

ONTARIO 360 – INCOME SUPPORT FOR LOW-INCOME WORKERS – TRANSITION BRIEFING

A holistic approach to supporting Ontario’s working poor

Issue

Ontario’s three major political parties have made election commitments to help the working poor.¹ This is a positive development – especially since low-income households have experienced minimal income (average adjusted market income) growth in recent years.²

There are two primary policies that can help the working poor: the minimum wage and targeted tax credits. Much of the policy discussion at the provincial level has centered on the minimum wage. Each party has indicated support for raising the minimum wage though they disagree on the timing, the magnitude, and certainty to future increases. What has received much less public discussion is the role for targeted tax credits, typically only mentioned as a substitute for minimum wage policies. Rather than these two policies being either/or propositions, they should be considered complementary policies and any incoming government should ensure that targeted tax credits are aligned with minimum wage changes and the broad-based goal of supporting the working poor.

Overview

Ontario’s median income growth lagged behind the other provinces between 2005 and 2015. The province’s median household income grew by 3.8 percent

¹ For more on the “working poor” including definitions and profiles, see Dominique Fleury and Myriam Fortin, Research Briefs - Canada’s Working Poor, Policy Horizons (Government of Canada), September 29, 2017. Available at: www.horizons.gc.ca/en/content/research-briefs-canada's-working-poor.

² See Exhibit #6 in Institute for Competitiveness and Prosperity, Ontario Economic Update October 2017: Lowest median income growth in Canada - what gives?, October 4, 2017. Available at: <https://www.competeprosper.ca/blog/ontario-economic-update-lowest-median-income-growth-in-canada-what-gives>.

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over this period versus 12.7 percent for Canada as a whole.³ Low-income households were particularly susceptible to modest growth.

It is understandable that the various political parties have committed to policies that will target this population group. The truth is that there is an under-recognized political consensus on the role of government and public policy to support low-income households. Just one example: the Working Income Tax Benefit (now called the Canada Workers Benefit) has been the subject of a political consensus at the federal level for several years.⁴

In Ontario, the current government has increased the minimum wage from \$11.60 to \$14 per hour effective January 1, 2018 and has legislated it to increase to \$15 in 2019. There has since been political debate about following through on the second scheduled increase or whether it is preferable to extend tax relief to minimum wage earners.

This focus on supporting the province's working poor is positive. There are no easy or right answers. While it has been shown that tax credits would have to be significantly enriched and modified to achieve the same after-tax income as an increase in the minimum wage⁵, it is also true that increases in the minimum wage erode purchasing power through increase inflation, reduce future labour market growth, and, as I will explain, risks reducing one's eligibility for current targeted tax benefits. If, instead, these two policies are used in a complementary fashion, it can help mitigate these negative effects and deliver much-needed support to the working poor.

³ Statistics Canada, Household income in Canada: Key results from the 2016 Census, September 13, 2017. Available at: <https://www.statcan.gc.ca/daily-quotidien/170913/dq170913a-eng.htm>.

⁴ Sean Speer and Rob Gillezeau, "The cross-party case for the Working Income Tax Benefit," Policy Options (IRPP), December 7, 2016. Available at: policyoptions.irpp.org/magazines/december-2016/the-cross-party-case-for-the-working-income-tax-benefit/.

⁵ Lindsay M. Tedds, "The Great Ontario Minimum Wage Debate of 2018," Dead For Tax Reasons, April 18, 2018. Available at: <https://deadfortaxreasons.wordpress.com/2018/04/18/the-great-ontario-minimum-wage-tax-debate-of-2018/>

It is important to remember that any policies to increase market- and after-tax incomes for low-income Ontarians will build upon the existing panoply of federal, provincial, and municipal transfers and benefits. There is insufficient room to cover the full range of programs here, but it is worth highlighting a couple – especially since they will necessarily interact with other provincial policies such as minimum wage increases.

Ontario Tax Reduction (OTR)

While the basic personal amount is often touted as a way to deliver tax relief to lower income workers, it is not well targeted. Every tax filer, regardless of income, benefits from raising the basic exemption so it is an expensive way to provide targeted tax relief. Think of it this way: someone who earns \$10,500 benefits the same as someone who earns \$1 million.

The Ontario tax system does already have another, more targeted feature designed to help low-income individuals called the Ontario Tax Reduction (OTR). The OTR is a non-refundable tax credit that acts to extend the Basic Personal Amount for lower income individuals. It has long been part of Ontario's personal income tax system. The historical record is difficult to fully discern but the earliest reference that can be easily found is the 1977 provincial budget.⁶ It has been adjusted or enriched several times over the years by governments led by the different political parties.⁷

The intent of the OTR is to reduce or eliminate provincial taxes for those with low to moderate income. A design feature that helps its effectiveness is that the OTR is factored into tax withholding. This means that an individual is not required to file a tax return⁸ to obtain the benefits of the OTR and the benefits

⁶ Ministry of Finance, Ontario Budget 1977. Available at: http://www.archives.gov.on.ca/en/historical_documents_project/77-81/ONTARIO_1977_BUDGET.pdf.

⁷ Jason Clemens, Amela Karabegović, and Niels Veldhuis, Ontario Prosperity Is Best of Second Best Good Enough?, Fraser Institute, April 2003. Available at: https://www.fraserinstitute.org/sites/default/files/OntarioProsperityExecSummary_0.pdf.

⁸ Generally, you are only required to file a tax return if you have to pay tax over and above what has already been withheld from your pay cheque.

are delivered regularly, through a higher regular paycheque.⁹ The Ontario government estimates that it presently costs about \$410 million per year in foregone revenues.¹⁰

The OTR, however, has several features that reduce its effectiveness. First, the OTR is household based and only the spouse with the higher net income can claim the OTR. This means that secondary earners in the household cannot benefit from this tax measure and thus reduces the economic autonomy for the lower income taxpayer. Second, it currently only reduces one's provincial income taxes up to an income threshold that is rather low. For single earners with no children the OTR currently only eliminates taxes owed by those with incomes between \$10,354 and about \$14,840 and is fully phased out at an income level of \$19,500. These are both well below the Low-Income Measure for Ontario, which is around \$21,000. In addition, a full-time worker earning the minimum wage would derive no benefit from the tax credit.

Ontario Tax Benefits

The Ontario government currently delivers a number of targeted tax benefits, including the Ontario Child Benefit and the Trillium Benefit, to support low-income families and their children.

The Ontario Child Benefit (OCB) is a refundable tax benefit that is delivered in conjunction with the Canada Child Benefit. It provides a maximum benefit of \$1,378 per child per year. Currently the maximum payment is received by those with incomes up to \$21,037 and then is phased out as incomes rise. As the OCB is indexed to inflation, increases in the minimum wage above inflation, as experienced this year, result in low-income families losing a significant portion of their Ontario child benefits. The outcome is the net benefit of a minimum wage hike is lower than advertised.

⁹ Ministry of Finance, Ontario Tax Reduction: Information Bulletin, April 2001. Available at: <http://www.ontla.on.ca/library/repository/mon/2000/10295403.pdf>.

¹⁰ Ministry of Finance, Transparency in Taxation, 2017. Available at: <https://www.fin.gov.on.ca/en/budget/fallstatement/2017/transparency.html>.

The Ontario Trillium Benefit (OTB) is a refundable tax benefit that combines payment of the Ontario energy and property tax credit, the Northern energy credit, and the Ontario sales tax credit. It was created in 2011 to simplify the range of benefits available to low-income households to provide relief for rent, property taxes, and electricity costs, depending on a tax filer's living situation. The annual OTB entitlement is usually divided by 12 and the payments are issued on the 10th of each month.¹¹

The various components of the Ontario Trillium Benefit are subjected to means-testing. The income thresholds and maximum benefits differ depending on one's circumstances including marriage status, age, and children.¹² But the key point is that a significant increase in the minimum wage without other policy adjustments will risk diminishing some of the benefits.

The need for reform

What does this mean for Ontario policymakers? This is not a criticism of increasing the minimum wage. Policy debates about the benefits and costs of raising the minimum wage are outside the scope of this transition briefing – especially since all major parties have essentially adopted it. But it does mean that the next government must consider the interaction between the minimum wage increase and existing transfers and benefits.

The goal of increasing the minimum wage is to raise the net income of low-income Ontarians. But this cannot be done in isolation. Sometimes individuals with lower incomes may experience situations where a small increase in income generates a steep reduction in one's transfers and benefits. There is a concern that some minimum-wage earners in Ontario may face that situation as their wage rate increases. In addition, increases to the minimum wage that are above inflation can itself contribute to inflation, thereby contributing to a

¹¹ Ministry of Finance, "The Ontario Trillium Benefit: More choice for people," Budget 2013, May 2, 2013. Available at:

<https://www.fin.gov.on.ca/en/budget/ontariobudgets/2013/bk4.pdf>.

¹² Government of Canada, 2018 Ontario energy and property tax credit (OEPTC) calculation sheets. Available at: <https://www.canada.ca/en/revenue-agency/services/child-family-benefits/provincial-territorial-programs/2018-ontario-energy-property-tax-credit-oeptc-calculation-sheets.html>.

loss of purchasing power that is acutely experienced by these minimum wage workers.

These concerns, however, can be addressed by thinking holistically about the tax and transfer system. There are several ways in which Ontario's policy framework could be modified to ensure that the tax system better supports both minimum wage and low-income workers.

How to move forward

As the minimum wage in Ontario is not currently indexed to inflation it means that wages will, again, decline in real value year to year, regardless of whether the minimum wage stays at \$14 or rises to \$15 in 2019. In addition, the design of the tax and transfer system means that low wage workers whose earnings fail to keep pace with inflation may see their tax benefits also fall, in cases where benefits increase as income rises. Indexing the minimum wage to inflation is needed policy to offset these effects and to provide a direct route for helping many low-wage workers.

Similarly, changes to tax credits are also needed to increase the effectiveness of minimum wage policies. If the OTR was changed into an individual-based tax credit, similar to a comparable credit in BC, adjusted automatically to increases in the minimum wage, and the threshold increased to accord with the LIM or the income of a full time, full year minimum wage earner, this would effectively eliminate taxes owed for many if not all minimum wage earners. In fact, doing so would be a simple and effective way for the Ontario Progressive Conservative Party to deliver on its election promise. In addition, this change would ensure that any fiscal gains from higher revenue and lower benefits from the minimum wage increase are essentially returned to these workers.

In addition, not all low-income Ontarians necessarily benefit from boosts to the minimum wage, either because they already earn more than the minimum wage, they are not covered by the minimum wage boosts (e.g., those in the gig economy), or they experience a reduction in hours that offsets the wage increase. They also face a rise in prices due to the inflationary effects of increases to the minimum wage.

Making the OTR refundable would help this cohort. It could be bundled with the Ontario Trillium Benefit or the new federal Canada Worker's Benefit to reduce administrative costs and ensure that beneficiaries receive regular payments which increases the effectiveness of the tax credit. Making the tax credit refundable brings the proposal closer to a Guaranteed Annual Income for the working poor, a commitment made by some of the parties in the Ontario election, though also increases the costs of the proposal.

While the personal income tax system provides a useful platform for delivering benefits to lower income individuals because it integrates the income testing of those benefits with the taxation system and is an administratively efficient mechanism, not all low-income individuals file tax returns as there is no requirement to do so if there is no tax owing. Further, many tax credits require the individual to claim them rather than being automatically considered for them. Filing itself and filing to optimize your tax position can be a significant barrier that prevents many people who qualify for and need benefits from actually receiving those benefits. Both the provincial and federal governments already provide some assistance to encourage tax filing among those who would benefit from refundable tax credits, but the enhancement of the refundable benefit program tied to minimum wage policies would justify a significant increase to that assistance.

Taken together these policy changes would go a long way towards achieving the broad-based goal of supporting the working poor.

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