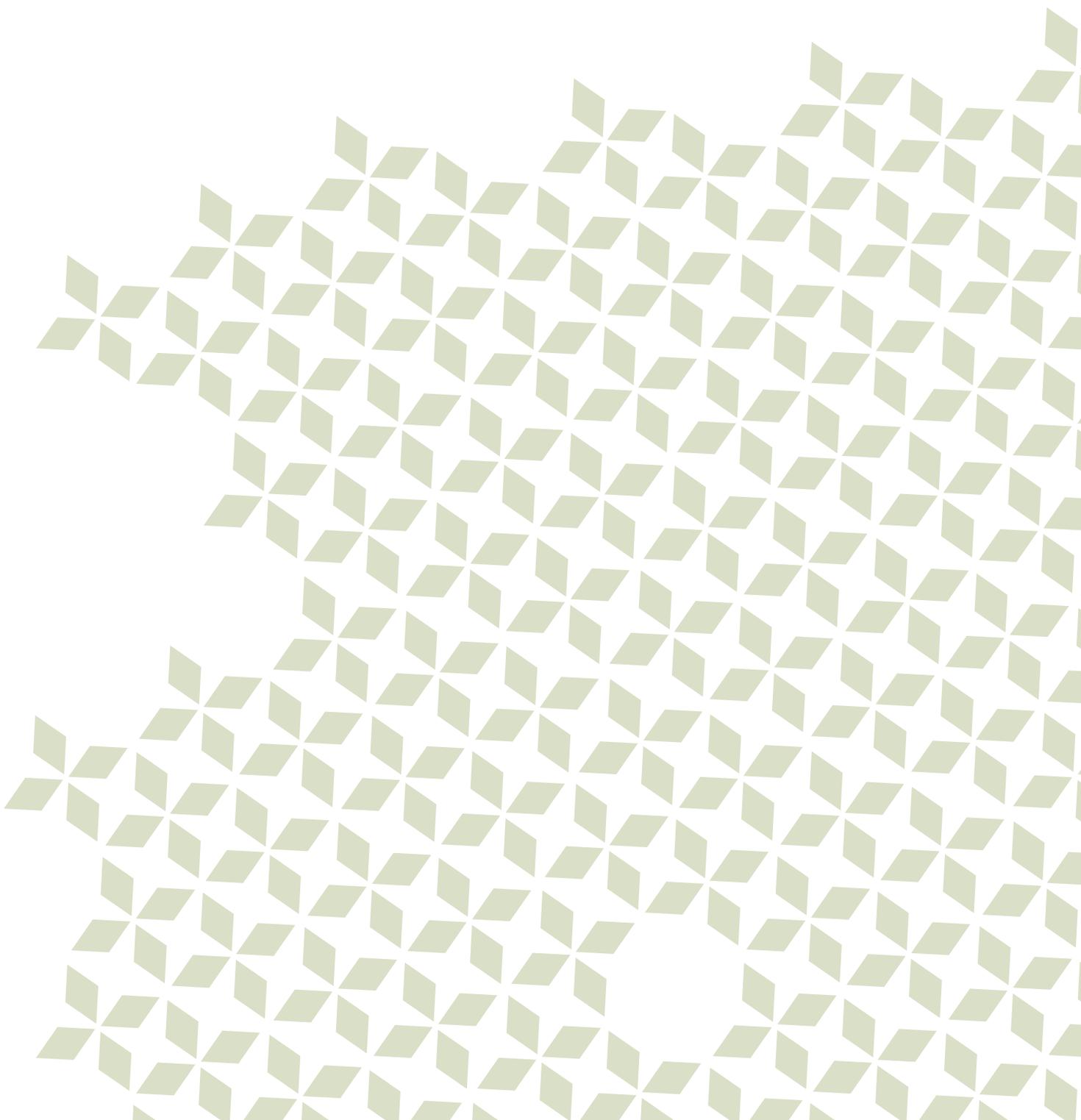
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RENEWING CANADA'S SOCIAL ARCHITECTURE

Renewing Canada's Social Architecture is a collaborative project involving researchers from the Mowat Centre, the Caledon Institute for Social Policy, the Institute for Competitiveness and Prosperity and the Institute for Research on Public Policy. The purpose of the project is to advance public dialogue on our social architecture, and highlight areas where our core social programs and policies require modernization to meet Canadians' needs. Each report contributed to the project is the responsibility of the authors alone, and does not necessarily reflect the views of the other contributors or organizations.

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