



The Distributional Impact of Ireland's Indirect Tax System

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Outline

1. Motivation for this paper
2. Data sources and data construction
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Motivation: Relative contribution of indirect taxes to total revenue

Excise duties	€4,864bn
Stamp duties	€1,600bn
Income tax	€10,077bn
Corporation tax	€5,348bn
Value added tax	€10,368bn
Total tax receipts	€33,400bn



Motivation: Int'l comparison of relative contribution

Germany	30.5%
France	35.2
Ireland	43.7
UK	38.9%
EU-15	34.6%
EU-25	34.8%



Motivation: Existing literature

- ◆ ESRI SWITCH analysis looks at direct side
- ◆ Scott and Eakins(2004) focus on energy
- ◆ Madden (1995, 1996)



Data sources and construction

- ◆ Household Budget Survey 1999-2000
- ◆ Interest is in distribution of indirect tax by household income so need to adjust for household size and structure
- ◆ Use ESRI equivalent scales
- ◆ Having established household equivalised income, rank households and create deciles



Data sources and construction

- ◆ Need to distil indirect tax component from spending figures
- ◆ DoF/Revenue provided data on excise and VAT rates by product and service (more complicated in the case of excise)
- ◆ Allowed us to calculate the proportion of gross income by household that was indirect tax

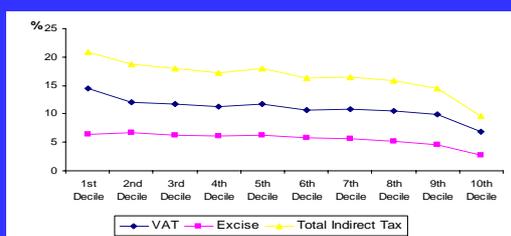


Findings – amount and % of gross income by decile

	1st	2nd	9th	10 th
Wkly inc	90.17	121.49	497.63	1085
VAT €	13.06	14.54	49.35	74.1
Excise €	5.72	8.17	22.76	29.9
Total €	18.78	22.71	72.11	104
VAT %	14.5	12	9.9	6.8
Excise %	6.3	6.7	4.6	2.8
Total %	20.8	18.7	14.5	9.6



Findings - graph



Findings – alcohol and tobacco

- ◆ Not a focus because benefit of increasing price likely to exceed cost
- ◆ Also need to be aware of understatement of spending in the HBS
- ◆ For lowest decile 6.2% of income in indirect taxes; 8.6% for second decile; then a (generally) linear fall to 4.4% in the 9th decile and 2.5% in the 10th



Simulation: Impact of imposing VAT on food

	1st	2nd	9th	10 th
Total % with VAT	25.2	22.9	16.3	10.6
Total % no VAT	20.8	18.7	14.4	9.6



Simulation: Increasing VAT on fuels

- ◆ Smaller impact than in the case of food
- ◆ For lowest decile, total % goes from 20.8 to 21.7; for highest decile, 9.6 to 9.7
- ◆ Reason, spending by lowest decile on fuel only a third of spending on food



Discussion

- ◆ Indirect tax appears regressive but conclusion may not be to amend (Kaplanoglou, 2004)
- ◆ Alternative approach is to increase progressivity/reduce regressivity elsewhere in the system
- ◆ One possible source – tax reliefs



Discussion contd.

- ◆ Tax Strategy Group lists objectives of tax reliefs
 - encourage investment in certain activities or areas (e.g. film relief, urban renewal)
 - reduce cost of capital and encourage business investment (e.g. interest relief and various capital allowances)
 - encourage certain expenditures (e.g. pensions)



Discussion contd.

- Encourage savings – SSIA's
- Assist with particular costs incurred by individuals (e.g. mortgage interest relief and health expenses)
- Assist certain individuals or activities (e.g. Revenue Job Assist for the long-term unemployed)



Discussion contd.

Scheme	Estimated cost (£m), 2000/1
Capital allowances	1,720
Pensions	1,292
SSIA's	433
Child-benefit exemption	315
Mortgage interest relief	211
CGT break on principle private residence	1,322



Discussion contd.

- ◆ Hughes (2000) provides a distributional analysis of the relief in respect of pensions
- ◆ Value of the relief as a % of gross weekly income: 0.06 for lowest decile, 0.8 in the middle, 1.6% in the top decile
- ◆ Top 20% of earners receive 60% of the benefits; bottom 20% receive less than 0.5%
- ◆ Is the objective worth such huge inequality in benefit?



Conclusions

- ◆ Indirect system is regressive
- ◆ Need to avoid changes that will make it more regressive
- ◆ Need to look elsewhere in the system to address regressivity
- ◆ Possible sources: reliefs but also rates of direct tax and property tax
- ◆ More information needed on the impacts before arriving at firm conclusions