Evaluation of Budget 2020 Compliance Measures

Budget 2020 included a compliance measure for Dividend Withholding Tax ("DWT") among the taxation policy changes.

The rate of DWT was increased from 20% to 25%, effective from 1 January 2020.

This measure was projected at the time of the Budget (October 2019) to yield an additional €80 million to the Exchequer in 2020.

DWT applies to dividend payments made by Irish resident companies to individuals. A lower level of dividend growth would be expected through 2020, due to the impacts of the COVID-19 pandemic.

However, the rate of DWT growth (19%) far outstripped that of general economic indicators in 2020. For example, Gross Operating Surplus (GOS), which is a measure of corporate profitability, increased by 1.7%.

There was an increase in DWT net receipts of €79 million in 2020.

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Given other economic indicators, it is reasonable to assume that the increase in the DWT rate (the Budget 2020 compliance measure) accounts for the bulk of share of the increase in receipts – at least €72 million on a conservative basis – and close to the €80 million target.

Revenue
Cáin agus Custaim na hÉireann
Irish Tax and Customs

Fionnuala Ryan
Strategy, Evaluation & Reporting Branch
Revenue Statistics Revenue Research statistics@revenue.ie

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1 Introduction

Budget 2020 included a "compliance measure" among the taxation policy changes:[1]

Increase rate of Dividend Withholding Tax from 20% to 25% from 1 January 2020

As the first step in a two-stage process, the rate of Dividend Withholding Tax (DWT) will be increased from 20% to 25% from 1 January 2020. This will better align the amount of tax remitted by companies with the income tax and USC that is ultimately payable by the individual taxpayer. The 25% rate is considered to be a reasonable combination of the standard 20% rate of income tax and the most common rate of USC which is the 4.5% that applies to income between €19,874 and €70,044. In the event that the 25% rate results in an overpayment of tax, the relevant amounts will be refunded, as is the normal procedure. It is important to highlight that this measure does not alter the underlying liability to tax for Irish tax residents.

This measure was projected at the time of the Budget (October 2019) to yield an additional €80 million to the Exchequer in 2020.

This measure was to be a first step, followed by the introduction of a modified Dividend Withholding Tax ("DWT") regime from 1 January 2021 using Revenue's newly modernised PAYE system. This second stage has been deferred to allow for the introduction of a new settlement system in the Irish Stock Exchange (in March 2021), and also due to disruptions caused by the COVID-19 pandemic.

This report assesses the rate increase to evaluate whether the target yield (€80 million) was realised. Conservative and prudent estimates are used, and it is acknowledged that some of the results may contain spill over effects or be otherwise affected by other factors. This follows the approach of similar analysis undertaken of compliance measures in earlier Budgets.[2] The outcomes of these prior year evaluations are summarised in Table 1.

Table 1: Summary of Recent Budget Compliance Measures Evaluations

Budget Year	Measure	Projected Yield	Estimated Yield
2016	Addressing non-compliance in the oil market	€10m	€35m
	Addressing non-compliance in the construction sector	€20m	€56m
	Deploy enhanced debt analysis tool to reduce tax arrears	€20m	€56m
	Increase resources to confront non-compliance	€25m	€26m
2017	Section 110 and Funds changes	€50m	€63m
	Tackling Offshore tax evasion	€30m	€88m
	Increase resources to confront non-compliance	€50m	€62m
2018	Employer PAYE compliance project	€50m	€77m
	eCommerce/Online business compliance project	€30m	€26m
	Tax avoidance and base erosion capacity	€20m	€20m
2019	Employer PAYE Compliance Implementation	€50m	€65m

Source: Revenue analysis.

[1] Summary of Budget 2020 Taxation Measures – Policy Changes, available at: http://budget.gov.ie/Budgets/2020/Documents/Budget/Budget%202020_Summary%20of%20measures_a.pdf.
[2] Evaluations of Budget 2016, 2017, 2018 and 2019 compliance measures are published at https://www.revenue.ie/en/corporate/information-about-revenue/research/reviews/index.aspx.

2 Dividend Withholding Tax (DWT)

2.1 Background

DWT applies to dividend payments made by Irish resident companies to individuals and was applied at the standard rate of Income Tax pre-2020. Dividend income should then be reported to Revenue on Income Tax returns for the purpose of the individual recipient paying the outstanding Income Tax at their marginal rate, as well as any PRSI and USC due.[3]

Gross and net DWT receipts since 2016 are summarised in Table 2. Repayment of DWT, the difference between gross and net, generally occurs where the underlying dividend was not taxable in the first place (for example, due to non-resident dividend recipients).

Table 2: DWT Receipts

Year	Gross Receipts	Net Receipts
2016	€375m	€272m
2017	€431m	€324m
2018	€458m	€353m
2019	€511m	€408m
2020	€613m	€487m

Source: Revenue analysis. Note: this table shows receipts in a given year, not the tax year for which the liability was due.

2.2 Budget 2020

The rate of DWT increased from 20% to 25% on 1 January 2020. This was projected to yield €80 million in 2020. As shown in Table 2, the increase in net receipts in 2020 (compared to 2019) was €79 million or 19.4 per cent.

As can also be seen in Table 2, there have been significant increases in DWT receipts in some recent years. This raises the question of whether the higher yield in 2020 is solely due to the increase in the DWT rate (from 20% to 25%).

Many factors influence dividend growth (and so DWT yield). The most significant of these is likely to be corporate profitability, one measure of this is Gross Operating Surplus ("GOS"). GOS as an economic growth factor is generally assumed to be relevant to growth in corporate profits and is the macro-economic factor used by the Department of Finance to forecast Corporation Tax receipts. Table 3 shows the increases in GOS over recent years, with the relative change in DWT receipts for comparison.

[3] PRSI was imposed on dividend income from 1 January 2014.

Table 3: Growth in Gross Operating Surplus and DWT

Year	Annual Change in GOS	Annual Change in Net DWT Receipts
2017	13.6%	19.1%
2018	10.5%	9.0%
2019	9.6%	15.6%
2020	1.7%	19.4%

Source: Revenue analysis.

As Table 3 indicates, other factors being relatively unchanged, a small increase in DWT receipts might have been expected in 2020 (in line with the GOS increase of 1.7 per cent). However, the actual increase of 19 per cent considerably exceeds this.

Intuitively, a lower level of dividend growth would be expected through 2020, as the impacts of the COVID-19 pandemic and related global economic slowdown spread across companies and sector. It is clear that the rate of DWT growth has far outstripped that of GOS and other general economic indicators.

With lower growth in the tax base (corporate profits and dividend payments), it is reasonable to conclude that the increase in the tax rate is primary driver of the higher yield. A 1.7 per cent growth in DWT (based on the GOS growth rate) would have yielded receipts of around €415 million in 2020, €72 million short of the actual net receipts of €487 million.

3 Conclusion

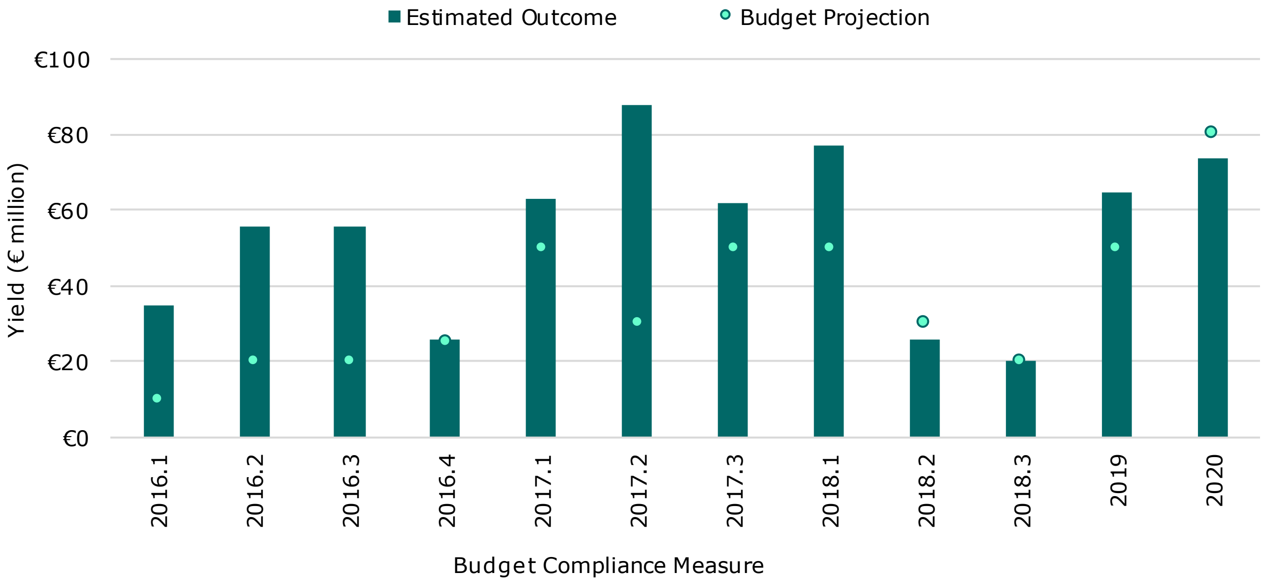
This analysis assesses the impact of the Budget 2020 compliance measure and attempts to identify the additional tax collection that may be attributable to the increase in the DWT rate.

There was an increase in DWT receipts of €79 million in 2020. Given economic indicators, it is reasonable to assume that the increase in the DWT rate accounts for the bulk of share of this increase (at least €72 million on a conservative basis). It is unlikely, given the prevailing economic conditions of the last year, that many companies would have been able to sustain higher dividends (the 19 per cent growth noted in DWT receipts).

In conclusion, the target of €80 million for the Budget 2020 compliance measure has likely been achieved or close to it, as borne out by the analysis of the data now available for the year.

Combined with the earlier analysis of Budgets 2016, 2017, 2018 and 2020 measures, this outcome provides confidence to support the introduction of similar measures in future Budgets.

Figure 1: Compliance Measures Evaluations 2016 to 2020



Source: Revenue analysis. Note: Compliance measures for each year described in Table 1.