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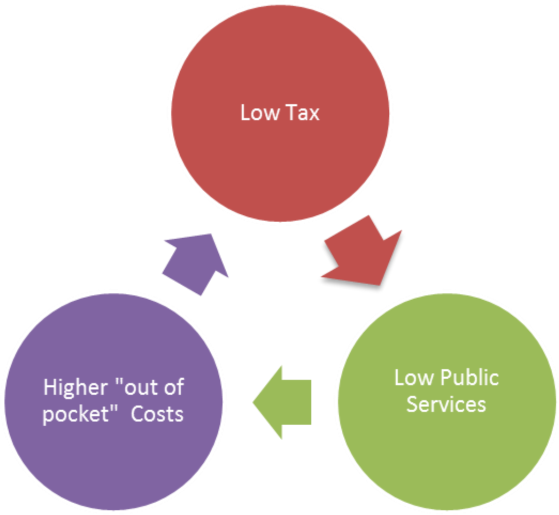
# How much tax do people pay on their incomes?

*Discussions of personal taxes in Ireland are often narrowly focused on 'headline' rates. Ireland is a low tax country and people pay much less than the headline rates. Two-thirds of income tax payers do not pay any income at the higher rate.*

### Low Tax Country

Ireland's total tax take in 2012 was only three-quarters of the EU average, at 30.2% of GDP compared to 40.7%. This is much lower than Scandinavian countries (45-50%) or France (47%)[1]. Ireland has maintained this position throughout the period of growth and collapse in the last ten years. Attempts to use GNP instead of GDP are incorrect, as all economic activity in the country is taxable.

Lower taxation means that, on the whole, lower social welfare payments and fewer public services are provided in Ireland than in many other European countries. As a result, individuals and families pay privately for services that would be public services in other European countries, and people may not see the value of Irish public services. With higher living costs, many people cannot afford higher rates of tax unless they receive more services publicly in exchange for their taxes.



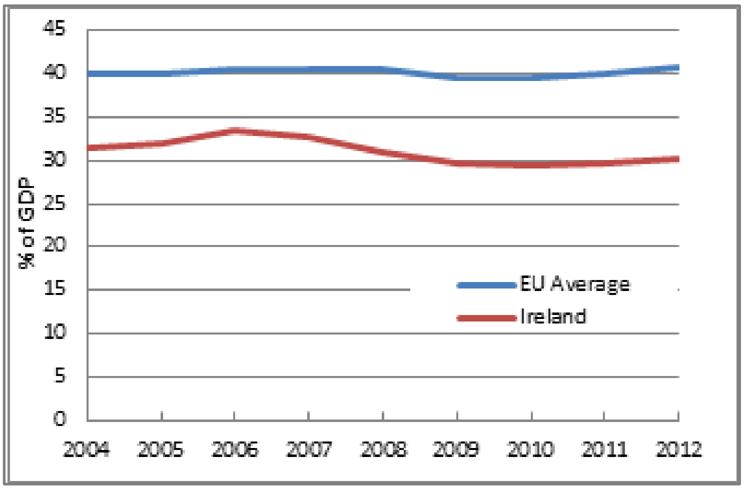




**Chart 1: Tax as a percentage of GDP[1]**

### Income Tax in Ireland

Income tax makes up 42% of the Government's tax revenue and is paid by less than 40% of the adult population[2].

Income tax also is a key feature of the economy and impacts on a number of sectors of the economy including employment levels, wages and consumption.

The income tax system in Ireland is complex, dynamic and is made up of a number of different rates, credits, bands, and reliefs.

When talking about taxes paid on people's income, social charges (USC) and social insurance (PRSI) should also be included to give a full picture of a person's contribution, although PRSI is technically not a tax because social insurance contributions are paid to the Social Insurance Fund to provide the Contributory State Pension and other entitlements.

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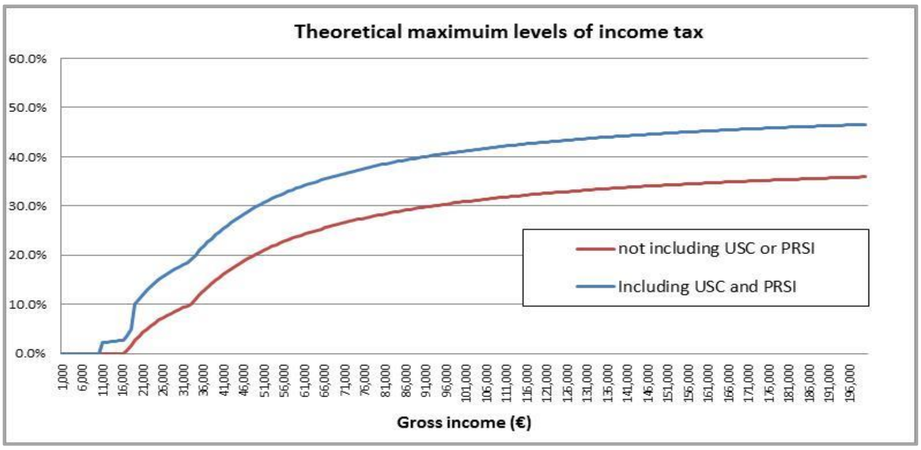


**Chart 2: Theoretical Maximum levels of personal tax[3]**

Data from the OECD shows that the 'tax wedge' on a typical family (at 6.8% of labour costs) is the second lowest in the OECD, after Chile and before New Zealand (Chart 3). The tax wedge on a single person is higher (at 26.6% of labour costs), but this is still the OECD's seventh lowest and the lowest among the OECD's EU members.[6, 7]

Chart 2 shows the theoretical maximum tax rate, for income tax alone (lower line), and for income tax, USC and PRSI combined (upper line). There is a smooth progression of maximum income tax payable as incomes rise. These taxes on income are initially more progressive as higher earners pay a higher proportion of tax, but this progressivity declines as the curve levels out.

The chart also shows that the theoretical maximum rates of income tax are far below the marginal rates. The vast majority of people pay far less than the marginal rate of 52%, which is made up of the highest rates of income tax (41%), PRSI (4%) and USC (7%) that apply to incomes above €32,800.

Also, because these are marginal rates, there is no sudden increase in tax when people move from the standard rate to begin to pay tax at the higher rate. The higher rate only applies to that part of earnings above the threshold.

Overall, personal tax and social security in Ireland is low, mainly because of low social insurance contributions. The average effective rate of income tax in Ireland (not including USC or PRSI) was just below 14% of gross income for households in 2010[4].

There is a perception that people lose 52 cents for every euro earned above €32,800. For example, this can be very visible to people in receipt of overtime payments or bonuses.

However, many workers earn less than €32,800. The CSO report average wages in Q1 2014 of €35,875 and Revenue figures show that just 38% of tax cases had gross income over €35,000 in 2011. Bearing in mind the lack of job opportunities, as well as those who cannot work due to disability or care duties, only a minority of adults in Ireland enjoy incomes above €32,800.

### Tax paid is lower than tax rates

It is sometimes argued that Ireland is unusual in having a system where workers begin to pay the highest income tax rate (41%) at less than average wage levels. However this must be understood in the context of other unusual features of the Irish income tax system.

Firstly, the Irish income tax system is highly unusual in the EU because of the very high level of tax credits, tax reliefs and tax breaks available. Secondly, Ireland is highly unusual for its very low level of PRSI, especially employers' social security contributions; effectively the lowest level of social insurance in the EU. Thirdly, Ireland's income tax system has also the relatively uncommon feature of only having two rates (20% and 41%) rather than more rates and bands.

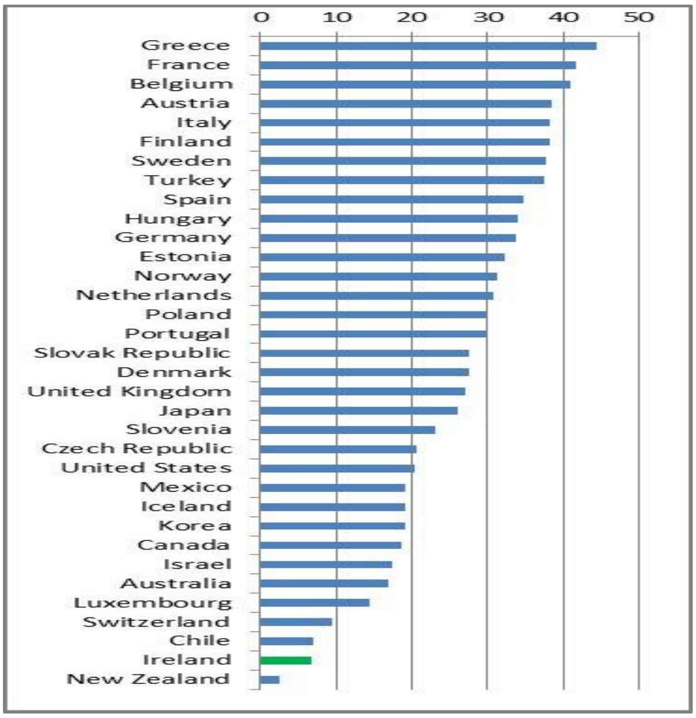


**Chart 3: 'Tax Wedge' on average earnings, single earner, married couple with two children, in OECD[6]**

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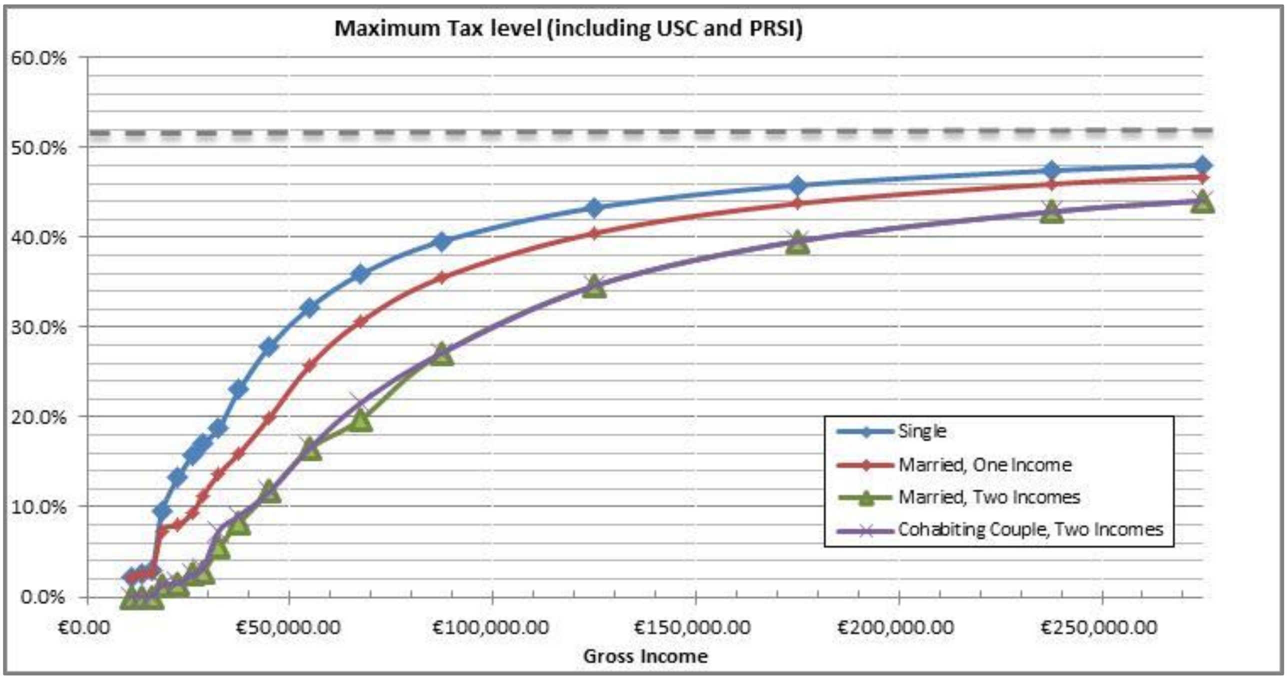


**Chart 4: Maximum Theoretical Personal Taxes – the dotted line is the 'marginal' rate for employees at 52%[3]**

### Theoretical Tax rates

Chart 2 uses the rules of the income tax system to show what the theoretical effective tax rates for different household types are when USC and PRSI are included. The dotted line represents the marginal personal tax rate for employees of 52% (income tax at 41%, USC at 7% and PRSI at 4%).

A single person who earns €37,500 is often portrayed as 'paying tax' at the marginal rate of 52%. However, Chart 2 shows us that single people on €37,500 (slightly above average wages) are only liable for a maximum of 23.2%, composed of income tax (13.8%), USC (7%) and PRSI (4%).[3]

### Actual Tax Paid

Even these maximum rates do not take into account the potential for people to use further tax breaks, which can lower the actual amount of tax paid to below the theoretical maximum.

Based on Revenue data[8] for the actual amount of tax paid by income groups and household types – and assuming no reliefs to PRSI and USC – it is now possible to see clearly the real effects of the tax system for a tax case with a gross income of €37,500.

As shown in the following tables, a single person on €37,500 pays (on average) income tax of 12.4% and his or her total taxation on income (income tax, PRSI and USC) comes to 21.6% – far less than 52%.

| Income €37,500 - Income tax only | |
|---|---|
| Headline rate | 41.0% |
| Maximum effective rate | 13.8% |
| Average actual tax paid (single person) | 12.4% |
| Average actual tax paid (all) | 8.7% |

**Table 1: Actual income tax paid on €37,500 (2011)**

| Income €37,500 - Income tax, USC and PRSI | |
|---|---|
| Headline rate | 52% |
| Maximum effective rate | 23.0% |
| Average actual tax paid (single person) | 21.6% |
| Average actual tax paid (all) | 17.9% |

**Table 2: Actual income tax, PRSI and USC paid on €37,500**

As the tables show, the average amount of tax paid by all tax units is even lower – due to the higher bands and ability to share some tax credits enjoyed by married couples who make a joint tax declaration.

*Further detail on how these calculations were made is available in O'Connor, Staunton and Sweeney (2014).*

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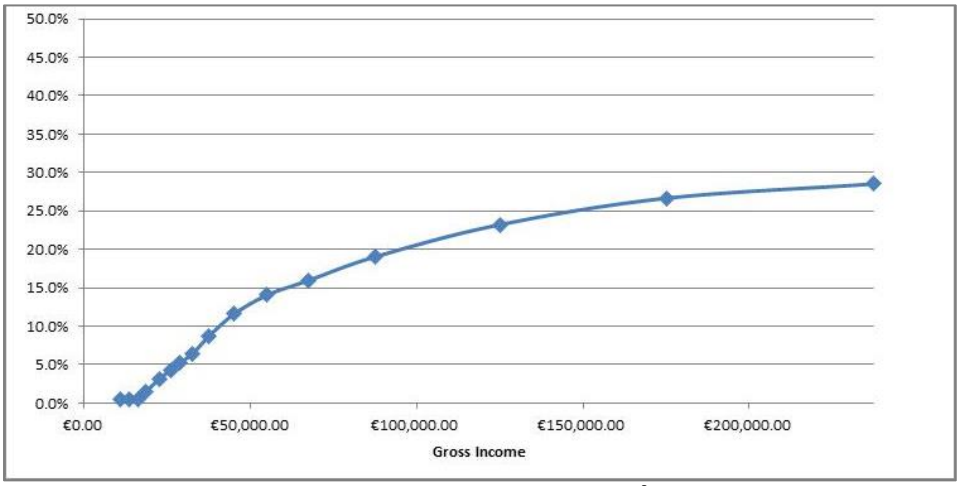


**Chart 5: Average actual income tax (only) paid by gross income[8]**

Focusing just on income tax, Chart 5 shows the stark difference between the popular perception of the onset of the higher rate (41%) and the actual amount of income tax paid.

Even a tax unit with a gross income of €237,500 pays less than 30% income tax, and this represents an individual or couple in the top 1% of income earners.

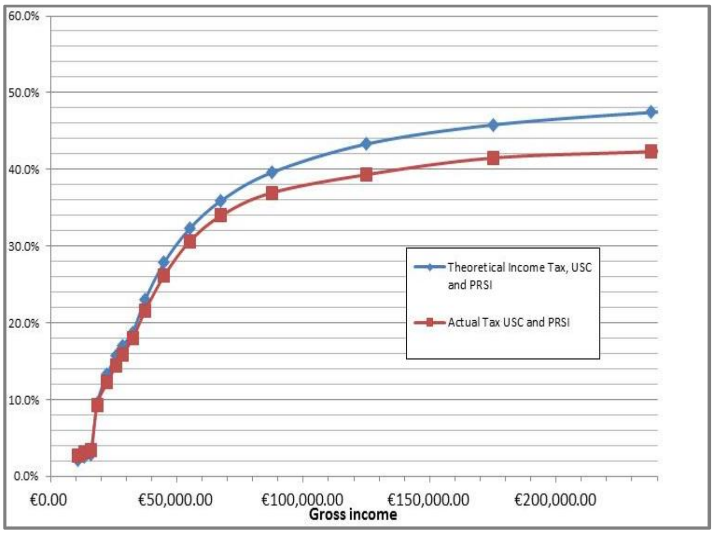


**Chart 6: Average tax paid v. theoretical maximum level – Single Person, including PRSI and USC**

In Chart 6, we show the difference between the theoretical rate and actual tax paid for a single person, which is assumed to be the value of tax breaks, which are more valuable for higher earners. This is consistent with the ESRI finding that the benefits of tax breaks accrue to top earners. For example, 80 per cent of the benefit of the tax break given to private pensions, which will cost the public finances €2,479 million in 2014, has been shown to go to the top 20 per cent of earners[9].

**Numbers paying income tax**

When estimating the impact of possible changes to income tax it is important to know how many people are likely to be affected in order to fully appreciate the distributional impacts.

Data from the 2011 census[10] tells us that there are 3.6 million adults in Ireland, and that 1.8 million are not in employment, either due to unemployment, full-time education, inability to enter the labour force or old age (although employment has risen since Census 2011).

This is a stark reminder that in Ireland the number of adults in employment is nearly matched by those who are not. Therefore any changes to the income system, such as income tax cuts, will have no direct benefit to half of the adult population.

Moreover, of the nearly 1.9 million people in employment, we see from the revenue data on gross incomes that the majority earn less than €35,000 (see Chart 7). This is an important consideration, because the cut-off point for paying the higher rate (41%) of income tax is €32,800 for a single person. The vast majority of these people will not benefit to any changes to the top rate of tax.

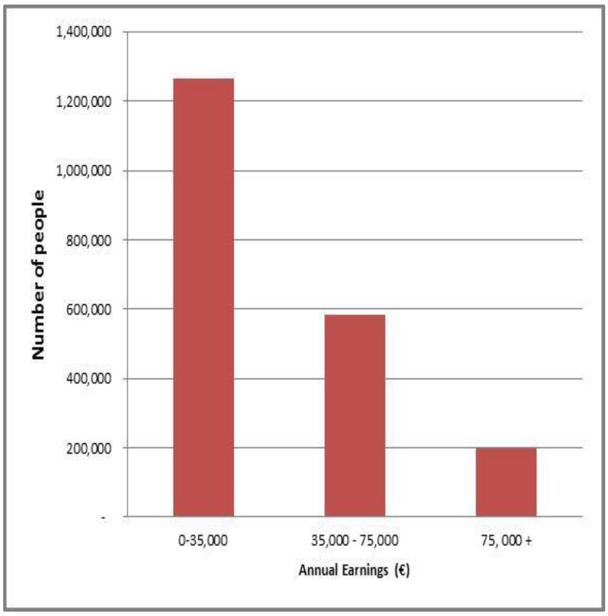


**Chart 7: Number of people by earnings cohort[8]**

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## Numbers paying higher rate tax

The point at which people begin to pay the higher rate of income tax is somewhat lower than the average level of pay, but probably not far from the median level of pay (i.e. the point at which 50 per cent of people in employment earn more or less).

Looking at the revenue data, we find that two-thirds (65%) of income tax payers do not pay any income tax at the higher rate, and 85% pay less than a quarter of their gross income at the higher rate.

Conversely, only 6 per cent of income tax payers are liable for the higher rate on more than half of their gross incomes.

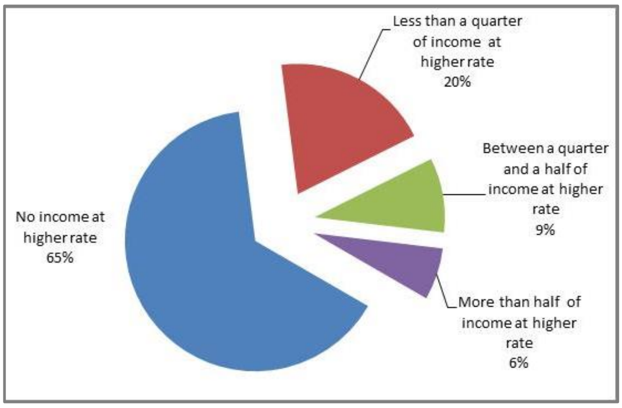


**Chart 8: How many people pay income tax at the higher rate**

From this analysis it is clear that very few people actually pay the 41% higher rate of income tax to any significant degree.

As such, rather than benefiting 'middle income earners' as some commentators have suggested, raising the onset of the higher rate of income tax, or changing the income tax bands, would disproportionately benefit higher earners.

The least inequitable income tax cut would be to provide all income tax payers with more tax credits, but even this will not benefit the lowest paid or part-time workers who do not earn enough to use up all of their credits.

## Conclusions

The current discussion about cutting income tax, especially reducing Ireland's 41% higher tax rate, has been based on incomplete data about the tax system. This brief attempts to address gaps in the analysis of Ireland's taxes on income.

Despite repeated expressions to the contrary, Ireland is a low tax country with low levels of public services. Low personal taxation and social insurance are contributing to this.

The level of tax actually paid is far lower than the headline rates, and the higher rate of income tax is neither unusual nor particularly important given that two-thirds of income tax payers do not pay anything at that rate. Table 3 below illustrates the actual income tax, PRSI and USC paid by different income groups.

The proposed beneficiaries of any changes to the higher rate of income tax are few in number and are those who already gain most from Ireland's economic system.

In order to tackle the high levels of economic inequality in Ireland, it is important that the income tax system is progressive, and can support sustainable growth and strong public services that benefit everyone.

| Gross Income | Single | Married Couple - One Income | Married Couple - Two Incomes |
|---|---|---|---|
| €11,000 | 2.6% | 2.9% | 2.4% |
| €13,500 | 3.1% | 3.1% | 2.7% |
| €16,000 | 3.4% | 3.3% | 3.0% |
| €18,500 | 9.3% | 8.1% | 7.6% |
| €22,500 | 12.2% | 9.1% | 8.4% |
| €26,000 | 14.4% | 9.9% | 9.0% |
| €28,500 | 15.9% | 10.8% | 9.5% |
| €32,500 | 17.9% | 12.3% | 10.4% |
| €37,500 | 21.6% | 14.3% | 12.1% |
| €45,000 | 26.1% | 18.3% | 14.9% |
| €55,000 | 30.6% | 23.2% | 18.1% |
| €67,500 | 34.0% | 27.8% | 21.5% |
| €87,500 | 36.9% | 32.1% | 26.5% |
| €125,000 | 39.3% | 36.2% | 32.0% |
| €175,000 | 41.5% | 38.8% | 35.9% |
| €237,500 | 42.3% | 40.8% | 37.9% |
| €275,000 | 43.2% | 42.8% | 41.0% |

**Table 3: Average level of actual tax paid by gross income band, including income tax, PRSI and USC – Data from Revenue on actual income tax paid, plus authors' calculations**

# How much tax do people pay on their incomes?

## References and Notes

[1] Eurostat Database
http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=gov_a_tax_ag&lang=en retrieved May 2014

[2] Revenue Commissioners (2014) Headline Results for 2013
http://www.revenue.ie/en/about/publications/headline-results-2013.pdf

[3] Authors own calculations, verified using the Deloitte Tax Calculator 2014, accessed June 2014: http://www.deloitte.ie/tc/

[4] Revenue Statistical Report 2011 (2012), Table IDS18
http://www.revenue.ie/en/about/publications/statistical/archive/2011/income-distribution-statistics.pdf

[5] Collins M and D. Turnbull, (2013) "Estimating Direct and Indirect Tax Contributions of Households in Ireland", NERI WP 2013/8

[6] OECD (2014) *Taxing Wages 2014*
http://www.oecd.org/tax/tax-policy/taxing-wages.htm Data from Table 0.4

[7] The ' tax wedge' is defined as the difference between the total salary costs of a single 'average worker' to their employer and the amount of net income ('take-home-pay') that the worker receives. The taxes included are personal income taxes, compulsory social security contributions paid by employees and employers, as well as payroll taxes.

[8] Revenue Commissioners, *Revenue Statistical Report* Income Distribution Statistics – data for 2011 (forthcoming). An example of earlier data from 2010 available here:
http://www.revenue.ie/en/about/publications/statistical/archive/2011/income-distribution-statistics.pdf

[9] ESRI (2009) *Pensions Policy – New Evidence on Key Issues* -
*http://www.esri.ie/UserFiles/publications/20091124152236/RS014.pdf*

[10] CSO (2012) *Census of Ireland 2011*
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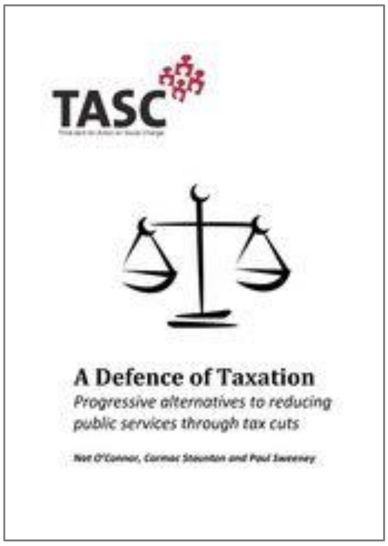
This briefing paper is based on:

Nat O'Connor, Cormac Staunton and Paul Sweeney (May 2014 ) *A Defence of Taxation*, TASC.

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