Irish Tax Institute

Perspectives on Ireland's personal tax system

A medium to long term approach

www.taxinstitute.ie
September 2016

For more information please contact:

Olivia Buckley
Communications Director
Direct: +353 1 663 1706
Email: obuckley@taxinstitute.ie

Cora O'Brien
Policy Director
Direct: +353 1 663 1719
Email: cobrien@taxinstitute.ie

Aidan Lucey
Senior Tax Policy Manager
Direct: +353 1 663 1709
Email: alucey@taxinstitute.ie

About the Irish Tax Institute Report on Personal Taxes

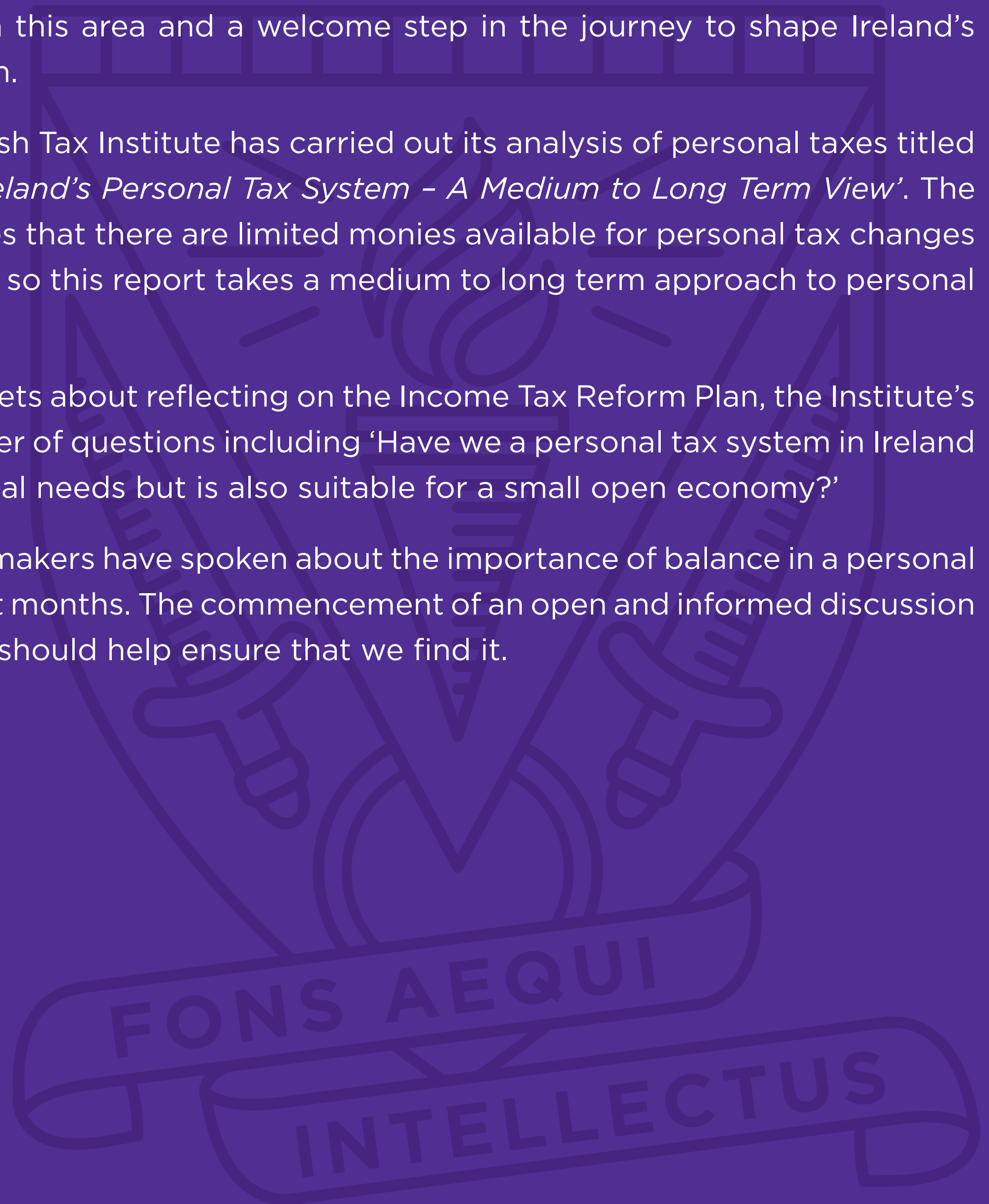
The Programme for a Partnership Government, published in May 2016, committed to the development of a medium-term income tax reform plan for consultation with the Oireachtas stating that “the purpose of the plan is to review Ireland’s system of personal taxation as a whole, to consider the socio-economic impacts of personal taxation, and to examine options for future reform within the personal tax system”.

In July, the Department of Finance published the Income Tax Reform Plan, the first ever reform plan in this area and a welcome step in the journey to shape Ireland’s personal tax system.

This autumn, the Irish Tax Institute has carried out its analysis of personal taxes titled *‘Perspectives on Ireland’s Personal Tax System – A Medium to Long Term View’*. The Institute appreciates that there are limited monies available for personal tax changes in Budget 2017 and so this report takes a medium to long term approach to personal tax issues.

As the Oireachtas sets about reflecting on the Income Tax Reform Plan, the Institute’s report asks a number of questions including ‘Have we a personal tax system in Ireland that meets our social needs but is also suitable for a small open economy?’

Experts and policymakers have spoken about the importance of balance in a personal tax system in recent months. The commencement of an open and informed discussion on all of the issues should help ensure that we find it.



INDEX

Summary of Ireland's Personal Tax System 5

Chapter 1: The four major questions to ask of our personal tax system 11

1. Can we continue to create and judge personal tax policy on a Budget by Budget basis? 12
2. Is there a point at which a country's personal tax system becomes overly progressive? 16
3. Do high tax rates above the average wage (squeezed middle and upwards) impact our competitiveness and create issues around incentive to work, labour costs and ability to attract talent and skills? 22
4. Have we a personal tax system in Ireland that meets our social needs but is also suitable for a small open economy? 25

Chapter 2: Global tax analysis 2016 – Ireland v competitor countries 27

Chapter 3: Special assignee relief programme (SARP) 31

Chapter 4: The complexity of our personal tax regime 32

Chapter 5: The self-employed are treated differently than employees in the tax code 34

Chapter 6: Do we have a sustainable tax base? 36

Chapter 7: Budget 2017 – the options 38

Chapter 8: Share options – the 2016 consultation: will new measures be in the budget? 42

Chapter 9: The story of the personal tax regime over the past 15 years 44

Chapter 10: Exchequer reliance on personal tax has increased 45

Chapter 11: Facts & figures on the personal tax system – additional information 46

Appendix: The PRSI credit 51

Summary of Ireland's Personal Tax System

Nine consecutive Budgets between 2009 and 2016 involved over 50 different tax changes that impacted Ireland's personal tax system. It brought about some unintended consequences in the system and created peculiar traits across all salary levels.

Lower Income Levels

- A worker on €25,000 earns almost 1.4 times the salary of a person on €18,000 but pays 5.6 times the tax.

Average Wage Levels

- A worker on €35,000 earns 1.4 times the amount of a person on €25,000 and pays 1.9 times the amount of tax.

Squeezed Middle

- At a salary level of €55,000, an Irish taxpayer pays more tax than in Sweden, Spain, Switzerland and the US. They pay over €800 more than a taxpayer in the UK.

€75,000 – The Cap Effect

- A worker on €75,000 earns 3 times the amount of a person on €25,000 and pays almost 8 times the amount of tax.
- A worker on €75,000 earns 2.1 times the amount of a person on €35,000 and pays over 4 times the amount of tax.
- At a salary level of €75,000, taxpayers in Ireland are paying rates close to France and they pay over €4,500 more tax than their equivalents in the UK.

Higher Income Earners

A worker on €100,000:

- Earns 5.6 times the amount of a person on €18,000 and pays almost 66 times the amount of tax.
- Earns 4 times the amount of a person on €25,000 and pays over 11.7 times the amount of tax.
- Earns 2.9 times the amount of a person on €35,000 and pays over 6 times the amount of tax.

A worker on €120,000:

- Earns 6.7 times the amount of a person on €18,000 and pays over 83 times the amount of tax.
- Earns almost 4.8 times the salary of a person on €25,000 but pays 14.8 times the tax.
- Earns almost 3.4 times the salary of a person on €35,000 but pays 7.6 times the tax.

The tax multiple accelerates steeply as you move to higher income levels.

Tax paid multiples at €75,000 and €100,000 have especially increased since 2012 – The Cap Effect

A closer analysis of the tax paid at income levels of €75,000 and €100,000 highlights the trend of increasing tax multiples since 2012.

- In 2012, an individual on €75,000 paid a multiple of 31.7 times the tax of someone earning €18,000. By 2016, this multiple had increased to 44.1.
- Similarly, an individual earning €100,000 paid a multiple of 46.5 times the tax of the €18,000 person in 2012 and this had increased to almost 66 times the tax by 2016.

Judging tax policy on a Budget by Budget basis – the consequences

- When we judge changes for individual taxpayers on a Budget by Budget basis we ought not to lose sight of the total Euro amount that people on different salary levels are paying before and after the individual Budget change. If we ignore this important context, then we risk creating a tax system which over time becomes uneven and skewed.
- For example, a Budget by Budget analysis can lead to the overall context being lost when looking at Euro gains benefiting low income earners. This is by virtue of the fact that their tax bills are already low in Ireland. Thus, any Euro amount gain in tax will be at a smaller scale at these income levels.
- The same issue can arise when looking at Euro amount reductions in mid to higher tax rates. If the mid to higher tax rates are reduced in any single Budget, those on higher incomes see a larger Euro amount reduction in their tax bill. This larger Euro reduction is inevitable because those taxpayers are paying much more tax at high rates in the first place. This is what happens in any progressive tax system globally and remember Ireland's is more progressive than most.

A look at progressivity and how it works

- Ordinarily when there is a rate cut across the board, those on the higher incomes receive a greater Euro amount reduction than those on lower incomes because they are paying a lot more tax to start with. After the rates are reduced they will still pay a lot more tax in real terms.
- The increases in the proportion of taxes paid by high income earners has become notable in recent years. For example, in 2015, the top 1% of income earners paid 19% of all personal taxes while just twelve months later this is estimated to be 22%.
- In 2017, it is estimated that the bottom 50% of income earners will pay 3.6% of the income tax take.
- Progressivity is about proportionality not about absolute Euro amounts. People can receive less in Euro terms in a Budget but gain proportionately more.

Tax measures that have driven progressivity in Ireland

Two recent strands in Ireland's personal tax policy have been factors in Ireland's high progressivity.

1. Measures targeting low and middle income earners: (i) USC rate reductions/band increases and (ii) Removal of lower income taxpayers from the tax net; spreading the tax burden across a smaller percentage of taxpayers.

2. Higher income earners - The Cap Effect; a tax policy intervention.
Between 2012 and 2016, during a period of consecutive tax reductions, the tax multiples being paid by high income earners increased although all taxpayers saw a reduction in their tax bills.

The Gini Coefficient - how far should tax policy go in re-distributing income?

- Ireland has a disposable income Gini of 0.30. This is close to the European average.
- Since 2004, Ireland's tax system has reduced its Gini coefficient to a greater extent than other OECD countries.
- Over one quarter of the reduction in the Gini coefficient in Ireland in 2012 was attributable to the tax system. This proportion was only larger for Australia and the United States.
- According to the latest available data, the reduction in Ireland's Gini coefficient - a standard measure of income inequality - due to the tax system is the third largest in the OECD and the largest among EU members.

Other Interesting Facts on Ireland's Personal Tax System

The big driver at squeezed middle salaries: Income tax & the step

- While much discussion in recent times centres on the USC, the big driver of high effective tax rates for Ireland's squeezed middle is income tax rates.
- This is driven by the fact that workers move from the 20% income tax rate to the 40% rate at low income levels.
- A move from €33,800 to €33,801 means that the income tax rate doubles on each additional euro earned. Irish taxpayers are in the top income tax rate even before they reach the average industrial wage.

The 50's Club – A high marginal rate in an open economy

- Ireland is one of only thirteen countries amongst the OECD's thirty-four member countries that has a marginal rate in the fifties[1]. It also ranks in the Top 10.
- Irish taxpayers enter the 52% rate at €70,045. In fact, at €33,801 we pay 49.5%, which is only 0.5% off the "Club".
- Spain's 52% marginal rate only applies from €300,000 and you must be earning almost €152,000 in France before you pay their marginal rate of 55.01%. The entry point to the 50's club in Finland is €100,000 and in Portugal it is €80,000.

1 Based on OECD data from 2014 (the latest available).

Personal Taxes – a major contributor to the tax take

- In 2007 and 2008, VAT was the highest contributor to the Exchequer. But in 2009, personal taxes outstripped VAT and the gap has continued to widen.
- Personal taxes now account for 40% of the total tax yield and according to the Tax Strategy Group, they are expected to generate almost €19 billion for the Exchequer in 2016.

The USC

- USC accounts for over €4bn in receipts, less than one-quarter of the total personal tax yield of €18.3bn .
- USC is a significant contributor to the Exchequer, accounting for 9% of total tax receipts in 2015.
- The top 1.2% of income earners earn 10.9% of total income and pay 22.1% of total USC to the Exchequer.
- In the past six Budgets the entry point to the USC system has changed three times, while the USC bands have changed twice.

Complex – so many moving parts

- Ireland's personal tax system has 53 different moving parts.
- We have three different tax charges each with a different entry point and a total of 10 rates, 15 bands and 22 personal tax credits.

Competitiveness

- At €100,000 and above, we continue to remain at the upper end of the global rankings ahead of taxpayers in France, Spain and the UK amongst others.
- The Institute's global research highlights the personal tax competiveness issues as workers reach higher salary levels. As salary levels increase to €100,000, we are paying effective rates near those in Sweden.
- For internationally mobile executives at this salary point, only Germans pay more tax than executives in Ireland (out of our key European competitor countries). This takes into account special tax reliefs for assignees (in Ireland's case this is SARP).

Getting the balance right: Have we a personal tax system that meets our social needs but is also suitable for a small open economy?

“A small and very open economy (such as Ireland) extends beyond national borders and cannot operate its tax policy in isolation from the international environment”[2].

Bird and Wilkie

“...high marginal tax rates can act as a disincentive to labour supply and may be harmful to overall economic growth, so it is necessary to maintain a balance between progressivity and relative competitiveness with other jurisdictions”[3].

Department of Finance, Income Tax Reform Plan

Ireland’s Tax Strategy Group had similar views:

“It is ....appropriate that the system of personal tax is reviewed regularly to ensure that it continues to meet the basic requirements of raising revenue in an efficient and equitable manner for the purposes of financing Government expenditures including social transfers, and contributing to the achievement of the Government’s social and economic objectives”.

TSG Paper 16/05

“Work by the OECD experts and many others on tax reform and economic growth stress the need to weigh up the extent to which high marginal tax rates on income can act as a disincentive, for instance, for investment in human capital or discourage entrepreneurship, and the fact that progressive taxation of income is one of the main ways for governments to redistribute incomes”.

Alan Carter, Head of International Tax Dialogue Secretariat, and Stephen Matthews, OECD Centre for Tax Policy and Administration

Conclusion

While it is clear that a planned and coherent approach is needed to Ireland’s personal tax system in the medium to long term, the publication of the Income Tax Reform Plan in July is an important and welcome first step.

2 Designing tax policy: constraints and objectives in an open economy, Richard M. Bird and J. Scott Wilkie: eJournal of Tax Research, December 2013.
3 Income Tax Reform Plan, Department of Finance, July 2016.

Chapter 1:

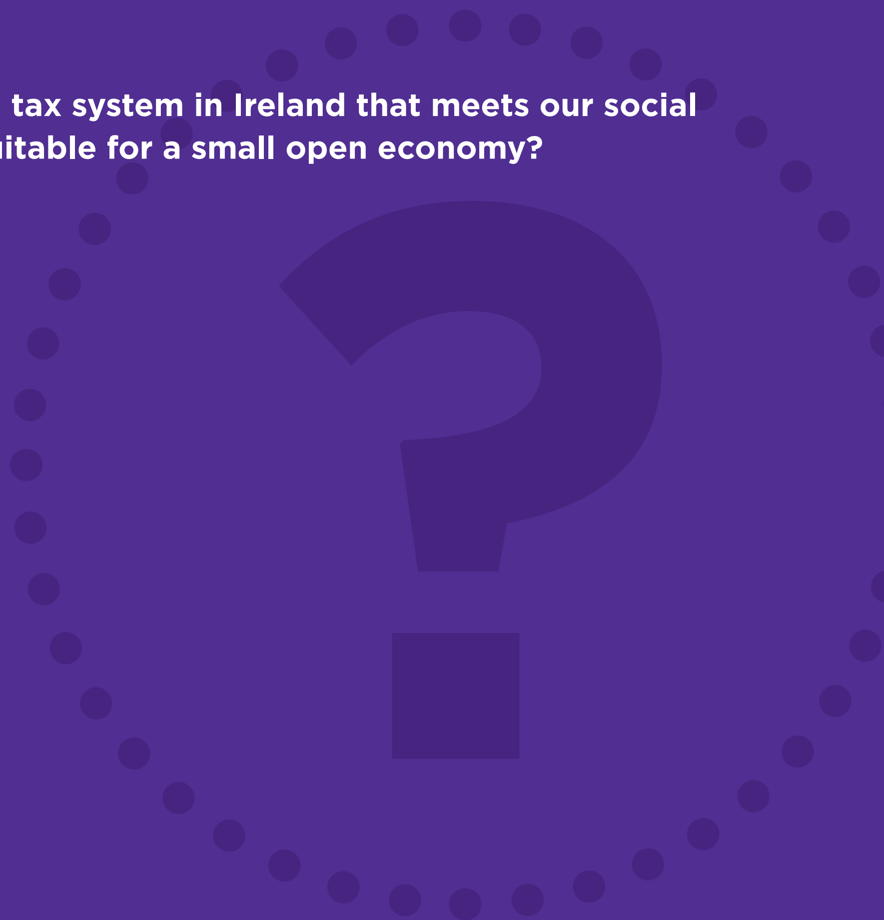
The Four Major Questions to ask of our personal tax system

Question 1: Can we continue to create and judge personal tax policy on a Budget by Budget basis?

Question 2: Is there a point at which a country's personal tax system becomes overly progressive?

Question 3: Do high tax rates above the average wage (squeezed middle and upwards) impact our competitiveness and create issues around incentive to work, labour costs and ability to attract talent and skills?

Question 4: Have we a personal tax system in Ireland that meets our social needs but is also suitable for a small open economy?



Question 1: Can we continue to create and judge personal tax policy on a Budget by Budget basis?

"We should have a tax system which looks like someone designed it on purpose".

William E. Simon - Former Secretary of the Treasury in the United States in the early 1970s

This view is supported by the two independent Commissions on Taxation (1982 and 2009)

Maintaining a focus on a well-designed tax policy system has a much greater capacity to achieve economic and social goals than could be promoted through individual tax changes or initiatives."

Nine consecutive Budgets set out to achieve many things:

Ireland had four tax increasing Budgets during the austerity years and five Budgets since the programme of tax reduction commenced from Budget 2012 onwards. The wide range of tasks that was asked of nine consecutive Budgets involved over 50 different changes which impacted the personal tax system. For example, in the past six Budgets the entry point to the USC system has changed four times, while the USC bands have changed three times.

We have reached a point where we have a personal tax system with 53 different moving parts – we have three different tax charges each with a different entry point and a total of 10 rates, 15 bands and 22 personal tax credits (being the main credits recognised by Revenue and the PRSI credit). [See our table on Tax Complexity on Page 32].

The nine budgets set out to do many things including the following:

In the tax raising Budgets: **Budgets 2009 - 2011** (includes a supplementary Budget in 2009)

- Increase substantially the Exchequer take from personal tax.
- Broaden the tax base.
- Minimise the impact of tax increases on lower and middle income earners. During the economic crisis, the tax burden on those earning 67% and 100% of the average wage was kept below EU and OECD average levels.
- Ensure those on higher incomes bore the heaviest weight of tax increases.

In the tax reducing Budgets: **Budgets 2012 - 2016**

- Take the lowest income earners back out of the tax net.
- Limit the gains for higher income earners through capped rate reductions, the intention being that those on higher incomes would not gain too much as rates began to fall.
- Reduce the impact of the step into PRSI for those earning the minimum wage by introducing a tapered PRSI credit. This ensured that the benefit of the minimum wage increase was not completely eroded upon entry to the PRSI net (See Page 51 for further details on the mechanics of this credit).
- Begin to equalise the tax treatment of self-employed taxpayers.

There was a universal appreciation that 'needs must' and that in the early years of the crash a blunt approach to increasing tax yields was essential. However, the combined impact of those changes and the way they have been 'to some extent' unwound has left some interesting marks on the Irish personal tax system. Marks that we should reflect on as we look towards the formulation of future personal tax policy; a journey whose welcome first step was the publication of the Income Tax Reform Plan in July 2016.

Some of the interesting marks left on the personal tax system by the 'Budget by Budget' approach: These tax computations reflect the position for tax year 2016.

- In the tables below, we examine the extent to which a person's tax bill multiplies as their salary increases.
- We take €18,000, €25,000 and €35,000 as three different salary base levels for the purposes of this analysis.
- It is interesting to note how the tax multiple increases as you move up through the salary scales.

Salary of €18,000 (Tax paid - €600)					
Salary	€25,000	€35,000	€75,000	€100,000	€120,000
Earning *X* times the salary of an individual on €18,000 (The multiples)	1.4	1.9	4.2	5.6	6.7
Paying *X* times the tax of an individual on €18,000 (The multiples)	5.6	10.9	44.1	65.8	83.1
Paying € more tax than individual on €18,000	€2,768	€5,958	€25,882	€38,882	€49,282

What does this table show us?

- A worker on €25,000 earns almost 1.4 times the salary of a person on €18,000 but pays 5.6 times the tax.
- A worker on €120,000 earns 6.7 times the amount of a person on €18,000 and pays over 83 times the amount of tax.

Salary of €25,000 (Tax paid - €3,368)				
Salary	€35,000	€75,000	€100,000	€120,000
Earning *X* times the salary of an individual on €25,000 (The multiples)	1.4	3.0	4.0	4.8
Paying *X* times the tax of an individual on €25,000 (The multiples)	1.9	7.9	11.7	14.8
Paying € more tax than individual on €25,000	€3,190	€23,114	€36,114	€46,514

What does this table show us?

- A worker on €35,000 earns 1.4 times the amount of a person on €25,000 and pays 1.9 times the amount of tax.
- A worker on €100,000 earns 4 times the amount of a person on €25,000 and pays over 11.7 times the amount of tax.

Salary of €35,000 (Tax paid - €6,558)			
Salary	€75,000	€100,000	€120,000
Earning *X* times the salary of an individual on €35,000 (The multiples)	2.1	2.9	3.4
Paying *X* times the tax of an individual on €35,000 (The multiples)	4.0	6.0	7.6
Paying € more tax than individual on €35,000	€19,924	€32,924	€43,324

What does this table show us?

- A worker on €75,000 earns 2.1 times the amount of a person on €35,000 and pays over 4 times the amount of tax.
- A worker on €120,000 earns almost 3.4 times the salary of a person on €35,000 but pays 7.6 times the tax.

Analysis:

At all income levels in these tables, the tax multiple is greater than the salary multiple.

The multiple accelerates steeply as you move to higher income levels. For example, taking a base salary of €18,000, the tax multiple is 5.6 for somebody earning €25,000 as compared to a multiple of 83.1 for somebody on a salary of €120,000.

Judging tax policy on a Budget by Budget basis – The consequences and the issues

- In general, the Budget is judged on the actual Euro amount gained by individual taxpayers both before and after that Budget. Questions that naturally receive sharpest focus on Budget Day include: How much more or less of a tax saving will John have after the Budget? How much more or less will John receive compared to Mary across a range of salary points? – and How will the Budget ensure that John does not receive too much of a benefit in Euro amount?
- This is understandable because taxpayers want to know the Euro amount difference the Budget will make to them. However, when we judge individual changes for different taxpayers on a Budget by Budget basis we cannot lose sight of how much overall tax that people on different salary levels are paying before and after the individual Budget change. If we ignore this important context, then we risk creating a tax system which over time becomes uneven and skewed.
- If the mid/higher tax rates are reduced in any single Budget, there can be comments that this is unfair because those on higher incomes see a larger Euro reduction in their tax bill. This larger Euro reduction is inevitable because those taxpayers are paying much more tax at high rates in the first place. This is what happens in any progressive tax system globally and remember Ireland's is more progressive than most.
- A Budget by Budget analysis is also problematic when looking at gains that would benefit low income earners. This is by virtue of the fact that their tax bills are already low in Ireland. Thus, any reductions in tax will be at a smaller scale in Euro terms at these income levels.
- Based on the explanations above about the difficulty of analysing cuts for high income earners as contrasted with lower income earners, we can see how a focus which is purely Budget by Budget driven can appear to give a distortive result.

Is there a point at which a country's personal tax system becomes overly progressive?

- We have seen the impact of progressivity on taxpayers at different salary levels in the previous section.
- The increases in the proportion of taxes paid by high income earners has become notable in recent years. For example, in 2015, the top 1% of income earners paid 19% of all personal taxes while just twelve months later this is estimated to be 22%.
- In 2017, it is estimated that the bottom 50% of income earners will pay 3.6% of the personal tax take.
- And between 2012 and 2016, changes to the personal tax system have been progressive at higher income levels.

- Average rate of progressivity for OECD countries is 125. Ireland, in contrast, has a progressivity rate of 179.
- We are second only to Israel in the entire OECD and we are highest in the EU.

Source: Department of Finance Analysis of OECD Taxing Wages - Comparative tables

Tax multiples at €75,000 and €100,000 have increased since 2012

We have already looked at some interesting marks left on the personal tax system by the 'Budget by Budget' approach. A closer analysis of the tax paid at income levels of €75,000 and €100,000 highlights the trend of increasing tax multiples since 2012.

Salary of €18,000 versus €75,000		
Salary	2012	2016
Earning *X* times the salary of an individual on €18,000 (The multiples)	4.2	4.2
Paying *X* times the tax of an individual on €18,000 (The multiples)	31.7	44.1

What does this table show us?

- In 2012, an individual on €75,000 paid a multiple of 31.7 times the tax of someone earning €18,000. By 2016, this multiple had increased to 44.1.

Salary of €18,000 versus €100,000		
Salary	2012	2016
Earning *X* times the salary of an individual on €18,000 (The multiples)	5.6	5.6
Paying *X* times the tax of an individual on €18,000 (The multiples)	46.5	65.8

What does this table show us?

An individual earning €100,000 paid a multiple of 46.5 times the tax of the €18,000 person in 2012 and this had increased to almost 66 times the tax by 2016.

Progressivity is about proportionality not about absolute Euro amounts. People can receive less in Euro terms but gain proportionately more.

Tax measures that have driven progressivity in Ireland

Two recent strands in Ireland's personal tax policy have been factors in Ireland's high progressivity:

1. Measures targeting low and middle income earners

(i) USC rate reductions/band increases

With taxpayers under financial pressure as a result of the financial crash, consecutive Budgets moved to bring some relief to lower and middle income earners by reducing the tax burden on them. For example, the entry point to the USC has increased three times since its introduction and in the last two Budgets, rate reductions have been made to the three lower USC rates (currently the 1%, 3.5% and 7% rates which apply to income below €70,045).

The Programme for a Partnership Government stresses that future tax reductions will continue to focus on low and middle income earners.

(ii) Removal of lower income taxpayers from the tax net spreads the burden on those who remain

If you take people out of the tax net you are putting more of the burden on those who remain in the tax base [See Chapter 7, Page 38].

The number of income earners who were out of the tax net had been reduced from 42% in 2008 to 12% by 2011 (See Page 37). Since 2012, 459,500 income earners have been taken out of the tax net again. Post Budget 2016, there are now approximately 29% out of the tax net. This Budget alone removed 42,500 lower income earners from the tax net by increasing the USC entry point to €13,001.

Ireland's progressivity rating has improved in recent years, moving from a score of 183 to 179. As the OECD calculates progressivity by comparing the tax due by a person on 167% of the average wage with the tax payable at 67% of the average wage, the recent USC changes to the lower rates/bands has improved Ireland's position. However, we still remain second in the OECD tables.

2. Higher income earners - The Cap Effect: a tax policy intervention

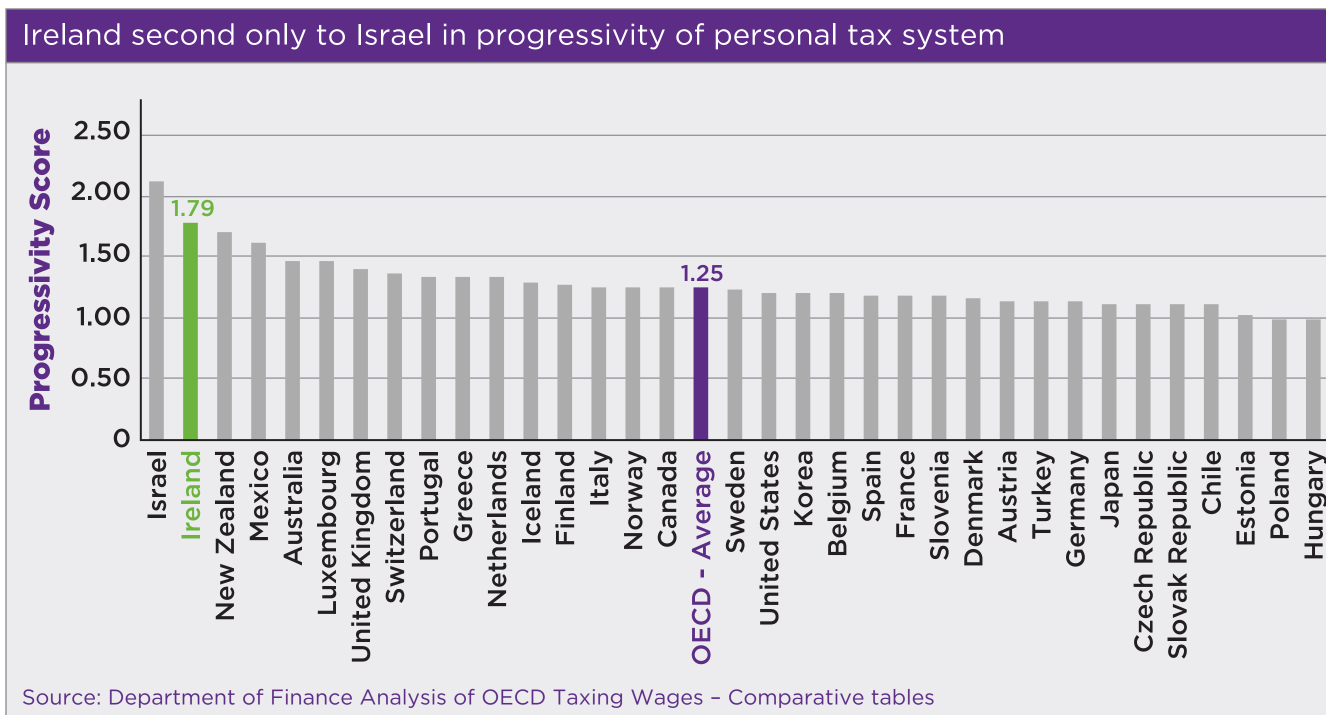
With sensitivity around how much higher income earners might gain from tax reductions in any individual Budget, a cap was introduced on incomes over €70,044. Budgets 2015 and 2016 both included capping mechanisms which increased the comparable multiples of tax that high income earners are paying. In Budget 2015, the top income tax rate was reduced by 1% for all taxpayers but the top USC rate was increased by 1% on incomes over €70,044. Therefore, any income over €70,044 could not benefit from the reduction in income tax rates; the gain from tax reductions was capped at €747. Similarly, in Budget 2016, the USC changes were targeted at the lower rates and bands, with the result being that the gain was capped at €902.

Between 2012 and 2016, during a period of consecutive tax reductions, the tax multiples being paid by high income earners increased although all taxpayers saw a reduction in their tax bills. This can be seen by comparing, for example, the tax due by somebody on €75,000 or €100,000 versus somebody on €18,000.

How Progressivity Works in Other Countries

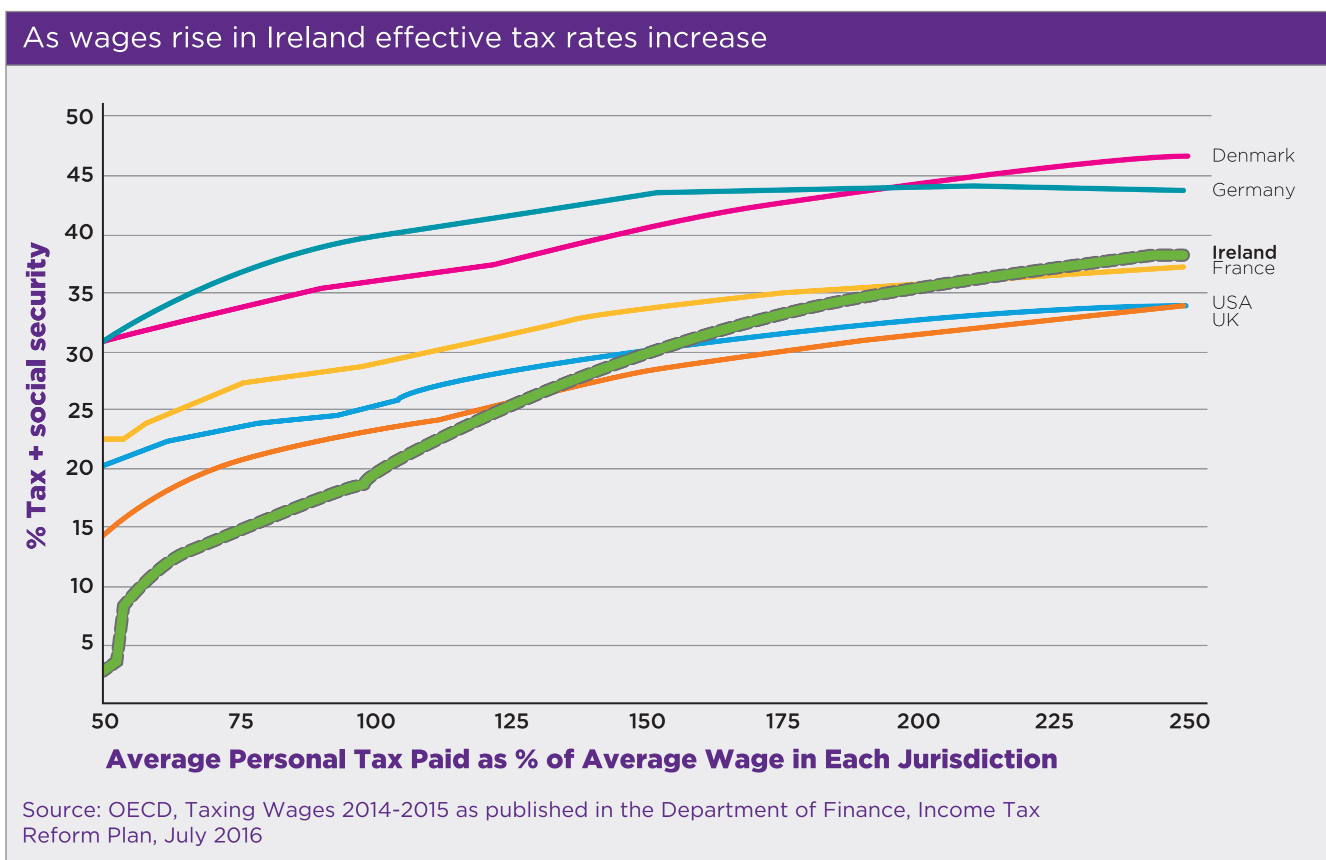
- Ordinarily when there is a rate cut across the board, those on the higher incomes receive a greater Euro amount reduction than those on lower incomes because they are paying a lot more tax to start with.
- After the rates are reduced they will still pay a lot more tax.
- This is what happens during rate reduction programmes in progressive tax regimes across the world.
- Ireland has intervened to cap these rate reductions.

Ireland second only to Israel in progressivity of personal tax system



Source: Department of Finance Analysis of OECD Taxing Wages – Comparative tables

As wages rise in Ireland effective tax rates increase



Source: OECD, Taxing Wages 2014-2015 as published in the Department of Finance, Income Tax Reform Plan, July 2016

> **Commenting on the graph above, the Tax Strategy Group said:**
> *"This comparison suggests that Irish employers could face difficulties in seeking to attract mobile international talent from certain competitor jurisdictions, all other factors being equal".*

How far should tax policy go in re-distributing income?

In considering the future shape of the personal tax system, it is also worth reflecting on the role of tax policy in re-distributing income.

Gini coefficient – *Universally understood as an income inequality measure*

The Gini coefficient is a measure of the distribution of income where 0 represents a situation where all households have an equal income and 1 indicates that one household has all national income.[4]

There are a few interesting international figures that may suggest closer observation as we formulate future tax policy:

- Ireland has a disposable income Gini of 0.30.[5] This is close to the European average.
- Since 2004, Ireland's tax system has reduced its Gini coefficient to a greater extent than other OECD countries.
- Over one quarter of the reduction in the Gini coefficient in Ireland in 2012 was attributable to the tax system. This proportion was only larger for Australia and the United States.

According to the latest available data, the reduction in Ireland's Gini coefficient - a standard measure of income inequality - due to the tax system is the third largest in the OECD and the largest among EU members"

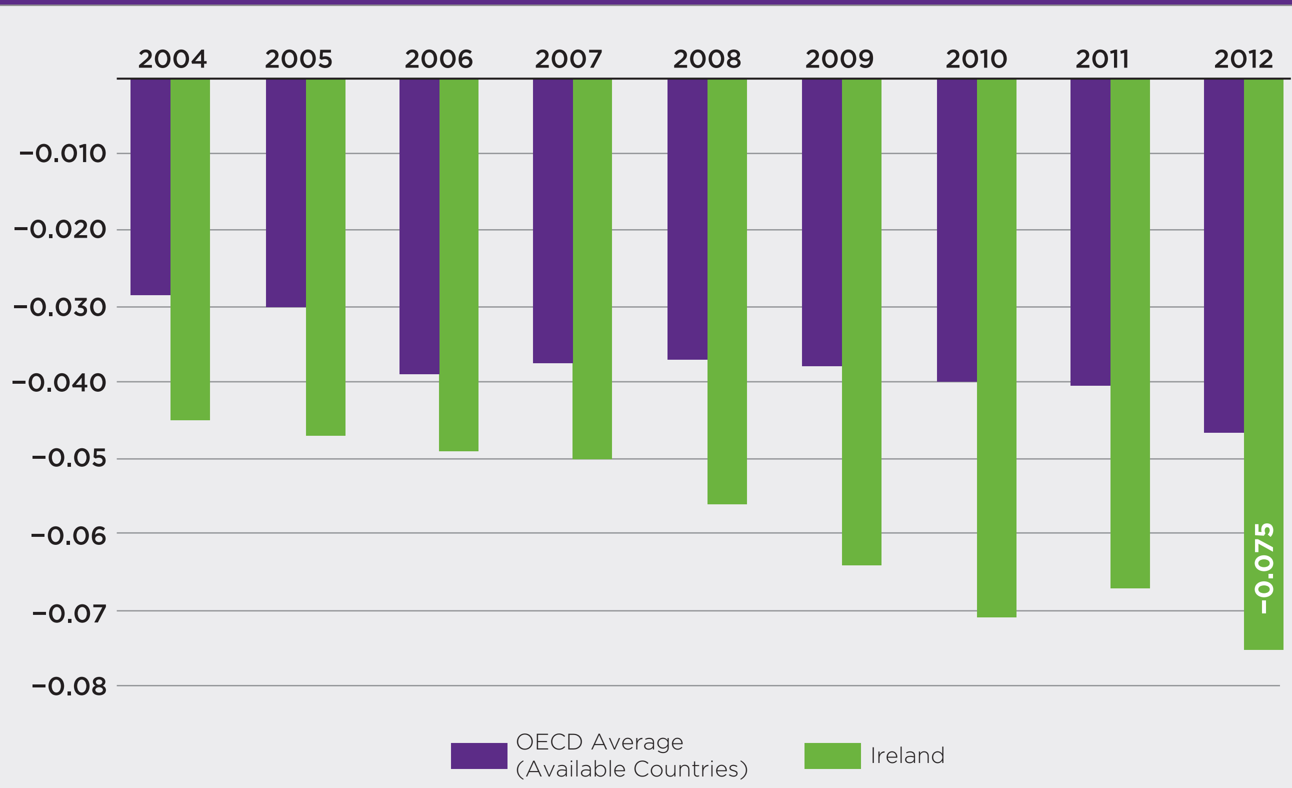
Minister Simon Harris, TD, October 2015

Some international bodies have made comments on the role of tax policy on income distribution:

Work by the OECD experts and many others on tax reform and economic growth stress the need to weigh up the extent to which high marginal tax rates on income can act as a disincentive, for instance, for investment in human capital or discourage entrepreneurship, and the fact that progressive taxation of income is one of the main ways for governments to redistribute incomes".

Alan Carter, Head of International Tax Dialogue Secretariat, and Stephen Matthews, OECD Centre for Tax Policy and Administration

4 Tax Strategy Group | TSG 16/05 Income Tax & USC



5 Income Tax Reform Plan

Question 3: Do high tax rates above the average wage (squeezed middle and upwards) impact our competitiveness and create issues around incentive to work, labour costs and ability to attract talent and skills?

The view of Ireland's Department of Finance is that:

"...high marginal rates of taxation as a result of progressive taxation can have a negative impact on incentives to work for income earners, and lead to increased labour costs for employers who may have to offer a certain level of net income in order to attract employees in a competitive labour market."

Department of Finance, Income Tax Reform Plan, July 2016

(1) The Squeezed Middle – A focus on €55,000 and over

International research carried out by the Institute (see below) shows that at a salary level of €55,000, an Irish taxpayer pays more tax than in Sweden, Spain, Switzerland and the US. They pay over €800 more than the equivalent taxpayer in the UK.

Once you go over the average wage in Ireland you quickly rise up to high levels of personal tax and Ireland quickly goes up the global tax tables [See our Global Tax Tables in Chapter 2, Page 27].

Middle income and higher income earners still pay more tax than they did seven years ago before austerity measures kicked in.

The top 50% of income earners, those earning above €30,000, pay over 96% of the personal tax take.

Issues around Costs and Incentive to Work:

From a growth and reward perspective can we afford to push taxpayers into such high levels of personal tax that it becomes less attractive to earn more, produce more or secure a promotion?

The squeezed middle includes our sales managers, lab supervisors and mechanical engineers. It includes those workers who look after logistics, business development, supplier relationships and projects. The very people we need to incentivise, promote and encourage if we are to drive the growth of thousands of Irish businesses every day.

Salary level of €55,000				
	Total Tax/Social Security ("SS")	Net Take Home	Employee Effective Tax/SS Rate	Difference in Taxes paid compared with Ireland
Germany	22,646	32,354	41.17%	6,188
Netherlands	19,926	35,074	36.23%	3,468
France	18,336	36,664	33.34%	1,878
Ireland	16,458	38,542	29.92%	
Spain	16,176	38,824	29.41%	-282
Sweden	15,732	39,268	28.60%	-726
United Kingdom	15,622	39,378	28.40%	-836
Switzerland	13,320	41,680	24.22%	-3,138
United States	11,951	43,049	21.73%	-4,507
Singapore	11,062	43,938	20.11%	-5,396

The Big Driver: Income Tax & The Step

- While much discussion in recent times centres on the USC, the big driver of high effective tax rates for Ireland's squeezed middle is income tax rates.
- This is driven by the fact that workers move from the 20% income tax rate to the 40% rate at low income levels. Taxpayers enter the highest income tax rate of 40% at €33,801. What happens from €33,801 onwards is what really drives the personal tax bills for the squeezed middle.
- A move from €33,800 to €33,801 means that the income tax rate doubles on each additional euro earned. Irish taxpayers are in the top income tax rate even before they reach the average industrial wage.
- Ireland's 'high rate meets low entry point' combination is at the heart of our personal tax problem. Global calculations carried out by the Institute really drive home the impact of this.

There is an appreciation that raising the entry point to the higher rate is extremely costly. It is estimated that the cost of increasing the marginal rate threshold by just €1,000 in 2017 would cost the Exchequer €188 million.

The Step Effect	
Income Level	Top Tax Rate
€18,000	23%
€25,000	29.5%
€50,000	49.5%
€75,000	52%
€105,000 (self-employed income)	55%

This early "jump" into the higher rate means that the tax bill in Ireland starts to climb steeply once a person earns more than the average wage.

Higher Income Earners – A Focus on €75,000 and Over

- At income levels above the average wage, Ireland moves quickly up the international table of effective tax rates.
- By the time you get to €75,000 we are a high tax country by international comparison and that remains the case as salaries increase.
- When you look at the Institute's Global Analysis across 10 countries, we see that Irish workers on €75,000 have risen up the tables to fourth position. [See Page 29]
- At €100,000 we continue to remain at the upper end of the global rankings ahead of taxpayers in France, Spain and the UK amongst others.

€75,000+

Have we a personal tax system in Ireland that meets our social needs but is also suitable for a small open economy?

A small and very open economy (such as Ireland) extends beyond national borders and cannot operate its tax policy in isolation from the international environment"[6].

Bird and Wilkie

The design of all our major taxes is now impacted by the international movement of income, capital and people.

The 50's Club – A high marginal rate in an open economy

It is worth noting that Ireland is one of only thirteen countries amongst the OECD's thirty-four member countries that has a marginal rate in the fifties[7]. It also ranks in the Top 10.

At a marginal tax rate of 52% (for employees) Ireland is in the 50's club (note that the marginal rate for the self-employed earning over €100,000 is 55%). However, Irish taxpayers enter the 52% rate at €70,045. In fact, at €33,801 we pay 49.5%, which is only 0.5% off the "Club".

Spain's 52% marginal rate only applies from €300,000 and you must be earning almost €152,000 in France before you pay their marginal rate of 55.01%. The entry point to the 50's club in Finland is €100,000 and in Portugal it is €80,000.

At a salary of just over €70,000, you pay Ireland's marginal tax rate. In Spain, you need to be earning more than 4.2 times this amount before the marginal rate kicks in.

Competitiveness

Global research carried out for the Institute (see the next chapter) highlights the personal tax competiveness issues as workers reach higher salary levels. At a salary level of €75,000, taxpayers in Ireland are paying rates close to France and they pay over €4,500 more tax than their equivalents in the UK. As salary levels increase to €100,000, we are paying effective rates near those in Sweden.

For internationally mobile executives at this salary point, only Germans pay more tax than executives in Ireland (out of our key European competitor countries). This takes into account special tax reliefs for assignees (in Ireland's case this is SARP - See Page 31).

6 Designing tax policy: constraints and objectives in an open economy, Richard M. Bird and J. Scott Wilkie: eJournal of Tax Research, December 2013.
7 Based on OECD data from 2014 (the latest available).

Where to next on income tax policy?

Ireland's first Income Tax Reform Plan was published in July this year and while there may be differing views on the options and proposals within it, the publication of such a plan is to be welcomed.

In the plan the Department of Finance said:

...high marginal tax rates can act as a disincentive to labour supply and may be harmful to overall economic growth, so it is necessary to maintain a balance between progressivity and relative competitiveness with other jurisdictions..."[8]

It is ... appropriate that the system of personal tax is reviewed regularly to ensure that it continues to meet the basic requirements of raising revenue in an efficient and equitable manner for the purposes of financing Government expenditures including social transfers, and contributing to the achievement of the Government's social and economic objectives".

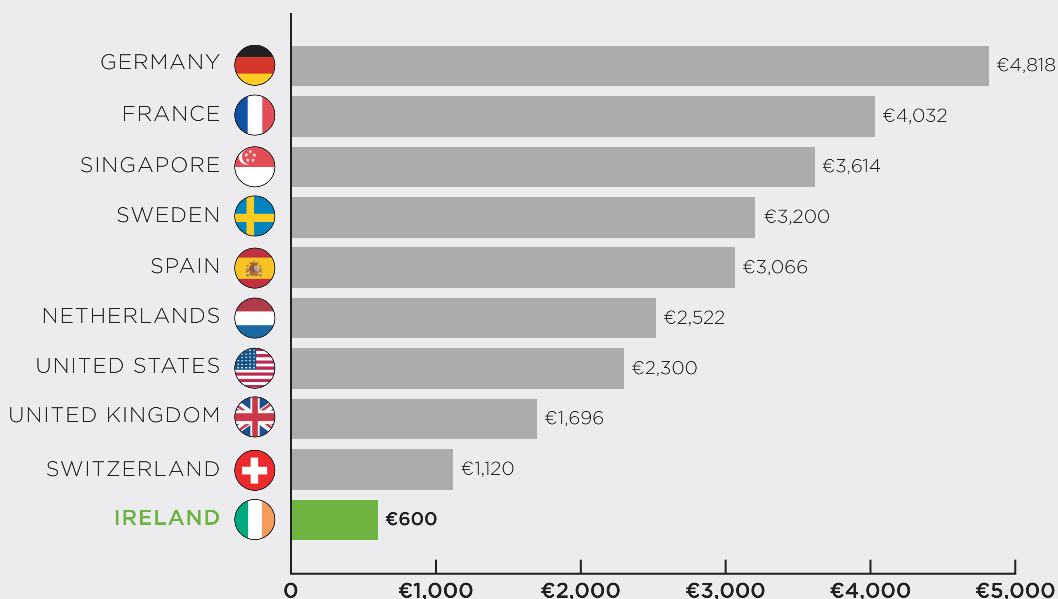
Tax Strategy Group, TSG Paper 16/05

Many experts and policymakers have spoken about the importance of balance in the personal tax system in recent months. The commencement of an open and informed discussion on all of the issues should help ensure that we find it.

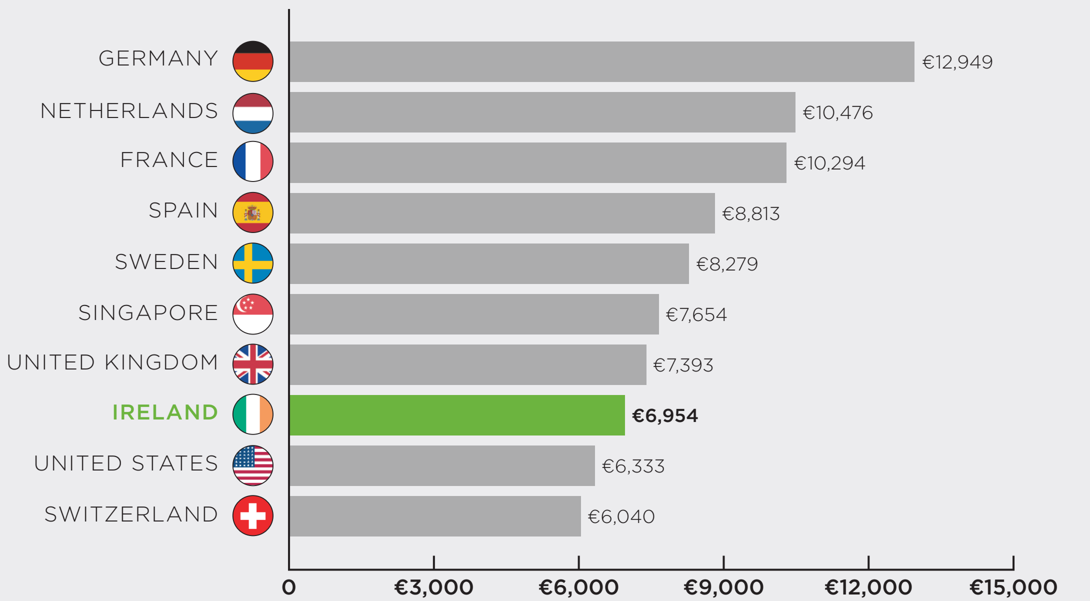
Chapter 2:

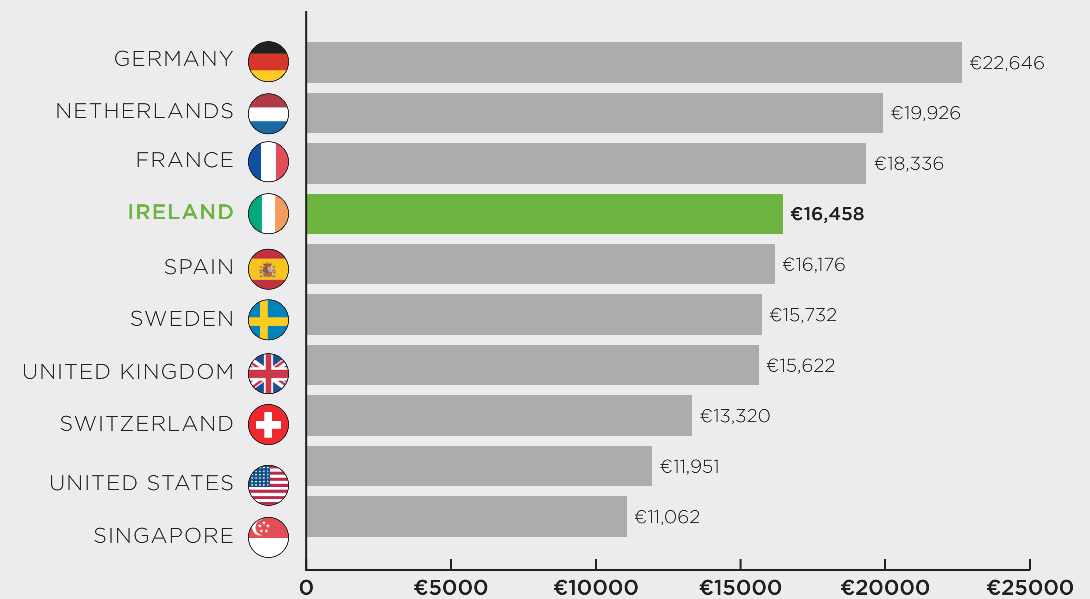
Global Tax Analysis 2016[1] – Ireland v Competitor Countries

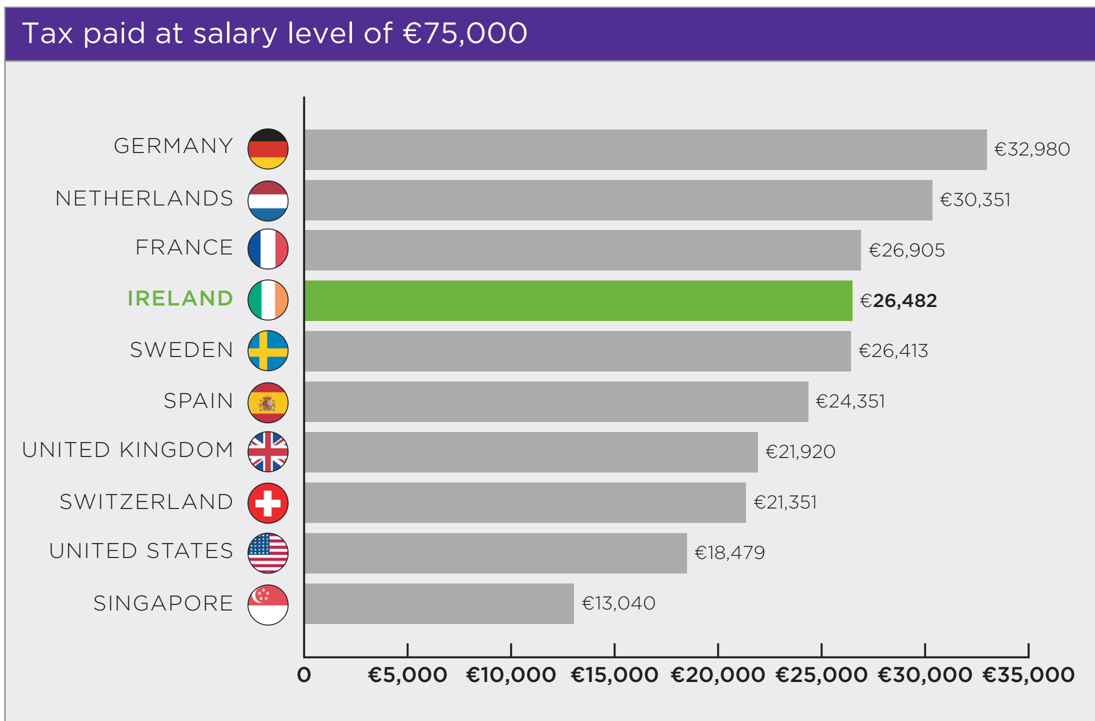
- At lower income levels, Ireland has the lowest effective personal tax rate of all ten countries examined.
- However as income levels rise, taxpayers in Ireland move quickly up the international tables.
- Once you start to move into the “squeezed middle” i.e. salaries of €55,000 and above, rates rapidly increase; taxpayers are paying 49.5% on salaries above €33,800 and 52% from €70,045.

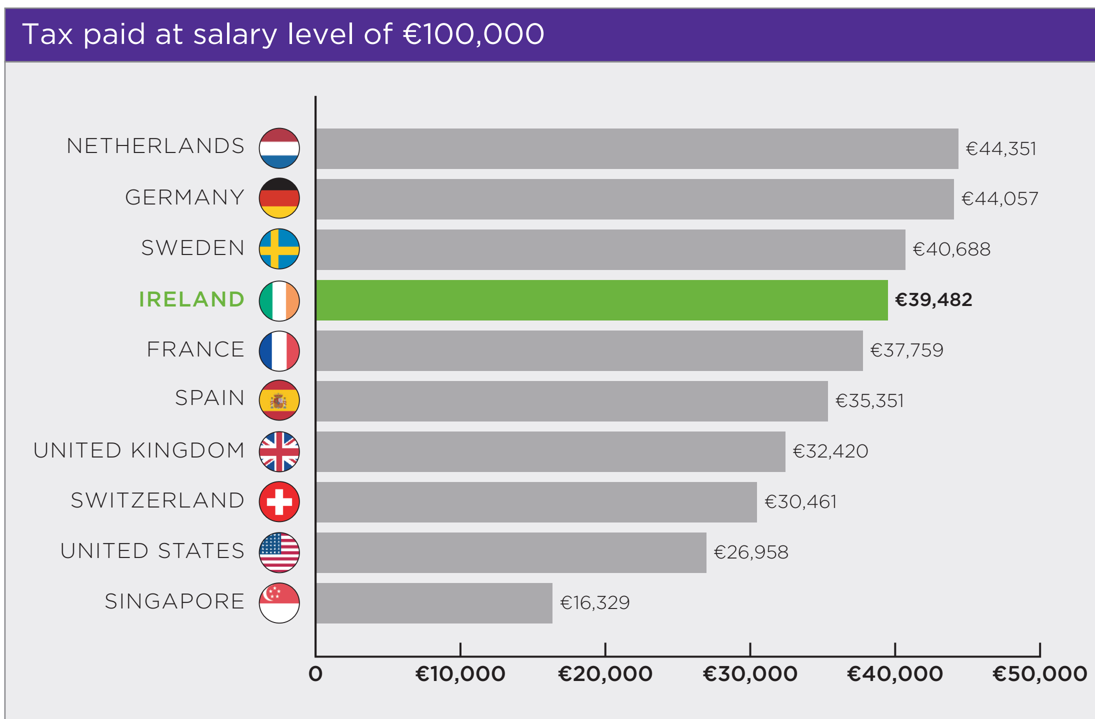


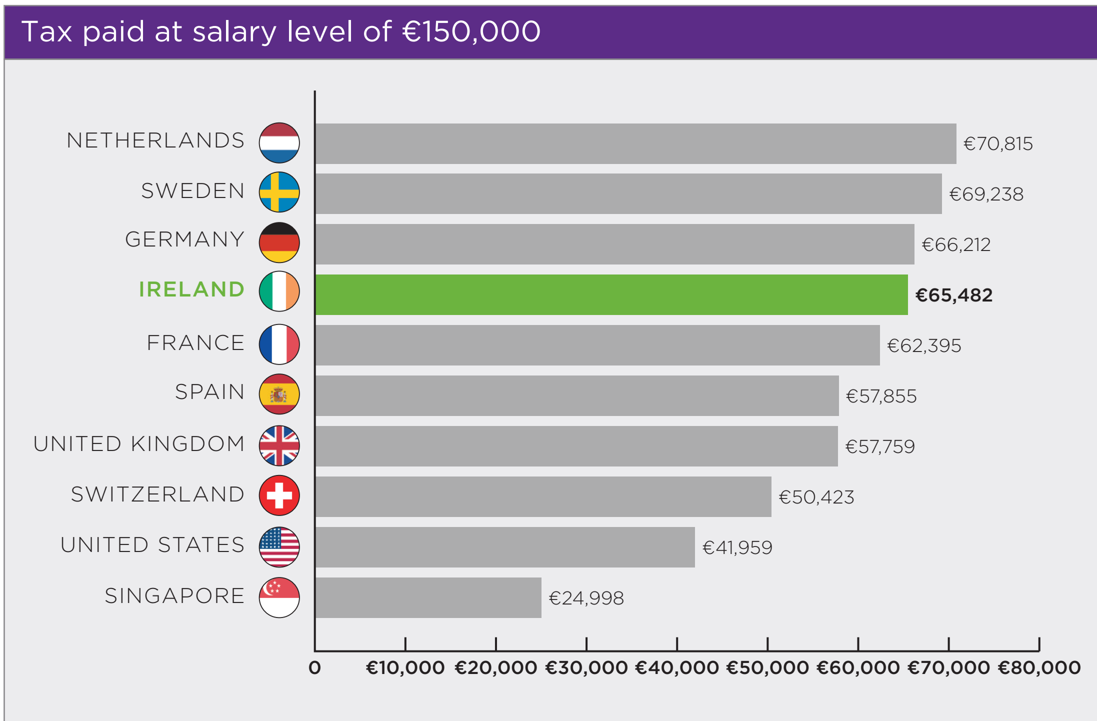
1 Based on information from KPMG Ireland.


Tax paid at salary level of €35,800
GERMANY
NETHERLANDS
FRANCE
SPAIN
SWEDEN
SINGAPORE
UNITED KINGDOM
IRELAND
UNITED STATES
SWITZERLAND
€12,949
€10,476
€10,294
€8,813
€8,279
€7,654
€7,393
€6,954
€6,333
€6,040
0
€3,000
€6,000
€9,000
€12,000
€15,000


Tax paid at salary level of €55,000
GERMANY
NETHERLANDS
FRANCE
IRELAND
SPAIN
SWEDEN
UNITED KINGDOM
SWITZERLAND
UNITED STATES
SINGAPORE
€22,646
€19,926
€18,336
€16,458
€16,176
€15,732
€15,622
€13,320
€11,951
€11,062
0
€5000
€10000
€15000
€20000
€25000


Tax paid at salary level of €75,000
GERMANY
NETHERLANDS
FRANCE
IRELAND
SWEDEN
SPAIN
UNITED KINGDOM
SWITZERLAND
UNITED STATES
SINGAPORE
€32,980
€30,351
€26,905
€26,482
€26,413
€24,351
€21,920
€21,351
€18,479
€13,040
0
€5,000
€10,000
€15,000
€20,000
€25,000
€30,000
€35,000


Tax paid at salary level of €100,000
NETHERLANDS
GERMANY
SWEDEN
IRELAND
FRANCE
SPAIN
UNITED KINGDOM
SWITZERLAND
UNITED STATES
SINGAPORE
€44,351
€44,057
€40,688
€39,482
€37,759
€35,351
€32,420
€30,461
€26,958
€16,329
0
€10,000
€20,000
€30,000
€40,000
€50,000

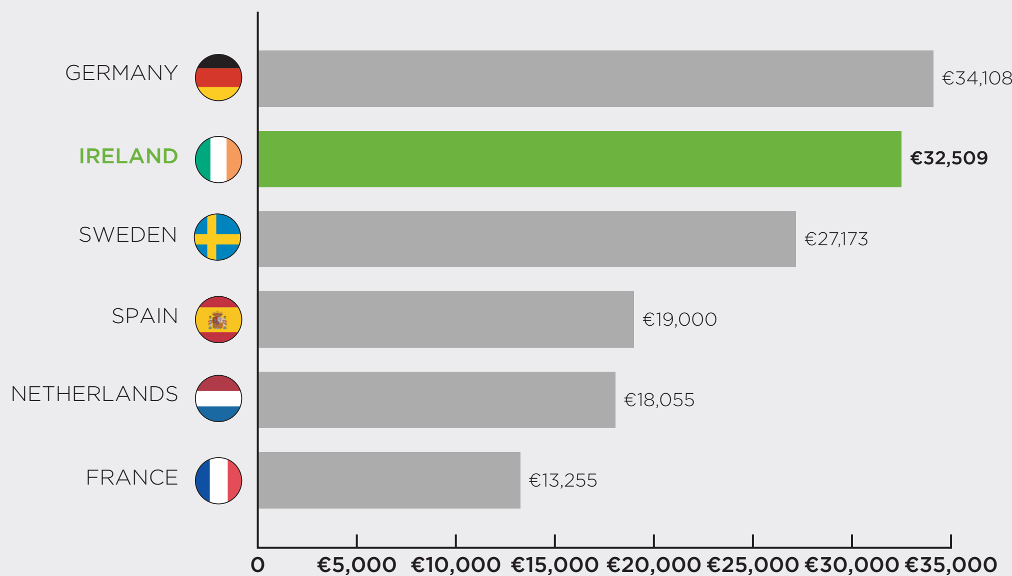

Tax paid at salary level of €150,000
NETHERLANDS
SWEDEN
GERMANY
IRELAND
FRANCE
SPAIN
UNITED KINGDOM
SWITZERLAND
UNITED STATES
SINGAPORE
€70,815
€69,238
€66,212
€65,482
€62,395
€57,855
€57,759
€50,423
€41,959
€24,998
0
€10,000
€20,000
€30,000
€40,000
€50,000
€60,000
€70,000
€80,000

Chapter 3:

Special Assignee Relief Programme (SARP)

- Many countries operate tax programmes to attract internationally sought after skilled foreign executives.
- Ireland offers an income tax relief known as the Special Assignee Relief Programme (SARP).
- SARP provides these executives with a 30% income tax exemption on salary above €75,000.
- It is available for up to a maximum of five years and certain conditions apply.
- After taking account of SARP, executives based in Ireland are only behind Germany in the global tables, while they pay over €19,000 more tax than their French counterparts.

Mobile executives in Ireland have high effective tax rates even with the SARP Programme. Tax paid at salary level of €100,000



Chapter 4:

The Complexity of Our Personal Tax Regime

Ireland's personal tax system has become increasingly complex.

Personal tax is made up of three different charges:

1) Income Tax,
2) Universal Social Charge (USC); and
3) Pay Related Social Insurance (PRSI).

Each has:

- different entry points,
- different bands and
- different credits.

A variety of rates apply:

- Income Tax has two rates
- USC has five rates; and
- PRSI has one main employee rate.

And there are differences in the definition of:

- income for Income Tax
- income for USC, and
- income for PRSI.

Employees are treated differently by the personal tax code than the self-employed.

More details on each of these taxes can be found in Chapter 11.

Moving parts in Ireland's tax system

	Income Tax	USC	PRSI
Entry Point	€16,501 (PAYE Income)	€13,001	€18,305
Rates	20% - Standard rate 40% - Marginal rate	1% 3% 5.5% 8% 11% rate for self-employed	Employee PRSI 4% Employer's PRSI 8.5% 10.75%
Bands	€16,501 to €33,800 - 20% €33,801 and above – 40% Note: These are bands for a single person	0 to €12,012 – 1% €12,013 to €18,668 – 3% €18,669 to €70,044 – 5.5% €70,045 and above – 8% €100,00 and above for self-employed - 11%	Employer's PRSI 0 - €19,552 – 8.5% €19,553 and above – 10.75%
Credits	21 main credits available for offset against Income Tax, for example; Personal Tax Credit PAYE Credit Home Carer Credit	No Credits	Tapered employee PRSI credit for income between €18,304 - €22,048
Reliefs	Various reliefs from income tax, e.g. EII investments Pension contributions	Different base from Income Tax - e.g. no relief for EII investment Pension contributions	Different base from Income Tax - e.g. no relief for EII investment Pension contributions

Chapter 5:

The Self-Employed are Treated Differently Than Employees in The Tax Code

- According to the CSO, there are almost a third of a million self-employed people in Ireland (328,500 people).
- 92,000 of these people employ staff and pay employer PRSI on their wages (in most cases this will be at the 10.75% rate).
- The majority of Ireland's self-employed are involved in the services sector which would include retail, finance professionals, IT consultants and mechanics.

Difference No. 1: The self-employed pay an extra 3% USC over €100,000

Once a self-employed person earns more than €100,000, they pay a 3% USC surcharge on income above that level, so that their marginal tax rate is 55% rather than 52%. This surcharge is currently paid by 28,700 tax cases.

Difference No. 2: The Earned Income Credit for the self-employed is less than the PAYE Tax Credit

A PAYE Tax Credit of €1,650 is available to all employees. In Budget 2016, an Earned Income Credit of €550 was introduced for the self-employed and proprietary directors. The difference between the PAYE Tax Credit and the Earned Income Credit is €1,100.

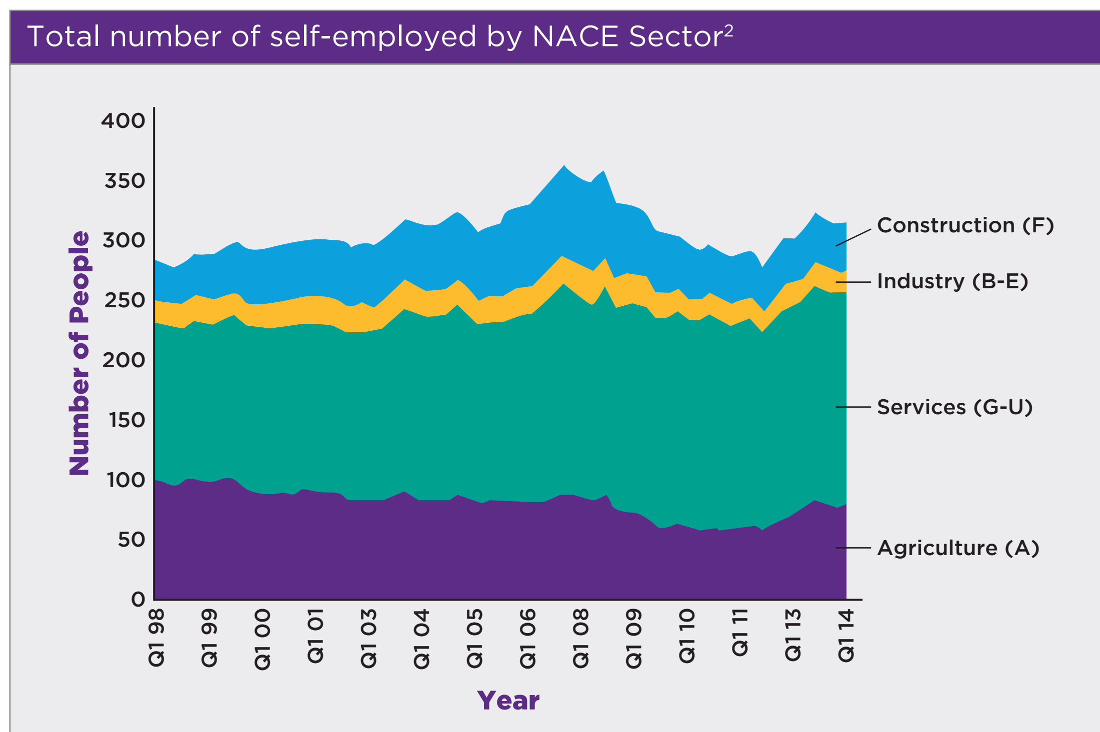
The Summer Economic Statement 2016 commits to "increasing the Earned Income Tax Credit for the self-employed to match the PAYE credit by 2018".

Difference No. 3: The "entry point" to PRSI is lower for the self-employed and they get no taper on entry

- Once their income exceeds €5,000 the self-employed pay 4% Class S PRSI.
- PAYE employees do not pay employee PRSI until their earnings exceed €18,304 (with a tapered credit up to €22,048).

- This means the self-employed have already paid €732 in PRSI before PAYE employees even start paying PRSI.
- The self-employed must pay a minimum of €500 PRSI for a year regardless of their income levels.
- These differences impact all self-employed individuals in Ireland.

Total number of self-employed by NACE Sector[2]



- In his research "Earnings and Low Pay in the Republic of Ireland", Micheál L. Collins suggests that 65% of the self-employed earn less than €25,000.
- A self-employed person earning €18,000 will pay €1,820 more in tax than a PAYE worker on the same salary.
- A self-employed person earning €150,000 will pay €2,600 more.

2 Department of Finance, Tax & Entrepreneurship review, October 2015.

Chapter 6:

Do We Have A Sustainable Tax Base?

What the European Commission says about Ireland's tax base:

"Overall, recent tax measures would not seem to be geared towards broadening the tax base"
European Commission Country Report Ireland 2016, May 2016

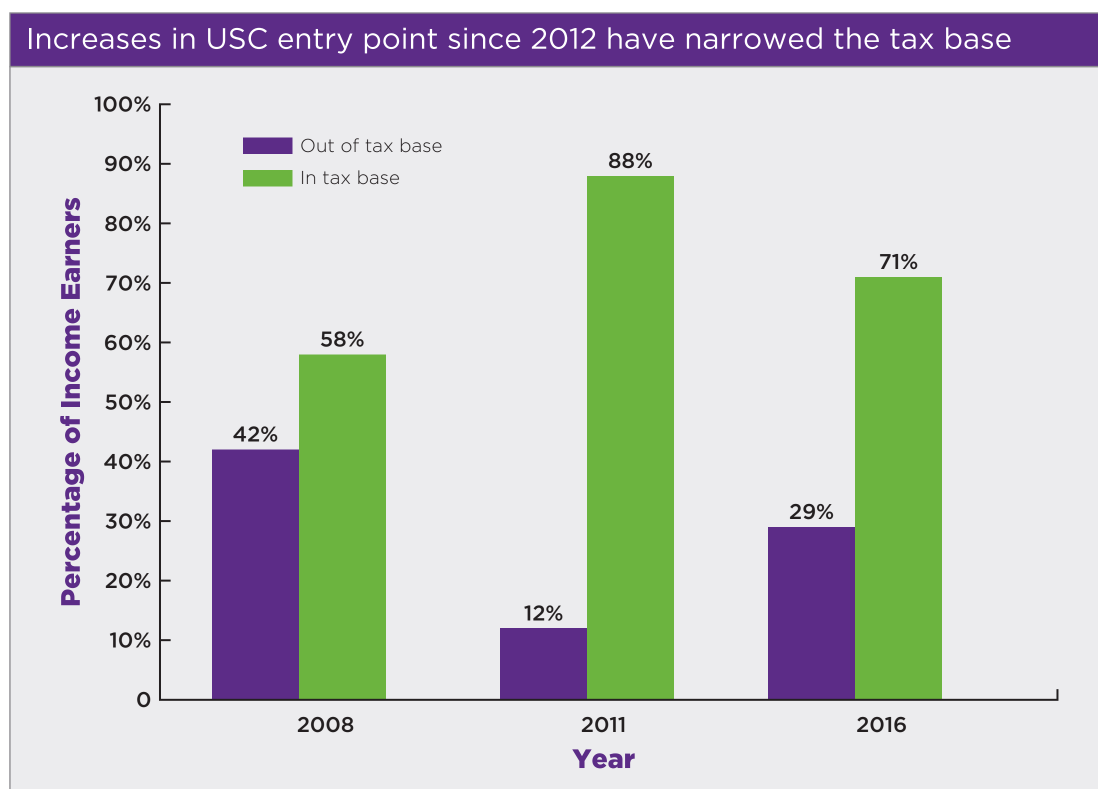
Ireland should *"reduce vulnerability to economic fluctuations and shocks, inter alia by broadening the tax base".*
European Commission Country Report Ireland 2016, May 2016

"Reducing the tax base, through for example raising the threshold for the USC, and postponing the revaluation of self-assessed property values weighs on the sustainability of revenue in the medium-term"
European Commission Post-Programme Surveillance Report, January 2016

29% of income earners are out of the personal tax net entirely

Total Income Earners	2,405,000
Number of income earners removed from the tax base in Budget 2016	42,500
Number of income earners removed from the tax base since 2012	459,500
Total number of income earners out of the tax base	703,800
% of income earners out of the tax base	29%

- A taxpayer's first point of entry into the tax system is the USC entry point.
- The higher you increase the USC entry point, the more taxpayers you take out of the tax base.



As the USC entry point increases, the tax base narrows

Year	Entry Point to USC	Number of income earners exempt from USC	% of income earners exempt from USC
2011	€4,005	259,512[1]	12%
2012	€10,037	↓	
2013	€10,037		
2014	€10,037	571,786[2]	25%
2015	€12,013	663,199	28%
2016	€13,001	703,800	29%

1 The Income tax Reform Plan notes that 12% of income earners were exempt from USC.
2 Tax Strategy Group, TSG 15/09.

Chapter 7:

Budget 2017 – The Options

Key documents on personal tax in chronological order

1. **Summer Economic Statement**

   It is estimated that €1 billion is available to provide for additional expenditure increases and taxation reductions in Budget 2017, of which circa **€330 million will be allocated to tax measures.**

2. **The Programme for Government**

   The Government has set out a number of personal tax proposals for its term of office. These include;

   - Phasing out the USC with an emphasis on low and middle income earners
   - Removing the PAYE Tax Credit for high earners
   - Increasing the Earned Income Tax Credit for the self-employed
   - Increasing the Home Carer Credit
   - Introducing a PRSI scheme for the self-employed
   - Publishing a medium-term income tax reform plan (which was subsequently published in July - referred to below)

3. **Tax Strategy Group**

   In addition to the income tax proposals referred to in the Income Tax Reform Plan (see below), the Tax Strategy Group also consider a number of possible changes to the PRSI system;

   - Introducing a new PRSI charge for low income earners to replace the USC (if phased out)
   - Extending additional social insurance benefits to the self-employed

4. **The Income Tax Reform Plan**

The purpose of the plan is to review Ireland's system of personal taxation as a whole, to consider the socio-economic impacts of personal taxation, and to examine options for future reform within the personal tax system."

Department of Finance

The Income Tax Reform Plan sets out a number of illustrative proposals which could be considered for Budget 2017. The plan is non-exhaustive and it should be noted that some of the media / political coverage of the Budget since the publication of the Plan suggests other variations may happen.

In analysing the Plan, we are strictly looking at proposals being considered for Budget 2017. These proposals focus on:

- USC reductions - three possible options have been put forward
- Tax credits - increases to the Earned Income Tax Credit and Home Carer Credit are considered

Budget 2017 – A focus on USC

USC Receipts

USC is a significant contributor to the Exchequer, accounting for 9% of total tax receipts in 2015.

Tax	Total Yield 2015 € million	% of total tax receipts in 2015
Total Exchequer Yield	45,786	100%
Income Tax	14,170	31%
USC	4,174	9%

- USC accounts for over €4bn in receipts, less than one-quarter of the total personal tax yield of €18.3bn.
- USC receipts are less than one-third of income tax receipts.
- Once an individual earns more than €13,000, they pay USC on all of their income (from the first Euro). This creates a 'step effect' of almost €150 per annum (i.e. €12,012 @ 1% plus €988 @ 3%).

USC Options In The Income Tax Reform Plan

The Income Tax Reform Plan presents some illustrative proposals which would reduce the USC burden for taxpayers. These options include:

- Reducing the USC rates
- Increasing the USC bands; or
- Increasing the USC exemption threshold

USC Option 1 Reducing Rates		
Current Rate	Possible rate post Budget 2017	Exchequer Cost
1% (on first €12,012)	0.5%	**€331m**
3% (€12,013 to €18,668)	2.5%	
5.5% (€18,669 to €70,044)	5%	

USC Option 2 Increasing Band Ceilings and Reducing the 3% Surcharge		
Current Bands	Possible bands post Budget 2017	Exchequer Cost
1% band: 0 - €12,012	0 - €18,000	**€296m**
3% band: €12,013 - €18,668	€18,001 - €21,000	
5.5% band: €18,669 - €70,044	€21,001 - €70,044	
8% band: over €70,044	8% band: over €70,044	
3% surcharge (on self-employed income over €100,000)	2% surcharge (on self-employed income over €100,000)	

USC Option 3 Increasing Exemption Threshold Under this option, the USC would in future only be calculated on the portion of income above the new €13,600 threshold. This would be different from the current system where the USC is calculated on all of a taxpayer's income (from the first Euro) where this exceeds the entry point of €13,000.		
Current Threshold	Possible threshold post Budget 2017	Exchequer Cost
€13,000	€13,600	**€297m**

The USC as it stands

Rate	Band	% of income earners	Number of income earners
Exempt	Less than €13,000	29%	703,800
1% rate	0 - €12,012	*No taxpayers pay USC at 1% only**	
3% rate	€12,013 to €18,668	19%	447,600
5.5% rate	€18,669 to €70,044	44%	1,052,600
8% rate	Over €70,044	7%	172,200
11% rate	On self-employed income over €100,000	1%	28,700

* If you earn more than €13,000, you pay USC at 1% on the first €12,012 and 3% on the balance up to €18,668.

> The top 1.2% of income earners earn 10.9% of total income and pay 22.1% of total USC to the Exchequer.

Budget 2017 – Increases in Tax Credits

The Income Tax Reform Plan also looks at increases to the Earned Income Tax Credit and Home Carer Credit in Budget 2017.

Earned Income Tax Credit **The Earned Income Tax Credit was introduced in Budget 2016 for the self-employed and proprietary directors who are not entitled to the PAYE Credit.**		
Current Credit	Possible credit post Budget 2017	Exchequer Cost
€550	€1,100	€45m

Home Carer Credit **The Home Carer Tax Credit is available to certain taxpayers who care for one or more dependent persons***		
Current Credit	Possible credit post Budget 2017	Exchequer Cost
€1,000	The Income Tax Reform Plan considers increases of between €100 - €250 in Budget 2017	
	€1,100	€6.5m
	€1,200	€12.9m
	€1,250	€16.2m

* Dependent persons are children under 16, a person aged 65 years or over, or incapacitated persons.

Chapter 8:

Share Options – The 2016 Consultation

The Programme for a Partnership Government makes a commitment to:

Explore the mechanisms through which SMEs can reward key employees with share options in a tax-efficient manner."

Why share based remuneration is important for SMEs

- Equity participation in SMEs in Ireland is low.
- But it can be a key contributor to:
  - profitability,
  - productivity and
  - employment creation.
- The result is a positive impact on economic growth and Exchequer yield.
- Ireland is falling behind competitor jurisdictions like the UK which offer a range of share initiatives for different types of business and at different stages in their development.

For SMEs with limited cash, share based remuneration can significantly reduce fixed labour costs and give them some chance of attracting key talent.

BUT

Our high rates of capital gains tax and income tax discourage participation by employees in share based remuneration schemes in Ireland.

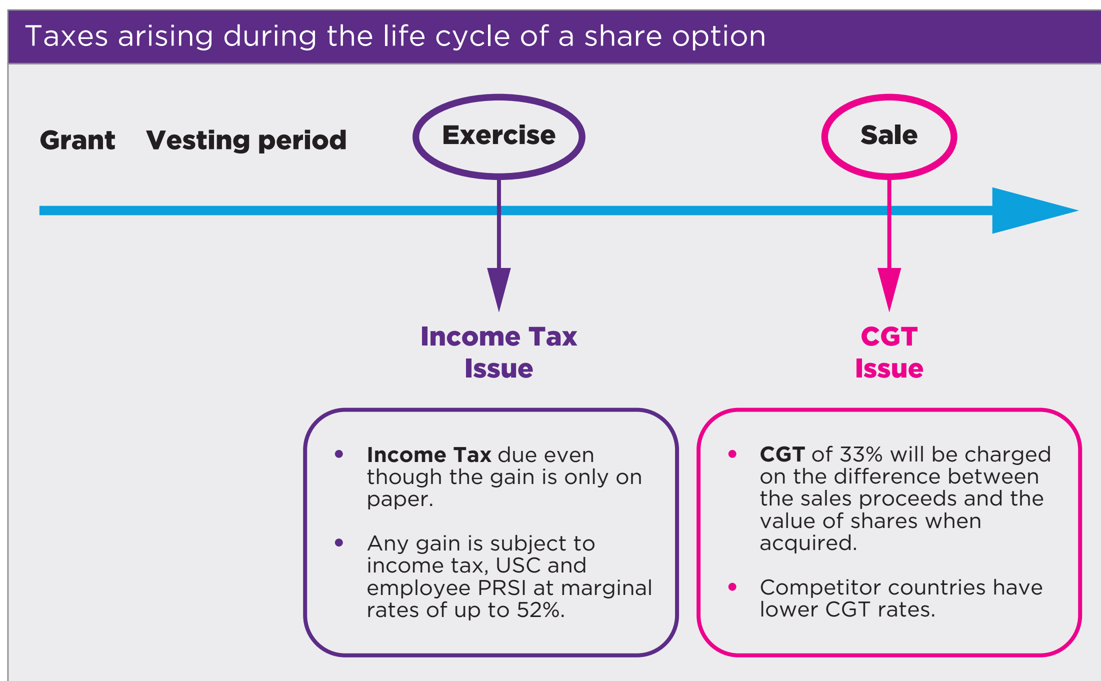
More about the problems with the current system

Approved schemes

- Revenue's approved share based remuneration schemes must be open to all employees in a company. But SME's need the flexibility to award equity to key staff on a targeted basis.

Unapproved schemes

- The employee has to pay tax on receipt of shares or on the exercise of a share option. They may have to fund this tax on a "paper gain" from their own resources or from borrowings.
- Often there is no ready market for the shares, so calculating the value of the shares and the tax due can be difficult.
- There may be no market for their shares when the employee is looking to dispose of them.
- A re-purchase of shares (buy back) by the employer can give rise to an income tax liability for the employee on disposal of the shares - higher than capital gains tax would be.



Chapter 9:

The Story of The Personal Tax Regime over The Past 15 Years

2000 – 2008: Effective rates fall

Between 2000 and 2008, a number of measures were introduced to reduce the personal tax burden for workers:

- The standard tax rate was reduced from 22% in 2000 to 20% in 2001
- The higher rate was reduced from 44% in 2000 to 41% by 2007
- The entry point into the income tax system increased from €7,238 to €18,300
- The PAYE tax credit increased in the period from €508 to €1,830 by 2008

2009 – 2014: Financial crisis triggers rate increases

The financial crisis triggered a continual increase in effective tax rates:

- In 2009, the income levy was introduced with rates as high as 6% on income over €174,000
- The rates of the health levy were doubled to 4% and 5% respectively
- Tax credits and bands were generally reduced by 10% (e.g. the standard rate band was reduced by approximately 10% from €36,400 to €32,800)
- The employee PRSI ceiling was abolished
- In 2011, the USC was introduced to replace the Income Levy and Health Levy

2015 – 2016: Personal tax burden reduces again

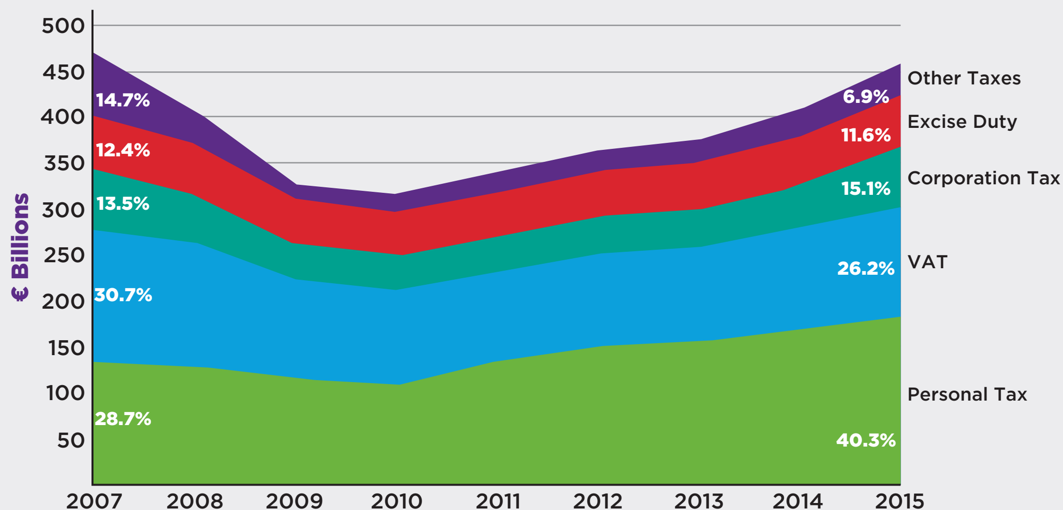
As the economy recovered, the Government sought to once again reduce the personal tax burden, particularly for low and middle income earners.

- Between 2012 and 2016, the entry point to the USC was increased from €10,037 to €13,001
- In Budget 2015, the income tax rate was reduced from 41% to 40% and the entry point to the higher rate of income tax was increased by €1,000
- An 8% rate of USC was introduced for income over €70,044, meaning that the benefit of income tax reductions was capped for income above this threshold
- In Budget 2016, the 2%, 4% and 7% USC rates were reduced to 1%, 3% and 5.5% respectively, while the latter two bands also changed. The 8% USC rate remained for those earning over €70,044

Chapter 10:

Exchequer Reliance on Personal Tax Has Increased

There has been an increasing reliance on personal taxes since 2007



Data source: Department of Finance

- Between 2007 and 2015, Ireland's tax revenue mix has changed although the overall tax yield in the fiscal years 2007 and 2015 was approximately the same.
- In 2007 and 2008, VAT was the highest contributor to the Exchequer. But in 2009, personal taxes outstripped VAT and the gap has continued to widen.
- Personal taxes now account for 40% of the total tax yield and according to the Tax Strategy Group, they are expected to generate almost €19 billion for the Exchequer in 2016.
- Personal tax receipts were €13.5bn in 2007 versus €18.3bn in 2015

"Overall net receipts [in 2015] amounted to €45.79 billion, up 10.6% on last year and 7.8% ahead of target. (This is the second highest figure for net receipts in the history of the State – only 2007 was higher, at €47.5 billion)."

Revenue Commissioners' Annual Report 2015

Chapter 11:

Facts & Figures on The Personal Tax System – Additional Information

Ireland has a very complex personal tax regime which consists of three different personal taxes – Income Tax, USC and PRSI. Each of these three taxes has different;

- **Entry points**
- **Rates and bands**
- **Credits**
- **Taxable income bases**

Each of these are considered below.

The Entry Points

Each of the three taxes have different **entry points**, meaning that you only pay that particular tax where your income exceeds certain euro thresholds;

- **Income Tax**

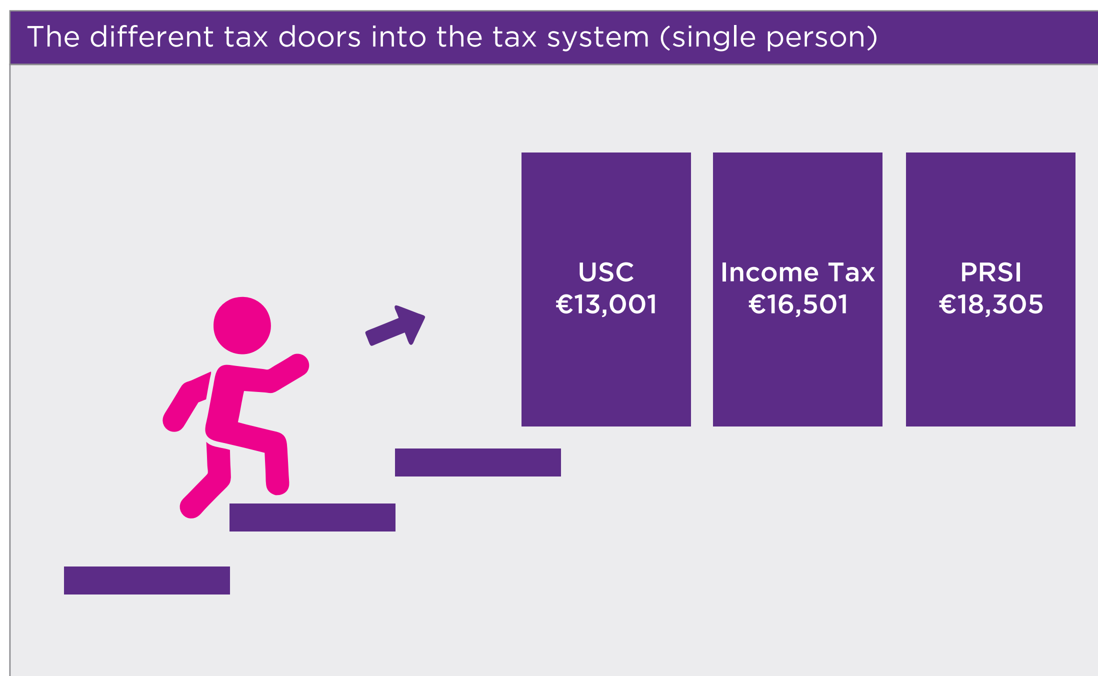
  The impact of the two main income tax credits – the Personal Tax Credit & the PAYE Tax Credit – which are available to all PAYE workers, means that employees do not pay Income Tax until their income exceeds **€16,500.**

- **USC**

  An individual is exempt from USC up to the point where they earn **€13,001**

- **PRSI**

  An individual is exempt from PRSI until they earn more than **€18,304**. (Note: For a self-employed person, the PRSI exemption is only €5,000. Once earnings go over this amount, PRSI is paid on all income and a minimum of €500 must be paid in any year.)



The rules for calculating the income subject to tax in each of the three systems

Where individuals enter each tax system, each has different rules for calculating the income subject to tax. Let's look at the rules for each;

1 Income Tax

Once an individual earns above €16,500, they will pay income tax on the income **only above this amount.**

2 USC

Once an individual earns more than 13,000, they will pay USC on all income **(i.e. from their first Euro).**

3 PRSI

Once an individual earns more than €18,304, in principle they will pay PRSI on all their income. However, since Budget 2016, there is a **sliding scale of relief** on the income between €18,304 and €22,048.

Rates and Bands

Income Tax

A single employee only pays income tax once they earn more than €16,500. Once they earn above this amount they pay:

- 20% tax on income from €16,500 up to €33,800*;and
- 40% tax on the remainder.

* This upper limit varies depending on marital and other status. See table below.

Personal income tax rates	20% on income up to	40%
Single Person pays	€33,800	Balance
Married couple (one income)	€42,800	Balance
Married couple (two incomes)	€67,600[1]	Balance
One parent/widowed parent	€37,800	Balance

USC

If you earn over **€13,000** you pay USC on all your income at the rates below:

Rate	Band
1%	All income up to €12,012
3%	€12,013 to €18,668
5.5%	€18,669 to €70,044
8%	€70,045 and above
11%	Non-PAYE income that exceeds €100,000

PRSI Rates

PRSI Rates	Income	%
Employee	All income	4%
Self-Employed	All income	4%

Credits

Income Tax - Most Common credits	
Single Person Credit	€1,650
Married Couple / Civil Partnership Credit	€3,300
Widow Person Credit	€1,650
Employee PAYE Credit	€1,650
Earned Income Credit	€550
Home Carer Credit	€1,000

1 For married couples with two earners, the first person has a standard rate band of €42,800 and the second person has a maximum standard rate band of €24,800.

PRSI – Tapered Credit

- The minimum wage rose in 2016 which increased the number of income earners in the PRSI net.
- As above, once an individual earns more than €18,304, in principle they will pay PRSI on all their income. However, since Budget 2016, there is a sliding scale of relief on the income between €18,304 and €22,048.
- Once a person earns more than €22,048, they pay PRSI on their entire earnings at 4%.

Different income bases for different taxes

The income base which is subject to each tax also differs. A number of reliefs are afforded from income tax but these do not extend to USC or PRSI. For example;

Relief	Income Tax	USC	PRSI
Pension contributions	Relief at marginal rate, subject to limits	No relief	No relief
Medical expenses	Relief at standard rate	No relief	No relief
Medical insurance	Relief at standard rate, subject to limits	No relief	No relief
Mortgage interest relief	Relief at standard rate, subject to limits	No relief	No relief
Employment & Investment Incentive	Relief for investments up to €150,000	No relief	No relief
Special Assignee Relief Programme	Relief on a portion of income over €75,000	No relief	No relief

Calculation of Marginal Tax

Tax Breakdown - the different elements for a PAYE person and a Self-employed person

The marginal tax rate is the rate at which each additional Euro earned is taxed. The marginal tax rate in Ireland varies depending on whether an individual is employed or self-employed. As mentioned above, the marginal rate comprises of three different elements – Income Tax, USC and PRSI.

Components of the marginal rate	Employed	Self-Employed
Income Tax	40%	40%
USC	8%	11%*
PRSI	4%	4%
Total marginal rate	52%	55%

* The 11% rate applies to self-employed income over €100,000

Appendix

The PRSI Credit

- On 1 January 2016, the minimum wage increased from €8.65 per hour to €9.15 per hour.
- For somebody working a 40-hour week, this equates to an annual salary of €19,032.
- Where a person earns more than €18,304, they pay PRSI at a rate of 4% on all their income.
- In Budget 2016, a tapered PRSI Credit was introduced for individuals earning income between €18,304 and €22,048 (subject to a maximum credit of €624 annually).
- The credit helps to alleviate the “step effect” for those entering the PRSI net on foot of wage increases.

Irish Tax Institute

Leaders in Tax

South Block
Longboat Quay
Grand Canal Harbour
Dublin 2
Ireland

T: +353 1 663 1700
F: +353 1 668 8387

E: info@taxinstitute.ie
W: www.taxinstitute.ie