TWO PROPOSALS TO EQUITIZE THE TAX AND TAXBACK IN RETIREMENT PLANNING OF LOW-INCOME CANADIANS

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Au Canada, une grande partie de la population générale tombe dans la catégorie dite des « personnes à faible revenu ». Leur modeste revenu avant la retraite suffit uniquement à rencontrer leurs besoins élémentaires immédiats. Pour ces gens, un régime d'épargnes-retraite est un luxe; le gros de leur revenu sert pour l'instant à payer le logement, la nourriture, les charges familiales et – chose étonnante – les impôts.

L'article développe la thèse que les économies réalisées en prévision de la retraite sont essentielles pour la sécurité de revenu plus tard dans la vie. Bien que le système fiscal actuel prévoie l'infrastructure des régimes de pension publics et privés au Canada, il serait bon que le gouvernement augmente la déduction personnelle de base des individus à faible revenu, sous réserve que les impôts autrement exigibles soient versés dans un régime d'épargnes-retraite. En outre, le gouvernement devrait établir un seuil de récupération en matière du supplément de revenu garanti, de façon à la rendre inapplicable lorsque le revenu annuel total du bénéficiaire tombe sous le seuil de la pauvreté.

In Canada, a large number of the general population falls within the descriptive category of "low-income." Their low level of pre-retirement income is enough only to satisfy basic current needs. For them, a retirement savings plan is a luxury; for now, the bulk of what they earn must go toward housing, food, support of the family and – surprisingly – tax.

This article argues that retirement savings is crucial for income security in later life. While the tax system currently provides the mainframe for the nation's public and private pension schemes, it is appropriate that the government raise the basic personal income tax exemption for low-income individuals, conditional upon the tax otherwise payable being contributed to a retirement savings plan. Additionally, the government should implement a threshold for "claw-backs' in the Guaranteed Income Supplement, so that no claw-back would apply where the recipient's total annual income falls below the poverty line.

†The author's purpose in writing this article is to draw attention to legislative options and changes in Canadian public pension policy that could be but are currently not being pursued. She thanks Ms. Agnes Kowalska for providing superlative guidance as editor to this likely controversial article, any surviving flaws of which lie with the author.

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I. INTRODUCTION

Should poor people pay taxes? Should low-income persons have retirement savings? Is it in the best interest of Canadian society and public policy to bring in an affirmative action plan in order to allow the poor to participate in government subsidies that are already provided to middle- and upper-income Canadians?

The above three questions frame the thesis underlying this article. The focus is on low-income Canadians as participants, or rather non-participants, in the public pension system. Surprisingly, a large number of the population falls within the descriptive category of "low-income". Between 1993 and 1996, approximately 12% of all Canadians lived in families that had low after-tax income.[1] In 1997, 10.83% (1.03 million) of Canadian households sampled had before-tax income of less than $20,000.[2] Given that the poverty line[3] in 1999 was drawn at $17,886,[4] the number of poor and

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[1] Statistics Canada, *To What Extent are Canadians Exposed to Low Income?* By M. Drolet & R. Morissette (Ottawa: Statistics Canada, 1999) at 5, referring to Statistics Canada, *Low Income after Tax, 1996* (Ottawa: Statistics Canada, 1998) at 33.

[2] Statistics Canada, *Income Distributions by Size in Canada, 1997* (Ottawa: Statistics Canada, 1999) at 1 and 126. A sample of 8,487,000 households with male heads disclosed that 7.87% of them had household income of less than $20,000. In stark contrast, of 1,063,000 households headed by females, 34.39% had household income of less than $20,000. The total sample size was 9.55 million.

[3] Poverty is a concept that even the government admits is very difficult to define. See Statistics Canada, *Crossing the Low Income Line* (Income and Labour Dynamics Working Paper Series) by N. Noreau *et al.* (Ottawa: Statistics Canada, 1997) at 7, where the authors explain that the definition of poverty depends on:

> "...an ideological context, or at least a set of value judgments about what constitutes an acceptable standard of living. In Canada, there is no agreed upon definition and no official poverty measure. However, Statistics Canada has since the 1960s produced estimates of the incidence of *low income* (*ibid.*)
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> The most widely known results are based on "low income cut-offs" (LICOs). Such measures refer to individuals or families with incomes below a certain pre-defined level. These cut-offs vary by family size and size of community. Separate cut-offs are calculated for unattached individuals (families of one) and for families of two to seven or more. Also, separate cut-offs are calculated for communities of different sizes, to reflect differences in the cost of living. Since after-tax income represents disposable income and since retirement planning is ideologically the responsibility of the individual rather than that of the family unit, this paper uses after-tax LICO for unattached individuals (families of one) when referring to the poverty line. While there has been some debate as to whether it is appropriate to use LICOs as indicators of poverty, Statistics Canada itself admits that:
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> "they reflect a consistent and well-defined methodology that identifies those who are substantially worse off than the average. In the absence of an accepted definition of poverty, these statistics have been used by many analysts who wanted to study the characteristics of the relatively worse off families in Canada:" Drolet & Morissette, *supra* note 1 at 3.

Accordingly, this article refers to the LICO when referring to the pov:rty line.

[4] Statistics Canada, *Low Income Cutoffs from 1990 to 1999 and Low Income Measures from 1989 to 1998* by B. Paquet (Ottawa: Statistics Canada, 2001) at 32. This figure is before tax and applies to an unattached individual - family of one - living in a community with a population exceeding 500,000 in 1999. The cut-off indicates that more than 63.6% of after-tax income is

marginally poor people in Canada is appallingly high. The table below shows the distribution of income – and of poverty – across age groups in Canada.[5]

Household Income Distribution by Age of Household Head, 1997							
	Age Group						
	24 and under	25-34	35-44	45-54	55-59	60-64	65 and over
Income groups ($ 000"s)	(percent)						
< 10	29.0	8.1	5.0	6.3	9.3	12.7	1.5
10.0-14.999	16.4	7.1	5.3	4.1	6.3	9.4	21.0
15.0-19.999	12.1	7.7	5.2	4.1	5.6	7.7	15.7
20.0-24.999	8.6	7.4	5.4	5.0	5.4	7.3	13.8
25.0-29.999	7.1	6.9	4.9	4.8	5.6	6.8	11.0
30.0-39.999	11.3	15.7	13.5	11.8	12.2	13.8	13.3
40.0-49.999	5.5	12.4	12.1	10.3	11.9	8.4	7.6
50.0-59.999	3.3	10.4	11.8	10.6	8.9	8.5	5.5
60.0-79.999	3.8	14.4	17.2	17.9	14.8	12.7	5.7
80.0-99.999	1.8	6.2	9.9	11.1	7.8	6.2	2.7
100.0 and over	1.2	4.0	9.5	14.1	12.3	6.6	2.1
Estimated numbers Male Female	427,000 343,000	1,871,000 536,000	2,447,000 540,000	1,944,000 440,000	681,000 157,000	560,000 159,000	2,907,000 1,924,000
Average income Male Female	$26,857 $18,918	$47,970 $26,378	$59,314 $31,724	$66,315 $35,188	$59,608 $23,011	$49,568 $20,758	$39,695 $20,758
Median income Male Female	$21,750 $13,154	$44,103 $22,984	$54,325 $27,488	$59,687 $31,086	$50,478 $24,106	$40,519 $18,247	$30,542 $16,302

According to Revenue Canada, in 1997[6] 10.91 million persons (over 51% of all individual taxfilers) had income of less than $20,000; within this group, 8.8 million (41.68% of all individual taxfilers) had income of less than $15,000.[7] 22.1% of all

spent on food, shelter and clothing. Statistics Canada has used various indicators of low income. For 1999, low income for a single-adult family unit ranged from $10,864 to $14, 771 after-tax. See *ibid.* at 33 and Statistics Canada, *Low Income Measures, Low Income after Tax Cut-Offs and Low Income after Tax Measure* (Ottawa: Statistics Canada, 1999).

[5] *Supra* note 2 at 126. Because of rounding, the percentage columns do not add exactly to 100. Statistics Canada derived the estimates from a survey of samples, which are subject to statistical error distributions and therefore the number columns do not add to the estimated totals. However, these features do not affect the general accuracy of the information that the table conveys.

[6] 1997 being the most recent year for which tax statistics on individuals are available at the time of this writing.

[7] Revenue Canada, *Income Statistics, 1999 Edition* (Ottawa: Revenue Canada, 1999) at Basic Table 2: All Returns by Total Income Class, online: Canada Customs and Revenue Agency<http://www.ccra-adrc.ca /tax/individuals/stats/gb97/pst/t2v-nil.htm> (date accessed: 29 October 2001). Taxable and non-taxable returns for the year indicating a loss or nil income: 895,800; $1 to $ 10,000: 4,781,240; $10,000 to $15,000: $3,128,400; $15,000 to $20,000:

households with a family head between ages 60 and 64 had annual income of less than $15,000. Where the family head was aged 65 or older, 22.5% had household income of less than $15,000. The majority of the latter two groups would have been retired, deriving most of their income from investments and pensions.

Studies indicate that while most Canadians do plan for their retirement through savings and home ownership, many do not partake in Registered Retirement Savings Plans (RRSPs) or Registered Pension Plans (RPPs).[8] While the reasons for this are varied, many people simply do not have a real choice. Their low level of pre-retirement income is only enough to satisfy basic current needs. For them, a retirement savings plan is a luxury to be had in the distant future; for now, the bulk of what they earn must go toward housing, food, support of the family and, surprisingly, tax.[9]

Canada's tax system provides the mainframe for the nation's public and private pension schemes. It distributes public moneys to eligible pensioners and manipulates private pension decisions by providing incentives and rewards. It serves these two functions under the rubric of "Canada's public pension system", which in reality weighs more heavily in favour of private retirement savings. In other words, the post-retirement welfare of Canadians rests largely on private, rather than public, funds.

Given that premise, the answer reached in this paper to the three questions initially posed is: low-income persons do need retirement savings. It is in their best interest as well as that of society at large – public policy – to support their participation in government subsidies directed at private retirement savings. To that end, low-income earners should be provided a special tax exemption in order to assist them in accumulating retirement savings. Such an exemption would divert what would otherwise be tax dollars paid into public coffers to locked-in savings and investment plans that will provide an income upon retirement.

The government's own figures plainly show that the lower one's income, the less likely they will make contributions to private savings plans like RRSPs and RPPs. In addition, the lower one's income, the lesser the contribution, if any is made at all. In 1997, less than 5.58% of all taxfilers who earned from $1 to $10,000 of income made a contribution to RRSPs/RPPs; the average amount contributed by persons in this income group was $853.08.[10] The proportion of contributors doubled in the $10,000 to $15,000 income group: 12.8% of all taxfilers in this group made contributions to an RRSP or RPP, their average contribution being $1,280.46.[11] Of all taxfilers in the

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2,107,210; total individuals in these income groups: 10,912,650; total number of individuals who filed tax returns for the year: 21,123,810.

[8] See C. Ragan, " A Case for Abolishing Tax-Deferred Saving Plans" in J. Richards & W.G. Watson eds., *When We're 65: Reforming Canada's Retirement Income System* (Toronto: C.D. Howe Institute, 1996) [hereinafter *When We're 65]*.

[9] In 1997, for example, 40.06% of all individuals who earned $20,000 or less paid income tax. That is 4,371,810 taxfilers out of a total of 10,912,650 in this income range. *Supra* note 7.

[10] *Ibid.* $227,644,000 in contributions divided by 266,850 taxfilers in this income group who made contributions to either an RRP, RRSP or both, given a total of 4,781,240 taxfilers in this income group.

[11] *Ibid.* at Table $10 - $15,000. $513,503,000 in contributions divided by 401,030 taxfilers in this income group who made contributions to either an RRP, RRSP or both, given a

$15,000 to $20,000 income group, 27.31% made contributions to an RRSP or RPP, averaging $1,556.46 per contribution.[12] Of all individuals in the $20,000 to $25,000 income group, a whopping 44.89% contributed, their average contribution being $1,762.38.[13] The message seems clear: Individuals in low income groups generally do not contribute to private pensions.

This article therefore proposes that the federal and provincial governments raise the basic personal income tax exemption of low-income individuals from the current $7,231 to, say, $17,886,[14] conditional upon the tax otherwise payable being saved for retirement.[15] The additional exemption equates to a tax saving of about $2,717, given an average combined federal and provincial tax rate of 25.5%.[16] (An exemption of $15,000 provides $1,981 in tax savings.) In making the exemption conditional on the taxpayer contributing the amount otherwise payable as tax into a retirement savings plan, the government can directly achieve the objective of targeting the tax expenditure[17] to providing RRSPs for low-income earners. The exemption would be an affirmative action measure, to allow low-income earners to participate in a program in which they can otherwise not afford to participate to a meaningful degree.[18] As an additional measure, the government should implement a threshold for "claw-backs" in the Guaranteed Income Support (GIS), such that no claw-back would apply where the recipient's total annual income falls below poverty-line income.[19]

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total of 3,128,400 taxfilers in this income group.

[12] *Ibid.* at Table $15 - $20,000. $895,772,000 in contributions divided by 575,520 taxfilers in this income group who made contributions to either an RRP, RRSP or both, given a total of 2,107,210 taxfilers in this income group.

[13] *Ibid.* at Table $20 - $30,000. $1,363,115 in contributions divided by 773,450 taxfilers in this income group who made contributions to either an RRP, RRSP or both, given a total of 1,723,130 taxfilers in this income group.

[14] In keeping with the intention that this exemption is to assist low-income earners to save for their retirement, its availability should be made available only to persons whose income falls below the poverty line.

[15] Insofar as the increased exemption is conditional upon the taxpayer contributing to a registered savings plan, the government can ensure that the tax revenues that it currently forgoes is not being diverted to another purpose.

[16] For a taxpayer who has total annual taxable income at or below $29,590, the federal tax rate is 17%. Assuming provincial tax to be 50% of federal tax, the combined federal and provincial tax would be approximately 25.5%. Actual provincial tax rates vary from province to province and from year to year. For 1998/1999, the provincial personal income tax rates as a percentage of basic federal tax was: Alberta 44.0%; British Columbia 50.5%; Manitoba 51.0%; New Brunswick 61.0%; Newfoundland 69.0%; Northwest Territories 45.0%; Nova Scotia 57.5%; Ontario 42.75%; Prince Edward Island 59.5%; Saskatchewan 49.0%; Yukon 50.0%. Quebec prescribes its own set of personal tax credits; its marginal tax rates range from 20 to 26 percent of taxable income, and do not piggyback the basic federal tax.

[17] A tax expenditure is any deviation from the benchmark tax system, usually in the form of tax exemptions, deductions, rate reductions, rebates, credits, deferrals and carry-overs. This is the definition used by: Department of Finance, *Tax Expenditures and Evaluations, 2000* (Ottawa: Department of Finance, 2000) at 9.

[18] Yet their participation would still be paid for with their own money. Similar to affirmative action measures in the employment sphere, the measure provides only opportunity; the beneficiary must still live up to the opportunity by working.

[19] For a discussion and explanation of the GIS claw-back, see *infra* note 28.

Can and should the government implement these two recommendations? Given what experts in this area have said, it could, in time.

II. THE CANADIAN PUBLIC PENSION SYSTEM

A wealth of expertise in this area can be found in many disciplines: public administration, economics, sociology. But the public pension system is managed according to, and is circumscribed by, legislation. The foremost authority in legal research and analysis of tax reform for pensions is Claire Young, a professor at the University of British Columbia and consultant to various levels of government. In many instances, her work has provided the fundamental building blocks for government policy.[20] In her study of public versus private pensions, Young has centered on identifying cusps of inequity that point to "systemic discrimination".[21] These cusps are everywhere in the tax system, wherever any one policy tends to favour those with money and other advantages vis-à-vis those without. This paper borrows from Young's various expositions, which invariably begin with an overview of Canada's tripartite public pension system, comprising of:

1 Old Age Security (OAS) and the Guaranteed Income Supplement (GIS),
2 the Canada Pension Plan (CPP) and the Quebec Pension Plan (QPP) for those with labour market earnings,[22] and
3 registered private retirement funds such as the RRSP and RPP, for which the government provides a tax subsidy.[23]

The first two schemes pay just enough benefits to allow recipients who have no other income a poverty-level standard of living. Under the OAS, Canadians who

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[20] C.F.L.Young's recent work includes: *Women, Tax and Social Programs: The Gendered Impact of Funding Social Programs Through the Tax System* (Ottawa: Status of Women Canada, 2000) [hereinafter *Women, Tax and Social Programs]*; *What's Sex Got to Do with It? Tax and the "Family"* (Ottawa: Law Commission of Canada, 2000); and "Spousal Status, Pension Benefits and Tax: *Rosenberg v. Canada (Attorney General)* " (1998) 6 Can. Lab. & Emp. L.J. 435.

[21] The Supreme Court has defined "systemic discrimination" as discrimination based on effect rather than on intention - i.e. unintentional discrimination. In *Egan* v. *Canada* [1995] 2 S.C.R. 513 at para. 38, 124 D.L.R. (4th) 609, para. 38 the court recognized that "[i]n many ways, this recognition flows from the fact that discrimination is as much an effect as a purpose, and that those individuals and groups that are more vulnerable in society are also more likely to experience the effects of distinction more severely".

In *Andrews* v. *Law Society of British Columbia* [1989] 1 S.C.R. 143 at 174, 56 D.L.R. (4th) 1 at para. 37, the Court did not offer a precise definition of systemic discrimination, but stated that "[i]f the barrier is affecting certain groups in a disproportionately negative way, it is a signal that the practices that lead to this adverse impact may be discriminatory."

[22] Quebec residents are entitled to receive benefits under the Quebec Pension Plan (QPP), which is the equivalent of the CPP.

[23] RRSPs are the alternative for those whose employers do not provide an RPP to employees.

have reached age 65 are entitled[24] to receive up to[25] $5,202.24 annually.[26] Between the ages of 60 and 64, prior to attaining entitlement to receive OAS benefits, seniors may receive the OAS Allowance or Survivor's Allowance.[27] While these benefits are not subject to income tax, the recipient must include such amounts in computing his or her taxable income for the year. As such, the net OAS benefit is subject to reduction by a tax component. In addition, it is subject to a claw-back, which means that the amount of the benefit may be reduced based on some criterion. Currently, the OAS claw-back is 15% for every dollar of income over $55,309 that the recipient had in the previous taxation year, inclusive of OAS benefits.[28] Ergo, a retiree who has $89,948 of income from other sources will receive zero OAS benefits,[29] as the OAS will have all been clawed back. I would say that this is fair, since a loss of $2,601 will not have much

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[24] *Old Age Security Act,* R.S. 1985, c. O-9. In addition to being over age 65, the recipient must also have lived in Canada for at least 10 years.

[25] See Human Resources Development Canada, "Old Age Security Payment Rates" (Ottawa: Human Resources Development Canada, 2001), online: Human Resources Development Canada <http://www.hrdc-drhc.gc.ca/isp/common/oastoc_e.shtml> (last modified: 17 December 2001) for a description of the OAS Program. As of April 2001, the OAS pays a maximum monthly benefit of $433.52, but the actual amount receivable is entirely dependant on how long the recipient has resided in Canada. The Canadian government explains the manner in which OAS benefits are calculated as follows: The OAS is like a large pie divided into 40 equal portions. A senior who qualifies for all 40 portions will receive the maximum amount. A senior who does not qualify for all 40 portions will receive only some part of the maximum amount. The number of portions that the senior qualifies for depends on how long he or she has lived in Canada. For each complete year of residence in Canada after age 18, the senior earns 1 of the 40 portions available. Someone who has lived in Canada for only 10 years would qualify for one-quarter of the maximum amount ($108.38 a month, as of April 2001), whereas someone who has lived in Canada for 40 years would receive the maximum OAS benefit available (subject to claw-back).

[26] *Ibid.* $433.52 maximum monthly benefit x 12 months, as of April 2001.

[27] See "Allowance" and "Allowance for the Survivor", *ibid.* The Allowance or Survivor's Allowance, as the case may be, is a payment of benefits that recognizes the difficult circumstances faced by surviving persons and by couples living on the pension of only one spouse or common-law partner. It is paid to the spouse or common-law partner of an OAS pensioner or survivor of such a pensioner who has died. To qualify, the recipient must be between the ages of 60 and 64, and must have lived in Canada for at least 10 years after turning 18 years of age; the combined annual income (not including OAS and GIS benefits received) of the couple or that of the survivor, must not exceed $23,088 and $16,944 respectively. Upon the recipient turning age 65 (at which point he or she becomes eligible for the OAS), his or her eligibility to receive either the Allowance or Survivor's Allowance ceases. Both the Allowance and Survivor's Allowance are subject to claw-back at rates that apply to the GIS, as explained in the text above.

[28] Pursuant to paragraph 180.2(2)(b) of the *Income Tax Act,* indexed by subsection 117.1 of that *Act* to take into account annual Consumer Price Index adjustments. In contrast with the GIS, OAS claw-backs depend on the income of the individual recipient, as opposed to income of the family of the recipient. The state's criterion for assessing economic need is therefore not uniform, which may be an indicator of other internal inconsistencies in the overall welfare policy and retirement philosophy that it follows. The definition of "monthly base income" in subsection 12(6) of the *Old Age Security Act* provides that the amount of GIS receivable depends on the aggregate incomes of the applicant and his or her spouse or common-law partner, rather than on the applicant's income alone.

[29] *Supra* note 25, at April-June 2001. The slight discrepancy between this figure and the formula is evident.

impact on most persons earning $89,948 annually,[30] and limited government resources are better spent if given to persons with much less income.

The GIS supplements the OAS, and its purpose is to guarantee a minimally acceptable standard of living for retirees who have little or no income other than public pension benefits. The primary goal of the GIS, as an instrument of social policy, is to redistribute income according to need. A single person can receive up to $6,182 annually,[31] while a married couple can receive up to $8,054.[32] GIS benefits are not subject to tax but are subject to a high claw-back rate of 50 cents for every dollar[33] of other income[34] that the senior has.[35] The mechanism responsible for clawing back the GIS is the tax system, which assesses the extent of entitlement on the basis of the proposed recipient's *family* income.[36] The assumption is that members of a family pool their income and share wealth.[37] Presumably family members are also expected to have

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[30] A taxpayer who earns $89,948 will pay tax at the highest tax rate. Assuming federal and provincial taxes combined produce the highest tax rate of 50%, a $5,202 OAS receipt will be reduced to $2,601 after tax.

[31] $515.21 x 12 months, as of April 2001.

[32] ($335.59 x 2 persons) x 12 months, as of April 2001.

[33] The claw-back rate is different depending on the marital status of the recipient. For a recipient who is single, widowed, divorced or separated, the maximum monthly benefit is reduced by $1 for every $2 of other income. However, where the recipient and his or her spouse or common-law partner both receive OAS benefits, the claw-back rate is 25 percent – a GIS reduction of $1 for every $4 of the couple's combined other income. For the couple, the first GIS reduction is made starting when their combined yearly income reaches 12 times the basic monthly OAS pension plus $48.

[34] "Other income" does not include OAS, Allowance or Survivor's Allowance, or GIS benefits received. It includes CPP/QPP benefits; private pension income and superannuation; withdrawals from RRSPs, RPPs and RRIFs; interest; capital gains; dividends; rental income; and any employment income. Previous year total income is generally used to determine the level of benefits in a current payment year.

[35] *Supra* note 25, at April-June 2001. The annual income for GIS cut-off is $12,384 for a single individual and $16,128 for an individual married to a pensioner, as of April 2001.

[36] If the senior is single, widowed, divorced or separated, the family unit is made up of one individual. If he or she is living in a recognized spousal relationship, the family comprises the couple.

[37] *Supra* note 25, at April-June 2001. Single persons can receive GIS benefits of up to $6,182 annually ($515.21/month x 12); while married couples can receive only $8,054. (Where both members of a couple are eligible to receive the GIS, each receives the lesser amount of $335.59; $335.59 x 2 x 12). This means that, if two GIS recipients live together but are not legally treated as spouses, they can receive $12,364 – significantly more than the maximum receivable by married couples. Conditioning the amount of entitlement on spousal relationship or absence thereof has questionable practical utility. The point has been discussed in the context of entitlement to tax subsidies by Claire Young in *What's Sex Got to Do With It? Tax and the "Family"*, (Ottawa: Law Commission of Canada, 2000) at 3. If pooling of income and economy of scale in cohabitation constitute the rationale for reduced *pro rata* benefits to couples, married status has very little to do with the equation. In fact, to link benefit entitlement to marital status accomplishes at least one of two things, if not both:

1 it encourages persons living in a conjugal relationship to cheat the system by disavowing official conjugal status for tax and related legal purposes; and

2 it gives rise to both real and perceived inequity, in that persons with official married

a sense of responsibility to support each other.

It has been suggested to me by an anonymous reviewer of this article prior to its publication that amending[38] the GIS is a much more sensible way to alleviate poverty amongst seniors than my two proposed measures. The shortcomings in merely amending the GIS, in my view, are at least two-fold:

1. Even if the amount of GIS is increased significantly, this program may be discontinued entirely by the time a taxpayer retires. Government-run public pension plans are not legally enforceable contracts, merely political undertakings. The state of Canada's public finances and social programs 20 or 30 years hence is not guaranteed. What, then, for persons who do not have a private pension?
2. The nature of the GIS, as evident in the claw-back mechanism, is that it is meant to be given only to the poor – retirees who have little or no income other than from the public purse. The point of encouraging RRSPs, which attract an increasingly greater amount of government subsidy as value in the plans accrues is so that annuitants will not have to rely on government distributions after retirement; these annuitants are less likely to be in the ranks of the poor. Even assuming that the amounts eventually receivable from an annuitant's RRSP are only as much as the maximum GIS otherwise available - currently $515 a month - such that it would be more strategically advantageous to the annuitant to obtain that money from the public purse, public policy mantra encourages employment during a person's employable years. There is nothing to be gained by the public from having people on welfare. In keeping with that mantra, the tax exemption proposal encourages workforce participation.

Some provinces already augment the federal GIS with their own supplements. Under Ontario's Guaranteed Annual Income System (GAINS), a senior who has less than $1,031 of income a month is eligible to receive a supplementary provision of up to $83 per month.[39] The objective is to ensure a certain standard of living for seniors. Clearly the government can only set the standard so high. Seniors must provide their own standard.

While there is also the CPP/QPP, which is payable irrespective of factors such as need, wealth and family, eligibility to receive it depends on the recipient having worked in "pensionable employment"[40] and having made contributions to the CPP/QPP during his or her years in the labour force. A senior who has attained age 60 may

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status receive less benefits compared to persons in a relationship who are in fact equivalent to married but do not admit to it.

[38] I suppose he or she meant increasing the amount of GIS.

[39] For instance, a senior who receives $1,025 of other income (including the OAS and GIS) can expect to receive a GAINS benefit of $6. GAINS pays no benefits at all where a single senior's monthly income exceeds $1,031.73. For married couples, the income cut-off is $1,704.22. See Ontario Ministry of Finance, *Information Bulletin #6490 GAINS-1* (Oshawa: Queen's Printer for Ontario, 1999).

[40] "Pensionable employment" is a defined term under s. 2(1) of the *Canada Pension Plan Act*, R.S.C. 1985 c. C-8 [hereinafter *CPPA*].

receive up to $9,300 of CPP/QPP annually.[41] Individuals with low income before retirement will have made a relatively low level of contribution to the CPP/QPP. Payouts to them from these plans will therefore be small.

Even assuming that a retiree receives the maximum amount possible under all of these public plans, without an additional private source of income he or she will still have less than $17,886 in after-tax annual disposable income.[42] According to Barnsley and Young, the OAS and CPP combined provide no more than an income of 39% of the annual industrial wage.[43] While the public purse provides working Canadians with two pension plans when they retire, the benefits available thereunder to low- and modest-income retirees are by themselves inadequate even to cover modest needs. Persons who have not participated in "pensionable employment[44] and therefore have no entitlement to the CPP/QPP, can count on the federal government for only $11,384 a year.[45] Without an additional private source of income, the plight of such retirees is truly forlorn.

Unfortunately, Canadians will have no additional guaranteed source of income after retirement unless they have personally made provision for it. If such provision is made by means of RRSPs and RPPs, they can also seize upon certain public subsidies which have been dedicated by the Canadian government to the third module of its tripartite public pension system. This third module is both public and private in nature. Government provides benefits out of the community chest but in order to access those

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[41] $775 maximum monthly amount, as of April 2001. *Forecasting, Information and Results Measurement*, online: Human Resources Development Canada <http://www.hrdc-drhc.gc.ca/isp/studies/trends/infocard/infocard2q01_e.pdf> (last modified: 28 September 2001). This amount is not subject to any sort of claw-back but is subject to income tax.

[42] Since the GIS and provincial income supplements are clawed back at 50 cents for every dollar of income including CPP/QPP benefits, these supplements would largely be offset by CPP/QPP receipts. The government's stated policy is to allow applications for a waiver of the claw-back, in the event that it causes financial hardship. Upon an application for relief being made, the Canadian Customs and Revenue Agency determines whether or not the terms of the claw-back should be modified for the applicant, on a case-by-case basis. Supposedly then, the claw-back is not set in stone.

[43] P. Barnsley & C.F.L. Young, *Understanding (In)equality for Women in Canada's Retirement Income System: Case Study of the Delivery of a Social Program by the Tax System* (Vancouver: West Coast LEAF, 1999) at 4.

[44] Pensionable employment does not include work as a homemaker or childcare provider of one's own children where no remuneration is paid. It also specifically excludes, by reason of the term "excepted employment" as defined under s. 6(2) of the *CPPA* (*supra* note 40), the following remunerated work performed pursuant to an arm's length employer-employee relationship: (a) employment in agriculture or an agricultural enterprise, horticulture, fishing, hunting, trapping, forestry, logging or lumbering by an employer who employs the employee, on terms providing for payment of cash remuneration, for a period of less then twenty-five working days in a year; (b) employment of a person by the person's spouse or common-law partner, unless the remuneration paid to the person may be deducted under the *Income Tax Act* in computing the income of the spouse or common-law partner; (c) employment of an Indian, as defined in the *Indian Act*, in respect of which the earnings are not included in computing income for purposes of the *Income Tax Act*. See *Indian Act*, R.S.C. 1985, c. I-5, s. 2(1).

[45] 12 months x ($433.52 OAS maximum monthly rate + $515.21 GIS maximum monthly rate), these benefit payment rates being for a single person in April 2001.

benefits, the recipient must have his or her own capital stock. The greater an individual's personal capital, the more benefits the government provides to help supplement it.

III. THE RICHLY SUBSIDIZED PUBLIC-PRIVATE THIRD MODULE

Under the third module, it is the taxpayer who determines how much of a public subsidy he or she will receive. The government's role is to provide some simplistic start-up rules[46] and then to reward those who stock their capital for retirement by giving them tax preferences. When a taxpayer makes a contribution to private pensions plans such as the RRSP or RPP, he or she is given a dollar-for-dollar deduction in computing taxable income.[47] RRSPs/RPPs are therefore government-approved, government-sponsored, and publicly-subsidized tax shelters. Tax is payable only upon withdrawals being made from the plans. In the meantime, funds maintained within the plans are invested and earn income, which is also completely exempt from tax until withdrawn.[48] Economist and McGill University professor Christopher Ragan has estimated that in 1994, there was $220 billion sitting in RRSPs.[49] Because the capital and income in these plans generate and accrue income tax-free, the aggregate amount that is tax-sheltered will steadily balloon over time.

The tax revenue that is indefinitely foregone as a result of these tax shelters is a cost borne not only by the government but by all Canadians. Every year, the government effectively makes available very substantial amounts to individuals to secure their own nest-eggs, whereby they are accorded the privilege of exercising their personal investment initiatives using the equivalent of a government-sponsored, indefinite-term, interest-free loan.[50] For the 1997 taxation year, Finance Canada estimated that it made $15.34 billion in net tax expenditures toward RRSPs and RPPs.[51] For the years 2001

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[46] A taxpayer is subject to monetary limits as to how much he or she can contribute annually to a registered retirement plan. But the sky is the limit as to the amount of tax deferral on the tax-sheltered income earned in the plan. If the taxpayer's investment fortunes are good, the income generated and held in the plan is, up to the time of its withdrawal, completely tax-exempt.

[47] For the year 2000, the maximum deduction is the greater of $13,500 and 18 percent of the previous year's income, this ceiling being subject to reduction for any contributions made for the benefit of the taxpayer to an employer-sponsored occupational pension plan. If the taxpayer has not used all of his or her deduction limit for the years 1991 to 1999, the unused amount may be carried forward.

[48] The tax deferral accorded to RRSP contributions is intended to allow taxpayers to spread their disposable income and corresponding tax liability over their lifetimes, by deferring a portion from their working years to their retirement years.

[49] *Supra* note 8 at 8.

[50] The analogy of an interest free loan is, I believe, the brainchild of Claire Young. She also reveals that, when tax is eventually paid, inflation will have caused the payment to be made in deflated dollars – an additional benefit that large contributors to registered retirement plans enjoy to a much greater extent then taxpayers whose contributions are limited by their lesser disposable income. See Barnsley and Young, *supra* note 43 at 14.

[51] Net of the tax levied on withdrawals from RRSPs/RPPs, the tax expenditure was $7.15 billion for RRSPs and $8.19 billion for RPPs. While some analysts create the impression that RRSPs garner the greater share of the subsidy, it appears that in fact RPPs represent the larger

and 2002, the Canadian government projects that it will give $15.285 billion and $15.54 billion respectively in net tax subsidies to RRSPs and RPPs.[52]

The operative rationale underlying RRSPs/RPPs rubs against the grain of need. Whereas the poorer the recipient, the more OAS and GIS benefits he or she receives; in the case of RRSPs/RPPs, the wealthier the retiree and the greater his or her capital stock, the more he or she can expect to receive out of the community chest. The values manifested by the overall system are therefore inconsistent and self-contradictory. With OAS claw-backs, need is determined by individual income. But in respect of a related program, the GIS, family income determines need. Moving farther afield into the area where the greatest expenditure is being made from public coffers, the criterion is not need at all, but wealth. Canada's tripartite public pension system certainly is an animal that caters to everyone. But poor people benefit the least and those with capital stock receive the most. The higher a taxpayer's income, the larger the government subsidy by way of tax exemption.

Again extracting from Barnsley and Young's work: a $3,000 contribution results in a tax reduction of $765 for a low-income taxpayer who pays tax at the lowest combined marginal rate of 25.5%. The same $3,000 contribution results in a tax savings of $1,500 for a taxpayer in the 50% high-income tax bracket. The inequity is obvious: the government provides larger public subsidies - by way of tax benefits - to higher-income earners.

Owing to differential tax rates between income brackets, a high-income taxpayer receives more than double the tax savings than a low-income taxpayer on the same dollar of passive income earned in an RRSP/RPP. Additionally, the higher frequency with which high-income earners access these subsidies exacerbates the inequity. The paradox is that, while it is the less wealthy who need government assistance to achieve income security in old age, it is the more wealthy who receive a greater measure of assistance to build that security.

Some economists have recommended that the government abolish RRSPs and other tax-deferred private savings vehicles.[53] In Ragan's view, tax-deferred savings plans (TDSPs) not only fail to increase the overall amount of national saving but instead effect a redistribution of wealth from lower-income to upper-income Canadians:

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capital stock and therefore lay claim to the larger share of tax subsidies by way of deferred tax revenues each year, notwithstanding that more contributions are made per year to RRSPs than to RPPs. In 1997 for example, the non-taxation of investment income generated by RPPs was $8.63 billion, compared to $3.19 billion in respect of RRSPs. *Supra* note 17 at 19. The net tax expenditure is larger on the RRSP side, only because each year a much larger amount is withdrawn from RPPs than RRSPs.

[52] *Ibid.* Finance Canada has projected for 2001 (in billions): deductions for RRSP contributions $7.675, non-taxation of RRSP investment income $4.68, taxation of RRSP withdrawals $3.21 (negative expenditure); deduction for RPP contributions $5.09, non-taxation of RPP investment income $ 9.605, taxation of RPP withdrawals $8.555 (negative expenditure). The projections for 2002 are: deduction for RRSP contributions $8.29, non-taxation of RRSP investment income $5.2, taxation of RRSP withdrawals $3.515 (negative expenditure); deduction for RPP contributions $5.16, non-taxation of RPP investment income $ 9.865, taxation of RPP withdrawals $9.46 (negative expenditure).

[53] *Supra* note 8 at 15.

> *Somebody* pays for TDSPs. The tax revenue that is foregone has to be made up with other taxes, with reduced spending, higher borrowing, or the printing of money, which causes inflation. While it is theoretically possible that the only people who suffer from these changes are TDSP contributors, that would be something of a fluke. It is much more likely that nonbeneficiaries also pay, which means that the income redistribution that occurs is very probably perverse. Contributors to RRSPs generally have higher incomes than noncontributors. In 1991, for instance, only 24 percent of contributors had incomes less than $20,000 a year, while 12 percent had incomes higher than $60,000. Moreover, since they are in higher tax brackets, high-income contributors gain more from their contributions than low-income contributors. They also tend to contribute more than low-income contributors. As a result of both effects, contributors in 1991 who made more than $30,000 a year received a tax reduction averaging $879, while those making less than $30,000 a year received only $307.[54]

Does this paradox make the system preposterous vis-à-vis its objective of assisting the poor? Not at all, because the government's objective underlying the third module of the public pension system is *not at all* to assist the poor. Rather, it is to shift the burden of poverty in retirement off the shoulders of government. The prevailing view is that preventing poverty is a personal responsibility. Whether or not that is relevant or even a correct statement of the government's actual position, Parliament continues to enhance -- enlarge -- the public subsidies given to private pensions, while progressively shrinking direct social programs that deliver actual money payouts to retirees. While I cannot earnestly argue that the state should have responsibility for providing a comfortable retirement for everyone (there will be some who have chosen not to assume responsibility for themselves), I believe there is no reason why the wealthy should receive any public subsidy whatsoever out of already constrained public finances. Since the government has chosen to gift public money to those who demonstrate no need for it, surely that same government has a definite responsibility to give a proportionately fair share to those in need. That fair share should be given now and not only upon retirement. High-income earners who have not yet retired receive subsidies by way tax exemptions now. I therefore argue that low income earners should receive the same – now, not when they retire at which time the government may have abandoned the GIS altogether.

Government subsidies, whether or not by way of tax benefits, find their best cause in being directed to those who need subsidies. A system that delivers subsidies should at the very least operate to include low-income earners on a large scale, and allow them to have regular (as opposed to haphazard) access to these same subsidies that high-income earners easily enjoy. The wealthy have capital assets which continue to generate significant amounts of passive income even after their owners have retired from the workforce. But low-income earners who have not amassed capital property over their working lives must look back on their pre-retirement income to sustain their livelihood after retirement. To the working person, then, pre-retirement savings are all the more important.

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[54] *Ibid.* at 10.

IV. PREMISE OF THE RECOMMENDATIONS

Tax deductions and exemptions comprising preferential tax treatment are an expenditure -- money out of the public purse because the government could have collected it, made it available for use by the general public, but has chosen not to do so. The opportunity cost is borne by everyone who does not receive something from the expenditure.

Since most of this expenditure is made to those who can afford to save for their retirement, arguably most of the cost is borne by those who cannot. The stakes are very high for those bearing the cost. The projected cost of tax expenditures for RPPs and RRSPs for the 2000/2001 fiscal year is 38.6% of the total value of all public expenditures for pensions.[55] Those who do not make use of RRSPs/RPPs miss out on at least one-third of government-provided retirement benefits.

A. *Everyone Needs a Private Pension*

Taxpayers who do not avail themselves of RRSPs/RPPs pay tax they can otherwise avoid. They collectively bear the opportunity cost of a community chest that subsidizes other taxpayers' nest-eggs without getting any benefit for themselves. Low-income earners who cannot presently contribute to a private pension, and therefore cannot avail themselves of the subsidy, lose out in two ways, one real and the other symbolic:

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[55] For the month of December 2000, the government paid 2,712,990 retirees $1.1346 billion in CPP benefits, and 937,675 retirees $330.8 million in QPP benefits. For the same month it paid 3,818,168 individuals $1.5771 billion in OAS benefits, plus an additional $421.2 million in GIS benefits to 1,365,102 individuals in need. In addition, the government paid out $32.1 million in Allowance and Survivor's Allowances to 94,146 recipients. For the year 2000/2001, the government estimates that its CPP expenditures will total $19.352 billion; QPP $6.093 billion; OAS $18.784 billion; GIS $5.092 billion; Allowance and Survivor's Allowance $403 million. (Source: Forecasting, Information and Results Measurement, Income Security Programs, Human Resources Development Canada.) Net tax expenditures in 2001 are projected to be $6.14 billion for RPPs and $9.145 billion for RRSPs. *Supra* note 17 at 19. However, CPP and QPP represent returns to the recipient of amounts contributed by the recipient and his or her employer before retirement. Hence, only the OAS, GIS, Allowance and Survivor's Allowance are true government expenditures, totaling therefore $24.279 billion for the year in question. In publishing its figures, the government should not refer to the CPP and QPP amounts that it has paid out as "public expenditures" sine both are funded by contributions from employers and employees. See *General Information About the Canada Pension Plan*, at para. 26, online: Human Resources Development Canada <http://www.hrdc-drhc.gc.ca/isp/cpp/genera_e.shtml#2> (last modified: 30 August 2001) where the federal government explains:

> The Canada Pension Plan is a "contributory" plan. This means that all costs are covered by the financial contributions paid into the Plan by employees, their employers and self-employed people, and from interest earned on the investment of that money. The Canada Pension Plan is not funded through general tax revenues.

Some analysts have in their work referred to the value of all public expenditures as including CPP and QPP. But to refer to these returns of mandatory contributions as a public expenditure by the government is to greatly exaggerate the government's largesse.

1 They will have limited and inadequate sources of income upon retirement.
2 They lose out on a public subsidy to which entitlement is supposed to be universal.

While critics have called for shrinkage of the third module in favour of larger OAS/GIS benefits and lower claw-backs, the government cannot expand the cash payouts from the system, as there is only so much money to go around. Tax expenditures are different in that they are not subject to the same public scrutiny and fewer bureaucratic obstacles are involved in the process of distribution. As economists explain it,[56] government-run pension schemes that distribute money involve a sharing of current national income; benefits currently paid to seniors out of the OAS and CPP/QPP are funded by taxpayers who have not yet retired. In order to expand these programs, the government must have people who are currently working pay more into government coffers -- an unpopular and politically suicidal notion.[57] Alternatively, the government must shrink other public programs -- another unwelcome but oft-seen phenomenon.

Instead, the government's preferred solution is to provide (invisible) tax subsidies to encourage private retirement saving.[58] But Barnsley and Young warn that such privatization of economic responsibility for retirement by way of tax expenditures veils government support of high-income individuals[59]. Increasing the role of tax incentives in responding to the social need of providing economic security for retirement only exacerbates the situation of the poor. Tax expenditures cannot be the solution even when there is a shortage of hard cash for distribution. But is there any real shortage of

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[56] See e.g. D.W. Slater & W.B.P. Robson, "Building a Stronger Pillar: The Changing Shape of the Canada Pension Plan" *C.D. Howe Institute Commentary* (Toronto: C.D. Howe Institute, March 1999) 123.

[57] Barnsley and Young, *supra* note 43, have asked: As long as there is economic disparity dictating that significant parts of society do not have access to the same opportunity to take advantage of the tax preferences for contributions to private pensions, then an argument can be made that those preferences should be removed from the tax system. Should we reduce, rather then eliminate, the tax preference for investment in pension plans? (*Ibid.* at 21.) I think that reduction or elimination of tax preferences for investment in pension plans will not be politically feasible because the State has already provided such preferences and people have become accustomed to having them. A less controversial, yet equally Budget-challenging, question is whether existing tax preferences can be made more accessible to persons who do not now enjoy them due to their lack of economic resources. If the government can take a step in that direction, to open up accessibility to such benefits by granting a special tax preference by way of a proposed low-income threshold tax exemption, this may relieve economic disparity and even enhance political cohesion. My view is that even the most stalwart supporter of retirement tax preferences will not object to making these preferences more accessible to the economically disadvantaged.

[58] Paula Barnsley observed in *Understanding Economic Inequality for Women in Canada's Retirement Income System: Reform, Restructuring and Beyond*, (LL.M Thesis, University of British Columbia ,1998) [unpublished] at 149, that "[t]he clear message is that individual initiative in planning for retirement will be rewarded by the government while collective (state) responsibility for economic well being in old age, reflected in the 'public' parts of the retirement income system, cannot be permitted to grow and must be contained."

[59] *Supra* note 43 at 18.

hard cash?

If the government did not choose to forego tax revenues but collected the tax otherwise payable on all RRSP/RPP contributions and in-plan earnings, it theoretically would have a tremendous surplus of funds to enhance its direct support of low-income seniors.[60] *If* the government targeted all such revenues to supporting the lowest-income groups, seniors living below the poverty line could be well looked after indeed. But then, higher-income Canadians would complain: how is it fair that we who work hard and save are not rewarded; those who have done nothing to deserve any more should get more -- at *our* expense?

There is, then, no real argument as to the scarcity of resources. The implementation of the third module of Canada's public pension system really comes down to choice. The real debate waged in respect of Canada's public pension system is between those who believe that the government should expand and enrich the OAS/GIS in favour of the needy and those who support larger tax incentives for private retirement savings in favour of those not in need. Advocates of enhanced distribution programs clearly believe that the government should assume responsibility for people's welfare, while those who support more tax preferences for private savings are willing to assume greater responsibility for their own. These two positions are not at all mutually exclusive -- unless, of course, those who are not in need want all the government subsidies for themselves.

I suggest that Canadians should be entitled to expect a measure of government support for private retirement initiatives as well as subsidized access to such support initiatives. With RRSPs/RPPs, the government subsidizes retirement savings. With a conditional increased basic personal exemption for low-income taxpayers, the government would subsidize *access* to subsidized private savings. It would be like opening a door -- wider. Subsidies should be given all around, and not only to persons who already have access.

Public policy in Canada's tripartite system is currently lopsided. Policymakers perhaps strive to do good, to encourage saving for retirement, but the third module is not – and has never been – properly aligned with its two siblings in providing for persons in need. It contributes to the accumulation of wealth by the wealthy, applying public moneys to benefit those without need to a far greater extent than those in need. But this is not to say that government should abolish RRSPs/RPPs, only that affirmative action measures are necessary to redress the imbalance.

B. *Raising Personal Exemption - Nothing New?*

Proposals to increase the personal exemption have been raised and considered before. However, those were premised on universal entitlement to a larger exemption, and not a targeted exemption made expressly applicable only to low-income taxpayers. Nor were they made conditional on the tax otherwise payable being directed to some defined purpose.

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[60] This is only theoretical because with money in hand, the government might very well spend it on a thousand other things, without necessarily allocating any more to supporting low-income retirees.

Economist Finn Poschmann considered raising the basic personal exemption as an option for lowering the effective tax burden borne by low- and middle-income Canadians, in his 1998 paper "How Do I Tax Thee? Choices Made on Federal Income Taxes".[61] But his analysis assumed that the exemption would be raised to (a paltry) $7,018 *for everyone*:

> As a one-time measure, increasing the basic exemption would not fare too badly. But it would mean that preserving the value of the tax change would require yearly discretionary action on the part of the prime minister and his cabinet. Inflation, even at 2.5 percent, would eliminate the real increase in the basic exemption in just over three years.
>
> As an economic incentive, however, increasing the basic exemption would not fair well at all. It would certainly be useful in removing very low-income taxpayers from the tax rolls, but the incentive would apply only to those whose taxable income remained below the value of the increased exemption. Everyone stepping above that low value would face a minimum federal plus provincial income tax rate of 25 percent. But just increasing the basic exemption for all would be a simple and clear improvement over the measures Finance Minister Martin has proposed, for the approach would worsen no one's incentives.[62]

Poschmann's concern about the real value of any tax savings and the limited effectiveness of a tax cut as an economic incentive does not impair a measure that raises the basic personal income tax exemption only for persons whose income falls below the poverty line. The incentive of the taxpayer is not a relevant question; the only real question is the incentive of the government to provide this measure. Given the choice between paying an amount as tax to the government - and theoretically never seeing that money again - and putting that same amount into a personal savings plan *instead of paying it to the government*, low-income earners would settle for the latter.[63] The question for the government is this: Since it currently gives an annual income tax deferral to $220 billion sitting in RRSPs and RPPs, is it willing to give an additional $4.8 billion deferral,[64] in order to extend full participation in Canada's public pension system to about 2 million low-income Canadians? If not, why not?

As Poschmann observed, increasing the basic exemption "would certainly be useful in removing very low-income taxpayers from the tax rolls".[65] The key would be

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[61] *Backgrounder* (25 February 1998), online: C.D. Howe Institute Homepage <http://www.cdhowe.org/pdf/Posch.pdf> (date accessed: October 24, 2001).

[62] *Ibid.*

[63] Many would call this a "no-brainer." The tax savings do not come without administrative cost to the taxpayer, who must take steps to set up an RRSP, make periodic contributions and investment decisions. Some "happy-go-lucky" people will not be inclined to do this. The tax exemption therefore will not capture every eligible taxpayer. Of course, there is an educational component required to inform taxpayers of any new measure, which some will resist.

[64] Assuming 2 million Canadians currently have taxable income falling below the poverty line, and that the tax otherwise payable by these persons is about $2,400 per person, a total exemption from such tax works out to $4.8 billion.

[65] *Supra* note 61 at 5.

to raise the exemption not by a paltry $1,000, but by an amount that would keep people who earn a poverty-line[66] subsistence off the tax rolls completely.

Although in absolute dollar terms the proposed exemption may appear generous, the amount of tax savings conferred per exempted taxpayer is not generous at all. Just as the government provides tax savings to high-income earners who have RRSPs, the government should provide a tax benefit to low-income earners to allow them to have resort to RRSPs. The cost to the government is, once again, foregone tax revenue. But in this case, what is foregone is in the name of affirmative action, expressly targeted to persons whose total income[67] falls below an amount considered to delineate the poverty line.

V. LET THE TAXPAYER MAKE THE CHOICE

As reasoned above, given the choice between paying an amount as tax to the government (and theoretically never seeing that money again)[68] and putting that same amount into a personal savings plan instead, low-income earners would choose to claim the exemption and make the tax-subsidized contribution to a RRSP. Is this the equivalent of the government telling the taxpayer what to do? Would the government be treading beyond its role in virtually prescribing a RRSP for low-income taxpayers?

The answer depends entirely on whether one views the tax-subsidized RRSP vehicle as something desirable for low-income earners. For if it is desirable, the government does no wrong in promoting it with tax expenditures.

One person who has advocated *against* RRSPs for low-income earners is notable economist Richard Shillington, who has advised that low-income Canadians would be better off investing for their retirement in ways other than through a private pension plan such as a RRSP. According to him, "any money that they save for retirement simply reduces their eligibility as seniors for income, health care, and social support."[69]

According to Shillington, low-income Canadians who invest in RRSPs will

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[66] There will inevitably be complaints of unfairness in borderline cases. The income tax system in Canada depends largely on self-assessment. There will be taxpayers not entitled to claim the exemption who will understate their income in order to claim it. There will also be taxpayers who fall a few dollars over the poverty line and who will complain of having to pay tax. But a line must be drawn somewhere.

[67] Total income, rather than taxable income, should be used as the gauge for these purposes. A person may have substantial non-taxable income but negligible taxable income. For instance, certain insurance and similar annuities are not subject to tax but nonetheless constitute income in the hands of the recipient. Since the exemption is meant to be provided to persons on the basis of need, it is mandatory not to permit those taxpayers who already benefit form tax-sparing measures to double the tax benefit they already receive.

[68] An anonymous reviewer of this article views paying tax as losing a tangible personal benefit in exchange for the receipt of (diluted) benefits as a member of the public. I think many taxpayers, rich and poor, believe they don't get value for their tax dollars, in light of how some government departments spend their budgets. To them, lost tangible personal benefits are simply lost.

[69] R. Shillington, "The Dark Side of Targeting: Retirement Savings for Low-Income Canadians" *The Pension Papers* (Toronto: C.D. Howe Institute, 1999) 1 at 3.

suffer reduced entitlement to any GIS they may otherwise receive by reason of its claw-back feature, which responds to an artificial indicator of wealth produced by RRSP income. Retirees who could otherwise be eligible to receive full GIS benefits fall victim to the RRSP regime, which purports to give (tax subsidies for retirement savings) with one hand while taking away (welfare payments) with the other. The blow to low-income earners, according to Shillington, is double: they must sacrifice current consumption in order to put money away into a RRSP,[70] and upon retirement they are deprived of maximum benefits available under the GIS and other income and health care support by reason of their having RRSP income. As claw-backs offset the tax advantages of RRSPs,[71] Shillington concludes that low-income Canadians should forgo RRSPs/RPPs as a retirement savings vehicle and instead undertake pre-retirement savings outside of RRSPs/RPPs.

Shillington's point is important and enlightening. It also brings to light that a tax exemption that diverts tax dollars to a RRSP does not call for any sacrifice of current consumption, since the dollars would otherwise have to be paid as tax anyway. However, it is true that income supplements are, under the current system, subject to claw-back which effects a disincentive for low-income earners to save for their retirement. If they nonetheless save through RRSPs, they will be penalized for having done so by a reduction in GIS benefits that they might otherwise receive.

VI. ESTABLISH A THRESHOLD

Shillington's point is not difficult to overcome. It requires that the government reinforce any increase to the basic personal exemption by setting a threshold for benefits like the GIS, where none currently exists. Retirees who have below the poverty line income would not have their GIS benefits clawed back and therefore would not be

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[70] The savings are locked-in and unavailable until withdrawal.

[71] Shillington writes:

> The system now in place ensures the majority of seniors a relatively comfortable retirement but makes it virtually impossible for low-income seniors to improve their retirement income. Their savings attempts are hardly rewarded at all. Under the current rules, any money they may have saved for retirement simply reduces their eligibility for income, health care, and social support.
>
> ...
>
> Canada's system of tax-subsidized retirement incentives and protections assists middle- and higher-income Canadians, but for lower-income seniors the effect of income testing support generally more than offsets the tax benefits and often punishes those who would have saved for retirement.
>
> ...
>
> For seniors, the evidence below suggests that income testing has gone so far as to create perverse outcomes: *supra* note 69 at 3 - 4.

Shillington depicts the reduction in welfare benefits as effectively a tax on the recipient whose entitlement is taken away – clawed back – by the government:

> Overall, my modeled estimate is that about one-third of all GIS recipients – about 25 percent of singles and 50 percent of couples, pay income tax. The implication is an effective tax rate of at least 75 percent for those paying income tax and receiving the GIS. That is, 50 percent taxback + 17 percent federal personal income tax + 8 percent assumed provincial personal income tax: *supra* note 69 at 6.

penalized for saving for their retirement. There would be one less disincentive to save, in conjuction with one more incentive. The threshold could be easily determined by using the poverty line as a benchmark.[72]

Shillington's further objection is that, under the present system, poor people pay tax at rates that are effectively far higher than those applicable to high-income earners. His explanation is as follows: the 50 percent clawback or reduction rate associated with the GIS is effectively a tax. Low-income seniors may also otherwise be eligible for other support programs like Ontario's GAINS. A senior with an additional $1,000 of monthly income receives $500 less in GIS benefits. If the GAINS benefit is also reduced by $500, the tax cost to the senior is 100 percent.[73]

Shillington's analysis adds to the outcry that federal and provincial governments could go a long way to alleviating hardship currently suffered by low-income seniors. His conclusion that income-assistance benefits should cease at income levels higher than they are now in effect supports an argument favouring a higher basic personal income tax exemption for low-income taxpayers.

VII. WOMEN AS INDIVIDUALS

The proposals made in this paper are meant to address the situation of all low-income earners. But any discussion of low-income groups cannot possibly ignore the prevalence of women within those groups. It is well known that more females than males have low income.[74] In the past decade, much attention has been drawn to the economic disparity of women vis-à-vis men in the paid labour force. Again with reference to the foremost authority in this area of research and advocacy, the following excerpt is drawn from research data meticulously assembled by Claire Young:

> ... [I]t is women in particular who are either fully excluded from these schemes or who receive less in benefits than men. Ascertaining exactly what percentage of women receive income from occupational pensions to which they have contributed is difficult. Nevertheless, it is clear that women receive less income from RPPs ... than men do. In 1993, 58 percent of men 65 and older received RPP income compared to 37 percent of women, and some of these women received this income as a spousal pension based on their male spouse's work history. In 1994, elderly women received only 12 percent of their income from private retirement pensions while for men the figure was almost 25 percent. While women's membership in RPPs has been increasing over the years, it still lags behind that of men. Perhaps the most unsettling

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[72] While the poverty line could be used as a benchmark, the threshold need not be set at the same line but could be set below it. To the extent that retirees require less income to sustain a given standard of living as compared to younger persons who have young children to support, the same line in terms of absolute dollars for all individuals may not provide a true reflection of their individual need.

[73] Shillington's arithmetic is premise-driven on $1,000 of benefits being lost when the retiree has $1,000 of other income. My view however is that this retiree will have received $2,000 but must give up $1,000; therefore the tax rate or cost is only 50%.

[74] See *supra* note 3 at 11. That study found in respect of seniors (aged 65 and over) for a two-year period, 10% of all women had low income compared with 2% of all men.

> statistic is that even though the gap between the number of male and female RPP beneficiaries has narrowed over the years, the gap between the value of those pensions has widened. In 1982, the average pension for women was 67 percent of the average pension for men. By 1992, the value had decreased to only 60 percent of the value of the average pension for men.[75]

Young discloses that various factors prevent women who are in spousal relationships from working for pay. These include the tax rules now in place; lack of accessible, affordable child care and low rates of remuneration.[76] Women who do not work in the paid labour force are dependent on two sources of income after age 65: OAS/GIS plus any provincial supplements available, and anything that might come by virtue of women's relationships to someone else. The recommendations made in this paper encourage women's participation in the paid labour force by ensuring that persons who earn a low rate of pay will be able to keep most of that pay. Given that low-income groups are comprised of more women than men, the proposed measures would likely benefit more women than men. That in itself is an endorsement of these measures as affirmative action, in that they assist women in overcoming traditional dependencies to make strides in their personal financial freedom and decision-making.

Young has also recognized that people who work part-time, or in non-unionized jobs, or for small employers generally do not have a RPP.[77] As women form the majority in these groups, women comprise the majority of persons who need their own RRSP, for want of employer-provided benefit schemes.

VIII. SHOULD THE SYSTEM BE MODIFIED BY WAY OF AFFIRMATIVE ACTION?

The difference for anyone – rich and poor alike – between saving for retirement with a RRSP/RPP, saving outside of an RRSP/RPP, and not saving for retirement at all is plain:

> They can save either entirely on their own, out of after-tax dollars, or with the help of their fellow taxpayers, in tax-assisted vehicles such as Registered Pension Plans (RPPs) or Registered Retirement Savings Plans (RRSPs). A second way in which they can provide for their future income is, in effect, to depend on the kindness of strangers and hope that younger Canadians will give them a share of whatever they may be earning in the years following 2010.[78]

It is not entirely clear what percentage of low-income earners currently have

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[75] *Women, Tax and Social Programs*, *supra* note 20 at 43-44.

[76] The table at page 3 of this article, which shows average incomes for male- and female-headed households, indirectly reveals that women's earnings consistently lag behind that of men, in every wage group and by substantial amounts, assuming that the bulk of the income in those households are earned by the head of the family.

[77] Between 1976 and 1991, women consistently represented at least 70 percent of part-time workers. In 1994, women held 69 percent of all part-time jobs and 26 percent of employed women worked part time. See *Women, Tax and Social Programs*, *supra* note 20.

[78] W. Watson, "The Study in Brief" in *When We're 65*, *supra* note 8 at 1.

tax-sheltered retirement savings by way of RRSPs and RPPs.[79] According to Ragan, the majority of Canadians do not; the returns generated on whatever amount they save and invest are fully taxed.[80] While this does not necessarily mean that they will fare badly after retirement, it does mean that they do not receive their fair share of benefits under our public pension system.

Government-run pensions such as the CPP/QPP and OAS are political undertakings, not legally enforceable contracts.[81] Accordingly, there is no guarantee that people will be able to receive CPP/QPP, OAS and GIS after they retire. There is even less of a guarantee that the public aspect of the system will provide adequately for one's personal needs, since peoples' needs vary. While Shillington worries that income drawn out of private savings will reduce eligibility for government benefits, there is no requirement that a retiree must withdraw his or her savings. If no withdrawal is made in a given year, the amount of GIS entitlement and other benefits that are subject to claw-back will not be reduced for that year. But the savings will be there for a rainy day, and in the event that the government fails to make adequate provision.[82]

The Canadian government's premise underlying the third module of its public pension system is correct: people have a responsibility for their own retirement, whether or not government also has this responsibility. It is not that people *should not* expect government to look after them in their old age; rather, they *cannot*. Governments never make promises that they can keep. A change in government can mean all bets are off. A RRSP or other private pension plan is therefore absolutely necessary – crucial – if one is not to be at the mercy of the state at a phase in life when one is most vulnerable.

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[79] Tax statistics only tell how many taxfilers made contributions to a RRSP/RPP in any given year. In 1997, there were 9,715,500 separate contributions made to RRSPs/RPPs, amongst a total of 21,123,810 tax returns filed. There is inevitably some overlap in that many taxpayers who contributed to an RRSP would also have contributed to a RPP. Therefore the number of individuals making contributions would have been less than 9.7 million. This means that less than 46% of all individual taxpayers made contributions in 1997 (assuming that everyone who made a contribution claimed it on their tax return). Furthermore, RRSPs can be collapsed anytime; persons who were contributors in 1997 may no longer have their RRSP in 2001.

[80] *Supra* note 8.

[81] *Ibid.* at 56.

[82] Government-run pension schemes like the CPP/QPP involve sharing of current national income between their beneficiaries and all taxpayers, with transfers generally running from younger to older persons. In other words, the government applies contributions currently made by workers into such plans to pay benefits to those who no longer work. Economist William Robson has likened the CPP to a Ponzi game – a pyramid scheme – "a scam under which contributions paid in by new members finance payouts to existing members. If the number of new contributors does not continue to grow, payments dry up and the scheme collapses. In the case of the CPP, as current payments to recipients begin to exceed current contributions by wage earners, the plan's small rainy day fund is almost certain to be depleted early in the next century unless payouts or payroll taxes are adjusted. And the CPP will collapse entirely if future wage earners decide they no longer wish to contribute." W.B.P. Robson, "Ponzi's Pawns: Young Canadians and the Canada Pension Plan" in *When We're 65, supra* note 8 at 25. The OAS is theoretically not much more sound, in that this latter program is financed from Government of Canada general tax revenues; in any given year should the government in power decide to reduce expenditures in this area, the program's viability could fall into jeopardy.

Despite Shillington's advice that low-income Canadians should forgo the RRSP as a vehicle for private retirement planning, the present tripartite system, dominated by the tax-subsidized registered private plan, is undeniably the status quo and promises to remain so. There is no reason why low-income Canadians should not partake in all of the benefits that the system has to offer. Rather than succumbing to arguments that the system does not serve them, why should they not be granted a system that does? As any law can be changed, the terms of application of any existing system are always subject to modification. All it takes is someone to make those modifications.

The two suggestions made in this paper – to provide a higher income tax exemption targeted exclusively to low-income earners conditional on the amount otherwise payable as tax being contributed to a retirement savings plan, and to establish a threshold for the GIS clawback – can help to alleviate poverty in retirement without freeing people from personal responsibility for their own future. Tax benefits provide public subsidies, but one must work for them. Implementing clawback thresholds for the GIS reduces the disincentive of retirees to look to income from private resources. I do not believe that the government can give any meaningful comfort to poor seniors. But I do believe that government can be just and should strive to be fair. It is not just for government to pay out public money, by way of tax benefits or otherwise, to well-off taxpayers while leaving the poor to fend for themselves. The reason there is no consensus amongst experts and other interested parties as to how to alleviate poverty in Canada is because there is no real solution – it cannot be done. But what can be done is to give those who do not presently receive a share of certain public benefits something of those very same benefits, even if it be only the chance of access. That is the only intended theme of this paper, really.[83] Hopefully, it will move political will to manifest itself along the same lines.

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[83] I would like to thank one of my anonymous reviewers who mistakenly had thought that the goal of my proposals is to increase the retirement income of low-income individuals. The underlying purpose of my paper is to say that certain tax preferences in the *Income Tax Act*, currently given to middle- and high- income earners, should also be provided to low-income earners. If low-income earners cannot access the tax preferences because of their low income, then the preferences should be made more accessible to them, in the event that they should want them. To you it's about money, to me it is about equality. The difference is that the concept of equality encompasses much more than money. Your comments ensured that I make this point clear.