Consultation on Ireland's Personal Tax System

4 April 2023

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Executive Summary

It is critical that the personal tax system is structured in a manner that stimulates labour force participation and encourages individuals to maximise their potential (whether as employees or entrepreneurs).

It is therefore essential that an appropriate balance is struck between the generation of necessary tax revenue for the Exchequer on the one hand and ensuring that the reward for work is not diminished or eroded excessively by personal taxation. Otherwise, there is a risk of lower participation rates which would increase the welfare burden, to be financed from diminished tax resources. Also, there is an increased risk of stimulating the shadow economy.

It is also important now more than ever with the advent of remote working and greater mobility that Ireland's personal tax regime is attractive relative to what is on offer elsewhere.

In our response to Question 1, we have provided some suggestions on how the personal tax system could be reformed or enhanced, while broadly maintaining the yield and ensuring it continues to provide a sustainable and stable source of revenue to the Exchequer to fund public services. Our key suggestions are as follows:

- ✓ Base broadening
- ✓ Increase the entry point to the marginal income tax rate and introduce intermediate tax rates and bands below the marginal rate
- ✓ Remove the 3% USC surcharge to equalise treatment of employed and self-employed individuals
- ✓ Make provision for automatic inflationary increases to tax rates and bands
- ✓ Enhance tax relief for personal pension provision
- ✓ Cap earnings subject to employer and employee PRSI
- ✓ Simplify the PRSI regime
- ✓ Simplify the taxation of investments

In our response to Question 5, we have highlighted key areas in the personal tax system for future policy consideration. These are grouped under four headings:

Supporting domestic entrepreneurship

A key tenet of Ireland's tax policy should be to encourage and support domestic entrepreneurship. Given the uncertain global corporation tax landscape, it is very important that indigenous Irish businesses and entrepreneurs are supported. In this regard, we recommend the following measures:

- ✓ Enhance the Employment Investment Incentive Scheme (EIIS)
- ✓ Extend the Start-Up Relief for Entrepreneurs (SURE) to individuals who were previously self-employed
- ✓ Apply a capped 20% rate of income tax to dividends received from SMEs which exist wholly or mainly to carry on a trade
- ✓ Amend the Key Employee Engagement Programme (KEEP) to make the scheme effective

Promoting Employment

Ireland has made a virtue of having available a deep pool of highly skilled workers with an excellent work ethic. If Ireland is to retain this good standing, it will be necessary that it pursues tax policies that encourage continuous learning and development, and foster high levels of labour participation. In this regard, we propose:

- ✓ Enhancement of the SARP regime
- ✓ Tax relief for childcare expenses
- ✓ Extension of the accelerated capital allowances regimes for employer constructed creches to other investors

- ✓ Introduction of tax relief at the marginal rate for third-level qualifications in STEM (science, technology, engineering, and math), and tax relief for professional subscriptions and on continuing professional development (CPD) course costs relevant to an individual's employment
- ✓ Tax relief for certain personal wellbeing costs

Housing

The shortage of affordable residential property must also be addressed, not only for young people living here, but also if Ireland is to remain attractive for foreign investment. We have suggested a number of tax measures which should assist in the resolution of the housing crisis, including:

- ✓ Re-introduction of mortgage interest relief
- ✓ Re-introduction of a controlled and targeted Section 23 style relief
- ✓ Reform of the tax treatment of landlords
- ✓ Introduction of the rent tax credit on an indefinite basis
- ✓ Introduction of tax measures to encourage the energy efficiency retrofit of homes

Promoting sustainability

Ireland has set ambitious goals of reducing greenhouse gas emissions by 51% by 2030, and to reach net-zero emission by no later than 2050.

The personal income tax system can play a role by encouraging desirable behaviours. Some suggested measures to promote sustainability include:

- ✓ Supporting ESG investing through pension investment
- ✓ Encouraging rural regeneration by introducing incentives to encourage entrepreneurship in rural towns and villages
- ✓ Reform the TaxSaver Commuter Ticket scheme to take account of hybrid working practices
- ✓ Delay the phasing out of the BIK exemption on electric vehicles to 2030

Question 1

Do you have any suggestions on how the personal tax system could be reformed or enhanced, while broadly maintaining the yield and ensuring it continues to provide a sustainable and stable source of revenue to the Exchequer to fund public services?

We believe that reforms aimed at supporting employment are essential in ensuring the resilience and stability of our taxation system going forward. Such measures should be aimed at supporting employment by both the multinational sector with operations in Ireland and Irish indigenous companies. Ireland's personal income tax system should continue to nurture a pro-enterprise environment, while also protecting those most vulnerable within Irish society when support is needed.

Ireland's personal income tax system has two income bands and tax rates. The standard rate of 20% applies to income up to €40,000 while the marginal rate of 40% applies to income above this amount. This structure has raised a few issues with regard to fair taxation and the incentive to work or seek promotion.

Firstly, the income tax base is too narrow and highly concentrated. In 2022, the top 1% of earners paid 23% of the income tax receipts, while 34% and 28% of individual taxpayers were exempt from income tax and USC respectively[1]. Between 2009 and 2014 reforms were made to the income tax system to broaden the base, mainly through the introduction of the USC in 2011. However, this base has been eroded in the last few Budgets through the reduction of USC rates and the increase in the entry threshold[2].

Secondly, the marginal rate of income tax kicks-in at too low a level of income. According to data[3] published by the Central Statistics Office (CSO), the average weekly earnings in Ireland in Quarter 4 of 2022 was €900.26, this equates to an annual income of €46,813. This means that some of the wages of the "average" earner in Ireland are subject to the higher rate of income tax, which is set at a relatively low entry level compared to competitor jurisdictions. For example, the 40% rate applies in the UK to incomes in excess of approximately €56,500.

Thirdly, there is a cliff edge effect due to the application of only two bands and rates. Therefore, a move from €40,000 to €40,001 means that the income tax rate doubles on each additional euro earned. Irish taxpayers are paying income tax at the top rate even before they earn the average wage.

We have identified below the areas where reforms are required to ensure that the income tax system supports and promotes employment and enterprise while also ensuring that everyone contributes to the Irish economy.

Base broadening

The data published by the Revenue Commissioners in connection with Budget 2023[4] demonstrates that personal tax is applied to a narrow base of taxpayers and is heavily concentrated on a relatively small number of individuals.

For 2023, it is projected that the top 25% of income earners will pay 82% of the total income tax and USC payable for 2023. Also, it is projected that the top 1% of earners will pay 22%

[1] Tax Strategy Group Paper: Income Tax (22/02): b4d0165d-044f-4b22-893c-7be810701352.pdf - https://www.gov.ie/

[2] The entry threshold for USC was increased from €10,036 to €12,012 in Budget 2015 and then subsequently increased to the current threshold of €13,000 in Budget 2016: https://www.gov.ie/pdf/?file=https://assets.gov.ie/231219/b4d0165d-044f-4b22-893c-7be810701352.pdf#page=null

[3] CSO: https://www.cso.ie/en/releasesandpublications/ep/p-elcq/earningsandlabourcostsq32022finalq42022preliminaryestimates/

[4] Revenue Ready Reckoner – Post Budget 2023: https://www.revenue.ie/en/corporate/documents/statistics/ready-reckoner.pdf

of the total income tax and USC payable for the period.

Since 2012[5], proportionately fewer people have been required to pay income tax in Ireland. Data from the most recent Budget 2023 shows that 34% of income earners were exempt from income tax in 2022.

It has now reached a point where there is an overreliance on a relatively small share of the population to fund a very significant proportion of the annual tax take. As observed by the Parliamentary Budget Office in 2021[6], a potential fiscal vulnerability arises from the high degree of concentration in the proportion of taxpayers paying income.

In our view, it would be prudent to undertake a review to assess whether any steps need to be taken in the medium term to broaden the base of taxpayers liable to pay personal tax.

Increase the entry point to the marginal income tax rate and introduce additional tax rates and bands between the standard and marginal rates

The Irish personal tax system imposes a high personal tax burden on employees and business owners / entrepreneurs.

While our dual rate income tax rate system is one of the reasons why Ireland has one of the most progressive income tax systems in the EU and OECD, that progressivity comes at a price. The entry point to the higher 40% income tax band, at a level of income that is lower than the average wage, discourages labour force participation and the desire of individuals to upskill and seek out higher paying jobs. It also has a negative impact on employers seeking to attract high-value talent to move to Ireland, particularly with the increase in popularity of remote working.

We strongly advocate the introduction of intermediate tax rate bands that would sit below the 40% rate and which would allow the entry point for the 40% rate to be increased. Individuals earning just over €17,500[7] or €40,000[8] currently experience a very sharp rise in their tax liability when their income exceeds those thresholds.

The 3% USC surcharge should be removed to ensure equal treatment between employed and self-employed individuals

It is also important that the tax treatment of different categories of income earners are aligned. An employee is subject to a marginal income tax rate of 52% on income above €100,000, while a self-employed individual is subject to a 55% income tax rate due to the 3% USC surcharge.

There does not seem to be a policy rationale for this difference in treatment. Accordingly, the 3% USC surcharge that applies to non-PAYE income above €100,000 should be abolished, in line with the Programme for Government[9], particularly as Ireland seeks to position itself as a place for enterprise and entrepreneurship in the short to medium term.

Make provision for automatic inflationary increases to tax rates and bands

According to the inflation figures published by the Central Statistics Office, prices rose by 7.8% in the year to January 2023[10]. While some of this increase in prices may be short-term in nature due to the geopolitical landscape, it seems clear that inflation will remain an issue for the economy for the medium term.

Rising inflation has and will continue to hinder the ability of businesses to provide employment and the purchasing power of an individual's income. Therefore, it is important that there is an automatic statutory mechanism to provide for an automatic increase in tax reliefs, bands and credits. The UK introduced a mechanism in 1977, the "Rooker-Wise amendment" - to provide that the main personal allowances and income tax

[5] It is projected that 28% of earners will be exempt from USC in 2022, versus 27% in 2012 (Income Tax TSG Paper, 2022)
[6] [Parliamentary Budget Office – An Assessment of the Resilience, Sustainability and Vulnerabilities of the Irish Tax Base – Publication 26 of 2021 (oireachtas.ie)]
[7] Income level at which an individual starts paying tax at the standard income tax rate of 20%.
[8] Income level at which the marginal tax rate of 40% applies.
[9] Programme for Government – Our Shared Future: https://www.gov.ie/pdf/?file=https://assets.gov.ie/130911/fe93e24e-dfe0-40ff-9934-def2b44b7b52.pdf#page=null
[10] Central Statistics Office: https://www.cso.ie/en/statistics/prices/consumerpriceindex/

thresholds be increased in line with inflation, unless Parliament determines otherwise.

To maintain the real value of tax thresholds, reliefs, bands etc., we recommend that a statutory mechanism be introduced to provide for their automatic indexation to take account of inflation. This would include the adjustment of:

- Tax credits and standard rate cut off bands
- USC and PRSI thresholds
- Other income tax allowances and exemption thresholds

Enhance tax relief for personal pension provision

In 2022, the CSO reviewed the extent of personal pension coverage[11] in Ireland. They found that 66% of persons in employment in Quarter 3 of 2022 had some level of occupational or personal pension coverage. Worryingly, 33% of the National workforce had no pension arrangements in place.

In 2020, the Interdepartmental Pensions Reform & Taxation Group carried out an extensive review of the pension regime and pension savings to address income adequacy in retirement. According to their report[12], the State's policy objectives regarding supplementary pensions are not being achieved. In 1998, the Pensions Board in the National Pensions Policy Initiative Report recommended that 70% of the workforce should have a supplementary pension with an income target of 50% of pre-retirement earnings[13].

This is particularly worrying as it suggests that there will be a significant level of dependence on the State pension by our aging population in retirement. There is a need to both encourage increased pension coverage and increased pension saving if we are to meet the objective that 70% of the workforce should have a supplementary pension with an income target of 50% of pre-retirement earnings. Failure to meet this objective will inexorably lead to overdependence on the State pension and welfare provision.

While the planned Government Auto-Enrolment Retirement Savings Scheme should help to increase the level of pension coverage, the existing limitations on tax relief for personal pension contributions make it difficult to achieve a meaningful supplementary pension in retirement.

Consistent with most OECD and EU countries, Ireland provides fiscal support for private pensions by way of tax relief. Relief is in the form of an 'Exempt, Exempt, Taxed' system of pension taxation where tax relief is provided on contributions, the investment returns on pension savings are not taxed, while actual pension drawdown is taxed at the individual's marginal tax rate. In this regard, our pension relief system should not be considered a tax expenditure over its full lifecycle, but rather a deferral of taxation with all contributions and investment returns ultimately taxed on drawdown (with the exception of the permitted tax-free lumpsum of up to €200k).

We have made a number of recommendations below that should help enable the ambition set out in the National Pensions Policy Initiative Report to be met and help to alleviate the risk of overdependence on State pension provision.

Increase the pension contribution limit

Currently, the amounts an individual can contribute to their combined pension schemes in any one year is determined by the individual's age and their yearly salary / earnings, capped at €115,000.

This system does not take into consideration the changes in an individual's work patterns over their working life. Individuals are now more likely to transition between a higher number of occupations and periods of training and development over their lifetime, which can result in volatility in an individual's earnings.

As a result of this shift in working dynamics, we advocate that the design of the limits placed on tax relief for funding pensions takes a whole of working life approach – supporting provision early in the working life as well as in a 'lumpy fashion'

[11] Key Findings - CSO - Central Statistics Office - https://www.cso.ie/
[12] Report of the Interdepartmental Pensions Reform & Taxation Group, prepared by the Interdepartmental Pensions Reform & Taxation Group, November 2020
[13] National Pensions Policy Initiative Report of The Pensions Board to the Minister for Social, Community and Family Affairs untitled (pensionsauthority.ie)

throughout the working life as the individual's financial resources allow.

This could be achieved by increasing the tax relief available for contributions and allowing for the carry forward of unused annual tax relief for contributions to accommodate 'lumpy' payments.

Indexation of the earnings limit and standard fund threshold

The earnings limit is €115,000 and has been set at this level since 2011[14]. In addition, the standard fund threshold (SFT), which is currently set at €2 million has been at this level since 2014[15]. Given the increases in wage levels and the standards of living in Ireland, it is necessary that these limits be indexed to maintain the real value of the reliefs and thresholds.

To help achieve this, we recommend that at a minimum the SFT and earnings limit be indexed to wage growth to preserve the level of reliefs available under the current system.

It is worth noting that the UK Government announced in its Spring Budget on 15 March 2023 the abolition of their SFT equivalent, the Lifetime Allowance (LTA)[16], from April 2024. In addition, the Annual Allowance will increase from £40,000 to £60,000 from 6 April 2023.

It is important that these limits be set at levels which enable individuals to adequately provide for themselves in retirement. Ultimately, this should reduce the dependence of those individuals on the State when they retire.

Introduce tax relief for spousal contributions

At present, an individual is only entitled to income tax relief in respect of pension contributions made to their own pension scheme or arrangement. To increase pension coverage, consideration should be given to the introduction of tax relief for contributions made by an individual to the pension scheme or arrangement of their spouse or spousal equivalent.

For example, where the annual income of the spouse (or spousal equivalent) does not exceed €31,000[17] (e.g., where a spouse has taken on a role as an unpaid care giver), it should be possible for the other spouse to obtain tax relief for pension contributions made on their behalf.

Simplify the PRSI regime

In our view, consideration needs to be given to the impact of increasing social insurance contributions on the marginal rate of tax for employees and the self-employed, and on the cost for employers of employing people in Ireland.

In addition, the existing structure of the PRSI regime is very complex and needs to be reformed. Currently, there are 11 PRSI classes covering five different headings, making it difficult for individuals to understand which rate applies to their income.

Our recommendations are as follows:

Cap social insurance contributions

PRSI is a very significant cost of employment for employers. In many competitor countries, the level of earnings upon which a social insurance charge is imposed is capped. For example, Austria, Canada, Germany, Greece, Luxembourg, and the Netherlands apply a monetary cap on contributions. In addition, some countries[18] provide for an income tax deduction for employee social security contributions.

We recommend that steps be taken to reduce the cost of employment for employers by:

- Capping the earnings base subject to employee's PRSI at €75,000
- Capping the earnings base subject to employers' PRSI to €100,000.

Reduce the number of PRSI classes

Consideration should be given to streamlining PRSI by reducing the number of PRSI classes. This would make it easier for individuals to determine their PRSI liability and understand the PRSI benefits available to them.

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[14] The earnings limit was €254,000 in 2006, €262,382 in 2007, €275,239 in 2008 and €150,000 in 2009 and 2010

[15] The standard fund threshold was initially introduced in 2005 and was set at 5 million. The €2 million limit applies from 1 January 2014

[16] The LTA is currently set at £1,073,100 and is to be abolished from April 2024: Abolition of Lifetime Allowance and increases to Pension Tax Limits - GOV.UK - https://www.gov.uk/

[17] The current amount a married individual that is jointly assessed will have to earn to be entitled to the full standard rate band of €80,000

[18] Austria, Belgium, Finland, France, Greece, Italy, Japan, Luxembourg, Portugal, Sweden, Switzerland. Source: OECD: https://stats.oecd.org/Index.aspx?DataSetCode=TABLE_III1

Simplify the taxation of investments

Our personal taxes system has become increasingly complex in recent years. Over the last decade the length of the income tax return has almost doubled from 22 pages in 2010 to 44 pages in 2022.

This increase in complexity is particularly noticeable with respect to the taxation of investment products. There are too many rules covering too many different situations for too many different types of investment vehicles. There are different rules for Irish collective investment funds, Irish insurance products, European Union (EU) investment products, non-EU investment products, etc. In many cases, each individual investment product requires a deep tax technical analysis to understand how it should be treated. Then each individual investment needs to be entered in significant detail in the correct part of the investor's income tax return.

While an investor in conventional shares is entitled to tax relief for capital losses, an investor in regulated Irish and EU funds is not entitled to the equivalent loss relief. The absence of loss relief discourages investors from switching out of loss-making investments as to do so would result in the taxation of the gain required to be made on the replacement investment to make good the loss – in effect, there would be taxation without any overall economic gain.

An overhaul of the taxation of funds is necessary to ensure ease of compliance and fairness in treatment of taxpayers with respect to their investment choices. It is also important that the taxation of investments is simplified as undue complexity in this area will make Ireland unattractive for high value talent and could also act as a deterrent for those who have moved abroad and are considering a move back to Ireland.

In this regard, we welcome the Minister for Finance's commitment to establish a working group[19] to consider the taxation of investment products. We recommend that a key aim of this group should be the simplification of the tax treatment of such products given the ever-increasing popularity of retail investment globally.

[19] As noted by the Minister for Finance during his Budget 2023 speech: https://www.gov.ie/en/speech/0ed8e-statement-by-minister-donohoe-on-budget-2023/

Question 2

Does the personal tax system sufficiently support a competitive economy to incentivise and encourage work?

It is critical that the personal tax system is structured in a manner that stimulates labour force participation and encourages individuals to maximise their potential (whether as employees or entrepreneurs).

It is therefore essential that an appropriate balance is struck between the generation of tax revenue for the Exchequer on the one hand, and ensuring that the reward for work is not diminished or eroded excessively by personal taxation on the other hand. Otherwise, there is risk of lower participation rates which would increase the welfare burden to be financed from diminished tax resources. Also, there is an increased risk of stimulating the shadow economy.

Our existing personal tax system imposes a high personal tax burden on employees and business owners / entrepreneurs. The marginal cost of employment for Irish employees (and their employers) is high relative to other jurisdictions – Ireland's marginal rate of tax (including social insurance) for employees is 52%. This figure is even higher for self-employed individuals at 55%.

A key issue is that individuals pay marginal rate income tax at a relatively modest level of income. While Ireland's dual rate income tax system is one of the reasons why Ireland has one of the most progressive income tax systems in the EU and OECD, that progressivity comes at a price. The entry point to the higher 40% income tax band, at a level of income that is lower than the average wage, discourages labour force participation and the desire of individuals to upskill and seek out higher paying jobs.

Based on data and tax rates applicable for 2022, at a salary level of €25,000, the personal income tax (income tax, PRSI and USC) paid by an Irish employee is ranked third lowest among 7 leading competitor jurisdictions[20]. However, at the €55,000 salary level and €150,000 salary levels, Ireland is ranked fourth highest.

There is an opportunity to make reforms to the personal tax system to encourage individuals to fulfil their potential, whether as employees or entrepreneurs, for the benefit of the economy as a whole, including the most vulnerable in society. We would strongly advocate the introduction of intermediate tax rates bands which would sit below the 40% rate and which would allow the entry point for the 40% rate to be increased. Individuals earning just over €17,500[21] or €40,000[22] currently experience a very sharp rise in their tax liability when their income exceeds those thresholds.

We believe that such measures would encourage individuals to seek higher paying jobs by upskilling or reskilling. It would also reduce the incentive for some to participate in the shadow economy. In a study commissioned by the European Parliament in 2022[23], Ireland's shadow economy was estimated to be 10.1% of GDP in 2022 and 9.4% in 2021. Although this is lower than the EU average of circa 17.5%, it is still a significant portion of the Irish economy[24] and has an adverse impact on tax revenues.

[20] France, Germany, Singapore, Sweden, Switzerland, the United Kingdom, and the United States.
[21] Income level at which an individual starts paying tax at the standard income tax rate of 20%.
[22] Income level at which the marginal tax rate of 40% applies.
[23] Taxation of the Informal Economy in the EU: https://www.europarl.europa.eu/RegData/etudes/STUD/2022/734007/IPOL_STU(2022)734007_EN.pdf
[24] Approximately €40 billion in 2021 (9.4% * GDP of €428,318 million)

Question 3

Do you have views on the progressivity of the personal tax system?

The personal tax system is a critical driver of Irish tax receipts. In 2022, income tax and USC accounted for 37% of total tax receipts[25].

In 2018 (the latest period for which such data is available), Ireland had the most progressive system of taxes and transfers of any OECD member. Ireland also has the most progressive system of taxation of any EU member of the OECD[26].

The data published by the Revenue Commissioners in connection with Budget 2023[27] demonstrates that personal tax is applied to a narrow base of taxpayers and is heavily concentrated on a relatively small number of individuals. For 2023, it is projected that the top 25% of income earners will pay 82% of the total income tax and USC payable for 2023. Also, it is projected that the top 1% of earners will pay 22% of the total income tax and USC payable for the period.

This high level of progressivity has been a key contributor to Ireland having a more equal system as measured by our Gini coefficient. While this is important in terms of ensuring that we have an inclusive society that functions effectively, we have significant concerns that such a high degree of progressivity may not be sustainable:

- Since 2012[28], proportionately fewer people have been required to pay income tax in Ireland. It has now reached a point where there is an overreliance on a relatively small share of the population to fund a very significant proportion of the annual tax take (with 25% of individual earners projected to account for circa 30% of the total tax take across all tax heads in 2023[29] and over 9% of total tax receipts in 2023 expected to be collected from 1% of individual earners[30]).

  This gives rise to a significant structural risk for the tax system. Previous economic shocks highlight the instability that such a highly progressive personal tax system can create. Ignoring income levy receipts which applied to a much wider base, the drop in earnings by many people who had been high earners before the financial crash caused a reduction in income tax receipts from a high of c. €12.25bn in 2007 to a low of €8.6bn in 2010 (a circa 30% reduction).

- Based on data and tax rates applicable for 2022, at a salary level of €25,000, the personal income tax (income tax, PRSI and USC) paid by an Irish employee is ranked third lowest among 7 leading competitor jurisdictions[31]. At the €55,000 salary level and €150,000 salary level, Ireland is ranked fourth highest (after Germany, Sweden and France).

  This "jump" in ranking at the higher income levels is driven by the early entry into the higher 40% income tax rate band, at an income level that is lower than the average wage, leading to a squeezed middle[32]. The introduction of additional tax bands and rates

[25] Revenue Commissioners Headline Results 2022: https://www.revenue.ie/en/corporate/press-office/annual-report/2022/headline-results-2022.pdf
[26] Ireland: Government at a Glance 2021, OECD (2021): gov-at-a-glance-2021-ireland.pdf (oecd.org)
[27] Revenue Ready Reckoner – Post Budget 2023: https://www.revenue.ie/en/corporate/documents/statistics/ready-reckoner.pdf
[28] It is projected that 28% of earners will be exempt from USC in 2022, versus 27% in 2012 (Income Tax TSG Paper, 2022)
[29] Being the top 25% of earners accounting for 82% of our income tax + USC take, with income taxes + USC projected to account for 37% of the total tax take in the same period.
[30] Being the top 1% of earners accounting for 25% of our income tax + USC take, with income taxes + USC projected to account for 37% of the total tax take in the same period.
[31] Germany, Sweden, Switzerland, the United Kingdom, Singapore, France, and the United States.
[32] Middle income earners are subject to income tax rates of between 48.5% and 52%

below 40% and an increase in the entry point to the 40% band would help ease the burden for middle income earners.

- The high personal tax burden on high earners (taking account of income tax, USC and social insurance contributions) has left us with a regime that does not adequately encourage entrepreneurship and an offering that is not as attractive as it needs to be for high earners in a post-BEPS and post pandemic world.

  Given the open nature of our economy and labour market, and the ability to travel freely within the EU and to the UK, it is critically important that our personal tax system is attractive to such individuals. They play a vital role in creating job opportunities and commercial activity in the economy.

Question 4

Do you think the personal tax system operates as an effective means of income redistribution?

We consider that the personal tax system achieves a very significant level of income redistribution in Ireland.

The Gini coefficient

Most leading observers (including the OECD) measure the redistribution effect by analysing the national Gini coefficient. The Gini coefficient is a standard measure of inequality representing the income distribution among individuals or households within a given country. It takes the value of 0 when all households have identical income and 1 when one household has all the income.

Based on the data available in 2018, which formed the basis for their 2021 "Government at a Glance Report"[33], the OECD ranked Ireland 32nd out of 34 OECD members reviewed for income inequality before taxes and transfers with a Gini coefficient of 0.48 (compared to the OECD average of 0.41). This means that the distribution of income in Ireland, prior to taxes and transfers, was more unequal as compared to the other 31 OECD member countries reviewed.

However, after taxes and transfers were taken into account, Ireland ranked 15th of the 34 OECD members reviewed with a Gini coefficient of 0.29 (as compared to the OECD average of 0.31). This is consistent with research conducted by the CSO[34] and the Economic and Social Research Institute[35].

While the OECD report does not distinguish the impact of tax measures from the impact of transfers, it is clear that their combined impact results in a very significant level of income redistribution in Ireland, which is comparable with our international peers.

The tax wedge

The "tax wedge" measures the difference between total labour costs to the employer and the corresponding net take-home pay of the employee.

According to the OECD, the tax wedge in Ireland for a single individual in 2021, who was paid 67% of the average wage[36], was 25% compared to 6.2% for a single individual at the same income level with two children.

This illustrates that Ireland's personal income tax system goes a long way in redistributing income. This is achieved through income tax credits and bands. For example, a single parent is entitled to a higher standard income tax band[37] or the single person child carer credit[38] - such credits and bands assist in the redistribution of income.

Conclusion

Taxation and income transfers to the poorest segment of society are the most direct way to keep inequality in check and reduce poverty. This is very important in terms of ensuring that we have a society that functions effectively.

Looking ahead, it will remain very important to ensure that the level of income redistribution achieved by the personal tax system is at sustainable levels. In particular, it will be very

[33] Ireland: Government at a Glance 2021, OECD (2021): gov-at-a-glance-2021-ireland.pdf (oecd.org)
[34] Survey on Income and Living Conditions (SILC) 2021: https://www.cso.ie/en/releasesandpublications/ep/p-silc/surveyonincomeandlivingconditionssilc2021/income/
[35] (ESRI) (Roantree et al., 2022): Poverty, Income Inequality and Living Standards in Ireland: Second Annual Report: https://www.esri.ie/system/files/publications/JR1.pdf
[36] Set at US$50,635 / €42,813 (Average exchange rate 2021: €1:USD1.1827) by the OECD: https://stats.oecd.org/index.aspx?DataSetCode=AWCOMP
[37] €44,000 for the 2023 tax year and subsequent years
[38] €1,650 for the 2023 tax year and subsequent years

important to ensure that those who can are incentivised to work and / or engage in entrepreneurial activity.

Achieving that balance is not a simple matter. However, unless we do so, the opportunity to realise the income generation capacity of individuals in the economy will be lost which will in turn place pressure on the capacity to re-distribute to those that are vulnerable or less well off in society.

Question 5

What are the key areas in the personal tax system for future policy consideration?

Internationally mobile executives play a significant role in creating job opportunities and commercial activity in our economy. They also contribute to the pool of skills necessary for businesses to develop and compete on an international stage. It is therefore very important that Ireland has a competitive offering which can attract that talent to Ireland.

Also, the changes in the last few years in the global corporation tax landscape and the forthcoming changes with respect to the OECD BEPS 2.0 Pillar Two GloBE rules serve to re-emphasise the importance of fostering the development and growth of our domestic SME sector. This must become a key focus for Irish tax policy, both as a means of stimulating economic growth and also to maintain Ireland's reputation as an international hub for innovation and collaboration. In this regard, it is necessary to introduce targeted tax measures that encourage and stimulate entrepreneurial spirit and rewards risk.

Key factors that impact on SMEs' ability to scale and grow are access to adequate finance and a skilled workforce. These are areas where the personal income tax system can play a significant role with targeted tax incentives and reliefs. It is also necessary to adapt the income tax system to the new working patterns accelerated by the Covid-19 pandemic.

It is important that a solution be found to the housing crisis to ensure that businesses and workers are not discouraged from living here and contributing to the Irish economy.

Outlined below are various recommendations to assist in meeting these goals.

Supporting domestic entrepreneurship

While much attention is focused on how Ireland might best continue to attract international investment and remain competitive, increasing challenges in the international tax landscape serve to highlight the importance of the Irish indigenous sector.

One of the barriers to SMEs scaling their business is access to finance, particularly risk finance. Incentives have been introduced over the years to assist SMEs in this regard. However, there is more that can be done. We have outlined our recommendations below.

Simplify the Employment Investment Incentive Scheme (EIIS) to increase its uptake

EIIS is an important building block in assisting domestic SMEs to raise the capital required to grow and scale their businesses. We believe that the existing EIIS rules need to be simplified, and that greater certainty needs to be provided for companies and individuals participating in the scheme.

At present, the EIIS provisions are very complex and are difficult for start-ups to understand. The penalties for getting it wrong are material. Improving certainty for participating companies could substantially increase uptake of the relief. In this regard, we recommend that:

- The EIIS provisions be amended so that where a company has provided correct and complete information to Revenue, a confirmation that it is eligible for EIIS can be issued to the company. This would be similar to the operation of the equivalent UK EIS

(Enterprise Investment Scheme) rules.

- The holding company rules should be amended to allow for subsidiary companies in a group to avail of the relief. This would enable groups to attract minority investors into specific subsidiaries that form part of a wider group.
- The connected party rules should be relaxed in line with the UK approach of only applying them where the individual holds a 30% interest in the EIS company.

  Relaxation of the connected party rules would ensure that Ireland remains competitive in this space and would also ensure that individuals are not prevented from availing of EIIS due to unduly strict rules.

Extend the Start-Up Relief for Entrepreneurs ("SURE") to individuals who were previously self-employed

Under SURE, an individual can obtain a deduction from their total income for investments of up to €700,000 (relief provided for up to €100,000 annually) made in a qualifying new venture.

This relief is only available to previously employed or unemployed individuals. Those that were previously self-employed are unable to claim the relief. This restriction to the scope of those who can qualify for SURE acts as a significant barrier to its effectiveness in meeting its intended purpose.

We recommend that the SURE scheme be extended to include new business founders who were previously self-employed.

Limit taxation of dividends paid by active SMEs

Currently, an individual is subject to tax at a marginal rate of up to 55% on dividend income.

In an era where Ireland is looking to boost its domestic indigenous sector and position itself as a place for entrepreneurs, a 55% tax rate acts as a disincentive to invest, which is a particular concern for SMEs who experience difficulty in raising finance and attracting investors. Applying such a high rate to investment income does not reward risk appropriately.

We recommend that a flat income tax rate of 20% should be applied to dividends received from SMEs that exist wholly or mainly to carry on a trade.

Reform the Key Employee Engagement Programme (KEEP) to make it effective

KEEP is a focussed share option programme, intended to help SMEs attract and retain talent in a highly competitive labour market. One of KEEP's aims is to help level the playing field between small and large enterprises in terms of the hiring and retention of staff. However, the scheme, as currently drafted, does not properly reflect the commercial structures used by SMEs or the working arrangements of their employees.

We welcome the changes to the scheme in Finance Act 2022. However, there are a number of vital changes which still need to be made to make the scheme effective. These include:

- Making various amendments to the definitions to align the relief to the commercial structures of SMEs and working arrangements for their employees.
- Introducing safe harbour provisions with respect to the valuation of the shares and options to provide a level of assurance that a valuation will not be challenged where the requirements for the safe harbour were met.
- Increasing the annual limit of €100,000 and lifetime limit of €300,000.

Further detail on these recommendations can be found in our June 2022 submission to the Department of Finance consultation on the scheme.

Promoting employment

A highly skilled workforce is an important tenet in fostering productivity and innovation in companies, which in turn should lead to growth in the economy, increased tax revenues for the Exchequer and a more equitable society. Therefore, it is important that Ireland's personal income tax system pursues policies that encourage high levels of labour force participation, and individuals to upskill and reskill.

A talented highly skilled workforce is also a vital factor in ensuring that Ireland continues to remain an attractive location for foreign direct investment.

To achieve this objective, we have identified a number of areas where changes should be made to the personal tax system below:

Introduce tax relief for childcare costs

According to data published by the CSO[39], the female labour force participation rate stood at 58.9% in Q3 2022, an increase of 2.8% from the Q3 2019 figure of 56.1%. Some of this increase was likely driven by the changes in working patterns arising from the Covid-19 pandemic.

Notwithstanding this positive increase, female participation remains well behind that of males at 70.8% in Q3 2022. One of the barriers to increasing female participation is the prohibitive cost of childcare. We therefore recommend that consideration be given to the introduction of income tax relief for the childcare cost for children below the age of 12. This should go a long way in helping to meet the Programme for Government objective of enabling higher female labour market participation.

Increase the pool of available creche spaces by extending the accelerated capital allowances regime for employer constructed creches to other investors

The availability and cost of childcare is a barrier to female participation in the workforce[40]. There is currently a shortage of creche places in Ireland, with reports of a two-year waiting list[41].

To encourage further supply of creche spaces, we recommend that Section 843B of the Taxes Consolidation Act (TCA) 1997, which provides for accelerated industrial building allowances (IBAs) for employer constructed creches and fitness centres be extended to apply to non-employer provided creches. In addition, Section 285B TCA 1997 which provides for accelerated capital allowances in respect of plant and equipment used in employer provided creches should also be extended to non-employer run creches.

Enhance SARP and extend its scope to Irish indigenous businesses

Internationally mobile executives play a significant role in creating job opportunities and commercial activity in our economy. They also contribute to the pool of skills necessary for businesses to develop and compete on an international stage.

However, the high personal tax burden in Ireland on high earners is potentially off-putting to executives who have the choice to work in other countries. It is therefore very important that Ireland has a competitive offering which can attract talent to Ireland.

A key element of the Irish offering is the Special Assignee Relief Programme (SARP). We believe that the relief should be enhanced in a number of areas:

- Extend SARP to Irish indigenous businesses who hire from abroad. Currently, the relief only applies where an employee has worked for a non-Irish group company. Thus, SARP is not available to Irish groups who do not have foreign operations.
- Reduce the 'base salary' entry requirement from €100,000 to €50,000. This would better address situations where individuals receive variable pay such as commissions or share-based remuneration as part of their package.
- Remove the €1 million cap: the introduction of the €1 million cap on the amount of income that could benefit from the relief limits the effectiveness of the regime in attracting senior executives to live in Ireland, relative to other locations.
- For non-Irish domiciled individuals, SARP relief should be extended to include USC and PRSI as well as income tax.
- Increase the qualifying period from 5 years to 8 years for non-Irish domiciled individuals. In

[39] https://www.cso.ie/en/releasesandpublications/ep/p-lfs/labourforcesurveyquarter32022/labourforce/
[40] https://joint-research-centre.ec.europa.eu/jrc-news/increasing-early-childhood-education-and-care-participation-can-promote-womens-employment-2023-03-08_en
[41] The Independent: Parents are warned of two-year wait to secure a creche place for their child - Independent.ie - https://www.independent.ie/

addition, the CAT exclusion for non-Irish domiciled individuals should be extended to 8 years to ensure coordination between the reliefs.

Support and encourage upskilling and continuous learning by the workforce

Ireland has built its reputation as a destination for foreign direct investment on the availability of a highly qualified and engaged work force. We recommend that further steps be taken to encourage individuals to upskill:

- A key aim of the STEM Education Implementation Plan to 2026[42] is to make Ireland a leader in STEM education by 2026. It is noted in the plan that one of the ways in which this aim can be achieved is to increase the number of individuals choosing STEM subjects in further education.

  To facilitate this endeavour and to encourage individuals to continually upskill, we recommend that an uncapped income tax credit should be provided at the individual's marginal rate for the tuition fees that they incur in obtaining a third level degree (up to PhD level) in STEM subjects and other critical areas. This is an important building block in assisting Ireland to become a R&D and innovation hub.

  Currently, the income tax credit is only available at the standard rate on the course fees over €3,000 subject to a maximum of €7,000.

- Membership of professional bodies and learned societies and organisations ensure that individuals maintain and develop their skills after they qualify.

  An employer can discharge professional subscriptions for an employee without giving rise to a taxable benefit where there is a legal requirement for that membership, or the employee can prove that they cannot complete their duties without the membership. Where the individual is a member of more than one professional body, the individual is only entitled to a deduction for the membership cost of one professional body.

  The existing rules are unduly restrictive. To ensure that Ireland continues to promote the highest professional standards and facilitates continuous learning to support business, we recommend that income tax relief (including a benefit-in-kind (BIK) exemption) should be available for: (i) membership subscriptions paid to recognised professional bodies and learned societies and organisations and (ii) related CPD costs, where the membership is relevant to the individual's employment.

Introduce tax relief for certain personal wellness costs

Millions of workdays are lost on an annual basis due to absenteeism on health grounds, at a very significant cost for the Irish economy in terms of productivity and the impact on the health services. Also, multiple studies have identified strong links between wellbeing and employee retention.

For both of these reasons a greater focus on the physical and mental wellbeing of employees is needed. The requirement for a healthy workplace is no longer just a worthy ambition.

In order to promote wellbeing, we recommend that an income tax deduction should be introduced for gym memberships and the costs of attending a broader range of accredited mental health practitioners. Where the cost is met by an individual's employer, it should not be treated as a BIK.

Housing

Ireland's ongoing housing crisis creates substantial challenges for Irish society, and its timely resolution is a matter of the utmost importance for Ireland and its communities.

The availability of accommodation at affordable prices will have an adverse effect on the attractiveness of a country as a location for investment.

In addition, there is a stock of residential property in Ireland that needs to be retrofitted and renovated to help Ireland meet its ambitious climate targets. The personal income tax system

[42] https://www.gov.ie/pdf/?file=https://assets.gov.ie/249002/3a904fe0-8fcf-4e69-ab31-987babd41ccc.pdf#page=null

can play a role in this regard by incentivising property owners to take action.

Outlined below are various proposals which we believe would complement the Government's housing strategy and help improve the supply of housing:

Reinstate mortgage interest relief for first time buyers

The ESRI noted in July 2022[43] that Ireland has experienced a marked drop in homeownership rates in recent years. This has been particularly acute for younger-aged households, with the share of 25-34 year olds living independently who own their own home more than halving between 2004 and 2019, falling from 60 per cent to just 27 per cent.

Until recently, the key challenges faced by home buyers were the lack of supply and spiraling house prices[44]. However, affordability has become a pressing issue for many with the recent rapid rise in mortgage interest rates. We therefore recommend that consideration be given to the re-introduction of mortgage interest relief for home loans.

Promote greater participation by landlords in the residential property market

The pressures in the housing market are not confined to home ownership. They also extend into the rental sector where there is a lack of properties to rent with many landlords choosing to exit the sector.

According to the latest Daft.ie Rental Price Report for Q4 2022, fewer than 1,100 homes were available to rent on 1 February 2023, down almost 22% on the position one year earlier.

Therefore, it necessary to introduce measures, including tax measures, to incentivise landlords to enter and remain in the Irish rental market. We have a number of suggestions as follows:

- Reintroduce a controlled and targeted Section 23 style relief which would permit landlords to claim relief for expenditure incurred on the purchase, construction, conversion or refurbishment of a qualifying rental property against the rent received from that property and other Irish rental income. Appropriate safeguards should be introduced with respect to the size, type, quality and location of property which would qualify. Also, appropriate sunset provisions could be defined at the outset to avoid the issues which arose with the previous iteration of the scheme.

- Reform the taxation of rental income so that it is taxable under Schedule D, Case I principles (i.e., those that apply to trading income). This would allow landlords to deduct a broader range of rental expenses than is currently provided for under Section 97 TCA 1997 (including Local property tax).

- We welcome the introduction of the rent tax credit in Finance Act 2022. However, given the significant rent burden borne by many households, we recommend that the credit be made available on an indefinite basis (rather than the 2 years currently provided for in the law).

Promoting sustainability

Ireland has set itself ambitious climate goals[45] which will undoubtedly present challenges and opportunities for individuals, communities and businesses. There is an opportunity to use tax policy to encourage individuals and businesses to engage in sustainable behaviour.

We have set out some measures which we believe should be introduced to encourage sustainable behaviour:

Incentivise homeowners to improve the energy efficiency of their dwelling

As a result of both positive changes to building regulations and market demand, newly

[43] Future retirees likely to face lower homeownership which may pose challenges for retirement income adequacy | ESRI - https://www.esri.ie/

[44] According to a Daft.ie report on Irish house prices for Q4 2022 notes that over the course of 2022, the average listed price nationwide increased by 6.1% compared to a slight decrease of 1.2% during 2019.

[45] Reducing greenhouse gas emissions by 51% by 2030 and to reach net-zero emissions by no later than 2050.

constructed dwellings in Ireland are constructed to very high levels of energy efficiency. However, there remains a considerable challenge ahead to bring Ireland's older residential property stock up to comparable levels of efficiency and sustainability.

To assist with this challenge, we recommend the introduction of an income tax credit (similar to the former home renovation incentive) which would be focused on providing tax relief for expenditure incurred to improve the energy efficiency of a dwelling.

Reform the Taxsaver Commuter Ticket Scheme to take account of hybrid working practices

The TaxSaver Commuter Ticket Scheme has been very effective in persuading many employees to avail of public transport for their commute to and from their workplace.

However, since the pandemic, there has been a change in work patterns. Now many employees who previously commuted daily, engage in hybrid working practices. In many cases, it has ceased to be economically viable for a hybrid worker (who commutes part-time) to purchase a taxsaver ticket as it was designed with daily commuters in mind.

It is therefore opportune to review the scheme to see how it could be reformed to accommodate new working practices. We would suggest that an income tax deduction against total income should be introduced for an employee's cost of commuting to and from work where the individual uses public transport.

It is important that commuters continue to be encouraged to use public transport thereby assisting Ireland in meeting its climate goal of net zero greenhouse gas emissions by 2050.

Defer the phasing out of the BIK exemption for employer provided electric vehicles to 2030

Finance Act 2021 made provision for the phase-out of the partial BIK exemption for employer provided electric vehicles by 31 December 2025.

Given Ireland's ambitious climate goals, the BIK exemption should be maintained at the current level and the sunset deferred until 2030.

Increase the tax-free lump sum payable on retirement where some, or all, of the lumpsum is derived from approved ESG funds

Pension funds have the potential to exert significant influence on the businesses that they invest in to implement environmentally and socially sustainable practices.

A greater level of ESG focused investment by pension funds could be promoted by using tax policy to encourage pension funds to invest in sustainable businesses. A possible approach would be to increase the tax-free lump sum payable on retirement where some or all of the lump sum is derived from approved ESG funds, providing a strong incentive to scheme members and managers to include ESG funds in their portfolios.

Incentivise sustainable entrepreneurship in rural towns and villages

The National Development Plan 2018-2027[46] sets a national strategic objective of strengthening rural economies and communities and achieving sustainable economic and social development in these areas. The shift to remote working presents a unique opportunity for the regeneration of rural towns and villages as many people no longer need to live close to the location of their employer.

In order to harness the opportunity afforded by hybrid working, a tailored incentive should be introduced to encourage sustainable entrepreneurship in rural towns and villages. For example, an enhanced start-up capital incentive (SCI).

[46] Project Ireland 2040: National Development Plan 2018 – 2027: https://assets.gov.ie/19240/62af938dce404ed68380e268d7e9a5bb.pdf

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