BRIEF ON TAX REFORM
PRESENTED TO THE STANDING COMMITTEE ON FINANCE AND ECONOMIC AFFAIRS
(The Blenkarn Committee)
AND
ANALYSIS OF THE COMMITTEE FINDINGS

December 1987

Canadian Advisory Council on the Status of Women

Reform of the tax system has been a concern of the Canadian Advisory Council on the Status of Women (CACSW) almost since its inception. We are in general agreement with the five principles of tax reform outlined in the federal government's White Paper:

- The tax system should be fair and should respect Canadian views of social justice. It should be a progressive system that will not impose a tax burden on those least able to pay;
- The tax system should have a broader base and lower rates, minimizing the special preferences that allow high-income individuals and corporations to pay little or no tax;
- The tax system should facilitate Canada's competitiveness and support regional development;
- The tax system should be more understandable and less complex than it is now;
- The tax system should provide reliable and stable revenues to finance public programs.

As an organization focussed on improving the status of women, we are particularly concerned with the first two of these objectives. We do not believe these objectives have been met in the tax reform proposals outlined by the Minister of Finance in the White Paper.

As many other groups appearing before this Committee have pointed out, many Canadians whose incomes are below the poverty level will still be required to pay taxes, even after tax reform. While 850,000 low-income people will be taken off the tax rolls by these proposals, at least a million low-income Canadians have joined the ranks of taxpayers over the past six years as a result of the limitation on indexing of the tax system and the abolition of the federal tax reduction. That so many poor people should still have to pay taxes does not seem to us to meet the Minister of Finance's objective that the tax system should not impose a burden on those least able to pay.

We strongly support the view that the tax system should be progressive. In this respect, we commend the government for the move it has taken in this direction by converting personal exemptions and some deductions to credits. This is consistent with recommendations adopted by the CACSW. However, as other groups appearing before this Committee have observed, the effect of this attempt to make the tax system more progressive is almost exactly cancelled out by changes reducing the number of tax brackets which will increase the rate of taxation on those with lower levels of taxable income and reduce the rate of taxation on those with higher levels of taxable income. We would also note that credits which are non-refundable do not benefit those at the very low end of the income scale who pay no taxes.

We must observe that, despite the Minister's stated desire to minimize preferential treatment for higher-income individuals, the tax reform proposals do not suggest changes in some significant tax breaks that benefit only higher-income Canadians. It is safe to assume that there are few women among them. We would mention, in particular, the continuance of provisions for tax-free capital gains, although investors will now be limited to a lifetime maximum of $100,000 instead of the $500,000 that was previously proposed.

We must also note that contributions to Registered Retirement Savings Plans (RRSPs) and registered pension plans continue to be tax deductible. Other deductions, such as eligible medical expenses and employee contributions to the Canada and Quebec Pension Plans, are to be converted to federal tax credits worth 17% of the amount of the expense, with a maximum dollar limit. A similar procedure could have been followed with contributions to RRSPs and registered pension plans.

This particular tax expenditure costs more than five billion dollars a year and will be even more expensive as the new higher contribution limits are phased in. The Finance Department's own figures show that it is used mostly by higher-income people, who are not in need and would no doubt continue to save for retirement even without this very expensive tax break. Very few of those who benefit are women. Only 37% of women in paid employment are members of registered pension plans,[1] and only 19% of employed women contribute to an RRSP.[2] We are particularly concerned when such huge amounts of tax dollars are allocated to programs to benefit high-income, primarily male taxpayers, while at the same time we are told that there is little or no money available for programs such as child care and other services so desperately needed by Canadian women and their families.

To the extent that high-income earners are favoured by the tax system, women for the most part are disfavoured. This happens directly and most visibly because they cannot afford to make use of favourable provisions. But indirectly, women have to bear the burden of tax breaks given to higher-income earners, who are mainly men, because taxes generally must be higher than they would otherwise be to compensate for the loss of revenue that tax expenditures involve.

Other groups and organizations appearing before this Committee have presented you with a detailed analysis of the tax reform proposals focussing on their impact on the poor and the disadvantaged in our society. (The brief presented by the National Council of Welfare has been particularly useful in this respect.) These briefs deal with many of the concerns we have about the tax reform proposals. Rather than present you with another detailed analysis of the proposals, we shall concentrate on a few key issues that we wish to draw to your attention.

Women's Incomes

Throughout many of the briefs presented to you, you will have heard concerns expressed about the impact of tax reform on low-income taxpayers. We must ask you to remember that a disproportionate number of these low-income taxpayers are women. As you are no doubt aware, the majority of adult women now work outside their homes. Among the younger generation of women — those now between the ages of 20 and 44 — more than 73% are labour force participants.[3] Almost six million Canadian women are now in the paid work force.

But these women, by and large, do not earn high salaries and their wages are not keeping up with inflation. The typical woman worker who was employed full-time for a full year in 1985 earned only $17,518. That was only two per cent more than she earned in 1984.[4] We would ask you to keep those facts in mind when you are considering the impact of tax reform on those with low earnings.

More and more women are now the sole support of their families. These women have become the poorest of the poor. We are alarmed that the poverty rate among single-parent families headed by women continues to increase steadily, so that in 1985, 60.4% of single-parent families headed by women under age 65 were poor.[5] We are even more concerned that the tax reform proposals seem to do so little to address the needs of these women. As the National Council of Welfare pointed out in its brief to you, under the current tax system, a single parent supporting two children on earnings of $20,000 — roughly the estimated poverty line in 1988 for a family of three in a large city — would owe $1,857 in federal and provincial income taxes. Tax reform will save her $532, but she will still have to pay $1,214 in income taxes. This is a situation that we find unacceptable.

The Move to Consumption Taxes

Although not specifically dealt with in the White Paper on tax reform, we are only too well aware that the second phase of tax reform is yet to come. We refer to the government's proposal to undertake extensive reforms of the federal sales tax through the introduction of a broad-based multi-staged sales tax which will replace the existing federal sales tax and the manufacturers' sales tax. This move is clearly an essential element in the overall program of tax reform. Without it, the government will be unable to recoup the loss of tax revenues that will result from the current round of changes. For this reason, we feel we must comment on this development now.

Indirect taxes like sales taxes are regressive because they impose the heaviest burden on those least able to pay. That is why we are concerned by the government's increasing reliance on these taxes as a source of revenue. Sales taxes penalize those who spend and favour those who can afford to save more of their income. As we have already noted, most women cannot afford to save because they earn so little. Most — and particularly those who are the sole support of their families — must spend a good part of their income on the essentials of food, clothing, and shelter. Consumption taxes will have major consequences for these women and for all those at the lower end of the income scale.

While the government proposes to increase the sales tax credit from the current level of $50 per adult and $25 for each dependent child under age 18, to $70 per adult and $35 for dependent children under age 18, these amounts do not protect low-income people from the effects of the current federal sales tax, and they would be totally inadequate as protection against a vastly expanded multi-stage sales tax that will come in the second round of tax reform. The National Council of Welfare estimates that the current refundable sales tax credit would have to be increased more than five-fold to fully protect low-income consumers from the impact of the existing federal sales tax.

Increasing reliance on consumption taxes certainly broadens the base of the tax system: it shifts much more of the burden on to those who can least afford it — those at the lower end of the income scale. This does not meet the Minister of Finance's professed objective of a "consistently progressive" tax system. As we have said, sales taxes are regressive. As the government gets more and more of its revenue from this source, the tax system will become less and less progressive. Instead of an expanded sales tax system, we believe the personal income tax system should be made more progressive. That means that the proportion of government revenue that comes from indirect consumption taxes should be reduced, not increased.

The Indexation of the Tax System

We must express our deep concern over the government's failure to restore full inflation indexing to the tax system. Although tax deductions are to be converted to credits, the fact that these will not be fully indexed will mean that their value will be steadily eroded as time goes by.

As you have heard from other groups that have appeared before you, partial indexation particularly hurts low-income taxpayers. The value of the tax reductions introduced as part of the tax reform package will decline steadily over the years. We are particularly concerned that inflation indexing is limited on benefits such as the child tax credit and the refundable sales tax credit and that the income thresholds at which these credits start to diminish are also not fully indexed. The limitation on indexing of family allowance payments, implemented in the 1985 budget, means that the real value of this benefit is now declining by three per cent a year. We question why a government that says it wants to offer support to families would undermine the value of benefits for families and children in this way.

Partial indexing results in an "inflation dividend" for the government. It will collect more and more revenue each year as long as inflation continues. The cost of continuing inflation will be borne by taxpayers and particularly by families who can least afford it. It has been estimated by the National Council of Welfare that, for a single parent raising two children on earnings equal to the poverty line ($19,544 in 1987), taxes increased each year from 1984 to 1987 as a result of various changes introduced by the federal government. In all, this family faced a tax increase of 31% over that three-year period. Total taxes payable by this family will drop by almost 13% as a result of tax reform — from $1,802 in 1987, to $1,355 in 1988. But we must emphasize that the amount paid in 1988 will still be greater than the taxes paid by this family in 1984.

Tax reform offers only a one-year respite in the ever-increasing tax burden for this family. Even with the substantial increase in the child tax credit, partial indexation will mean taxes will start to go up again in 1989, rising by almost 14% between 1989 and 1991. By that time, the taxes paid by this family will be almost 22% more than it paid in 1984. (These calculations are all in 1987 constant dollars.)

The Treatment of Child-care Expenses

We notice that the possibility of converting the current tax deduction for child-care expenses into a credit was considered, but that a decision has been deferred pending final development of the federal government's policy on child care. Because the deduction for child-care expenses represents tax expenditures allocated to child care, we feel it is important at this stage to reiterate our position on child care.

The CACSW believes that child care — like education and health — is an essential service which should be universally accessible. We believe that the federal government can and must take a major role in rectifying the current inadequate state of access to child care. In the long term, we believe there must be a major restructuring of federal funding for child care to ensure that child-care services are provided as a universal program comparable to education and health. We are concerned that public funds, allocated through the tax system, will not result in a universal child-care program with services accessible to all families that need them.

The Deductibility of Child-support Payments

We are disappointed that the tax reform proposals failed to address the question of deductibility of child-support payments. The current tax system allows a non-custodial parent to claim a deduction for the full amount of child support paid to the custodial parent. The parent with custody must then declare those amounts as income and pay tax on them. Because in the vast majority of cases, mothers are still granted custody of the children in divorce actions, these provisions allow a father to deduct the cost of money spent to support his children when he no longer lives with them — a right that is not granted to mothers or fathers still living in the same household with their children.

Because in most families with young children, both parents are in the paid work force, we may safely assume that where a mother is the custodial parent, she also contributes to the financial support of her children, but she is not allowed a tax deduction for the amount she spends. (We must emphasize that the custodial parent contributes to the support of her child in non-pecuniary ways through caring and being responsible for the raising of the child.) Moreover, she must pay tax on the amounts given her by her former spouse for the support of the children. This subsidy for divorce contained in the *Income Tax Act* cost $95 million in 1983. We can see no logic in, or justification for, such a policy.

The CACSW has recommended that:

- the *Income Tax Act* be amended so that the estranged spouse who receives child-support payments will no longer be required to report these sums as part of her/his income for tax purposes;
- the *Income Tax Act* be amended so that the estranged spouse who pays child support will no longer be allowed to deduct these sums from her/his income for tax purposes;
- the *Income Tax Act* be amended to allow for the splitting of the children's exemptions between estranged spouses who both contribute to the financial support of their children;
- the *Income Tax Act* be amended to allow one estranged spouse to claim the children's exemptions while the other spouse will report family allowances as part of her/his income.
- the equivalent-to-married exemption be replaced by a tax credit.

We are gratified to note that the government intends to implement the fifth recommendation. We would like to see the third and fourth recommendations applied to the new credits for dependent children.

The Unit of Taxation

We are pleased to note the Minister of Finance's statement in the White Paper that the individual and not the family will continue to be the filing unit for personal income taxation purposes, even though the House of Commons Standing Committee on Finance and Economic Affairs, in its report on tax simplification released on June 17, 1986, recommended consideration of the advisability of allowing spouses to file joint income tax returns.

The CACSW is well aware that Canadian women do not enjoy full economic equality within marriage and we believe it is very important that no new measures be introduced that will erode the independent financial position of married women. A joint taxation system would have the effect of reducing the independent financial security of married women and we are opposed to its introduction.

Nevertheless, we feel compelled to observe that, in spite of the government's affirmation of individual filing, the Canadian tax system seems to have increased the use of the marital unit in recent years. A number of important provisions assume a marital unit, for example, the spousal tax credit, the transfer of unused deductions between the spouses, the attribution rules, the refundable child tax credit, and the refundable sales tax credit.

We are of the view that the *Income Tax Act* should reduce the recognition of marital status to a minimum. The existence of such provisions creates barriers to women who may want to enter the work force and may affect the choice they must make between work in the home or work in the paid labour force. Basing tax measures on the marital unit also implies that spouses share their incomes and that both have control over their assets. Indications are that both of these assumptions may be incorrect.

The Reduction of Benefits to Families with Children

We have already noted how partial indexation of the tax system will have particularly serious consequences for families in receipt of benefits such as the child tax credit and family allowances. The National Council of Welfare's analysis shows that most families with children will lose benefits as a result of tax reform. We find this incomprehensible.

Child benefits to middle-income families, with incomes around $45,000 a year, will be cut by 28% in the first year of tax reform. Most families will lose in the longer term. As you were told by the National Council of Welfare, the poorest families with no earnings, many of which are social assistance recipients, will be no better off in 1991 than they were in 1984. (To facilitate comparisons, these calculations are all in 1987 dollars.) All other families with children, including the working poor, will face substantial losses in child benefits. Middle-income families will be hardest hit, losing more than half of their total child benefits.

We find these reductions to be completely unacceptable. Furthermore, we cannot understand why a government committed to the family, and particularly to families with children, should contemplate penalizing families in this way. We strongly urge that these measures be reconsidered so that the package of benefits going to families with children is not diminished.

Conclusions

As we indicated at the beginning of this presentation, we have not attempted to undertake a detailed analysis of the tax reform proposals in this brief. We have concentrated our remarks on broad issues that cause us concern.

The CACSW will shortly publish a discussion paper raising issues that we feel may stimulate further debate on how reform of the income tax system might be accomplished to the benefit of women as well as men. As well, in view of the fact that the tax system is not neutral in its effects on family decisions, we recommend that:

- a full investigation of the influence the tax system has on family decisions be undertaken by the federal government through a provision such as a Task Force;
- the federal government continue its reform of the tax system with special emphasis on inequalities between men and women which are inherent in the system.

In the meantime, we must reiterate what we said at the beginning of this presentation: the tax system must be fair and progressive; it must not impose tax burdens on those least able to pay (and that may include middle-income families as well as those at the lowest end of the income scale); it should minimize preferences that allow high-income individuals to pay little or no tax; and it must respect Canadian views of social justice. These were the objectives set by the Minister of Finance himself for tax reform. We believe they are not met by the current proposals.

NOTES

1. Canada, Statistics Canada, *Pension Plans in Canada* (Ottawa: 1984), Table D.

2. Calculation based on the number of women who claimed an RRSP deduction in 1984 and the number of women employed in that year. Data from Canada, Revenue Canada, Taxation, *Taxation Statistics* (Ottawa: 1986 Edition), p. 170; and Canada, Statistics Canada, *The Labour Force* (Ottawa: December 1984), Table 58.

3. Canada, Statistics Canada, *The Labour Force* (Ottawa: December 1986), Table 56.

4. Canada, Statistics Canada, *Income Distributions by Size in Canada* (Ottawa: 1985), Table 72, and *Income Distributions by Size in Canada* (Ottawa: 1984), Table 72.

5. Canada, Statistics Canada, *Income Distributions by Size in Canada* (Ottawa: 1985), Text Table IV.

The federal government's White Paper on tax reform, issued in June 1987, was referred to the House of Commons Standing Committee on Finance and Economic Affairs (Blenkarn Committee) for study. After holding hearings and receiving briefs, the Committee then issued its own report, containing some 81 recommendations, on November 16, 1987. Both the Liberal and New Democratic Party members of the Committee issued their own minority reports and recommendations. In this analysis, the Canadian Advisory Council on the Status of Women (CACSW) raises issues relating to tax reform and the Blenkarn Committee reports.

Much of the majority report endorsed the changes to the tax system proposed by the White Paper. However, some of the Committee's recommendations proposed changes to measures put forward by the White Paper. The Finance Minister is under no obligation to accept the recommendations which have been categorized by some tax experts as merely "minor tinkering".

While many of the recommendations dealt with corporate taxes, write-offs of business expenses and incentives for investors, this analysis concentrates only on the recommendations that might be of particular concern to women and that relate to the criticisms of the White Paper put forward by the CACSW and other advisory groups.

Issues of concern to women

The CACSW's brief (October 5, 1987) to the Blenkarn Committee raised these key concerns about the White Paper:

- While many tax deductions were to be converted to tax credits, major tax expenditures were to be left untouched, such as the deduction for pension plan and RRSP contributions which benefits mainly high-income taxpayers and costs more than $5 billion in lost tax revenues.

- Many of the proposed changes will still leave lower- and middle-income taxpayers no better off after tax reform and, in most cases, worse off than they were when the federal government came to power in 1984. Since women's incomes are generally low, a disproportionate number of the lower-income taxpayers adversely affected by tax reform would be women.

- The major part of tax reform — the move to a broad-based multi-staged sales tax, which will have a major adverse impact on those at the lower end of the income scale — was not addressed in the White Paper, but is a crucial part of the government's tax reform proposals.

- The government's failure to restore full indexing to the tax system will mean that the value of the new tax credits will decline every year. The erosion of the value of measures such as the child tax credit will mean that families with children will receive less and less in real terms as time goes by. Most families with children will lose benefits as a result of tax reform.

- Child-care expense deductions were not dealt with in the White Paper. The government put off any changes to this part of the tax system until it announces its national child-care policy.

- No changes were proposed in the deductibility of child-support payments. The CACSW recommends that the payments should not be deductible by the person who pays them and the parent who receives them should not have to pay tax on them.

- Measures introduced into the tax system in the past have moved it away from the individual as the unit for taxation, although the White Paper said that the individual and not the family will continue to be the filing unit for taxation purposes.

The Blenkarn Report

The report of the Blenkarn Committee does not respond directly to most of the concerns raised by the CACSW.

The major points raised by the majority report were:

- Regarding the continued deductibility of pension plan and RRSP contributions, the Committee said officials from the Department of Finance convinced Committee members that getting rid of these deductions or converting them to credits (as CPP/QPP contributions will be) would be too complicated because it would mean re-examining how pension benefits should be taxed.

- No response was offered to the many representations received from organizations such as the CACSW and the National Council of Welfare that the tax reforms proposed in the White Paper would still impose an unacceptable tax burden on lower- and middle-income taxpayers and that people with incomes below the poverty line should not have to pay taxes at all.

- In commenting on the future move to the multi-staged sales tax, which is the second phase of tax reform, the Committee agreed that the existing federal sales tax creates all kinds of inequities. However, it focussed only on the inequities faced by different kinds of businesses and not on the impact on lower-income people who must ultimately bear the cost of such regressive taxes. The Committee actually recommended that until the new sales tax system is introduced, a three per cent surtax be added to the current federal sales tax.

- The Committee made no recommendation to restore full indexing of the tax system. While acknowledging that lack of indexing will hurt lower-income taxpayers and erode the value of tax credits, the Committee said that "the fiscal situation of the federal government rules out full indexing". (Without full indexing, as the CACSW brief pointed out, the federal government reaps the benefits of inflation. The higher the inflation rate, the bigger the tax take accruing to the government.) Inexplicably, the Committee did recommend a type of indexing in the taxing of certain capital gains such as stock market profits. Minority reports from the Liberals and New Democrats, however, called for restoration of full indexing.

- There was no recommendation on the deductibility of child-care expenses. Indications are that the federal government's policy announcement on child care will consist largely of tax credits to families with children. The CACSW will be responding to this as part of its reaction to the child-care policy when it is announced.

- The one attempt made by the Committee to address the needs of families with children whose benefits will be eroded each year by the failure to restore full indexing was a series of proposals on child benefits. While these are rather limited in scope, the Committee said it felt there would be "other opportunities to address family benefits in future". The proposals are as follows:

  i) To deal with concerns about the low level of the tax credit which will replace the exemption for dependent children, the Committee proposes that the credit be doubled — but only for the third child and subsequent children. While this measure is intended to help large families, it must be noted that most young families these days have only one or two children, so they will not benefit from this proposal. The credit would be refundable and would be delivered in the form of a top-up of the federal refundable child tax credit of up to $100 per child.

  ii) For dependent children between the ages of 19 and 21, for whom parents would receive no credit or exemption under the White Paper, the Committee recommends a tax credit of $130 per child. The parent would not be able to claim this credit if the child is a student entitled to tuition and education credits, some of which are transferred to the parent.

iii) The level of income at which the refundable child tax credit starts to phase out should be increased from $24,000 to $25,500. According to the Committee, this will "slow down the erosion of the child tax credit for families with incomes near and above the turning point". However, since it is only intended as a one-time boost, erosion of benefits because of limited inflation indexing will merely resume in subsequent years.

iv) The Committee said it would be fairer if taxation of family benefits were based on family income, as is done with the child tax credit. But extending this method to family allowances would be too complicated. It recommended that the parent with the higher income be required to include family allowances in income. (Under the current system, the person who claims the personal exemption for the child must also declare the family allowance.)

v) A spouse or dependant should be able to report up to $1,000 in net income (instead of the $500 proposed in the White Paper) before the full value of the tax credit available to the supporting taxpayer begins to be reduced.

The cost of these five measures was estimated by the Committee at $225 million. The Committee proposed that the money to pay for these and its other suggested measures be raised by increasing taxes on banks, other financial institutions, and real estate companies by $400 million a year and by the surtax on sales taxes which it said would raise another $125 million a year.

Ironically, the sales tax increase would hit hardest at lower-income families with children — the very families the Committee claimed to be helping with the child benefit changes. Higher taxes on financial institutions are likely to be strongly resisted by the powerful lobbies of the financial industry.