Think-tank for Action on Social Change

Independent research challenging inequality and promoting a flourishing society

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Debunking IBEC's Income Tax Myths: *Response to IBEC's Income Tax Analysis*

IBEC have produced a misleading analysis of income tax based on selective and highly contorted use of available data[1]. TASC's immediate response addresses six major points from IBEC's analysis.

(1) *IBEC claim: "Ireland is not a low income tax country, particularly for middle and high earners: Since 2010, income tax as a percentage of national income has risen from 8.7% to 11.6%, well above the EU average of 9.5%. Ireland is now the fifth highest personal income tax jurisdiction in the EU."*

IBEC have claimed Ireland is not a low income tax country but they have ignored the role of social insurance as part of personal taxation and social charges. IBEC are only looking at one part of the tax paid on incomes when examining income tax.

In particular, IBEC's analysis ignores the very low employer's social security contributions in Ireland, which reduces total labour costs considerably. This is an unusual omission, since total taxes and social charges on labour is the standard unit of analysis for employers when calculating the cost of employing people.

Ireland's overall government revenue is three-quarters of the EU average level[2], and the main reason for overall low government revenue in Ireland is due to the very low level of social security contributions paid by employers, and the relatively low level of employee contributions. **Ireland ranks 27th out of 28th in the EU for social security contributions** (effectively last, as Denmark uses other taxes instead of social contributions). Social security contributions in Ireland are 4.4% of GDP, versus an EU average of 11.1%[3].

In addition, because overall Irish tax revenue is significantly lower than the EU average, income tax may provide a larger slice of this smaller pie, but it does not logically follow that Ireland is a high income tax jurisdiction. If Ireland had EU average levels of social insurance, the overall tax take would grow but income tax (excluding PRSI) would diminish as a proportion of all tax. Eurostat provides a comparable indicator of taxes on employees, which is total implicit tax rate on labour[4]. According to Eurostat: "The implicit tax rate on labour should be seen as a summary measure that approximates an average effective tax burden on labour income in the economy."[5] Ireland ranks fifth lowest out of 28 EU countries, in 24th place overall. This undermines IBEC's claim that Ireland is the "fifth highest" income tax jurisdiction.

(2) *IBEC claim: "Over half of all taxpayers would benefit from a cut in the marginal rate: Suggestions that only 17% of income taxpayers pay tax at the marginal rate and that the average tax rate is only 14.1% are factually incorrect. The analysis shows that the majority of taxpayers are paying tax at the marginal rate."*

The claim of 'half' is false and the calculation to reach this figure is highly misleading.

Minister Noonan said "*I am informed by the Revenue Commissioners that they estimate that just over 17% of income earners were liable to Income Tax at the 41% rate in 2013"* [6]. Minister Noonan also said *"Regarding a reduction in the marginal tax rate, it is assumed that the Deputy refers to a reduction in the 41% Income Tax rate. On this basis <u>the Revenue Commissioners estimate that, a reduction of that rate would affect approximately 392,000 (18%) income earners</u>."* [7] That is the source of TASC's initial citation that 'one-in-six' tax payers would benefit from a cut to the higher rate.

IBEC arrive at the figure of 'half' (actually 54%) by some unreasonable contortions of the data. Firstly, they identify that some people are liable to pay a small amount of tax at 41%, but their tax credits are sufficient to take them out of the higher tax net, and Revenue's official statistics do not count them as part of the one-in-six who currently pay some income tax at the higher rate. IBEC estimate that 607,000 people *may* be liable to pay the 41%, although many have sufficient credits not to. The point, which is valid, is that a change to the rate would benefit some of these people, although it may be marginal in some cases – e.g. a single person on €32,801 who pays 41% on just one euro would gain 21 cent if the 41% rate occurred at a higher income but is counted as a '41% payer' in IBEC's calculation.

Even if one accepts the sum of 607,000 people, this only represents 25.3% of the 2.4 million people represented by Revenue's 2.1 million tax units in the relevant data. But IBEC then exclude pensioners and seasonal workers, and others. A further estimated 50,000 are added in on the basis that although they are not currently eligible to pay any tax at 41%, they are within two hours of overtime per week of doing so. This brings up the total affected by changes to the higher income tax rate, allowing IBEC to claim 54% of income tax payers would benefit. Except this is only achieved by contortion and by ignoring many people who do not have the opportunity to work full-time but who are nonetheless income tax payers.

In order to claim 'half' would benefit from a cut to the higher income tax rate, IBEC only counts 1.2 million people as income tax payers, rather than the 1.9 million in employment or the 2.1 million tax cases (2.4 million earners) in Revenue's data.

(3) *IBEC claim: "The Irish tax system is highly progressive and redistributive in a European context: The income tax system is the most progressive in the developed world and Ireland's tax and transfers system is the most redistributive in Europe."*

The OECD database shows that Ireland has the highest level of income inequality before tax and transfers in the whole OECD[8]. **Ireland needs a progressive tax system to reduce the very high initial level of income inequality**.

IBEC claims that Ireland's income tax system is "radically progressive", which suggests that it over-compensates, yet **Ireland's tax and welfare systems do not reduce inequality as completely as some other countries do**. Eurostat show that Ireland still has the highest level of income inequality after tax, but before social transfers[9] and the fifth highest inequality if pensions are included[10]. Social transfers therefore play an important role as well as income tax in reducing inequality. **After both tax and transfers, Ireland moves from having the highest income inequality in the OECD to around the EU average for income inequality**[11], which does demonstrate progressivity and redistribution through the tax and welfare systems. Why dilute this?

(4) *IBEC claim: "Middle and high earners pay the vast majority of tax: Low earners pay less tax than the OECD average, but at the average wage and above Irish tax rates are relatively high. Those earning €39,000 upwards are taxed higher than their OECD counterparts."*

It is true that low paid workers pay less tax and social insurance in Ireland than the EU or OECD average, but they also face more out-of-pocket costs for health, education, etc. that would be free-of-charge or subsidised public services in other countries.

Total labour taxes – the 'tax wedge' including employers' social security contributions – is low on average wage workers too. When they calculate tax on workers, IBEC are ignoring an essential part of labour costs. Employers' social insurance is very low in Ireland. The tax wedge on average and above average workers can be seen in a series of OECD charts produced for the benefit of employers and investors as well as researchers.

For all of the standard comparators, Ireland's tax wedge on workers is lower than the OECD average, and in several cases it is among the lowest.

IBEC's claim that "Those earning €39,000 upwards are taxed higher than their OECD counterparts" is contradicted by the OECD's charts. Based on average industrial wages of €692.43 per week[12], Irish annual 'average wages' (red lines in the charts) are around €36,000.

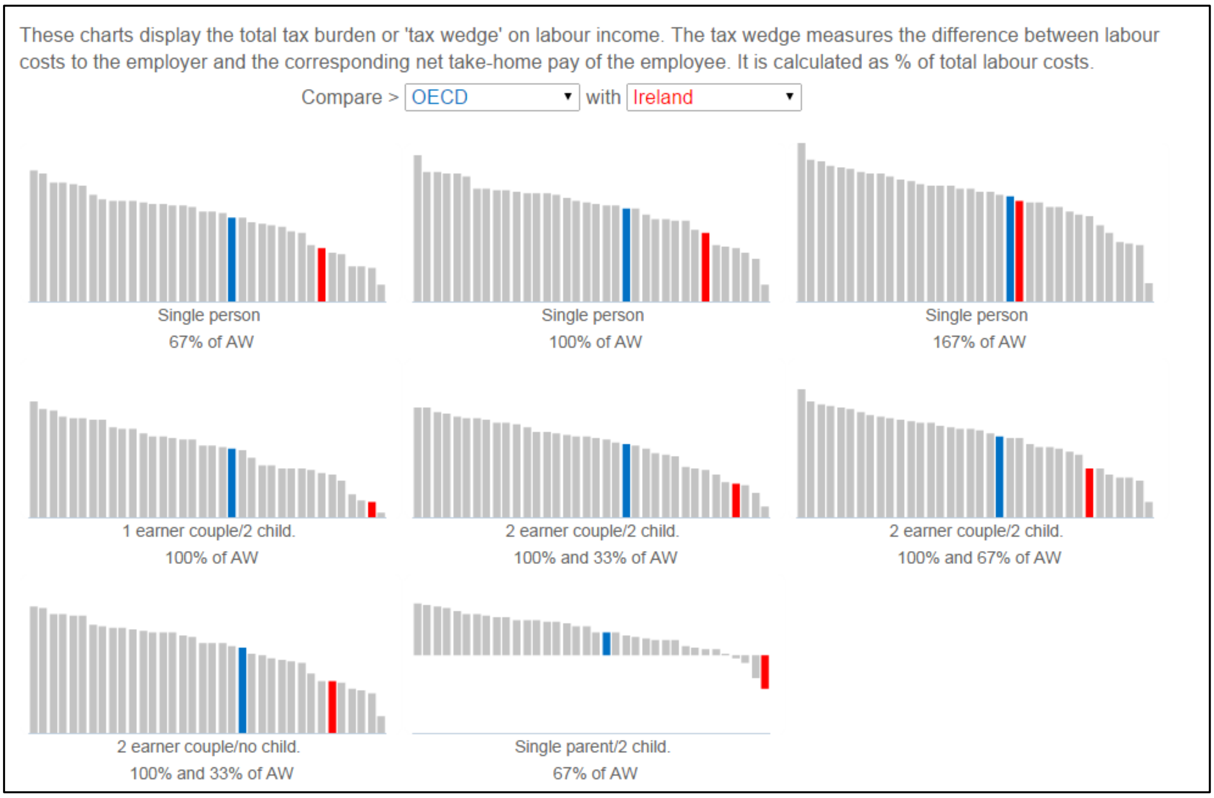

Chart: Irish tax wedge on labour incomes are consistently lower than the OECD average. AW = average wages. Blue = OECD average. Red = Ireland. Source: OECD[13]

Another flaw in the IBEC analysis is that despite the focus on single people paying the higher rate of income tax from €32,800, married couples in Ireland do not pay the higher rate until their joint income is between €45,400 and €65,600[14]. Sharing tax credits takes a lot of married couples out of the higher tax rate. Tax breaks - like the generous pension tax breaks - also reduce the actual amount of tax paid by people on higher incomes.

For those earning above average incomes, Ireland does increase income tax, USC and PRSI to higher levels – but this is for relatively few workers. IBEC focuses on the fact that someone on an income of 2.5 times the average wage of €36,000 pays more than the EU average level of taxation.

The counter argument is that someone on this income level (i.e. €81,500) is single-handedly in the Top 10% of all tax cases and already has a higher disposable income than the vast majority of employees. The Top 10% are those where the income of the tax case is €75,000 or greater, and this group includes dual earner married couples as well as single earners. Giving tax cuts to benefit this group would worsen Ireland's level of income inequality.

Revenue data for 2011 is shown in the chart below[15]. Out of 2.1 million tax cases (representing 2.4 million earners), just under 200,000 tax cases (representing c. 330,000 earners) had a gross income of over €75,000 - and that includes couples, which indicates that significantly fewer than 330,000 single earners have an income of €81,500 or more, despite IBEC's focus on this group.

Table: Revenue data on income tax cases (2011)

Position[16]	**Gross Income Group**	**Total number of tax units**	**Number of single earner tax units**	**% Single earner tax units**	**Number of dual earner tax units**	**% Dual earner tax units**
Top 1%	€200,000 or more	18,741	8,438	45%	10,303	55%
Top 2% to 5%	€100,000 to €200,000	80,388	26,533	33%	53,855	67%
Top 6% to 10%	€75,000 to €100,000	100,673	35,349	35%	65,324	65%
Top 11% to 20%	€50,000 to €75,000	253,897	137,070	54%	116,827	46%
Middle 51% to 80%	€27,000 to €50,000	586,128	469,881	80%	116,247	20%
Bottom 50%	Zero to €27,000	1,009,790	952,056	94%	57,734	6%

(5) IBEC claim: "Certain features to the Irish tax system are a major disincentive to work, especially the marginal rate at average earnings: A skilled graduate moving from gross pay of €20,000 to gross pay of €60,000 over the first ten years of their career will see an increase of annual net pay of just €22,888 in Ireland; the same person would see an equivalent increase of €30,287 in the UK; a difference of €7,399."

IBEC's argument seems to hinge on Ireland competing with the UK on low taxes, which is a race to the bottom. The UK has announced major cuts to public services and social transfers[17]. Ireland can surely offer much more than 'tax incentives' for its citizens to remain. We have the option of taking a different path, by following a North-West European model of higher quality public services, real security against ill health, strong pensions, public investment in infrastructure, and an overall higher quality of life and greater social mobility.

It is argued that Ireland is losing foreign investment due to Irish income taxes on top executives. But Ireland offers the lowest employers' social security contributions of all EU members of the OECD. This considerably lowers the cost of employing someone, which in many cases will outweigh any labour costs associated with compensating employees for higher income tax in Ireland.

It is claimed Irish graduates emigrate to pay less tax in the UK. A comprehensive survey by UCC academics in 2013 showed that emigration is a complex picture[18], but neither high tax nor seeking higher incomes were mentioned in the report as reasons to leave. Many emigrants were employed, but left due to under-employment or only having part-time work. However, the vast majority (82%) said that improvements in the Irish economy would make it more likely for them to return.

(6) *IBEC claim that "The top 1% of all income tax cases in Ireland earn 9.1% of income and pay 30.4% of the taxation." and "The top 5% pay almost 55% of all taxation from 22.7% of the income".*

In this case, IBEC's calculations based on Revenue data appear to be incorrect.

Using Revenue data for 2011[19], the Top 1% pay 19.7 per cent of all income tax not 30.4 per cent as IBEC claim. The Top 1% is 18,741 cases, with a combined income of nearly €7 billion and €2.1 billion income tax paid, which is 19.7 per cent not 30.4 per cent.

IBEC's appear to have taken €2.1 billion as a percentage of this income group's €7 billion income, whereas this number is the actual amount of this group tax paid – 30.4 per cent of their gross income. A total of €10.8 billion income tax is paid by all income tax cases. Tax of €2.1 billion paid by the Top 1% represents 19.7 per cent of total income tax.

The 30.4 per cent figure reinforces TASC's analysis that even those on the highest incomes pay considerably less than the 41% higher rate of income tax, due to tax credits, tax reliefs and tax breaks. When combined with the maximum rates of 4% PRSI and 7 or 10% USC, even those on the highest incomes pays considerably less than the 'marginal rate' of 52%. For example, actual income tax paid of 30% (net of tax reliefs) plus 7% USC and 4% PRSI comes to 41% actual tax paid, not the marginal rate of 52%. (That is 44% versus a 55% marginal rate for the self-employed).

IBEC appear to make a similar error for the Top 5%, but their calculation of 54.6 per cent is not worked out in their document, and it is not easily replicated.

The Top 5% is 99,129 cases, with a combined income of nearly €17.4 billion and €4.7 billion income tax paid, which is 43.0 per cent of all income tax paid, not 54.6 per cent.

A total of €10.8 billion income tax is paid by all income tax cases. The €4.7 billion paid by the Top 5% represents 43.0 per cent of that.

Aside from the calculations, IBEC's argument is presumably that higher income tax payers are paying an excessive amount of tax. However, consider the following: the average gross income of the Top 1% is €373,288. This may be skewed by extremely high incomes but the minimum gross income is €200,000 (as that is the bottom of this income band). The average after-income tax income of the Top 1% is €259,749.

Reducing this further by 10% for self-employed USC and 4% for PRSI, the average after-tax income for the Top 1% would still leave €223,384[20]. Most Irish citizens are likely to regard this as a fair, if not excessive level of pay, given the high level of inequality in the distribution of incomes in Ireland, and the lack of social mobility.

Conclusion

In Ireland, employers enjoy among the lowest nominal and effective rates of corporation tax and social charges, yet business lobbyists continue to advocate for further tax reductions.

The large majority of workers are not affected by the higher rate of income tax, including when they are asked to work overtime or to accept additional responsibilities.

Income taxation and social charges are higher for the Top 10% of income earners, but reducing the amount of tax they pay will undermine the role of Ireland's tax system in reducing inequality. By extension, less tax revenue will undermine social transfers and public services, further worsening income inequality.

The argument that tax cuts would spur sufficient growth to generate a net boost in tax revenues describes an implausible, high risk strategy that might have some merit in a high tax country, but is unlikely to work when revenue is already only three-quarters of EU average levels. Income tax cuts are an indirect strategy, whereas an IMF staff paper[21], among other analysis, has shown that public investment has a higher multiplier effect in the economy than is achieved through tax cuts.

As TASC has argued in its separate Budget 2015 Commentary[22], now is not the time for tax cuts that will only benefit those on high incomes. Maintaining and building quality public services and public investment must be the first priority, which is also demonstrably a pro-business strategy, as demonstrated by the continued competitiveness and productivity achieved in many of North-West Europe's countries.

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[2] EU 28 total government revenue 44.7% GDP. Ireland total government revenue 35.9% GDP. http://epp.eurostat.ec.europa.eu/portal/page/portal/product_details/dataset?p_product_code=TEC00021

[3] see Table 22, p. 195 of *Tax Trends in the European Union*: http://ec.europa.eu/taxation_customs/resources/documents/taxation/gen_info/economic_analysis/tax_structures/2014/report.pdf

[4] http://epp.eurostat.ec.europa.eu/portal/page/portal/product_details/dataset?p_product_code=TEC00119

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[13] http://www.compareyourcountry.org/taxing-wages?cr=oecd&lg=en

[14] http://www.citizensinformation.ie/en/money_and_tax/tax/income_tax/how_your_tax_is_calculated.html#l2729c

[15] Revenue data in chart is taken from Table IDS1 in http://www.revenue.ie/en/about/publications/statistical/2012/income-distribution-statistics.pdf

[16] Due to the organisation of the Revenue data, these bands are actually: top 0.9%, next 4.4%, next 4.9%, middle 28.6% and bottom 49.3%.

[17] See, for example, coverage here http://www.theguardian.com/society/public-sector-cuts

[18] http://www.ucc.ie/en/news/fullstory-371828-en.html

[19] Revenue data from Table IDS1 in http://www.revenue.ie/en/about/publications/statistical/2012/income-distribution-statistics.pdf

[20] Even this is a slight over-estimate as the maximum rates of USC and PRSI are not paid for all income, but the difference is minor.

[21] http://www.imf.org/external/pubs/ft/wp/2010/wp1073.pdf

[22] http://www.tasc.ie/researchpolicy/projects/equality-budget/

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