

# Budget Perspectives 2024

## DATE

15<sup>th</sup> June 2023

## VENUE

The Royal College of  
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# Cliff Edges in the Irish Tax-Benefit System

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# Introduction

- Trade-offs exist in protecting those on lower incomes and ensuring an adequate incentive to work.
- Supports that assist those on low incomes can also disincentivise work, generally they therefore get withdrawn as income rises.
- Cliff edges in the tax-benefit system – points where tax or PRSI liabilities rise, or benefits are withdrawn, sharply – can disincentivise employment or working more.

# Introduction

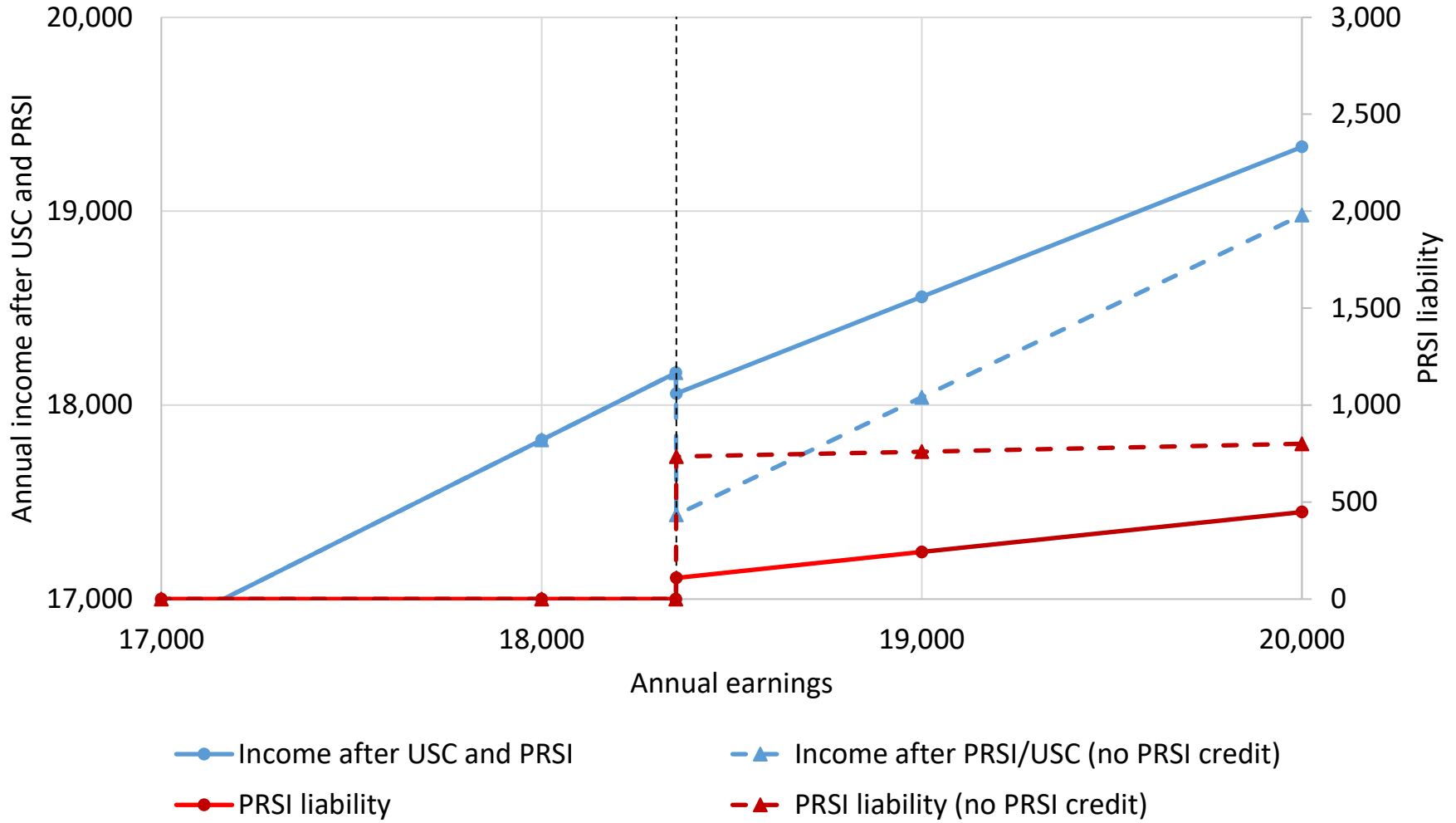
- Research has shown that individuals adjust their behaviour when faced with such points.
- The OECD has highlighted some cliff edges in the Irish tax-benefit system (Browne et al., 2018)
- The Commission on Taxation and Welfare (2022) recommends that ‘cliff edges in the taxation and welfare system should be removed’.
- What such cliff edges exist in the Irish system?

# Taxation and Social Insurance System

## PRSI and USC

- Both PRSI and USC have a cliff edge whereby a small increase in gross income results in a larger drop in net income.
- Driven by the fact that both have a ‘threshold’ (€352 per week PRSI; 13k p.a. USC) below which no PRSI/USC liability exists. Once threshold is crossed the entire income becomes liable for the charge.
- This can distort behaviour e.g. Hargaden and Roantree (2019), using administrative income receipt data, find a clustering of incomes just below the PRSI liability threshold.

# PRSI



# PRSI and USC Reforms

We examine two (revenue neutral) reforms in the case of both PRSI and USC:

PRSI (weekly):

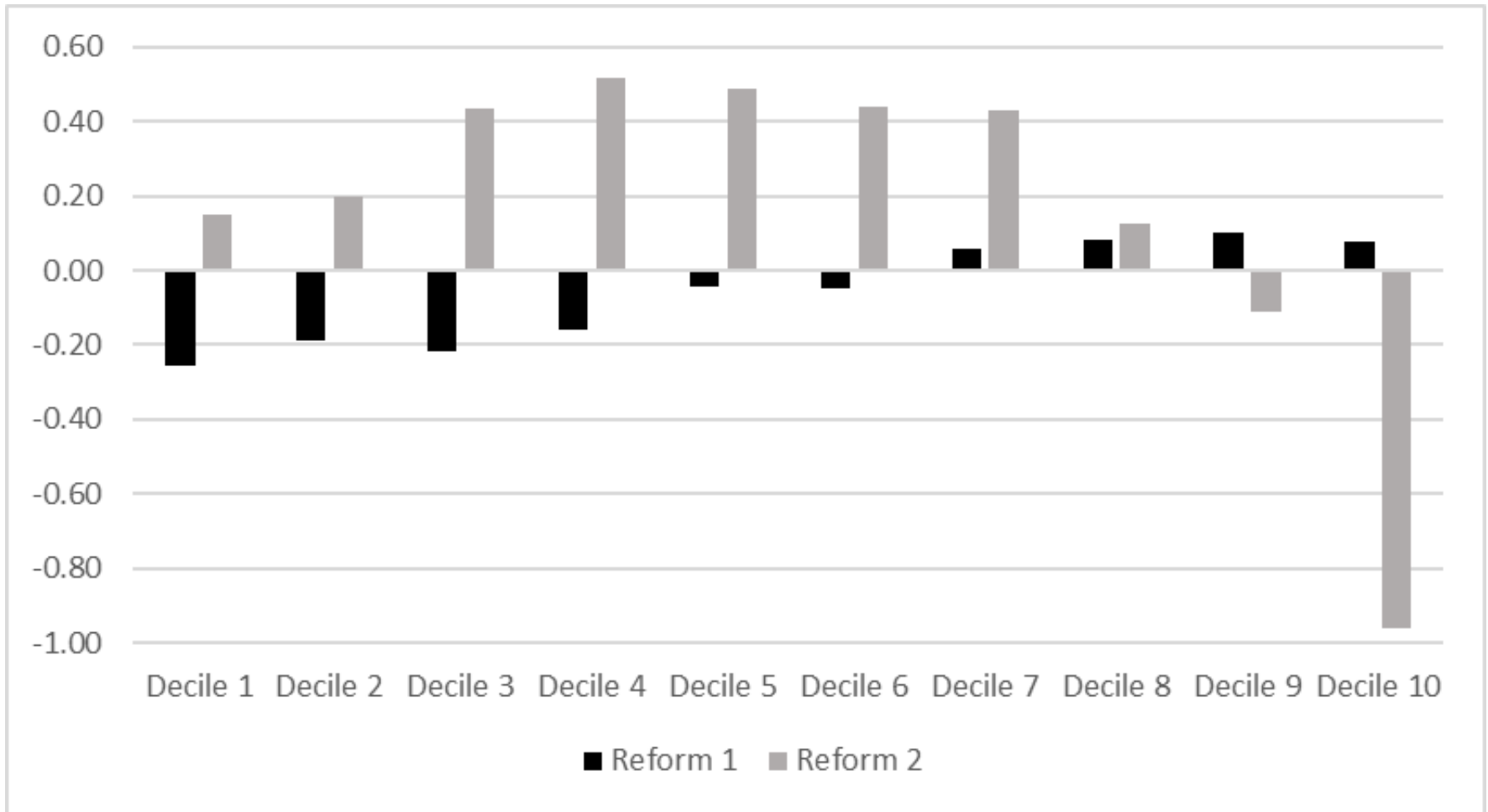
- Reform 1: €0 – €32 : 0% ; >€32: 4%
- Reform 2: €0 – €352: 0% ; >€352: 5.8%

USC (annual):

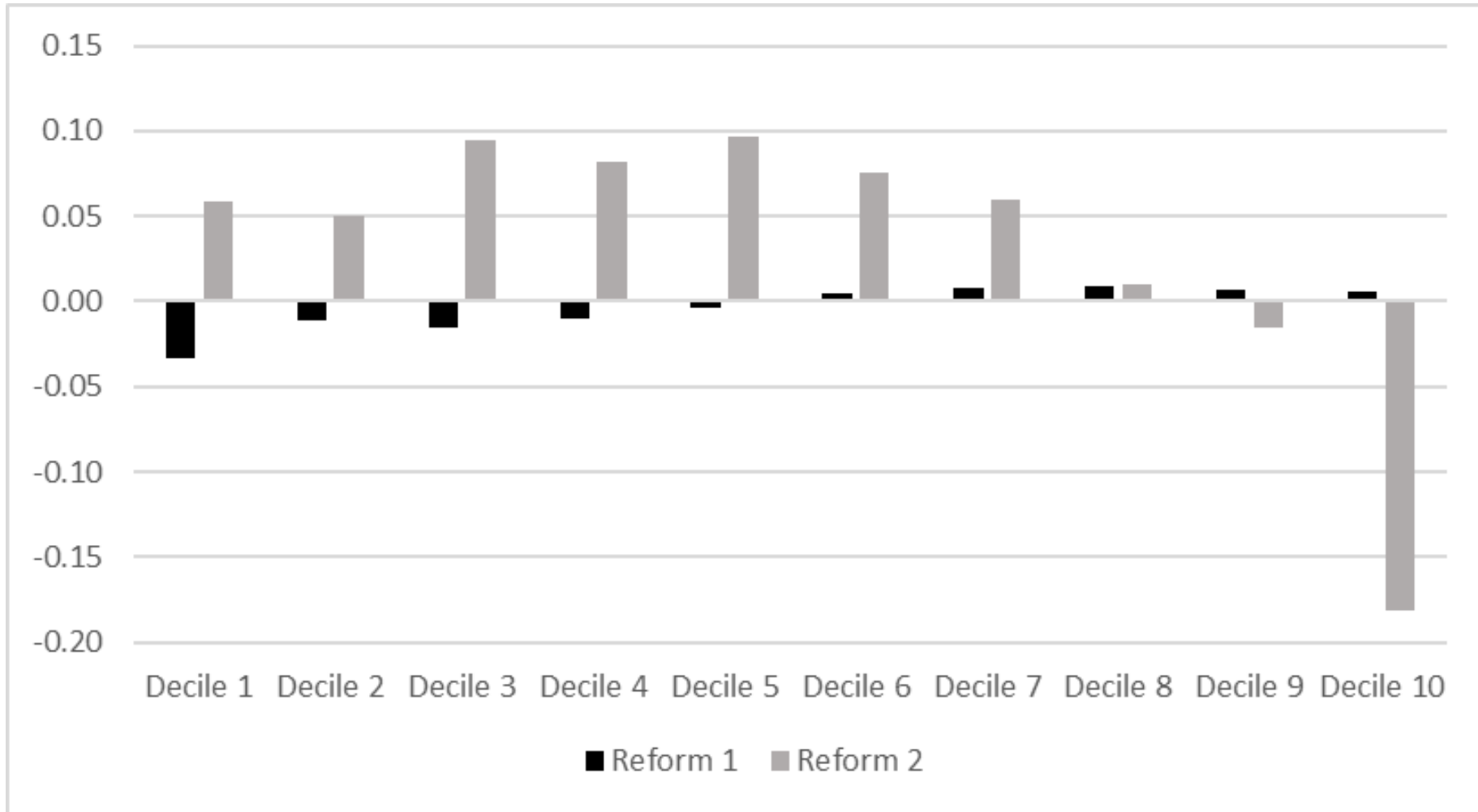
- Reform 1: €0-975: 0% ; >975: current rates
- Reform 2: €0-13k: 0% ; >13k: +.02 p.p. on current rates



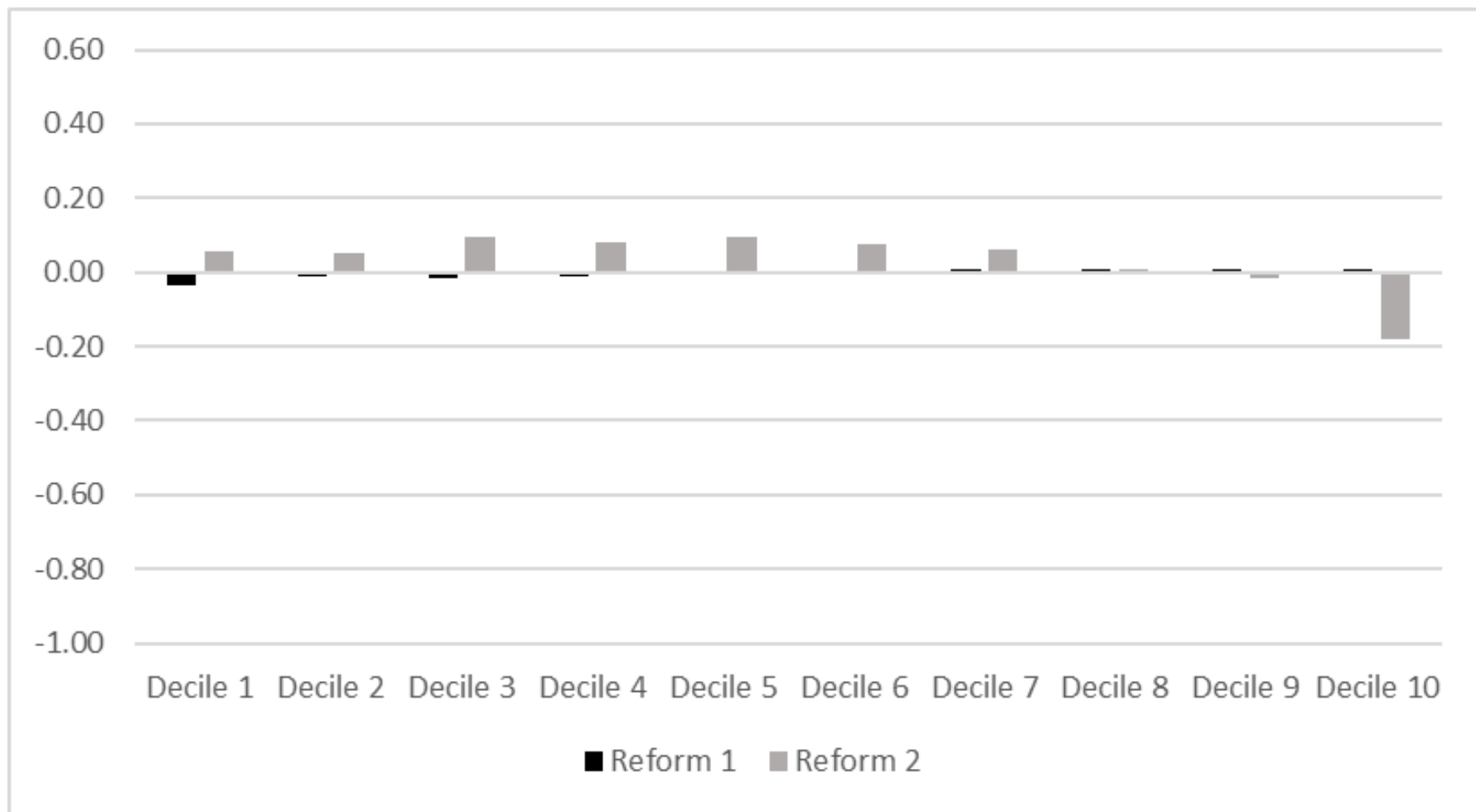
# Distributional impact of PRSI Reforms



# Distributional impact of USC reforms



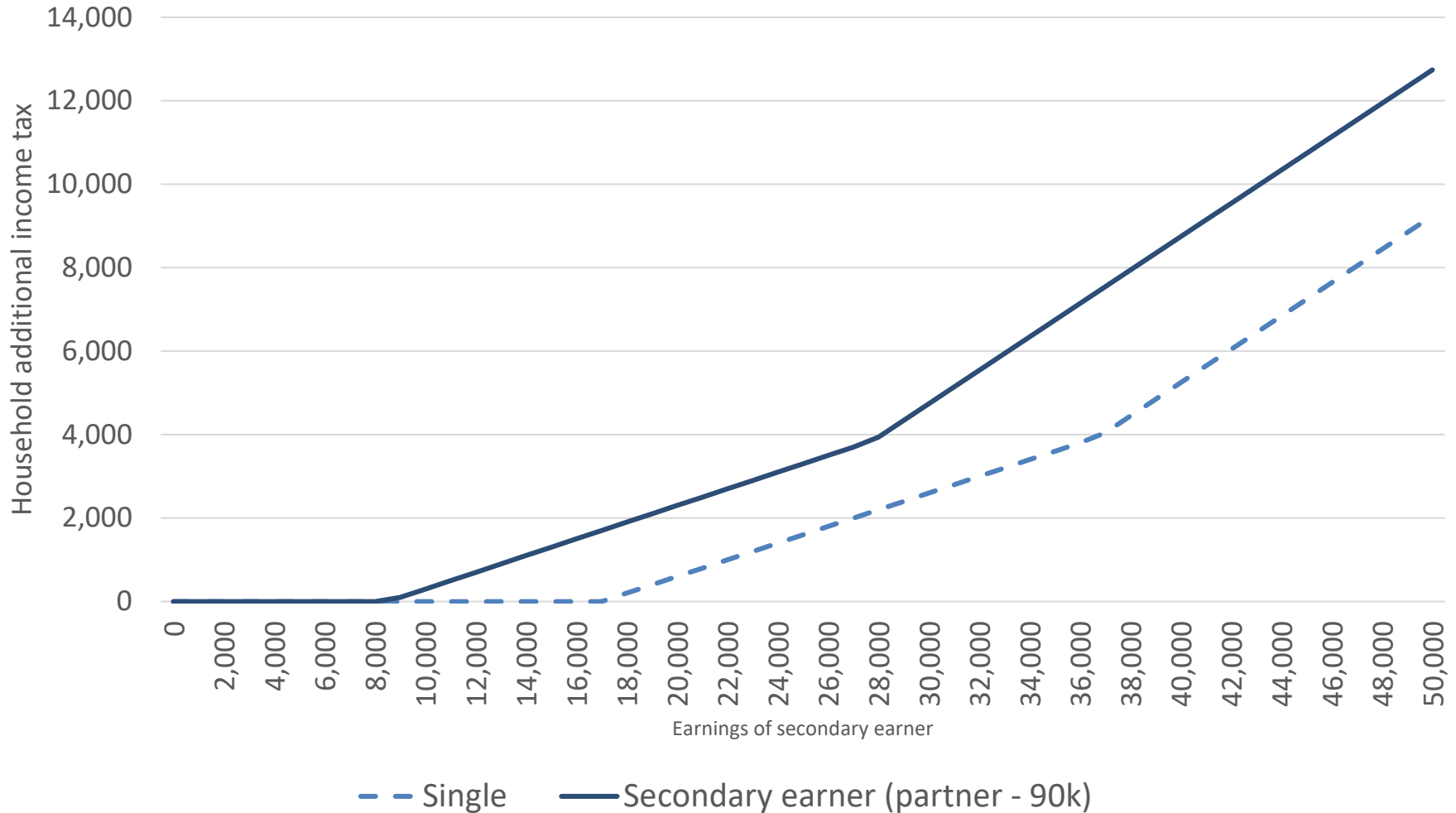
# Distributional impact of USC reforms



# Income Tax

- Income tax system does not have a cliff edge, bands of income can have a 0%/20%/40% tax liability.
- One group faces a quicker rise in taxation than others however – secondary earners in married couples.
- Due to the fact that the tax system is only partly individualised – partial sharing of the SRB and tax credits.
- Disincentive for 2nd earners in married couples to enter employment. Doorley (2018) found the move in 2000 from a joint taxation system to the current partly individualised system led to a 5/6 p.p rise in the participation rates of married women.

# Additional income tax liability by earnings



# Social Welfare System

# Social Welfare Cliff Edges

- Most means-tested welfare payments have a gradual withdrawal.
- ‘Four-in-seven’ rule: those working part-time can receive **JSA**, at a pro-rata rate if unemployed for 4/7 consecutive days +. Two lower-income individuals working part-time can have different JSA entitlements depending on their workdays.  
This requirement was not included in the JST payment - ‘would allow you to work mornings only while your child or children are in school’ ([www.gov.ie](http://www.gov.ie))
- **Working Family Payment** is a weekly tax-free payment for employees with at least one child. Only available to an individual working at least 38 hours per fortnight. This issue of a lack of in-work support for those on low pay is heightened by the four-in-seven rule.

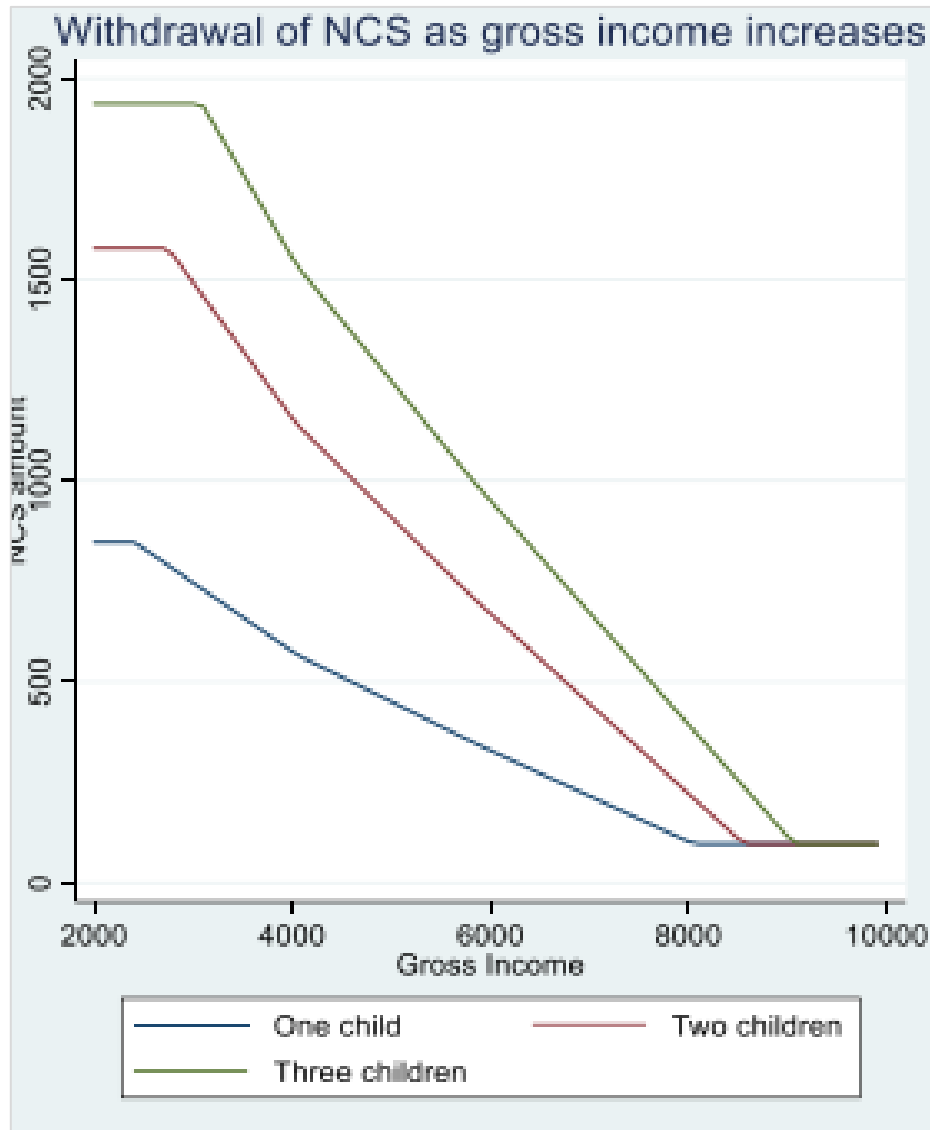
# Other Benefits



# National Childcare Scheme

- NCS provides hourly subsidies for Tusla-registered childcare for children between the ages of 6 months and 15 years.
- Means – tested and universal element.
- The scheme specifies a lower income limit, below which the max subsidy can be received and an upper limit whereby only the universal subsidy can be received.
- The rate of withdrawal therefore rises as the number of children increases.

# Doorley et al (2019)



# Medical Cards

- Most medical cards are means tested.
- Harder to tackle this cliff edge.
- 2005 introduction of GP-Visit cards; retained card; discretionary cards.

100% social welfare rule: If an individual's assessable income is above the income limit and all of this income comes from social welfare, they will receive a medical card.

- Creates a work disincentive
- Creates horizontal inequity
- Heightened by a failure to increase/index income limits – static since 2005.

# Medical card income limits/SW rates 2005-2023

<b>Under 70s (net income) – 2005-2023</b>	<b>€</b>
Single person living alone aged up to 65	184
Single person living alone aged 66 and over	201.50
Single person living with family aged up to 65	164
Single person living with family aged 66 and over	173.50

	<b>2005 (€)</b>	<b>2023 (€)</b>	<b>% Change 2005– 2023</b>
<b>Jobseeker’s Benefit (JSB) /Jobseeker’s Allowance 25+ (JSA)/ Disability Allowance (DA)</b>			
Personal rate	148.80	220	48%

# Student Grants and Housing Supports

## 3<sup>rd</sup> Level Grants:

- Bands exists so that as parental income rises by a small amount, grant entitlement drops sharply – tapering?
- 30km rule - Indecon (2022) suggested graduated bands of support (e.g., 0–10km, 11–20km).

## Housing Supports:

- Income limits for social housing/HAP
- Retained if income grows – targeting issue (1/5 in top half of income distribution).
- Rent contribution increases with income, but usually not to full cost.
- Exacerbated by multi-year freezes in the income limits (e.g. 2011-2022).

# Conclusions

- A variety of cliff edges exists in the Irish tax-benefit system.
- Individuals may face multiple cliff edges.
- These can create work disincentives or inequities between similar groups.
- COTW recommends removing cliff edges.
- Possible for most of the cliff edges identified, harder for non-cash benefits such as the medical card.

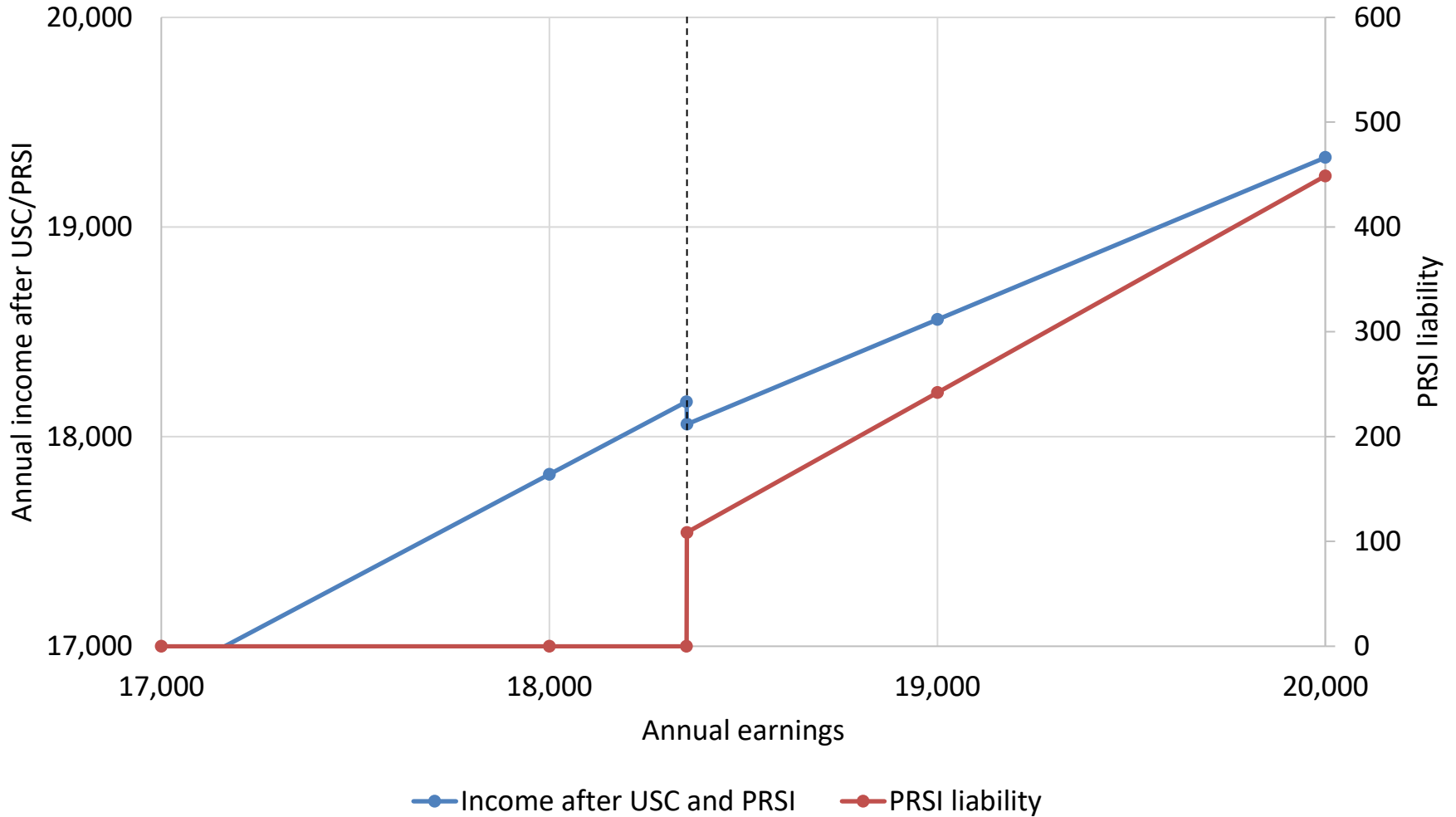
# Additional Slides

# Housing Supports

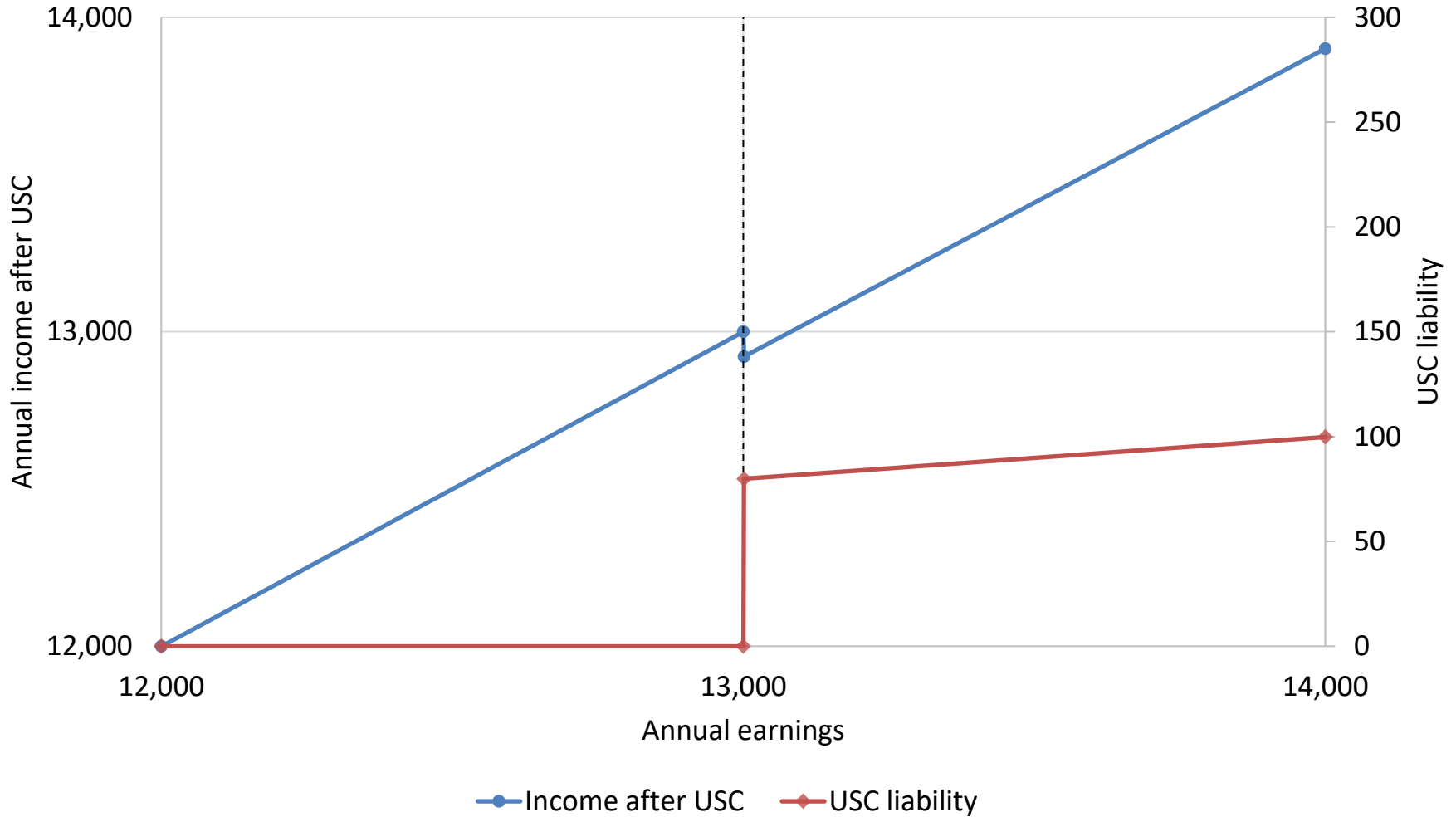
- Income limit exists for those wishing to apply for social housing.
- This helps to avoid work disincentives as an individual can earn more and will not have their rental support removed entirely.
- However, the increasing contribution the individual makes is based on paying a proportion of their income and not a proportion of the market rent.
- This generally means that the renter does not end up paying the full rental cost of the property.
- The targeting, or lack thereof, of housing supports is highlighted in Doolan et al. (2022) – almost one-fifth of supported renters are in the top half of the income distribution, while many lower-income renters receive no state support for their housing costs.
- The existence of a threshold above which individuals cannot apply for social housing or HAP is exacerbated by multi-year freezes in the income limit.



# PRSI CLIFF EDGE



# USC cliff edge



# PRSI Reforms

Bands	Rate (%)
Current PRSI	
If earnings > €352 (EE) or > €96.15 (SE) per week...	
All earnings	4
Reform 1: Remove cliff edge, maintain rates and reduce 0% threshold	
Applied to all weekly earnings...	
€0 – €32.45 (EE or SE)	0
>€32.45 (EE or SE)	4
Reform 2: Remove cliff edge, increase rates and maintain 0% threshold	
Applied to all weekly earnings...	
€0 – €352 (EE) or €0 - €96.15 (SE)	0
>€352 (EE) or >€96.15 (SE)	5.79

# USC Reforms

Bands (€)	Rates (%)
Current policy	
If earnings greater than €13,000...	
0–12,012	0.5
12,012.01–22,920	2
22,920.01–70,044	4.5
70,044.01 +	8
SE income > €100,000	11
Reform 1: Remove cliff edge, maintain rates and reduce 0% threshold	
0–975	0
975.01–12,012	0.5
12,012.01–22,920	2
22,920.01–70,044	4.5
70,044+	8
SE income > €100,000	11
Reform 2: Remove cliff edge, increase all rates and maintain 0% threshold	
0–13,000	0
13,000.01–22,920	2.2
22,920.01–70,044	4.7
70,044.01 +	8.2
SE income > €100,000	11.2