

TAXATION OF ONE- AND TWO-EARNER FAMILIES

Position statement by the
New Brunswick Advisory Council on the Status of Women
August 2005

Issue:

- One-earner and two-earner dual-parent families with dependent children are treated differently by the tax system, sparking controversy about tax fairness:
 - The same total family income may be taxed at a different rate depending on whether there is one earner or two.
 - The child care expenses deduction is only available to families using paid non-family caregivers.
 - Stay-at-home parents are not allowed to contribute to RRSPs in their own names while not earning an income.

Background:

- **The debate around the fairness of tax rules as they affect different types of families with dependent children has been raging for a number of years. A House of Commons Finance sub-committee held hearings on the question in 1999.**¹
- Some groups and individuals claim that Canada's income tax system financially penalizes one-earner families with stay-at-home mothers and favours families where both parents are out working for pay.²
- Others, including gender equity-seeking groups and some economists, argue that the tax discrimination claim is unfounded and sets up a false antagonism between different family types.³

¹ The Sub-Committee on Tax Equity for Canadian Families with Dependent Children concluded that the Canadian tax system does not treat one-earner families inequitably. However, it did recommend that the federal government consider introducing some new tax benefits and options to improve the situation of stay-at-home parents, including: reviewing the child care expense deduction to make sure it meets its policy objectives efficiently and effectively; options for stay-at-home parents to contribute to pension plans during their caregiving years; improvements to the maternity and parental leave provisions of Employment Insurance, including greater flexibility and extension of the leave period to one year; and introducing a new refundable tax credit under the Canada Child Tax Benefit for parents who "provide direct parental care." The 2000 federal budget extended maternity and parental leave provisions, but did not introduce the other recommended reforms. *For the Benefit of our Children: Improving Tax Fairness*, Nineteenth report of the Standing Committee on Finance, Sub-Committee on Tax Equity for Canadian Families with Dependent Children, June 1999.

² See for example, REAL Women of Canada, "Pension and Tax Reform", available at www.realwomenca.com/papers/pension_and_tax_reform.htm; Kenneth J. Boessenkool and James B. Davies, "Giving Mom and Dad a Break: Returning Fairness to Families in Canada's Tax and Transfer System," C.D. Howe Institute *Commentary*, November 1998.

³ See Nova Scotia Advisory Council on the Status of Women, *Where is the Inequity?: A Comparison of Tax Paid by Two-Earner Families that use Child Care and One-Earner Families with Pre-School Children at Home*, May 1989; Canadian Centre on Policy Alternatives, B.C. Office, *Submission to the House of Commons Finance Sub-Committee on Tax Fairness for Canadian Families with Dependent Children*, May 1999; Lisa Philipps and Kim Brooks, *Supporting Families, Supporting Gender Equality: Improving Canada's Tax and Transfer System*, NAWL submission to the House of Commons Finance Sub-Committee on Tax

• **It is important to take a closer look at the various elements of the debate and to set it in the larger context of the tax system and social policy.**

- In most New Brunswick two-parent families with young children, both parents are wage earners. Of 76,600 families with a youngest child under 16 in 2004:
 - 61,200 are two-parent families
 - o both parents were in paid employment in 43,500 or 71% of these two-parent families
 - o one parent was in paid employment and the other was not in the labour force in 17,700 or 29% of these two-parent families
 - 15,400 are lone-parent families (13,200 female-headed; 2,200 male-headed) of which 11,200 or 73% of the parents were in paid employment.

In all, in 54,700 families or 71% of families with a young child/children, the parent or parents are in the labour force.

• **Differences in taxes paid by one- and two-earner families with the same total family incomes are largely the result of two basic characteristics of Canada's tax system: the individual unit of taxation and "progressive" tax rates.** Married or common-law couples must file separate tax returns if both spouses have income and their income is assessed separately for tax payment purposes. Individuals with higher incomes are expected to contribute a higher percentage of their income through taxes (see tax rates below).

Federal and New Brunswick tax rates for 2004

Federal tax rate	N.B. tax rate
16% on the first \$35,000 of taxable income	9.68% on the first \$32,183 of taxable income
22% on the next \$35,000 of taxable income	14.82% on the next \$32,185 +
26% on the next \$43,804 of taxable income	16.52% on the next \$40,280 +
29% of taxable income over \$113,804	17.84% on the amount over \$104,648

Source: Canada Revenue Agency, at www.cra-arc.gc.ca/tax/individuals/faq/2004_rate-e.html

• Take the example of a one-earner family with a taxable income of \$50,000 and a two-earner family in which one spouse has a taxable income of \$30,000 and the other a taxable income of \$20,000. Using the 2004 tax rates, the lone earner would owe a total of about \$14,600 in federal and provincial taxes or 29% of his/her taxable income. The lower-income earner in the two-earner family would owe about \$5,100, and the higher-income earner about \$7,700, or 26% of their combined taxable income.

• Some have suggested making the family the unit of taxation, or at least allowing couples the option of filing joint tax returns.⁴ However, basing taxes on combined family income would tend to disadvantage women since:

- Women earn on average much less than men. If spouses had to combine their income for tax purposes, the female spouse's income would likely be taxed at a

Fairness for Canadian Families with Dependent Children, May 1999; Richard Shillington, *The Tax Debate over One- and Two-Earner Families*, April 2000, available at <http://www.shillington.ca/benefits/benefits.htm>

⁴ REAL Women of Canada has urged the federal government to allow for joint spousal tax filing with a lower tax rate for single income families. REAL Women of Canada, "Pension and Tax Reform", available at www.realwomenca.com/papers/pension_and_tax_reform.htm

higher rate than if she filed an individual return. The male spouse would typically benefit from the tax relief.

- Moreover, income is not necessarily shared equally within the family. In practice, many women have limited or no access to the financial resources of the household.

• When comparing the tax treatment of one-earner versus two-earner families with children, it should also be noted that the one-earner family is entitled to a benefit that is generally denied to two-earner families, the spousal tax credit.

- The spousal amount is a non-refundable credit that can be claimed if one partner in a couple has little or no income. The earning spouse is entitled to claim the non-earning spouse as a dependant and receives a tax break because of it. This credit can reduce taxes owing by up to about \$1,700.⁵

- While some people view the spousal tax credit as a recognition of the value of unpaid work done by women in the home, if that were the case it should be made a refundable credit paid to the stay-at-home spouse.⁶

• At the heart of the tax fairness debate is the deduction for child care expenses, which is not available to families where one parent is at home caring for the children. The child care expense deduction allows one of the parents or supporting persons (generally the lower-income person) to deduct child care expenses of up to \$7,000 for each child under 7, \$4,000 for each child between 7 and 16 (or for older children who have a mental or physical infirmity for whom the disability amount cannot be claimed) and \$10,000 for those under 1 for whom the disability amount can be claimed.⁷

- The provision for the deduction of child care expenses was introduced by the federal government in 1972, to help women with children to enter the paid labour force.⁸ While this deduction may encourage some parents to use formalized child care, it was clearly not intended

⁵ Federally, individuals supporting a spouse or common-law partner whose net income is less than \$7,484 may claim the spousal credit. They may claim the maximum credit of 16 per cent on \$6,803, or \$1,088, if the spouse or common-law partner's income was \$681 or less. That credit is reduced if the spouse or common-law partner's net income is more than \$681 but less than \$7,484, where the credit is eliminated. Provincially, New Brunswick taxpayers supporting a spouse or common-law partner whose net income is less than \$7,245 may claim the spousal credit. They may claim the maximum credit of 9.68% on \$6,586 or \$637, if the spouse or common-law partner's income was \$659 or less. That credit is reduced if the spouse or common-law partner's net income is more than \$659 but less than \$7,245 where the credit is eliminated.

⁶ It has also been argued that this spousal tax credit may in some cases discourage women's labour force participation, since the loss of the tax credit may weigh in a decision to take on what are often low-paying jobs. More than 30 years ago, a background study for the Royal Commission on the Status of Women in Canada (1967-1970) suggested that rather than giving a tax break to husbands whose wives do not work outside the home, it should be recognized that the unpaid work done by homemakers in the household has a value. The husband should be required to pay tax on it. Townson, *Tax Facts: What Every Woman Should Know*, p. 20-21; see also Canadian Advisory Council on the Status of Women, Maureen Maloney, *Women and Income Tax Reform: Background Paper*, Ottawa, CACSW, October 1987, p. 10-13.

⁷ See Canada Customs and Revenue Agency, Child Care Expenses Deduction for 2004, available at: <http://www.cra-arc.gc.ca/E/pg/tf/t778/README.html>

⁸ Claire F.L. Young, *Women, Tax and Social Programs: The Gendered Impact of Funding Social Programs Through the Tax System*, Ottawa, Status of Women Canada, October 2000, p. 20.

as a child care program. It is simply a deduction for work-related expenses, a means of compensating the taxpayer for the cost of earning income.⁹

- Because it is a deduction that reduces taxable income rather than a fixed amount credit provided to all taxpayers, the CCED is more beneficial to higher income taxpayers. This is a flaw of the deduction as it presently stands. It should also be noted that many two-earner and lone-parent earner families cannot benefit from this deduction because they pay in cash for informal child-care arrangements and are unable to provide the required receipts.

- **Tax provisions regarding restrictions on who may contribute to RRSPs have also been criticized as discriminatory. Only earning spouses can contribute to RRSPs in their own name, thus excluding the usually female stay-at-home spouse. The earning spouse can, however, contribute to an RRSP on behalf of the spouse without an income. In any case, it is usually the male spouse who benefits most from the tax subsidy of the deduction.**¹⁰

- Fewer women contribute to RRSPs and those who do contribute less than men in N.B. In 2003, only 15% of the province's female taxfilers compared to 21% of male taxfilers invested in RRSPs. Women's median contribution was \$1,600 in 2003, compared to \$2,400 for men in N.B. Women's share of total contributions was 36% in 2003.¹¹

- This discrepancy in RRSP savings is a problem, since N.B. women are also less likely than men to be covered by an employer-sponsored or union pension plan: in 2002 as in 2001, 37% of female paid workers and 43% of male paid workers had a private pension plan.¹²

- **In order to test the unfair treatment claim, we need to take into account not only the tax paid but also the work-related expenditures of the one- and two-earner families, such as child care, transportation, extra clothes, and so on.**

- **Some in-depth analyses of the after-tax income situation of one- and two-earner families suggest that the concerns about discrimination against one-earner families are unfounded.**

- In their 1999 study, economists Gordon Cleveland and Michael Krashinsky concluded that one-earner families with children are in fact *advantaged* by the tax system compared to two-earner families with children. While two-earner families may pay slightly less tax, they have child care costs and other work expenses not shouldered by one-earner families. At the end of the day, one-earner families have more income left to spend than do two-earner families.¹³ In addition, the

⁹ Christa Freiler, Felicite Stairs and Brigitte Kitchen with Judy Cerny, *Mothers as Earners, Mothers as Carers: Responsibility for Children, Social Policy and the Tax System*, Ottawa, Status of Women Canada, March 2001, available at:

http://www.swccfc.gc.ca/pubs/pubspr/0662655206/200103_0662655206_1_e.html; see also Michael Krashinsky and Gordon Cleveland, *Tax Fairness for One-Earner and Two-Earner Families: An Examination of the Issues*, Canadian Policy Research Networks Discussion Paper, December 1999, available at <http://www.cprn.org/en/doc.cfm?doc=792>

¹⁰ Young, *Women, Tax and Social Programs*, p. 46-47.

¹¹ Canadian patterns are similar, with greater taxfiler participation (24% of Canadian females and 29% of Canadian males in 2003) and larger median contributions. Statistics Canada, Small Area and Administrative Data Division, Financial Databanks, 2003 RRSP Contributors.

¹² Statistics Canada, Income Statistics Division.

¹³ See Krashinsky and Cleveland, *Tax Fairness for One-Earner and Two-Earner Families: An Examination of the Issues*, Canadian Policy Research Networks Discussion Paper, December 1999, available at <http://www.cprn.org/en/doc.cfm?doc=792>. The federal sub-committee on the question invoked the same arguments regarding additional employment-related expenses and the value of unpaid work in the home. See Krashinsky and Cleveland, *Tax Fairness for One-Earner and Two-Earner Families*, p. 5.

non-taxation of household production is an important, though rarely considered, tax break for one-earner families. Under the current system, only one replacement for household work (child care expenses) is tax deductible, but all the others (cleaning services, take-out foods, etc.) are not.¹⁴

• The Nova Scotia Advisory Council on the Status of Women came to a similar conclusion in its analysis of the tax paid by the two types of families in 1989.¹⁵

Advisory Council position:

Families with young children face particular financial challenges, whether just one or both parents are in the paid labour force. We believe that people with dependent children should pay lower taxes than people without, to compensate for the costs of raising children. Many of the larger problems involving the well-being of women, men and children can only be partially addressed through the tax system.

With regards to Canada's income tax system, the NB ACSW recommends:

- ▶ That individual taxation should remain the basis of the tax system. Taxation provisions that have the effect of reinforcing the economic dependency of women on their spouses, such as the spousal tax credit, should be revisited.
- ▶ That the child care expense deduction should remain for two-earner and lone- parent earner families only, as exists currently, since they must bear the burden of this necessary employment expense. Rather than an unfair advantage for two-earner families, this deduction related to earnings also partially corrects for the advantage enjoyed by one-earner families in the non-taxation of household work.
- ▶ That a significant tax credit for dependent children be made available to all families with children so that they may be better compensated for the costs of raising children. In order to further benefit low-income families who may pay little tax, this should be made a refundable tax credit.¹⁶

Policy changes beyond the tax system are also evidently needed to improve the well-being of

¹⁴ The argument is echoed by Frances Woolley, Professor of Economics, Carleton University in "For a Radical Redesign of Our Tax Treatment of the Family", *Policy Options*, September 1998, p. 8-9, available at: <http://www.irpp.org/indexe.htm>.

¹⁵ *Where is the Inequity?: A Comparison of Tax Paid by Two-Earner Families that use Child Care and One-Earner Families with Pre-School Children at Home*, May 1989.

¹⁶ Such a measure is favoured by the economists Michael Krashinsky, Gordon Cleveland, and Frances Woolley, and by many social scientists. Note that Canada for many years provided a universal child benefit to families with dependent children. Beginning in 1945, Canada used the Family Allowance program to provide a monthly benefit to families regardless of income or labour force status. The program underwent changes in the 1960s and 1970s and in 1979, a refundable tax credit was introduced as a complementary measure. In 1993, the family allowance, along with existing child tax credits, were replaced by a new income-tested child tax benefit that provided monthly benefits based on the number of children and the level of family income. See Government of Canada, 1944 - Family Allowance Program, at: <http://canadianeconomy.gc.ca/english/economy/1944family.html> ; see also Christa Freiler *et al.*, *Mothers as Earners, Mothers as Carers*.

women and families with children:

- The provincial and federal governments must work together to provide universally accessible, publicly funded, quality early childhood education and care programs.
- The design of and investment in social programs such as employment insurance and pensions must take into account the needs of those involved in caregiving work, including wage earners and stay-at-home women and men. Stay-at-home caregivers should have independent access to social and labour benefits including worker's compensation, disability and retirement benefits, employment insurance and retraining programs.
- More attention must be directed towards improving the standard of living for low-income families, and particularly female lone-parent families, through increases and indexing of the minimum wage, social assistance and provision of quality job opportunities.