

# Policy Briefing

There are major challenges facing Ireland in the period ahead if it is to develop a tax system that is both fair and sufficiently adjusted to the new economic realities of the 21st century.

Ireland's per capita income has risen dramatically over the past decade to a point where it is among the highest in the EU. At the same time Ireland's tax-take (p.2) is among the lowest in Europe (measured either as a percentage of GDP or GNP). As a direct consequence of this low tax-take Ireland's expenditure on social provision is also among the lowest in Europe. Consequently, the question needs to be asked: if we expect our economic and social infrastructure to catch up to the rest of Europe, how can we do this while simultaneously gathering less tax than it takes to run the infrastructure already in place in other European countries?

CORI Justice Commission believes we will never bridge the social and economic infrastructure gaps unless we gather a larger share of our national income and invest it in building a fairer and more successful Ireland. In this *Policy Briefing* we outline

lems in the Irish taxation system and suggest policy initiatives (p.7) that would make it fairer and more capable of addressing the changed realities of the 21st century.

For example, some of the unfairness of the present system could be eliminated by ensuring Ireland's top earners paid a fair share of tax (p.4). Likewise, addressing the unfairness of the present tax relief schemes which benefit those who are better off but do not benefit the State or Ireland's poorer people, would also be a step in the right direction (p.4).

Government also needs to face up to the reality that its rejection of an EU-based minimum corporation tax rate could see Ireland being forced to reduce its corporation tax rate to zero in a relatively short period of time (p.3). The consequences of such an outcome are extremely problematic in terms of ensuring fairness in society.

There are a number of other ways in which the tax-base could be broadened. We suggest that tax credits be made refundable that tax bands be broadened, that tax rates not be

ent under-declaration of taxable income be investigated more thoroughly (p.5). We also suggest there is a role for carbon taxes, windfall taxes, a site value tax and a Tobin tax as means of broadening the tax base while also making the tax system fairer (p.6).

The tendency of Government in recent years to increase indirect taxes has hit those who are poorest inordinately (p. 7) while far too little has been done to rebalance this impact. Likewise with the process of individualising the tax system which has produced a range of anomalies that are likely to have major negative impacts in any down-turn in the economy in the years ahead (p.8).

Finally, we argue for the introduction of a Basic Income (BI) system to replace the present tax and welfare systems. The present tax system is deeply unfair and biased towards the better off. A BI system has the capacity to ensure everyone pays a fair share of tax while also ensuring that everyone has sufficient income to live life with dignity. That would be a huge improvement on the present situation. We would be glad to hear of any alternative

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*Policy Briefing* is a regular publication issued by the CORI Justice Office. It addresses a wide range of current policy issues from the perspective of those who are poor and/or socially excluded. Comments, observations and suggestions on this briefing are welcome.

# Ireland's tax take among the lowest in Europe

Over recent years Ireland has evolved into a too-low tax economy. During the last year the OECD published a review of Revenue Statistics which showed that in 2002 Ireland collected a lower proportion of GDP in tax than any other country across the European Union.

Ireland's total taxation as a percentage of GDP equalled 28 per cent. This figure has fallen by more than 1 per cent since the equivalent examination by the OECD for 2001. The second lowest European figure is recorded by Portugal where 34 per cent of GDP was collected in taxes.

From an international perspective the Irish taxation burden is also seen as very low. Across the entire 30 OECD countries only Japan and Mexico possess a lower tax take. Furthermore a comparison between Ireland and the United States, traditionally seen as a very low tax economy with limited social care policies, reveals that US taxes exceed Irish taxes. The US tax take equals 28.9 per cent of GDP in 2002, almost 1 per cent higher than the corresponding Irish figure.

As there is some argument for calculating Ireland's tax burden using GNP these results

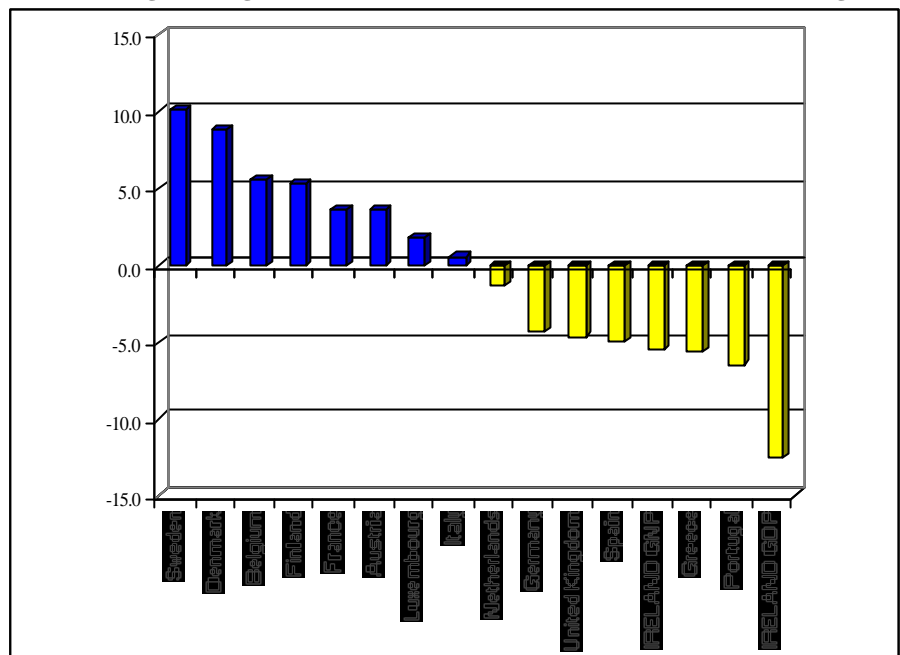
have also been presented in the above chart and in table 1. When compared to the EU average tax burden of 40.5 per cent both figures indicate that Ireland's taxation rate is at least 5.5 percentage points below the EU average.

In the context of these figures, the question needs to be asked: if we expect our economic and social infrastructure to catch up to that in the rest of Europe, how can we do this while simultaneously gathering less taxation income than it takes to run the infrastructure already in place in those other European countries?

Simply, we will never bridge the social and economic infrastructure gaps unless we gather a larger share of our national income and invest it in building a fairer and more successful Ireland.

Small increases in taxation are cer-

Percentage Divergence in National Taxation levels from the EU average



tainly feasible and are unlikely to have any significant negative impact on the economy. An increase of just one per cent in the GDP to tax ratio (from 28.0 to 29.0) would produce an extra

increase our tax burden towards the levels of some other States in Europe". CORI Justice Commission has been to the fore in calling for this change. Continually we have stated that, in

## *we are a "too-low-tax economy" and the effect of this phenomenon continues to have visible and expensive social and economic repercussions*

recent years, Ireland has evolved into a too-low tax economy where the tax burden is such that it is incapable of adequately supporting the economic, social and infrastructural requirements necessary to complete Ireland's convergence with the rest of Europe.

€1.3bn each year in taxation income for the government.

Were Ireland to increase its total taxation levels to that of the UK (from 28.0 to 35.9), a country hardly regarded as being high tax, the exchequer would have an additional income each year of €0.2bn.

In Budget 2004 the Minister for Finance questioned "those who mistakenly call for us (the Government) to

increase our tax burden towards the levels of some other States in Europe".

Ireland may wish to retain its international position as a "low tax economy" but currently we are a "too-low-tax economy" and the effect of this phenomenon continues to have visible and expensive social and economic repercussions.

Table 1: Total tax revenue as a % of GDP, for EU Countries in 2002

Country	% of GDP	Country	% of GDP
Sweden	50.6	Netherlands	39.3
Denmark	49.4	Germany	36.2
Belgium	46.2	United Kingdom	35.9
Finland	45.9	Spain	35.6
France	44.2	<b>Ireland GNP</b>	<b>35.0</b>
Austria	44.1	Greece	34.8
Luxembourg	42.3	Portugal	34.0
Italy	41.1	<b>Ireland GDP</b>	<b>28.0</b>



# Tax Relief Schemes: the cost and who gains?

The tax system incorporates a sizeable number of tax expenditures, primarily in the form of tax reliefs. The scale and distribution of these expenditures is of interest.

Table 2 outlines some of the major tax expenditures and the cost of providing them per annum. The cost of these schemes is calculated in the amount of tax revenue foregone (i.e. not collected).

A recent Eurostat (2003) report points out that the Department of Finance is unable to provide details and costs for some of the tax expenditure schemes due to the fact that some of these reliefs are provided without any requirement for formal reporting (stallion stud fees etc).

The distribution of these tax expenditures is primarily in the direction of the better off elements of Irish society. To take one example, the National Economics and Social Council recently examined which households in

the income distribution gained as a result of tax relief on employee's occupational pensions during 1998.

The results of that study found that the bottom 20 per cent of households received zero per cent of the relief. Overall the bottom 50 per cent of households received just 4.6 per cent of the value of the relief.

This contrasts to the 56.8 per cent received by the top 20 per cent and the fact that over one third of all the relief

(36 per cent) flowed to the ten per cent of Ireland's households with the highest incomes.

CORI Justice Commission believes that serious questions need to be raised about the appropriateness and distribution of some of these reliefs. In particular we need to consider if the value of some of these reliefs could be spent in a more beneficial way. The tax system should not have an inbuilt bias in favour of those who are better

**Table 2: The annual cost of income tax allowances and relief's.**

	No's availing	Cost in €m's
Capital allowances	n/a	1649
Exemption of Pension Fund Income SSIA scheme	n/a	1274
Employers Pension Contributions	1,170,200	525
Employees Pension Contributions	n/a	645
Resort Relief	n/a	456
Mortgage Interest Relief	n/a	106
Self Employment Pension Contributions	462,000	205
Medical Insurance Relief	104,500	170
Employee Expenses	533,000	160
Artists Relief	856,900	61
	941	30

## Ireland's top earners pay little tax

One of the central tenets of any taxation system is that it should be progressive. This means that as a person's income increases they should pay more tax. To assess the success of a country's taxation system in achieving this we can examine effective tax rates. A person's effective tax rate is the percentage of their income which they pay in taxation.

The suggestion that it is the better off who principally gain from the provision of tax exemption schemes is underscored by a report published by the Revenue Commissioners entitled *Effective Tax Rates for High Earning Individuals* (2002). This report provided details of the Revenue's assessment of the top 400 earners in Ireland and the rates of effective taxation they faced.

Table 3 presents their findings and shows that many of Ireland's highest earning individuals successfully use tax planning, schemes and loopholes to reduce their tax liability. The study found that property tax reliefs, such as those provided for hotels and car parks, were the most effective in reducing the tax rates of the highest earners.

CORI Justice Commission believes that many of these reliefs serve minimal societal purpose. They do, however, add substantially to the gains of the better-off. Consequently it is apparent that all these reliefs should now be reviewed via an assessment of the economic and social benefits that they provide. Only in cases where the societal benefits surpass the costs should the reliefs be retained. Furthermore we believe that any proposed reliefs should be assessed in a similar way.

**Table 3: The Distribution of Effective Tax Rates of the Top 400 Earners.**

Effective Tax Rate	% of Total
Less than 15%	18.0
15% -29%	11.2
30% -44%	57.8
45% +	13.0
Total	100.00

## Refundable tax credits

The move from tax allowances to tax credits was completed in Budget 2001. This was a very welcome change because it put in place a system that had been advocated for a long time by a range of groups including CORI Justice Commission.

One problem persists however, a problem that the old system of tax allowances also had. If a person does not earn enough to use up his or her full tax credit then he or she will not benefit from any tax reductions introduced by government in its annual budget. In effect this means that, under the present system, those with the lowest pay

will not benefit in any way from tax changes announced in the budget.

A simple solution exists to rectify this problem: make tax credits refundable. This would mean that the part of the tax credit that an employee did not benefit from would be "refunded" to him/her by the state.

The major advantage of making tax credits refundable would lie in addressing the disincentives currently associated with low-paid employment. The main beneficiaries of refundable tax credits would be low-paid employees (full-time and part-time). Furthermore, when implemented in a targeted way the impact of making tax credits

refundable can be shown to result in income gains flowing exclusively to lower income households with income levels below €15,000 where there is one earner and €25,000 where there are two earners (more detail in our Social and Economic Review *Priorities for Fairness*, p62-63)

Following the introduction of refundable tax credits, all subsequent increases in the level of the tax credit would be of equal value to all employees.

The cost of this move would not be nearly as high as sometimes suggested by official sources. Targeting is the key to successful implementation.

## Lower tax rates and broader bands: who gains?

Cutting the top tax rate by one or two per cent in the next Budget will be an option open to the Minister for Finance. Similarly, the prospect of widening the current tax bands is also under consideration.

To assess the distributive impact of these two measures CORI Justice Commission recently calculated how both these measures would impact on households with incomes ranging from those dependent on social welfare to those earning €100,000 per annum.

A reduction in the top tax rate from 42 per cent to 41 per cent would result in benefits flowing only to those house-

holds with incomes in excess of €50,000. Of these it is those households with one earner who gain most. In a full year a couple with one earner earning €25,000 would gain nothing from this change while a similar couple earning €100,000 would be €27 better off.

Broadening the tax bands results in a similar inequitable outcome. If tax bands were widened by €1,000 per person (€2,000 per couple) again it is only those households with incomes in excess of €50,000 a year who gain. The contrast between the situation of a couple comprised of two earners with

an income of less than €50,000 and a similar couple with an income of €75,000 is remarkable. Under this policy the lower income couple gain nothing while the higher income couple gain €438 a year.

It is clear that future tax changes need to be carefully considered given that they possess the potential to further widen Ireland's rich-poor gap. In recent years CORI Justice Commission has continually charted the broadening of that gap due to budgetary and Government policy. If equity and fairness are the priorities then refunding tax credits must be the first priority.

## How much income is escaping the tax net?

An assessment of the Revenue Commissioners statistical reports raises some interesting issues surrounding the entire structure of Ireland's income tax system and in particular suggests that a sizeable amount of income is escaping the tax net.

The latest report available is for the tax year 1999/2000 and it records that: 70,874 people declared incomes between €35,000 and €40,000; 88,411 people declared incomes between €40,000 and €50,000; 47,489 people declared incomes between €50,000

and €60,000; 37,027 people declared incomes between €60,000 and €75,000; 23,340 people declared incomes between €75,000 and €100,000; 12,580 people declared incomes between €100,000 and €150,000; and 9,891 people declared income in excess of €150,000.

Included in these figures are many married couples with two incomes being assessed jointly for taxation purposes. Discussing these figures, Fintan O'Toole contrasts them with the high numbers of new car sales, luxury car sales (13,749 new BMW's

and Mercedes in 1999 and 2000), credit card transactions and average total salaries of households with two public sector incomes (*After the Ball* p130-135).

Simply put, these figures suggest there is a large amount of income still being hidden. Much work is required to ensure that this situation is addressed and that people pay their fair share.

If we are to have a fair tax system then it is essential that those who have more pay more in taxation while those who have less pay less.

# Broadening the tax base: four approaches

## Carbon taxes

In recent years the sheer increase in the volume of economic activities has often negated regulatory gains. A key step would be to include in prices – and thereby internalise – the environmental costs occasioned by economic activity. It is difficult to devise any methodology capable of tracing and attributing with any accuracy all the costs/damage wrought upon the environment by a particular activity. Thus in many cases the internalisation can be achieved only in an arbitrary way, i.e. by taxes/charges based on broad national assessment.

The success of the plastic bag tax in reducing consumption of bags by 95 per cent in its first year while simultaneously raising €1m for environmental projects highlights the benefits of these types of taxes. CORI Justice Commission welcomed the Budget 2003 commitment by government to impose carbon taxes and awaits their introduction. Assessments of Ireland's Kyoto requirements make clear that Ireland should now follow other EU countries, such as Denmark, France and Germany, and introduce carbon taxes. CORI Justice Commission believes that such taxes can be introduced in a manner that will simultaneously benefit the environment without compromising business competitiveness and without undermining the economic position of low income families.

## Site value taxes

A site value tax is a tax on the annual rental site value of land. The annual rental site value is the rental value which a particular piece of land would have if there were no buildings or improvements on it. It is the value of a site, as provided by nature and as affected for better or worse by the activities of the community at large. The tax falls on the annual value of land at the point where it enters into economic activity, before the application of capital and labour to it.

The arguments for a site value tax are to do with fairness and economic efficiency. Most of the reward of rising land values goes to those who own land, while most of the cost of the activities that create rising land values does not. This is because rising land values - for example, in city centres or prime agricultural areas - are largely created by the activities of the community as a whole and by government regulations and subsidies, while the higher value of each particular site is enjoyed by its owner.

This means that it often pays land owners to keep sites unused in order to sell them later when (they hope) land values will have risen. In short, site value taxation would lead to more efficient land use within the structure of social, environmental and economic goals embodied in planning and other legislation

## Windfall taxes

The vast profits being made by property speculators on the rezoning of land by local authorities raises questions. In response CORI Justice Commission has suggested two approaches. In the short-term we believe that a substantial windfall tax should be imposed on the profits earned from such decisions. As rezonings are made by elected representatives in the interest of society generally, it seems appropriate that a sizeable proportion of the windfall gains they generate should be made available to local authorities and used to address the ongoing social housing problems they face.

In the longer term, we believe that a number of changes should be made to the way in which zoning decisions occur. The principal change we propose is the introduction of a law confining the rezoning of land to those lands in the ownership of local authorities. Operationally, this change would require local authorities to first purchase land (either voluntarily or compulsorily) before then proceeding to rezone it. The rezoning would then occur while the land was in local authority ownership and so the windfall gain on the land's value would be internalised to the local authority. CORI Justice Commission believes that the profit from this process should then be targeted on addressing the ongoing social housing problems being experienced in Ireland.

## The Tobin tax

Global currency trading has been increasing dramatically throughout the last few decades. It is estimated that a very high proportion of all financial transactions traded are speculative currency transactions. There is growing support worldwide for the introduction of a tax on such speculative exchange transactions. The Tobin tax, proposed by the Nobel Prize winner James Tobin, provides a potential solution.

The scope of the Tobin tax varies. Each country enacting the tax would determine its rate, but the tax range recommended to produce moderate market calming and revenue-raising outcomes is between 0.1 and 0.25 per cent. While this may seem very small to consumers, relative to VAT rates and income taxes, the impact on the margins of currency speculators would be enough to curb their activities. Furthermore, the revenue from the tax would be considerable - somewhere in the region of €50 -100 billion per year. According to the United Nations, the amount of annual income raised from the tax would be enough to guarantee to every citizen of the world basic access to water, food, shelter, health and education.

CORI Justice Commission believes the EU region should adopt policies towards the introduction of this financial speculation/trading tax.

# Main Policy Recommendations on Taxation

## CORE POLICY OBJECTIVE

**To collect sufficient taxes to ensure full participation in society for all, through a fair tax system in which those who have more, pay more, while those who have less, pay less.**

- Commit to increasing Ireland's total tax take towards the EU average. (This would not require Ireland to reach the EU average; a substantial positive impact can be achieved while remaining below that average.)
- Make tax credits refundable.
- Increase tax credits substantially so as to move towards taking the minimum wage out of the tax net.
- Integrate Family Income Supplement (FIS) with the tax system.
- Proceed with individualisation in the income tax system in a fair and equitable manner.
- Ensure that changes in the income-tax system benefit those on low to middle incomes as much as they benefit the better off in cash terms.
- Poverty-proof all budget tax packages to ensure that tax changes do not further widen the gap between those with low income and the better off.
- Increase the corporate tax rate and move to negotiate an EU wide agreement on minimum corporate taxation rates.
- Ensure that the distribution of all changes in indirect taxes discriminate positively in favour of those with lower incomes.
- Move decisively to shift the burden of taxation from income tax to eco-taxes on the consumption of water, fuel and fertilisers, as well as on the disposal of waste. In doing this, government should ensure that the impact of this on people with low incomes should not be negative.
- Introduce the promised carbon and environmental taxes.
- Develop policies which allow taxation on wealth to be increased.
- Investigate the possibility of introducing a tax on currency transactions such as the Tobin Tax.
- Investigate the possibility of introducing a site value tax. This, and the preceding proposal, could lead to substantial reductions in income tax.
- Standard rate all discretionary tax expenditures.
- Introduce a cap of €1.5m as the maximum amount of money that any individual can have in their pension fund. Introducing this policy would follow similar schemes adopted elsewhere, such as in the UK.
- Increase the rate of capital gains tax from 20 to 25 per cent.
- Introduce a windfall tax on the profits generated from all land rezoning.

## Indirect taxes and poverty

**I**n the last few years there has been a series of alterations to the rates of indirect taxation. Budget 2001 reduced the standard rate of VAT by one per cent while Budget 2002 and 2003 both increased that rate by one per cent.

These increases have given rise to higher prices for fuel, electricity, transport and postage while other tax and duty changes have increased the cost of cigarettes.

It is important to note that the impact of increases in indirect taxation is felt most by those who are poorest in society. Indirect taxes are a tax on consumption, and within society it is poorer people who consume the largest proportion of their income.

In future, policy reforms should ensure that the distribution of all changes in indirect taxes discriminate positively in favour of those with lower incomes.

Overall, an analysis of the impact of the present approach reflects a clear need for Government to engage in more detailed poverty proofing of their budgetary strategies.

## Basic Income and taxation

**W**e have over many years argued for the introduction of a Basic Income system to replace the present tax and welfare systems. One of the reasons we have done so is that we believe the present taxation system to be deeply unfair and biased towards those who are better off. This Policy Briefing has shown this to be the case in a variety of different ways.

A Basic Income system has the capacity to ensure that everyone pays a fair share of taxation i.e. that those who have more, pay more, while those who have less, pay less. It can do this while also ensuring that every man, woman and child has sufficient income to live life with dignity. It would ensure that an employee had a real gain from every hour they worked while also respecting the choices of those who wish to prioritise caring roles over labour force participation.

The Government's *Green Paper on Basic Income* provides a wealth of material on this issue. This should be reflected upon and developed so as to ensure our taxation system faces up to the new economic and social realities of the 21st century.

# Individualisation and the tax system

**C**ORI Justice Commission has long supported the individualisation of the tax system. However, the current process of individualisation followed by government is deeply flawed and unfair.

The cost to the exchequer of this transition has been in excess of €0.75 billion, and almost all of this money has gone to the richest 30 per cent of the population.

A significantly fairer process would have been to introduce a basic income system that would have treated all people fairly and ensured that a windfall of this nature did not accrue to the best off in this society.

Current predictions indicate that there may well be a further increase in the level of unemployment. Given the present form of individualisation, couples who see one partner lose his/her

job will end up even worse off than they would have been had the current form of individualisation not been introduced.

Before individualisation was introduced, the standard-rate income-tax band was €35,553 for all couples. After that they would start paying the higher rate of tax. Now, the standard-rate income-tax band for single-income couples is €37,000, while the band for dual-income couples is €56,000.

If one spouse (of a couple previously earning two salaries) leaves a job voluntarily or through redundancy, the couple loses the value of the second tax band.

Such an outcome is unfair and unjust. The government needs to address this and related issues to ensure a fairer tax system is developed.

**For more information on taxation reform see our website:**

[www.cori.ie/justice](http://www.cori.ie/justice)

**Taxation policy is discussed in more detail in our 2004 Socio-Economic Review, *Priorities for Fairness*.**

**CORI Justice Commission plans to advance the debate on taxation reform over the forthcoming months through further publications and a conference (details below).**

## Other Justice Commission Publications

The following documents are available for purchase from the Justice Commission Office:

- **Priorities for Fairness (Justice Commission's annual socio-economic review) - April 2004**
- **Policy Briefing on Housing and Accommodation - March 2004**
- **Policy Briefing on Work, Unemployment and Job Creation - February 2004**
- **Budget Analysis and Critique - December 2003**
- **Policy Briefing on Budget Choices - October 2003**

You may also download these documents, and many more, for free on our website.

We're on the web  
[www.cori.ie/justice](http://www.cori.ie/justice)

## Social Policy Conference 2004

CORI Justice Commission's 17th annual social policy conference will focus on taxation policy. The conference will address a wide range of issues including major challenges facing Ireland today on issues such as how the tax-base could be widened and how the tax system could promote social inclusion.

Put the date in your diary

**October 20th, 2004**