BREAKING CANADA'S WELFARE TRAP

By Jason Dean

Jason Dean Would you spend more time at work if it were to make you worse off financially? I know I wouldn't. But this is the unfortunate reality for many low-income Canadians who rely on social assistance to make ends meet. By working, or working more, recipients lose a large portion of each new dollar they earn – to taxes, reduced income support and withdrawal of other in-kind benefits. This phenomenon has been called the "welfare wall" or "welfare trap." Workers run into when they start moving from welfare to self-sufficiency and, as they earn more, start losing government support and paying taxes like ordinary workers.

It's the very problem the Canada Workers Benefit (CWB) was meant to address when it was introduced in 2007. Its stated aim was to "make work pay" by enabling low-income workers to keep more of their earnings, thus further encouraging their return to employment.

The first problem with the CWB is the timing of its disbursements. It is handed out once a year, during tax season. But the lost benefits and new taxes incurred by low-income Canadians currently relying on welfare and looking to take on a new job occur in real-time – and can be substantial. In Quebec, for instance, every dollar you earn past $200 per month loses you a dollar in benefits. That's a 100 per cent tax rate! Ontario is not as bad – you only lose 50 cents for every dollar earned – but it's still a very sharp clawback, and it's made even worse when you add income and payroll taxes to the mix, as well as the loss of non-monetary benefits such as insurance coverage.

In both provinces, benefits are lost the moment you start earning income, thus digging a hole worth a few hundred dollars in the monthly budgets of those who already have very little. For someone living paycheque to paycheque now, the prospect of being compensated a year from now for lost benefits is scant comfort. Unlike the Canada Workers Benefit, your bills don't wait until the end of the year to pile up. To its credit, the federal government has recognized this problem. Unfortunately, its proposed solution of making payments quarterly as of this year falls short of the ideal. How many bills are due only every three months?

The government must make CWB payments bi-weekly – the same frequency as most people's paycheques. Bi-weekly payments would directly link the decision to work with the mechanism designed to reduce the impact of lost benefits. It's not as if more frequent deposits are unprecedented. Ottawa already makes monthly deposits of the GST/HST tax credit and the Canada Child Benefit.

Reform also needs to address the work disincentive directly. As it stands, the CWB is almost entirely phased-out once a person starts working full-time – even at minimum wage. It is so low, in fact, that the CWB does almost nothing to offset clawbacks on earnings.

Without the CWB, an Ontarian working full-time at minimum wage would give back to the government 44 cents of every dollar they earn once clawbacks and taxes are taken into account. With the paltry CWB payments they would get, it goes down to 43 cents per dollar. As far as motivating tools go, this can't be very effective. The net effect is to spend more of taxpayers' money keeping people dependent because of a failure in policy design.

It's estimated that in Ontario alone, a targeted 20 per cent top-up for transitioning to full-time work on the Canada Workers Benefit – if paid biweekly – could help convince 190,000 Ontarians to take full-time jobs instead of part-time or welfare payments. This alone would generate $120 million in net savings for taxpayers. This is the conclusion we reached based on data from the Self-Sufficiency Project, a rigorous Canadian study looking at the effects of monetary incentives for welfare recipients and the adoption of full-time employment.

This $120 million in net savings for taxpayers is even after the costs of program expansion are taken into account, as it would lower what we have to spend on welfare and yield new tax revenues from those new jobs. And that's just in one province, albeit Canada's largest.

It's also important to note that this change would only impact those who are able to work but are stuck behind the welfare wall, not all welfare recipients, many of whom can't work.

As it stands, the Canada Workers Benefit simply doesn't work for Canadian workers. Fifteen years into this experiment, it's time to make the changes that will allow it to succeed as intended.

Jason Dean, associate researcher at the Montreal Economic Institute, is assistant professor of economics at King's University College at Western Ontario.