



# **Child Benefit Reform in Canada: an evaluative framework and future directions**

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## EXECUTIVE SUMMARY

Momentum has been building over the past several years for fundamental reform of federal and provincial child benefits, based on the concept of an integrated child benefit. A half century-old idea whose political time finally has come, an integrated child benefit would replace the various federal and provincial child benefit programs with a single system providing equal benefits to all low-income families with children, regardless of their source(s) of income.

The 1997 federal Budget announced complementary actions on the part of the federal and provincial/territorial governments to build together a National Child Benefit System. The federal government will enrich and reconfigure its Child Tax Benefit/Working Income Supplement to create a single Canada Child Tax Benefit paying the same maximum benefit to all low-income families with children, while continuing to provide partial benefits to the majority of non-poor families. The provinces and territories will reduce their welfare benefits on behalf of children by the amount of the increase in federal child benefits, though they have agreed to reinvest the resulting savings in other programs and services for low-income families with children. Such programs could include income-tested child benefits, earnings supplements for the working poor, child-related social services (e.g., child care) and provision of in-kind benefits (e.g., supplementary health care) to all low-income families.

The main purpose of this report is to develop key elements of an evaluative framework as a means of monitoring and directing the shape that the National Child Benefit System will take in the coming years. The proposed evaluative criteria flow from the authors' vision of a fully-developed and effective integrated child benefit for Canada. This vision, in turn, is grounded in our understanding of the history of Canadian child benefits – the public purposes upon which they have been constructed in the past, the influences surrounding them, and their role in the larger context of Canadian social security and economic development.

Canada's child benefit system has undergone major changes throughout this century which, in both philosophy and substance, reflect the evolution of the welfare state in general. Born during the First World War as a tax-delivered, selective and regressive children's tax exemption geared to the minority of families with taxable incomes, the federal child benefit system expanded by adding toward the end of World War Two a universal base of Family Allowances serving all families with children, regardless of income. Changes in the 1970s introduced important elements of progressivity with the introduction of the refundable child tax credit for lower-income and middle-income families, taxation of Family Allowances, a substantial increase in Family Allowances and the all-important protection of full indexation of benefits and thresholds. Under the Conservative regime of the 1980s and 1990s, federal child benefits underwent a revolution which transformed them from a universal though overall not progressive system to a progressive and income-tested system serving the low-income and middle-income majority of Canadian families with children. In 1993, Family Allowances and the refundable and non-refundable child tax credits were replaced by the income-tested Child Tax Benefit, which also provides a Working Income Supplement for working poor families with children.

Though not widely recognized as such, child benefits also are delivered by the provincial and territorial governments, traditionally through their welfare systems in the form of cash and in-kind bene-

fits paid to families on behalf of children. The infusion of federal cash through the enriched Canada Child Tax Benefit and reinvestment agreement with the provinces is intended to reduce and eventually replace welfare benefits for children with a child benefit system geared to all low-income families with children. But even before the announcement of the National Child Benefit System in the 1997 federal Budget, BC had created Canada's first integrated child benefit; in July of 1996, the BC Family Bonus replaced income assistance (i.e., welfare) benefits on behalf of children with an income-tested benefit payable to all low-income families with children in the province as well as to modest-income families. Saskatchewan, Quebec and New Brunswick also are creating their own integrated child benefit programs. Quebec already offers an earnings supplement for working poor families with children, and Alberta, Saskatchewan and New Brunswick plan earnings supplements as well.

The roots of the concept of an integrated child benefit can be traced as far back as the architecture of Canada's postwar social security system drawn by Leonard Marsh in 1943. But his proposal for a single, stand-alone, federal child benefit program was not implemented, and instead a hodgepodge of federal and provincial child-related benefits grew like Topsy after the war. The idea of an integrated child benefit resurfaced in the 1980s as a key element (albeit not legislated) for reforming Ontario's welfare system, and in the 1990s in the federal Social Security Review and the work of the Caledon Institute of Social Policy. The integrated child benefit progressed from concept to political reality largely due to the efforts of the provincial and territorial governments in the landmark *Report of the Ministerial Council on Social Policy Reform and Renewal* of 1995. In 1996, a federal-provincial/territorial working group of officials was established to design the National Child Benefit System announced in the 1997 federal Budget, and is continuing to work on its implementation. The federal government has committed an additional \$850 million to the original \$850 million infusion of new money to create the Canada Child Tax Benefit.

The authors of this report offer their own vision of the essential characteristics of a mature integrated child benefit system. These features include: a broadly-based, income-tested system based on gross family income; fully-indexed benefits and thresholds; a substantial increase in maximum benefits over time first to fully replace welfare expenditures on behalf of children (a \$2,500 maximum benefit target) and then to raise the level to cover the cost of raising a child for low-income families (a \$4,000 maximum benefit target); and improvements in benefits for modest-income families along with future increases to the maximum benefit to avoid additional increases in the marginal tax rate of low-income families.

Based on this vision of an integrated child benefit, the report presents key evaluative criteria to guide and measure progress in constructing the National Child Benefit System and offers some measures of the objectives that governments have put forward, as well as additional objectives proposed by the authors. Governments have set three main objectives for the National Child Benefit System – preventing and reducing the depth of child poverty, promoting attachment to the workforce (thus reducing welfare caseloads), and reducing overlap and duplication of child-related benefits. The report adds to this list the objectives of adequacy, fairness, promoting dignity and independence, and economic stabilization.

The report argues that depth of poverty, not incidence of poverty, is the more appropriate measure of the National Child Benefit System's anti-poverty impact – particularly during the developmental

stage when maximum benefits have not yet reached their mature level. The National Child Benefit System legitimately can be expected to reduce the average and total depth of poverty among low-income families with children, though in its initial phase only for low-income families not on welfare (i.e., the working poor and low-income families on Employment Insurance). However, over time a mature child benefit system with a higher maximum benefit should reduce the depth of poverty among all low-income families with children, and may even reduce the poverty rate to some extent. The report cautions governments and social groups not to tout the National Child Benefit System as a way of preventing poverty.

Over time, the National Child Benefit System should help reduce welfare caseloads by reducing the number of families going on and increasing the number going off welfare, though other factors (especially the state of the economy) all too easily can swamp this effect. The National Child Benefit System should not be sold as a Pied Piper of welfare reform, promising to lead legions of families off social assistance and into the labour market.

The report argues strongly for tangible measures of the objective of adequacy, which is crucial to the successful growth and performance of the National Child Benefit System. One clear criterion of adequacy is the level of maximum benefits, which by the year 2000 should reach the \$2,500 annual target required to supplant welfare-delivered child benefits, and \$4,000 within the first decade of the next century as a rough proxy for the cost of raising a child (this target amount is subject to revision depending on the findings of the recommended study of the cost of raising children in low-income families). Another requirement of adequacy is full indexation of both benefits and income thresholds for the Canada Child Tax Credit when it comes into force in 1998 and of provincial child-related benefits. The long-forgotten child benefit objective of economic stabilization should be measured using econometric methods.

The development of the National Child Benefit System should not be assessed solely by government. The report proposes that an independent body be established to track progress in implementing the National Child Benefit System. This important function could be vested in a Parliamentary institution – such as a national Ombudsman for children – or it could be undertaken by a non-governmental organization. In addition, Statistics Canada could be asked to develop a regular series of statistical reports specifically meant to measure progress in implementing child benefit reform. Social groups have a vital role to play in this process by monitoring both the development of the National Child Benefit System and its formal evaluation.

The current child benefit system is assessed against the evaluative criteria and found wanting in several important respects. Maximum benefits are too low. Partial deindexation of federal child benefits and non-indexation of provincial welfare-delivered child benefits constitute a persistent and pernicious social policy virus that weakens the child benefit system's capacity to achieve all three of its basic objectives – anti-poverty, horizontal equity and economic stabilization. Partial deindexation results in an ever-changing child benefit system that does not perform in practice the way government portrays it in theory.

The federal-provincial child benefit system overall is complex and inconsistent in key elements of its design. It does not treat all low-income families with children equally, and thus forms a major part

of the welfare wall. The economic stabilization role of child benefits has been weakened not only by inadequate indexation, but also substantial cuts in benefits for non-poor families during the 1980s which have not been fully compensated by improved payments to low-income families. The use of a net family income definition for federal child benefits is cost-ineffective and introduces both horizontal and vertical inequities.

Although it is far too soon to evaluate the new child benefit system, which is in its infancy, its overall philosophy and design hold out great promise – if the federal government continues to invest the money required to fully replace welfare benefits on behalf of children and then enriches the system further to reach the \$4,000 target. Details are sketchy at the time of writing on provincial child benefit initiatives, but if the BC experience is any guide, the income-tested integrated programs planned by Saskatchewan and Quebec bode well for the future. Though the BC Family Bonus has been operating for just over a year, our analysis (which included focus groups of recipients and front-line workers) is generally very positive. BC's pioneering social program can offer valuable lessons for the federal and other provincial governments in reforming their respective child benefits.

The report raises several issues involving the design and future development of the National Child Benefit System and offers suggestions on how to deal with them. The resolution of these issues will be important for the future development of the National Child Benefit System from its promising beginnings into the fully mature and effective integrated child benefit that we envisage.

Although contentious among welfare rights advocates and social groups, the requirement not to 'pass through' increased child benefits to welfare recipients during the first phase of reform is a necessary part of the sea-change of child benefits; the rationale for this decision should be explained by governments and debated openly. The report argues that the use of net income introduces vertical and horizontal inequities into the child benefit system and wastes valuable resources on well-off families; it recommends the use of gross income, though with special attention paid to the potential negative impact of this change on self-employed groups. Federal and provincial child benefits should fully index both their rates and income thresholds to stem the erosion of benefits and steady compression of child benefits down the income spectrum with each passing year. Governments should investigate potential problems with the definition of family for child benefit purposes; as benefits increase, the temptation to not report a spouse's income could increase, resulting in waste and unfairness. The report reiterates its rationale and recommendations as to the amount and timing of future increases in the level of maximum child benefits.

## INTRODUCTION

The provinces and the federal government have set out on a joint endeavour to develop a National Child Benefit System. The foundation of the new system will be an integrated child benefit, which itself will take a number of years to fully mature. This report develops a framework for the evaluation of the integrated child benefit, as a means of monitoring and directing the shape it will take in the coming years.

The proposed evaluative criteria flow from the authors' vision of a fully-developed, adequate integrated child benefit for Canada. This vision, in turn, is a product of our understanding of the history of Canadian child benefits – the public purposes upon which they have been constructed in the past, the influences surrounding them, and their role in the larger context of Canadian social security and economic development. Consequently, the first section of the report briefly summarizes the development of the Canadian child benefit system in this century, dealing mainly – though not exclusively – with federal programs. The second section then discusses the roots of the concept of an integrated child benefit and presents our vision of the essential characteristics of a mature integrated child benefit system. It is this vision which provides the basis for the remainder of the report.

The report's third section presents key evaluative criteria to guide and measure progress towards an effective integrated child benefit for Canada. The fourth section assesses the current child benefit system against the evaluative criteria, and does the same for federal and provincial child benefit reforms – except for British Columbia, whose new BC Family Bonus is discussed separately in the fifth section. The sixth section raises several issues involving the design and future development of the child benefit system and offers the authors' suggestions on how to deal with them.

It is our hope that this report will prove useful and timely in this formative stage of the National Child Benefit System as the federal and provincial/territorial governments continue to build together this important new social program for families with children.



## DEVELOPMENT OF CHILD BENEFITS

In July 1996, British Columbia launched the BC Family Bonus, the first integrated child benefit program in Canada. Late in 1995, the provincial and territorial governments (except for Quebec) released a joint *Report of the Ministerial Council on Social Policy Reform and Renewal* which, *inter alia*, called upon the federal government to work with them to create an integrated child benefit system for Canada. The 1997 federal Budget announced that Ottawa and the provincial/territorial governments are working together to build a National Child Benefit System through complementary and cooperative reforms of their child benefits and welfare systems.

These recent and planned changes hold out the promise of creating a stronger, fairer and more effective child benefit system that will form an essential component of a comprehensive strategy to tackle child poverty. But the emerging federal and provincial child benefits reforms are not entirely new ideas. Rather, they build upon the trend to income-tested social programs over the past two decades as well as a half century-old concept – an integrated child benefit. This section sketches the evolution of child benefits, while the next section traces the development of the concept of an integrated child benefit.

### Objectives of child benefits

The child benefit system today – and the new one that is emerging with the creation of the National Child Benefit System – differ significantly from the system that was born in the two world wars. At the same time, though, the current and nascent child benefit systems still have strong roots in the purposes that were established many years ago. Over time, federal and provincial child benefit programs in Canada have assumed among them three broad objectives:

*horizontal equity*

- to recognize the fact that parents have heavier financial demands than childless couples and single people with the same employment incomes, and acknowledge the contribution that all parents make to society in raising future citizens, workers and taxpayers.

*anti-poverty*

- to supplement the incomes of poor and modest-income families with children.

*economic stabilization*

- to put cash into the hands of parents and thereby stimulate consumer demand, aiding recovery from recession.

### Federal child benefits

We briefly summarize here the key changes to federal child benefits, dividing their history into four phases. Overall, the long-term – and continuing – trend is toward greater ‘targeting,’ meaning

gearing child benefits to need as measured by family income. Since the late 1970s, the anti-poverty objective has taken on greater weight at the expense of the horizontal equity objective.

#### *the first phase – regressive targeting*

Federal child benefits throughout most of the first half of this century were inversely geared to need, excluding the lower-income majority of families and delivering benefits only to the better-off minority. Benefits were delivered through the income tax system in the form of income tax savings from the children's tax exemption (temporarily changed to a non-refundable credit from 1942 to 1946). The children's tax exemption distributed its benefits in a regressive manner: The higher the claimant's tax bracket, the larger his (it was mainly 'his' in those days) income tax savings because the children's tax exemption reduced taxable income. The federal child benefit system excluded families which did not owe income tax – the majority, in those times of widespread poverty and low average incomes.

#### *the second phase – untargeted universality*

Family Allowances added a new child benefit in 1945, delivered as a non-taxable monthly cash payment to all mothers on behalf of their children, which established a universal foundation for the child benefit system. Family Allowances extended child benefits to poor families, which from 1945 until 1978 received their federal child benefits from this single program. However, from 1947 on, non-poor families with children received both Family Allowances and income tax savings from the children's tax exemption; better-off families received larger income tax savings from the children's tax exemption. Poor families which did not qualify for the children's tax exemption got smaller total child benefits than did non-poor families. The new system was universal, but was not geared to need as measured by income.

#### *the third phase – progressive universality*

The 1970s brought significant increases in child benefits and several changes which geared the child benefit system more positively to income. In 1973, Family Allowances were tripled and fully indexed to the cost of living: Both changes benefited poor families most since child benefits form a larger proportion of their income and they suffered most in relative terms from unindexed benefits that lost value to inflation. Along with the 1973 increase, Family Allowances became taxable, which made them 'progressive' in distribution since their value decreased as incomes increased and vice versa: The higher taxpayers' marginal tax rate, the more income tax they paid on Family Allowances and the lower their net (i.e., after-tax) benefits. However, the children's tax exemption offset the taxability of Family Allowances. In 1978, the federal government created a new child benefit program, the refundable child tax credit, which provided its maximum benefit to low-income families, a declining amount to middle-income families and nothing to the well-off. Like Family Allowances, the refundable child tax credit was indexed to the cost of living – both its benefits and the income threshold for maximum payments. For the first time, the income tax system was used to deliver benefits to families too poor to owe income tax.

Despite these various changes which benefited lower-income families in particular, the overall distribution of child benefits still bore no logical or defensible relationship to need as measured by family income. A family earning \$50,000 received more child benefits than families earning \$15,000 or less. In

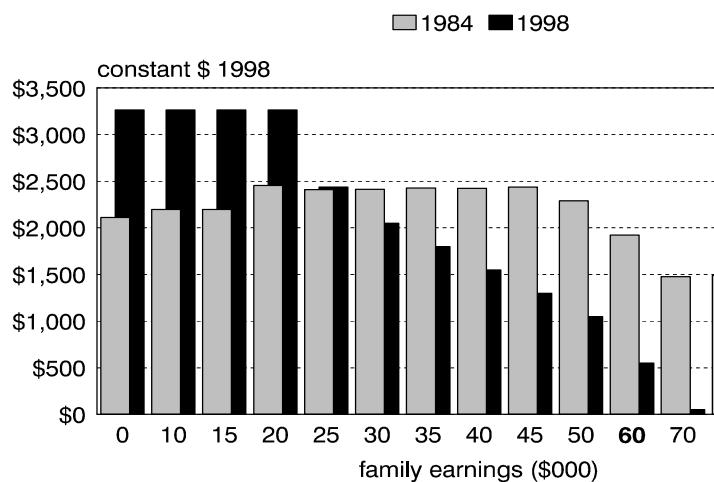
1984, the final year of this phase of federal child benefits, a two-earner family earning \$100,000 with two children got \$1,515 worth of child benefits; a family earning \$10,000 received \$2,197 in child benefits – only \$682 more than the family with ten times as much earned income. A \$100,000 family got larger child benefits than families earning between \$70,000 and \$90,000.

*the fourth phase – progressive targeting*

The 1980s brought additional targeting. The children's tax exemption was reduced in 1987 and then, in a reprise of the 1942-46 interlude, converted to a non-refundable child tax credit in 1988. Whereas the children's tax exemption was a regressive social program providing benefits in the form of income tax savings that increased with income, the non-refundable child credit gave virtually all taxpaying families equal income tax savings. However, the non-refundable child tax credit still excluded families below the taxpaying threshold and was worth less than the maximum in the case of families whose income tax liability was less than the value of the credit. The equivalent-to-married exemption, a benefit paid on behalf of the first child in single-parent families, also was converted to a non-refundable credit. The refundable child tax credit enjoyed a substantial boost in the latter half of the decade, including a new supplement for children under 7.

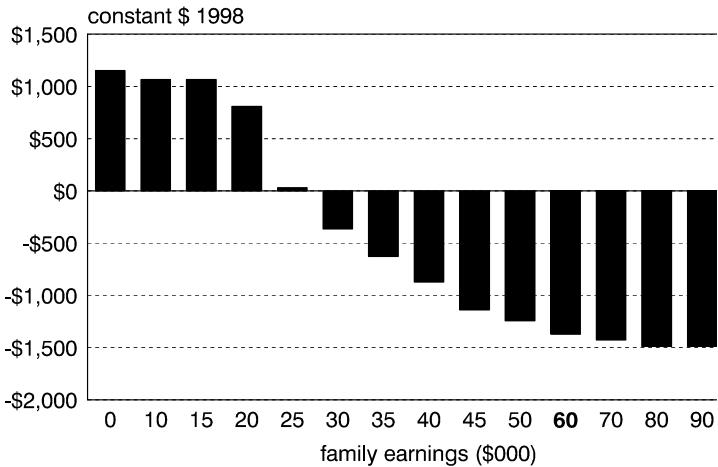
The federal child benefit system, which had been fully indexed to the inflation rate since 1973, was partially deindexed as of 1985 – a profound change that is still in effect today. As explained later, partial deindexation is a regressive measure which works against the progressive changes.

**Figure 1 TOTAL FEDERAL CHILD BENEFITS, TWO-EARNE  
WITH TWO CHILDREN, BY FAMILY EARNINGS, 1984 AN**



*data: Caledon Institute of Social Policy*

**Figure 2 CHANGE IN TOTAL FEDERAL CHILD BENEFITS, TWO-EAF  
COUPLE WITH TWO CHILDREN, BY FAMILY EARNINGS, 1984/19**



*data: Caledon Institute of Social Policy*

Ottawa announced the imminent demise of universal child benefits in 1989 by requiring upper-income families to repay more or (if their incomes were high enough) all of their Family Allowances by means of a clawback administered through the income tax system. The measure was phased in over three years between 1989 and 1991, one-third each year. As of 1991, well-off families received what amounted to temporary Family Allowances since they had to pay back through the clawback at income tax time the benefits they had received the previous year. This get now/pay back later, pretend-universal Family Allowance was one of the more peculiar episodes in the history of Canadian social policy.

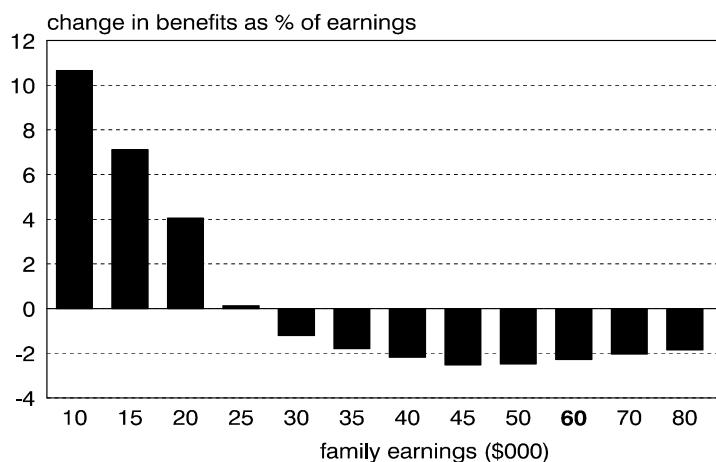
The 1990s brought a formal break with universality and a shift to a wholly income-tested federal child benefit system. In 1993, the three major federal child benefits – Family Allowances, the refundable child tax credit and the non-refundable child tax credit – were replaced by a single income-tested Child Tax Benefit which increased payments to working poor families with children (by paying a Working Income Supplement), maintained the level of benefits to other low-income families, reduced benefits for middle-income families and removed benefits from upper-income families. The 1997 federal Budget announced further significant changes which are the main subject of this report – an increase and restructuring of the Child Tax Benefit into the Canada Child Tax Benefit which will provide equal federal payments to all low-income families with children, and reinvestment of provincial government savings from reduced provincial welfare expenditures on behalf of children (resulting from increased federal child benefits) in other provincial income programs or social services for low-income families with children.

The striking changes since 1985 are summarized in Figure 1, which compares the distribution of federal child benefits under the old system in 1984 and the Canada Child Tax Benefit in 1998. (The 1984 numbers have been converted to 1998 dollars to allow a valid comparison by adjusting for the impact of inflation on the value of the dollar.) The old system was universal and not progressively geared to income. The new system, though no longer universal, still serves the majority of Canadian families with children but distributes its benefits in a progressive fashion.

Figure 2 shows the change in federal child benefits in dollar terms. For two-earner couples with two children, low-income families will enjoy increases in federal child benefits of up to around \$1,000, while non-poor families will suffer losses that range from \$360 for those earning \$30,000 to \$1,500 for those earning \$80,000 or more.

Figure 3 expresses the gains and losses in federal child benefits as a proportion of family earnings. Families earning less than \$25,000 will experience increases in federal child benefits ranging from 10.7 percent of earnings for those earning \$10,000 to 0.1 percent of earnings for families earning \$25,000 (i.e., no significant change). Families earning over \$25,000 lose child benefits, the amount rising with income. In relative terms, middle-income families in the \$40,000-\$60,000 group (the latter is about the average earnings for a family with two children) have been hardest hit, those earning just \$45,000 – \$15,000 below average earnings – most of all. However, measured in proportion to families' total earnings, the cuts in child benefits for middle-income and upper-income families are relatively small, whereas the increases in benefits for low-income families – though not spectacular – are more significant.

**Figure 3 CHANGE IN TOTAL FEDERAL CHILD BENEFITS, TWO COUPLE WITH TWO CHILDREN, AS % OF FAMILY EARNINGS, ·**



## **Provincial child benefits**

The provinces and territories operate various child benefit programs which in almost all cases are aimed at the anti-poverty objective. Quebec provides not only benefits for low-income families with children, but also a universal child income tax credit to all families in support of the horizontal equity objective.

### *welfare benefits for children*

Most provincial and territorial governments make payments on behalf of children through their social assistance (welfare) systems at an estimated total cost of \$2 billion, or 40 percent of the \$5 billion federal Child Tax Benefit. The significant exceptions are British Columbia and Quebec which, as explained in a later section, recently launched innovative social programs replacing their welfare benefits for children with income-tested child benefits for low- and modest-income families with children, whether they are on welfare or in the workforce.

The amounts and design of welfare benefits for children, as for adults, vary considerably from one province to another. Welfare benefits for children range in most provinces from around \$1,200 to \$1,800 per child per year for basic needs (excluding shelter costs), though a few provinces pay below or above this range. In addition to cash payments, welfare programs may pay on behalf of children special allowances (e.g., winter clothing allowances), in-kind benefits (e.g., supplementary health and dental care, and prescription drugs) and housing subsidies. To qualify for social assistance, applicants must undergo a comprehensive and intrusive ‘needs test’ which scrutinizes their incomes, fixed and liquid assets, and budgetary needs.

### *other provincial child benefits*

Several provinces also operate other income security programs for children. In the 1970s, Saskatchewan pioneered an income-tested program for children – the Family Income Plan (FIP) – payable to both welfare and working poor families. Manitoba’s Child Related Income Support Program (CRISP) is another income-tested program directed to poor families with children. Eligibility for both FIP and CRISP is determined on the basis of family income and an assets test. Until this year, Quebec provided a variety of cash child-related benefits, including Family Allowances for all children, benefits for newborns and young children, and earnings supplements for working poor families; changes to this system are noted below.

### *new provincial child benefits*

Several provinces are undertaking innovative reforms of their child benefits. Some provinces are replacing welfare benefits for children with income-tested child benefits payable to all lower-income families with children, including the working poor. Some provinces are providing cash supplements to bolster the earnings of working poor parents.

Alberta to date has not planned to create a truly integrated child benefit. Instead, it has opted to create a new wage-based program for working poor families with children, while continuing to pay

welfare benefits on behalf of children in welfare families. Alberta has announced that its Family Employment Tax Credit will be phased in between January 1997 and January 1998. Like the soon-to-be-eliminated federal Working Income Supplement, the Alberta Family Employment Tax Credit is intended to supplement the earnings of working poor families with children. The maximum Family Employment Tax Credit will equal the 1996 federal Working Income Supplement and will be phased in at the rate of a maximum \$500 per family per year (\$250 per child) in 1997 and a maximum \$1,000 per family per year (\$500 per child) in 1998.

The credit is calculated as 8 cents for every dollar of family employment earnings (either from wages or self-employment) above \$6,500 and is reduced by 4 cents for every dollar of family net income above \$25,000. The maximum Family Employment Tax Credit will go to families between \$19,000 and \$25,000; benefits will disappear when net family income reaches \$50,000.

Some 130,000 low- and middle-income families with 200,000 children are expected to benefit from Alberta's new program. Revenue Canada will deliver the Family Employment Tax Credit using the Canada Child Tax Benefit administrative apparatus. The Alberta credit will be delivered twice a year, based on federal income tax data.

Saskatchewan, which created Canada's first income-tested child benefit in 1974 with its Family Income Plan, has proposed a two-tier system of income support for low-income families. The first tier will be the Saskatchewan Child Benefit, replacing welfare benefits on behalf of children with an income-tested benefit for all low-income families, whether on welfare or in the workforce. The design parameters of Saskatchewan's new integrated child benefit program had not been finalized at the time of writing.

Saskatchewan's second tier will be an Employment Supplement to bolster the employment earnings of low-income families, including welfare families with part-time earnings. The maximum benefit and other design features will vary according to family type and size. The proposed Saskatchewan Employment Supplement will replace all or almost all of the 'work incentives' in the welfare system but will provide equal work incentives to the working poor. Details are still to be announced.

Quebec is undertaking a major redesign of its various child-related benefits as part of a new family policy. A new family allowance program for low-income and modest-income families with children, including the working poor as well as those on welfare, will provide for the essential needs of children. Benefits are paid on a monthly basis. The new family allowance program came into effect in September 1997.

For two-parent families, the maximum new family allowance is \$975 a year each for the first and the second child and \$398 for the third and each additional child, payable to families with net income under \$21,825 – the threshold for maximum benefits. Above this threshold, payments are reduced at the rate of 30 cents for every dollar of net family income between \$21,825 and \$25,920, 50 cents for every dollar of net family income between \$25,921 and \$49,999, and 5 cents for every dollar of net family income above \$50,000. Eligibility for benefits ends at net family income of \$52,620 for families with one child, \$56,100 for families with two children and \$64,060 for families with three children.

Single-parent families receive an additional maximum annual family allowance of \$1,300 per family on top of the rates for two-parent families. The threshold for maximum benefits is \$15,532 in net family income. Above this threshold, benefits are reduced by 50 cents for every dollar of net family income between \$15,532 and \$20,920, 30 cents for every dollar of net family income between \$20,921 and \$25,920, 50 cents for every dollar of net family income between \$25,921 and \$49,999, and 5 cents for every dollar of net family income above \$50,000. Eligibility for the new family allowance ends at net family income of \$52,620 for families with one child, \$56,100 for families with two children and \$64,060 for families with three children.

The new family allowance replaces four child benefit programs – welfare (known as social aid in Quebec) benefits for children, the Quebec family allowance, the allowance for young children and the allowance for newborns. The new family allowance integrates in one program welfare benefits on behalf of children and the Quebec basic family allowance – and eliminates the allowance for young children and allowance for newborns (the latter program will be phased out between 1997 and 2002 and recipient children born before October 1, 1997 will continue to receive the benefit). Although the universal Quebec family allowance program is gone, the child benefit system will retain a universal base by means of the Quebec child income tax credit, which is worth \$520 for the first child of a two-parent family, \$780 for the first child in a single-parent family and \$480 for the second and each additional child for both types of family. We regard the child income tax benefit *de facto* as part of Quebec's child benefit system.

To take into account changes in the federal child benefit system (i.e., the shift in 1997 from a per-family to per-child Working Income Supplement to be followed in 1998 by the Canada Child Tax Benefit), Quebec is adding a top-up for welfare families with children to ensure that they will not lose any benefits during the transition to the new system. The monthly top-up is \$63 for the first child and \$35.42 for the second child; single-parent families (but not two-parent families) get an additional \$18.50 per month for the third child. The top-up will end in July 1998 when the Canada Child Tax Benefit comes into effect.

Quebec's Parental Wage Assistance Program, an earnings supplement for working poor families with children, will continue though with some changes in its parameters. In 1997, the Parental Wage Assistance Program phases in at the rate of 28.5 cents for each dollar of employment earnings above \$1,200. The maximum supplement is \$3,534 for two-parent families and \$2,422 for single-parent families, payable up to \$13,600 for couples and \$9,700 for one-parent families. Benefits are reduced by 43 cents per dollar above the thresholds, disappearing at \$21,825 for two-parent families and \$15,332 for single-parent families.

New Brunswick announced in its most recent Budget a two-tier provincial child benefit system combining an income-tested child benefit and an earnings supplement which parallel the current federal Child Tax Benefit and Working Income Supplement, though with different benefit levels. Both programs will be delivered by Revenue Canada, taking advantage of the federal Child Tax Benefit administrative machinery.

The New Brunswick Child Tax Benefit will pay up to \$250 per child per year for families with incomes up to \$20,000; an estimated 50,000 low-income families will receive benefits. However, in its initial form at least, this program will not pay a large enough benefit to replace welfare payments on behalf of children.

The New Brunswick Working Income Supplement will pay up to \$250 per family per year. Benefits will phase in above family earnings of \$3,750 and will reach the maximum amount between \$10,000 and \$20,921 to phase out once family income reaches \$25,921. An estimated 24,000 working poor families will receive this earnings supplement.

As noted, BC was the first jurisdiction to create an integrated child benefit. Launched in July of 1996, the BC Family Bonus delivers an income-tested benefit to all low- and modest-income families with children in the province. We examine this major advance in social policy in some detail in a later section.



## AN ADEQUATE INTEGRATED CHILD BENEFIT

The essence of the concept of an ‘integrated child benefit’ is to provide a common child benefit to all low-income families with children, whether they get their income from work, welfare, Employment Insurance or some combination thereof. Children are ‘removed from welfare’ in the sense that their income benefits come from outside the welfare system. Children in working poor families and other low-income families (e.g., those on Employment Insurance) receive equivalent levels of benefit from the same integrated system as children in welfare families. The term ‘integrated’ denotes the aim of combining current diverse income support expenditures on low-income children into a single new system.

### Origins of the concept of an integrated child benefit

The idea of an integrated child benefit gained prominence when it was proposed by the Ontario Social Assistance Review Committee in its 1988 report *Transitions*. However, the concept is much older, dating at least as far back as World War Two. Social policy pioneer Leonard Marsh’s famous 1943 blueprint for Canada’s postwar social security system proposed a ‘children’s allowance’ which today we would label an integrated child benefit [Marsh 1943: 85]. He argued that child benefits should be delivered through a new program separate both from welfare, which then (as now) provided benefits for children, and from proposed social insurance programs for unemployment, health care, disability and old age (which, with the exception of the fledgling 1940 Unemployment Insurance program, did not exist at that dawn of the modern welfare state).

Marsh characterized child benefits as ‘the key to consistency’ to the social insurance-based social security system that he and other social reformers wanted politicians to build as a key element of the postwar reconstruction of Canada. Marsh proposed a federal child benefit program, financed out of general revenues, to operate independently of social insurances financed through payroll taxes. Contemporary policy-makers should be reminded of the reasons for Marsh’s recommendation – which remain as valid today as they were a half century ago – as they build an integrated child benefit for Canada.

If social insurance programs were to function properly in Marsh’s ideal social security system, they should not themselves provide children’s benefits because recipients families would receive income not available to families in the workforce at similar or even lower levels of income. Children’s benefits tied to social insurance programs would result in inconsistent treatment of families on and off social programs. The same argument went for welfare, which then – as now – paid benefits on behalf of children, resulting in inconsistent treatment of families on welfare and other low-income families. In today’s parlance, Marsh was concerned about equity and disincentive problems created when child benefits are provided by social insurance and welfare programs.

Moreover, social insurance schemes were intended to meet either temporary or (in the case of old age pensions) end-of-life-cycle income needs. But many – in those days, most – parents needed

child benefits to supplement their inadequate wages throughout their child-rearing years, not just when contending with income losses from unemployment, illness or accidents which social insurances were intended to replace. Marsh argued that child benefits should be financed out of general revenues rather than the payroll taxes that would fund social insurance programs because society as a whole benefits from parents' child-rearing work and has a stake in helping offset the cost of raising children. In the model social security system envisioned by the social policy visionaries of the 1930s and 1940s, social insurances, children's allowances and employment each had clear, distinct and essential – though inter-related – roles to play in providing the security that the economy had proven so incapable of delivering during the terrible years of the Great Depression.

Marsh's framework for social security was only partly put in place after the war. One of the major omissions was a separate program of children's allowances that would replace child benefits in other programs. The children's tax exemption was resurrected when Family Allowances were introduced. The new Family Allowances program was pegged at such a low (and unindexed) level that it could not provide an adequate supplement to the earnings of lower-wage families. To help correct this flaw, in the 1970s Ottawa boosted and indexed Family Allowances and created a refundable child tax credit to substantially increase total federal child benefits for low- and modest-income families. In 1993, Family Allowances and the refundable and non-refundable child tax credits were replaced by the Child Tax Benefit, which added a benefit for the working poor in the form of the Working Income Supplement. Other social programs also paid benefits related to the number of children in the family. Welfare continued to provide benefits for some poor children. Additional child income benefits grew over the years in Unemployment Insurance and its successor Employment Insurance, the Canada and Quebec Pension Plans, veterans' benefits, workers' compensation, the refundable GST credit and various provincial tax reductions and credits.

### **An adequate integrated child benefit**

The heart of the concept of an integrated child benefit is to provide a common level of child benefits to all low-income families, ideally by recombining all federal and provincial income benefits and tax expenditures on behalf of children into a single system or program, along with additional financing to raise the level of maximum benefits. (We distinguish between 'system' and 'program' because an integrated child benefit could be delivered in the form of separate federal and provincial programs which mesh together in a single system – and, in fact, will be so configured in the immediate future in the several provinces which are mounting their own income-tested child benefit programs.)

A single, common level of child benefit is required for purposes of fairness and to avoid financial penalties for work. The principle of horizontal equity, normally associated with middle- and upper-income families, also should apply to low-income families; regardless of their source and mix of income, all low-income families should receive equal child benefits. Child benefits thus should be 'portable,' providing a stable and assured source of income for eligible families regardless of where they live and work (or do not work, in the case of families receiving Employment Insurance or welfare). To avoid potential work disincentives, eligible families in the workforce should receive the same amount of child benefits as those which are unemployed or not in the labour force.

But if there is to be a fully integrated child benefit delivering payments equally to all low-income families with children, it obviously must fully replace child-related welfare benefits. Welfare is the program of 'last resort' for people who have little or no other assets, so the amount of child benefits for families on welfare ideally would be sufficient to raise a child. Thus, while an integrated child benefit pursues the goals of fairness and removal of financial penalties to work, its ultimate objective should be to pay for the incremental cost of raising a child for low-income families with children.

We are not alone in our position. In introducing its innovative new family allowance program (a form of integrated child benefit), the government of Quebec stated that: "The objective of the new program is to consolidate existing programs to cover all of the essential needs of the children of low-income families, whether the parents are receiving social aid or are working" [Quebec 1997]. While we do not mean to suggest that the government of Quebec supports our view as to the level of child benefits required to meet this standard, nonetheless the Caledon Institute and Quebec agree on the basic objective of an integrated child benefit.

The standard of adequacy for a fully-integrated child benefit system must be an amount sufficient to pay the added cost of raising a child for families with low incomes. However, even an adequate child benefit cannot be expected to address adult poverty, so this single social program alone cannot solve the problem of poverty among families. Child benefits must be complemented by other social and employment policies of vital importance to low-income families, such as an adequate minimum wage, affordable and good quality child care, family support services, employment development services, adequate adult welfare and Employment Insurance benefits, and a low-income tax credit to ease the rising income, payroll and GST tax burden on low-income taxpayers and to stop the steady decline in the taxpaying threshold. In designing an adequate integrated child benefit, we are developing a cornerstone of Canada's social security system, not a stand-alone program purporting to be a magic panacea for all the ills of poverty, inequality and unemployment.

The cost of raising children is a complex and unresolved issue which requires further research. No commonly accepted estimates exist. Rather, there are bits and pieces of data from various points in time which bear directly or indirectly on this question. We offer only a few such results here for purposes of illustration.

The Social Planning Council of Metropolitan Toronto periodically conducts detailed studies of the cost of living for families in the region which include data on children. The most recent figures are for 1991; we have converted them to constant 1997 dollars. The amounts vary by age and sex of child and by family type (one-parent and two-parent).

For single-parent families, the average annual amount was \$5,716 for an only child; for two children, the average was \$5,263 for the older child and \$5,454 for the younger child. The average for an only child in a two-parent family was \$5,653 [Social Planning Council of Metropolitan Toronto 1992].

Another study estimated the cost of raising a child in Ontario in 1988 to be \$3,273 for a family with income of \$25,000, excluding housing and child care expenses, and \$4,281 including these costs

(all figures have been converted to 1997 dollars). Expenditures on children were found to rise substantially with income – e.g., for a family with income of \$57,000, \$9,631 without housing and \$13,031 with housing [Douthitt and Fedyk 1990].

The federal government's new child support payment guidelines are a valuable source of information since they are based on up-to-date data on expenditures on children according to number of children, parental income level and province. Since the custodial parent is expected to contribute a similar amount as the support-paying parent, we doubled the child support amounts (which are for the support-paying person only). For example, the support amounts for BC parents with one child range from \$2,592 for parents with income between \$10,001 and \$12,000, to \$4,824 for incomes between \$20,001 and \$22,000; \$6,696 for incomes between \$30,001 and \$32,000; \$12,216 for incomes between \$60,001 and \$62,000; and \$25,792 for incomes between \$148,001 and \$150,000. The amounts decline with the number of children. For example, the support guidelines for parental income of \$22,000 are \$4,824 for one child, \$8,064 for two children (which averages to \$4,032 per child) and \$10,680 for three children for an average \$3,560 per child [Government of Canada 1996].

Statistics Canada's low income cut-offs vary according to size of community and number of family members. For metropolitan centres of 500,000 or larger, the estimated low income cut-off in 1997 for a family of three (\$29,032) is \$5,297 more than the cut-off for a family of two (\$21,735); the cut-off for a family of four (\$32,722) is \$5,689 more than for a family of three; and the cut-off for a family of five (\$36,577) is \$3,855 more than for a family of four. While the low income cut-offs do not distinguish between children and adults, these increments offer at least a rough proxy for the cost of raising a child for low-income families.

We recommend that the federal and provincial governments, in consultation with social groups and non-governmental experts, undertake a study of the cost of raising children. While the main focus for National Child Benefit System purposes should be on the cost of raising children in low-income families, other income levels as well as other relevant characteristics should be examined – e.g., family type, order and age of child, province and community size.

For purposes of our report, we propose that a mature integrated child benefit provide a maximum benefit of \$4,000 per child. Obviously no single amount can reflect the varying costs of raising a child even among low-income families, since so many variables come into play. Nor would we recommend a complex rate structure for child benefit purposes, since that would give rise to difficult boundary problems and associated inequities. However, some variation according to age and/or order of children could be considered – as is the case for Alberta and Quebec, which took up the federal offer to vary their federal Family Allowance and Child Tax Benefit rates, though Quebec has decided not to vary its Canada Child Tax Benefit rates. But a \$4,000 target would seem to be in the ball park, and is not a high figure in light of available figures. Since it will take some years to reach that target, there will be ample time to conduct the recommended research and come up with options for a benchmark maximum payment for a mature integrated child benefit system.

Admittedly, \$4,000 is substantially more than the current \$1,233 maximum federal Child Tax Benefit for a child under 7 and the rough average of \$2,500 in combined federal and provincial (i.e.,

welfare) child benefits currently paid to welfare families with children. A \$4,000 target is also far above the new Canada Child Tax Benefit's maximum payment of \$1,625 for the first child and \$1,425 for each additional child. An intermediate target should be to extend the average level of child benefits for welfare families – \$2,500 per child – to all low-income children. This intermediate target would permit welfare-related child benefits to be fully replaced. The next stage – raising child benefit levels above \$2,500 to reach the target of \$4,000 – would increase child benefits for all low-income families, including those on welfare.

An adequate child benefit system must fully index both its benefit rates and family income thresholds for maximum payments to provide a stable and consistent level of benefit over time. Fully-indexed benefits and thresholds are essential to maintain the broadly-based child benefit system which we consider necessary for the emerging National Child Benefit System. While the amount of benefit should be geared to level of family income, with maximum payments to those with low incomes and diminishing payments to those with higher incomes, further increases in the maximum child benefit required to achieve a mature system should improve benefits for modest-income families (e.g., \$25,921-\$35,000) by easing the reduction rates, which otherwise would have to become steeper – thereby elevating the marginal tax rates for families in this income range and thus potentially posing a stronger disincentive to improve earnings.

Opinions differ on the importance of a universal base for child benefits, which in any case is now a matter of historical interest since it ended in 1991 when the clawback of Family Allowances was fully implemented. We do not propose to resurrect this age-old and largely academic debate here. However, we believe that a model child benefit system must be broadly-based, serving not just poor families but modest- and middle-income families as well.

A child benefit reserved for poor families alone would require very high marginal tax rates that would pose significant barriers to employment. Suppose the child benefit paid a \$4,000 per child maximum benefit and imposed a 25 percent taxback rate – itself quite high when stacked on income taxes and other social benefits. There would be a \$32,000 income range over which child benefits declined for a family with two children, extending partial benefits to modest-income families, though benefits would end at far below average income in this hypothetical example (the average income for couples with children was \$60,082 in 1995). The only way to confine all child benefits to low-income families and prevent any payments from going to those with modest incomes is to impose confiscatory taxback rates of 40 percent or higher. But extremely high taxback rates would defeat the very purpose of the integrated benefit. An integrated child benefit paying adequate maximum benefits must spread payments over a very broad band of income, extending at least into average income range, thereby serving the majority of families with children and, for most families, meeting horizontal equity objectives.

A broadly-based, income-tested child benefit also has other advantages. It will not stigmatize low-income families with children and – if experience over the past two decades is any guide – stands a far better chance of being sustained and even enhanced. It will serve the economic stabilization objective better than a for-the-poor-only approach.

In summary, our vision of an adequate child benefit system includes:

- a broadly-based, income-tested monthly cash child benefit serving low- and middle-income families with children.
- maximum benefits payable to all low-income families with children regardless of their source(s) of income, with diminishing payments to non-poor families.
- under a mature system, maximum benefits should cover the cost of raising a child (e.g., \$4,000 per child as a provisional target) for low-income families; the interim target should be to extend to all low-income families the level of child benefits currently paid to welfare families (around \$2,500 per child on average).
- benefits and income thresholds should be fully indexed to the cost of living.
- as maximum benefits rise, increases must be extended to modest-income families to prevent taxback rates from becoming unacceptably high and to improve child benefits for families which are above the poverty line but still substantially below average income.

## MEASURING PROGRESS

An essential task in building a new child benefit will be to measure progress. This section develops an overall framework for evaluating the National Child Benefit System. We hope that this framework can provide a basis for a more detailed, comprehensive evaluation plan to be developed jointly by the federal, provincial and territorial governments, in consultation with social groups and non-governmental experts.

### **The governments' objectives: a critical assessment**

Evaluation requires that a set of objectives be established against which to measure performance. Therefore, to permit evaluation, governments need to set clear objectives for the National Child Benefit System. However, as the first major social policy response to Parliament's 1989 Resolution to fight child poverty, the National Child Benefit System is prone to unrealistic expectations, and it may be tempting to set out unrealistic and ultimately unachievable objectives. It is all the more important in these circumstances to define the objectives with great care and precision.

The federal and provincial governments have proposed three objectives for the National Child Benefit System according to the 1997 federal Budget paper *Working Together Towards a National Child Benefit System*:

1. to help prevent and reduce the depth of child poverty.
2. to promote attachment to the workforce – resulting in fewer families having to rely on social assistance – by ensuring that families will always be better off as a result of finding work.
3. to reduce overlap and duplication through closer harmonization of program objectives and benefits and through simplified administration.

Before turning to other objectives not included in the above list, we critically review these three objectives as proposed by government.

#### *1. to help prevent and reduce the depth of child poverty*

##### *a. reduce the depth of child poverty*

The federal, provincial and territorial governments chose their words judiciously in specifying that the National Child Benefit System aims at reducing the 'depth' of child poverty. The most common measure is the 'incidence' (also known as 'rate') of child poverty, meaning the percentage of children in families with incomes below the poverty line. The 'depth of poverty,' sometimes known as the 'poverty

gap,' is the number of dollars below the poverty line that the average low-income family falls. In 1995, the average depth of poverty was \$9,298 for two-parent families with children and \$8,345 for single-parent families, using Statistics Canada's low income cut-offs as poverty lines.

Statistics Canada cautions that its low income cut-offs are neither measures of poverty nor official measures of low income. However, the low income cut-offs are so widely (mis)used that they have become *de facto* official poverty lines. This report follows common practice and uses the low income cut-offs (and estimates of the incidence and depth of 'low incomeness' derived from them) as poverty/low income lines. The use of different poverty lines would not materially affect our argument.

Depth of poverty is superior to incidence of poverty as a measure of the impact of social programs such as child benefits. Indeed, incidence is an inappropriate way to evaluate the effectiveness of anti-poverty programs. A simple hypothetical illustration makes this point.

Suppose a population of 100,000 people, of whom 10,000 or 10 percent have incomes below the poverty line (i.e., the incidence of poverty is 10 percent). One hypothetical social program pays \$1,000 to 1,000 people who are near (within \$1,000 of) the poverty line, for a total cost of \$1 million. Our other hypothetical program pays \$1,000 to the 1,000 people who fall farthest below the poverty line, for the same \$1 million program budget. The first program reduces the poverty rate from 10 percent to 9 percent – that may not seem significant, but in fact it is in relative terms – and helps only the least worse-off 10 percent of the poor. The second program helps the poorest 10 percent of the low-income population but has no impact on the rate of poverty since a \$1,000 increase in the incomes of the poorest, though very important to them, can lift none of them anywhere near the poverty line. Which is the better, more sensible anti-poverty program? We would choose the second program, because it improves the living standards of the poorest. The first program only skims the top of the poverty population and does nothing to help those with incomes substantially below the poverty line.

While this is a contrived example, it makes an important point for real-world social policy: *If we evaluate anti-poverty programs by the extent to which they reduce the incidence of poverty rather than depth of poverty, for any amount of money we would always be more 'effective' concentrating the money as much as possible only on people close to the poverty line.* In an epidemiological analogy, this approach would be like saying a treatment is better that cures only those who are not very sick, as opposed to a treatment that might not 'cure' but which much more significantly reduces the intensity of the illness among those who are most ill. It is precisely because of this kind of problem that epidemiological studies in the health field have developed outcome measures such as 'number of quality adjusted years of life' rather than merely looking at the question of 'cure' or 'not cure.' ('Number of quality adjusted years of life' is a measure of the added number of years of life a person has as a result of the intervention, adjusted to take account of the quality of life so that a person continuing to live in a vegetative state is not counted.)

Moreover, the criterion of reducing incidence stacks the deck against anti-poverty programs and leads to the charge that 'nothing works.' The sad reality is that it would cost an enormous amount of money for government to pay enough benefits to lift all families above the poverty line. The total depth of poverty for families with children amounted to \$6.7 billion in 1995. As a result, unless Canadian taxpayers become much more generous, it is unlikely that government income programs will ever

entirely ‘solve’ the problem of poverty. But we can ease considerably the intensity of poverty, by improving the incomes of low-income Canadians through income security programs such as child benefits. To return to our epidemiological analogy, it is unlikely that government programs will ever ‘cure’ poverty, but they can increase substantially the ‘number of quality adjusted years of life’ by reducing the depth of poverty.

A real life example serves to make the point. When the Canada Child Tax Benefit is introduced in 1998, it will increase the maximum payment for a low-income family with two children under 7 from \$2,466 to \$3,476 – an increase of \$1,010. The average income of two-parent families below the low income cut-off was \$20,020 at last count (1995). The low income cut-off for a family of four ranged from \$31,753 for a metropolitan centre (500,000 or larger) to \$21,944 for rural areas in 1995. A \$1,010 increase in federal child benefits would raise an average low-income couple with children to \$21,030, which is still \$10,423 below the low income cut-off for a metropolitan centre; \$6,105 below the low income cut-off for a city of 100,000-500,000; \$6,016 below the cut-off for centres in the 30,000-100,000 size; \$4,137 below the line for communities of less than 30,000; and \$914 below the low income cut-off for rural areas.

On the other hand, \$1,010 more per child is not an insignificant increase in income to a poor family. The lower the income, the more important the child benefit improvement in relative terms. The average income of low-income single-parent families headed by women was only \$14,612 in 1995. A \$1,010 increase in child benefits for a one-parent family with two children and average low income represents a 6.9 percent boost to their income. This indeed will reduce the depth of poverty.

#### *b. prevent child poverty*

Some programs and policies are intended to help prevent poverty, while others reduce poverty by providing income. Preventive policies include the wide range of programs and services intended to invest in human capital and improve workers’ employability, including education (in the broad sense, from cradle to retirement), training and other ‘employment development programs.’ Also important are programs which enable parents to work and help balance their worker/parent roles, including affordable, quality child care and family-friendly workplace practices. One could stretch the boundary of poverty-prevention programs to include social services such as sex education and marriage preparation and counselling which are aimed at preventing marriage breakdown and unwanted pregnancies – two important causes of child poverty.

Child benefits, however, unlike social services that may prevent or ameliorate the effects of poverty, should neither be touted nor assessed as a measure to ‘prevent’ poverty. Instead, the National Child Benefit System will directly reduce the depth of poverty by providing additional income.

By equalizing child benefits among all low-income families, the National Child Benefit System may help some parents leave welfare for work and assist those who already have jobs to remain in the workforce. To the extent that the new child benefit will help some families to secure and maintain a foothold in the workforce and eventually ‘work their way out of poverty’ if they are able to advance to better-paid employment, it might be said to help ‘cure’ poverty and perhaps even to ‘prevent’ poverty in

the very literal sense that such families will earn an above-poverty income. But this ‘to the extent’ is something of a stretch, and we cannot really expect the National Child Benefit System to have a strong causal effect on ‘curing’ or ‘preventing’ poverty in this manner. Consequently, we suggest that poverty *reduction* through the National Child Benefit System’s income transfers and poverty *prevention* through a range of other programs, mainly social services, be carefully distinguished and that ‘prevention of poverty’ not be considered one of its objectives.

*2. to promote attachment to the workforce – resulting in fewer families having to rely on social assistance – by ensuring that families will always be better off as a result of finding work*

a. promoting workforce attachment and ensuring that families are always better off working

This objective addresses the problem of the welfare wall – the financial barrier whereby families on welfare sometimes have higher incomes, and in most cases income in-kind as well, than they could have working even at a job paying somewhat more than the minimum wage. Extending to the working poor and other low-income families child benefits equivalent to child benefits currently paid to welfare families will substantially lower the welfare wall, but this reform in itself cannot completely eliminate the welfare wall for all families. While the National Child Benefit System will promote attachment to the workforce, and will increasingly do so as the program is improved, the objective of “ensuring that families will *always* [our emphasis] be better off as a result of finding work” is too ambitious and should be reconsidered and reworded.

First, let us see why the promotion of labour force attachment is a reasonable objective for the National Child Benefit System. De-coupling child benefits from the welfare system and replacing them with a payment for all low-income families will promote attachment to the labour market in two main ways: First, such a change will help encourage parents to risk leaving welfare for work because they will no longer lose thousands of dollars in cash benefits for their children. Second, it will help encourage working poor parents to remain in the workforce and not fall (back) onto welfare, since they will receive the same child benefits as families on welfare. Conceivably, the National Child Benefit System also will bolster the incomes of some families in which a parent is unemployed and help tide such families over a bad patch until the parent can find work, rather than having to turn to welfare.

However, the new child benefit system alone cannot guarantee that families will be better off financially at work than on welfare, because it is only one of five major factors that enter into the welfare/work calculus – along with wages, welfare benefits for adults, in-kind child benefits and employment-related costs (e.g., payroll and income taxes, child care, transportation and clothing). Governments control four of these factors fully and one – wages – partly. Governments can go a long way toward ensuring that work provides a better income than welfare by using all these policy levers, not just child benefits alone.

In all provinces and territories, an adult working full time at the minimum wage makes more before-tax income than the amount provided for one adult on welfare. As a result, when the National Child Benefit System fully replaces welfare-delivered child benefits, any single parent will be better off working full time, just taking into account wages. However, it still would be possible for two adults to

have higher income with *both* on welfare rather than just *one* working full-time (which would disqualify the family from welfare), even with a child benefit fully replacing welfare benefits for children. This problem is not related to the presence of children and cannot be solved by reform of the child benefit system.

There is another important instance in which the introduction of an integrated child benefit cannot ensure that wages always provide higher income than welfare: Part-time employment – even somewhat above the minimum wage – plus an adequate National Child Benefit System still could provide a lower income than welfare plus the latter. Again, as the issue of part-time work relates to the ‘adult portion’ of the welfare benefit, this is not a problem that can be solved by reform of child benefits.

Most provinces offer various in-kind benefits, the most important of which is drug costs, that are more generously subsidized for welfare recipients than for non-recipients, even those with low incomes. Until provinces extend these benefits equally to all low-income families on the same basis, in-kind benefits will remain a part of the welfare wall that is not resolvable by reform of child benefits paid in cash.

Finally, another factor that enters into the work/welfare calculus is employment-related expenses. Payroll and income taxes directly lower take-home pay. The cost of items such as child care, clothing for work and transportation effectively reduces income. Governments can take action to lower or eliminate these costs of going to work for low-income parents. Governments could boost relief from Canada/Quebec Pension Plan contributions and Employment Insurance premiums paid by low-earning families and put in place a low-income tax credit to reduce or remove the burden of income taxes. They could remedy the long-lamented lack of affordable, quality child care for low- and modest-income families. Conceivably, governments even could create some sort of refundable tax credit to offset such work-related expenses as clothing and transportation, though a solid system of payroll and income tax relief and child care is the priority. None of this, however, is resolvable through the child benefit system.

To summarize, an integrated child benefit will lower the welfare wall and help remove barriers to parents seeking work. However, the full elimination of all financial disincentives will require that *all* the bricks making up the welfare wall are removed. This goal of the National Child Benefit System should specify that ‘families will always have a higher gross income as a result of finding *full-time* work.’

#### b. fewer families having to rely on social assistance

An integrated child benefit makes employment a more economically feasible alternative because families will not forfeit their child benefits when they move into the workforce: Families will carry their benefits with them when they leave welfare and carry them back if they have to return to welfare. If a family is not on welfare, an integrated child benefit could provide enough additional assistance to make it unnecessary to apply for welfare in the first place. Both of these effects could reduce welfare caseloads; however, the *extent* of the effects, and whether they will have a measurable impact on caseloads, remain an open question. As we discuss below, early results of the BC Family Bonus are promising, but it is too soon to tell whether there will be a longer-term impact.

The objective of reducing welfare caseloads is reasonable, but governments should take care not

to portray the National Child Benefit System as a Pied Piper of welfare reform, leading legions of families off the welfare rolls and into the labour market. An upswing in unemployment easily can swell welfare caseloads and swamp the anticipated labour market incentive effects of an integrated child benefit.

The National Child Benefit System can go a long way toward lowering the welfare wall, but it cannot go the whole way on its own. Complementary policies – such as better and indexed minimum wages, child care, and relief from payroll and income taxes – are required to ensure that work pays better than welfare. Furthermore, economic and employment policies which will increase the supply of jobs are needed. Therefore, in evaluating the extent to which the National Child Benefit System is meeting this objective, it will be very important to isolate its particular effects from that of the ‘background,’ rather than simply looking for (or promising) huge decreases in caseloads.

### *3. to reduce overlap and duplication through closer harmonization of program objectives and benefits and through simplified administration*

The current collection of federal, provincial and territorial child benefits is a prime candidate for rationalization and simplification. The various programs differ in terms of their objectives, design and delivery. While potential savings in administrative costs are not large compared to the amount of benefits paid out, there are some real savings possible through the improved efficiency of delivery through the income tax system.

More importantly, from the perspective of low-income families, a fully integrated child benefit system will reduce the administrative burden imposed on families receiving benefits. An integrated national child benefit system will be much less intrusive than current welfare systems, reducing demands on families’ time, tolerance and privacy. This advantage is of tremendous importance to families receiving welfare.

In measuring progress over the next several years, both reduced administrative cost for government and reduced administrative burden for citizens should be assessed. Because of its importance to recipients, we believe that ‘reducing intrusiveness’ should be recognized explicitly as a separate objective, as discussed later.

### **Other objectives upon which to base evaluation**

The above discussion dissects the stated objectives of governments, but there are several potential objectives that have not been included in the list. The following discussing proposes additional objectives for the National Child Benefit System.

### *adequacy*

One of the long-standing challenges to evaluation is that social programs such as welfare and child benefits have no stated criteria for adequacy. We have urged the federal and provincial governments to adopt two long-term objectives related to adequacy for the income benefits provided under the National Child Benefit System. First, maximum benefits for low-income families should meet the cost of raising a child. Second, both benefits and income thresholds should be fully indexed to the cost of living.

It will take some time for the National Child Benefit System to reach the objective of meeting the cost of raising a child for a low-income family. We have proposed that the Canada Child Tax Benefit be increased to \$2,500 per child by the year 2000, which is approximately the amount required to replace the combination of welfare benefits for children and the federal Child Tax Benefit with a Canada Child Tax Benefit for all low-income families with children. We tentatively propose a \$4,000 per child maximum benefit as the ultimate target to meet the cost of raising a child for low-income families, so the \$2,500 target for the formative stage of the new child benefit system would go only part of the way. Further increases are required in the first decade of the next century to reach the \$4,000 level.

Some provinces could reach those targets sooner than later. Quebec's new family allowance, combined with its child income tax credit and the Canada Child Tax Benefit, will exceed the \$2,500 replace-welfare-benefits-for-children level and, indeed, will move substantially toward the \$4,000 target for a mature child benefit system. For example, combined maximum Quebec and federal child benefits for one child under 7 will total \$3,333 in 1998. (We do not include Quebec's Parental Wage Assistance Program and we assume that Quebec's new family allowance rates for 1998 are the same as 1997.) If British Columbia makes no compensating reduction to its BC Family Bonus to take into account increased federal benefits under the Canada Child Tax Benefit in 1998, the combined maximum BC-federal benefit payable to all low-income families in BC would come to \$3,074 for the first child under 7, which also is not impossibly far off a \$4,000 objective. This target is not utopian and provides a useful standard against which to measure adequacy.

### *fairness*

'Fairness' means treating families equally if they are in like circumstances. For the National Child Benefit System, this means above all that low-income working families should have the same child benefits as those on welfare.

However, there are other features of the current child benefit system which create unfairness and which the National Child Benefit System should remedy – the use of net income and the definition of family. Both of these problems introduce unfairness into the child benefit system because they treat families in like circumstances unequally. The use of net income to calculate eligibility for and the amount of child benefits leads to situations where families which in fact have a high income report a lower net income and so receive the same or even larger child benefits than a family with a lower gross income. The problem with enforcement of the family definition can lead to unfairness if the practice of not

reporting joint income is widespread, so that people who do obey the rules and report their joint income end up with lower child benefits despite being in the same actual circumstances as others not reporting joint income. We discuss these problems in greater detail later.

### *promote dignity and independence*

As noted, while governments naturally seek to harmonize and simplify the administration of their child benefit programs, the families which use them should gain ‘administratively’ as well. The National Child Benefit System should respect the dignity and independence of families with children, and be evaluated accordingly.

Welfare is a highly stigmatizing social program which socially and economically marginalizes its recipients. Characterized as ‘the tangled safety net,’ welfare uses an intrusive needs test which rigorously investigates applicants’ and recipients’ resources, assets and needs as determined by a maze of rules and regulations which beneficiaries sometimes find to be arbitrary in their content and application [National Council of Welfare 1987]. While welfare remains an essential safety net, one of its unfortunate side effects is that it tends to place recipients in a dependent and subservient position.

By contrast, income-tested child benefits like the BC Family Bonus, the federal Child Tax Benefit and its successor the Canada Child Tax Benefit, test income anonymously through the tax system which applies to all Canadians, not just a sub-group of the poor. Because income-tested social programs require no face-to-face contact between families and officials, they minimize bureaucratic interference in people’s lives. Eligibility for benefits is determined by governments using a simple test of families’ net income and the number and age of children. There are no special reporting requirements demanded of families other than that they file their income tax return just like everybody else. The Canada Child Tax Benefit, which underlies the National Child Benefit System, will continue to serve eight in ten families with children, including modest- and middle-income families – not just those with low incomes. It does not question how families spend their benefits but rather assumes and expects parents to spend the money appropriately. It respects families’ privacy and parents’ primary responsibility for their children. The same holds for the BC Family Bonus, although it serves only families with low or modest incomes, and will apply to other provinces’ income-tested child benefits and earnings supplements.

The fact that these contrasting characteristics of welfare and income-tested social programs are less tangible than such matters as benefit levels and design does not make them any less worthy of evaluation. As discussed in the section of this report on British Columbia, our research found that recipients of the BC Family Bonus view these characteristics of the new program as extremely valuable and contrast them to welfare. Evaluating the extent to which the National Child Benefit System meets the objective of promoting dignity and independence requires more than an accounting review of payments and economic analysis: Evaluators must ask recipients about their views and must undertake qualitative analysis. This requirement for qualitative evaluation should not be an impediment to explicit recognition of the objective of promoting dignity and independence, which may be one of the most important of all from a recipient’s perspective.

### *economic stabilization*

To the extent that child benefits maintain demand for goods and services during periods of economic downturn, such benefits may have a beneficial economic spin-off that should be weighed against their direct cost to the taxpayer. This advantage was one of the main reasons given for Family Allowances when that program was introduced in 1945. Economic stabilization, although less often recognized nowadays, remains a valid objective for the National Child Benefit System.

Low-income families have what economists call a ‘high marginal propensity to consume,’ meaning that they need to use every cent they get to meet their current needs. By contrast, wealthier families have a ‘high marginal propensity to save,’ meaning that much of their high incomes goes into savings. Because the new National Child Benefit System is geared to income, more will go to families whose income is falling in bad economic times, and they will spend the income, helping the economy to recover. Conversely, when the economy improves, incomes should go up and child benefits to low-income families should in total decrease relative to the economy as a whole, thereby decreasing demand for goods and services and helping to cool off the economy.

One of the challenges of a modern economy is to ensure that there are no sudden downturns or upturns in demand for goods and services. This goal is achieved partly by what are called ‘automatic stabilizers,’ namely programs like child benefits that increase demand when the market is down and dampen demand when the economy is going up. The National Child Benefit System, especially if it matures and increases in value as we recommend, can function as an important automatic stabilizer.

Measuring the economic effects of child benefits is no easy matter. But despite the difficulty of obtaining an objective evaluation, contributing to stabilization of the economy is a reasonable objective for the National Child Benefit System.

### **Keeping track**

In the preceding discussion, we identified a number of possible objectives for the new National Child Benefit System. To summarize, a broadly-based, integrated child benefit system should have the following objectives (not in order of priority):

- 1. anti-poverty** – reduce the depth of poverty among Canada’s low-income families, initially among the working poor and, over time, among families relying upon welfare.
- 2. fairness and reduce barriers to employment** – provide like treatment to families in like circumstances, especially equivalent child benefits to all low-income families, regardless of their source(s) of income, thus helping to break down the welfare wall that can discourage some parents from moving off social assistance and into the workforce.
- 3. adequacy** – over time, provide a child benefit sufficient for a low-income family to raise a child (e.g., \$4,000).

**4. reduce welfare caseloads** – over time, diminish the number of families on welfare by reducing the number going on and increasing the number leaving welfare.

**5. promote dignity and independence** – reduce bureaucratic interference in people's lives; diminish reporting requirements; and decrease the number of families on special programs outside the mainstream.

**6. simplify administration** – reduce administrative costs, complexity and duplication.

**7. economic stabilization** – stimulate demand when the economy is sluggish; reduce demand when the economy is growing too rapidly.

In proposing these seven objectives, we do not expect that they will be achieved in one or two years. Rather, we see these as goals to guide the development of the National Child Benefit System over the next several years, permitting Canadians to measure progress and keep a clear eye on the eventual destination.

To understand whether we are getting closer, or further away, from the realization of these objectives requires that they be translated into measurable standards so that they can be tracked objectively over time. But developing measurable standards for every objective of the National Child Benefit System is no simple task.

It seems self-evident in evaluating a program that only its effects, and not the effects of other causes all together, should be assessed. Yet in assessing the impact of many social programs, commentators often have been guilty of assessing the 'state of society' rather than the effects of the programs *per se*. The most glaring example of this error is the many critics, particularly in the US, who claim that social programs do not work because there is still a lot of poverty.

In Canada, the distribution of income remains highly unequal and has not improved despite the many billions of dollars spent on our various income programs. However, on further analysis, it turns out that income security programs are working much better than people believe in redistributing income and reducing income gaps: The problem is that market income is becoming more unequal, and income programs are just keeping up. If we want to evaluate the effectiveness of transfer programs, we have to understand what *they* are doing – not what is happening in society at large, where income programs are only one influence among many upon income distribution. Similarly, to evaluate social programs in general, it is *their* effects we have to analyze; to do so, these effects have to be isolated from the general background.

This means, for example, that we cannot evaluate the effect of child benefits on the poverty gap just by looking at changes in the poverty gap. The poverty gap may be increasing or decreasing for reasons that have nothing to do with child benefits. Instead, we must look at that part of the reduction in the poverty gap that stems solely from the larger child benefit. For this reason, general measures of social 'outcomes' (for example, a decrease in family break-ups) are not usually very helpful in evaluating the extent to which social programs like child benefits are meeting their objectives. Such general out-

comes are the consequences of many causes; we cannot gauge easily the effect of any single program, such as the child benefit, on such an outcome.

However, there are some exceptions to this rule. Where a carefully designed social experiment is undertaken, such as has been done for some interventions, a control group may be established where all other factors are held constant. In this circumstance, it is possible to isolate the effect of the program by looking at the differences in outcomes for the control group, which does not enjoy the benefits of the program, and the experimental group which does. A ‘natural’ control group also may be available where large databases allow researchers to apply sophisticated statistical techniques to estimate the relative effects of a number of different causes. We may, for example, be able to look at the effects of the BC Family Bonus on some more general outcomes using data such as that being developed by Statistics Canada’s National Longitudinal Survey of Children and Youth.

However, the complexity of evaluation does not stop there. There are both static and dynamic effects of programs. The static effects are what happens if we assume that there is no behavioural change as a consequence of the program, and we take a simple snapshot in time. For example, in measuring the impact of the National Child Benefit System on the poverty gap, a static analysis would look only at the amount of money going to low-income families through the child benefit and subtract that from the poverty gap. This was roughly the methodology used by the Mendelson report on the effects of the BC Family Bonus on poverty among working poor families (Mendelson 1997).

This approach is all right as far as it goes, but it does not take account of people changing their behaviour as a result of the new child benefit. For example, what about families that leave welfare and stay off as a consequence of the program? To capture this effect, one has to undertake a dynamic analysis that looks not only at the effects at a point in time, but at the changes over time as a result of the program. Of course, a dynamic analysis is much more difficult and the results are more easily subject to alternative interpretations.

Our purpose here is not to develop a detailed evaluation plan for the National Child Benefit System. Instead, we propose that a set of standards based on objectives be developed and that these standards be tracked and measured through careful analysis and research over time. In Table 1, we have attempted to illustrate what some of these standards might look like. The standards, which essentially are meant to measure progress in developing the National Child Benefit System, in turn should be distinguished from outcome measures (e.g., percentage of income from employment, correlates of poverty such as low birth weight, risk of wide range of illnesses, school drop-out rate and poor performance) which attempt to understand better the broader consequences of the various anti-poverty measures (including child benefits) and other potential causal factors. Outcome measures are, of course, of great interest. Measuring them will be an even more complex and challenging undertaking.

Who is going to do all this measuring? We would hope that, in the normal course of events, government would undertake internal tests and evaluations. However, it is unlikely that governments will be enthusiastic about promoting the results of the evaluations where these show they are making slow progress, or are downright negative. Moreover, even where results are positive, they are suspect if the research is being undertaken by an involved party.

We therefore propose the establishment of a funded independent body for the express purpose of tracking progress in developing the National Child Benefit System. This function could be vested in a Parliamentary institution – such as a national Ombudsman for children – or it could be undertaken by a non-governmental organization. A complementary approach would be to request Statistics Canada to develop a regular series of statistical reports meant specifically to measure progress in implementing child benefit reform.

**Table 1**  
**National Child Benefit System Evaluation - Objectives and Measures**

Objective	Measure
<b>anti-poverty</b>	a decrease in the poverty gap <i>attributable to the child benefit program</i> , where the poverty gap is measured as the amount of income needed for all families to be above the poverty line.
<b>fairness and reduce barriers to employment</b>	<p>i. according to the rules and regulations governing welfare in each province, a decrease in both the number of possible family situations, and the number of actual families, in which those on welfare can get higher net income plus benefits than the working poor just as a consequence of welfare and associated benefits paid due to the presence of children in the family.</p> <p>ii. according to the rules and regulations governing child benefits, a decrease in the number of situations in which families of the same structure with equal available incomes do not get equal child benefits, and a decrease in the number of such families (net income and family definition issues).</p>
<b>adequacy</b>	the extent to which the maximum child benefit is adequate for a low-income family to meet the incremental costs of raising a child (we have used a conservative estimate of \$4,000, but this issue deserves more investigation and refinement).
<b>reduce welfare caseloads</b>	econometric analysis of what welfare caseloads would have been in the absence of the initiative (not simply an analysis of whether caseloads are up or down, as this trend will be due mainly to other factors such as unemployment levels).
<b>promote dignity and independence</b>	assess the number of special forms, reports or requirements of poor and modest-income families compared to others and undertake qualitative research (focus groups, surveys) of satisfaction with the system.
<b>economic stabilization</b>	this is the most difficult of the objectives to measure: would require special econometric analysis and would doubtless be subject to many interpretations.



## **EVALUATING THE CURRENT AND EMERGING CHILD BENEFIT SYSTEMS**

This section assesses the current and emerging child benefit systems according to the evaluative criteria set out in the previous section.

By 'current' child benefits, we mean the federal Child Tax Benefit/Working Income Supplement and provincial welfare benefits (and other child benefit programs offered by a few provinces) payable in cash on behalf of children. We have not included in our study the various provincial income tax reductions, sales tax credits, child care and in-kind benefits (e.g., supplementary health care) payable on behalf of children, which are not part of the child benefit system *per se*.

The National Child Benefit System is emerging from the current child benefit system. The federal government is phasing in over two years its recently-announced reconfiguration of the current Child Tax Benefit, the Canada Child Tax Benefit. However, the Canada Child Tax Benefit's initial program parameters are temporary, in that they should be the first stage of an evolving program. And the provinces and territories also are at different stages in the evolution of their child benefits: Some have announced or initiated major new programs, but others have yet to make public how they intend to reinvest their welfare savings from the increased federal child benefit in other programs for low-income families with children. Similarly, although British Columbia brought in the BC Family Bonus in 1996, its parameters also will have to change as the federal child benefit system evolves, so it too is part of an emerging system.

Applying evaluative criteria to a system in change is not a simple task. Does one evaluate the system as it is, or as it will be? Our choice at this point is to compromise by applying the evaluative criteria we have developed to both the current system and the system as it has been *announced* to date. The latter imposes limitations. Clearly, it is not possible to review, for example, Saskatchewan's planned provincial child benefit initiative when no details have been released. Moreover, empirical evaluation is not possible until there has been a program in place long enough to assess, at least in a preliminary way, the data and other evidence that have been collected. For this reason, we cannot evaluate the emerging system's performance on evaluative criteria such as 'reducing welfare caseloads' that require actual results.

In sum, we can offer only a very preliminary and speculative assessment of some new provincial child benefit reforms, other than BC's Family Bonus (which we discuss at length in the next section). We assess the Canada Child Tax Benefit as announced in the 1997 federal Budget, although we hope and expect that some of the program's parameters will be changed prior to implementation – not least, to deal with some of the weaknesses we point out in this report. First, however, we apply our evaluative criteria to the current child benefit system.

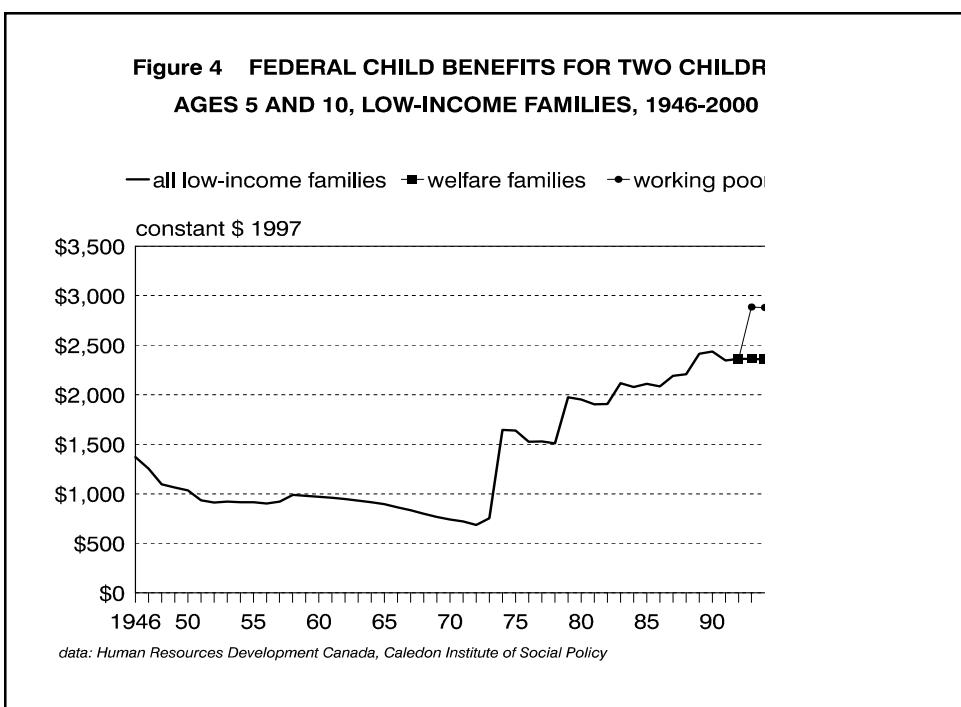
## The current child benefit system

### *adequacy*

#### a. benefits

Over the long term, the federal government has substantially boosted child benefits for low-income families. Figure 4 illustrates the value of federal child benefits from the creation of Family Allowances to the current Child Tax Benefit and the new Canada Child Tax Benefit announced in the 1997 federal Budget. The example is a low-income family with two children, one under and one over age 7; however, the trends are similar for families with different ages and numbers of children. Child benefits include past programs (Family Allowances and the refundable child tax credit), the current Child Tax Benefit/Working Income Supplement and the new Canada Child Tax Benefit. The children's tax exemption and its successor, the non-refundable child tax credit, are not included because no trend data are available for them. In any case, the children's tax exemption provided little or no benefit to most low-income families and the non-refundable child tax credit was worth only \$65 in federal income tax savings per child per year for families owing income tax (i.e., the value to low-income recipients of the children's tax exemption).

Despite the social policy termite of partial deindexation, since the war the federal government has improved child benefits for low-income families. In 1946, Family Allowances for a family with two children were worth \$1,371 in inflation-adjusted 1997 dollars; in 1996, the Child Tax Benefit paid \$2,792 for working poor families and \$2,285 for other poor families (e.g., those on welfare or Unemployment Insurance). Between 1946 and 1996, benefits for working poor families increased by \$1,421 or by 104 percent in real terms (i.e., adjusting for the impact of inflation) and by \$914 or 67 percent for other low-income families.

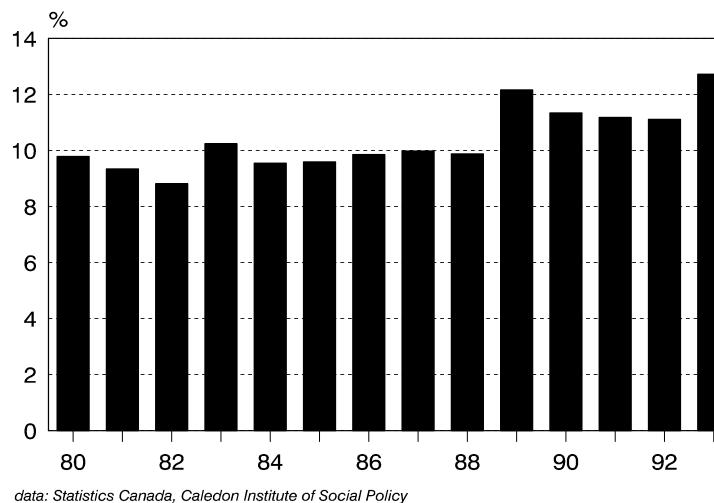


However, since 1945 per capita GDP has grown by about 300 percent in real terms, so Ottawa's contribution to child benefits has not kept pace with economic growth over the whole period since the Second World War. Federal cash benefits for all families with children were substantially boosted and fully indexed in 1974, but subsequent increases focussed mainly on low- and modest-income families at the expense of middle-income and upper-income families, which have experienced substantial losses in their child benefits since the mid-1980s.

Consistent long-term time series data on provincial welfare benefits for children comparable to federal programs are not available. However, National Council of Welfare estimates of the value of welfare benefits show a decrease in half the provinces between 1992 and 1995 and in all but one province between 1994 and 1995. These data reflect only one month's worth of the 21.6 percent cut in benefits which Ontario made in December of 1995, which certainly will show up in the 1996 figures (National Council of Welfare, 1997). While some provinces have made overt reductions in benefits in recent years, in most cases governments have harnessed inflation to erode the value of unindexed welfare benefits and thus trim costs.

Federal child benefits for low-income families have improved in real terms over time, but still make a limited contribution to their incomes. Figure 5 plots the trend in maximum benefits for two children expressed as a percentage of the average income of two-parent working poor families. The child benefits are Family Allowances and the refundable child tax credit from 1980 to 1992, and the Child Tax Benefit and Working Income Supplement since 1993. Federal child benefits represented 9.8 percent of their average income in 1980 and 12.8 percent in 1995.

**Figure 5 FEDERAL CHILD BENEFITS FOR 2 CHILDREN, AS A  
AVERAGE INCOME, WORKING POOR COUPLES, 1980-1**



Welfare families also receive provincial child benefits, mainly in the form of social assistance benefits for children. Benefits vary from around \$1,200 to \$1,800 per child in the majority of provinces, not including shelter-related benefits. Combined federal and provincial/territorial child benefits range from around \$2,220 to \$2,820 per child. With the additional \$213 a year in federal benefits for each child under 7 for whom child care expenses are not claimed, combined federal and provincial/territorial child benefits for children in welfare families range from \$2,433 to \$3,033.

Child benefits for low-income families not on welfare (i.e., mainly the working poor) fall considerably short of our \$4,000 per child target for a mature system. For a working poor family with one child under 7, maximum federal child benefits come to \$1,733 or 43 percent of the estimate of raising a child. With two children (one under and one over 7), benefits amount to \$2,753 or just 34 percent of the assumed cost of raising children: The percentage drops because the Working Income Supplement is the same maximum \$500 no matter how many children there are in the family. Welfare families fare considerably better when it comes to child benefits, though there is still a gap between benefits and child-rearing costs: For a welfare family, combined child benefits for one child under 7 range from 61 percent to 76 percent of the estimated cost of raising a child.

#### b. indexation

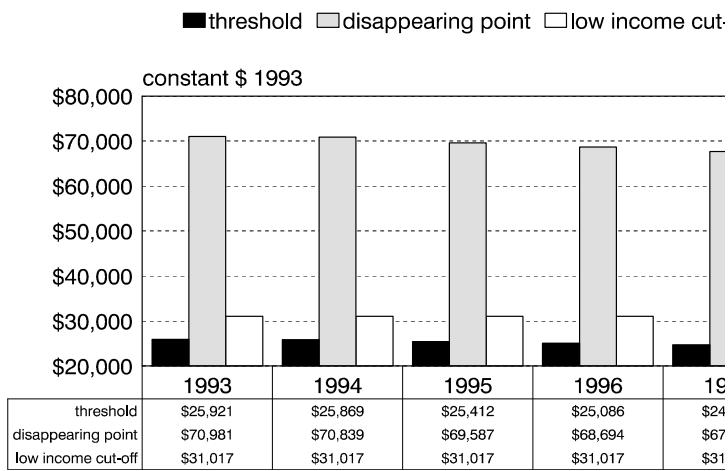
Working in opposition to increases in federal child benefits for low-income families in the mid-1980s was the change from full to partial indexation in 1985. Partial deindexation results in an ever-changing child benefit system that does not perform in practice the way government portrays it in theory.

Under the current indexation formula (inflation over three percent), if inflation runs three percent or more, the value of child benefits falls by three percent. If inflation is less than three percent, child benefits' value declines by an amount equal to the inflation rate. Moreover, the 'threshold' for the Child Tax Benefit – the level above which maximum benefits are reduced gradually according to income – is also partially indexed. Each year, the income threshold for maximum benefits declines, which means that fewer low-income families qualify for the maximum amount. At the other end of the income spectrum, partial deindexation causes a steady decline in the 'disappearing point' – i.e., the income level above which families do not qualify for any Child Tax Benefit. These changes are arbitrary, unrelated to the purpose of child benefits and seem to have the sole purpose of saving government costs by cutting benefits in a stealthy way that few people understand.

Figure 6 shows the decline in both the income threshold and the disappearing point for the Child Tax Benefit from 1993 to 1997, using the case of families with two children (one under 7, the other 7-17). In constant 1993 dollars, the threshold fell from \$25,921 in 1993 to \$24,715 in 1997. The low income cut-off for a family of four living in a metropolitan centre in 1993 was \$31,017, so the threshold for the maximum Child Tax Benefit fell from 83.6 percent of the low income line in 1993 to 79.7 percent in 1997. The disappearing point for benefits also declined, from \$70,981 in 1993 to \$67,679 in 1997.

The power of partial deindexation derives from a version of the 'miracle of compound interest.' Even when inflation is low, over time partial deindexation increasingly reduces the value of benefits and lowers both the threshold for maximum benefits and the disappearing point. Partial deindexation of the

**Figure 6 CHILD TAX BENEFIT THRESHOLD AND DISAPPEARING TWO CHILDREN (ONE UNDER 7, ONE 7-17), 1993-1997**



*data: Caledon Institute of Social Policy*

Child Tax Benefit is estimated to save the federal government \$170 million a year [Canadian Council on Social Development 1997: 3].

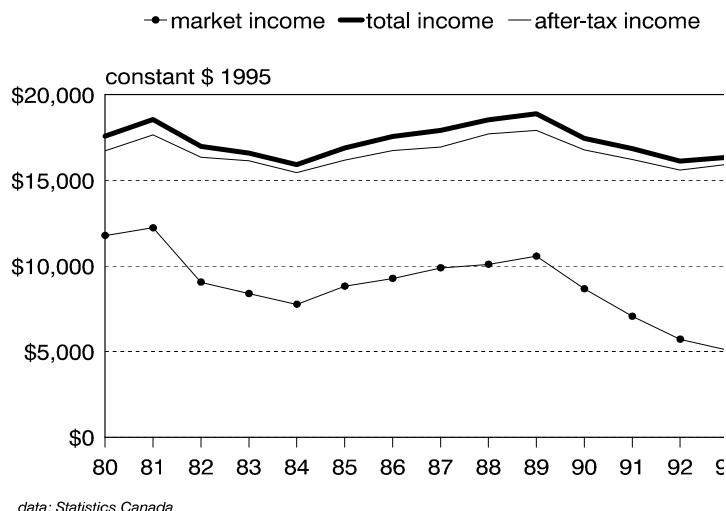
Though provincial welfare benefits vary, in all cases they are not indexed, not even partially. Lack of indexation amounts to an automatic, invisible built-in reduction in welfare benefits – including benefits for children – equal to the rate of inflation.

### *anti-poverty*

We do not have direct evidence of the impact of child benefits on the depth of family poverty over time. However, there is indirect evidence to suggest that child benefits have played an important role in easing the decline in low-income families' incomes as market income inequalities have widened in recent years.

Figure 7 traces the trend between 1980 and 1995 in the average income of families with children which are in the bottom income quintile – in 1995, those with total incomes under \$26,401. Average market income (i.e., income from employment, savings and investments, private pensions and other private sources) declined considerably from \$10,565 in 1989 to \$6,306 in 1995 – a hefty loss of \$4,350 or 41 percent in real terms, though there has been a slight recovery since 1993. But income security programs, which include child benefits, substantially improve the incomes of low-income families and help offset the decline in market income. Total income – i.e., market income and cash benefits from

**Figure 7 AVERAGE INCOME, FAMILIES WITH CHILDREN  
BOTTOM QUINTILE, BY DEFINITION OF INCOME, 1980-1995**

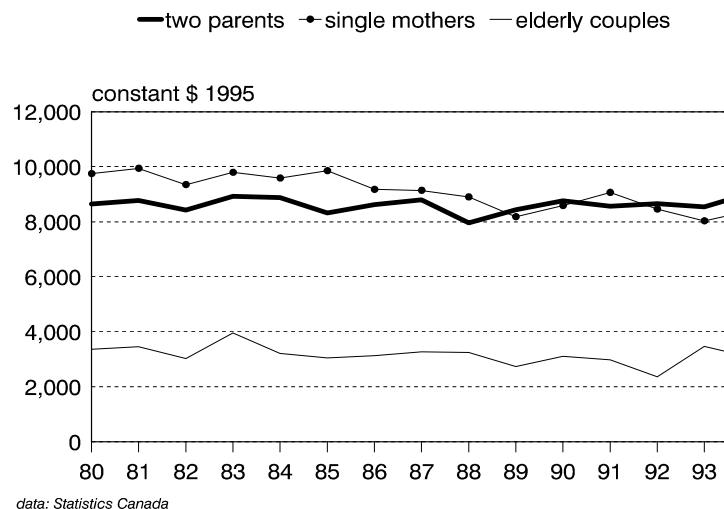


social programs – also declined, from \$18,895 in 1989 to \$16,579 in 1995, but less in both absolute and relative terms than market incomes – by \$2,316 or 12 percent. (All figures are expressed in inflation-adjusted 1995 dollars.) The data do not permit an estimate of the contribution of child benefits to income from social programs, but the improvement in federal child benefits over time must have played a positive (albeit unquantifiable) role.

We also know that the depth of poverty among families with children has remained roughly constant over the years. In 1980, the average low-income two-parent family with children fell \$8,643 below the low income cut-off; in 1995, the average was \$9,298. The comparable figures for female-led one-parent families are \$9,945 and \$8,345, showing modest improvement. Figure 8 plots the trends. Since we know that market incomes have declined considerably among low-income families, then income security benefits have largely made up the difference. Again, we cannot make any definitive statement about child benefits' contribution, except that we do know that they have increased while welfare benefits have declined in several provinces and Unemployment Insurance has undergone several bouts of belt-tightening in the 1990s.

Federal child benefits have increased modestly as a percentage of the average income of working poor families, which have enjoyed larger increases than other low-income families because of the Working Income Supplement (albeit at a \$500 maximum payment per family, a very modest increase). Provincial child benefits, mainly welfare, have had a mixed record, with both increases and decreases between 1986 and 1995 depending upon the particular province. Overall, Canada's child benefit system has helped cushion the impact of falling market incomes and thus helped prevent the depth of poverty from significantly worsening.

**Figure 8 AVERAGE DEPTH OF POVERTY, FAMILIES WITH CHILDREN AND ELDERLY COUPLES, 1980-1995**



### *fairness and reduction of barriers to employment*

#### a. the welfare wall

Although working poor families receive larger federal child benefits than families on welfare, most welfare families still end up with more *total* child benefits once welfare payments on behalf of their children are included. As well as regular cash benefits, welfare families in some provinces may be eligible for special assistance for their children, such as a winter clothing allowance, as well as supplementary health-related benefits.

Take the generic example of child benefits for families with two children (one under and one over 7) in 1996. We use \$1,500 for each child as a rough average for welfare benefits. On the federal side, the maximum Child Tax Benefit is \$2,253 (\$1,233 for the younger child and \$1,020 for the older child) and the maximum Working Income Supplement is \$500 per family. Adding welfare benefits for children to the federal Child Tax Benefit, total benefits for the welfare family amounted to \$5,253 – close to double the \$2,753 worth of federal benefits (\$2,253 from the Child Tax Benefit and \$500 from the Working Income Supplement) available to a working poor family with two children which could have the same or even less total income than the welfare family.

Actual figures confirm the existence of the marked differential in child benefits between welfare and working poor families. Before the BC Family Bonus was introduced in July 1996, a welfare family with two children 7 and 11 got \$4,725 (\$2,253 from the federal Child Tax Benefit and \$2,472 from BC

income assistance) as opposed to a maximum \$2,753 for a working poor family – or 1.7 times as much – even if their total incomes were the same.

Child benefits form part of what the Caledon Institute of Social Policy has called the ‘welfare wall.’ Parents who leave welfare for the labour force take some serious risks which can place a barrier in their way of taking paid work. They forfeit a significant amount of income – thousands of dollars in the case of two or more children – in lost welfare payments on behalf of their children. Their job may not pan out, or may not survive in the unstable economy of our time which is both creating and killing jobs at a rapid rate. They have to come up with money for work-related expenses such as clothing and transportation. Even if (as is often the case) they can find only low-paid and/or part-time job(s), their take-home pay is reduced by income taxes, Canada Pension Plan or Quebec Pension Plan contributions and Employment Insurance premiums. Single parents and couples in which both parents leave welfare for work must find affordable and decent child care. Families often give up some valuable benefits when they leave social assistance – a relatively stable (albeit low) income, supplementary health care and prescription drugs, as well as welfare benefits on behalf of their children.

This differential treatment is unfair. Working poor parents struggle to raise their families on low-wage, unrewarding and often unstable jobs. Unequal child benefits act as a discouragement in two ways – to leave welfare for the labour force and to remain in the workforce. This is not to say that welfare families ‘have it good’ – a popular misconception easily disproved by talking to welfare recipients or by consulting the annual report on welfare incomes published by the National Council of Welfare. Nor are we arguing that provincial child benefits are the only reason that families remain on welfare; lack of jobs and child care are two common problems. But there is no justification for a two-tier child benefit system that puts financial barriers in the way of parents who do have an opportunity to obtain employment.

#### b. net versus gross family income

Another test of fairness is that the child benefit system should provide equal benefits to recipient families with equal income. The present federal Child Tax Benefit/Working Income Supplement is flawed in this respect because it calculates eligibility for and amount of benefits on the basis of net rather than total family income. ‘Net family income’ means ‘gross income’ (i.e., income from wages and salaries, self-employment, savings and investments, private pensions, social programs and other sources) minus a variety of deductions including contributions to Registered Pension Plans and RRSPs, child care expenses, union and professional dues, attendant care expenses, certain employment expenses, carrying charges and interest expenses, business investment losses, moving expenses and alimony or maintenance payments (though no longer for children) and investments in oil, gas or mining ventures.

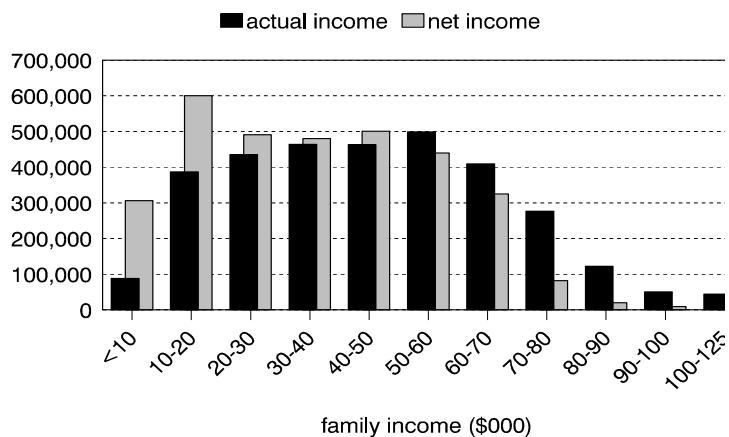
The net family income definition results in both vertical and horizontal inequities in the distribution of child benefits. A number of the deductions allowed for net income are very much the preserve of well-off taxpayers and provide little or no benefit to low- and modest-income Canadians. Such deductions can enable some upper-income families to reduce substantially their income for Child Tax Benefit purposes so that they end up with similar payments as middle-income families; some non-poor families get the same maximum benefit as poor families. Families with the same total income receive different child benefit payments depending on how much money they are able to deduct to reduce their net income.

The effect of the net family income definition is not trivial. The current Child Tax Benefit pays \$3.7 billion to families with incomes over \$25,000 (close to the \$25,921 threshold), which amounts to a sizable 72 percent of total (\$5.1 billion) expenditures. If the program calculated benefits on the basis of total income, only \$2.6 billion would go to families above \$25,000, meaning the maximum benefit and perhaps even the threshold could be increased.

Figure 9 compares the number of families which receive the Child Tax Benefit based on the current definition of income (i.e., net income, after deductions) and families' actual income (i.e., total income, before deductions). Families which receive the Child Tax Benefit are more evenly distributed throughout the income range when we look at their actual as opposed to net income. Many more families with incomes above \$50,000 receive the Child Tax Benefit when we look at their actual income – 1,423,721 – than according to their net income – 882,797. The reason for this large difference is that the current system allows middle-income and upper-income families to claim deductions which reduce their income, sometimes considerably. Some well-off families which otherwise would not qualify for any Child Tax Benefit in fact do receive partial benefits, and other families which would receive some benefits even under our preferred definition receive larger benefits under the current system.

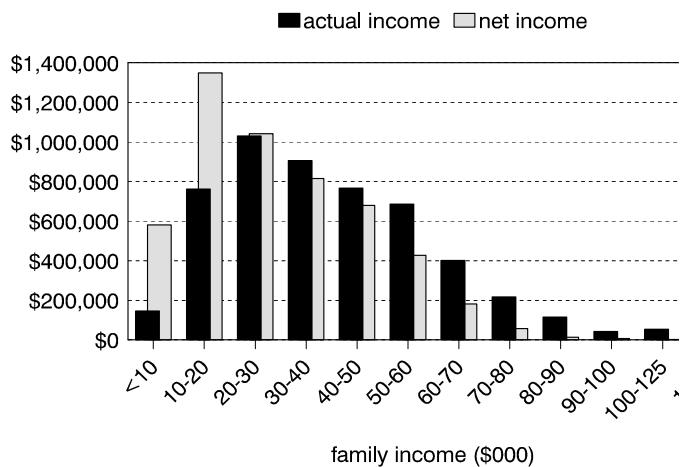
Figure 10 gives the total amount of Child Tax Benefit payments by income level using the net and actual income definitions. Figure 11 shows the percentage distribution of Child Tax Benefits by income level (i.e., each income group's share of total benefits). The distribution of benefits is more progressive than the distribution of families because the Child Tax Benefit gears the amount of benefit to family income. Nevertheless, non-poor families receive substantial amounts of Child Tax Benefit, particularly when we take into account their actual as opposed to net income.

**Figure 9 NUMBER OF ALL FAMILIES WITH CHILD TAX BENEFIT, BY NET AND ACTUAL INCOME, 1996**



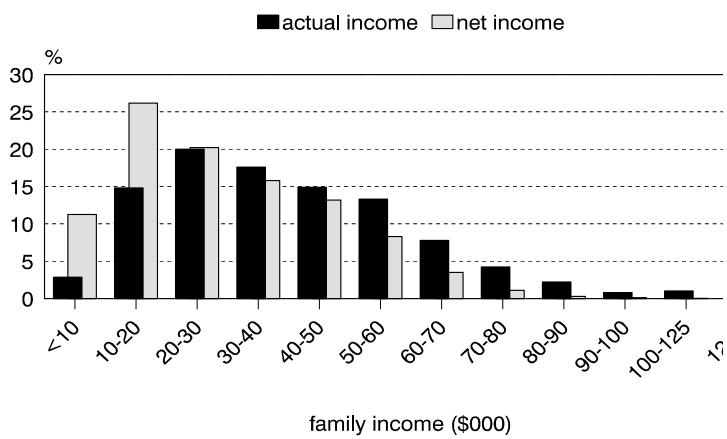
*data: Human Resources Development Canada*

**Figure 10 TOTAL CHILD TAX BENEFIT PAYMENTS,  
ALL FAMILIES, BY NET AND ACTUAL INCOME, 1996**



*data: Human Resources Development Canada*

**Figure 11 % DISTRIBUTION OF CHILD TAX BENEFIT PAYMENTS:  
ALL FAMILIES, BY NET AND ACTUAL INCOME, 1996**



*data: Human Resources Development Canada*

### c. the Working Income Supplement and the welfare wall

When the federal government introduced the Child Tax Benefit in 1993, it created a special benefit for working poor families called the Working Income Supplement. The Working Income Supplement was intended to help offset the cost of going to work for low-income families, and thus lower the welfare wall to some extent.

At a maximum \$500 per family, the Working Income Supplement makes only a modest contribution to the incomes of working poor families with children – not enough in itself to have much influence in convincing parents on welfare to risk joining the labour force at a possible loss of income, or working poor parents to stick with a low-paid job that can leave the family worse off than if it were on welfare. Moreover, the Working Income Supplement does not arrive until the year after a welfare parent joins the workforce, which means it is not available during the family's difficult early months off welfare. It is a 'retrospective' incentive program.

Because the Working Income Supplement is paid on a per family rather than per child basis, it is worth more in relative terms to small families and less to larger families. This feature diminishes further its capacity to offset part of the loss of welfare benefits paid on behalf of children for families moving from welfare to the paid labour force.

Not only is the Working Income Supplement modest in value, but it is also relatively invisible to its recipients. The Working Income Supplement is delivered as part of the Child Tax Benefit, and the calculations for both benefits are done by the federal government. It is difficult to imagine the Working Income Supplement acting as an incentive to work if its recipients do not know they are getting the benefit or for what reason.

There also is a conceptual confusion at the heart of the Working Income Supplement, having to do with its basic purpose. Is it meant to provide an incentive for people to work or is it meant to provide additional income to the working poor? Or is it intended to do both?

If the Working Income Supplement is meant to be an incentive, it is an expensive instrument. Almost all the people getting the Supplement surely would have been working anyway: Its effectiveness as an incentive must be measured in the *additional* number of people working who would not otherwise have done so. This is no doubt a small number, making the program quite costly for any extra impact it may have. For most of its income range – from \$10,000 to \$20,921 – the Working Income Supplement remains the same (\$500 per family annually between 1993 and 1996), so it does not reward families in this broad income group which increase their earnings.

In any case, if a fully integrated child benefit is in place (as it is in BC), anyone working full time already has more income than someone on welfare, so the additional 'incentive' of the Working Income Supplement is relevant only for people working part time who would not otherwise have done so. This is undoubtedly a very small number of families.

If, on the other hand, the purpose of the Working Income Supplement is to provide the working poor with additional income, it is a strangely designed program. It pays less in absolute terms to work-

ing poor families with low earnings than to working poor families with higher earnings. This is not a sensible design for a program whose goal is to increase the incomes of families with low earnings.

The argument for programs like the Working Income Supplement came from the United States, which operates a similar program called the Earned Income Tax Credit. But the situation in the United States is quite different than in Canada. Generally, American minimum wages are much lower and there is greater income disparity. Moreover, the US has nothing like our child benefit system.

The federal government announced in the 1997 Budget that it would phase out the Working Income Supplement as of 1998. In 1997, the Working Income Supplement changes from a per-family (maximum \$500) to a per-child payment (maximum \$605 for the first child, \$405 for the second child and \$330 for the third and each additional child). In 1998, the new Canada Child Tax Benefit will replace both the Canada Child Tax Benefit and Working Income Supplement and will deliver the same maximum payment (\$1,625 for the first child and \$1,425 for each additional child) to all low-income families with children, regardless of their source(s) of income.

#### *promote dignity and independence*

Canada's current child benefit system has a mixed record on this criterion. Welfare is an essential income safety net which has helped millions of disadvantaged Canadians over the decades, but it is a tangled and fraying safety net. Needs-tested welfare imposes an intrusive, exhaustive and complex test of applicants' resources and needs, and recipients' circumstances are monitored continually. It remains the most reviled of all social programs and thus stigmatizes its beneficiaries – both in their eyes and the public's. Welfare tends to place its beneficiaries in a dependent and subservient position which exacerbates their social and economic marginality.

By contrast, the income-tested federal Child Tax Benefit/Working Income Supplement uses the income tax system to assess applicants' eligibility for and amount of benefits, and does so in a simple, anonymous and impersonal manner which does not stigmatize or demean its beneficiaries; it tests only a few key characteristics including net family income, number and age of children and use of the child care expense deduction. Unlike welfare, the Child Tax Benefit involves little or no direct contact between recipients and administrators. As noted earlier, the Child Tax Benefit does not investigate how families spend their benefits, but rather assumes and expects parents to spend the money appropriately. It respects families' privacy and parents' primary responsibility for their children. Whereas welfare is restricted to only one group among the poor, the Child Tax Benefit is a mainstream program which serves the large majority of families with children (eight in ten). The same advantages can be claimed for the income-tested BC Family Bonus, described later.

#### *simple and efficient administration*

Although federal child benefits have been rationalized to a considerable extent, the system as a whole – federal and provincial – remains largely uncoordinated, complex and highly variable. Families in similar circumstances can be treated quite differently. Administrative costs are higher than they would

be under a wholly income-tested system. Some child benefits are more responsive to changes in families' economic circumstances than others.

The federal Child Tax Benefit and provincial social assistance programs use different definitions of common-law status, which can result in some families being administratively defined as single-parent by one program and a couple by another program, thus affecting their eligibility for and amount of benefits. A family claiming refugee status is not eligible for the Child Tax Benefit but may be eligible for provincial welfare. Some families which might be eligible for social assistance do not apply because of the stigma attached to welfare, and so forgo this source of income support for their children and receive federal child benefits only.

One of the advantages of provincial welfare over federal child benefits is that the former responds quickly to changes in family circumstances, whereas the latter is slow to respond. A family which suffers a major loss of income can apply for welfare and, providing it meets the needs test, receive immediate assistance; the family's circumstances are monitored closely and regularly once it goes on welfare, so that an increase in income as a result of part-time earnings will quickly trigger a decline in welfare benefits. However, eligibility for and the amount of benefits from the Child Tax Benefit/Working Income Supplement are based on last year's income as assessed through the income tax form.

The Child Tax Benefit's slower responsiveness to income changes has one advantage. A family which receives the maximum benefit but then experiences an increase in income (e.g., due to finding a job, winning a promotion or pay increase) will continue to receive the larger Child Tax Benefit until its income is assessed in the next tax form. This lag constitutes a *de facto* earnings supplement which can help offset employment-related expenses for a parent who finds work.

The income-tested part of Canada's child benefit system is much cheaper to administer than the highly labour-intensive welfare benefits on behalf of children. Welfare administration costs from about 5 to 7 percent of total program costs (Mendelson 1979), while income tax-administered benefits require about 1 percent of total program costs, judging by the amounts charged to administer the BC Family Bonus. The current system is thus more expensive to operate than a totally income-tested child benefit system.

#### *economic stabilization*

A major argument in favour of Family Allowances among wartime social planners, the economic stabilization objective of child benefits is rarely heard today. Yet it is still a relevant aim, and is important to assess as part of the cost-benefit calculus of child benefits.

In the absence of the required econometric studies, we can only speculate on the current child benefit system's performance according to the economic stabilization criterion. On the plus side, as noted in the section on the evaluation framework, lower-income families are the most likely of all income groups to spend all of their limited income. This economic tenet, coupled with increases in federal child benefits for low-income families in the mid-1980s and in 1993 (though the latter only for the working poor), might suggest that the child benefit system more effectively achieves the economic

stabilization objective. The income-tested Child Tax Benefit pays more to the rising number of lower-income families in bad economic times, which in turn spend their benefits and thus help economic recovery. The same can be said for welfare expenditures, which also increase during recessions. And when the economy improves, incomes should go up and federal and provincial child benefits to low-income families should decrease relative to the economy as a whole, thereby reducing demand for goods and services and helping to cool off the economy.

On the other hand, a substantial amount of money was removed from the federal child benefit system as a result of various changes in the 1980s which reduced payments to middle- and upper-income families, as well as partial deindexation which gradually lowers benefits for all recipients. These losses to some extent must have offset improvements to the child benefit system's economic stabilization performance resulting from increased payments to low-income families with children.

## **The emerging child benefit system**

### *adequacy*

#### a. benefit levels

In 1998, the new Canada Child Tax Benefit will pay a maximum \$1,625 for the first child and \$1,425 for the second and each additional child, while retaining the \$213 supplement for each child under 7 for whom child care expenses are not claimed. Working poor families will see increases in their child benefits which rise with the number of children because the per-family Working Income Supplement is being replaced by a per-child larger basic child benefit. Working poor families' child benefits will be \$105 or 6.9 percent more than under the current Child Tax Benefit/Working Income Supplement for families with one child, \$510 or 20.1 percent more for two children, \$840 or 23.1 percent more for three children and \$1,170 or 24.7 percent more for four children. However, for working poor families, the Canada Child Tax Benefit still will leave a considerable gap between child benefits and the cost of raising a child. For example, a working poor family with two children (one under and one over 7) will receive a maximum \$3,263 Canada Child Tax Benefit, which is only 41 percent of our posited cost of raising two children (\$8,000).

Welfare families will not be better off in cash terms under the Canada Child Tax Benefit because provinces will be allowed to deduct the amount of the larger federal child benefit from child-related welfare benefits. On average, then, welfare families will continue to receive roughly \$2,500 per child or 63 percent of the estimated cost of raising a child.

The Canada Child Tax Benefit is the foundation but not the whole of the National Child Benefit System, whose development hinges on complementary actions on the part of the provinces and territories. The nature of provinces' reinvestments is expected to vary a good deal. Some provinces plan to deliver cash transfer payments to low-income families in the form of income-tested child benefits and/or earnings supplements, while others will reinvest in child-related services such as child care or may extend in-kind benefits such as supplementary health care to the working poor.

The welfare wall can be lowered by providing services as well as cash transfers, although these are quite different kinds of social program, as discussed in the next section. While we are not arguing that income programs are superior to services, we do believe that the National Child Benefit System must progress quickly to reach the replace-welfare-for-children level (\$2,500) and thereafter be raised higher to reach the \$4,000 mark by early in the next century. The best way to guarantee these targets is for the federal government to enrich the Canada Child Tax Benefit appropriately in the coming years. However, in the short run, progress will be faster in provinces which supplement the federal Canada Child Tax Benefit with a provincial integrated child benefit – i.e., an income-tested program replacing welfare benefits on behalf of children and extending coverage to all lower-income families with children.

In BC, depending upon the extent to which the full increment in the federal benefit is passed on, combined payments from the BC Family Bonus and the Canada Child Tax Benefit could be as much as \$3,074 for the first child under age 7 for all lower-income families (whether working or on welfare), or 77 percent of the \$4,000 target. Saskatchewan presumably will be in a somewhat similar position when it announces details of its income-tested child benefit and employment earnings supplement, depending upon their level of benefits.

Alberta is going the earnings supplement route. The Alberta Family Employment Tax Credit is worth a maximum \$500 per family in 1997 and \$1,000 per family in 1998. This provincial initiative will bring maximum combined federal-provincial child benefits to \$2,838 in 1998 for a family with one child (under 7) or 71 percent of the \$4,000 target, though only for families with earned income in the maximum range. To date, Alberta has not announced plans to create an integrated child benefit, in the sense of replacing its welfare payments on behalf of children with an income-tested child benefit for all low-income families. However, the Alberta Family Employment Tax Credit will substantially close the child benefits gap between welfare and working poor families and thus will lower the welfare wall considerably. Combined federal-provincial child benefits for welfare families will remain as they are under the current system – about \$3,000 for a child under 7.

As described in more detail earlier, Quebec's new family allowance program pays two-parent families up to \$975 a year each for the first and second child and \$398 for each additional child; in addition to these rates, single-parent families also receive a supplementary benefit worth up to \$1,300 a year. Moreover, working poor families in Quebec are eligible for the Parental Wage Assistance Program, which pays a maximum annual benefit of \$3,534 for two-parent families and \$2,422 for single-parent families.

Combined maximum payments from the Canada Child Tax Benefit and Quebec's new family allowances for two-parent families with one child under 7 will total \$2,813, which is 70 percent of our \$4,000 target for a mature child benefit system; counting the child income tax credit, the amount is \$3,333 or 83 percent of the target. Some working poor two-parent families with one child under 7 qualifying for the maximum Parental Wage Assistance benefit could receive as much as \$6,867, which is considerably above our \$4,000 target.

New Brunswick has announced its own versions of the federal Child Tax Benefit and Working Income Supplement. The New Brunswick Child Tax Credit and Working Income Supplement will provide modest benefits – a maximum \$250 per family per year for each program – and so will neither replace welfare benefits on behalf of children nor substantially supplement the level provided by federal child benefits. But New Brunswick’s new programs are an important step forward and will furnish the necessary platform for an enriched provincial child benefit system in future.

b. a note on reinvestment: income versus services

The reinvestment framework poses a challenge to policy-makers, evaluators and advocates alike. Ideally, measuring progress toward the National Child Benefit System should investigate all the different programs, services and in-kind benefits which receive funding under the reinvestment formula. However, these are apples and oranges programs that vary widely in purpose, design, clientele and impact. At the very least, their diversity and number will complicate evaluation.

It is one thing to evaluate child benefits in the usual sense of the term – i.e., income programs which provide cash or income tax savings and share common elements of design and purpose. But it is quite another to assess the performance of a ‘system’ composed of a mixture of cash benefits, income in-kind and social services that, to complicate matters even more, varies from one province to another.

Income benefits are a different animal from services and in-kind benefits. The chief difference is that cash child benefits are paid to all low-income families each month, their essential purpose being to deliver a stable and regular income supplement to help parents provide generally for the needs of their children. However, services (such as child care) and in-kind benefits (such as supplementary health and dental care and subsidized or free prescription drugs) are used by only some families and usually on an episodic or time-limited basis. Low-income families should not be expected to use their child income benefits to pay for the services and in-kind benefits that are to be provided for separately by other programs.

In fact, the only thing that really makes the National Child Benefit System a ‘system’ is the agreement between the two levels of government that the provinces will spend federally-enabled savings on welfare benefits for children on programs and services for low-income families. The boundaries of such programs and services currently are being negotiated but doubtless will be defined broadly and flexibly. At the very least, evaluation can monitor provincial governments’ allocation of welfare savings and ensure that the money does go to acceptable children’s programs. But it is not at all certain that the National Child Benefit System can be perceived and evaluated as a system rather than simply a loose collection of programs and services with varying purposes and content. The only guidance provided so far has been the statement in the 1997 federal Budget paper that such programs should be “targeted at improving work incentives and supporting children in low-income families” [Department of Finance Canada 1997: 19]. Policy-makers will have to put meat on these bones before evaluators can assess the performance of the National Child Benefit System.

We believe that income benefits and social services for families should work together. An integrated child benefit must provide an adequate basic income floor for all low-income families with chil-

dren. Social services and in-kind benefits, in turn, serve groups within the low-income population and will function more effectively if a firm foundation of income support exists.

c. adequacy of child benefits for non-poor families

Aside from the anti-poverty objective, child benefits also are supposed to serve non-poor families in pursuit of the horizontal equity objective – i.e., helping offset the cost of raising children so that such families will be (somewhat) less worse off financially than childless households at the same level of income. To our knowledge, there never have been any standards by which to gauge the adequacy of child benefits paid to non-poor families, so it is difficult to evaluate the system's performance in terms of this long-standing but vaguely-defined objective.

A lower-middle-income family with two children (one under 7, one 7-17) and net income of \$30,000 (about half the \$62,082 average income for a two-parent family headed by someone under 65) gets \$2,049 from the current Child Tax Benefit and will receive the same amount from the new Canada Child Tax Benefit. However, an average-income family with two children and net income of \$60,000 gets federal child benefits worth only \$549, which is modest by any standard.

Our analysis shows that middle-income and well-off families have lost substantial amounts of child benefits as a result of the various changes since 1985. However, this round of child benefits reform will leave non-poor families with the same level of benefits as they currently receive.

On the other hand, the Canada Child Tax Benefit will remain partially deindexed. This feature gradually will weaken, through stealth, the federal child benefit system's capacity to achieve the horizontal equity objective for non-poor families, as benefits erode in value and the disappearing point falls steadily each year.

d. indexation

The emerging child benefit system is jeopardized by the continuing lack of adequate indexation. Like the present Child Tax Benefit, the Canada Child Tax Benefit presumably will be only partially indexed, with indexation kicking in only if inflation goes above three percent. This formula reduces the value of benefits and thresholds every year by either the amount of inflation (if inflation is less than three percent) or three percent (if inflation runs more than three percent). Worse still, provincial welfare systems and income-tested child benefits are unindexed; their benefits and thresholds fall by the amount of inflation each year.

We estimate that the maximum Canada Child Tax Benefit for families with two children will fall from \$3,050 in 1998 to \$2,405 in 2010 and \$1,973 in 2020 if the program remains partially indexed. Measured as a percentage of the low income cut-off for a family of four living in a metropolitan area of 500,000 or larger, the Canada Child Tax Benefit threshold will decline from 63 percent of the low income line in 1998 to 50 percent in 2010 and 41 percent by 2020 (assuming an average inflation rate of two percent).

If the Canada Child Tax Benefit is partially indexed, the threshold for maximum benefits will fall from its 1998 level of \$20,921 or 63 percent of the low income cut-off (for a family of four living in a city of 500,000 or more) to \$16,496 or 50.7 percent of the low income line by 2010 and \$13,533 or just 41 percent of the low income line by 2020. The family income level where benefits end will decline from \$70,981 in 1998 (114 percent of the average income for a non-elderly couple) to \$55,968 in 2010 (90 percent of average income) and \$45,913 in 2020 (74 percent of average income). In other words, over time more and more middle-income families no longer will qualify for the Canada Child Tax Benefit.

While it is unlikely that future governments will freeze the Canada Child Tax Benefit for many years – indeed, we urge them to substantially enhance benefits over time – nonetheless governments still can profit from partial deindexation even when they announce ‘increases’ in the benefit and its thresholds, since such so-called increases likely will make up only partly for lost ground. Say, for the sake of argument, that a future federal government announced in the 2010 Budget that the maximum Canada Child Tax Benefit would be ‘increased’ from \$1,625 to \$1,825 for the first child and from \$1,425 to \$1,600 for the second and each additional child. In fact, however, the original Canada Child Tax Benefit rates would be \$2,061 and \$1,807 in inflation-adjusted 2010 dollars. The so-called ‘increase’ in benefits still would leave families in 2010 worse off than in 1998; the losses would amount to 11 percent – \$236 for the first child and \$207 for the second and each additional child.

Partial deindexation undermines all three objectives of the child benefit system – anti-poverty, horizontal equity and economic stabilization – and hurts low-income families with children most. The anti-poverty objective suffers because child benefits represent a larger proportion of lower-income families’ limited income, as do losses in benefits that result from partial deindexation. Partial deindexation also means that increasing numbers of upper-middle-income families are disqualified from benefits each year; over time, the disappearing point will begin to fall into middle-income territory and eventually to modest income levels. The result will be further erosion of the horizontal equity objective, which already has been weakened by the abolition of universal Family Allowances and the children’s tax exemption. By siphoning money out of the child benefits budget, partial deindexation erodes the system’s capacity to perform its economic stabilization function.

#### *anti-poverty*

The increase in federal child benefits under the Canada Child Tax Benefit will be small for working poor families with one child but more substantial for those with two or more children. For example, a working poor family with two children will see a \$510 or 20 percent boost in its federal child benefits (comparing the 1998 Canada Child Tax Benefit with the 1996 Child Tax Benefit/Working Income Supplement). However, that improvement can make only a small dent in the depth of poverty among working poor families.

Since the child benefit improvement is meant to move working poor families’ benefits closer to those currently paid to families on welfare, families on welfare (with no employment earnings) will see no increase in their child benefits at this stage of the development of the National Child Benefit System. In later stages, when the child benefit exceeds the value of welfare benefits, all low-income families will

be raised equally – i.e., when the income-tested child benefit moves above \$2,500 to reach a higher level (such as our proposed target of \$4,000).

Even if child benefits for low-income families achieved our provisional standard of adequacy for a mature system (i.e., a \$4,000 maximum payment per child to cover child-rearing costs for low-income families), they would not in themselves be sufficient to ‘end child poverty.’ The reason is that children live in families, with parents. Even if low-income families could have the *incremental* amount needed to raise each child, they still are not assured access to the means of obtaining a basic adequate income floor on which to add the child benefit. Low-income families in Canada fall far below the low income cut-offs – on average \$9,298 for two-parent families and \$8,345 for single-parent families, even with child benefits. While it is reasonable to look to a future when maximum child benefits are \$1,000 to \$2,000 higher than today, it is clearly neither sensible nor desirable to expect them to be \$6,000 to \$8,000 higher.

In other words, adults have to start with an income at least equal to the poverty line for one or two persons. We are far from providing the opportunity for everyone to have such a basic income in Canada – whether through work or through benefits. However, this problem must be addressed by a broader range of policies and cannot, indeed *should* not, be resolved by the child benefit system. The issue, rather, is one for macroeconomic policies, labour market programs and minimum wages as well as income security programs such as welfare and Employment Insurance. As noted above, the child benefit system is not the single magic bullet that will solve all problems: There are no magic bullets in public policy.

We were unable to come up with reliable estimates of the impact on the total and average depth of poverty of the Canada Child Tax Benefit and our proposed \$2,500 and \$4,000 targets because the model available to us (Statistics Canada’s Social Policy Simulation/Database Model) was in the process of being updated at the time of writing. We urge the federal and provincial governments to undertake such estimates and make them public.

#### *fairness and reduction of barriers to employment*

##### a. the welfare wall

Reducing if not eliminating that part of the welfare wall constituted by the current two-tier child benefit system is an explicit objective of the National Child Benefit System. At this very early date, we cannot make any definitive assessment of progress in lowering the welfare wall, though we can make some preliminary observations.

To date, only British Columbia and Quebec have put in place fully-integrated child benefits; Quebec’s program is so new (September 1997) that we cannot make any comments on its performance, though we do have more information on the BC Family Bonus which began in July of 1996. Saskatchewan plans a fully integrated child benefit which, with variations in program parameters, likely will resemble the BC Family Bonus and Quebec’s new family allowance – and the federal Child Tax Benefit and its

successor the Canada Child Tax Benefit. The BC Family Bonus provides maximum benefits to all low-income families with children in the province and has extended the level of child benefits previously paid only to welfare families to the working poor and other low-income families; modest-income families receive partial benefits. Early data indicate that the extension of coverage is significant: More low-income families not on welfare receive the BC Family Bonus (150,000) than are on welfare (70,000). Thus in terms of reach, British Columbia is achieving the desired objective of fully replacing welfare benefits for children with an income-tested child benefit program for all low-income families with children. We can expect Quebec and Saskatchewan to do the same.

Alberta is not going the route of replacing welfare benefits for children with an income-tested child benefit for all low-income families, opting instead for an earnings supplement for the working poor in the form of the Alberta Family Employment Tax Credit. Nonetheless, Alberta will go a considerable way to lowering its welfare wall in the sense that working poor families will receive a new provincial child benefit that – though not equal to welfare benefits for children – will significantly reduce the child benefits gap between welfare and working poor families with children.

Progress in reducing the welfare wall in other provinces is uncertain at this time. So far, Ontario – home to almost one-third (32 percent) of Canada's low-income children and 44 percent of all recipients of welfare – has not announced plans for either a new child benefit like BC, Saskatchewan, Quebec and New Brunswick or an earnings supplement like Alberta, Saskatchewan, Quebec and New Brunswick. Instead, Ontario is using its savings from the increase in federal child benefits to help finance an individual child care subsidy program. In its initial form, Ontario's Child Care Tax Credit (a maximum \$400 per family) will be too modest to make much of an impact on the welfare wall, and will reduce the wall only for families with eligible child care expenses. New Brunswick's Child Tax Benefit and Working Income Supplement also are much too small (\$250 maximum) to remove many bricks from the welfare wall. But these provincial initiatives could be expanded in future as additional infusions of federal money into the Canada Child Tax Benefit allow provinces to enrich and/or expand their reinvestment projects.

Other provinces are yet to make public their reinvestment plans. Those which opt to put their savings into income programs for low-income children will be reducing the welfare wall, formally in the case of integrated child benefits such as the BC Family Bonus and Quebec's new family allowance and *de facto* in the case of earnings supplements such as Alberta's Family Employment Tax Credit. However, provinces which reinvest their welfare savings in services – such as child care, early childhood development and extension of in-kind benefits (e.g., supplementary health, dental or prescription drugs) – will attack the welfare wall through a different route.

The federal government has a pivotal role to play in reducing the welfare wall. The Canada Child Tax Benefit will increase child benefits for working poor and other low-income families (not on welfare) but not for those on welfare. To fully replace welfare benefits for children with an income-tested benefit that will provide all low-income children the same amount that goes to welfare children under the present two-tier system will require a maximum benefit of around \$2,500 per child, though even that will fall short in a few provinces which pay higher child-related welfare benefits.

## b. net versus gross family income

The continued use of the net income definition for child benefits has more serious implications as governments invest in a stronger child benefit system than they did 20 years ago with the refundable child tax credit. A lot more money is at stake now because the entire federal child benefit system is based on net family income, as are the several provincial child benefit innovations that have been launched or announced to date in BC, Saskatchewan, Quebec and New Brunswick. As noted earlier, the use of net income raises questions of fairness and efficiency.

So far, there are no plans for the new child benefit system to address this matter. We return to the net family income problem later in the section *Issues*.

### *promote dignity and independence*

Again, it is too soon to evaluate the emerging child benefit system according to how well it meets this important criterion. However, to the extent that the emerging National Child Benefit System manages to shrink and finally eliminate the role of welfare in the child benefit system, it should be able to meet this test.

Evidence from focus groups held for our research into the BC Family Bonus (reported in the next section) shows that recipients perceive the new program as non-stigmatizing and non-invasive, in sharp contrast to the demeaning, rule-bound and dependence-engendering welfare system. There is every reason to believe that the experience will be similarly positive when other provinces create income-tested child benefits, so long as governments are able to distinguish the new programs in their recipients' and the public's mind as separate and distinct from welfare. As provinces develop their various child benefit initiatives in the evolving National Child Benefit System, evaluators should make use of focus groups and polls to plumb recipients' experience with and their and the public's perception of federal and provincial child benefits.

There is no reason to suggest that the Canada Child Tax Benefit will be any less successful than the present Child Tax Benefit (of which it is only a variant) in meeting this criterion of promoting dignity and independence. However, to our knowledge no research has been done into this matter; it is extremely important and any future formal evaluation of the National Child Benefit System must include it.

### *simple and efficient administration*

British Columbia's Family Bonus is delivered by Revenue Canada on behalf of the province, using the existing federal Child Tax Benefit administrative machinery in assessing eligibility for and amount of benefits and making within-year adjustments to benefits in the case of such events as the birth of a child or change in family type. Obviously, this arrangement produces significant savings over the cost of setting up a separate provincially-delivered system. As noted in the next section, the BC Family

Bonus's administrative cost is less than one percent of the total cost and is expected to decline further as more families opt for direct deposit into their bank accounts over cheques.

With the exception of Quebec, other provinces also likely will take advantage of the existing federal child benefit administrative machinery to deliver their new child benefit programs. Even in Quebec, the incremental cost of delivery through their own income tax system should be small.

#### *economic stabilization*

To the extent that the National Child Benefit System increases payments, most of which goes to lower-income families with a high marginal propensity to consume, it can be expected to perform better in terms of economic stabilization. We specify 'most' because some of the increase will leak to non-poor families due to the net family income definition.

In its initial phase, the National Child Benefit System will allow provinces to reduce their welfare benefits commensurably and reinvest the resulting savings in a variety of ways, not necessarily into income programs. The net incremental increase in child benefits is substantially less than the total increased cost to the federal government, which means that the effectiveness of the program as an economic stabilizer in its first phase will not be much larger than the current program. Of course, to the extent that provinces actually do treat their savings as 'new' money and do not use it just to offset spending they would have otherwise made, there still will be an overall initial stimulus to the economy equal to the full size of the increased federal spending in the first round. Nevertheless, as a long-term economic stabilizer, the Canada Child Tax Benefit's effectiveness will be muted to the extent that its increases could be offset by future provincial decreases (e.g., in adult-related welfare benefits). We would anticipate that the federal role, and the use of this instrument as part of economic policy, will become clearer when and if the federal government fully takes over responsibility for child benefits, minimizing the future interaction between federal and provincial benefits.

Of course, as noted before, partial deindexation will erode future increases in the National Child Benefit System over time and thus gradually will undermine any gains that might be expected in performing its economic stabilization role.

## THE BC FAMILY BONUS

In July of 1996, BC introduced its new Family Bonus, becoming the first province to replace completely its welfare-based child benefits with a new child benefit program available equally to *all* low-income families. In so doing, BC has made an historic advance in child benefits. As one social policy analyst put it: "...a lot of governments have talked about issues like these for the last twenty years but not much has happened across the country, so, in a sense, we in BC are having a quiet revolution in social policy reform" [Prince 1996]. This child benefit 'quiet revolution' gives the other provinces and Ottawa an invaluable opportunity to learn from the results in BC in designing the new National Child Benefit System.

This section first describes the design of the BC Family Bonus and how it is administered. We then undertake a preliminary assessment of the BC Family Bonus according to the objectives described in the section *Measuring Progress*.

To better understand and assess the BC Family Bonus, we held two focus groups in Victoria – one with low-income families receiving the BC Family Bonus and another with community agency personnel ('front-line' workers). Information on the attendance is provided in Tables 2 and 3. These focus groups are not a representative sampling, but they furnished a rich store of lived experience that cannot be obtained from large-scale surveys. We learned a great deal from the focus groups, especially from the recipients' group, and their views have informed our perspective throughout this report.

We also interviewed the BC Minister of Human Resources and a number of provincial public servants. We are grateful to the BC government for facilitating and helping us arrange these interviews.

### What is the BC Family Bonus?

The BC Family Bonus replaced needs-tested welfare payments for children with an income-tested benefit, equally serving all low-income and modest-income BC families with children – including the working poor as well as those on welfare or Employment Insurance. Like welfare and the federal Child Tax Benefit, the BC Family Bonus is delivered on a monthly basis.

The maximum annual Bonus is \$1,236 per child under the age of 18, equivalent to what was provided previously through the welfare system. The maximum benefit is paid to families with net family incomes under \$18,000. For every dollar of income above the family income threshold of \$18,000, benefits are reduced by 8 cents for families with one child and 16 cents for those with two or more children. Table 4 displays the benefits paid by the Family Bonus for families with various numbers of children at different income levels.

The BC Family Bonus is targeted to families with below-average incomes, since maximum benefits are payable only to those with incomes below the Statistics Canada low-income lines. The \$18,000 net family income threshold for maximum benefits from the Family Bonus is less than Statistics Canada's

low income cut-offs, which vary by size of family and community – e.g., ranging in 1997 from an estimated \$27,032 for a family of three living in metropolitan Vancouver to \$18,682 for a rural area; for a family of four, the low income cut-offs range from an estimated \$32,722 for a metropolitan area of 500,000 or more to \$22,613 for families living in rural areas. The Family Bonus diminishes to zero at \$33,540 for families with one or two children. This disappearing point for the BC Family Bonus is substantially below the average income of families with children, estimated at \$65,000 for British Columbia.

For welfare recipients, the BC Family Bonus replaces the child benefit of the same amount that used to be provided through welfare. Welfare recipients moving into the labour market continue to receive the Bonus – the same amount as they got while on welfare, if their net family income is under \$18,000. If they lose their job and have to return to welfare, they continue to receive the Family Bonus.

Working poor families with income under \$18,000 now receive the maximum Family Bonus, which represents a significant increase in income. For example, a single mother of two earning a net income of \$18,000 a year, substantially *above* the minimum wage (even in BC, which at \$7.00 an hour or \$14,560 for full-time year-round work pays Canada's highest minimum wage), will get an extra \$2,472 in income – a sizable increase in net income of 13.7 percent.

The BC Family Bonus is delivered by Revenue Canada on behalf of the province through the existing Child Tax Benefit administrative machinery. Inquiries are handled by a federal government call centre. Recipients can opt to receive their Family Bonus payment in the form of a cheque or as a direct deposit to their bank account. About 46 percent of recipients are now paid by cheque and 54 percent by direct deposit. It is expected that the percentage of direct deposits will gradually increase.

## **Anti-poverty objectives**

### *additional income for the working poor*

The Family Bonus is being paid to some 220,000 families for the year ending June 1997, representing 45 percent of BC families. According to the 1997 BC Budget, total payments will amount to about \$290 million for the nine months the program operated in the 1996-97 fiscal year. This means that the BC Family Bonus will cost approximately \$385 million for a full fiscal year. This is not all incremental cost as roughly \$145 million of this would have been paid anyway to families on welfare. Moreover, there are other offsetting savings for the BC government. For example, the federal government refunds to BC the cost of the Bonus paid to Native families on reserves which receive income assistance (i.e., welfare).

Of the total benefits, 95 percent go to families with net incomes less than \$30,000 a year and 74 percent to those with annual net incomes under \$18,000, so it appears that the program is well targeted to low-income families. Since welfare recipients used to receive an equivalent child benefit from welfare which was replaced by the Family Bonus, they did not experience an increase in child benefits. But of the 220,000 families getting the BC Family Bonus, around 150,000 are not on welfare and, while some of these are on Employment Insurance or other income transfer programs, most are working. The

program has been successful in including the working poor, a group traditionally difficult to identify and to reach with public programs.

The Family Bonus has had a big impact on the 150,000 low-income and modest-income families not on welfare, for whom it has meant substantial additional income. A study commissioned by the government of BC and conducted by one of this report's authors, Michael Mendelson, estimated the reduction in the depth of poverty among working poor families as a result of the BC Family Bonus [Mendelson 1997].

The study found that the Family Bonus reduced the poverty gap by an estimated 19 percent for all working poor families (defined in the study as families below the low income cut-offs which are not on welfare, some of which will be on Employment Insurance or other transfer programs) and by 25.5 percent for single-parent families among the working poor. The study also calculated what effect the program has on depth of poverty using lower poverty lines set at 75 percent of the low income cut-offs. The result using these lower poverty lines was a 28 percent reduction in the depth of poverty for all working poor families and a 38 percent reduction in the depth of poverty among single-parent working poor families.

The results should not be too surprising. After all, the BC Family Bonus is paying substantial benefits to families; the program is targeted to pay maximum benefits to low-income families; and the majority of the money is going to working poor families because they substantially outnumber those on welfare.

The Mendelson study did not attempt to measure the reduction in the number and percentage of families below the poverty line for the reasons discussed earlier in the section on evaluation. Nor did the research attempt to measure the dynamic effects of the new program; it is too early to attempt such an estimate in any case.

The effectiveness of the BC Family Bonus in reducing the depth of poverty among the working poor is not unrelated to its method of administration. The BC Family Bonus has almost 100 percent take-up, by virtue of its administration through the tax system. The working poor are traditionally a very difficult group to reach. The experience of most social programs is that if they require a separate special application, there will be far less than full take-up – especially if the applicant is required to visit a welfare office.

One of the participants in our community workers' focus group observed that:

*For the families who are working poor, and we see a lot of them, the Bonus is a real help. A lot of those families are really struggling. They won't ask for help. They're hungry, their situations are difficult. So for them the Bonus is great...There are families where both parents are working, often part-time at minimum wage. They see the Bonus as making a real difference in their lives.*

If our recipients' focus group is any indication, the BC Family Bonus is indeed making a real difference in the lives of children. Many of the families see the Bonus as money meant specifically for

their children, although families are not always able to use it for children's items because they have other competing expenses (e.g., food or rent). In some instances, the Bonus allows them to get some of the 'extras' for their children that they could not otherwise afford. One mother said she spent one cheque on a \$100 enrollment fee so that her son could play junior hockey. Another said that she used it to buy her son's size 13 running shoes.

#### *what does the BC Family Bonus mean for people on welfare?*

The BC Family Bonus extends important income benefits to working poor families, but the strongest and loudest criticisms of the new program have come from welfare advocates, traditionally supportive of any program for the poor. Much of that criticism is related to the other changes in welfare benefits when the BC Family Bonus was introduced and is not really relevant to the Bonus *per se*. But some of the criticism arises from the fact that the BC Family Bonus is not additional income for welfare recipients. This view was expressed in our focus group for community workers. For example, one worker said, "*If it's a bonus, dammit, it should be more. It shouldn't mean getting the same thing at different times of the month.*"

Some of the reaction was caused by confusion over the name of the program. Some people felt that if it was advertised as a Bonus, then it should not just be a replacement for their welfare benefits. According to one community worker: "*The name has confused some families on social assistance, who were expecting a 'bonus.' We had to have meetings to explain that to people, who saw the program as a loss for them.*"

Since the BC Family Bonus did not increase income for welfare recipients, critics argue that welfare recipients do not benefit in any way from the new program. However, this criticism implicitly suggests that the welfare caseload is static and unchanging, and that people on welfare are so different from the working poor that a program to benefit the latter will never reach anyone on welfare. This view is wrong. In fact, in a sense there is no such thing as 'the' welfare caseload. Instead, there is a rapidly changing group of people who are forced to rely on welfare at some points in their lives but are off welfare again as soon as they are able. Even in this time of high unemployment, about four percent of the BC caseload leaves the welfare rolls every *month*. Almost all families with children which leave welfare will continue to get the maximum Family Bonus for at least a year; those which go into low-wage jobs will receive the maximum amount for as long they earn low wages. Moreover, in light of the unstable labour market, the BC Family Bonus offers an important element of income security for unemployed parents who have to turn or return to Employment Insurance: They can always count on their income from the Bonus.

In our recipients' focus group, it became clear during the course of the conversation that several of the participants had been on welfare at some point. The statistics show that this is not at all unusual. For welfare recipients who aspire to get off welfare, which seems to be almost all, the Family Bonus allows households with children to leave welfare and take a job without a big loss in income. The Bonus removes a penalty standing in the way of the aspirations of many, perhaps most, people on welfare.

In sum, the Family Bonus does not hurt families on welfare in BC, but the introduction of the program may have resulted in some expectations not being met. Other governments might take note and initiate more aggressive communication with welfare recipients during the introduction. In the *Issues* section, we discuss further the more general question of whether programs such as the BC Family Bonus should be ‘passed on’ to welfare recipients as an increase in their income.

### **Fairness and reducing barriers to work**

Clearly, the BC Family Bonus has changed the treatment of working poor families with children compared to those in like circumstances but relying on welfare. All low-income families now are entitled to the same level of child benefits. In this sense, the new program is clearly fairer than the previous system and removes barriers to work.

However, there are two other aspects in which the BC Family Bonus may be less fair – the definition of family and the use of net rather than gross income for the purpose of calculating payments. With regard to the former matter, we are concerned that joint reporting of income may be sporadic, penalizing honest families. With regard to the latter issue, we believe that the use of net income introduces unjustified differences in treatment whereby families with substantial gross income end up being treated the same as lower-income families. But both problems originate in the federal child benefit and are only reflected in the BC Family Bonus. Therefore, these matters are discussed further in the *Issues* section of this report as a problem which all tax-administered child benefits have in common.

### **Adequacy**

We are proposing that the first standard of adequacy, to be reached by the year 2000, be a minimum payment of \$2,500 per child, sufficient to get all child-related cash benefits out of the welfare system. By this standard, BC is already very close to achieving the first signpost. All cash benefits on behalf of children have been removed from the welfare system; total federal and BC child benefits are \$2,469 for a child under 7 and \$2,256 for a child over 7.

The second signpost of adequacy is to provide sufficient funds for a modest-income family to pay the additional costs of raising a child, which we have pegged at a provisional estimate of \$4,000. When the larger federal benefits from the Canada Child Tax Benefit come into play, if British Columbia made no compensating reduction to its BC Family Bonus, the maximum combined benefit payable to all low-income families in BC would come to \$3,074 for the first child under 7, which is not impossibly far off the \$4,000 objective.

### **Effects on welfare caseload**

One of the hopes in introducing a program such as the Family Bonus is that it will result in a decrease in the welfare caseload. The Mendelson study found an accelerated decrease in BC welfare caseloads when the BC Family Bonus was introduced.

It is expected that the BC Family Bonus over time will affect caseloads in two ways. By removing financial penalties facing welfare recipients considering potential employment, it may encourage a more rapid departure from welfare into the workforce. But the impact on caseloads may result from some families finding it unnecessary to apply for welfare in the first place, so that the number of families enrolling might be expected to decline. Over the long term, even a small increase in stops and a small decrease in starts will have a big cumulative effect on total caseload. The same effects can be expected for any similar integration of child benefits in other provinces.

It is over many years, rather than immediately, that the BC Family Bonus likely will make a substantial difference in welfare caseloads. The Bonus will have to become a regular and expected part of the income security system, so that families know it is there as a secure source of income when they need to make decisions. It takes a long time for a program to become embedded in the culture of a province or country.

Nevertheless, there is preliminary evidence suggesting that the BC Family Bonus is having a sustained effect on reducing welfare caseloads among families with children. A recent quantitative analysis done by the BC Ministry of Human Resources compared predicted starts and stops (i.e., families enrolling on welfare and leaving welfare, respectively) to actual starts and stops. This analysis found a continuing decrease in the number of stops, above the predicted level, and a continuing decline in starts, below the predicted level. The positive change was most pronounced among single parents.

These early findings on the BC Family Bonus are very encouraging for the potential of an integrated child benefit system in Canada as a whole. While the results are preliminary, they likely will become larger still as the program is more established. Moreover, the process is cumulative; as stops increase and starts increase, the welfare caseload will decline substantially over time relative to where it would have been without child benefit reform.

## **Simple and efficient administration**

As noted, the BC Family Bonus is delivered through the federal Child Tax Benefit machinery. This is a relatively inexpensive way to administer the program. The federal government charges BC about \$3 million a year for this service. There are only a few BC public servants working on the program. BC has had to hire only three more staff to help administer this very large program. As a result, administrative cost is less than one percent of the total cost and only a few dollars per year per recipient family, and these amounts likely will decrease as more families use direct deposit.

### *the ‘two cheques’ issue*

The introduction of the BC Family Bonus initiated a change in payment arrangements for welfare families with children. In June 1996, they went from a single welfare cheque plus a federal Child Tax Benefit cheque to a welfare cheque, a BC Family Bonus cheque and a federal Child Tax Benefit cheque (or direct deposit in some cases). Apparently, some welfare recipients were upset by this change.

Many welfare recipients know the precise amount of their cheque. It is not totally unheard of for seemingly arbitrary changes to appear on cheques, and recipients must follow up on such changes to ensure that they are correct. In this context, it is not surprising that there was some difficulty when \$103 a child each month was moved from welfare to the BC Family Bonus. Even though the Family Bonus comes only a few days later, there is still a lot of worry until it arrives.

A longer-term welfare recipient at our focus group expressed this concern:

*...having two cheques is kind of scary because I get \$800 a month. That's it. But now I don't get \$800 a month. I get \$700 and they make you wait for a couple of days, and then you phone all your friends and you go: "Did you get that \$103 one yet?" Because it totals the same amount, but you know...So you're waiting, and then you think: "Well, maybe there's a new policy that I haven't seen on TV yet.*

Interestingly enough, the one new recipient of welfare in our recipients' focus group did not see things this way at all, having never experienced anything else. Indeed, she preferred two cheques:

*So I like it that way because I've always got money. I run out of money and then, you know, two days later I have another cheque that's come in.*

It would appear that the problem of 'two cheques' is another adjustment problem, difficult perhaps, but temporary. Possibly, it could have been eased by more advance preparation, but it likely will disappear after at most a few years when everyone is used to the new system. If the BC Family Bonus and the federal Child Tax Benefit are combined in a single cheque, this would move up delivery of the BC Family Bonus by two days and reduce the number of cheques to two from three. This change would simplify further administration and perhaps help reduce the confusion, although it also would require another period of adjustment.

### *visibility*

The BC Family Bonus is paid each month two days after the federal Child Tax Benefit is paid. Where the Family Bonus is in the form of a cheque, the cheque shows both the BC crest and identification and the federal maple leaf and identification. In future, the cheques will display more prominently BC identification. In addition, at the beginning of each year, the BC government sends a letter to each recipient family saying how much Family Bonus it will be getting during the year.

Most of the staff we interviewed for this study felt that recipients do not always understand what the payment is or that it is coming from the government of BC. However, many of the participants in our recipients' focus group knew what the Bonus is, that it is a BC government initiative and, because they have to budget so carefully, exactly when it arrives and how much it pays. Admittedly, this group may not be representative of all recipient families, since participants in the focus group were selected on the basis that they know they receive the Bonus. Despite this knowledge, several participants said that they and their friends referred to the Bonus as the 'Family Allowance,' as a kind of generic term for child-

related benefits of any kind. (The actual Family Allowance program was replaced in 1993 by the Child Tax Benefit.)

For the general public, this issue of the jurisdictional identity of government programs might seem to be just a political game. After all, who really cares whether people know they are getting a government benefit and which government is paying for it, as long as the program is working? But democratic governments have to get elected; programs that people do not know about, but that cost a lot of taxpayer dollars, usually will not be too successful in attracting public support. Anti-poverty programs have to compete for funding with popular programs like health and education, so if the former programs fail to provide much positive political visibility for the government, they will be hard to fund and maintain over time.

It is our sense that visibility may be a little better than most BC officials think, at least among working poor families, but we have no polling data to back this up. In any case, the cheque paid by the federal government on behalf of BC does not seem to help all that much in jointly crediting BC and Ottawa. Perhaps the new cheque design will be better, though more people likely will be going to direct deposit anyway.

The administration of the BC Family Bonus through the federal tax system has immense advantages – low administrative costs, non-intrusiveness and simplicity. But one disadvantage may be that it reduces somewhat BC's political credit for the program.

## **Promote dignity and independence**

### *lack of stigma and intrusiveness*

Administration through the income tax system means that the payment of the BC Family Bonus is automatic, based on the previous year's income tax report, and does not require a special application of any kind to be submitted. If a parent files an income tax return, and meets the eligibility requirements for family net income and number of children as determined from the tax returns, a Family Bonus payment is initiated.

For the recipient focus group, the automatic nature of the BC Family Bonus is extremely important – probably one of its best qualities. The program delivers a non-intrusive and non-stigmatizing payment that is theirs without demanding any special applications, without answering any questions other than those every citizen must answer on his or her tax form and without any demeaning sense of being deemed specially needy. The BC Family Bonus clearly is not welfare, which imposes a complex, highly intrusive and typically stigmatizing test of applicants' needs and resources. Some of the comments on this issue were:

*“...this way I can make anything I want and only have to answer to the taxman.” “There’s no stigma.” “You don’t have to answer to anybody about what you made.” “You’re independent of it. It’s your life.”*

### *responsiveness*

Since the tax form reports income from the previous year and it does so during the spring of the following year, the income upon which the BC Family Bonus (and the federal Child Tax Credit) is based may be out of date. For example, say a single mother with one child is earning \$4,000 a month and then is laid off in November so that her employment income falls to nothing (of course, in reality she might qualify for Employment Insurance or, failing that, welfare). When she fills out her tax form in April, she will report \$40,000 in employment income for the previous year as well as any benefits she receives from Employment Insurance or welfare. If she has few or no deductions, she will not be entitled to any Family Bonus payments in the current year when she is unemployed.

The disjunction between current income and current child benefits could pose a serious problem for parents struggling to cope with a sharp reduction in income. The tax system is based on retrospective reporting of last year's income and is therefore not responsive. Any program using the tax system must find a way to deal with this problem of responsiveness to mid-year changes in current family income.

There are two types of changes to family income or needs that occur in mid-year. One type of change results from new family composition: A couple splits up; one of the spouses dies; a child is born or dies. A second type of change may be due to loss of a job, finding a job, enjoying a pay increase or experiencing some other change in income.

The federal Child Tax Benefit administration allows parents to submit a special application to Revenue Canada at any time during the year if there is a change in family composition. The federal Child Tax Benefit may then be initiated in mid-year without waiting for a new tax form to be filed; the BC Family Bonus also is paid if eligibility is established. But the federal system does not accommodate mid-year changes in income due to other causes.

In BC, this issue is addressed through the welfare system. Temporary welfare is available to income assistance families not receiving the full Family Bonus, so that the amount of welfare they get per child (combined with any partial Family Bonus they may be getting) is equal to the full Bonus. When the full Bonus begins later in the year, the additional welfare is no longer required and is removed. Since welfare is available only to those with very few assets and little or no income, many low-income families in BC which otherwise would be eligible due to a drop in their income, must wait several months or more before they start getting the BC Family Bonus.

We asked participants in the recipients' focus group how they would react to a Family Bonus that instead required them to file a monthly report to be more responsive to change in income. There was a strong reaction consistent with their preference for a tax-based, non-intrusive system. Most participants thought that such a system would be too much like welfare. Some of the reactions to a suggestion for a monthly report were:

*"No." "No way." "That's too much." "They'd better talk to some people." "Too intrusive."*  
*"Oh, it wouldn't be worth it." "It would drive me nuts if I had to fill out an application every month."* *"That would be worse than welfare."*

In sum, the experience in BC is that the responsiveness problem has not turned out in practice to be a major source of complaint. The welfare alternative for those in dire straits appears to be working. From a recipient's perspective, the trade-off of responsiveness for non-intrusiveness is worthwhile.

**Table 2**  
**Recipients' focus group - Victoria, B.C.**

Family	Single or couple	Number of Children	Family income	No. of adults employed	Use day care	Day care subsidized
1.	single	2	under \$20,000	part-time	yes	yes
2.	couple	3	under \$20,000	one full-time one part-time	no	n/a
3.	single	1	under \$20,000	one	yes	yes
4.	single	2	\$20,000-\$30,000	one	no	n/a
5.	couple	1	\$30,000-\$40,000	two	yes	no
6.	single	1	welfare	none	no	n/a
7.	single	3	\$20,000-\$30,000	part-time	yes	yes
8.	single	3	under \$20,000	one	yes	yes
9.	couple	3	under \$20,000	one	no	n/a
10.	single	3	under \$20,000	part-time	yes	yes
11.	single	1	welfare	none	no	n/a
12.	single	1	\$20,000-\$30,000	one	yes	yes
13.	single	3	\$20,000-\$30,000	one	yes	yes
14.	single	2	under \$20,000	one	yes	yes

Note: Attendees were selected mainly by random phone calls (approximately 800) in the Victoria area and by referrals from community workers.

**Table 3**  
**Affiliations of community workers**

1.	Blanshard Community Centre
2.	James Bay Community Project
3.	Fairfield Community Place Society
4.	Capital Regional District (Health)
5.	Capital Families Association
6.	Single Parent Resource Centre
7.	Together Against Poverty
8.	Salvation Army
9.	Coastal Community Services

**Table 4**  
**Annual BC Family Bonus, by Number of Children and Net Family Income**

net family income	1 child	2 children	3 children	4 children	5 children
\$	\$	\$	\$	\$	\$
18,000	1,236	2,472	3,708	4,944	6,180
20,000	1,080	2,148	3,384	4,620	5,856
22,000	912	1,836	3,072	4,308	5,554
24,000	756	1,512	2,748	3,984	5,220
26,000	600	1,188	2,424	3,660	4,896
28,000	432	876	2,112	3,348	4,584
30,000	276	552	1,788	3,024	4,260
32,000	120	228	1,464	2,700	3,936
34,000	0	0	1,152	2,352	3,624
36,000			828	2,064	3,300
38,000			504	1,740	3,976
40,000			192	1,428	2,664
42,000			0	1,104	2,340
44,000				780	2,016
46,000				468	1,704
48,000				144	1,380
50,000				0	1,056
52,000					744
54,000					420
56,000					96
58,000					0



## ISSUES

During the course of the analysis, five issues arose which we consider crucial to the development of the National Child Benefit System: not ‘passing through’ increased child benefits to welfare recipients; net versus gross income; indexation; definition of family; and necessary future increases in the level of maximum benefit. Each of these issues is important for the future evolution of the National Child Benefit System and its capacity to get from where we are today to the fully mature and effective integrated child benefit sketched out in this report.

### **Not passing through increased child benefits to welfare recipients**

In its formative phase, as Ottawa and the provinces move towards the goal of replacing welfare benefits for children with income-tested child benefits, only working poor families and other low-income families not on welfare (e.g., those on Employment Insurance) will get additional income. For welfare recipients, the added child benefit will displace some (and eventually all) of the welfare-related child benefit. This first phase in the development of the National Child Benefit System is not intended to improve child benefits for welfare families, desirable as that might be. Instead, it is meant to ensure that under the new system such families maintain the level of child benefits they previously got from welfare. Once child cash benefits in the welfare system have been fully displaced by a broadly-targeted child benefit, any further increases in the benefit will add equally to the income of welfare recipients and other low-income families.

It is understandably difficult for many anti-poverty groups and social advocates to accept governments’ decision to not pass through the increase in federal child benefits to families on welfare in the first stages of constructing the National Child Benefit System. This feature of the first phase of child benefit reform has caused many activists to become disenchanted with the whole enterprise. While we are sympathetic to these concerns and share similar objectives in combatting poverty, we have concluded that the increase in the child benefit should not be passed through to families on welfare. There are several reasons for this position.

The essential objective of the National Child Benefit System is to replace child-related welfare benefits with a broadly-based income-tested system paying the same benefit to all low-income families with children. Such a child benefit system is the only hope of achieving adequacy in benefits for poor families, including those on welfare. If welfare families in Canada ever are to get an adequate income, it surely will not come from increased welfare rates. In Ontario, for example, two successive governments increased welfare rates substantially, only to have the whole system cut right back again with barely a ripple of public concern. If ever there was a graphic demonstration of the futility of traditional welfare as an effective anti-poverty strategy, this experience was surely it.

A successful anti-poverty strategy will require the transformation of our basic income safety net from extremely unpopular welfare programs, which are narrowly targeted at a small group of relatively powerless Canadians, to a diverse range of social programs that have broad public appeal and acceptance. A comprehensive anti-poverty project for Canada cannot be constructed on the platform of

welfare as we know it. Replacing child benefits in the welfare system with a broad, income tax-based, non-stigmatizing system of benefits is the first step in building an acceptable foundation for an effective anti-poverty strategy.

As long as the provinces genuinely reinvest their savings from welfare expenditures on children into programs for all low-income families with children, *the same amount of money will go into programs for poor families with children – regardless of whether the increased benefit is passed on to welfare recipients*. The difference is how the extra money is spent – to improve (non-welfare) income programs and services for low-income families with children, or to increase welfare benefits. While some social groups still might prefer the latter, the point is that the former is *not* a reduction in spending on children.

Of course, provinces must be honest in their reinvestment policies and not simply use the extra money to offset what they would have spent anyway. In this regard, the reinvestment guidelines and the transparency of the reinvestment strategy are critical to the integrity of the National Child Benefit System strategy.

The argument for passing through the increased federal child benefit to welfare recipients may be somewhat naive. The pass-through case is based on the premise that the child benefit increase indeed will be successfully passed on to welfare recipients as long as provinces do not formally acknowledge they are reducing welfare benefits. But provinces remain keenly aware of the total income of recipients. Over the next several years, their welfare rate policies would take into account the existence of recipients' additional income from federal child benefits. The result could be slow erosion of the increased benefits simply by freezing welfare benefit levels and allowing inflation to do the job; no province indexes its welfare rates. In that case, the extra money would be permanently lost to children's programs. While the same slow erosion also can happen in the reinvestment strategy, at least the latter could allow for more political and administrative accountability – aided by scrutiny from social groups which will be vigilantly monitoring the developing National Child Benefit System.

Indeed, this argument is one of the more powerful reasons why those who are most concerned about families on welfare should be in favour of the idea of fully replacing welfare benefits for children with a broadly-based integrated child benefit system. Until that happens, increases in federal child benefits – even past increases that in theory were fully passed through to welfare recipients – can and have been easily neutralized by the erosion of provincial welfare benefits.

Finally, as we have argued throughout, the vast majority of welfare recipients are trying very hard to get a job and leave the welfare system. The large turnover in caseload proves that many people succeed. But the present practice of effectively imposing financial penalties on those who do succeed is unfair to recipients and puts a barrier in the way of their aspirations. The policy of not passing through the increased federal child benefit lowers those barriers by reducing the welfare wall. But, on the other hand, passing through the increased child benefit to welfare recipients simply will leave the welfare wall untouched. There is a third option – raise child benefits for all low-income families, including those on welfare – but this would prove much more costly; governments have chosen first to seek to equalize child benefits for all low-income families before boosting child benefits for them all.

Canada is not alone in grappling with this issue. Frank Field, a social policy expert and newly-appointed Minister for Social Security in the United Kingdom, and one of the founding spirits of the British Child Poverty Action Group, argues that “any successful disengagement from means-tested assistance must inevitably result in this outcome; those drawing means-tested assistance will see no immediate increase in their standard of living, while others receive additional help as the new benefit structure begins to take effect. Here is another crunch point where it is vital that the reformer’s nerve does not crack. This strategy offers the only realistic possibility of disengaging from means-tested welfare” [Field 1996: 19].

In assessing the impact of the National Child Benefit System, it is important not to use the single criterion of families’ cash benefits before and after the change. This is too narrow and mechanistic an approach. Although families on welfare initially will see no increase in the amount of their child benefits, they still stand to benefit in other important ways.

The Canada Child Tax Benefit and the new child benefits that several provinces are providing or plan to create are income-tested benefits that come with none of the stigma of welfare. Instead, they are delivered anonymously and impersonally, eligibility being determined on the basis of income as reported on the income tax return rather than assessed through the intrusive needs test used by welfare. Like the existing Child Tax Benefit, the Canada Child Tax Benefit will serve the large majority (85 percent) of Canadian families with children, including middle-income and some upper-income families. The BC Family Bonus is more targeted than the federal child benefit, but still serves modest-income families (e.g., benefits for a family with one or two children disappear above net family income of \$33,540, which is above the low income cut-offs).

In an era of restraint in public spending, income-tested benefits have proven to be the safest of all income security programs in Canada. In fact, income-tested child and elderly benefits have been increased in real terms. By contrast, needs-tested welfare has been reduced in most provinces in recent years, social insurance has proven vulnerable (especially Unemployment Insurance/Employment Insurance) and universal programs – supposedly the safest of all – are extinct in the case of child and elderly benefits. Politically, the chances of improving benefits under an income-tested integrated child benefit are far superior to winning increases in welfare benefits. In future, after the National Child Benefit System is put in place, governments can and should raise the maximum level to improve child benefits for welfare (and other) families, up to a level sufficient for a low-income family to pay for the additional costs of raising a child.

The important caveat to our claim that income-tested programs have fared best is that federal child benefits – unlike elderly benefits – have been only partially indexed since 1985. The issue of partial indexation is discussed below. However, partial indexation is better than none at all, which is the case for welfare benefits. Welfare families would be better off receiving more (and eventually all) of their cash child benefits from the federal government; at least they will be getting partially-indexed child benefits as opposed to unindexed welfare benefits for their children. Better still, if Ottawa can be persuaded to fully index the Canada Child Tax Benefit, welfare families and other low-income families will have a stable source of income from child benefits.

If the increased child benefit had been added on top of existing welfare benefits for children, the

existing gap between people working and those on welfare would have been perpetuated. The result would have been that working poor families with children would have remained just as badly off relative to families on welfare as they were under the old system, which is not fair to the working poor. Moreover, many people on welfare who went back to work would have lost a substantial amount of income rather than increasing their income, leaving a significant obstacle in their path towards becoming independent of welfare. In short, income for people on welfare would have been higher than under the proposed treatment of the child benefit increases but the structural flaws in the social security system – the welfare wall – would have remained.

In the face of these consequences, it would be more consistent with the goals of reducing child poverty and strengthening the social security system for advocates to argue instead for higher child benefit levels, which would increase benefits for *both* the working poor and those on welfare. After all, the complaint about not ‘passing through’ the increase in federal child benefits is about the amount of benefits available to families on welfare: It is not an argument that welfare families should, everything else being equal, receive *more* child benefits than the working poor.

One of the phrases often used to criticize the National Child Benefit System’s strategy is that it ‘pits the poor against the poorest.’ But we believe that a better case can be made for just the opposite: The National Child Benefit System will have the effect of better public and political support for families on welfare because they will be joined in a single broadly-based program not only with the larger group of working poor, but also with the majority of non-poor families with children.

### **Net versus gross income**

The Canada Child Tax Benefit, like the current Child Tax Benefit, will calculate eligibility for and amount of benefits on the basis of net, not gross, family income. The same definition is used by the BC Family Bonus and also will be used in child benefit initiatives in other provinces including Alberta, Saskatchewan, Quebec and New Brunswick. Use of net rather than total family income could have serious negative consequences for the future integrity and efficiency not only of the federal Canada Child Tax Benefit but the federal-provincial National Child Benefit System overall.

The net income definition allows the deduction from gross income of a variety of items, including contributions to Registered Pension Plans and RRSPs, child care expenses, union and professional dues, attendant care expenses, certain employment expenses, carrying charges and interest expenses, business investment losses, moving expenses and alimony or maintenance payments (though no longer for children) and investments in oil, gas or mining ventures. Non-poor families, with incomes above the threshold for maximum benefits, are able to reduce their income for purposes of determining their eligibility for and payments from income-tested child benefits. Upper-income families profit the most because they are more likely to have such deductions and to deduct larger amounts than families with less income.

As noted earlier, the net family income definition results in both vertical and horizontal inequities in the distribution of child benefits. Vertical inequity stems from the fact that an upper-income family can end up with similar child benefits to a middle-income family, and in some cases even more; some

non-poor families get the same maximum benefit as poor families. Horizontal inequity occurs because families with the same total income receive different child benefit payments depending on how much money they are able to deduct to reduce their net income.

The definition of income has significant implications for the distribution of federal and provincial child benefits and the effectiveness of future increases in maximum benefits for poor children. The net family income definition means that child benefits are less cost-effective in achieving their primary anti-poverty objective. For the same overall expenditure, low-income families could be paid larger benefits if the Canada Child Tax Benefit and income-tested provincial child benefits took total family income into account; modest-income families could be given larger amounts; and/or the programs could be fully indexed to inflation.

We estimate that the current Child Tax Benefit pays \$3.7 billion to families with incomes over \$25,000 (close to the \$25,921 threshold), which amounts to a sizable 72 percent of total (\$5.1 billion) expenditures. If the program calculated benefits on the basis of total income, for the same total budget only \$2.6 billion would go to families above \$25,000. The new Canada Child Tax Benefit will pay out an estimated \$4.1 billion or 69 percent of its total \$5.9 billion to families over \$25,000 on the basis of net family income, but would spend only \$2.6 billion on those over \$25,000 if total family income were used to calculate benefits.

The new Canada Child Tax Benefit and the present Child Tax Benefit inherited the net family income definition from the refundable child tax credit which was legislated in 1978. The designers of the refundable child tax credit believed that the program should use net income rather than total or taxable income. Their main argument was that net income comes closer than the other two definitions of income in the income tax system (total income and taxable income) to disposable or take-home pay – i.e., the income that families actually have to meet their expenses and raise their children. By basing the refundable child tax credit on net income, the federal government allowed families to deduct a number of compulsory costs that reduced their disposable income, including C/QPP contributions, Unemployment Insurance premiums, Registered Pension Plan contributions, and union and professional dues. It also allowed the deduction of child care expenses, which are a cost of going to work for parents. While RRSP contributions are not compulsory, the federal government justified their deduction because they are the only private pension available to self-employed workers and to the majority of the labour force which does not work for employers offering private pension plans.

The case for choosing a net income definition for child benefits on the grounds that it best approximates families' disposable income is problematic, in our opinion. For one thing, when the federal government reformed the income tax system in 1988, it no longer allowed the deduction from net income of two mandatory costs of working – Canada /Quebec Pension Plan contributions and Unemployment Insurance premiums – which all workers face, including those with low incomes. Yet Ottawa continued to allow the deduction of other items, such as contributions to employer-sponsored pension plans and RRSPs, and receipted child care expenses, which in fact only a minority of working parents – mainly those in middle-income and upper-income categories – can use to reduce their net income. There would appear to be an inconsistent – if not double – standard at work here regarding what should be taken into account in determining families' disposable income. Moreover, the net family income definition does not capture another major item which significantly affects families' disposable income –

their federal and provincial income taxes. Not that we are arguing in favour of such an approach, but the logic of the government's position that child benefits should be based on a definition of income which measures disposable income also should allow the deduction of income taxes.

It is not at all clear why parents fortunate enough to work for an employer offering a pension plan or who enjoy the benefits of union or professional association membership should be provided, in effect, a larger child benefit than a family with the same income but no employer pension plan or union or professional association membership. Nor is it fair that families which contribute to RRSPs or invest in mining ventures should receive a bigger child benefit than families without RRSPs or oil and gas investments. After all, taxpayers already receive a tax break for their Registered Pension Plan and RRSP contributions and union or professional dues in the form of federal and provincial income tax savings from tax deductions.

A number of the deductions allowed for net income are very much the preserve of higher-income taxpayers and provide little or no benefit to low- and modest-income Canadians. The deduction for contributions to RRSPs – at an estimated \$10 billion in combined federal and provincial tax expenditures for 1997, the single largest tax deduction – is a revealing case in point. The most recent income tax data, for 1994, show that only 26.6 percent of all taxpayers claimed the deduction for RRSP contributions. Use of the deduction varied enormously according to income, ranging from just 3.1 percent of taxfilers with incomes under \$10,000 to 74.7 percent of those over \$100,000. The average contribution went from \$892 for the tiny group of taxfilers under \$10,000 who contribute to RRSPs to \$13,612 for the 74 percent of taxfilers with incomes over \$250,000 who contribute to RRSPs. Higher-income RRSP contributors also reap much larger federal and provincial income tax savings from their deductions because the value of deductions increases with marginal tax rates.

Several important deductions have grown significantly over the years. Canadians claiming the income tax deduction for contributions to RRSPs increased from 1.9 million or 13.0 percent of all taxfilers in 1980 to 5.4 million or 26.6 percent of all taxfilers in 1994; the total amount of RRSP contributions claimed went from \$7.2 billion to \$19.3 billion in 1994. The total amount claimed under the tax deduction for contributions to Registered Pension Plans rose from \$5.9 billion in 1980 to \$6.9 billion in 1994. Claimants of the child care expense deduction numbered 393,224 in 1980 and claimed in total \$704 million or an average \$1,791 per claimant; in 1994, 704,397 taxfilers claimed \$2.1 billion or \$2,629 per claimant. (All figures are expressed in constant 1994 dollars).

One reason for the substantial growth in such deductions is the rising labour force participation of women. Most families with children now have both parents in the workforce, which has increased the need for child care and, as a result, the number of taxfilers claiming the child care expense deduction. While only a minority of women have employer-sponsored pension plans or contribute to RRSPs, nonetheless their numbers have been growing over the years as more women join the workforce.

Another important factor is the federal government's changes to the income tax system in the 1980s and 1990s which served to increase the amounts deducted for some major items. The child care expense deduction was doubled for children under 6 (from a maximum of \$2,000 to \$4,000) and the \$8,000 maximum family limit eliminated in 1988; in 1993, the maximum amounts were increased again to \$5,000 for each child under 6 and \$3,000 for each child aged 7-14 for whom child care receipts are

available. Ottawa substantially boosted the tax deduction limit for contributions to Registered Retirement Savings Plans and removed the limit on the tax deduction for contributions to Registered Pension Plans.

We believe that the Canada Child Tax Benefit and provincial income-tested child benefits should use gross rather than net family income. Note that we are not here debating the pros and cons of deductions themselves – even though we have views on that matter – since that is another issue entirely. Rather, we simply argue that such deductions should not be allowed in defining the income upon which eligibility for and the amount of payments from federal and provincial child benefit programs are determined.

One group that requires special attention is farmers and fishers, whose gross and net incomes typically differ a good deal because they can deduct business expenses. Use of gross family income could disqualify some low- and middle-income farmers and fishers from child benefits. We recommend that governments investigate carefully the potential impact of a change to gross income and decide whether a special definition of income would be required. Governments should consider whether other families operating small businesses with substantial expenses should be specially treated as well.

### **Inadequate indexation**

The preceding analysis dealt at some length with the impact of inadequate indexation on child benefit rates and thresholds. Partial indexation of federal child benefits, and non-indexation of provincial child benefits, base the current child benefit system and the emerging National Child Benefit System on a bed of sand rather than the firm foundation that is required. The value of child benefits is eroding in a stealthy manner which allows governments to reduce expenditures surreptitiously. The declining threshold means that fewer low-income families qualify for maximum child benefits and fewer middle-income families receive partial benefits. Inadequate indexation is a regressive measure – poor and modest-income families suffer the largest proportionate loss – which weakens the progressive nature of the current and emerging child benefit systems. All three objectives of the child benefit system – anti-poverty, horizontal equity and economic stabilization – are jeopardized by inadequate indexation.

The entire child benefit system – federal and provincial, benefits and thresholds – should be adequately indexed, which means one thing only: full and automatic adjustment on an annual basis to the increase in the cost of living, as was the practice for the federal child benefit system between 1973 and 1985.

### **Family definition**

The federal Child Tax Benefit (and consequently the BC Family Bonus and any other provincial program making use of the federal program's income calculations) is based on *net family* income, as reported on the income tax form. An individual who is part of a married or common-law couple is required to supply the social insurance number and first name of his or her spouse. The tax rule is that

individuals of opposite sex living in a conjugal relationship and sharing a dwelling for 12 consecutive months, with no more than a 90-day interruption, are treated as a couple and must report the other's social insurance number.

The Child Tax Benefit provides a very powerful incentive *not* to report oneself as part of a couple on the tax form. For example, a couple in which one parent had net income of \$20,000 and the other \$30,000 qualified for a Child Tax Benefit in respect of one child under 7 of \$631 in 1996, based on combined net income of \$50,000. However, if the \$20,000 parent did not declare the income of her partner, the Child Tax Benefit would be \$1,233 – double the proper amount. As provincial benefits are layered on, the incentives not to report joint income are greatly magnified. There are few countervailing incentives in the tax structure.

We have no way of knowing whether non-reporting of family income has become a large problem, except that we seemed to run across a few examples of it in the course of our random phoning for attendees at the BC Family Bonus recipients' focus group. Revenue Canada, apparently, is attempting to develop some better estimates of the extent of the problem. We do know, however, that human nature being what it is, there likely will be an increase in non-reporting of family income as federal child benefits increase. If this rule is not fairly and evenly enforced, the family income definition effectively becomes a tax on honesty.

On the other hand, if the family income reporting rule is not or cannot be enforced, then the federal government must consider changing the rule. As an extreme example, the Child Tax Benefit could be made claimable by the lower earning spouse, with only one income being taken into account, so that family income no longer would need to be reported and everyone would be treated the same. However, this reform would add substantially to costs and would change the targeting of the programs. Costs could be offset partly by phasing out the tax credit for spouses, so that a family with a low-income spouse would have a net increase in income unless it had no children.

We are *not* advocating this or any other change. It would seem much fairer to find a way to enforce a reasonable family income reporting rule. Family income reporting issue is an important issue for the National Child Benefit System – indeed for the future development of tax-based instruments of income redistribution generally – and should be tackled as a very high priority. It is, of course, first and foremost, a problem for the federal Department of Revenue. But, given Ottawa's commitment to working with provinces and the extent to which all the provinces may use the tax system for their programs, the federal government should be careful to consult with the provinces before implementing a resolution to this potentially growing problem.

## **Raising child benefit levels**

We have argued that the goal of replacing welfare benefits for children with an income-tested child benefit for all low-income families with children is a necessary but not sufficient condition for building an effective integrated child benefit. To finish the job, the federal government must raise the maximum benefit level to cover the cost of raising a child for low-income families. Low-income parents

should receive an income benefit which enables them to provide for their children's essential needs – just as Canada already assures a basic income for all seniors.

The National Child Benefit System cannot achieve the integrated child benefit vision without further federal investment in the Canada Child Tax Benefit beyond its initial maximum level in 1998 of \$1,625 for the first child and \$1,425 for each additional child, plus the \$213 young-child supplement. If the Canada Child Tax Benefit remains at its 1998 level, the federal government will have done nothing more than modestly enrich and sensibly reconfigure its child benefit program, and the National Child Benefit System would be stillborn.

The federal government should move quickly to increase the maximum Canada Child Tax Benefit to at least \$2,500 per child – the amount required to displace welfare benefits for children in most provinces. Such an increase is within the realm of political and fiscal possibility, since the 1997 Speech From the Throne promised another \$850 million infusion. The final target should be a child benefit of around \$4,000 to cover the cost of raising a child for low-income families.

Further increases in the maximum Canada Child Tax Benefit should provide higher benefits to modest-income families (e.g., those between \$25,921 and \$35,000) by reducing the taxback rate on incomes above \$20,921 to avoid ever-steep marginal tax rates on low-income families between \$20,921 and \$25,921. Moreover, modest-income families (like middle-income and upper-income families) have suffered sizable losses in child benefits since the mid-1980s.

It is instructive to put the issue of further federal investment in child benefits into historical context. In 1984, when the federal child benefit system was made up of Family Allowances, the children's tax exemption and the refundable child tax credit, the total cost came to \$6.7 billion (in 1997 dollars) – only \$300 million short of the \$7 billion that a \$2,500 per child Canada Child Tax Benefit would cost! The extra \$2 billion needed to create a replace-welfare-benefits-for-children Canada Child Tax Benefit amounts to just 1.9 percent of total federal program spending.



## CONCLUSION

This report has put forward a number of key requirements for an evaluative framework based on the integrated child benefit concept which underlies innovative provincial child benefit programs such as the BC Family Bonus and the National Child Benefit System announced in the 1997 federal Budget. We have applied our evaluative criteria to the current child benefit system and, necessarily in a preliminary fashion, to the recently-launched BC Family Bonus and the other federal and provincial elements of the nascent National Child Benefit System.

Several issues arose from our analysis which we believe must be addressed in order to build an effective child benefit system. These issues are: the politically tough matter of not passing through initial increases in child benefits to welfare families, the use of net family income for calculating eligibility for and payments from income-tested child benefit programs, lack of adequate indexation, family definition and the imperative of future increases in child benefits. We offered some suggestions for dealing with these issues.

The National Child Benefit System is in its infancy, but it could become one of the most important social policy innovations of our generation. However, achieving that vision will require adherence to the basic requirements of the integrated child benefit model presented in this report, and upon which an evaluative framework for the National Child Benefit System should be built.

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