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ANALYSIS OF SOCIAL SAFETY NET REVEALS MAJOR GAPS, SAYS TASK FORCE OF CIVIC LEADERS

TORONTO – A new report prepared by TD Economics on behalf of the Task Force for Modernizing Income Security for Working Age Adults (MISWAA) highlights the need for broad-based income security reform in Canada. The MISWAA Task Force, of which TD Bank Financial Group is a member, was launched last year by the Toronto City Summit Alliance (TCSA) and Toronto's St. Christopher House to identify failings in the present income security system and recommend a road map for change. The Task Force is composed of leaders from the business, academic, government and non-profit sectors, including those with first-hand experience dealing with income security issues.

"While Canadian governments have made great strides in recent years in improving the financial security of children and senior citizens, the needs of low-income working age adults have been comparatively neglected," said David Pecaut, Chair of the Toronto City Summit Alliance and co-Chair of the MISWAA Task Force. "There is overwhelming evidence that current policies and programs do little to support adults in gaining economic independence and forming a stable attachment to the labour force – and, in some cases, run contrary to this objective." There is a social and an economic urgency to tackling these problems. "The challenges posed by an aging population make it imperative that no effort be spared to bring adults who can work into the labour force," noted Pecaut. "And, while this is true across the country, it has particular relevance in Ontario, where changes in the way that income security programs are funded and delivered mean that municipal governments will face a serious financial crunch during the next economic downturn."

The TD paper being released today focuses on a segment of the working age population that is particularly at risk – recipients of social assistance, who have been hard hit by a decade of cuts to welfare delivered by provincial governments intent on trimming deficits. "TD's report is a major contribution to the work of the Task Force," said Pecaut. It clearly lays out the scope and complexity of the problem, and provides valuable insight into the policy recommendations the Task Force is weighing."

TD study highlights challenges associated with welfare reform

In the mid-1990s, the Ontario government took steps to reduce the size of its welfare program, by tightening eligibility requirements for social assistance and slashing benefits. "The provincial government defended the measures on the grounds that they would help nudge more adults into workforce, thereby laying the groundwork for a more enduring solution to the problem of poverty," said Don Drummond, Senior Vice President and Chief Economist of TD Bank Financial Group. "But, while welfare caseloads did fall in the ensuing years, a closer look at the data suggests the real driver was fewer people being able to get on welfare – not the intended exodus of welfare recipients into the workforce."

Part of the reason is that, even when the real value of welfare allowances is substantially reduced, the structure of most welfare programs gives recipients little financial incentive to get off social assistance. When people exit welfare, they lose cash and non-cash benefits, and incur new work-related expenses, that their employment earnings often aren't sufficient to cover, leaving them no better, or even worse off, as a result of taking a job. "It's important to recognize that this is not a problem that policy makers can completely resolve," cautioned Drummond. To keep the income security system affordable, needs-tested benefits like welfare have to be scaled back as recipients' incomes rise. But, the phase-out inevitably raises marginal effective tax rates, limiting the gains that people realize from earning extra income. "Still, while the trade-off can't be eliminated, better program design can mitigate some of its worst aspects."

In August 2005, the McGuinty government made an effort to do just that with Ontario's welfare system, introducing a new set of rules for Ontario Works (OW). The TD report studies the impact of those changes on a couple of hypothetical welfare recipients in the province, to see how well the new rules live up to their stated purpose of helping OW clients make a permanent and successful transition into the workforce.

Main findings of the TD report:

- With respect to the primary goal of 'making work pay', the new Ontario Works rules represent an improvement over their predecessors, delivering a measurable reduction in the marginal effective tax rates that OW recipients face as they try to work their way off welfare. "This was one of the principal criticisms of the old system, with welfare recipients facing marginal effective tax rates of 100 per cent or more at most stages along the welfare/work spectrum – giving them virtually no incentive to boost their market income," remarked Drummond. "The new earnings exemption, which lowers the taxback rate on employment income, goes a long way toward easing this problem, as does the temporary extension of the drug and dental benefits, which makes the welfare wall at the point of exit from OW a little more permeable."

- Still, the reality is that, even with the changes, welfare recipients in Ontario still face marginal effective tax rates of well over 50 per cent. "That's higher than the top marginal rate faced by Canada's highest income earners," noted Drummond, "and for OW clients, these high taxback rates go hand in hand with disposable incomes that are very low in absolute terms." However, there is only so much the welfare system alone can do to remedy the latter problem.

- Similarly, the August 2005 rules exacerbate existing inequities between low-income adults inside and outside the welfare system, but a closer examination of the reasons why suggests that the main cause is weaknesses in the rest of Canada's income security apparatus. "Welfare can and should be reformed to improve work incentives for social assistance recipients," argued Drummond. "But, it is not a substitute for a well-defined set of social policies, and when it's called upon to play that role, no one is well served."

More clarity needed regarding welfare's proper scope

"It's essential to have realistic expectations about what welfare can and cannot be expected to do," said Drummond. In recent years, welfare systems have been pressed into service to paper over too many cracks in the rest of the income security system – a prime example being poverty among working adults. Many adults outside the welfare system today aren't earning an adequate income, despite having a significant attachment to the labour force. “No amount of tinkering with welfare rules can solve this. Complementary measures are needed to boost after-tax incomes at the low end of the income scale – and, the welfare system is the wrong vehicle to provide them.”

Susan Pigott, CEO of St. Christopher House and co-Chair of MISWAA, said, “This is where TD Bank’s research showcases the importance of what the Task Force is trying to do. As a front-line agency working in the community, St. Christopher House has firsthand experience with the struggles that low-income adults encounter, and it’s clear that these problems are not confined to the welfare system.” Social assistance recipients do face major barriers to entering the workforce. But, even if they succeed in making that transition, their problems are far from over. “People want to work, but when they find a job and still can’t make ends meet, it’s terribly discouraging for them,” said Pigott. “And, it should be for us, too. We shouldn’t settle for a system where people are working but still not able to support themselves and their families.”

Comprehensive approach means tackling welfare, and the world beyond

While the August 2005 OW rules achieve their primary goal of strengthening work incentives, there is room for further improvement in the system.

- **Asset limits:** “One area that stands out in particular – and received no attention with last month’s rule changes – is the asset side of the equation,” remarked Drummond. At present, OW clients are permitted to accumulate savings equivalent to only 1-2 months’ worth of their monthly cash allowance. “That suggests insufficient attention to enhancing opportunities to save – surely an important corollary to promoting incentives to work,” he added. “In the financial community, we’re always urging Canadians to save more, because we know how important even a small pool of savings can be in cushioning families through a financial shock.”

So, a clear case can be made for raising OW asset limits, to give people more room to build up their savings. But, that is about the only additional reform that Ontario Works can be expected to make on its own. The remaining flaws in the system arise largely from situations where welfare has had to expand beyond its natural domain of providing short-term income support, into offering broader forms of assistance. As such, these flaws cannot be corrected without supporting changes in the rest of the income security system.

The TD report raises several ideas for consideration that MISWAA Task Force will be taking under advisement as it proceeds with its work:

- **Working income supplement/refundable tax credit for low-income Canadians:** One of most pervasive needs is tackling the broader problem of poverty, among people on and off welfare. "Raising welfare rates to help the former group isn't the answer, because it reduces the relative attractiveness of work," warned Drummond. "And, substantially increasing the minimum wage risks labour market repercussions". Two options that might be considered are a working income supplement and a refundable tax credit for low-income adults. Some jurisdictions in Canada have had success with measures of both sorts, on a smaller scale. "It's not a perfect solution – there would be a net cost, and because both measures would need to be income-tested, they would raise marginal effective tax rates over some range of income. But, if properly designed, the two measures would take some of the pressure off welfare to shore up the financial security of low-income adults. And, they would have the virtue of doing so through anonymous, rules-based programs that are free of the stigma and intrusive administrative oversight that go along with discretionary programs like welfare."

- **Completing the National Child Benefit (NCB) initiative:** The 1998 NCB initiative offers provincial and territorial governments an opportunity to use the federal NCB Supplement as a platform for developing an integrated, income-tested benefit for Canadian children that would eventually replace welfare-based child benefits. "Ontario is part of the way there, with the Ontario Child Care Supplement for Working Families (OCCS)," commented Drummond, "but the program serves only a small segment of the low-income population – namely, low-income families with children under the age of 7." That leaves a healthy chunk of income support for low-income children in Ontario to be paid through the welfare system. As a result, OW has to pay parents a substantially higher allowance than it pays single adults, and this produces a number of distortions in the work incentives and opportunities available to these two household types. Completing the NCB initiative would eliminate the source of these distortions, enhancing OW's ability to function as a temporary income support program that provides genuine and fair work opportunities to all recipients.

- **Employment Insurance (EI) reform:** A decline in the share of the unemployed population covered by the federal government's EI program has left low-income adults with fewer resources to fall back on when they lose their jobs. This has put more pressure on provincial welfare systems, and many have responded by raising entry barriers – chiefly, by imposing disqualification periods during which earnings exemptions that existing clients can claim are denied to new applicants. The result is a growing problem with horizontal inequity, where two households with similar financial profiles end up in very different economic circumstances, because one has access to all the supports of OW and the other doesn't.

  "It's possible that reforms to EI implemented in the 1990s may have gone too far in raising hours of work requirements, particularly in areas with low unemployment rates," acknowledged Drummond. "But, the problem seems to be related more to shifts in the composition of the labour force that the present EI system is ill-equipped to deal with." A rising trend toward self-employment, and an increase in the number of recent immigrants, who have no prior work experience in Canada – two groups who would have been ineligible for EI benefits even prior to the 1990s rule changes – stand out as obvious examples. "Complementary, stand-alone programs might be of some use here, to ensure that individuals who are not eligible for direct unemployment insurance do not also lose out on related services, like assistance with skills development and training," said Drummond. If unemployed adults were better served by EI, there should be correspondingly less need for provincial governments to keep entry barriers to welfare so high that they risk denying access to people who are legitimate candidates for social assistance.

The TD report, *From Welfare to Work in Ontario: Still the Road Less Travelled*, is available in PDF format on TD Economics' Home Page at www.td.com/economics.

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About the Task Force on Modernizing Income Security for Working Age Adults (MISWAA)

MISWAA was launched in late 2004 by the Toronto City Summit Alliance (TCSA) and Toronto's St. Christopher House and comprises over fifty civic leaders from many sectors including business, academia, community service, and organized labour, as well as low-income adults and front-line agencies with first-hand experience dealing with income security issues. MISWAA's goal is to discover why the current system of income security is failing and to make recommendations for reform aimed at the federal, Ontario and municipal levels of government, as well as other parts of society that can be part of the solution. MISWAA will then focus on ensuring that its recommendations are implemented.

The Atkinson Charitable Foundation is MISWAA's lead sponsor and provided seed money to set up the Task Force. Additional funding is being provided by the private sector including TD Bank Financial Group and KPMG, the United Way of Greater Toronto, and foundations including the Laidlaw Foundation, the Law Foundation of Ontario, the Maytree Foundation, and The J.W. McConnell Family Foundation.

About the Toronto City Summit Alliance

The Toronto City Summit Alliance (TCSA) is a non-partisan coalition of civic leaders from the private and public sectors, labour, voluntary associations and agencies, think tanks and academia in the Toronto region, as well as a network of hundreds of volunteers – who all share a concern about the challenges to the future of the city region such as poor economic integration of immigrants, decaying infrastructure, and lack of affordable housing. In April 2003, the TCSA published Enough Talk: An Action Plan for the Toronto Region. Since then it has been advocating for its recommendations and working with community partners and governments towards their implementation.

About St. Christopher House

St. Christopher House is a Toronto-based neighbourhood centre with 93 years of experience working with diverse individuals, families and groups. It provides support to people of all ages, including immigrants and people who are lower-income, and is strongly committed to community development in all aspects of its work.