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Tax Policy Decisions Risk Locking Ireland into an Unequal Economic Model: *Response to the Irish Tax Institute's Analysis of Higher Income Tax*

Tax on Ireland's Higher Earners Reflects their Higher Pay

The Irish Tax Institute have pointed out that 23 per cent of income tax payers will pay 81 per cent of all income tax in 2014 (*The Irish Times*, 24th September 2014)[1]. What they have neglected to mention is the stark difference in income between the top income tax payers and the rest.

The top 22 per cent of tax units paid 80 per cent of income tax but had average incomes of €91,353, whereas the remaining 78 per cent of tax units (1.6 million singles or couples) had average incomes of €22,154 (Revenue data for 2011)[2].

Even the very highest earners pay no more than 30 per cent in income tax, as shown below, not the top rate of 41%, and similarly they pay far less than 52% even when the top rates of USC and PRSI are included[3]. When these facts about income inequality are considered, it is obvious that those with the highest pay and most disposable income will pay most income tax, but top earners are not excessively taxed.

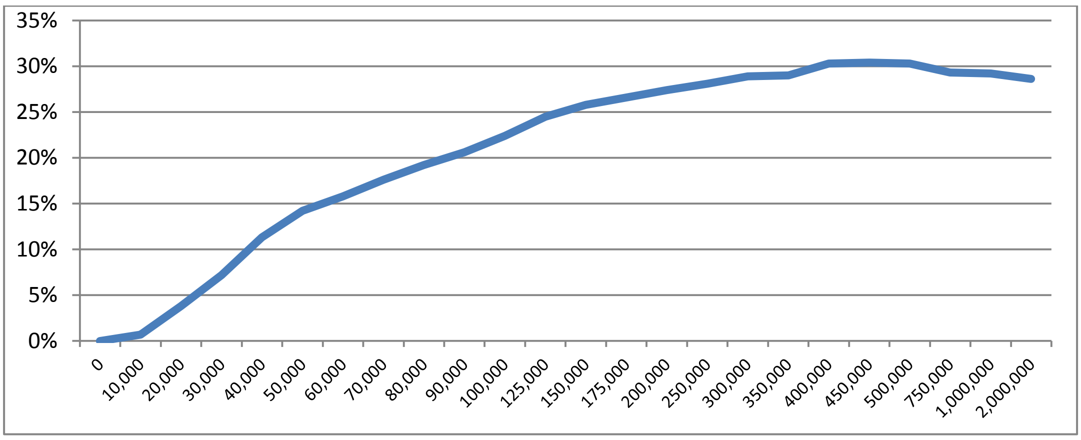


Chart: Actual Income Tax paid by Gross Income (Revenue Data, 2011)[4]

Low Tax as a 'Strategy for Growth'?

More importantly, as reported in *The Irish Independent* (23rd September 2014), the Irish Tax Institute President has claimed that "Ireland's personal taxes are 'out of sync' globally, especially with countries competing with Ireland for foreign direct investment."[5] This response from TASC investigates and analyses this claim.

The Irish Tax Institute (ITI)[6] has published *A Tax Strategy for Growth*[7], which provides one of the few detailed arguments explaining why the Government might consider cutting the higher rate of income tax in Budget 2015. The ITI analysis has a number of weaknesses. Low tax represents a weak basis for Ireland's future economic and social development. Just as importantly, a growth strategy based on tax cuts is flawed from an equality perspective.

The report produce tables[8] comparing Ireland's marginal tax rate at different earnings levels with seven other countries. For minimum wage workers, Ireland charges the least tax and social insurance of their eight sample countries (8th/8); for average wage workers Ireland's tax and PRSI is still low (6th/8), although higher than the USA; for those on €75,000, Ireland's tax is 4th/8; and for those on €150,000, it is 3rd/8.

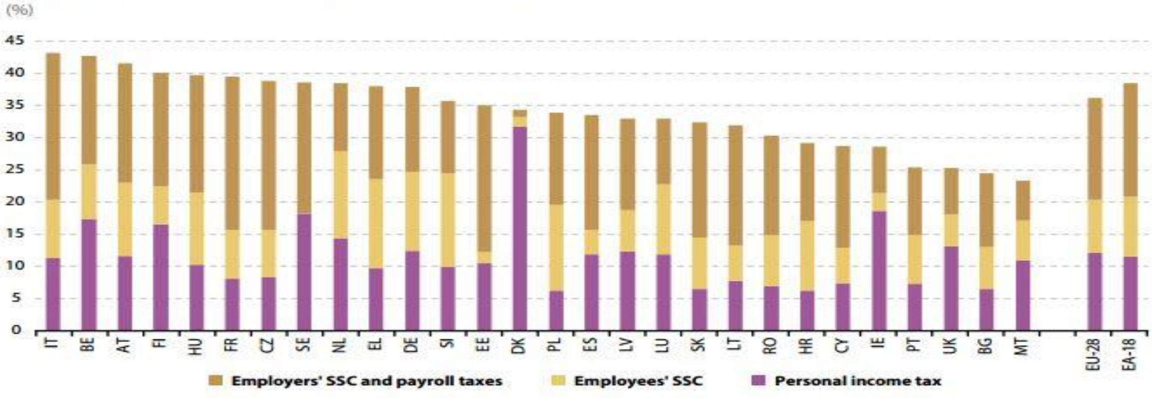
Social Insurance

What the ITI fail to mention is that Ireland's employers' social insurance (PRSI) is second lowest in the EU. In fact, it is essentially the lowest as Denmark largely uses taxation instead of social security. When this fact is included, the suggestion that tax levels in Ireland are similar to Sweden or the Netherlands is immediately shown to be false. When employer's social contributions are included, the implicit tax on labour in those countries is nearly a full third higher than in Ireland.

The EU's statistical service, Eurostat, provide a graph of implicit tax on labour (shown below)[9] . Ireland's top tax rate is at the low end of the chart: Ireland (IE) is between Cyprus (CY) and Portugal (PT). The purple income tax element is relatively high but the mustard-coloured employer social security contribution (SSC) is relatively small and the yellow employee SSC is relatively tiny. In other words, Ireland's low level of social insurance makes the overall implicit tax on labour among the lowest in the European Union. And employers and investors are well aware of this, as it reduces the cost of employing people here.

Graph 13: Composition of the implicit tax rate on labour, 2012

(%)



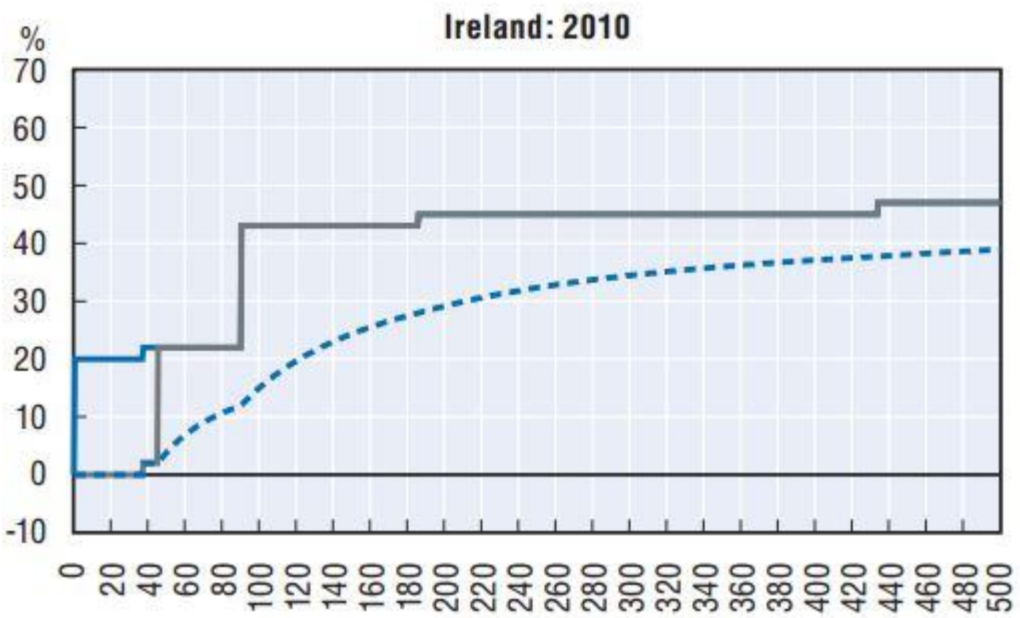
Source: DG Taxation and Customs Union and Eurostat (online data code: gov_a_tax_itr)

In the same publication, Eurostat show that social contributions in Ireland are the second lowest in the EU at just 4.4% of GDP compared to an EU average of 11.1%[10] and also second lowest at 15.3% of total taxation compared to an EU average of 30.9%[11]. Comparable OECD data shows that social security in the USA represents 5.4% of GDP and 22.3% of all taxation[12]. Irish social security contribution levels are therefore not only less than half of EU average levels, but they are significantly lower than social security levels in the USA.

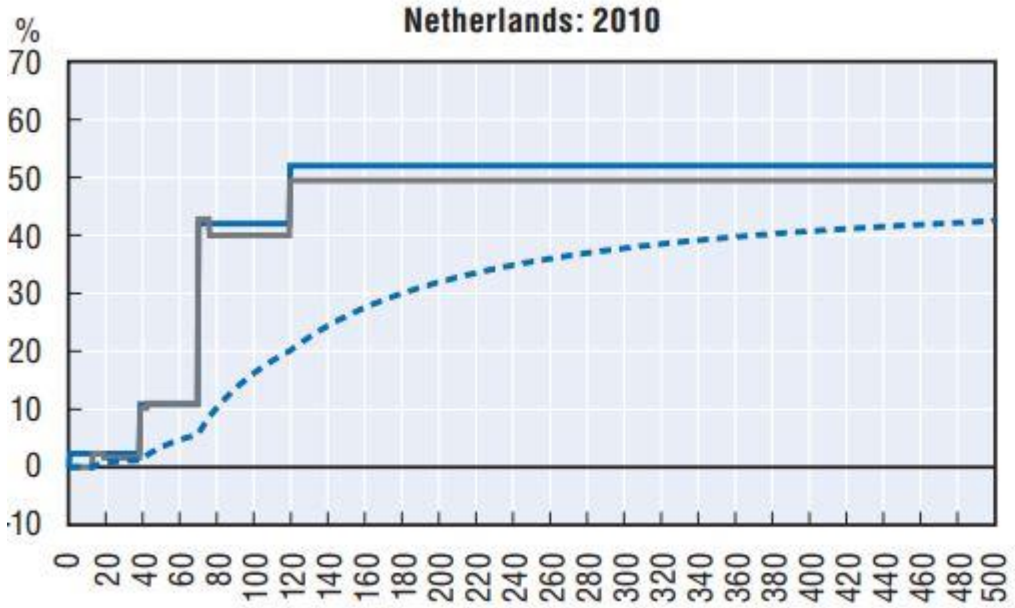
Comparing Income Tax

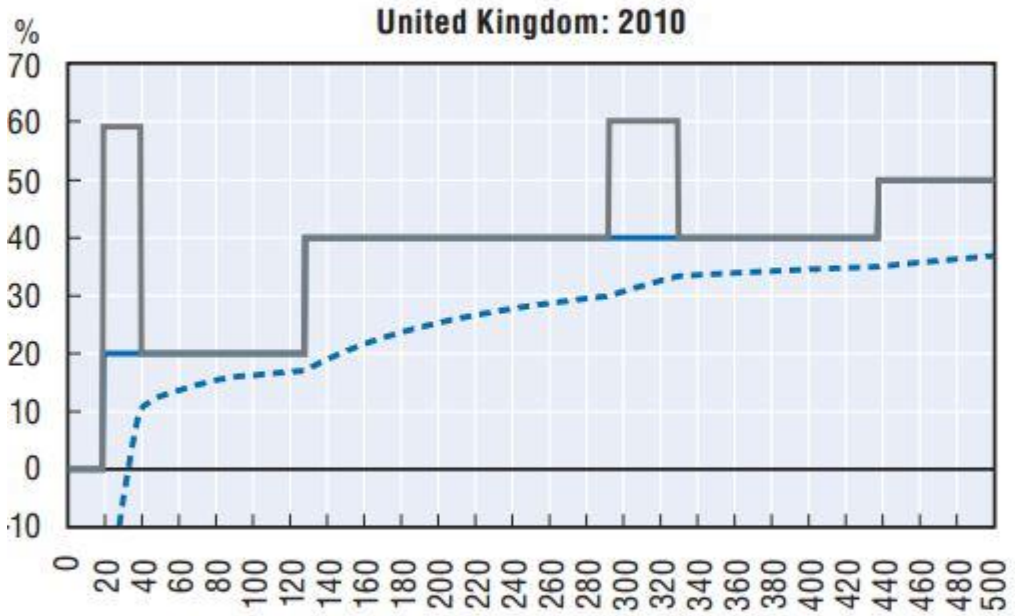
The OECD provides very precise graphs of both marginal and effective rates of income taxation, which are useful for cross-country comparisons[13]. The following graphs compare Ireland with the Netherlands, the USA and the UK (using 2010 data). The dotted line is average tax paid, and the horizontal axis represents multiples of the average wage.

From this comparison, it is clear that Ireland has lower taxes on high incomes than the Netherlands. For example, at 300% of average wages, Irish average tax is around 35% but Dutch tax is closer to 40%. The reason is that Ireland provides a much wider range of tax credits, reliefs and tax breaks, which leads to a lower level of tax paid.



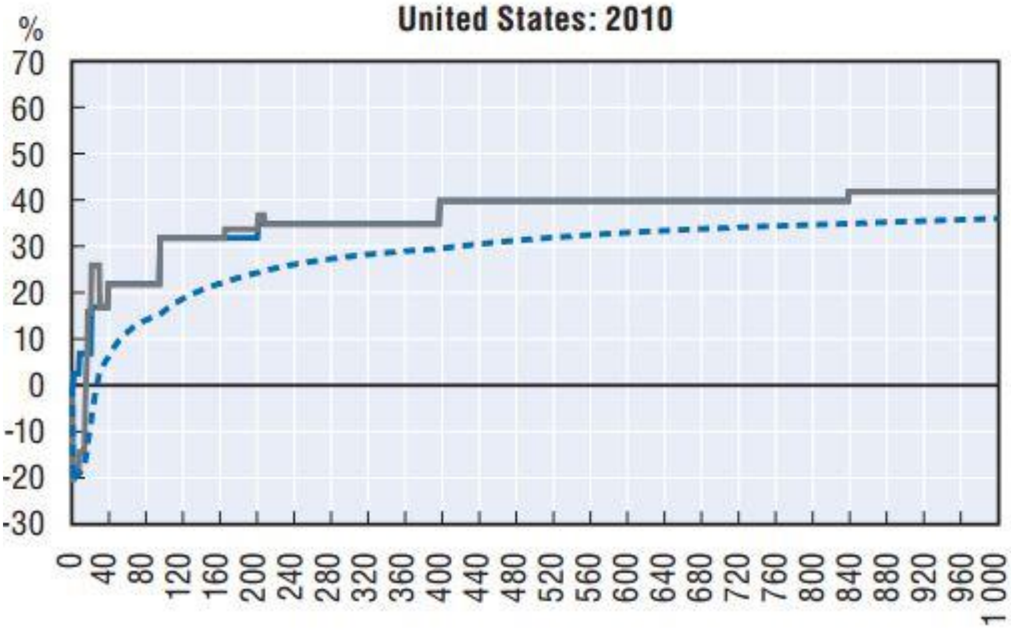
The dotted line is average tax paid, and the horizontal axis represents multiples of the average wage: i.e. 100 = Average Wage, 200 = Double the Average Wage, etc.





The UK has lower tax than Ireland for a single person on three times average wage levels, who pays an average tax rate of 30% there. However, the gap closes for very high earners (on five times average wages, c.€175,000 in Ireland). For these top earners, average tax in the UK is around 38% and tax in Ireland is around 40%. That is because the UK has a third, top rate of tax that only applies to very high incomes (£150,000+).

The USA does have lower average tax levels, as shown below.



Note: different scale horizontal axis

At 300% of average incomes, US personal taxation is under 30% and at five times average wages it is around 32%. Even at 10 times average wages, US tax doesn't reach 40%, although the high level of property tax in the USA, as well as higher local and State taxes, are missing from this comparison.

A "Strategy for Growth" or a "Race to the Bottom"?

Based on the above figures, the real argument underlying the ITI's analysis is not about Ireland taxing nearly as much as Sweden or the Netherlands (despite that claim being made) but it seems to be that Ireland should compete with the UK and USA, based on the assumption that lower tax for high-paid CEOs and other senior executives will lead to more foreign direct investment in Ireland.

The Irish Tax Institute point to the OECD's findings that lowering direct personal and corporation taxation is more growth-friendly than cutting consumption taxes. However, the OECD's argument relies on a supply-side view of the economy, and their models assume higher income companies and individuals will invest more. This is conspicuously not happening in Ireland, despite our already relatively low corporation taxes and income taxes. Ireland has had the lowest investment levels in the EU for several years[14]. Also, multinationals may not necessarily reinvest their profits in Ireland.

On the contrary, raising wages, social transfers and/or cutting consumption taxes will increase spending power across the breadth of society, which will drive consumer growth more effectively than cuts to direct taxation. Likewise, maintaining the tax and social insurance base - including taxes on high earners - will provide the funds necessary to pay for health and education, as well as to permit investment by public bodies on key infrastructure for business, such as roads and broadband internet, as well as direct business supports like Enterprise Ireland.

Similarly, while the UK and USA rank in the World Economic Forum's Global Competitiveness Index Global Top 10[15], so do Finland, Germany, the Netherlands and Sweden, indicating that higher taxes and strong public services can support economic performance.

Moreover, many high income earners in Ireland are not based in global enterprises. These 'domestic' high earners would also benefit from tax cuts, yet are not guaranteed to invest more or create jobs in Ireland as a result.

We must acknowledge that Ireland's tax system and basic welfare state are not the same as the USA. Even the UK is moving to dismantle the pillars of its welfare state, such as the NHS. Does Ireland really want to compete with the USA and UK in a race to the bottom on personal taxes and therefore weak or non-existent health, education and other public services?

Also, the USA and UK are two countries that perform among the worst for economic inequality. Economic inequality not only results in a range of health and social problems[16], but was also a factor that helped bring about the recent global economic crisis.

Ireland already offers lower labour costs, as employers pay far less social insurance in Ireland than in any other EU member of the OECD. This fact is obscured by only examining the tax paid by employees. Employers and investors know this, which makes it more likely that the arguments against higher income tax are being driven by senior executives based on their own self-interest, rather than as employers.

When the false data is stripped away, there is a much more honest argument to be had. Should Ireland embark on a programme of cutting personal taxation in order to compete with the UK and USA for foreign direct investment, or should Ireland maintain its current, relatively low level of tax (or indeed increase tax and social insurance) in order to continue spending on health and education to provide all citizens with a quality of life and opportunities that are provided in other European social democratic countries, but increasingly denied in the unequal liberal economies. See, for example, evidence of higher social mobility in the Nordic countries, Canada and Germany, compared to the UK and USA[17].

Conclusions

TASC's analysis suggests that investment in people through quality public services is a stronger long-term economic strategy than a race to the bottom in competing to lower personal taxation, which will benefit many non-investors on high incomes while further weakening public services and public investment.

This is one of the major strategic choices facing the Government in Budget 2015 and beyond, as they lay out their plans on taxation for the coming years. The same strategic question faces all political parties as they prepare their economic and social policy proposals for the next general election: Should Ireland seek economic growth through an Anglo-American model or through a more equitable North-West European model? Ireland needs a major public debate on this choice.

CONTACT DETAILS

For further information or to arrange a briefing in person or by email or telephone, please contact Nat O'Connor at TASC on **01-6169050, 085-8269093** or by email **noconnor@tasc.ie**

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[2] http://www.revenue.ie/en/about/publications/statistical/2012/income-distribution-statistics.pdf
[3] Rates: 4% PRSI and 7% USC for employees and 4% PRSI and 10% PRSI for the self-employed.
[4] Parliamentary Question Written Response, 51353/13:
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[10] Table 22, p. 195 of *Tax Trends in the European Union*
[11] Table 23, p. 196 of *Tax Trends in the European Union*
[12] http://data.oecd.org/tax/social-security-contributions.htm
[13] See Annex from page 67 in a Special Feature report on tax http://www.oecd.org/tax/tax-policy/50131824.pdf
[14] http://epp.eurostat.ec.europa.eu/portal/page/portal/product_details/dataset?p_product_code=TEC00011
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TASC is an independent progressive think-tank promoting action on social change through evidence-based policy proposals. Our vision is of a flourishing Irish society based on equality, social justice, transparent democracy and sustainable economic activity. TASC is a charitable organisation (CHY 14778).

Second Floor, Castleriver House, 14-15 Parliament Street, Dublin 2, Ireland

www.tasc.ie **contact@tasc.ie** **+353 1 6169050**