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Income Splitting in Canada

Inequality by Design

David Macdonald

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Income Splitting in Canada

Inequality by Design

Executive Summary

Canada's experimentation with income splitting began with pension income in 2007 and the federal Conservatives have pledged to extend income splitting to all families with children under 18 after the budget is balanced.

This study examines the cost in terms of lost government revenues and the distributional impact of three scenarios: pension income splitting; income splitting for families with children under 18; and income splitting for all families, whether they have children or not.

Pension Income Splitting

This study finds that, in 2015, Canada's federal government will give up an estimated $1.2 billion in lost revenue due to pension income splitting and the provinces will lose another $500 million in revenue for mimicking this tax change—for a total revenue loss of $1.7 billion.

The study also looks at the distributional impact of pension income splitting among seniors. It finds the gains from the pension income splitting loophole go disproportionately to senior couples in the richest four deciles — the richest 40% of the Canadian senior population.

In fact, the richer the senior family, the more it receives from this loophole. The poorer the senior family, the less support it receives:

- The poorest 10% of seniors receive an average of 10 cents in terms of a tax break from this loophole, whereas the richest 10% receive an average of $820 in perks.
- One out of five among the richest 10% of Canada's senior families receive a cheque for over $1,000 from this program while three out of five make some gain from it.
- Of the poorest half of all senior families, only one out of every 1,000 seniors gets more than $1,000 from pension income splitting.
- Seven out of 10 seniors enjoy no benefit at all from this tax loophole.
- The poorest half of all senior families — they're making less than $36,000 a year — receive only $2 out of ever $100 paid out by this loophole.
- The richest 10% of senior families, making over $85,000, receive $30 out of every $100 paid out.
- The richest 10% of senior families receive more than the bottom 70% of families.

The study concludes that the cost of this tax loophole is large and gets larger every year. While most of this program's payouts are going to Canada's richest seniors who don't need extra support, there remain seniors who live below the poverty line.[1] In fact, to lift all Canadian seniors out of poverty, it would cost approximately $1.5 billion a year — slightly less than Canadian governments are currently spending to bolster Canada's richest seniors through pension income splitting measures.

Income Splitting for Families with Children Under 18

Given the 2011 Conservative party promise to expand income splitting measures to include families with children under the age of 18, this study utilizes custom SPSDM tax modelling software to estimate the potential cost to both federal and provincial governments as well as to ascertain which families stand to gain the most from income splitting and which stand to gain the least.

In this second income splitting scenario, the study evaluates the cost associated with income splitting for families with children under 18 years old, with up to a maximum of $50,000 transferred between spouses, projected for the year 2015. The customized SPSDM tax model estimates such a tax shift to cost $3.0 billion a year in lost revenue federally and an additional $1.9 billion provincially. That represents a total annual loss of $4.9 billion in 2015 alone. This cost is over and above the cost of pension income splitting in the first scenario.

Meanwhile, much like pension income splitting, the perks of extending income splitting to families with children under 18 overwhelmingly go to families in the upper 40% of Canada's income distribution:

- The bottom 60% of all families (those making $56,000 or less) would receive, on average, $50. Most families would receive no benefit whatsoever.
- In contrast, the richest 5% of all Canadian families — those making over $147,000 — would see an average benefit of $1,100, with one in 10 of this elite group gaining more than $5,000 from this loophole.
- The top 5% of all families would see more benefit than the bottom 60% of families.
- In fact, none of the bottom six deciles would receive anywhere near 10%, its equal share; whereas each of the top four deciles receives far more than 10% of the total benefit, or far more than their equal share.
- 86% of all families would gain no benefit whatsoever from this tax loophole.
- 4% of all families would gain less than $500.
- 1% of all families would get more than $6,500. Most of those $6,500 gainers are already among Canada's richest.

Income Splitting for All Families

What would happen if income splitting was extended to all families, regardless of whether they have children or not and the pension income splitting loophole was maintained? The customized SPSDM tax model estimates it would cost the federal government an estimated $7.5 billion in lost revenue annually and it would cost the provinces $4.3 billion in lost revenue annually for a total annual revenue loss of $11.8 billion in 2015.

In terms of who would gain and who wouldn't:

- The top 10% of families do even better under this third scenario, gaining a whopping 34% of all benefits — the highest of any of the three scenarios.
- None of the bottom six deciles gains an even share of 10% of all benefits. Their benefits fall below the equality line.
- The average benefit for the bottom 60% of Canadian families making $56,000 or less would be just $175, while the richest 5% of families (with family income more than $147,000) would receive an average benefit of $3,100.
- Of those top 5% of families, one in five would receive a cheque for more than $5,000.
- These lavish benefits are almost completely absent for the bottom half of all families.
- The bottom half of families — those making under $46,000 — three in 100 would gain $1,000 or more and four in 10,000 families would get more than $5,000. The 10% of Canada's poorest families — those making less than $17,000 a year receive an average benefit of only $7.

The study concludes that the impact of income splitting in all three scenarios is very unequal. In essence income splitting exacerbates income inequality, by design.

The study also concludes the cost in lost revenue for Canadian governments would be substantial — especially since it disproportionately benefits those who are on the upper end of the income spectrum. If Canadian governments are concerned about supporting families with children, a far more equitable way of doing so would be to provide a universal child care program similar to the Quebec model, reducing child care costs from their current $40 to $50-a-day to the $7-a-day range. This would be of particular benefit to lower income families, since it would allow both parents the flexibility to work and thereby contribute to family incomes. Increased female workforce participation in Quebec is one of the prominent effects of high-quality, affordable child care.

Introduction

Canada is flirting with further changes to its tax code through income splitting for tax purposes. This paper examines the implications of such a policy direction.

The first implementation of income splitting in Canada occurred in 2007, when the federal government allowed seniors to split their pension income in order to lower the tax bill for the higher income earner within a senior couple.[2] While this measure was introduced by the federal government, all of the provinces went along with it, allowing pension splitting on provincial income taxes as well.[3]

In the 2011 federal election, the federal Conservative party advocated for general taxable income splitting to also be applied to families with children under 18, limiting the transfer to $50,000.[4] However, advocating for income splitting is not limited to the federal Conservative party. The federal Green party also included it as part of its last election platform.[5] The Progressive Conservative Party of Ontario has also pledged to implement provincial income splitting.[6]

This paper provides an updated estimate of what income splitting will cost governments, both federal and provincial. It focuses more specifically than previous papers on the distribution of benefits, laying bare who the ultimate beneficiaries of income splitting are.[7]

Income Splitting: A Brief Primer

The foundation for income splitting is based on the progressive income tax system in place for at the federal and provincial level.[8] The premise of a progressive income tax system is this: as one's income rises past a certain threshold, one pays a higher proportion of taxes. That is, those who have more are counted on to contribute more in terms of income taxes. As *Figure 1* shows, if a Canadian has taxable income of $44,000 in 2014, he or she will pay 15% of that total income to the federal government. If that same person makes $44,001 in 2014, that extra dollar pushes them into a higher income threshold which is subject to a higher tax. As a result, they will pay 15% on the first $44,000 of their income, but they will pay 22% on that additional dollar over the $44,000 threshold.[9] Each province, except Alberta, has an income tax system of this type, although the income thresholds and tax rates vary by province.

FIGURE 1 Federal Income Tax Rates (2014)[10]

Income Range (Individuals)	Income Tax %
0–$44,000	15%
$44,000 to $88,000	22%
$88,000 to 136,000	26%
Over $136,000	29%

Source Revenue Canada[11]

FIGURE 2 Income Splitting Example

	Family 1 (2 Earners)		Family 2 (Sole Earner)	
	Income	Federal Taxes	Income	Federal Taxes
Spouse 1	$40,000	$6,000	$80,000	$14,080
Spouse 2	$40,000	$6,000	$0	$0
Total Family	$80,000	$12,000	$80,000	$14,080

Income taxes in general in Canada are levied in individual, not family, units. The premise behind income splitting is to create a tax loophole for certain types of family income. The income splitting argument is simply this: allow some families to "split" their income evenly among the spouses, irrespective of whether one person makes far more than the other.

Returning to *Figure 1*, if a family has two income earners and each makes $40,000 in taxable income, as individuals they would both fall into the first federal tax bracket and pay 15% federal income tax.[12] They would each have $6,000 deducted from their paycheques in federal tax, or $12,000 as a family. In other words, the family's total income of $80,000 is subjected to a 15% federal tax which amounts to a $12,000 total family contribution to federal revenues, as shown in *Figure 2*.

Let's take a look at the tax rate for a couple where one person makes $80,000 and the other person makes no income.[13] The $80,000 sole earner is taxed at 15% on the first $44,000 and 22% on the remaining $34,000. The sole earner in this case would have $14,080 deducted in federal taxes.[14] As a family, they have the same total family income of $80,000 as the previous family, but they contribute $14,080 in taxes instead of $12,000, as illustrated in *Figure 2*.

Income splitting purports to remedy this perceived inequity by allowing families to split their incomes on the tax form in order to contribute the lowest possible amount. Under income splitting, both families would contribute $12,000 in taxes because the single earner family can split the difference and wind up in a lower tax bracket. The theory only works in practice if there is a large income difference between a couple. If the income difference between the two earners in a family is small, they are likely already in the same tax bracket. Therefore, adding up and then splitting family income would not change the amount of taxes owed by a family. Income splitting is of no use for single parent families, since there is no one to split the difference with at tax time. It should also be noted that single parent families tend to have lower family incomes in the first place.

The Cost of Income Splitting

This report focuses more attention than previous papers on the distributional impacts of three different versions of income splitting in addition to updating their fiscal costs:

1. pension income splitting, which is already allowed in Canada;
2. non-pension, general income splitting for families with children under 18, up to a maximum of $50,000; and
3. the combined impact of pension income splitting and general taxable income splitting for all families.

All cost estimates and distributional impacts are estimated for 2015 using customized SPSDM 21.0. [See Appendix One for study methodology and assumptions.]

The first category under examination is pension income splitting, which is already in place at both the federal and provincial levels. As such, these are real revenue losses that will be incurred by both levels of government in 2015: the federal government will give up an estimated $1.2 billion in lost revenue and the provinces will give up $500 million in lost revenue at a time when both levels of government are combating fiscal deficits incurred in part because of the 2008–09 recession.

The second income splitting scenario estimates the cost in lost revenue that would be associated with income splitting for families with children under 18 years old, with a maximum of $50,000 transferred between

FIGURE 3 Cost and Family Distribution of Income Splitting, Canada ($million)

Family Ttype	Pension Income Splitting	Taxable Income Splitting (children <18, Max $50,000 Transfer)	Pension Income Splitting and Taxable Income Splitting for All Families
Couples with Children Under 18	$80	$3,010	$3,220
Couples with Children 18 or Over	$60	$0	$750
Couples Without Children	$230	$0	$2,380
Couples with One Person Over 65	$810	$0	$1,160
Single Parent and Single Person Families	$0	$0	$0
All Families (Federal)**	**$1,190**	**$3,010**	**$7,500**
All Families (Provincial)	$510	$1,940*	$4,330*
All Families (Federal & Provincial)**	**$1,690**	**$4,940***	**$11,830***

Source SPSD/M 21.0 and author's calculations[16]
* These figures are contingent upon provincial adoption of federal changes in the definition of taxable income
** Totals may not add due to rounding

spouses. This essentially costs out the federal Conservative party's 2011 proposal, although these figures are projected for 2015. The provincial estimate assumes the provinces implement the same proposal for their income taxes as they did with the federal move to allow pension income splitting. The second scenario is estimated to cost $3.0 billion a year in lost revenue federally and an additional $1.9 billion provincially. That represents a total annual loss of $4.9 billion in 2015 alone. This cost is over and above the cost of pension income splitting in the first scenario.[15]

The third income splitting scenario examines the total cost of pension income splitting and general taxable income splitting for all families. As with scenario two, the provincial estimate assumes the provinces implement the same proposal for their income tax as they did with pension income splitting. Full taxable income and pension income splitting would cost the federal government an estimated $7.5 billion in lost revenue annually and it would cost the provinces $4.3 billion in lost revenue annually for a total annual revenue loss of $11.8 billion. The $11.8 billion figure represents an upper bound on what income splitting could cost in Canada. All three scenarios are represented in *Figure 3*.

Clearly, these tax changes are very expensive. To date, approximately $1.7 billion in revenue is already lost annually due to pension income splitting at the federal and provincial level. Income splitting for families with children under 18 would represent an additional $4.9 billion a year in lost revenue. If pension and taxable income were available to all families, the cost could be almost $12 billion in lost revenue a year, assuming the provinces follow suit.

Pension Income Splitting

In contrast to income splitting for non-senior families, pension income splitting for seniors does two things: it can reduce the taxes senior couples owe, and it can also increase government transfers. Pension income splitting allows one person who is having their Old Age Security (OAS) clawed back, due to high pension income, to avoid this situation by transferring pension income with their spouse. This allows the higher earner to receive the full OAS benefit, without clawbacks. In fact, of the $1.2 billion federal cost for pension splitting in 2015, $250 million of that cost is due to increases in OAS payments that wouldn't have otherwise occurred.

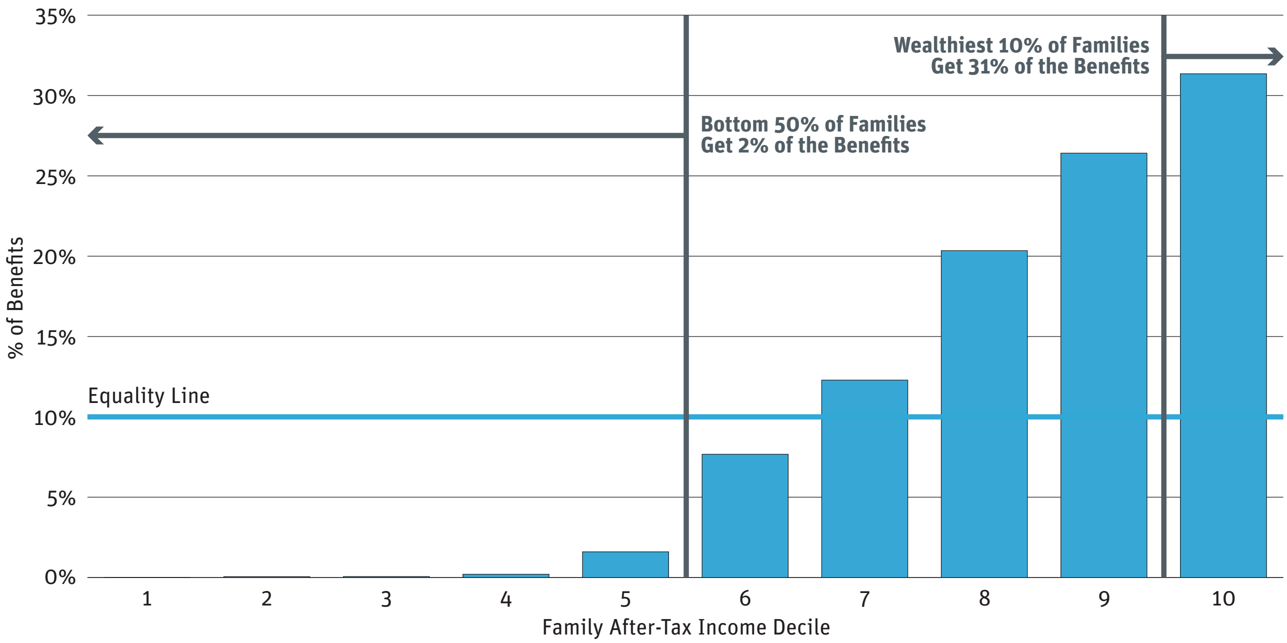
SPSDM, the tax modelling software used for this analysis does not estimate the behavioural changes that may occur due to a policy change. In the case of income splitting, it doesn't estimate how many additional families will decide to have one person stay home with children, for example, because of income splitting. It only estimates the "morning after" costs. But since pension income splitting has actually been implemented in Canada, it is indeed possible to compare both the actual revenue loss with the SPSDM estimated revenue loss. This can provide some insight into how SPSDM estimates of taxable income splitting might compare to the actual tax expenditures once behavioural changes are taken into account.

SPSDM 15 estimated pension income splitting would cost $750 million in lost tax revenue in 2007. The actual revenue loss was $840 million.[17] This difference may not be due entirely to behavioural changes. Other differences in growth estimates, for instance, may also be to blame. However, there may be evidence that the estimated SPSDM cost for pension income splitting and taxable income splitting may underestimate the final cost, since the model cannot capture behavioural change induced by policy shifts.

Distributional Impact of Pension Income Splitting: Who Wins?

While the income splitting tax loophole would be expensive, there is another problem that income splitting creates: the distribution of who receives the largest benefit is disproportionately weighted towards the richest Canadians. Canada's poorest families receive almost no benefit from this loop-

FIGURE 4 Pension Income Splitting (Distribution Seniors Families)



Source SPSDM 21.0 and author's calculations

hole. And, as mentioned before, single-parent families and Canadians living alone would gain no benefit from the creation of this tax loophole.

The distribution of the benefits from the pension splitting loophole are not even close to even. *Figure 4* shows the proportion of total tax perks that go to families, by income decile. The income deciles represent senior families in slices of 10%, going from the poorest 10% to the richest 10%. The solid line the 10% mark in *Figure 4* illustrates the point at which income splitting perks would be equally meted out. If senior couples in one decile receive less than the equality line, then it is not getting its equal share. If a senior couple in a decile is getting more than the equality line it is getting more than its equal share.[18]

As *Figure 4* shows, the gains from the pension income splitting loophole go disproportionately to the richest four deciles — the richest 40% of the Canadian senior population. In fact, the richer the senior family, the more it receives from this loophole. The poorer the senior family, the less support it receives. The poorest 10% of seniors receive an average of 10 cents in terms of a tax break from this loophole, whereas the richest 10% receive an aver-

FIGURE 5 Costs of Pension Income Splitting

Estimate	Price Tag
Federal Cost	$1.2 billion
Provincial Cost	$0.5 billion
Total Government Cost	$1.7 billion

Source SPSDM 21.0 and author's calculations

age of $820 in perks. The richest 10% of senior families receive more benefit from this loophole than the bottom 70%.

Looking at it from another vantage point, one out of five of the richest 10% of Canada's senior families receive a cheque for over $1,000 from this program while three out of five make some gain from it. Of the poorest half of all senior families, only one out of every 1,000 seniors gets more than $1,000 from pension income splitting. Seven out of 10 seniors enjoy no benefit at all from this tax loophole.

The poorest half of all senior families — they're making less than $36,000 a year — receive only $2 out of ever $100 paid out by this loophole. In contrast, the richest 10% of senior families making over $85,000 receive $30 out of every $100 paid out.

Most of the seniors in the bottom 40% of the income distribution are single women. As such, there is no one to split with and therefore no benefit from this loophole.

The cost of this tax loophole is large and gets larger every year. While most of this program's payouts are going to Canada's richest seniors who don't need extra support, there remain seniors who live below the poverty line.[19] In fact, to lift all Canadian seniors above the After-Tax Low Income Measure (AT-LIM) poverty line in Canada, it would cost approximately $1.5 billion a year — slightly less than Canadian governments are currently spending to support Canada's richest seniors.[20]

As with many government decisions, budgets are all about policy choices: in the case of pension income splitting, the political choice is to support rich senior families instead of lifting all seniors out of poverty — even though they both cost approximately the same.

Income Splitting for Families with Children

During the 2011 federal election campaign, the Conservative party advocated for a particular version of taxable income splitting that would allow only families with children under 18 years old to income split. It further specified that a maximum of $50,000 could be transferred to a spouse.

The restriction to families with children under 18 is an odd one. If income splitting is a compelling redistributive tool, shouldn't all families have access to it? The restriction to families with children under 18 instead of, for instance, families with pre-school aged children, means the promise of income splitting would tend to be maximized by a traditional family unit, where the mother stays home until children moved away from home (a minority reality for most Canadian families with young children). While income splitting for families with children under 18 does not explicitly require women to stop earning income to maximize the benefit, they remain the most likely to do so because women are disproportionately more likely to earn a lower income than men. Used in this way, tax policy is fiscally rewarding certain types of families over others without addressing commensurate supports needed as family structures change, such as when a women returns to work or gets divorced.

The $50,000 transfer restriction has been marketed as a means to limit this loophole to middle class families. However, all families, including the rich, will have access to the loophole. In fact, the $50,000 transfer restriction only cuts the cost of this loophole by $210 million, or 4%, compared to a loophole with no such restriction. That is to say that it has very little impact on the families that can use it and the value of the tax breaks it affords them.

The cost in 2015 of taxable income splitting for families with children under 18 — including the $50,000 restriction — is much higher than pension income splitting, which was implemented in 2007. The following estimate is over and above the cost of pension income splitting. It also assumes that the provinces go along with the federal loophole, as they did with pension income splitting.

As *Figure 6* shows, the federal cost would be $3 billion a year in 2015. Previous costing of the creation of this loophole has put it at $2.5 billion[21] to $2.9 billion annually,[22] adjusted to 2015 dollars. However, the most recent data available suggests that the costs would have risen by 2015.

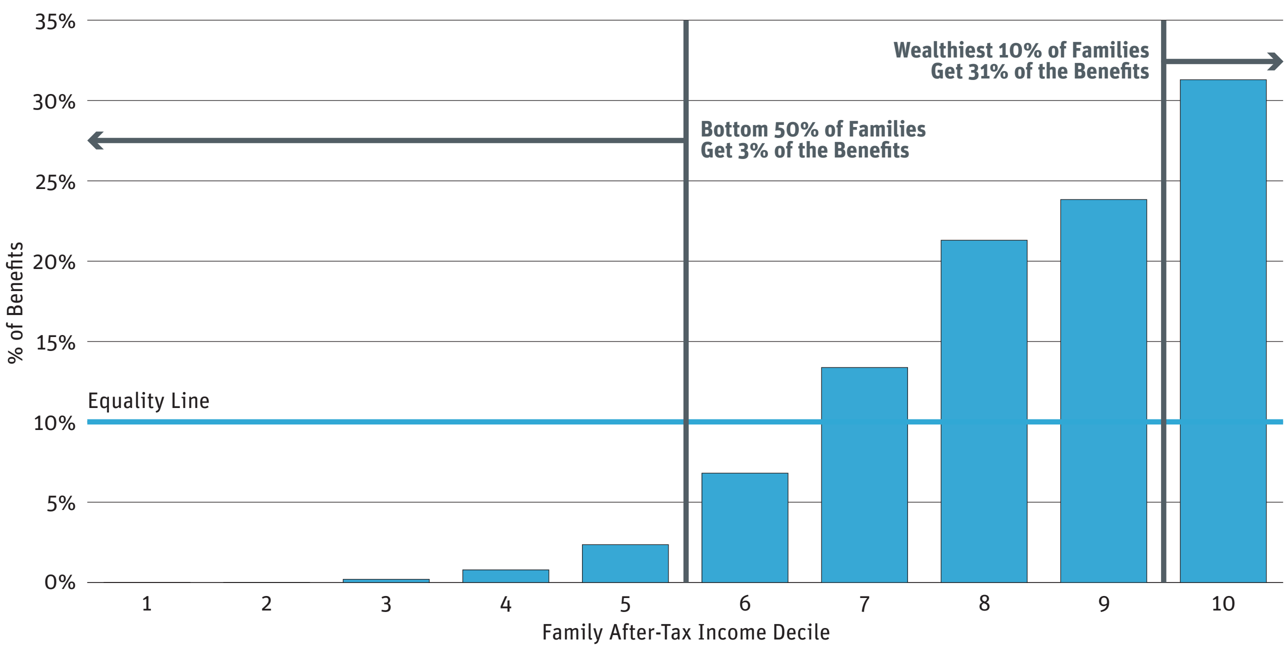
In addition to federal costs, almost $2 billion would be lost by the provinces. The annual cost of this loophole across all Canadian governments

FIGURE 6 Costs of Income Splitting for Families with Children (Max Transfer $50,000)

Level of Government	Price Tag
Federal Cost	$3.0 billion
Provincial Cost	$1.9 billion
Total Government Cost	$4.9 billion

Source SPSDM 21.0 and author's calculations

FIGURE 7 Income Splitting for Families with Children (Distribution All Families)



Source SPSDM 21.0 and author's calculations

would approach $5 billion. Meanwhile, as *Figure 7* shows, the perks overwhelmingly go to families in the upper 40% of Canada's income distribution.

The distribution of this loophole for families is similar to that of pension income splitting benefits for seniors — it is very unequal. The benefits are heavily concentrated among the richest families. The bottom 60% of families (those making $56,000 or less) would receive, on average, $50. Most families in this group would receive no benefit whatsoever. In contrast, the richest 5% of Canadian families — those making over $147,000 — would see

FIGURE 8 Breakdown of Income Splitting Tax Benefit, Canadian Families[23]

Amount of Income Splitting Tax Benefit	Share of Income Splitting Tax Benefit
Nothing	86%
Under $500	4%
Between $500 and $6,500	9%
Over $6,500	1%

Source SPSDM 21.0 and author's calculations

an average benefit of $1,100, with one in 10 of this elite group gaining more than $5,000 from this loophole.

The top 5% of Canada's richest families would gain more benefit than the bottom 60% combined.

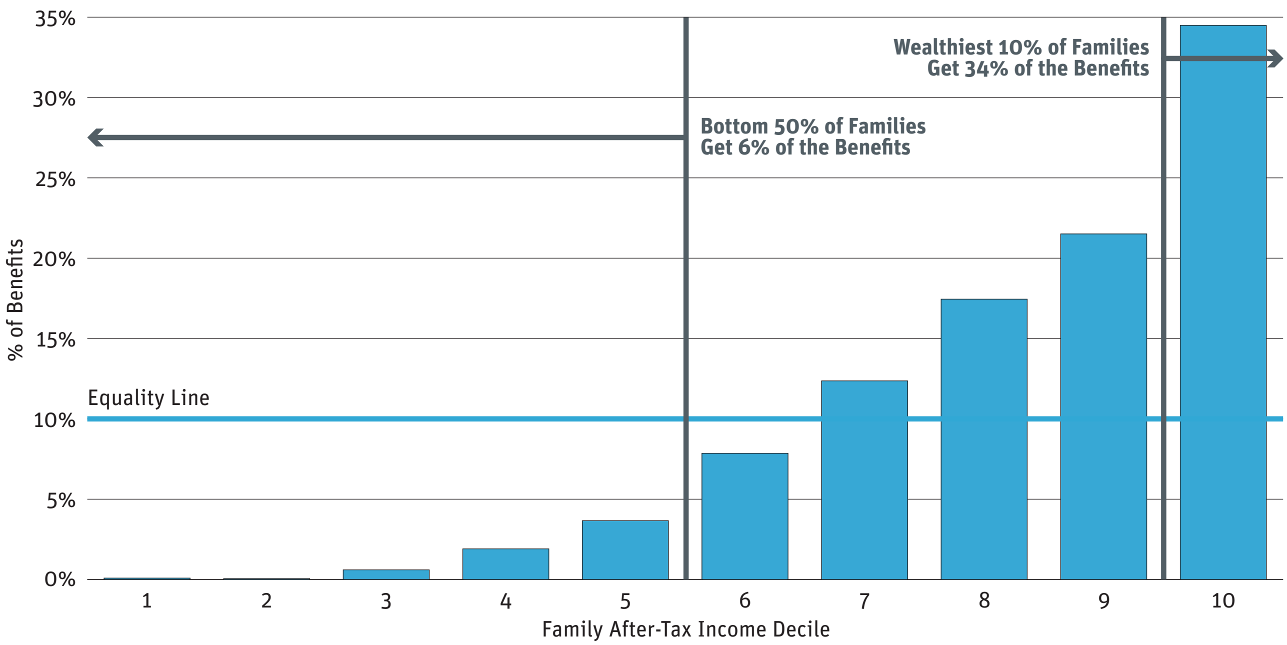
In fact, none of the bottom six deciles receives anywhere near 10%, its equal share; whereas each of the top four deciles receives far more than 10% of the total benefit and, therefore, far more than their equal share.

As *Figure 8* shows, 86% of all families would gain no benefit whatsoever from this tax loophole; 4% of families would gain less than $500; and 1% of all families would get more than $6,500. Most of those lucky $6,500 gainers are already among Canada's richest. Through this loophole, they would improve their already handsome incomes.

The cost in lost revenue for Canadian governments would be substantial — almost $5 billion a year and rising. If Canadian governments are concerned about supporting families with children, a far more equitable way of doing so would be to provide a universal child care program similar to the Quebec model, reducing child care costs from their current $40 to $50-a-day to the $7-a-day range. This would be of particular benefit to lower income families, since it would allow both parents the flexibility to work and thereby contribute to family incomes. Increased female workforce participation in Quebec is one of the prominent effects of high-quality, affordable child care.

As with pension income splitting, there are real consequences by creating a $5 billion a year loophole that sends tax breaks to rich families that don't need them. For the cost of taxable income splitting, universal affordable child care could become a reality in Canada. Child care would have a much more meaningful impact on middle-income families and could help single-parent families work their way out of poverty.

FIGURE 9 Pension & General Income Splitting (Distribution All Families)



Source SPSDM 21.0 and author's calculations

Taxable Income Splitting for All Families + Pension Income Splitting

The third income splitting estimate considers the impact of allowing taxable income splitting for all families, whether they have children or not. It also includes the cost of pension income splitting and the interaction between these programs. This third scenario estimates an upper bound for the cost of income splitting in 2015.

This particular version of income splitting has not been formally proposed at the federal level. However there is a clear income splitting policy creep that began with pension income splitting for senior families in 2007 and spilled over into a consideration of income splitting for families with children in 2011. It is likely that this third scenario would be the next step of income splitting policy.

Compared to the scenarios above, the bottom half of families are slightly less slighted in this third scenario. Instead of the bottom half of all families receiving only 2%–3% of the benefits as above, they would receive 6% of the benefits. However, the top 10% of families do even better under this

FIGURE 10 Costs of Pension and General Income Splitting

Level of Government	Price Tag
Federal Cost	$7.5 billion
Provincial Cost	$4.3 billion
Total Government Cost	$11.8 billion

Source SPSDM 21.0 and author's calculations

third scenario, gaining a whopping 34% of all benefits — the highest of any of the three scenarios.

None of the bottom six deciles gains an even share of 10% of all benefits. Their benefits fall below the equality line. The average benefit for the bottom 60% of Canadian families making $56,000 or less would be just $175, while the richest 5% of families (with family incomes of more than $147,000) would receive an average benefit of $3,100. Of those top 5% of families, one in five would receive a cheque for more than $5,000. The benefits going to the top 5% is more than the total going to the entire bottom 60%.

These lavish benefits are almost completely absent for the bottom half of all families. The bottom half of families — those making under $46,000 — three in 100 would gain $1,000 or more and four in 10,000 families would get more than $5,000. The 10% of Canada's poorest families — those making less than $17,000 a year — receive an average benefit of only $7.

As *Figure 10* shows, full taxable income and pension income splitting would be incredibly expensive. The federal government alone would lose more than $7.5 billion a year in revenue. If the provinces followed suit, they would lose more than $4.3 billion a year in revenue. The loss to governments in total would be almost $12 billion a year in 2015. If implemented, full income splitting would be on par with cutting corporate income tax rates in half or lopping 2% off the GST. It would join the ranks of the most expensive tax changes in decades.

Conclusion

The evidence in this study of income splitting reveals that it creates a tax loophole big enough to drive a Rolls Royce through. In essence, it's a tax gift to Canada's rich.

While income splitting is often touted as a loophole for middle class Canadians, this study illustrates how in reality, it is actually a loophole for Canada's richest families. The richer the family, the more it stands to gain; the poorer the family, the more it stands to lose. Under any income splitting scenario, the bottom six deciles of Canadian families wouldn't even get an equal share of the benefits. Their benefits would have been shifted to the upper third of Canada's richest families, who would receive $3 of every $4 spent on income splitting. At the same time, cutbacks in services would likely be necessary to pay for creating such a large tax loophole. Those service cutbacks are most likely to have the greatest affect on the poorest Canadians.

The creation of further income splitting loopholes comes with a steep price tag. The estimates in this report will likely understate the true cost, since they do not include the impact of behavioural changes due to tax policy shifts. Nonetheless, pension income splitting will cost Canadian governments $1.7 billion in 2015 alone. Taxable income splitting for families with children, including the $50,000 limit, would cost $4.9 billion. Full taxable income splitting for all families combined with pre-existing pension income splitting would cost a whopping $11.8 billion a year.

The creation of these loopholes is so expensive and so inequitable that other programs with laudable social goals — such as lifting all seniors out of poverty or helping working families by implementing universal $7-a-day child care — would provide far greater societal benefits for the buck.

In an era of worsening income inequality, income splitting in all of its guises would only exacerbate the problem. In contrast to external factors that may be driving inequality but that are hard to manage, income splitting represents a purposeful policy choice that would make a bad situation worse. Income splitting is income inequality by design, not by accident.

Appendix 1

Methodology and Assumptions

THE ESTIMATES IN this report, unless otherwise specified, are from "glass box" changes made to Statistics Canada's Social Policy Simulation Database and Model (SPSDM) version 21.0. The assumptions and calculations underlying the simulation results were prepared by the author and the responsibility for the use and interpretation of these data is entirely that of the author.

All estimates, unless otherwise specified, are for 2015 in nominal dollars as calculated by SPSDM 21.0. All estimates are net of all federal and provincial taxes. That is to say, estimates are based on the change in consumable income. They therefore include all increases in commodity tax revenue due to decreased income taxes paid and therefore more disposable income for families.

The taxable income splitting portion of scenarios allows families a Boolean decision to split or not split their family income. This Boolean decision applies for both federal and provincial taxes. If families were allowed a separate choice to split or not to split at the federal and provincial levels, tax losses would likely be higher. This is in contrast to the implementation of pension income splitting which allows families to choose the exact amount to transfer to a spouse so as to optimize taxes paid and GST tax credit received. However, the pension income splitting choice of transfer amounts is maintained for pension income splitting in scenarios where it is calculated.

In all scenarios, it is assumed that the provinces will also allow taxable income splitting and maintain the same definition of taxable income as the federal government. While Quebec does not have the same definition of taxable income, it is assumed that Quebec allows a parallel taxable income splitting based on its own definition. While the provinces did follow the federal government's pension splitting change in 2007, they need not necessary follow it in the future. As such, most totals are broken down by federal and provincial tax losses.

Notes

1 The poverty line in question is the After-Tax Low Income Measure.

2 Finance Canada, 2007 Federal Budget, pg 222.

3 All of the provinces, except Quebec, have the same definition of taxable income as the federal government. As such to deviate from federal government definitions, they would have to set up their own different taxable income definitions. Such a change would certainly increase the complexity of income tax forms. Quebec already has a different definition of taxable income. However, they as well have allowed pension income splitting.

4 Conservative Party of Canada, "Here for Canada: Stephen Harper's Low-Tax Plan for Jobs and Economic Growth", 2011, pg 26.

5 Green Party of Canada, "Vision Green" 2013, Section 4.2 https://www.greenparty.ca/vision-green/p4.2

6 Karen Howlett, "Ontario Conservatives Pledge Income-tax Splitting for Families", The Globe and Mail, May 28th, 2011 http://www.theglobeandmail.com/news/politics/ontario-conservatives-pledge-income-tax-splitting-for-families/article581258/

7 Several previous reports also examined the cost and benefit distribution of income splitting see: Alexandre Laurin, "Income Splitting: A Brief Overview", The Library of Parliament, Parliamentary Information and Research Service, Jan. 2007 (SPSDM 14.1) ; Alexandre Laurin & Jonathan Rhys Kesselman, "Income Splitting for Two-Parent Families: Who Gains, Who Doesn't, and at What Cost?", C.D. Howe Institute, Oct. 2011 (SPSDM 18.1); Matt Krzepkowski and Jack Mintz, "No More Second Second-Class Taxpayers: how income splitting can bring fairness to Canada's single income families," School of Publicy Policy Research Papers, University of Calgary, 6(15) April 2013.

8 This isn't entirely true for Alberta which has a flat income tax system. However, even in Alberta there is an exemption for incomes under $18,000 which could still reduces taxes paid for certain couples under income splitting.

9 The threshold for 2014 is acually $43,953 but figures are rounded here for simplicity.

10 http://www.cra-arc.gc.ca/tx/ndvdls/fq/txrts-eng.html

11 See http://www.cra-arc.gc.ca/tx/ndvdls/fq/txrts-eng.html

12 This simplified example overlooks the basic personal amount of $11,038 (in 2014) and other non-refundable tax credits.

13 The higher earner is almost always a man with the lower earner being almost always a woman. This occurs for three reasons: woman generally make less than men; women are more likely reduce or quit working to raise children; and men are generally older than their spouses and therefore make more due to the age effect.

14 $44,000×15%=$6,600+($34,000×22%)=$6,600+$7,480=$14,080

15 There will be some interaction between pension income splitting and income splitting for families with children for families that receive pension income and have children, however, this is a fairly small group of families.

16 This analysis is based on Statistics Canada's Social Policy Simulation Database and model version 21.0. The assumptions and calculations underlying the simulation results were prepared by David Macdonald. The responsibility for the use and interpretation of these data is entirely that of the author's.

17 Department of Finance Canada, "Tax Expenditures and Evaluations: 2012", 2012, pg.18.

18 In fact, having equal distribution may not even be fair in a broader sense. Most government transfer programs that support seniors provide more support for low-income seniors who need it more. Programs like OAS and GIS taper off so that high-income senior families don't get additional cheques from the government that they don't need.

19 The poverty line in question is the Low Income Measure.

20 See the "Seniors and Retirement Security" chapter of "Alternative Federal Budget 2013: Doing Better Together", Canadian Centre for Policy Alternatives, March 2013.

21 $2.5 billion was the value estimated for 2015–16 by the Conservative party in Conservative Party of Canada, "Here for Canada: Stephen Harper's Low-Tax Plan for Jobs and Economic Growth", 2011, pg.65.

22 This estimate of $2.7 billion in $2012 comes from SPSDM 18.1 independently from Alexandre Laurin & Jonathan Rhys Kesselman, "Income Splitting for Two-Parent Families: Who Gains, Who Doesn't, and at What Cost?", CD Howe Institute, 2011 and Kathleen Lahey, 2013 Op-Ed.

23 Note that this includes both provincial and federal tax reductions due to income splitting.

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