

ent crisis are much deeper and more difficult to untangle. Strident appeals to national unity are not likely to breathe new life into Canada's political and economic system. Far from it. What is happening is that tugging at one thread now causes the rest of the body politic to unravel more quickly. What then is our best hope in the face of a dysfunctional federation?

FINDING THE COMMON GROUND: THE NEED FOR PLAN C

Getting out of the present cul-de-sac requires demolishing old psychological barriers and stereotypes. Canada can no longer afford to live in a world

The 1982 Constitution made provincial rights the keystone of Canadian federalism and this has changed the theory and practice of Canadian federalism at Quebec's expense.

of legal and political fictions. Even if history cannot be undone, a country's institutional arrangements can be made or unmade, revised or overhauled when the old order has to give way to the new. This means finding out how the federation has to be reorganized so that it functions as a country no longer at war with itself. Stock-taking has many elements, but four critical areas of state policy are key:

The 1982 Constitution

The 1982 Constitution made provincial rights the keystone of Canadian federalism and this has changed the theory and practice of Canadian federalism at Quebec's expense.

Should we continue with the 1982 settlement? Or do key provisions that deny Quebec's bi-national status need to be scrapped? Do we want a country in which provincial premiers, never elected on constitutional issues, become the principal gatekeepers of the Constitution?

A New Partnership with Quebec

If Confederation collapses, it will be due to the fact that two national entities cannot live within a set of uni-national political structures. At a minimum, Canadians need to know more about any new kind of partnership before they decide whether a new relationship is feasible and possible. Is there a need for a new social and political union? What does economic partnership entail with respect to the core issues such as NAFTA, debt and deficit, social policy, and citizenship? Political partnership is a second phase. What kinds of political models of partnership are on offer? Which, if any, suit both our needs?

Social Policy

Canada's social programs have long been the cement of modern confederation. Government must provide the people with the means and resources to make decisions about the present and the future. Preserving our social cohesion in a globalized economy is the keystone of society. What new principles, practices, and values will improve the social well-being of the majority? What kinds of policies are needed to enable Canadians and Quebecers to address their growing social deficit?

North American Integration

In 1988, Canada signed the Free Trade Agreement and later joined NAFTA to create

continued on page 52

THE ECONOMIC RATIONALE FOR THE ONTARIO WELFARE REDUCTIONS

BY JACK CARR

The current social assistance system in Ontario involves two programs: General Welfare Assistance (GWA) is for shorter-term cases, such as employable singles and families and those experiencing temporary ill health, and is delivered primarily by municipalities; *Family Benefits Act* (FBA) allowances are paid to specific categories of people such as sole-support parents, persons with disabilities, those permanently unemployed for medical reasons, and the aged.

On October 1, 1995, the Ontario government reduced welfare rates. The FBA rates for all recipients, other than the disabled, permanently unemployed, and aged, were reduced by 21.6 percent. For this welfare reduction to be properly assessed, it must be placed in the appropriate historical context. A single employable individual received \$202 per month in GWA benefits at the end of 1980, and \$663 per month at the end of 1994. On October 1, 1995, the same individual received \$520 per month. Clearly, individuals received more social assistance in October 1995 than they did in 1980. However, this increase in income from social assistance does not mean that individuals are better off in 1995 than they were in 1980; prices of goods and services have increased from 1980 to 1995.

The table below presents social assistance rates in real terms, after adjusting for the effects of a changing price level, and measures all social

assistance rates in terms of June 1995 dollars. The Consumer Price Index is used to arrive at the real rates. For ease of comparison, real social assistance rates for 1981 are set at 100. The number in any year in the table can be interpreted as the level of real social assistance expressed as a percentage of the 1980 level. For example, the index number of 125 for single employable individuals in 1984 means that real social assistance rates in 1984 were 125 percent of their level in 1980. In other words, real social assistance rates increased 25 percent from 1980 to 1984 for single employable individuals.

The table shows the trend in real social assistance rates in Ontario since 1980. For all seven cases, real social assistance rates increased from 1980 to the early 1990s. In 1994, in all seven cases, real welfare rates were anywhere between 46 percent and 69 percent higher than they were in 1980. Real Ontario welfare rates increased *substantially* from 1980 to 1994. Welfare recipients in 1994 were *substantially* better off in 1994 than they were in 1980.

The economic well-being of welfare recipients improved from 1980 to 1994, not only in an absolute but also in a relative sense. Data reported in Statistics Canada *Family Income* (#13-208) show that average Ontario family real income increased 2.5 percent from 1980 to 1993. Although the average Ontario family real

continued on page 52

BUILDING COMMON GROUND: THE POLICY OF CHOICE

from page 51

a continental common market with the United States and Mexico. These agreements are no longer about trade, but about reorganizing state policy on a continental footing. Eight years later, no government has made a major assessment of this fundamental change in economic and social orientation of the Canadian federation. Canadians need a full-scale study of the costs and benefits of trade liberalization. Has trade liberalization worked to Canada's advantage? To Quebec's? What new problems have emerged? How should this conditioning framework be adjusted to address these new realities?

It is only by having full answers to these critical issues that reconfederating Canada will happen. Plan C is the third option — finding common ground that is acceptable to both English Canada and Quebec. Is investing in such a national effort not worth one last try?

In the coming days, all of us will have to choose. If not, complex events inevitably chart their own course. ❖

Daniel Drache is director of the Roberts Centre for Canadian Studies and professor of political economy at York University.

THE ECONOMIC RATIONALE from page 51

income increased slightly from 1980 to the early 1990s, social assistance real income increased substantially during the same period.

The table shows that even after the cuts in social assistance rates in October 1995, real social assistance rates are still significantly higher now than they were in 1980. In the seven cases, real social assistance rates are anywhere between 18 and 43 percent higher in October 1995 than they were in 1980. Considering only the cases of the non-disabled, real social assistance rates are 18 to 29 percent higher in October 1995 than they were in 1980.

*The welfare reductions of
October 1995 have
returned real welfare rates
back to the levels that
existed in the mid-1980s.*

From a historical perspective, real welfare rates are higher in October 1995 than they were in 1980, and are currently at about the same level as they were in the mid- to late-1980s. The welfare reductions of October 1995 have returned real welfare rates back to the levels that existed in the mid-1980s.

ADVERSE INCENTIVE EFFECTS OF INCREASED WELFARE RATES

The table shows that welfare rates increased substantially from 1980 to 1994. Increases in welfare rates can have adverse incentive effects. Consider the case of employable low-income individuals who, because of bad economic times, receive social assistance. Individuals compare incomes from various options. As social

assistance rates increase and, as a result, income from social assistance increases relative to the income that could be earned in the labour market (or, equivalently, if labour market income falls relative to social assistance income), there is an increased incentive for individuals to stay on social assistance and not participate in the labour market. This incentive exists even when economic conditions improve and jobs become more plentiful. High welfare rates relative to labour market income can, thus, result in a "welfare trap."

A significant increase in social assistance rates will lead to a reduction in labour force participation rates and an increase in social assistance cases. When individuals stay out of the labour force and become welfare dependent, this has negative economic consequences for the economy, for the following two reasons.

First, if employable individuals stay out of the labour force and on social assistance, there are fewer people engaged in productive labour market activity and, as a result, total output is reduced. Second, if fewer working individuals have to support more individuals on social assistance, tax rates on working individuals and businesses will increase. Higher tax rates will themselves cause individuals to want to reduce their work effort, and will provide an incentive for business to seek alternative, lower-tax jurisdictions in which to operate.

Firms today are very mobile; with the North American Free Trade Agreement (NAFTA), Ontario firms can locate their plants in the United States or Mexico and still sell their goods duty-free in the Ontario market.

*What is crucial to the
work-versus-welfare
decision is the income level
obtained on welfare
compared to the income
level obtained from work.*

If firms leave Ontario for a lower-tax environment, this will result in lower levels of employment, output, and economic well-being for the average Ontario resident.

In 1981, the total Ontario social assistance caseload was 197,491 (a total of 379,771 beneficiaries). By 1994, the total number of cases was 673,010 and the total number of dependents stood at 1,329,415. This dramatic increase in cases and beneficiaries cannot be explained solely by population growth. From 1981 to 1994, the Ontario population grew by 24 percent, while the total caseload increased by 240 percent and total number of beneficiaries increased by 250 percent. In 1981, total beneficiaries represented 4.3 percent of the Ontario population but, by 1994, they represented 12.1 percent. By 1994, approximately one out of eight Ontario residents was on social assistance.

This increase in social assistance cases cannot be explained solely by the economic recession. The Ontario and Canadian economies were in recession at the beginning of the 1980s. As a consequence, one would expect higher welfare caseloads during these recession years. The Ontario and Canadian economies exhibited substantial growth in the period from December 1982 to March 1990.

In the absence of changes in other factors, the good economic times for most of the 1980s should have led to declines in welfare caseloads during the decade. However, from 1981 to 1989, the total number of beneficiaries of social assistance increased by 52 percent, while the population increased by 15 percent.

The number of employable individuals on GWA increased from 30,896 in 1981 to 227,771 in 1994. From 1981 to 1989, the number of employable individuals on GWA increased by 84 percent, while the Ontario population increased by 15 percent. During the good economic times of the late 1980s, large numbers of employable individuals were on welfare. This occurred in spite of low unemployment rates (in 1989, the Ontario unemployment rate was 5.1 percent).

THE WELFARE TRAP

Why did the number of welfare cases and beneficiaries increase from 1981 to 1989? Why was the increase during this period greatest for employable individuals? I believe a major factor explaining this dramatic increase in welfare cases was the equally dramatic increase in social assistance rates. The table shows that from 1980 to 1988, real welfare rates increased by 43 percent for employable individuals on GWA. (If it takes a year for people to adjust to higher welfare rates, one should look at the eight-year period 1980-88 to explain the growth in welfare cases for the eight-year period 1981-89.)

What is crucial to the work-versus-welfare decision is the income level obtained on welfare compared with the income level obtained from work. Dr. David Brown, in his 1994 C.D. Howe study, showed that from 1982 to 1990-92, the bottom 10 per-

cent (decile 1) of the earnings of Ontario men working full-time, full-year increased by 11 percent. For decile 2, earnings increased 2 percent, and for decile 3, earnings increased 4 percent. For the three deciles (the bottom 30 percent of the earnings distribution), the income from social assistance in Ontario increased relative to the income from labour market earnings between 1982 and 1992.

In addition, for decile 1, welfare benefits were 69 percent of labour market earnings in 1982, and 117 percent of labour market earnings in the period 1990-92. This means that in the period 1990-92, for the lowest decile of earnings, individuals would have 17 percent higher income on welfare than they would by working. This provided a strong economic incentive for individu-

als to opt not to work and to choose social assistance.

A plausible interpretation of the 1980s data is that the deep recession at the beginning of the decade resulted in a major increase in welfare cases for employable individuals. However, as the Ontario economy improved and moved toward full employment, employable individuals on welfare did not re-enter the labour market. Increased real welfare rates in the 1980s and stagnant or decreased labour market incomes provided a powerful incentive for employable individuals to stay on social assistance and *not* re-enter the labour force, in spite of a plentiful supply of jobs. Employable individuals in the 1980s were caught in the "welfare trap."

There have been a number of formal studies in the United

States on the incentive effects of welfare; there are few such studies in Canada. A study by Professor Allen in the *Journal of Economics* (January 1993) examined the effect of the financial incentives provided by welfare on the family structure and on labour force decisions of low-income Canadian women. Professor Allen found that an increase in welfare payments results in a statistically significant increase in women receiving welfare and a statistically significant decrease in labour force participation of low-income women. (It should be noted that Professor Allen obtained similar qualitative results from a sample containing data for both men and women.)

Jack Carr is a professor of economics at the University of Toronto.

SOCIAL ASSISTANCE REAL RATE INDEX, ONTARIO 1980-95 SELECTED CASES, 1980 = 100 (YEAR-END RATES)*

Year	Single employable	Single disabled	Sole support +1 child	Sole support +2 children	Sole support +3 children	Couple +2 children	Couple +2, 1 disabled
	GWA	FBA	FBA	GWA	GWA	GWA	FBA
1980	100	100	100	100	100	100	100
1981 ^a	117	117	116	110	110	109	114
1982	124	405	105	108	107	107	103
1983	118	110	108	102	102	101	105
1984	125	113	111	105	104	103	107
1985	128	115	114	108	108	107	109
1986	139	129	129	122	121	126	119
1987	140	134	129	123	122	127	125
1988	143	136	132	125	124	129	127
1989 ^b	143	136	132	133	135	134	129
1990	158	146	146	149	151	150	142
1991	165	150	151	161	162	154	146
1992	170	153	155	165	167	159	149
1993	169	152	154	167	166	158	148
1994	169	152	153	164	165	154	146
1995 ^c	129	148	118	125	127	118	143

* Assume recipient is renting accommodation (not boarding) with heat included in rent. All children aged 10-15 years.
 a Figures from November 1981 onward include maximum shelter subsidy payable (basic and basic shelter).
 b As of October 1989, all children aged 0-12 years.
 c Rate effective October 1, 1995.