

LOW INCOME MEASUREMENT IN CANADA

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ABSTRACT

There is no one "correct" measure that expresses all the complexities of low income. This presentation describes three measures of low income that are used in Canada: the Low Income Cutoffs (LICOs), the Low Income Measures (LIMs) and the Market Basket Measure (MBM). Each of these measures approaches the topic in a different way and has its own advantages and disadvantages.

RÉSUMÉ

Il n'y a pas de mesure "correcte" qui reflète toute la complexité du faible revenu. Cette présentation décrit trois mesures de faible revenu qui sont utilisées au Canada : les seuils de faible revenu (SFR), les mesures de faible revenu (MFR) et la mesure de la pauvreté fondée sur un panier de consommation. Chacune de ces mesures approche le sujet d'une manière différente et a ses avantages et désavantages propres.

1. BACKGROUND

There is no consensus on the meaning of poverty. Some people would define poverty as the inability to purchase the bare necessities, while others would say that it is the inability to participate fully in the life of one's community. Poverty measurement does not have to be focused on income adequacy: in developing countries the focus is often on caloric intake. Even in developed countries issues such as security and health may enter into definitions of poverty. While these are important issues, the presentation will discuss poverty as a function of income.

There are two major approaches to measuring poverty. The absolute approach involves the specification of a basket of goods and services and the calculation of how much it would cost to purchase that basket. The relative approach looks at income relative to other families.

2. LOW INCOME CUTOFFS (LICOS)

A low income cutoff is an income threshold below which a family is likely to spend significantly more of its income on food, shelter and clothing than the average family. Low income cutoffs and their associated rates have been produced since the 1960s and are probably the most frequently used low income measure in Canada. Statistics Canada has consistently maintained that these are not poverty lines, though some groups do choose to use them as such.

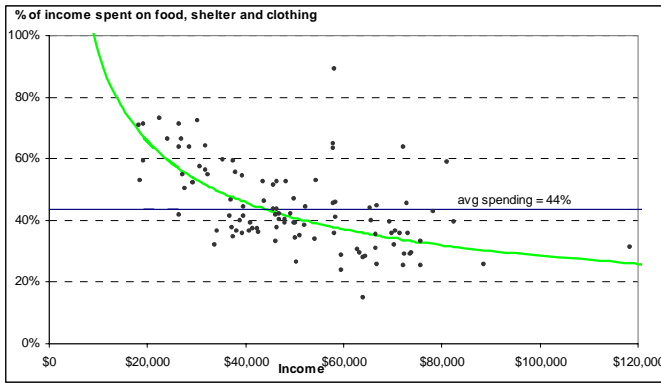
The starting point for producing a set of cutoffs is data from the Family Expenditure Survey - now retooled as the Survey of Household Spending. This survey publishes the amounts that families spend on a wide variety of items. However the items that are of interest for LICOs are food, shelter and clothing because at the heart of the low income cutoffs is how a family's spending on food, shelter and clothing is related to its income.

Families with high incomes tend to spend a smaller proportion of their income on these necessities - they may spend more dollars than families with lower incomes, but they spend less as a percentage, and have more left over for spending on items that are not necessities. To produce the low income cutoffs a regression line is fitted to the relationship between each family's income and its spending on basics. The income at which a family tends to spend 20 percentage points more of its income on food, shelter and clothing than the average family is the low income cutoff. A set of 35 cutoffs is produced for combinations of seven family sizes (from one to seven or more) and five community sizes (from rural areas to cities of over 500,000). It has been the practice to update the cutoffs by applying the annual CPI.

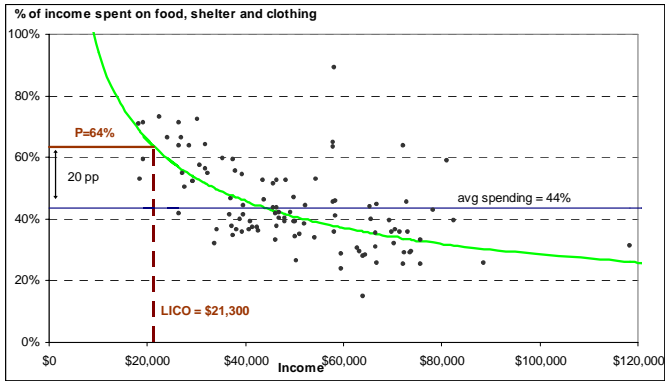
If a family's income is lower than the cutoff that corresponds to the appropriate family size and the size of area of residence, then that family (and all its members) are counted in low income.

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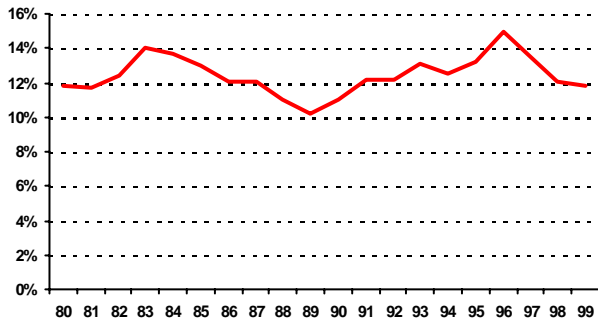
Graph 1
Calculation of a low income cutoff (1)



Graph 2
Calculation of a low income cutoff (2)



Graph 3
Low income prevalence (LICO) – All persons



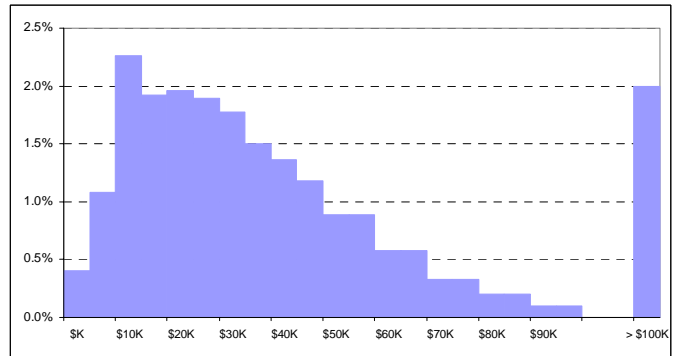
3. LOW INCOME MEASURES (LIMS)

Low Income Measures are defined as 50% of median adjusted family income. LIMS have been produced by Statistics Canada since 1991, and are available back to 1980. While the advocacy groups in Canada tend to use LICOs, the LIMS are more commonly used in international comparisons.

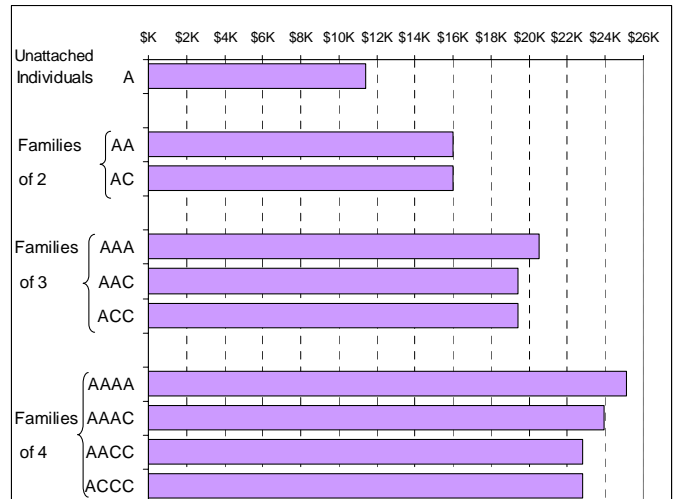
The starting point in the calculation of LIMs is family income. The next step is to adjust income by family size and composition. To take account of the economies of scale, this adjustment is done by using an equivalence scale. The scale used in the LIM production allocates 1.0 to the oldest person in the family, 0.4 to the second oldest person, 0.4 for each additional adult and 0.3 for each additional child. Therefore a family of two adults and two children is assigned a size equivalent to two times (1.0 + 0.4 + 0.3 + 0.3 = 2.0) the size of a family consisting of a single adult.

Each family's income is divided by its adjusted size to produce adjusted family income. The median of this distribution is, of course, the middle income and the LIM for a one person family is set at half the median. LIMs for other family sizes are obtained by converting the one person amount back to other sizes, using the same equivalence scale.

Graph 4
Unadjusted distribution of income for families and unattached individuals

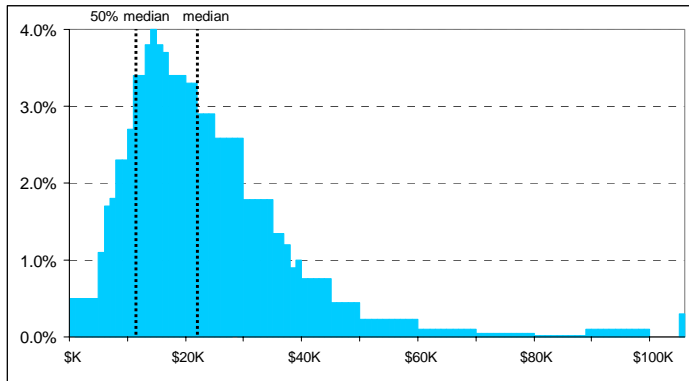


Graph 5 **Distribution of income after adjustment for family size and composition**



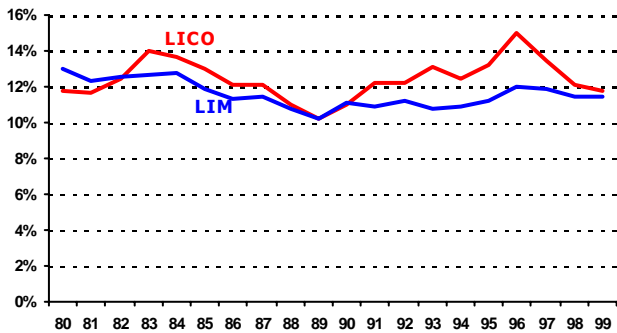
Graph 6

Use equivalence scale to derive LIMs for various family sizes and compositions



Graph 7

**Low income prevalence
LICO and LIM - All persons**



4. MARKET BASKET MEASURE

Canadian Federal, Provincial and Territorial Ministers of Social Services have asked a working group to develop a measure that would provide another perspective on low income and would complement the existing LICO and LIM. Part of the motivation for this request came from the desire to evaluate the effectiveness of various programs, including the National Child Benefit.

Human Resources Development Canada (HRDC) and the working group developed the Market Basket Measure (MBM), a basket of goods and services that would allow a family to eat a nutritious diet, buy clothing for work and social occasions, house themselves in their community, satisfy basic transportation needs for work, school, shopping and participation in community activities and pay for other necessary expenses. HRDC has provided specifications to Statistics Canada so that a cost of the basket may be determined.

- The food portion was provided by Health Canada's Nutritious Food Basket.
- The list of clothing items came from the Social Planning Council of Winnipeg's Acceptable Living Level 2000.
- The cost of the shelter component is the average of median rent for a 2 bedroom unit and median rent for a 3 bedroom unit, including heat, electricity and water.
- In urban areas, the transportation component consists of two annual transit passes, plus 12 round trip taxi rides. In areas not served by public transit, the transportation component is based on the amortized cost of purchasing a used vehicle, plus the annual cost of operating a vehicle.
- Other expenses such as basic telephone service, school supplies, personal care items and modest levels of recreation and entertainment are estimated through a "multiplier" approach.

The basket will be priced for a reference family of two adults and two children and adjusted for other family sizes with the same equivalence scale that is used to produce the LIMs.

The working group proposed a definition of a disposable income that would remove non-discretionary expenses to come as close as possible to the amount of money that a family would actually have to purchase the items described in the basket. Therefore, the following items are subtracted from a family's total income:

- federal, provincial and territorial income tax
- the employee portion of payroll taxes (CPP/QPP and EI contributions)
- non-discretionary payments to Registered Pension Plans (RPP)
- union and professional dues
- child care expenses incurred to enable both parents (or a lone parent) to work
- child and spousal support payments
- out-of-pocket cost of medically-recommended health care expenses.

5. CONCLUSION

There is no one "correct" measure that expresses all the complexities of low income. A more complete examination of low income should take account of factors such as transitions into and out of low income, the characteristics of persons who are persistently below a low income line and the depth of low income.

