

ANNOTATED RECOMMENDATIONS OF THE ADVISORY COUNCIL ON THE  
STATUS OF WOMEN ON THE SUBJECT OF WOMEN AND TAXATION

At its January, April and June 1977 meetings, the Advisory Council on the Status of Women (ACSW) adopted recommendations on the following subjects: 1) the issue of joint taxation of the incomes of spouses; 2) the taxation of the incomes of wives or husbands working as employees in unincorporated businesses or farms wholly or partly belonging to their spouses; 3) the tax treatment of husband-wife partnerships; 4) tax benefits for child care expenses; 5) tax benefits to parents of young children; and 6) the tax deductibility of alimony/maintenance payments.

These recommendations will be reviewed in the order in which they were adopted, with the exception of those on child care expenses which were adopted partly in January and partly in April.

1. JOINT TAXATION OF THE INCOMES OF SPOUSES

The ACSW's statement on this subject gives the following explanation of the way in which a joint taxation system would work:

"Unlike the present Canadian system, which taxes the income of each spouse on a separate basis, the joint taxation system calls for one tax return for both spouses. It determines the spouses' rates of tax on the basis of their combined income, and it links the tax situation of one spouse to the income of the other spouse."

The reasons why the ACSW has felt it necessary to examine the joint taxation proposal are as follows:

- 1) The Royal Commission on the Status of Women recommended that a joint taxation system be introduced in Canada (although commissioner Elsie Gregory MacGill strongly disagreed and chairman Florence Bird later reversed her stand);
- 2) The 1975-76 federal government inter-departmental committee on the taxation of women seriously considered the possibility of introducing a system of joint taxation in Canada and eventually rejected it by a narrow margin; and
- 3) There is continuing pressure from federal Revenue Department officials to have this system introduced in Canada.

As the report of the Royal Commission on the Status of Women contained no discussion of the issues involved (the whole matter is disposed of in 1½ paragraphs), the ACSW taxation committee did a complete analysis of the subject.

The arguments in favour of joint taxation were as follows: a) a joint taxation system, because it lumps together the incomes of the spouses for tax purposes, would do away with the present necessity of keeping a strict control over transfers of income between spouses (who can now reduce their total tax burden by artificially splitting their incomes between them); b) if spouses are true economic partners, the present system is unfair because it taxes one-earner couples at a higher rate than two-earner couples; and c) from an administrative point of view, the system would be simpler because fewer tax returns would be filed.

On the other hand, the arguments against joint taxation were the following: a) the introduction of a joint return system would impose higher taxes on the lower-income spouse (usually the wife) in order to subsidize lower taxes for the higher-income spouse (generally the husband); b) because two-earner couples' taxes would be considerably increased, there would be a great disincentive for married women to work outside the home; c) if measures could be introduced to remedy the first of these problems (a), the system would become so complex that it would become difficult to administer, which would defeat the purpose; and d) some people oppose joint taxation as a violation of their human rights (it is discrimination because of marital status).

After analyzing and weighing these arguments, the ACSW endorsed the following statement in January 1977:

- "1) Joint taxation of the spouses might prove to be the ideal system in a society where spouses enjoyed full financial equality and were true economic partners;
- 2) In spite of the ACSW's repeated calls for modifications in Canadian matrimonial property laws to make them reflect its conviction that spouses should be true economic partners, progress has been extremely slow in this area and a great deal remains to be done before women can achieve financial equality within the institution of marriage;
- 3) Until Canadian women enjoy full economic equality within marriage, it is very important that no new measure be introduced that will further erode the independent financial position of married women;

- 4) As demonstrated in the Appendix, a joint taxation system would have the effect of reducing the independent financial security of married women who have personal sources of income;
- 5) Taxation statistics issued by the Revenue Department for the year 1974 (the last year for which data is available) indicate that 45.5% of all married Canadian women had income on which they filed tax returns. Labour force statistics indicate a continuing increase in the proportion of married women joining the labour force;
- 6) In view of the above, the ACSW believes that it would be premature on the part of the Canadian government to introduce a system of joint taxation of the spouses in Canada."

## II. WIVES OR HUSBANDS EMPLOYED IN THEIR SPOUSES' UNINCORPORATED BUSINESSES

The following ACSW recommendations on this subject, adopted in April 1977, are self-explanatory:

"At the present time, subsections 74(3) and 74(4) of the Income Tax Act forbid the owner of an unincorporated business or farm to deduct as an expense the salaries paid to his or her spouse. This discourages husbands from paying salaries to their wives, and denies wives access to unemployment insurance, pensions and other fringe benefits.

According to Revenue Department officials, the purpose of this prohibition is to reduce possibilities of artificial income-splitting between the spouses. On the other hand, the Income Tax Act does not prohibit the owner of an

unincorporated business or farm from deducting wages paid to his or her adult children, nor does it prohibit owners of incorporated businesses or farms from deducting salaries paid to their spouses or children.

The ACSW believes that it is undesirable to discourage women from working in their husbands' businesses: wives' contributions are often essential to the viability of the enterprise, and many women find themselves in a situation where they have to run the family business or farm after their husband's death.

We would also argue that if the Revenue Department can police cases of artificial income-splitting between parents and children, as well as between spouses who work in an incorporated family business, there is no reason why it should not also be able to police similar cases involving spouses working in unincorporated businesses and farms.

As a result, the ACSW recommends that subsections 74(3) and 74(4) of the Income Tax Act be repealed as soon as possible."

### III. HUSBAND AND WIFE PARTNERSHIPS

The following recommendations, which were adopted at the same time as the preceding ones, are also self-explanatory:

"When spouses enter into a partnership together, subsection 74(5) of the Income Tax Act allows the Revenue Department, at its discretion, to deem one spouse's share of the partnership income to be the income of the other spouse for tax purposes. This means that a husband may be forced to

pay tax on his wife's partnership income, even though he has no legal right to any part of that income. Needless to say, this provision discourages spouses from entering into partnerships with each other.

The ACSW has concluded that apart from being discriminatory, subsection 74(5) is totally unnecessary in preventing abuse as the Income Tax Act contains other adequate provisions designed to ensure that partners do not engage in practices that would artificially reduce their combined tax burden.

Consequently, the ACSW recommends that subsection 74(5) be repealed as soon as possible."

#### IV. DEDUCTIONS FOR CHILD CARE EXPENSES

In 1970, when the Royal Commission on the Status of Women presented its report, the present child care deduction had been proposed but not yet introduced. The RCSW expressed the following two main objections to it:

"First, allowing the deduction of actual expenses would tend to be more profitable to taxpayers in the higher-income brackets than it would to those in the lower-income groups, as this is the normal effect of an exemption. We are opposed to this tax relief being granted in the form of deductions, because it tends to give an undue advantage to the people who already have a greater ability to pay.

Our second objection is that the deduction is contingent on the mother being in the labour force. The proposed change does not recognize the care given to a child by a mother who stays at home."

As shown in the following, the ACSW's views are very similar, although not quite as visionary, as those of the Royal Commission:

In January 1977, the ACSW urged the federal government to adopt immediate temporary measures designed to reduce the tax system's present discrimination against men in the area of child care expense deductions. More specifically, the ACSW stated that: "At present, only women in the labour force can claim child care expenses when a spouse is a student. The ACSW recommends that when either spouse is a student, the wage-earning spouse be allowed to claim child care expenses regardless of sex."

In April 1977, after further study of this subject, the ACSW stated the following:

"The ACSW has found that the child care expense provisions of the Income Tax Act are inadequate in many respects. First, this benefit is given as a deduction, which means that the same expense will give rise to a larger tax saving for women having the highest incomes. Secondly, for various reasons many babysitters refuse to provide receipts, with the result that many women cannot produce the necessary proofs of the real expenses they have incurred. Thirdly, the present system discriminates against men, who can only claim the deduction if they are single parents with custody or if their wives are disabled or institutionalized. Finally, the present system totally fails to recognize the value of child care services provided by homemakers who are not in the labour force.

After a study of the many possible alternatives, the ACSW has found that the first three of the four above-

mentioned problems could be remedied by replacing the present child care deduction with a flat-rate no-receipts credit to be granted to single parents in the labour force and to two-earner families with young children. In the latter case, this credit should be given to the lower-income spouse, regardless of sex.

The ACSW recommends that the federal government introduce this new system as soon as possible.

However, the Council is aware that this would still fail to recognize the child care contribution of the mother who works in the home. As the Royal Commission on the Status of Women reported in 1970, 'Any compensation for the cost of caring for a dependent should not be contingent on the mother being in the labour force, because these services have to be provided whether the mother works in the home or outside. For the mother who works at home, this cost might be valued in terms of the cash income she foregoes by looking after children at home instead of taking paid employment'.

The ACSW realizes that child care credits that were made refundable to all mothers at home would represent a considerable change in the nature and size of government's present financial commitment for child care. At the same time, the ACSW believes that such refundable credits should be among the government's long-term goals, because it is only when child care benefits are substantially increased and made available to homemakers that mothers of young children will have a true choice of working inside or outside their home."



V. EXEMPTIONS FOR DEPENDENT CHILDREN

The following ACSW recommendations, adopted in April 1977, are essentially an endorsement of the recommendations of the Royal Commission on the Status of Women on exemptions for dependent children:

"The ACSW wishes to commend the federal government for its recent introduction of a credit for dependent children in the 1977 taxation year. Although this measure is not totally satisfactory, because it gives little or no benefits to families whose federal tax is lower than the amount of the credit, the ACSW sees it as a step in the right direction in making all provisions for dependent children more equitable.

The children's exemptions, however, still continue to exist, and like all other deductions they grant larger benefits to higher-income families.

The Royal Commission on the Status of Women recommended that the solution would be to provide substantial cash allowances for dependent children. 'This allowance should be taxed to avoid subsidizing wealthy families and to enable the government to recoup part of the money distributed', said the Royal Commission.

The ACSW agrees with this position and consequently recommends that children's exemptions be abolished and the funds thereby saved be used to increase taxable family allowances."

VI. TAX DEDUCTIBILITY OF ALIMONY/MAINTENANCE PAYMENTS

The following recommendations were adopted in June

1977. A few comments were added in January 1978 for additional clarification:

"The federal Income Tax Act (subsections 60(b), 60(c), 56(b) and 56(c)) presently states that periodic alimony or maintenance payments for the support of an estranged spouse and/or children of the marriage can be deducted from the income of the paying spouse (usually the husband) and must be included in the taxable income of the receiving spouse (usually the wife).

Women have reported many problems with this system. In theory, it should be advantageous to them: as the husband's marginal tax rate is usually higher than his wife's, the splitting of income between the spouses for tax purposes reduces their total tax burden. The tax saving thus effected is presumably passed on to the wife in the form of an increased amount for support.

In practice, however, many women know that the tax saving was not taken into account when lawyers and judges set the level of their alimony and/or maintenance payments. Also, some lawyers admit that tax is not often considered in the bargaining process that establishes the alimony/maintenance amounts. And one fact has been substantiated by numerous complaints: women who separate and/or divorce are very seldom adequately informed of the tax implications of these procedures.

The result of this lack of information is that many women get all the disadvantages of the system (having to pay tax on their alimony/maintenance payments) and none of its advantages (the benefit of the possible tax savings).

Another serious drawback for women who collect alimony and/or maintenance is that their tax burden will be quite high if they decide to return to the labour force. As even women who are well informed on the subject of tax can seldom predict their future income levels (and marginal tax rates), this element can almost never be taken into account at the time of their original alimony/maintenance settlement.

The ACSW believes that any analysis of tax measures concerning alimony and/or maintenance payments must make a distinction between support paid for the maintenance of spouses and that paid for the maintenance of dependent children.

Money received by an estranged wife for her own support can truly be said to be under her full control. As she can spend these sums in any way she wants, the ACSW believes that it is fair to add them to her own income for tax purposes.

On the other hand, money received by an estranged wife for the maintenance of the children in her custody is not under her full control. She is in a position similar to that of a trustee holding money for the benefit of the children, and she is not free to spend this money in any way she wishes. As trustees are not expected to pay tax on the money they administer for others, the ACSW believes that women in this position should not have to pay tax on the money they receive for child support.

THE ACSW THEREFORE RECOMMENDS 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.

Except for the standard children's exemptions, fathers who live with their families are not allowed to deduct from their income the sums of money they spend on the support of their children. The ACSW believes that there is no justification for allowing estranged fathers to do so, nor is there any justification for obliging estranged wives to subsidize their husbands by paying the tax on these amounts.

THE ACSW THEREFORE RECOMMENDS THAT 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 HIS/HER INCOME FOR TAX PURPOSES.

If estranged fathers are required to pay the tax on the money they give for child support, the ACSW believes that they should be entitled to claim the regular tax exemptions presently allowed for dependent children (Note: The problem of equity between ordinary and estranged fathers would not exist if the government accepted the ACSW's April 1977 recommendation that children's exemptions be abolished and the funds thereby saved be used to increase family allowances.)

THE ACSW THEREFORE RECOMMENDS AS A TEMPORARY MEASURE THAT THE INCOME TAX ACT BE AMENDED TO ALLOW ESTRANGED SPOUSES WHO PAY CHILD SUPPORT TO CLAIM THE REGULAR TAX EXEMPTIONS FOR DEPENDENT CHILDREN.

Where both estranged spouses contribute to the financial support of the children, the ACSW believes that provision should be made for splitting the present children's exemptions between them. However, the ACSW also believes that the parent who has custody of the children and receives family allowances should continue to report those allowances as part of her/his income.

THE ACSW THEREFORE RECOMMENDS THAT 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.

At the present time, the Income Tax Act requires that the spouse who claims the children's exemptions also be the one who declares the family allowances as part of his/her taxable income. This should be changed to allow for the implementation of the two recommendations which were made above.

THE ACSW ALSO RECOMMENDS THAT 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.

Single parents (whether unmarried, divorced, separated or widowed) are presently allowed to claim a special "Equivalent-to-married" exemption when they keep a separate household for themselves and their dependent children. This exemption is in most cases allowed instead of the regular exemption for one of the dependent children.

The ACSW believes that the "Equivalent-to-married" exemption is unfair because, like all deductions, it grants larger benefits to upper than to lower-income people.

THE ACSW THEREFORE RECOMMENDS THAT THE EQUIVALENT-TO-MARRIED EXEMPTION BE REPLACED BY A TAX CREDIT.

At the present time, only periodic alimony/maintenance payments are deductible from a paying spouse's income. This has the effect of discouraging husbands from making lump sum settlements when a marriage is dissolved. Many women resent

this because they want to be able to choose between periodic or lump sum settlements. In some cases, it may be that women would prefer lump sum payments as making them more independent and better able to reorganize their lives.

FOR THESE REASONS, THE ACSW RECOMMENDS THAT LUMP SUM PAYMENTS FOR THE SUPPORT OF ESTRANGED SPOUSES BE MADE DEDUCTIBLE FROM THE INCOME OF THE PAYING SPOUSE OVER A REASONABLE PERIOD OF TIME."

APPENDIX

Joint taxation would raise the tax burden of the lower-earning spouse (usually the wife) to the benefit of the higher-earning spouse. The joint taxation rate schedule developed in 1975 for the Law Reform Commission of Canada gives the following results:

TABLE I

Couple A

<u>Taxable Incomes</u>		<u>Tax before Marriage</u>	<u>Tax after Marriage</u>	<u>Difference after Marriage</u>
Man makes	\$10,000	\$1,870	\$1,640	- \$230
Woman makes	\$ 5,000	\$ 650	\$ 820	+ \$170

Couple B

<u>Taxable Incomes</u>		<u>Tax before Marriage</u>	<u>Tax after Marriage</u>	<u>Difference after Marriage</u>
Man makes	\$20,000	\$4,830	\$4,328	- \$502
Woman makes	\$ 5,000	\$ 650	\$1,082	+ \$432

Joint taxation would also cause the rate of tax on the income of the lower-income spouse (normally the wife) to be greater. In effect, the wife's income would be taxed at the highest marginal tax rate of the husband. Again, using the Law Reform Commission joint taxation rate schedule, we see the following results:

TABLE 2

<u>Wife's Taxable Income</u>	<u>Husband's Taxable Income</u>	<u>Average Rate of Tax on Wife's Income</u>	<u>Additional Income from Wife's Work</u>
\$5,000	\$10,000	23%	\$3,850
\$5,000	\$20,000	32%	\$3,400
\$5,000	\$30,000	43%	\$2,850
\$5,000	\$40,000	50%	\$2,500

Table 2 shows that the average rates applied to married women's earnings under a joint taxation system would go from high to exorbitant. A comparison with the present Canadian tax system shows that 20% average tax rates are not now applied to incomes of less than \$15,000 to \$25,000 (depending on the taxpayer's exemptions and deductions).



A PRELIMINARY STATEMENT ON TAXATION

CACSW  
(Jan. 1977)

CHILD CARE

At present, only women in the labour force can claim child care expenses when a spouse is a student. ACSW recommends that when either spouse is a student, the wage-earning spouse should be allowed to claim child care expenses regardless of sex.

JOINT TAXATION OF THE INCOMES OF SPOUSES

The Advisory Council on the Status of Women is at present making an in-depth study of the Canadian income tax system and of the ways in which it affects women's financial positions and choices of lifestyles, and will make further representations on this subject at a future date.

As a first step in this study, the Council has considered the advisability of introducing in Canada a system of joint taxation of the incomes of spouses similar to that presently in force in the United States. Unlike the present Canadian system, which taxes the income of each spouse on a separate basis, the joint taxation system calls for one tax return for both spouses. It determines the spouses' rates of tax on the basis of their combined income, and it links the tax situation of one spouse to the income of the other spouse.

The ACSW's analysis of the present system and of the joint taxation alternative has led it to the following preliminary proposal:

- 1) Joint taxation of the spouses might prove to be the ideal system in a society where spouses enjoyed full financial equality and were true economic partners;
- 2) In spite of the ACSW's repeated calls for modifications in Canadian matrimonial property laws to make them reflect its conviction that spouses should be true economic partners, progress has been extremely slow in this area and a great deal remains to be done before women can achieve financial equality within the institution of marriage;
- 3) Until Canadian women enjoy full economic equality within marriage, it is very important that no new measure be introduced that will further erode the independent financial position of married women;
- 4) As demonstrated in the Appendix, a joint taxation system would have the effect of reducing the independent financial security of married women who have personal sources of income;
- 5) Taxation statistics issued by the Revenue Department for the year 1974 (the last year for which data is available) indicate that 45.5% of all married Canadian women had income on which they filed tax returns. Labour force statistics indicate a continuing increase in the proportion of married women joining the labour force;

- 6) In view of the above, the ACSW believes that it would be premature on the part of the Canadian government to introduce a system of joint taxation of the spouses in Canada.

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Joint taxation would also cause the rate of tax on the income of the lower-income spouse (normally the wife) to be greater. In effect, the wife's income would be taxed at the highest marginal tax rate of the husband. Again, using the Law Reform Commission joint taxation rate schedule, we see the following results:

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