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Social Justice Ireland's Policy Research Series 2010-

Cost of making tax credits refundable would be less than 5% of Department of Finance’s estimate

Making tax credits refundable would benefit 113,000 low-income individuals in an efficient and cost-effective manner according to a new study published by Social Justice Ireland on July 5, 2010. When children and other adults in the household are taken into account the total number of beneficiaries would be 240,000. The cost of making this change would be €140m which is in stark contrast to the estimate provided by the Department of Finance to the Oireachtas Committee on Social and Family Affairs which claimed the cost would be €3,000m (i.e. €3bn).

The Social Justice Ireland proposal to make tax credits refundable would make Ireland’s tax system fairer, address part of the working poor problem and improve the living standards of a substantial number of people in Ireland.

Entitled ‘Building a Fairer Tax System: The Working Poor and the Cost of Refundable Tax Credits’, the study also raises serious concerns regarding the Department of Finance’s wrong calculations. Evidence based policy making should be based on solid evidence. The costings supplied by the Department of Finance were wrong by more than 95% so the proposal has been very badly served by poor ‘evidence’ from a source on whom we should be able to rely.

Mr David Begg, General Secretary of the Irish Congress of Trade Unions responded to the study at its launch in Buswell’s Hotel.

Details of Study

Issues addressed in this study

- The need to reform and develop Ireland’s taxation system so that it becomes fairer.
- The need to address the issue of the ‘working poor’ as so many people with jobs receive an income that is below the poverty line – one in every three households at risk of poverty is headed by a person with a job.

What is a refundable tax credit?

- When an individual’s income is insufficient to use up all of his or her tax credits, the remaining credit is paid to the individual by means of a cash transfer.
- In the present system low paid employees i.e. the working poor, lose out as they do not benefit from increased tax credits after any budget.

Making tax credits refundable: the benefits

- Would address the problem identified already in a straightforward and cost-effective manner.
- No administrative cost to the employer.
- Would incentivise employment over welfare as it would widen the gap between pay and welfare rates.
- Would be more appropriate for a 21st century system of tax and welfare.

Details of Social Justice Ireland proposal

- Unused portion of the Personal and PAYE tax credit (and only these) would be refunded.
- Eligibility criteria in the relevant year:
  - Individuals must have unused personal and/or PAYE tax credits (by definition).
  - Individuals must have been in paid employment.
  - Individuals must be at least 23 years of age.
  - Individuals must have earned a minimum annual income from employment of €4,000.
  - Individuals must have accrued a minimum of 40 PRSI weeks.
  - Individuals must not have earned an annual total income greater than €15,600.
Married couples must not have earned a combined annual total income greater than €31,200.

Data used in study

This study uses the EU Survey on Income and Living Conditions (EU-SILC), provided by the CSO.
This survey collects information on individuals’ direct incomes, social transfers, tax and social insurance contributions in extensive detail.
This study uses household income data from a representative sample of 14,634 individuals across 5,386 households in order to estimate the costs and impact of the refundable tax credits proposal.

2006 data

Cost of implementing the proposal

The total cost of refunding unused tax credits to individuals satisfying all of the criteria mentioned in this proposal is estimated at €140,051,823.

Previous estimates: In a presentation to the Oireachtas Committee on Social and Family Affairs in February 2009, the Department of Finance estimated that the cost of implementing the proposal outlined here would be €3bn

Major findings

Almost 113,300 low income individuals would directly benefit from a refund and would see their disposable income increase as a result of the proposal.
The majority of the refunds are valued at under €2,400 per annum (or €46 per week) with the most common value being individuals receiving a refund of between €800 to €1,000 per annum (or €15 to €19 per week).
Considering that the individuals receiving these payments have incomes of less than €15,600 (or €299 per week), such payments are significant to them.
Almost 40 per cent of refunds flow to low-income working poor households who live below the poverty line.
A total of 91,056 individuals (men, women and children) below the poverty threshold benefit either directly (through a payment to themselves) or indirectly (through a payment to their household) from a refundable tax credit.
Of the 91,056 individuals living below the poverty line that benefit from refunds, most (over 71 per cent) receive refunds of more than €10 per week with 32 per cent receiving in excess of €20 per week.
A total of 148,863 individuals (men, women and children) above the poverty line benefit from refundable tax credits either directly (through a payment to themselves) or indirectly (through a payment to their household). Most of these beneficiaries have income less than €120 per week above the poverty line.
Overall, almost 240,000 individuals (91,056 + 148,863) living in low-income households would experience an increase in income as a result of the introduction of refundable tax credits, either directly (through a refund to themselves) or indirectly (through a payment to their household).
Once adopted, a system of refundable tax credits as proposed in this study would result in all future changes in tax credits being equally experienced by all employees in Irish society. Such a reform would mark a significant step in the direction of building a fairer taxation system and represent a fairer way for Irish society to allocate its resources.

Conclusions

The Social Justice Ireland refundable tax credits proposal has been costed at just over €140 million. While the costs of the proposal will change in line with variations in the structure of the taxation system and the labour market, the costs are unlikely to significantly vary from this study’s findings.
The costing identified in this study, contrasts with the previously published figures for refundable tax credit systems for Ireland. The difference between these costings is significant and should raise some concern regarding the occasional updates to the costing of this proposal presented, with limited accompanying empirical detail and analysis, by the Department of Finance. Simply, evidence based policy making should be based on solid evidence and, as this analysis shows, to date the consideration of this proposal has been badly served by poor ‘evidence’.
The study demonstrates that although the costs of this proposal are small in the context of the overall taxation system, its impact is significant for low income employees and their dependents.
A further important implication of the proposal is that its implementation would mark a significant step in the direction of building a fairer taxation system where resources are more equally distributed.

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