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# Low Income Lines and Financial Security in Retirement

## In Support of the New Veterans Charter Review

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## INTRODUCTION

The New Veterans Charter (NVC) compensates for economic and non-economic losses associated with service-related conditions. Economic loss includes loss of earnings as well as non-wage compensation such as benefits, medical and rehabilitation costs, and non-work losses (e.g., housework, child care). Non-economic loss includes "pain and suffering" and loss of quality of life. Under the NVC, economic loss is compensated for through the Rehabilitation program, Earnings Loss (EL), the Permanent Impairment Allowance and Supplement and the Supplementary Retirement Benefit. Non-economic loss is compensated through the Disability Award.

While economic loss benefits are aimed at replacing earnings, earnings potential and retirement benefits due to service-related conditions, there are two components of the NVC that are concerned with the social adequacy of benefits: the Canadian Forces Income Support (CFIS) program and the minimum EL benefits. Recently the Office of the Veterans Ombudsman (2013) determined that among Veterans deemed Totally and Permanently Incapacitated, more than one-quarter appeared to be at financial risk. This number included Veterans who were not in receipt of benefits that extend beyond age 65, such as Permanent Impairment Allowance, and were not in receipt of Canadian Armed Forces superannuation pension, when their EL benefits end. While financial risk was never defined it is likely related to social adequacy of income or low income and financial security in retirement.

This paper compares Statistics Canada low income lines to benefits in Canada and to the NVC components concerned with social adequacy, examines findings on low income among Veterans and their families, and reviews selected literature on financial security in retirement.

## METHOD

Information on low income lines was derived from the latest Statistics Canada publication entitled “Low Income Lines, 2011-12.” This publication contains descriptions of three low income lines: the Low Income Cutoffs (LICOs), the Low Income Measures (LIMs) and the Market Basket Measure (MBM). LIM and MBM were available up to 2011. LIM and MBM thresholds for a household size of four were adjusted for inflation to 2012 and converted to household sizes of one to three using a formula provided in the Statistics Canada publication. LICO lines for 2012 for household sizes of one to seven or more were provided in the publication. The 2012 adjusted (LIM and MBM) and actual (LICO) low income lines for both before and after tax were then compared to low income benefits provided by the Government of Canada (OAS/GIS); Canadian workers compensation boards (WCBs); provincial/territorial welfare rates and the components of the NVC concerned with social adequacy, namely CFIS and the minimum EL benefit. Selected literature concerning financial well-being in retirement was reviewed.

## RESULTS

### *Statistics Canada Low Income Lines*

Statistics Canada produces three low income lines: the Low Income Cutoffs (LICOs), the Low Income Measures (LIMs) and the Market Basket Measure (MBM). The first two lines were developed by Statistics Canada, and the MBM is based on concepts developed by Human Resources and Skill Development Canada.

LICOs are income thresholds below which families devote a larger share of income than the average family to the necessities of food, shelter and clothing. The MBM defines low income in relation to the cost of a predefined set of goods and services representing a modest, basic standard of living. The price of this "basket" of goods and services accounts for regional differences in the cost of living. Both LICO and MBM lines are based on household income and size as well as community size or region. LIM measures income relative to the median income of Canadians. It is a fixed percentage (50%) of median household income adjusted for household size. While similar to LICO and MBM, LIM is based on household income and size (Table 1 presents lines up to a household size of four but lines for greater household sizes are available) there is no adjustment for community size or region.

Statistics Canada (2013) produces both before- and after-tax total income lines for LICO and LIM (Table 1). After-tax reflects income after the redistributive impact of Canada's tax/transfer system; since the purchase of necessities is made with after-tax dollars, this approach more closely reflects overall economic well-being. MBM is calculated using after-tax income only. LICO lines are lowest in rural areas and highest in areas of 500,000 inhabitants or more. MBM lines also vary by community size from the lowest in areas of Quebec with 30,000 to 99,999 inhabitants to a high in Toronto. LIM lines across household sizes up to four are generally about 10% higher than the highest LICO and about 2% higher than the highest MBM lines.

### *Low Income Among Veterans and Their Families*

LIM was used in the Life After Service Studies as it does not require census geographical information which was not available for the survey and income tax data family information is better suited to calculating LIM (economic family rather than a census family). The 2010 Income Study (MacLean *et al*, 2011) examined low income one year pre release and up to nine years post release using the Statistics Canada Low Income Measure (LIM) and found that 15% of Regular Force Veteran households experienced low income any one year post-release. While NVC clients had slightly higher rates of low income (18%) compared to non-clients (17%), the majority of the Veteran population were not clients and, therefore, most (75%) low income Veterans were not clients of VAC. In addition, the rates of low income among Veterans have been found to be lower than that of the general population. The Survey on Transition to Civilian Life (Thompson *et al*, 2011) found that rates of Veteran households who experienced low income (below LIM) in 2009 were half that of the comparable general population; 4% vs. 9% for those working and 13% vs. 31% for those not working. Findings from the Canadian Community Health Survey 2003 (MacLean *et al*, 2013) also showed low income rates among CAF Veterans released post Korea to 2003 (4.2%) that were almost half that of other Canadians (7.4%).

Veteran families rely on spousal income both pre and post release. MacLean *et al* (2011) found that spousal and other family income increased from 30% of total household income in the year prior to release to 34% in the year following release. Some families were found to be more risk than others. Larger families as well as families of Veterans who served for shorter periods of time or were involuntarily released have been found to be at greatest risk of persistent low income (MacLean, Sweet and Poirier, 2012). Further, rehabilitation clients had almost double the rate of *living in low income post release compared to other Veterans; 27% vs. 15% (MacLean et al*, 2011).

A recent study (MacLean and Pound, 2014) found that 20% of all clients who have participated in the Rehabilitation program have been deemed Totally and Permanently Incapacitated (TPI) and that the numbers being deemed had tripled over the previous two year. Although the same proportion of TPI Veterans and other Veterans experienced low income, TPI Veterans were much more likely to be dissatisfied with their finances. While this designation has been interpreted as meaning the Veteran can no longer work, it really means they have been deemed not able to earn two-thirds of their pre-release salary. In fact examination of LASS 2010 data for this study found that while the majority of TPI Veterans were either not in the labour force or reported being permanently unable to work, 27% were working in the year following release.

Although available from three sources, data is limited on the incomes of CAF Veterans aged 65 or older. The 2010 LASS Income Study included 225 Veterans who were aged 65 and older as of March 2009. In the first three years post release the average income among those aged 65 and older ($83,900) was higher than among those aged 60-64 ($81,700). However, as this cohort was released fairly recently (1998 to 2007), those aged 65 and older in 2009 would have been older at release (aged 55 plus) and likely to have had a full career in the military. Those aged 65 and older in 2009 would not be representative of younger Veterans releasing from the military. Therefore, little is known about the incomes at retirement age of those younger at release. The LASS 2010 Survey on Transition to Civilian Life included only 28 Veterans age 65 or older at the time of the survey. Since the cut-off for analysis is generally 30 cases, this group is too small to analyse. The third source of data on incomes beyond age 65 is the Canadian Community Health Survey 2003. More than 30% of the CAF population were aged 60 and older. The rate of low income among those aged 60 to 84 appears[1] not different from that of other Canadians (MacLean *et al*, 2013). This data, however, is now a decade old and VAC does not have income breakdowns for aged 65 plus.

*Veterans Affairs Canada-NVC Benefits*

The CFIS benefit is a form of income support available to qualified Canadian Armed Forces Veterans, survivors or orphans who are no longer eligible for an Earnings Loss (EL) benefit. The CFIS program uses, in part, the definition of income contained in the *Old Age Security Act* (OAS). As of December, 2012 the CFIS maximum rate for a single Veteran of $16,728 was between the lowest ($12,819) and highest ($19,587) LICO and lower than LIM ($20,289). The maximum rate for a Veterans and spouse of $25,370 was greater than the highest LICO ($23,850) but lower than LIM ($28,693) (Table 1).

Enhancements to the NVC, enacted on October 3, 2011, provided additional monthly support to seriously ill and injured Canadian Armed Forces personnel and Veterans. These enhancements introduced a minimum EL benefit aimed at ensuring a reasonable standard of living for Veterans. The base salary was raised from Senior Private to Basic Corporal; from about $35,000 (75% of $46,932 as of April 2010) to about $40,000 (75% of $53,712 as of April 2010) per year. Currently (April 2013), the minimum EL benefit is $42,426. These rates are taxable and therefore comparable to before-tax low income lines. Assuming the Veteran's income is the sole source of household income the rate of $42,426 exceeds LIM lines for smaller households (one [$16,279] to three [$40,061]) and is lower than LIM for larger household sizes (four [$46,258]).

*Government of Canada Benefits*

The Old Age Security (OAS) pension is a taxable monthly payment available to most people 65 years of age and older who meet the Canadian legal status and residence requirements. Employment history is not a factor in determining eligibility. In other words, OAS is available to those who have never worked, who have worked some, or are still working. The monthly OAS rate, currently $550.99 (December 2013), is the same regardless of marital status. The Guaranteed Income Supplement (GIS) provides a monthly non-taxable benefit to Old Age Security (OAS) recipients who have a low income and are living in Canada. Income tax information is used to establish maximum income thresholds for GIS eligibility. As of December 2013, the maximum benefit of combined OAS/GIS for a single person ($15,577) was more than 20% lower than both LICO and LIM for one-person household. However, the married or common-law couple

[1] Caution needs to be used due to small sample size.

rate ($25,113) was slightly higher than the highest LICO line ($23,850) but lower than LIM for a household of two ($28,693).

*Worker Compensation Boards (WCBs)*

MacLean and Pound (2014) found that WCBs in seven provinces and territories had a minimum earning loss payment. The minimums ranged from about $16,000 in Quebec to about $24,000 in Saskatchewan. Similar to the NVC minimum Earning Loss payment, the WCB minimums do not vary with household size. Assuming injured workers are their household's sole source of income for their households, the highest minimum for WCBs in 2013 exceeded LIM lines for a household size of one but was lower at larger household sizes.

*Welfare or Social Assistance Benefits*

All provinces/territories have assistance programs. These programs are designed to alleviate extreme poverty by providing a monthly payment to people with little or no income. The rules for eligibility and the amounts vary between the provinces. In addition to basic social assistance, there are regularly paid special welfare allowances (e.g., back to school benefits, disability supplements), child benefits (federal and provincial) and tax credits (federal and provincial). Social assistance is not taxable and the rates vary by household size. The National Council of Welfare (2011) previously produced a summary report comparing welfare rates across the country but, due to budget cuts, is no longer producing this report. In its last report, reflecting 2011 welfare rates, the highest rates ranged from $17,326 for a household of one employable person to $36,647 for a couple and two children. These rates were lower than the after-tax LIM and the highest LICO and MBM.

Table 1: Comparison of Low Income Lines and Benefits in Canada

| Source | Measure | | Before Tax | | | | After Tax | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | | | Household Size | | | | Household Size | | | |
| | | | 1 | 2 | 3 | 4 | 1 | 2 | 3 | 4 |
| Statistics Canada (2012) | LICO* | Low | 16,279 | 20,266 | 24,914 | 30,250 | 12,819 | 15,602 | 19,429 | 24,237 |
| | | High | 23,647 | 29,440 | 36,193 | 43,942 | 19,597 | 23,850 | 26,699 | 37,052 |
| | LIM | | 23,129 | 32,709 | 40,061 | 46,258 | 20,289 | 28,693 | 35,141 | 40,577 |
| | MBM** | Low | - | - | - | - | 15,732 | 22,249 | 27,249 | 31,464 |
| | | High | - | - | - | - | 19,501 | 27,579 | 33,777 | 39,003 |
| VAC – NVC£ | CFIS (Dec 2012) | | - | - | - | - | 16,728 | 25,370 | 29,279 | 33,187 |
| | EL (min April 2013) | | 42,426 | 42,426 | 42,426 | 42,426 | - | - | - | - |
| Gov't of Canada€ (Dec. 2013) OAS/GIS | | | - | - | - | - | 15,577 | 25,133 | - | - |
| WCBs ö (2013) | EL (min) | Low | - | - | - | - | 15,787 | 15,787 | 15,787 | 15,787 |
| | | High | - | - | - | - | 23,792 | 23,792 | 23,792 | 23,792 |
| Welfare× (2011) | Low | | - | - | - | - | 6,696 | 14,932 | - | 20,062 |
| | High | | - | - | - | - | 17,326 | 26,502 | - | 36,647 |

* Low: rural area, High: 500,000 inhabitants or more
** Low: Quebec 30,000 – 99,999 inhabitants, High: Toronto
£ NVC Earnings Loss (EL) benefits are taxable. CFIS is non-taxable.
€ GIS is non-taxable.
ö WCB earnings Loss (EL) benefits are non taxable Low: Quebec, High: Saskatchewan, 2013 rates Source: MacLean MB and Pound T. Compensating for Permanent Losses: Totally and Permanently Incapacitated. VAC.
× Social assistance payments are non-taxable, Includes basic welfare allowances, regularly paid special welfare allowances (e.g. back to school benefits, disability supplements), child benefits (federal and provincial) and tax credits (federal and provincial). Source: National Council of Welfare. Household size: 1 – single employable, 2- lone parent, one child and 4 – couple, 2 children Low: household size 1 NB and 2 and 4 Manitoba High: household size 1 & 2 NWT, 4 Yukon. Nunavut excluded as rates were significantly higher than any other province or territory.

## FINANCIAL SECURITY IN RETIREMENT

Financial security in retirement can be measured in both in terms of income continuity and poverty or low income. There are two main measures of income continuity: income replacement and standard of living.

One of the most widely-used indicators of retirement income continuity is the income replacement rate. This rate is obtained by dividing family income (adjusted for family size) at a given age (e.g., age 75) by the income received at the time when the person was most likely earning his or her highest employment wages (typically around age 55) (LaRochelle-Coté, 2012). Two main approaches are used to determine an adequate replacement rate. The first approach and the one most commonly used in the financial planning industry is the "rule of thumb" of a gross replacement rate of 70%. In addition, many defined benefit pension plans provide benefits that, after 35 years of service, are equal to 70% of an individual's financial earnings (MacDonald and Moore, 2011). This approach, however, has limitations. For example, it does not account for accumulated wealth (e.g., a mortgage-free home) or for the decline of some expenses (e.g., work-related expenses) in retirement.

More recently, however, adequacy has been measured in terms of maintaining the same standard of living. The standard of living or consumption approach takes into account taxes, savings and debt as well as changes in expenditures. The target for a consumption replacement rate (post-retirement consumption as a fraction of pre-retirement consumption) would be 100% thereby allowing the same standard of living.

While these approaches often account for household income and size, neither account for low income. Replacement rates in retirement have been found to be 80% overall and 70% for those in the top quintile while those with the lowest income generally have replacement rates in excess of 100% (LaRochelle-Coté, Myles and Picot, 2010).

Low income or poverty among seniors was an import social welfare policy concern in Canada which led to the introduction of the Guaranteed Income Supplement (GIS) in 1967. A recent study (Schirle, 2013) examined the contribution of historical policy changes and seniors' characteristics on senior poverty rates in Canada. Poverty was measured using the elderly relative poverty measure (ERPM) and the LICO. The ERPM is a relative poverty measure similar to the LIM and measures the proportion of seniors with income below 50% of the median income among the working-age population. The study found that retirement income policy, mainly Old Age Security, Guaranteed Income Supplement and Canada and Quebec Pension Plans, is an important determinant of senior poverty rates. In Canada, the expansion of these benefits has been credited with declining senior poverty rates. However, senior characteristics also play a role. While only a small proportion of the reduction in poverty rates between 1977 and 1994 was explained by seniors' characteristics, educational attainment was found to significantly reduce senior poverty rates. Therefore, those with lower education may be at higher risk. The author also noted that while the maximum OAS/GIS benefit available to a married couple was close to the highest LICO for a household of two (in urban areas with population of 500K+) the benefits available to single individuals was much lower than LICO.

## DISCUSSION

The choice of low income line depends on the policy goals. All three income lines discussed above are based on household income and size, but each measures slightly different types of low income: relative low income compared to other Canadians (LIM); large share of income spent on necessities (LICO) or maintaining a modest basic standard of living (MBM). While no one measure is superior, LIM would be less administratively burdensome to use in benefits design as it does not require geographical information while LICO and MBM thresholds vary by community size or region. For this same reason, the LASS Income Study and Survey on Transition to Civilian Life, which both had limited information on the geographic location of Veterans, examined LIM. With respect to levels, in most cases the Statistics Canada low income lines were higher than CFIS, OAS/GIS and provincial/territorial welfare rates. Of the three, LIM lines were slightly higher than LICO and MBM lines.

Statistics Canada low income lines as well as OAS/GIS, welfare and VAC CFIS take into account both family income and size, while minimum EL benefits under the NVC and WCBs do not. Both household income and size are important considerations since

Veteran families rely on spousal income as well, which can be limited by both the characteristics of military life and caring for Veterans with service-related conditions. Further, larger Veteran families have been found to be at greater risk of persistent low income. As low income lines are generally higher than OAS/GIS rates, Veterans age 65 and older with OAS/GIS as a sole source of income may also be at risk of experiencing low income.

There are two main measures of income continuity: income replacement and standard of living. While these measures also account for household income and size, providing benefits based on these measures may not be effective in preventing low incomes. Replacement rates in retirement have been found to be 80% overall and 70% for those in the top quintile while those with the lowest income generally have replacement rates in excess of 100%. Those with lower incomes often experience an increase in income post-age 65 as they become eligible for OAS/GIS. However, this group may still be living below low income lines as OAS/GIS rates, and in particular the rate for a single person, are often lower than low income lines. Therefore, a policy setting for example, a minimum replacement rate of 70% would be more likely to benefit those with higher income levels who tend to have lower post-age 65 replacement rates.

This study found that retirement income policy in Canada has contributed significantly to reducing poverty among seniors. Although little is known about the income situation of Veterans post-age 65, Veterans like other Canadians are eligible for the same retirement benefits as other Canadians. As well employment and related contributions to retirement savings through the Canada Pension Plan and employer plans does reduce the risk of low income in retirement. The question then becomes whether these benefits and the benefits available under the NVC are adequate in relation to standard measures of low income in Canada and whether there are opportunities to improve labour-force participation among injured Veterans.

## CONCLUSION

Of the three low income lines produced by Statistics Canada, LIM lines, which have been used in LASS, are slightly higher than LICO and MBM lines. All three measures account for family income and size. While CFIS also accounts for family income and size, the rates are lower than LIM. OAS/GIS rates and provincial welfare rates were also found to be lower than LIM. The minimum EL amount, which does not account for family income or size, is higher than LIM for smaller families (less than four) and lower for larger families (four or more). Income security in retirement can be measured in both in terms of income continuity and poverty or low income. The two, however, require different policy responses.

Low income rates among Veterans has been found to be half that of the Canadian population and among those deemed TPI their rates of low income were no different from other Veterans. However, little is known about the incomes of Veterans aged 65 and over. The department may want to consider developing clear policy goals for income security in retirement including whether income continuity into retirement is an important goal. In terms of social adequacy of benefits, the department may want to consider examining the adequacy of CFIS rates, whether EL minimums should take into account family income and size and opportunities to reduce the risk of low income in retirement through efforts to improve labour-force participation among injured Veterans.

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