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Understanding Income Inequality in Canada, 1980–2014

Stephanie Procyk

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Executive Summary

This review outlines the main changes leading to the growth of income inequality between households and individuals in Canada since the early 1980s, and in Toronto in particular. The purpose is to answer two questions: (1) Why has income inequality grown in Canada? (2) What policies and programs have traditionally been used to prevent or reduce further growth in income inequality and why are they no longer having this effect?

The review considers four forms of income inequality:

- **Employment-related inequality**: inequality of wages only or earnings inequality (wages, salaries, and self-employment income).
- **Market income inequality**: inequality of employment-related income, plus investment income, and private pension income.
- **Before-tax (but after transfer) income inequality**: inequality of market income plus government transfers (Employment Insurance benefits, social assistance, workers' compensation, GST/ HST tax credit, child tax benefits, and public pensions), also referred to as *total income inequality*.
- **After-tax income inequality**: inequality of all forms of income, plus transfers and minus taxes, also referred to as *disposable income inequality*.

Income inequality in all its forms has grown partly because of globalization and changing technology, which have led to a restructuring of the Canadian economy that has had profound effects on the labour market. It has also partly grown because of widespread economic trends, including recessions.

In the past, Canadian institutions and government policies limited the growth of income inequality. Policies such as minimum wages, the job protection afforded by unions, and the stable employment and good wages available in manufacturing work also limited the growth of income inequality. Today, minimum wages have not kept pace with inflation, unions have declined in importance, and well-paid manufacturing jobs have largely declined. The jobs that have been increasing in prevalence are often low-paid service jobs, or short-term, contract, and temporary jobs that do not offer a secure position in the labour market, as well as managerial and other high-wage jobs that have seen pay rise at much faster rates than other occupations.

At the same time, measures that once compensated for the growth of income inequality, such as progressive taxes and redistributive transfers, have been restructured so that they now compensate less for this growth. Programs such as Employment Insurance benefits and social assistance have been weakened in the extent to which they protect middle- and low-income workers.

The rising cost of living and increased accumulation of wealth in the form of real estate and other assets for those with high incomes have further widened the gap between those with high (and rising) incomes and those with stagnating or declining middle-level or low incomes.

This review shows the many factors that contribute in different ways to growing income inequality. Canadians face a new political and economic reality, different from the one that existed in the 1960s and 1970s. In the future, Canada will need to address income inequality with both "tried and true" methods that are proven to be effective as well as new and innovative solutions that reflect this changing economic environment.

Author

Stephanie Procyk joined United Way Toronto in December of 2011 as Manager of Research, Public Policy and Evaluation. There she has focused on how precarious employment is impacting our wellbeing and how access to opportunity in Toronto is being impacted by income inequality. She previously worked in social policy consulting with Open Policy Ontario, on issues ranging from income security to youth in care. She has also worked as a mental health case worker and union organizer in Chicago. She completed her BA at McGill University and her Master of Public Policy at the University of Michigan Ford School of Public Policy.

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Note on Building Opportunity

This paper is one in a series of papers that are part of the *Building Opportunity* initiative at the United Way Toronto. *Building Opportunity* is a United Way Toronto initiative that seeks to build understanding, foster dialogue, and consider action on the issue of growing income inequality and its impact on equitable access to opportunity in our city. By both creating new research and leveraging the research of our partners, *Building Opportunity* seeks to create a common understanding of income inequality in Toronto. This knowledge will be used to generate a city-wide conversation about why income inequality matters to Torontonians and how we can all work together to mitigate its impacts.

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1. Introduction

Income inequality in Canada declined between the Second World War and the mid 1970s (Yalnizyan, 2010). However, this situation began to change during the 1980s, as market income inequality began to grow, while after-tax income inequality did not. In the 1990s, both market and after-tax income inequality grew. This trend of growing inequality continues today.

The term “income inequality” has only recently become part of the public discourse, inviting many conversations about the source and solutions to its growth. Oftentimes, these conversations have centred on individuals, and have not captured the breadth of systemic changes that have impacted the growth of income inequality in Canada.

This review outlines these systemic changes and illustrates the main contributing factors that have impacted growth in income inequality between households and individuals in Canada, particularly in Toronto, since the early 1980s. This review is intended to answer two questions: (1) Why has income inequality grown in Canada? (2) What policies and programs have traditionally been used to prevent or reduce growth in income inequality and why are they no longer having this effect?

This review explains the role of the following factors: the global environment, macroeconomic and institutional changes, the labour market and employment opportunities, and the demographic composition of the labour force. These factors have impacted growth by limiting the growth of income inequality; compensated for the growth of income inequality after it occurs; or actually contributed to the growth of income inequality. This review also looks at other factors that have indirectly aggravated the growth of income inequality.

This paper is important for two reasons. First, it clarifies how systemic issues have contributed to income inequality and demonstrates that present levels of income inequality are not inevitable: we have tools at our disposal that have limited and compensated for the growth of income inequality in the past. Second, it illustrates how these changes work in concert with one another: this means that modifications in one area will not on their own reverse the wider imbalances in income distribution. We can use this knowledge to address those areas that have enabled income inequality to grow.

1.1 What is income inequality?

Income inequality is the extent to which income is distributed unevenly in a country or region. Inequality exists when one group receives income that is disproportionate to the group's size. In other words, income inequality is a snapshot at any given time of "who gets how much compared to other people." This review looks at the factors that led to change in this snapshot over time.

1.2 How is income inequality measured?

The term "income inequality" is used as a catch-all term to describe several different measures of income distribution. Income inequality further breaks down into the following categories:

- **Employment-related inequality**: inequality of wages only or earnings inequality (inequality of wages, plus salaries and self-employment income).
- **Market income inequality**: inequality of employment-related income, plus investment income, and private pension income.
- **Before-tax (but after transfer) income inequality**: inequality of market income plus government transfers (Employment Insurance benefits, social assistance, workers' compensation, GST/ HST tax credit, child tax benefits, and public pensions), also referred to as *total income inequality*.
- **After-tax income inequality**: inequality of all forms of income, plus transfers and minus taxes, also referred to as *disposable income inequality*.

Each measure shows us a different facet of the full picture of income inequality. Measures of wage inequality and earnings inequality tell us whether changes in income inequality are coming from the labour market. Market inequality measures tell us whether changes in income inequality are being generated from the economy as a whole. After-tax measures tell us whether our policy system is keeping pace with the income inequality that has been generated from the economy.

1.3 Method

This review was developed using information from research institutes, universities, the media, governments, and think tanks. More than 450 articles were used to prepare this review, and every effort was made to include information from a range of perspectives and political affiliations. The extensive literature covering the rise of income inequality in the United States is largely excluded to ensure that the structural changes particular to Canada are highlighted and not conflated with those of the United States.

2. The Role of a New Global Environment

2.1 Economic globalization

The term *economic globalization* describes the process that has rapidly linked economic activities on a global scale, across countries. The linking of economic activities is not a new phenomenon: money and goods have flowed between countries for hundreds of years (CBC, 2006). What is new is the speed and ease with which this business between countries occurs. These elements are collectively referred to as globalization.

The Canadian government's response to globalization in the form of policy changes has intensified globalization's impact on Canada.[1] Beginning in the late 1980s, the federal government made several policy changes that liberalized trade (Ens, 2009). Generally, trade liberalization means that a government reduces taxes on imports and exports and reduces other barriers to allow trade to happen more easily (Less, 2005). In Canada, the federal government signed 10 free-trade agreements, including the influential 1988 Free Trade Agreement with the United States and the 1994 North American Free Trade Agreement (NAFTA),[2] and 24 Foreign Investment Promotion and Protection Agreements (FIPAs) with other countries to protect and promote foreign investment (Foreign Affairs, Trade and Development Canada, 2013a). The purpose of these agreements was to increase the trade and investment that occurred between Canada and other countries, with the intent of expanding the economy.

Technological change also helped business across countries occur more quickly and easily. New computer, communications, and transportation technologies allowed international transactions such as trade and the movement of goods and services to happen faster, more easily, and more cheaply than ever before (International Monetary Fund, 2008; Stanford, 2008). In addition, these technological improvements enabled the fragmentation of value-chains (International Monetary Fund, 2011), meaning that product inputs could be made in one country and completed in another (Hart, 2012).

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1 Although there are many reasons that globalization occurred, we have highlighted the reasons that had the largest impact on income inequality.

2 Ten free trade agreements are in force, 1 has been signed, 2 are concluded; 11 are still being negotiated; and 3 are in the exploratory stage as of time of publication (Foreign Affairs, Trade and Development Canada, 2013b).

Policy changes and technological changes contributed to the growth of income inequality by enabling companies to move goods and service production to countries where wages are lower, a process called "offshoring."[3] Offshoring can have two effects: a decline in employment in the goods and service production sectors in Canada and a decrease in wages for Canadians who are still working in the goods and services production sectors in Canada who must now compete with workers who are paid less in other countries.[4] In Canada, most offshoring has shifted production of goods and services to the United States, with a rising shift to developing countries in the 2000s (Baldwin and Gu, 2008).

The decline in goods and services production jobs such as manufacturing is significant, because these jobs once played an important role in limiting the growth of earnings inequality in Canada (Bolton and Breau, 2012). Manufacturing jobs used to have high wages and full-time hours. These jobs are disappearing in Canada (Bartlett and Tapp, 2012), and in Toronto (Hodgson and Arcand, 2011), and high-paying unionized manufacturing jobs were lost at twice the rate of non-unionized jobs between 1998 and 2008 (Bernard, 2009). These lost jobs are being replaced with service-sector jobs which are often lower paying and more precarious (short-term, contract, part-time) (Noack and Vosko, 2011).[5]

2.2 Technological advances

Technology has profoundly changed the nature of jobs. Many jobs now require extensive technical knowledge, although these qualifications may not lead to higher wages. For instance, an auto mechanic must now understand computers to diagnose and solve problems. This shift to higher skill requirements for work is called *skill-biased technological change*.

Skill-biased technological change is widely cited as a major contributor to the growth in income inequality. The evidence for this theory, however, is not so straightforward.

First, the role of technological change in increasing income inequality is difficult to disentangle from that of globalization (Breau, 2007; OECD, 2011a). These factors have not only decreased the number of jobs available for Canadian workers in manufacturing, but also increased the number of jobs available for more highly skilled workers. In this sense, both globalization and technological change have affected income inequality in Canada, but the extent and source of the impact is difficult to determine.

Second, the people with the highest skill levels are not the people experiencing rises in their income. The majority of the change in the income distribution has occurred in the top decile, which experienced marked growth in income over the past three decades (Heisz, 2007; Saez and Veall, 2003). If skill-biased technological change were a strong contributor to income inequality, most people working in highly skilled jobs would have experienced growth in their in-

3 Offshoring refers to moving production to another country, while outsourcing refers to moving production outside the firm (Baldwin and Gu, 2008).

4 These effects have occurred throughout the world.

5 For example, 85 percent of job losses during the 2008 recession were in the goods-producing sector, while almost 75 percent of jobs created after the recession are in the services-producing sector (Bartlett and Tapp, 2012).

comes. This would have resulted in income growth in the top *half* of the distribution, not just the top decile (Saez and Veall, 2003).

Third, if skill-biased technological change were a major contributor to the growth of income inequality, those individuals with postsecondary education—many of whom have higher skills—would experience growth in their incomes over time, not just those in the top decile. However, the average person graduating from postsecondary education today will extract the same economic gain from the investment in their education as a person in the 1980s (Gordon, 2010; Morissette, Ostrovsky, Picot, 2004; Burbidge, Magee, and Robb, 2002 in Howitt, 2007).[6] In other words, the value of a university education has stayed the same over the past three decades.

Finally, it is not clear whether hard skills such as computer knowledge or soft skills such as adaptability are contributing to income inequality (Howitt, 2007). Furthermore, some have argued that one's survival in the workforce does not depend on high skill level, but on the ability to do work that cannot be replaced with technology, such as being a barber or waitress.

In sum, elements of skill-biased technological change seem to be having some impact on income inequality; however, the evidence for Canada suggests that it is not a strong contributor to the growth of income inequality (Green and Townsend, 2013), and cannot be isolated from the impacts of globalization.

6 For more information on how returns to education differ for different demographic groups and locations see Bourbeau, E., Lefebvre, P. And Merrigan, P. (2010). Returns to Education for 21 to 35 year olds across Canada: Results from the 1991–2006 Canadian Analytic Censuses Files, Statistics Canada.

3. The Role of Macroeconomic and Institutional Changes

3.1 Macroeconomic changes

Macroeconomic changes are changes that affect the entire Canadian economy, such as recessions and economic growth. (Other key changes that affect the economy, such as employment and interest rates, will be addressed in later sections.) Recessions are generally characterized by a slowdown of economic growth and increased job loss. As the country recovers from a recession, the economy generally grows and employment rates increase.

In Canada, the growth and retraction of rates of income inequality has historically followed the business cycle. In the 1960s and 1970s, income inequality grew during recessions and subsided during periods of economic growth (Beach, Finnie, Gray, 2006; Brzozowski et al., 2010).[7] During the recession of 1981–82, income inequality grew, but the slower economic growth that followed in the 1980s was no longer effective on its own to reduce income inequality to pre-recession levels. However, the tax and transfer system was able to compensate for the growth (Brzozowski et al., 2010; Rashid, 1998). This means that market income inequality grew during this period, but after-tax income inequality did not.

The recession of 1990–92 again led to growth in income inequality, but neither subsequent economic growth nor the tax and transfer system could fully compensate for this growth in the 1990s (Brzozowski et al., 2010; Green and Milligan, 2007; Rashid, 1998). Several reasons could account for this outcome. First, the economy grew at a slower pace in the 1980s and 1990s than it had in the 1960s and 1970s. Second, the economy grew in the context of globalization and technological change (Beach, Finnie, and Gray, 2006). Globalization and technological change led to the reorganization of companies, and a web of changes that impacted the type and quality of jobs available (Beach, Finnie, and Gray, 2006). Third, the amount of money redistributed by the government through the tax and transfer system was reduced in the 1990s (Green and Milligan, 2007). Fourth, low earners tend to experience more job losses than other groups during recessions, which keep earnings down for this group in recessionary periods.

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7 Recessions are periods in the business cycle in which economic deterioration occurs, including a decrease in incomes, declines in output, and sometimes declines in employment (Cross and Bergevin, 2012).

(Green and Milligan, 2007). Therefore, major factors that *increase* income inequality were magnified, and major factors that *decrease* income inequality eroded.

3.2 Institutional changes

Institutional changes in the Canadian government have affected taxes and transfers. Government transfer payments to persons are financial support given from the government to individuals through programs and services such as social assistance (Ontario Works and the Ontario Disability Support Programs in Ontario), the Canada Pension Plan (CPP), and the Working Income Tax Benefit (WITB). Health and postsecondary education services financed and subsidized by the government may also be considered as transfers, although some authors refer to them as government spending. The three government transfer programs that have the greatest impact on decreasing income inequality—in order of most to least impact—are social assistance, Employment Insurance, and various child benefit programs (Brzozowski et al., 2010).[8]

Taxes and transfers redistribute income to individuals who would not otherwise have enough income to meet their needs. Depending on economic conditions, different forms of redistribution are more helpful in reducing income inequality. For example, increased income inequality in the 1980s was associated with higher unemployment, so the transfer system—which directly helps the unemployed—was more useful than the tax system in decreasing inequality (Johnson, 1995).

The tax and transfer system is the primary means of compensating for the growth in market income inequality. Before the mid-1990s, the Canadian tax and transfer system was just as effective as the tax and transfer system of Nordic countries in reducing income inequality. It offset more than 70 percent of the rise in market income inequality during that time; after the mid-1990s, the Canadian tax and transfer system offset only 40 percent of the rise in market income inequality (OECD, 2011a).

The tax and transfer system has since become much less effective in reducing income inequality, except for particular segments of society such as seniors and children (Boadway, 2011). This change is due in part to a shift that occurred during this time in many developed countries, including Canada, to promote economic growth by allowing the free market to regulate itself (Hennessy, 2011; Lewchuk, Clark, and de Wolff, 2011; OECD, 2011a). The shift involved reducing transfers, reducing taxes, and limiting government regulation of the labour market.

The role of taxes in redistributing income and decreasing income inequality weakened over the past three decades as tax rates were cut. Tax rates for most Canadians fell by about 2 percentage points between 1990 and 2005, and the tax rate for the top 1 percent in the income distribution fell by 4 percentage points during this time, while the income of the top 1 percent increased greatly (Lee, 2007).[9] Marginal income tax rates fell for people in the top tax bracket in both Canada and Ontario from the early 1980s to 2010 (OECD, 2011a; Yalnizyan, 2010).[10] In addition, the

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8 Social assistance is under provincial jurisdiction. Employment Insurance is under federal jurisdiction. Child benefits are under both federal and provincial jurisdiction.

9 This change can have a multiplier effect, as provincial governments tax rates are impacted by federal rates.

10 The marginal tax rate is the rate that applies to the last dollar of a person's income. This is important to understand, because Canada has a progressive system of taxation. The OECD (2011) notes that federal marginal in-

number of federal tax brackets fell from 11 to 4 in 1988 (Dahlby & Ferede, 2011), which meant that taxes increased for those at the bottom and decreased for those at the top (Veall, 1999). Between 1980 and 2012, the general corporate tax rate also fell from 36 percent to 15 percent (Stuckey and Yong, 2011), and capital gains taxes were cut by a third between the mid-1990s and today (CBC, 2000).[11] As a result, Canadians now pay $38 billion less in individual income tax and $19 billion less in sales tax, while corporations pay $18 billion less in annual taxes compared with what they paid in 2000 (Hennessy, 2012). Altogether, this represents $75 billion less in government revenues. When tax rates decrease, the amount of money that the government collects and redistributes through transfers and spending also decreases.

Transfers help decrease income inequality by raising the lower end of the income distribution (Jackson, 2007). In the mid-1990s, Ontario cut social assistance by 22 percent and since then, increases to social assistance have not kept pace with the cost of living (Stapleton, 2008). In addition, the federal government made changes to the Employment Insurance program in the early 1990s, resulting in the wage replacement rate falling from 60 percent to 55 percent (Coward, Gellatly, and Moussaly, 2012), and eligibility declining to 46 percent of unemployed Canadians in 2008–2009, compared with 76 percent in 1990–92 (Mendelsohn and Medow, 2010; Stapleton, 2009).

In contrast, transfers through child benefit programs have increased since the 1990s (Brzozowski et al., 2010; Stapleton 2008). The maximum Canada Child Tax Benefit payment grew by 67 percent between 1997 and 2007, taking inflation into account (Battle, 2008), and a Universal Child Care Benefit was introduced in 2006 (Battle, Torjman, and Mendelson, 2006). Ontario introduced a new Ontario Child Tax Benefit in 2007 that currently pays up to $1,310 per child per year (Ontario Ministry of Children and Youth Services, 2014). However, the value of transfers can erode over time if they are not indexed to inflation, decreasing their effectiveness in offsetting income inequality. Social assistance, the Ontario Child Benefit, and the Universal Child Care Benefit are not indexed to inflation (Khanna, Rothman, and Rubin, 2013; Ontario Ministry of Community and Social Services, 2013).

Transfers through government spending on health care and education also play a redistributive role, but affect a greater range of people in the income distribution. Transfers to postsecondary education tend to benefit the top 80 percent of people in the income distribution because the bottom 20 percent are less likely to attend postsecondary schooling (Canada 2020, 2011). Health care spending, however, has an equalizing effect on the entire income distribution, because health care dollars go disproportionately to people who have low incomes (Canada 2020, 2011).

Overall, the ability of the tax and transfer system to redistribute income and decrease income inequality, on both the federal and provincial/territorial levels, began to weaken in the mid-1990s; this trend has continued to the present day (Conference Board, 2011; Hay, 2007; OECD, 2008). This weakening is illustrated by the Centre for the Study of Living Standards, where research has found that taking taxes, transfers, and government spending on health and education into account, government expenditure in 2005 actually benefited people in the middle of the income dis-

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come tax rates fell from 43 percent in 1981 to 29 percent in 2010, while Yalnizyan (2010) notes that the marginal tax rate for the top tax bracket in Ontario fell from over 80 percent in 1948 to 43 percent in 2009.

11 Before 1972, capital gains were not taxed at all (Yalnizyan, 2010). Since then, capital gains taxes have fluctuated between 50 and 75 percent, before settling to their current taxation rate of 50 percent (CBC, 2000).

tribution the most—almost twice as much as people in the bottom quintile of the distribution (Canada 2020, 2011).[12]

12 A household in the bottom quintile received $4,245 in net government expenditure, $6,065 in the second quintile, $7,588 in the middle quintile, $4,707 in the fourth quintile, and -$9,821 in the top quintile.

4. The Role of Labour Markets and Employment Opportunities

The labour market is the place where labour services are exchanged between employers and workers, and where wages, benefits, and conditions of employment are determined (Ontario Ministry of Training, Colleges, and Universities, 2005). These conditions can include whether a worker receives benefits, whether the worker is defined as an employee or self-employed, and whether an individual has access to job protection through a union.

4.1 Wages and earnings

Wages are the compensation received by a worker in exchange for his or her labour, while earnings are wages plus any salaries, benefits, and self-employment income. Wages and earnings have a large impact on income inequality, as wages and earnings for individuals in the bottom and middle of the distribution have remained largely stagnant, while wages and earnings of people in the top decile have grown greatly over the past three decades.

Canada has the fourth-largest incidence of low-paid work in all OECD countries (OECD, 2012).[13] Based on this high incidence of low-paid work, Saunders (2005) writes, “placed in an international perspective, Canada has a relatively low wage economy,” compared to other developed nations. This is notable as there is a correlation between high rates of earnings inequality in an economy and high incidence of low-paid jobs (OECD, 1996).

Wage disparities have also increased between different occupational classes in Canada. This means that there are larger differences in wages paid between different occupations (Walks, 2010, 2013). Between 1990 and 2005, people employed in managerial occupations, the highest-income-earning occupation class, saw rapid increases in their income compared to the Toronto CMA average. At the same time, the average incomes of people in manufacturing, utili-

13 Saunders (2005) cites Nolan and Marx (1999), who found that Canada in the 1980s and 1990s had the second-highest rate, at 21 percent of low-paid workers. These workers were defined as “those full-time, full-year workers earning less than two thirds of a country’s median annual earnings” (p. 5). In addition, the OECD (2012), using the definition “share of workers earning less than two-thirds of median earnings,” found that Canada had an incidence of low pay equal to 23 percent in the year 2000 and 21 percent in 2010. Canada’s place compared to other countries has fallen, not because Canadian rates have improved, but because other countries’ rates have increased.

ties, construction, transportation, services, security, sales, arts, literary, and recreation fell, not only in Toronto but across virtually all large metropolitan areas (Walks 2013). In addition, between 2008 and 2011, full-time employment grew for high-wage workers in most sectors in Canada, and declined for most middle- and low-wage groups in the same sectors (Jacobson, 2012).[14]

Alongside these trends, the highest income Canadians are now more likely than ever to be earning higher wages compared to the average Canadian worker (Yalnizyan, 2010). In 1995, as part of NAFTA, highly skilled workers could more easily obtain temporary work visa permits than they could in the past (Saez and Veall, 2003). As a result of this, highly skilled executives or professionals could more easily migrate to the United States to obtain higher wages. This trend created an upward pressure on professionals' wages in Canada in an effort by employers to retain these professionals, and a surge in income for the top 1 percent of Canadians (Atkinson and Leigh, 2010; Saez and Veall, 2003). In 2012 the gap between the average wage and the median wage was the largest it had been since 1997, which points to growth in the upper end of the wage distribution (Bartlett and Tapp, 2012). [15]

Stock options are increasingly being offered as a form of compensation to employees. Stock options give employees the opportunity to purchase a given number of shares in a company at a given price (Smith and MacLean, 2012). Stock options have become more popular because they can encourage workers to stay with a company as their stock grows, and they are seen as a way to motivate more people to feel invested in the company they work for. Employees are not taxed on their stock options until they sell them, at which point they are generally taxed at a rate of 50 percent (Saez and Veall, 2003; Tedds, Sandler, and Compton, 2012). Top executives appear to benefit more from this trend than other workers (Saez and Veall, 2003), as higher incomes can enable people to purchase more stock.

In sum, changes in compensation practices have resulted in stagnating incomes at the bottom and middle of the distribution and rising incomes at the top, both of which have contributed to increasing income inequality.

Minimum wages are "the lowest wage rate an employer can pay an employee" (Ontario Ministry of Labour, 2012). The minimum wage for Ontario is decided by the provincial government, and just like other wages, it requires annual increases to keep up with the cost of living.[16] In 2011, 32 percent of minimum wage workers in Ontario were under the age of 25, and 19 percent were recent immigrants (Block, 2013). Since those who spend good portions of their careers working at or close to the minimum wage tend to be women, visible minorities, [17] and less edu-

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14 High wages are defined as $1,000/week and over, middle wages $500-$999/week, and low wages less than $500/week.

15 When the average income is higher than the median income, this means that there are a smaller group of people with incomes that are disproportionately higher compared to the full range of people.

16 Increases in the minimum wage can also have a spillover effect, where firms boost the wage rates of individuals earning close to the minimum, in order to retain a certain wage structure.

17 *Racialization* describes the process through which certain groups are designated as different and on that basis subjected to differential and unequal treatment. Some authors use the term 'racialized,' while others use the term 'visible minorities,' which is the term used in most data sources. For purposes of consistency with the literature, we are using both the terms 'visible minorities' and 'racialized' to refer to the same groups of people.

cated individuals (Gunderson, 2005), changes in the minimum wage disproportionately affect women, visible minorities, recent immigrants, less educated individuals, and young people.

Minimum wage increases have helped limit the growth of wage inequality in Canada (see Card and DiNardo, 2002; Card and Krueger, 1995; Gunderson, 2005; Lee, 1999; Lemieux, 2005; Tuelings, 2000). This was evident in the 1980s and 1990s on a national level (Card, Lemieux, Riddell, 2003). However, the minimum wage did not change in Ontario between 1995 and 2003, and there were no increases for cost of living. The minimum wage was increased to $10.25 an hour in Ontario between 2010 and 2014, and $11.00 an hour beginning in June 2014. Although there has traditionally been no system for automatic cost-of-living increases to the minimum wage, beginning in 2014, the minimum wage in Ontario will now be adjusted to the cost of inflation. The periods during which the minimum wage did not increase enough, however, have eroded the equalizing power of the minimum wage.

4.2 Self-employment and precarious work

A self-employed worker is defined as a person who owns his or her own business (Canada Revenue Agency, 2011). If a worker is self-employed, he or she must pay for both the employee and employer contributions to the Canada Pension Plan, Employment Insurance, and workers' compensation. Some workers prefer self-employment, while others choose self-employment as a stopgap measure until they find paid employment. Still other workers believe themselves to be paid employees, while being misclassified as self-employed or independent contractors by their employers (Workers Action Centre, 2010).

Workers in precarious employment are those who work in insecure employment such as short-term, contract, and temporary work (PEPSO, 2013). Some self-employed people could be considered in precarious employment. People in precarious employment are more likely to earn less, compared to people in secure work. A recent study revealed that 40 percent of the workforce in the Greater Toronto and Hamilton Areas are working in some degree of precarious employment (PEPSO, 2013), and that precarious employment has grown by 50 percent in the past 20 years in Canada (Vosko et al., 2009 in PEPSO, 2013). This finding points to the growing trend of replacing permanent jobs with more short-term contracts.

Canada is unique among OECD countries in that "self-employment" is a major contributor to the increase in earnings inequality. Self-employment can explain more than one-quarter of the increase in earnings inequality between 1975 and 2010 in Canada (OECD, 2011a). During this time, self-employment grew from 1.54 million Canadians in 1983 to 2.67 million in 2011 (Statistics Canada, 2012).

Although the OECD suggests that self-employment has contributed to the growth in income inequality (OECD, 2011a), the reasons for this effect are unclear. It may be due to different taxation policies. Another reason may be that the growth of precarious employment has contributed to the growth of income inequality by exerting downward pressure on wages. People in precarious employment are more likely to earn less, compared with people in secure work (PEPSO, 2013).

4.3 Collective bargaining

Job protections are the regulations that support employees and increase their wages where the market economy would not do so on its own. Protections in the form of labour unions and collective bargaining have traditionally played an important role in limiting the growth of income inequality. Conversely, the erosion of these protections has contributed to the growth in income inequality.

Labour unions are organizations of workers formed to improve working conditions and income security for their members. Unions compress wage structures for their members and can boost wages in an entire sector, because managers in non-unionized workplaces will often raise wages in their firm to discourage unionization (Mendelson, 2012) and remain competitive. In Canada, unions have often negotiated pay raises that exceed cost of living increases (Canadian Autoworkers Union, 2008).

Unions have been found to limit the growth of wage and earnings inequality, but this impact is different for men and women. Unionized men tend to work in fields such as manufacturing, which tend to be in the middle of the income distribution.[18] When comparing employed men (unionized and non-unionized), unions create a more equal spread of individuals across the distribution of income. Unionized women tend to work in fields such as the public sector, which tend to be closer to the top of the income distribution. Although unions improve wages for these women, unions also move these unionized women's wages further from non-unionized women's wages. Thus, unions have the effect of *increasing* income inequality among women.

However, when men and women are taken together, de-unionization, or the loss of unions in Canada, contributed to the growth of income inequality in the 1980s, 1990s (Breau, 2007), and 2000s (Canada 2020, 2011; Green et al., 2011).

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18 Unions have traditionally provided better-paying jobs for men with lower levels of education, but not necessarily for women with lower levels of education.

5. The Role of the Demographic Composition of the Labour Force

The type of people who make up the workforce can affect income inequality. It is not the demographic characteristics of the workers in themselves that make a difference, but how these characteristics are treated within the larger economic system. For example, a person does not raise income inequality because he or she is an immigrant, but immigration status can raise income inequality based on how immigrants are treated in the labour market.

5.1 Family composition

Family composition refers to whether the family unit consists of a single person, a couple, a lone parent, or a two-parent household.[19] This is important, because a household composed of two adult employed workers will likely earn more than a household composed of one adult employed worker. In Canada, a rise in the numbers of lone-parent families and unattached individuals (Fortin and Schirle, 2003) has contributed to growth in income inequality (OECD, 2008).

Another element of family composition is *assortative mating*, or the tendency of educated people with higher earnings' potential to partner with one another. This tendency has the reverse effect of the family composition change mentioned above. When two people with higher incomes pair off, the household will be in the high portion of the income distribution, but when two people with lower or middle incomes pair off, the household will be in the bottom or middle of the income distribution. This trend is illustrated in recent work on precarious employment showing that those working in precarious jobs tend to have a partner working in precarious work as well (PEPSO, 2013). In the past three decades, assortative mating has been a small contributor to increased earnings inequality in Canada (Fortin and Schirle, 2003; OECD, 2011b).

5.2 Gender

One of the biggest changes to the labour force in the past 30 years is the increased participation of women. Female labour force participation is important because it can mean a two-earner

19 This definition does not capture the wide variety of Canadian families. However, these are the definitions used in the literature on income inequality.

household instead of a one-earner household. In Canada, female labour force participation has tended to limit the growth of earnings inequality (Breau, 2007; Fortin and Schirle, 2003; OECD, 2011a). One possible reason for this is that women have begun to earn more money relative to men. In 1980, women in both Ontario and Canada earned on average 49 cents to the dollar men earned, and in 2011, this gap had closed to 67 cents for women in Canada and 68 cents for women in Ontario (Statistics Canada, 2014). On the national level, however, racialized[20] women earned only 56 cents to the dollar of non-racialized men in 2006 (Block and Galabuzi, 2011). In addition, women are now more likely to be employed at older ages, which has increased incomes at the middle and top of the distribution (Schirle, 2009).

5.3 Visible minority status

Visible minority status is an important demographic component for a city such as Toronto, which has a high percentage of visible minority individuals. Evidence suggests that racial discrimination has contributed to increased earnings inequality by depressing wages of visible minorities. Bolton and Breau (2012) found that the proportion of people in a Canadian metropolitan area that are visible minorities positively correlates with earnings inequality.

Reasons for this correlation may include the fact that those who are racialized have higher unemployment rates (Block, 2010), are disproportionately represented in low-wage jobs (Gunderson, 2005), and are over-represented in sectors that have experienced losses such as the manufacturing sector (Block, 2010). Bolton and Breau (2012) also found that the effect of visible minority status on income inequality has decreased over time, and hypothesize that increased education levels are the reason behind this decrease.

5.4 Immigration

Immigration to Canada has increased in the past three decades, and many immigrants have settled in Toronto. Half of Toronto's population is estimated to be foreign-born. While Breau (2007) found that immigration did not affect income inequality in Canada on the national level in the 1980s and 1990s, Moore (2003) found the opposite for the same time period in Canadian metropolitan areas. However, this increased income inequality seems to be a short-term phenomenon mostly affecting newcomers. Moore (2003) found that income inequality still grows at the metropolitan level when newcomers are excluded from the analysis, but at a much slower pace.

Immigration can also have another form of impact on income inequality. For example, temporary foreign workers who are filling low-skilled positions may put downward pressure on wages for people at the low end of the income distribution (Worswick, 2013).

20 *Racialization* describes the process through which certain groups are designated as different and on that basis subjected to differential and unequal treatment. Some authors use the term 'racialized,' while others use the term 'visible minorities,' which is the term used in most data sources. For purposes of consistency with the literature, we are using both the terms 'visible minorities' and 'racialized' to refer to the same groups of people.

5.5 Education

The economic gain of attaining a postsecondary education has not changed over the past three decades, in that the additional wages that a person earns for having a university education has remained mostly unchanged since the early 1980s (Morissette, Ostrovsky, and Picot, 2006). However, the additional wages that a person can earn with a high school diploma have declined since the early 1980s, and only recently started to grow again (Green et al., 2011). Male high-school graduates entering the labour market in the mid-1990s received wages 20 percent lower than they would have earned in the early 1980s, a gap that has closed to 10 percent today (Fortin et al., 2012). Thus, despite the more recent narrowing of the wage gap between high school graduates and university graduates, university graduates still earn more than high school graduates, a trend that has contributed to the growth in income inequality (Green et al., 2011).

6. The Role of Aggravating Factors

So far, we have looked at factors that research has shown to have affected incomes in the past three decades. However, a set of aggravating factors *indirectly* impact income inequality by either limiting or enabling movement within the income distribution, otherwise known as economic mobility. These factors are related to how individuals spend or invest the income they receive.

6.1 Rising costs of living

Currently, many households have to pay for more goods and services out of pocket at an increasingly higher cost. Part of the shift away from the use of institutional policies and regulations to more reliance on market driven adjustments in the 1990s had the effect of putting more responsibility and costs onto individuals (Lewchuk, Clarke, and de Wolff, 2011). Goods and services previously available from the government or from employers now must be paid for by individuals. For example, worker pension plan coverage has declined in the past twenty years (Ontario Ministry of Finance, 2010). At the same time, costs for necessities (such as food and shelter) have been rising. In both situations, households with high income can afford to pay for these goods and services, while households in middle and low income may experience downward or stagnant mobility that can reinforce existing income inequality patterns or contribute to their growth. In addition, these middle and low income households may be compelled to go into debt to afford these basic necessities.

For example, the cost of food in Ontario has been rising faster than the cost of living, especially since about 2005, making it harder for some to afford food (Milway et al., 2010). One indicator of this trend is the fact that Canadians are turning to food banks more than ever before (Food Banks Canada, 2012). In Toronto, the cost of rental housing has been exceeding the median income of renters, most notably since 1990 (Tyndorf, 2006). This is due in part to incomes falling during recessions, while rental costs have continued to climb. Home owners have also seen housing costs rise faster than their incomes, but to a lesser degree than renters (Tyndorf, 2006). In addition, the growth in precarious work points to a reduction in the people covered by benefits (PEPSO, 2013), which means that benefits such as prescription drug coverage and pension payments must be covered by the individual. In a survey of workers in the Greater Toronto and Hamilton labour market, fewer than 10 percent of precarious workers had extended health benefits compared to 95 percent of those in secure jobs (PEPSO, 2013).

Another set of costs that individuals now have to bear more often than in the past relate to programs and services that enable people to participate in the labour force or get a better job. These costs have also been rising. For example, as female labour force participation has increased, the demand for child care has risen as well. Only 30 percent of women with a youngest child under six were employed in 1976 compared to almost 70 percent in 2003 (Bushnik, 2006). Although child care funding through the province has increased, regulated child care services in Canada only cover one-fifth of children five years old and under (Childcare Resource and Research Unit, 2013). In 2012 in Ontario, median parent fees ranged from $835 to $1,152 a month (Flanagan, Beach, Varmuza, 2013). The $100 per month per child Universal Child Care Benefit introduced in 2006 does not cover these high costs of child care.

The costs of postsecondary education are also being downloaded to individuals while costs increase. The portion of government revenue used to fund operations in postsecondary education fell from 80 percent in 1976 to 58 percent in 2004, while average tuition fees grew significantly. In 1980, families in the lowest quintile would have needed to pay 17 percent of their after-tax income for tuition, compared to 46 percent in 2004 (Canadian Association of University Teachers, 2006).

In sum, rising costs have put downward pressure on the income of people in the middle and lower end of the income distribution, hampering their economic mobility.

6.2 Changes in Wealth

Another area of spending is the money put aside for savings, investments, and liabilities. Wealth contributes to upward economic mobility, and its effects can aggravate or reinforce income inequality. Wealth, or net worth, is defined as:

- Financial assets, such as pensions, stocks, and savings accounts; plus
- Non-financial assets, such as homes, and vehicles; and minus:
- Liabilities, such as mortgages, credit card debts, and educational loans (Jantti, Sierminska, and Smeeding, 2008).

Wealth helps protect people from income shocks such as loss of employment or illness. Wealth inequality is related to income inequality, but it is distinct. In 1984, the top 10 percent of families and unattached individuals owned 52 percent of the wealth in Canada, while the bottom half of the income distribution owned only 5 percent of the wealth in Canada. By 2005, the top 10 percent of the income distribution owned 58 percent of the wealth (Morissette and Zhang, 2006).

Several factors contributed to the growth in wealth inequality. The first is the aging of the population: as people age, they can accumulate more assets (Morissette and Zhang, 2006) and the number of seniors is rising. Another factor is that interest rates were high before 2000, which allowed families with initial stocks of wealth to benefit from compound growth on their assets, while families who needed to pay off debt had a more difficult time doing so (Osberg, 2008).

Second, registered savings instruments such as RRSPs, stocks outside of RRSPs, and mutual[21] and investment[22] funds are predominantly owned by the top quintile (CMHC, 2009; Kerstetter, 2002). In 1999, the top quintile owned 72 percent of RRSPs and other registered savings instruments, 94 percent of the stocks outside of RRSPs, and 81 percent of the mutual and investment funds outside of RRSPs (Kerstetter, 2002).

Third, the 1990s stock market boom contributed to a rise in wealth inequality, as most stock was owned by people in the top part of the income distribution (Yan, 2000). Similarly, the housing boom contributed to growth in wealth inequality through the 1990s and early 21st century. Homeownership is the most important source of household wealth, representing 33.4 percent of the total assets in Canada (Drummond, 2006). Those with higher incomes have more money to invest, and therefore benefit more from stock market and housing booms.

The role of capital gains in asset accumulation is important to note. Many people believe that capital gains, or asset price movements, have played a large role in increasing income inequality, because people with higher incomes have more money to invest in capital. However, capital gains are not a more important source of income for the wealthiest Canadians today than they were 30 years ago, as other sources of income have grown more than capital gains income (Yalnizyan, 2010). On the other hand, liabilities (debts) may have led to greater wealth inequality because higher interest rates on loans are more challenging for those with lower or middle incomes to repay. In addition, the top 4 quintiles tend to incur debts with lower interest rates such as mortgages, while the bottom quintile tends to incur more debts with higher interest rates such as credit card debt (Meh et al., 2009).

A key liability that has been cited as a potential strong contributor to rising wealth inequality is student debt from postsecondary education loans. Increased debt loads in the 1980s and 1990s likely led to decreases in the real median wealth of these students as they grew older (Finnie, 2000 in Morissette, Zhang, and Drolet, 2002). In 1990–91, the average Canadian tuition and compulsory fees were $2,500 (in 2011 dollars), and rose to an average of $6,500 in 2011, with Ontario experiencing a 244 percent real tuition fee increase (Macdonald and Shaker, 2011). In addition, easier access to credit in the 1980s and 1990s may have led families to go into debt, which decreased their overall wealth (Morissette, Zhang, and Drolet, 2002).

In sum, we see similar patterns in wealth inequality as we do in income inequality: much of the growth is occurring in the top quintile, while the other quintiles have either stagnated or declined.

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21 “A mutual fund is a type of investment fund…Unlike most other types of investment funds, mutual funds are ‘open-ended,’ which means as more people invest, the fund issues new units or shares” (Canadian Securities Administrators, n.d.).

22 “An investment fund is a collection of investments, such as stocks, bonds or other funds” (Canadian Securities Administrators, n.d.).

7. Conclusion

A wide range of factors has impacted rates of income inequality in Canada over the last three decades. Changes that have traditionally limited the growth of income inequality include minimum wages, collective bargaining, and manufacturing work. Changes that have compensated for the growth of income inequality after it occurred include taxes and transfers.

Changes that have contributed to the growth of income inequality fall into two categories. The first is a weakening of the levers that limit or compensate for the growth of income inequality: a reduction in the effectiveness of minimum wages, unions, manufacturing jobs, and, most importantly, taxes and transfers. The second are factors that have directly contributed to the growth of income inequality: economic globalization, technological change, changes in compensation practices, self-employment and precarious work, and changes in the demographic composition of the labour force.. Certain changes have aggravated the income distribution such as rising costs of living and increased wealth inequality.

Together, these systemic changes have contributed to stagnating income for the bottom and middle of the income distribution, and fostered a rise in income for the top of the income distribution. It is important to remember that these factors work together to create income inequality, and each factor has a different magnitude.

The levers once used to limit or compensate for the growth in income inequality have lost their power while those that increase income inequality continue to grow. In addition, other factors are aggravating the current income distribution and impeding economic mobility. We also live in a new political and economic reality, different from that of the 1960s and 1970s, and so we need to address income inequality with both tried-and-true methods that we know are effective *and* a set of new and innovative solutions that reflect our changing economic environment.

8. Glossary

After-tax income inequality: inequality of all forms of income, plus transfers and minus taxes, also referred to as *disposable income inequality*.

Assortative mating: the increased tendency of higher educated people with higher earnings potential to partner with one another.

Before-tax income inequality: inequality of market income plus government transfers (Employment Insurance benefits, social assistance, workers' compensation, GST tax credit, child tax benefits, and public pensions), also referred to as *total income inequality*.

Capital gains: the financial gain resulting from selling capital, such as land, buildings, shares, bonds, and other capital (Canada Revenue Agency, 2013a).

Capital gains tax: a tax levied on the profit from the sale of a property or an investment.

Child tax benefit: a tax-free monthly payment for families with children under 18.

Collective bargaining: a formal process of negotiating wages and other working conditions conducted by a group of workers, most often through a union.

Demographics: statistical data on a population and groups within the population (gender, ethnicity, race/racialization, etc.).

Economic globalization: the process that has rapidly linked economic activities on a global scale, across countries.

Economic mobility: the ability of people to move within the range of income distribution.

Earnings: wages plus any salaries, benefits, and self-employment income.

Employee stock options: a benefit offered to employees that gives them the opportunity to purchase a given number of shares in a company at a specified price.

Employment-related inequality: inequality of wages only or earnings inequality (inequality of wages, plus salaries and self-employment income).**Employment Insurance:** a federal temporary insurance program for eligible unemployed individuals.

Family composition: the structure of a family unit or household (e.g., a single person, a couple, a single parent with one or more children, a two-parent household, etc.).

Fragmentation of value-chains: product inputs made in one country and completed in another country.

Government transfers to persons: financial support from the government to individuals through programs and services.

Goods production sector: industries that create or extract products, including agriculture, forestry, fishing, mining, quarrying, oil and gas; as well as utilities, construction, and manufacturing.

Income Inequality: the extent to which income is distributed unevenly in a country or region; inequality exists when a group receives income that is disproportionate to the group's size.

Indexing: increasing government transfer payments by some measure such as inflation.

Inflation: a general increase in prices and fall in the purchasing value of money.

Interest rate: a percent of money paid by a borrower to a lender as a cost for using the money. In Canada, the Bank of Canada sets interest rates according to inflation, unemployment, and other economic events.

Investment fund: a collection of investments, such as stocks, bonds, or other funds (Canadian Securities Administrators, n.d.).

Labour Market: the place in which labour services are exchanged between employers and workers, and where wages, benefits, and conditions of employment are determined (Ontario Ministry of Training, Colleges, and Universities, 2005). These conditions can include whether a worker receives benefits, whether the worker is defined as an employee or self-employed, and whether an individual has access to job protection through a union.

Labour union: an organization of workers created to improve working conditions and income security for its members.

Macroeconomic changes: changes that affect the entire national economy, such as recessions and overall economic growth.

Marginal income tax rate: the amount of tax paid on an individual's last dollar of income; the highest percentage of taxes paid on income, based on federal or provincial tax brackets.

Market income inequality: employment-related inequality, plus inequality related to investment income, and private pension income.

Minimum wage: the lowest wage rate an employer can pay an employee by law (Ontario Ministry of Labour, 2012).

Mutual fund: a type of investment fund in which investments are pooled and allocated to a variety of investment vehicles.

North American Free Trade Agreement (NAFTA): free trade agreement between Canada, the USA, and Mexico.

Offshoring: moving production from one country to another country.

Ontario Child Tax Benefit: a tax-free monthly payment for certain Ontario families with children under the age of 18.

Ontario Disability Support Program: social assistance system for people with disabilities.

Ontario Works: the name given to the social assistance system in Ontario.

Outsourcing: moving certain tasks outside of one firm and contracting with another firm to provide those tasks.

Partial indexing: increasing government transfer payments by the increase in the cost of living only when inflation reaches a level of 3 percent or more.

Precarious work: insecure employment such as short-term, contract, and temporary work, characterized by a degree of uncertainty, insecurity, and lack of control by the individual over his or her terms of employment.

Public Policy: activities undertaken by the government to address public issues (Johns Hopkins Institute for Public Policy, 2013).

Racialization: the process through which certain groups are designated as different and on that basis subjected to differential and unequal treatment.

Recession: a pause or decline in economic growth that is severe, persistent, and pervasive (Cross and Bergevin, 2012).

Registered Retirement Savings Plan (RRSP): a type of retirement savings that is registered with the Canada Revenue Agency and to which individuals can contribute without being taxed (Canada Revenue Agency, 2013b).

Self-employed worker: a person who owns his or her own business (Canada Revenue Agency, 2011). Such workers must pay for both the employee and employer contributions to the Canada Pension Plan, Employment Insurance, and workers' compensation.

Skills-biased technological change: the shift to higher skill requirements for work.

Universal Child Care Benefit: a federal monthly child care benefit paid per child.

Visible minority: a term traditionally used to describe people not of the majority race in a country. In Canada, *visible minority* is used to describe people who are not white.

Wages: compensation received by a worker in exchange for labour.

Wage inequality: inequality of wages only.

Wealth: financial assets, such as pensions, stocks, and savings accounts; non-financial assets, such as homes, and vehicles; minus liabilities, such as educational loans (Jantti, Sierminska, and Smeeding, 2008).

Working Income Tax Benefit: refundable tax credit for eligible working low-income people.

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