Response ID ANON-U45Z-ZZN7-H

Submitted to Your Vision, Our Future
Submitted on 2022-01-17 15:07:44

About You

1 What is your name?

Name:
Paul Mac Flynn

2 What is your email address?

Email:
paul.macflynn@nerinstitute.net

3 I am responding as:

A representative of an organisation

4 If you are responding on behalf of an organisation, please enter your organisation name here:

Organisation:
Nevin Economic Research Institute

Chapter 1 - General Questions

1 What elements of the taxation and welfare systems do you feel are working well?

Please elaborate below::

When considered in combination the taxation and welfare systems perform well overall as a system of income redistribution. This redistribution ameliorates the potential negative economic and social impacts that might otherwise arise from the very high level of market inequality that is prevalent in Ireland.
The combined system also succeeds in significantly reducing the incidence of poverty and deprivation. Indeed, Ireland is one of the best performing countries in Europe in terms of reducing poverty rates through its welfare system. While the welfare system performs the most significant role in this regard, the strongly progressive structure of labour taxation also plays an important role. Tax rates are low for most low paid workers relative to other OECD countries and this helps maintain strong incentives to engage with the labour market while reducing the propensity of in-work poverty.
The system of tax administration is relatively straightforward to engage with and imposes a minimal compliance burden on employees. Finally, policymakers and the tax and welfare systems displayed impressive agility and speed in their responses to the economic disruption caused by the Covid-19 pandemic. This shows that these systems will be capable of engaging with and implementing large-scale reforms when needed.

2 What elements of the taxation and welfare systems do you feel are not working well?

Please elaborate below::

While the overall tax system is reasonably well designed it does not consistently adhere to the core principles of well-designed taxation i.e. simplicity and transparency, vertical and horizontal equity, impact on economic efficiency, and avoidance of economic distortions. These design failures manifest most clearly with regard to the overuse of tax expenditures. Tax expenditures fundamentally undermine the principle that individuals should pay tax in proportion to their ability to pay, cause economic distortions, are non-transparent, and generally reduce the progressivity and equity of the tax system. The overall system could be improved over time via a general reduction in the availability and generosity of these tax reliefs. One way to do this would be to gradually shift the composition of taxes on earned income away from the income tax and in favour of the USC and PRSI. Another alternative would be to cap the life-time value of individual reliefs.
A second issue relates to sustainability. Ageing demographics, the cost of the green and the digital transitions, and addressing the housing crisis, will all require significant additional public resources in the years ahead. Alongside this will be the need to move fiscal policy in a more growth friendly direction. For example, by reversing the state's structural under-spends on childcare, on education, and on public R&D. The state's revenue yield will need to be increased in future years in order to meet these additional costs. In addition, there is significant uncertainty about the sustainability of the current yield from corporation tax. Our view is that the Irish system does not generate sufficient revenue and the underlying fiscal position is fragile to international developments in globalisation, tax and trade.
Cross country comparisons with other high-income EU countries shows that Ireland collects less in revenue than other high-income EU countries, whether on a per capita basis or on a percentage of output basis (GNI* or GDP). Its notable that many of these countries have higher employment rates than Ireland suggesting a weak relationship between aggregate economy-wide taxation and labour market outcomes. Ireland's shortfalls in revenue are in social insurance (employers and self-employed) and in the broad area of capital stocks. The NERI would encourage the COTW to identify a range of potential options for increasing the overall revenue yield consistent with employment, equity, adequacy, and sustainability principles.
Income protection is very weak in Ireland. Ireland's welfare supports do not all meet minimum levels of adequacy and we do not have a meaningful system of pay related income supports for illness, unemployment, and family leave. By contrast, most other high-income EU countries provide short-term contributory benefits that protect households from economic shocks and provide the space to find employment or entrepreneurship opportunities appropriate to their human capital while meeting their financial obligations in the short-run. This system also ameliorates the volatility of the economic

cycle by supporting short-run aggregate demand during a recession. Overall, the policy focus should be on strengthening the contributory principle and the provision of heavily subsidised or free essential public services (e.g. health and childcare) as a virtual income, and should move away from means tested income top-ups to purchase services.
Finally, the pandemic has shown that our tax and welfare system were not initially robust enough to deal with significant exogenous shocks. We had to introduce the Pandemic Unemployment Payment and the Temporary Wage Subsidy Schemes because it was recognised that supports of this nature were necessary to protect incomes and prevent an economic collapse. The success of the hastily devised and imperfect PUP scheme shows the value of partially linking unemployment benefits to past income (some defined percentage below 100%) for a time limited period, while the wage subsidy schemes were important innovations that helped protect the economy's productive capacity. Time limited and conditional wage subsidy schemes for temporarily troubled sectors are common to other EU countries and should become a permanent feature of the Irish system.

3 Good quality public services, welfare provision and infrastructure are financed mainly from taxation and PRSI. What are the features that you think our taxation and welfare systems should have in order to meet these needs?

Please specify::

The key objectives of any tax system are to raise a meaningful amount of money for the exchequer while at the same time minimising administration and compliance costs, reducing inequality, minimising economic distortions, and changing behaviour. It is challenging to design a good taxation system that adheres to the core principles of equity, efficiency and simplicity.
The tax and welfare systems should seek to be consistent with the following basic principles:
• It should be compatible with fiscal sustainability (short-run and long-run) and not overly rely on volatile sources of revenue
• It should reward positive externalities (e.g. engaging in R&D or education) and punish negative externalities (e.g. GHG emissions and other polluting activities)
• It should reduce inequality, adhere to vertical equity (progressivity) and horizontal equity (avoid tax expenditures and treat all sources of income and wealth equally), and should not facilitate aggressive tax planning by individuals or corporations
• It should promote economic efficiency and avoid economic distortions (e.g. avoid excessive use of tax expenditures, equal tax treatment of income regardless of source, and minimise policy deadweight)
• It should ensure net income adequacy for all households and should seek to minimise income shocks
• It should avoid employment disincentives (e.g. through shallow tapering of benefits and ensuring low marginal effective tax rates for low paid workers) and promote competitiveness
• It should have strong automatic stabilisers (short-term income replacement rates) in order to minimise the volatility of the economic cycle
• It should have as broad a tax base as possible
• It should promote social and economic inclusion, it should be widely perceived as fair, and it should be characterised by reciprocity and the contributory principle
• It should minimise compliance and administrative costs
• There should be transparency in the rules and in the application of those rules
Not every part of the system need share all of these characteristics. For example, consumption taxes are generally regressive but their utilisation is essential to the raising of a sufficient amount of revenue. Similarly, many welfare policies involve unavoidable trade-offs between adequacy, deadweight and simplicity. It is the impact of the overall system that matters.

4 In your view, what main reforms are necessary so that the Irish taxation and welfare systems can embrace the opportunities and meet the challenges that Ireland may face over the next 10-15 years?

Please outline your views::

Overall
The NERI's view is that the fiscal position will deteriorate on a no policy change basis over the medium-to-long term. A declining working age ratio will reduce the tax base while an ageing population puts increasing pressure on health spending and pension spending. We should also consider existing spending shortfalls in areas like education (per pupil basis), childcare, housing, infrastructure investments needed for the green transition, the uncertain sustainability of corporation tax receipts, and the long-term sustainability of existing environmental taxes.
The COTW should therefore aim to develop an overall package of reforms that meaningfully raises net revenue in aggregate. Such reforms should reflect long-run well-being, growth, equity, adequacy, fiscal sustainability and environmental sustainability considerations.
Irish government revenue from taxes and Social Security Contributions (SSCs) is lower than the EU average as a proportion of output (GNI*). Ireland's revenue yield was 37.7% of GNI* in 2019, which was 2.4 percentage points, or €5.1 billion, below the EU average (see McDonnell, 2021). The consequences of the relatively low revenue yield are Ireland's relative under-spends in growth-friendly areas of public spending such as subsidised childcare, per pupil education spending, per capita public R&D. Its notable that aggregate revenues from consumption and capital are above the EU average as a percentage of GNI*, whereas revenues from labour are below the EU average.
The NERI's view is that once Ireland's structural deficit has reached a sustainable position, it would then be prudent for the annual growth of non-cyclical public spending (net of revenue measures) to be explicitly linked to the economy's medium-term growth potential. The sustainable level for the structural deficit is itself a function of the economy's growth potential, while the economy's growth potential is in turn endogenous to the quality, amount and type of public spending investments and the structure of the tax system.
We need to understand the sustainability of public debt and deficits as dynamic phenomena that are endogenous to compositional policy choices as well as choices related to the fiscal stance and the market perception of that stance. In other words, fiscal sustainability is not just an accounting exercise of matching income and expenditure in the short-run. A longer-term perspective is required. For example, a failure to make strategic long-run investments such as in education may save money in the short-run but will weaken the economy and therefore fiscal sustainability over a longer time horizon.
Taxes on Labour and Self-employed
Income tax, USC and PRSI collectively make up almost half of Ireland's tax revenue. Even so, revenues from labour income are below the EU average on a GNI* basis. Ireland's low overall yield relative to the EU average is an outcome of the 'under-taxation' of labour income (see McDonnell, 2021 and Goldrick Kelly, Mac Flynn and McDonnell, 2020). European Commission data shows that Ireland also has a relatively low Implicit Tax Rate (ITR) on labour income at 33.5% compared to an EU average of 38.1% (European Commission, 2021). The ITR is the tax yield divided by the tax base. We can think of it as an economy-wide average effective tax rate on a particular type of economic activity.

Our view is that labour taxes will need to form part of the overall net revenue raising exercise. OECD (2021) analysis Ireland's labour tax wedge is low relative to the OECD average for most low- and middle-income households. This suggests potential scope to increase the yield from these groups. However, care must be taken around work incentives for low paid workers as well as the potential to cause in-work poverty. To ensure adequacy, any tax increases on low paid workers might need to be offset on the welfare side thereby potentially counteracting the fiscal benefits and increasing the marginal effective tax rate.

Even so, there is a strong case for reducing the entry rate thresholds for USC and PRSI at modest rates (a new lower rate in the case of PRSI) as a way of broadening the tax base. Labour taxes for all workers should generally shift over time to a greater emphasis on USC and PRSI and a lesser emphasis on income tax. These taxes have broader bases than income tax and are less distorted by tax expenditures.

The relative 'under-taxation' of labour income is explained by the low yield from employer social contributions. Whereas revenue from employees exceeds the EU average, employers are 'under-taxed' on a percent of output basis, by close to €8 billion. Similarly, the ITR on employer contributions is just 9.2%, compared to 17% for the EU as a whole (i.e. just 54% of the average), whereas the ITR for employees, at 24.3%, actually exceeds the EU average of 21.1%.

Over the medium-term, self-employed PRSI should be aligned with combined employee and employer PRSI rates via modest annual increases in the rate. At the same time, benefit coverage should be brought in line with benefits available to employees. Employers PRSI should also be increased slowly over time as part of a wider process of enhancing contributory benefits and with a view to future pressures on the social insurance fund arising from the ageing population and declining working age ratio. Reforms to PRSI are considered below in the 'Social Welfare System' section of our response to this question.

The Class A PRSI 'cliff edge' anomaly needs to be reformed as it can distort hours worked and create disincentive effects. The step effect arises because there is no charge on employee PRSI until income is over €352 per week and then all income is subject to the charge. The cliff edge can be eliminated on a revenue neutral basis by making the PRSI system more progressive and reducing the entry rate threshold.

The old age exemption limits for income tax and PRSI have no basis in equity and should be reduced or eliminated. Any issues of poverty and deprivation should be dealt with via a welfare system that ensures adequacy, as well as via the expansion of free or heavily subsidised public services.

We do not agree that the standard rate cut-off should be increased. Increasing the SRCO by €1,000 is very costly (€230 million in a full year), and would be highly regressive, providing no benefit to the majority of workers. The potential for growth in the employment rate arising from an increase in the SRCO would be negligible and should be set against the extremely high revenue and opportunity costs. If the sharp jump in the marginal income tax rate is considered a problem then smoothing can be achieved by gradually increasing the middle USC rates and introducing a third (middle) income tax rate on a revenue neutral basis.

The differential treatment of married couples compared to single people has no justification in equity and is clearly discriminatory. Our view is that Ireland should move to full individualisation over the medium-term via annual small reductions in the SRCO for married one earner couples. The current system creates disincentives for labour force participation and may be contributing to Ireland's relatively low female participation rates.

The COTW should examine whether there is scope to reduce or abolish tax expenditures on labour income. For example, the costly help-to-buy scheme (circa €100 million per annum) is a poorly targeted policy that is contributing to upward price pressure in the housing market, has significant deadweight cost, and disproportionately benefits middle-and higher income households. There is no obvious reason why this scheme should not be abolished at the earliest opportunity. Similarly, the income tax relief on private health insurance runs counter to the public policy goal of implementing Sláintecare. This relief should be discontinued.

The pension tax free lump sum and the Standard Fund Threshold are both excessive and should be reduced. Their value could be linked to some multiple of median or mean income. At the same time, the overall pension tax system should be reformed to ensure that it fully adheres to the EET principle. The Special Assignee Relief Programme is highly regressive and undermines the notion of horizontal equity between taxpayers. While this relief may add to Ireland's attractiveness to mobile labour it does so at the cost of social solidarity.

Taxes on Consumption

Ireland's revenue yield from consumption taxes in 2019 (11.3% of GNI*) was marginally above the EU average of 11.1%. Ireland's implicit tax rate on consumption was also above the EU average at 19.4%.

Consumption taxes are generally regressive when considered in isolation unless they are targeted at luxury goods and services. The marginal decline in utility from an increase in consumption taxes is also likely to be higher for low-income households. Even so, their net impact can be to contribute to an overall reduction in income and poverty to the extent that such revenues contribute to funding social transfers and basic services. For example, the Nordic economies of Denmark, Sweden, Finland, Iceland and Norway all have high taxes on consumption but generally low levels of income inequality.

The NERI's view is that increases in consumption tax should focus on ameliorating negative externalities. In particular, the environmental tax reliefs and fuel subsidies should be phased out over a short time horizon. These reliefs cost over €2 billion per annum and run directly counter to Ireland's environmental objectives. The excise on auto diesel and petrol should be equalised at the next budget. Sequencing around alternatives is important. Even so, poverty impacts related to the green transition should be addressed in the short-term via the social welfare system and in the medium-term via the provision of public subsidies (e.g. for retrofitting), provision of subsidised and widely available public services (e.g. public transport), provision of infrastructure (e.g. energy, private transport).

There is also scope for additional forms of green taxation that should be considered by the COTW including congestion charges, car park charges, a methane tax, air travel taxes and tourist/city taxes.

As Ireland gradually achieves its green transition then the yield from environmental taxes will fall. This creates a fiscal sustainability issue. The logical way to resolve this tension is to explicitly link (hypothecate) the tax yield from environmental taxes to public expenditures linked to realising the green transition (e.g. green infrastructure) and managing the just transition (e.g. related to temporary cost of living increases and income supports in affected sectors). A dedicated fund should be established to achieve this goal. The fund could be wound down in the future once/if the green transition has been achieved. This would mean that core public spending on areas like health, pensions and education would not become reliant on unsustainable green taxes.

Consideration should be given to enhancing the yield from VAT. However, reducing the number of zero-rated goods and services should be approached with caution due to the potentially severe impact on the cost of living for low income households. On the other hand, the temporary 9% VAT rate should not be extended. The benefits of this reduced rate is likely to be regressive.

Capital Taxation

Ireland has a relatively high yield from capital compared to the EU average (GNI* basis) despite having a relatively low ITR on capital income. This is a function of the relatively large proportion of income accruing to capital within the economy and the elevated receipts from corporation tax. It is not clear to what extent Ireland's extremely high receipts from corporation tax are sustainable. On the other hand, revenues from other capital sources such as stocks of capital and especially the incomes of the self-employed are below the EU average on a percent of output basis.

A greater emphasis on the taxation of capital stocks would be beneficial from the perspective of long-run economic growth. Property taxes are generally

the most growth friendly form of taxation and reorienting the composition of our tax base towards property taxes would be an important structural reform with positive labour market and equality outcomes. The NERI's view is that recurrent taxes on immovable property should be significantly increased where they already exist (e.g. the Local Property Tax) and, additionally, should be extended to include all land not currently covered by the Local Property Tax. This extension could be achieved through a site value tax or, where relevant, a commercial property tax. Commercial rates should be replaced with either a site value tax or a commercial property tax. Either option is preferable to the current system and the new tax should be centrally administered before redistribution to the councils.

There are strong theoretical arguments in favour of recurrent taxes on immovable property:

• Property taxes have been shown empirically to have a minimum negative impact on GDP; in other words they are growth friendly taxes
• They are very difficult to avoid or evade
• Unlike transaction based property taxes, they are reasonably stable throughout the economic cycle
• They do not, by and large, penalise productive activity
• Taxes on immovable assets are particularly appropriate in the context of increasing globalisation where the factors of production are increasingly mobile
• They do not create a barrier to labour mobility (unlike transaction based property taxes which potentially add an additional cost to moving for economic reasons)
• They disproportionately fall on wealthier households and can be progressive if correctly designed and
• They enable the state to recoup some of the costs of public infrastructure provision through the increased (and unearned) value that will accrue to the property

Potential hardship concerns arising from property taxes can be resolved through liens and deferment systems. The NERI's view is that the yield from the local property should, at minimum, be increased three-fold from its current yield and that additional yields should be sought from the taxation of other forms of immovable property, whether via a site value tax, a tax on commercial property, or some combination of the two.

Economic inequality is a function of income inequality and wealth inequality amongst other factors. While our tax system does a good job of recognising and ameliorating income inequality, it only very modestly addresses wealth inequality.

The distribution of wealth is much more concentrated than that of income, and wealth inequality grows over time in the absence of progressive capital taxation and the taxation of acquired wealth. Most wealth is inherited and therefore unearned. Modest taxes on wealth (net wealth taxes, estate taxes, and inheritance and gift taxes) are likely to have minimal impacts on economic growth and poverty relative to taxes on labour, taxes on consumption, or taxes on capital income.

The current range of reliefs and loopholes related to Capital Acquisition Tax (CAT) is very generous and enables the very wealthy to minimise their CAT liability. For example, the business and agricultural reliefs enable the inheritance of over €3 million in unearned income before attracting any liability and thus the tax-free transfer of substantial amounts of wealth across generations. This is obviously repugnant to horizontal and vertical equity and depletes the tax yield. It is also unclear whether there is any economy-wide return on these reliefs. The absence of a ceiling on these reliefs is particularly difficult to justify. One argument is that business and agricultural property reliefs might prevent businesses splitting up. However, the retention of medium-term businesses across generations might actually harm the efficiency of the economy through inferior management practices. One possibility is to offer an instalment relief for businesses and farms, which could enable tax payment over multiple years at very low rates.

The tax-free threshold for CAT is itself generous and consideration should be given to reducing the threshold. However, the main focus of reform should be on the system of reliefs. Finally, there should be a review of the exemption for spouses as the absence of a ceiling on the exemption is difficult to justify.

Wealth is a function of past endowments (mainly inheritances), past income flows, past value changes, as well as past saving and consumption decisions. A tax on net wealth would have important political economy benefits. In particular, the perception of social solidarity would make easier the introduction of other desired tax and welfare reforms. However, Ireland should not pursue the type of wealth tax that has tended to prevail internationally. These taxes have been characterised by high rates and numerous exemptions.

The OECD point out that the way that a wealth tax is designed will have an enormous impact on its effectiveness and fairness. In addition, the equity goals underpinning the wealth tax imply the need to tax 'excessive wealth disparities' rather than 'all wealth'. An NERI working Paper by McDonnell (2013) summarises the arguments for and against the introduction of a tax on net wealth with regard to the key underlying objectives of (A) meaningful yield, (B) horizontal and vertical equity, (C) minimising economic distortions and risk of capital flight, and (D) minimising administration and compliance costs. He argues that the most compatible structure is one with (1) either zero or very few exemptions and reliefs, (2) a high threshold of liability (e.g. €1 million net wealth), and (3) a flat marginal rate that is set at a low level (i.e. below 1%). Overall, he finds that such a net wealth tax is feasible as a complement to income tax and would yield in the low hundreds of millions of euro, although precise estimates are impossible in the absence of up-to-date wealth distribution data.

See Lawless and Lynch (2016), McDonnell, (2018) for tentative yield estimates. Lawless and Lynch describe a scenario with a 1% rate, a €1 million personal threshold (doubled if married) and an additional €250,000 per child. This would have generated €248 million in 2013 and affected just 1.5% of households. Net household wealth has increased significantly in the interim. In practice, a rate of 0.5% might be more appropriate. As an example, a threshold of €2 million for a couple, with a marginal tax rate of 0.5% implies an effective tax rate of just 0.17% (€5,000) for a household with net wealth of €3 million.

Overall, the NERI's view is that the tax system should be compositionally reoriented towards taxes on property and wealth relative to other tax types. However, this statement does not apply equally to all property taxes. For example, stamp duty receipts tend to be volatile and are often sharply pro-cyclical. Stamp duty also discourages capital transactions and acts as a barrier to economic efficiency. As such, there is an argument that stamp duty should gradually be replaced with other taxes on assets or wealth.

The NERI's main concerns in relation to Capital Gains Tax (CGT) are related to the significant reliefs that are available. Reliefs of concern are the exemption from CGT on the disposal of the principal private residence (PPR relief), entrepreneurs' relief and retirement relief. The PPR relief is obviously incompatible with horizontal equity and has no obvious economic justification. The PPR relief also creates an economic distortion in so far as it biases saving in the form of owner-occupied housing and therefore contributes to higher house prices while disincentivising investment in other potentially more productive assets. It's notable that homeowners are also benefiting from zero taxation on the imputed rental income arising from owner-occupied housing. This problem could theoretically be addressed, at least partially, via a higher rate for the local property tax.

Kakoulidou and Roantree (2021) point out that entrepreneur relief creates an array of economic distortions. Notably it discourages the disposal of business assets to those who could manage them better. The entrepreneur and retirement reliefs are difficult to justify on equity grounds and are of unclear economic efficacy. The NERI is of the view that supports for entrepreneurship should emphasise the start-up stage rather than the disposal/transfer stage. This is discussed further in the section on 'supporting economic activity'. At a minimum, it is reasonable that a lifetime ceiling on the total value of CGT reliefs claimed (excluding the exemption on the first €1,270 of gains in any year) should be introduced.

The Welfare System

Our view is that Ireland's welfare system should evolve from one of poverty amelioration to a system that also provides income security when faced with unemployment, illness, disability or other absences from work e.g. due to maternity/paternity and support in the first year of life. Adequacy of income for all should remain the primary goal of the welfare system. This suggests that all welfare payments should be benchmarked to a relevant cost of living baseline and should increase at faster rates than inflation where currently below that baseline. We note that per capita public spending in Ireland is amongst the lowest amongst high-income European states with the annual shortfall relative to the peer country average usually well in excess of €10 billion (see Goldrick Kelly et al, 2020). Our low age-related expenditure explains only a small proportion of this gap.

Our view is that rather than simply focusing on direct cash payments, welfare and well-being policy should gradually move to a more holistic 'cost-of-living' perspective. In particular, expanded provision of universal basic services (UBS) would be one of the most structurally important policy shifts that any government could take from an economic inequality and cost-of-living perspective. (see McDonnell, 2020 for a discussion). Universal right of access to basic services should be on the basis of need and not ability to pay. A non-exhaustive list of essential needs might include health, education, housing, transport, childcare and adult care. Such a policy programme of free or heavily subsidised provision, where relevant to context and need, would amount to a de-commodification of the affected range of services. As such, it would provide a virtual income and diminish the importance of market-based income – particularly significant in a country with high market inequality.

UBS can also support other policy goals. For example, expansion of services such as free child and elder care would have a positive impact on potential growth by reducing barriers to labour force participation and education, while widely accessible free or heavily subsidised public transport would assist with achieving our national climate goals in a manner consistent with just transition principles.

Social insurance

The pandemic led to the creation of new systems of support for the unemployed that have shown that the capacity for such a system change is possible and that change is desirable. Providing income security in times of economic disruption not only alleviates distress for individuals and families, it is also a key investment in economic recovery. The next twenty years will be characterised by the green and digital transitions, and indeed other transitions. This will lead to significant economic upheaval and the need for a just transition amid periods of unemployment for workers in declining sectors or with out-of-date skills. Our view is that a European style social insurance system for employees and the self-employed funded through PRSI is the best way to respond to future transitions and the vagaries of the economic cycle.

Social insurance should deliver adequate basic income security for all employees. Achieving this will require significant increases in PRSI contributions even before one considers the future costs of funding the pension system for an ageing population. Our view therefore is that the changes proposed by the Pension Commission do not go far enough in terms of future additional revenue needs.

Nearly all EU countries operate some form of unemployment insurance with varying degrees of coverage and a wide variation in terms of replacement rate of previous income. Ireland is a notable outlier in terms of the weakness of its social insurance system. Ireland's net replacement rate for short-term unemployment benefit was just half of the EU27 average in 2019. A sudden fall in household income puts strain on the ability to make ends meet and means that Ireland has weak automatic stabilisers during recessions. Higher replacement rates would act as a form of countercyclical stabiliser that reduces the amplitude of recessions. The low replacement rate can force people into jobs that may not suit their skillset – thereby causing a misallocation of human capital. The reduced freedom to engage in short-term risk-taking will also lead to lower levels of entrepreneurship.

In some countries, unemployment insurance stands separate to other unemployment benefits and in other cases, unemployment insurance interacts with unemployment benefits. In Sweden unemployment insurance stands alone. The inkomstbortfallsförsäkring (income-related benefit) provides 80% of pre-unemployment benefit for 200 days, falling to 70% for the following 100 days. Both rates are subject to maximum awards. At the other end of the scale, Estonia pays 50% of previous earnings for the first 100 days followed by 40% thereafter. In the case of Finland unemployment allowance and insurance interact. There is a basic unemployment allowance of between €33-38 per day. The earnings-related unemployment allowance then pays 45% of the difference between the basic allowance and what the pre-unemployment earnings of the recipient were. This rate falls to 20% for very high earners.

Before the onset of the pandemic, the only other countries in the EU beyond Ireland and the UK not to offer earnings linked unemployment insurance were Greece, Poland, Malta and Romania. These countries, along with the UK and Ireland, operate flat rate unemployment benefits with degrees of variation. Malta is the only EU country to operate a flat rate scheme with no relationship to previous labour market status. Within the other flat rate schemes there are linkages to previous earnings and employment, but they do not proportionately determine the level of payment. For instance, in Greece, the basic unemployment allowance is €399.25 per month, but this is also the maximum basic allowance. There are two lower band monthly payments of €299.50 and €199.75 which are paid if the claimants income falls below a certain percentage of the average wage. In this case previous earnings determine the level of flat benefit, but they do not proportionately determine the level of that benefit. In Poland, there is a similar system, but it is determined by years of employment rather than previous earnings. There is a basic unemployment allowance of PL 881.30 (€197) per month. However, depending on the years of economic activity a claimant may be entitled to either 80%, 100% or 120% of the basic unemployment allowance. In both cases the key difference is that previous earnings and experience influence what pre-determined allowance the claimant is entitled to unemployment insurance model.

Having unemployment insurance avoids individuals having to make their own savings pot to deal with unemployment. This is one of the benefits of any type of insurance whether it be for cars, travel or indeed life itself. Insurance covers contingencies that could happen but might not happen. If everyone makes allowance for the fact that they might become unemployed, you have a situation where every household is saving money for an event that is only likely to affect a small minority. By any analysis that is not an efficient outcome. Unemployment insurance therefore enables 'risk-pooling' whereby all workers pay a fraction of the cost of providing the cover that ends up paying out to those unfortunate enough to experience unemployment.

The benefits of insurance are not just limited to the payments that are forthcoming in the event of adverse outcomes. There is also a 'security benefit' that such insurance provides. In other forms of insurance, this security effect can be troublesome if it goes too far and encourages risky behaviour. However, with unemployment insurance the reduction in risk aversion can have a significantly positive effect by pushing people towards newer and better jobs. Jobs in newer areas of economic activity may not seem as secure and workers may be unsure about moving to such jobs, irrespective of higher potential salaries. This is crucial when we consider the kind of shift in jobs that will be necessary to tackle climate change. Many of these jobs will be with new firms and the jobs themselves may be unknown to most people. Unemployment insurance removes this risk and enables workers to take a gamble on one of these new jobs. More broadly unemployment insurance can encourage entrepreneurship, as starting a business or expanding a business requires taking a significant risk with an individual income. Without unemployment insurance, that risk can be too high for many households. Therefore, unemployment insurance also has the benefit of boosting economic performance even if it never has cause to pay out any significant amount. Household earnings are therefore a natural candidate for insurance, however the benefits outlined above could just as easily apply to private insurance schemes as they do to state social insurance schemes. Why then is state provision of unemployment insurance as pervasive as it is? If the alleviation of risk aversion is the key benefit of providing insurance of any type, the countervailing disadvantage is moral hazard. In the example of car insurance,

providing cover can allow people to make full use of their car without fear of being finically crippled by accidents. On the other hand, it can also encourage some people to go too far and increase risky behaviours such as speeding. It is not possible to know whether the person you are insuring will go too far and this problem is referred to as information asymmetry. To combat this, car insurers have several strategies to screen customers and apply price premiums appropriately along with conditionality to benefits to tame such behaviours. Such strategies do not apply to unemployment insurance. It is one thing to seek to identify whether personal traits, financial circumstance and other behaviours are likely to indicate whether a person is a responsible driver or not. It is quite another matter to be able to glean from these data whether a person is likely to become unemployed at any time of their working life. The information asymmetry involved in unemployment insurance is simply too complex to overcome and for this reason state provision has always been the norm. The state has the financial clout and can amass the scale of risk pool necessary to make any such scheme financially viable (see Mc Flynn, 2021a and Mac Flynn, 2021b for a more in-depth discussion).
Our view is that social insurance should be reformed to include a pay-related element, to incorporate unemployment benefit, family benefits, illness and disability benefits, with contribution rates and benefits gradually converging on average EU levels over the medium-to-long-term. However, an upper threshold for benefits should be introduced that caps benefits at a level close to the annual median full-time wage. We note that employer social insurance contributions are particularly low relative to EU average and that self-employed contributions are disproportionately low relative to other workers. Raising self-employed contributions may also reduce the prevalence of bogus self-employment.
These proposed reforms should take place over the medium-term and revenues needed are in addition to the additional PRSI resources required to meet rising pension costs over the medium-to-long term.

Chapter 2 - Fiscal Sustainability

1 What reforms to the taxation and welfare systems should be considered to ensure the system is sustainable and resilient and that there are sufficient resources available to meet the costs of public services in the medium and longer term?

Please specify taxation reforms you consider important::

We agree that efforts must be taken in upcoming years to ensure sufficient and stable revenues in order to place debt on a downward trajectory as a percentage of GNI*. While Ireland's high public debt is of concern the high debt per capita is somewhat counterbalanced by its high income per capita. Ireland's pre-pandemic fiscal position was relatively strong with a deficit in 2019 of just 0.5% of GNI*, albeit with an overreliance on corporation tax receipts. The likelihood is that the European Central Bank's monetary policy will start to tighten in 2023 and that this will eventually feed through into higher borrowing costs. The chances of a debt spiral are very low given the ECB's willingness to do whatever it takes to underpin euro area governments. Ultimately, the optimal way to increase fiscal sustainability is to undertake reforms that structurally increase employment rates over the economic cycle. Total revenue will need to be calibrated to medium-term spending needs. However, this does not necessarily imply that Ireland should avoid running modest deficits on average over the economic cycle. Modest deficits are consistent with a falling debt to output ratio in the context of an economy with potential growth capacity of 4% to 5%. Investments in productive capacity are necessary to grow the economy and to make it more sustainable over the longer-term. For example, it makes sense to borrow for the cost of the green transition. Tackling climate change will require enormous capital investment by the Irish government over the next 30 years.
Ireland should commit to an expenditure rule whereby annual increases in non-cyclical public spending net of revenue measures should be aligned to the medium-term growth potential of the economy. The expenditure rule would need to be able to react to possible fiscal shocks such as a reversal of recent gains in corporation tax receipts. Structural losses of this nature would need to be compensated with revenue raising from other sources with these net revenue increases timed to fiscal upswings. As stated previously, the sustainable level for the structural deficit is itself a function of the economy's growth potential, with the economy's growth potential endogenous to the quality, amount and type of public spending investments and the structure of the tax system. Sustainability is therefore not just a short-run accounting exercise. Composition matters with the long-run impact of, e.g. public investments, fundamental to our understanding of sustainability dynamics.

Combined tax and SSC revenues are low relative to the EU average, and especially low compared to other high-income EU countries. In addition, the future trajectory of corporation tax receipts is highly uncertain and it would be unwise to assume that the current level of receipts can be maintained. The NERI's view is that net revenues will need to rise significantly in the coming years.
Consumption tax reform should focus on negative externalities, in particular those related to GHG emissions. However, tax yields related to the green transition (e.g. carbon tax) may not be relied upon to generate meaningful yields in future decades and will therefore not enhance fiscal sustainability over the long-term. It is important therefore that these yields are not embedded into paying for day-to-day current expenditure. Instead, these resources should be placed into a hypothecated fund that is used to pay for the investments needed to fund Ireland's green transition. The yields from the relevant environmental taxes will naturally decline as our national GHG emissions decline and so it is appropriate to distinguish these resources from more sustainable tax yields from sources like the income tax and VAT. Once we achieve the green transition then the investments required for that transition will no longer be needed and therefore the hypothecated tax revenues will no longer be needed.
The two areas of significant under-taxation in Ireland are the taxation of capital stocks and the very low PRSI rates. Our view is that the taxation of capital stocks should be increased in a number of areas including Capital Acquisitions Tax (CAT), the Local Property Tax (LPT), a new tax on all property unaffected by the LPT (e.g. a Site Value Tax) and a new tax on net household wealth.
We are also of the view that employer PRSI and self-employed PRSI rates should both increase. These are both very low by EU standards. In practice, we anticipate that the incidence of higher employer PRSI will at least partially fall on employees in the form of lower medium-term wage growth. We note that the implicit tax rate borne by employees (income tax, USC, employee PRSI) is already in excess of the EU average. Even so, there is scope to broaden these tax bases
Finally, the use of tax expenditures should be curtailed over time. Tax expenditures are hidden public spending that narrow the tax base, making it necessary to set average tax rates higher than they would otherwise have to be on households not in a position to avail of many tax reliefs.
Our taxation proposals are discussed in greater depth in our response to section 1.

Please specify welfare reforms you consider important::

Our view is that increased emphasis on public services, the UBS model, is preferable to a system based on secondary income benefits and that policy should increasingly move in that direction.
Specific reforms are discussed in greater depth in our response to section 1. In particular, our view is that we should move from a system based on

poverty amelioration to one based on security (social insurance) and income adequacy. Marginal effective tax rates should be kept low for low income households. This means that there should be no cliff-edges (step effects) in terms of welfare supports or in terms of effective tax rates (for employees and employers). Shallow tapering should be applied to welfare benefits so as not to disincentivise employment, with additional supports for cohorts finding it difficult to take up work such as lone parents and people with disabilities. Ireland's tax base is hampered by its low wage model. Progression to a living wage would reduce dependency on in-work payments from government and would assist in the long-term transition to a high road model based on high productivity and high wages.

2 Rate each issue below in terms of strategic importance to the taxation and welfare system over the next 10-15 years (1 being least important and 5 being most important):

importance options - Achieving good public health outcomes for our people:
5

importance options - Addressing the climate crisis:
5

importance options - Adequate social transfers and benefits:
5

importance options - Growing employment:
5

importance options - Sustainability of public finances:
5

importance options - Sustained economic growth:
5

3 Given approaching demographic pressures and future uncertainties, future funding of public services is a critical issue. In order to meet these challenges, what is the appropriate balance between the taxation of a) earned income, b) consumption e.g. VAT and c) wealth e.g. capital acquisitions tax?

Please outline your views::

It may be unhelpful to seek to achieve a specific percentage terms balance between earned income, consumption and wealth. The desirability of individual reforms should be considered in terms of how they impact on the general policy goals of income adequacy, equity including the perception of solidarity, economic efficiency, and sustainability as well as more specific policy goals such as in areas of healthcare and housing. The overall package of reforms recommended by the COTW should, in aggregate, enhance the attainment all of these goals. Certain reforms, for example abolishing the help-to buy scheme, are consistent with all of the general goals, whereas other potential reforms such as the abolition of environmental tax reliefs or the Special Assignee Relief Programme require consideration of the trade-offs between the general goals.
Our view is that contributions to net revenue raising will require contributions from all three of the areas described in the question above. That being said, our view is that the system should increasingly emphasise the taxation of wealth (e.g. LPT, CAT, SVT) due to the regressive impact of increasing consumption taxes and commensurate risk of increasing poverty, and due to the need to stay competitive other jurisdictions and not disincentivise the earning of income. The composition of the taxation of earned income should gradually deemphasise income tax and move towards greater taxation of USC and PRSI.

Chapter 3 - Promoting Employment

1 What reforms to the taxation and welfare system should be considered to ensure that taxation and welfare work in tandem to support economic activity and promote employment while also supporting those most vulnerable in an equitable way?

Please outline what reforms should be considered::

We are of the view that Ireland should move to a European style social insurance system for the reasons outlined earlier. This system will better enable Ireland to manage the upcoming economic transitions, will encourage entrepreneurial risk-taking and human capital development, and will help reduce the amplitude of economic recessions by smoothing aggregate demand. Aligning the rates of PRSI will help reduce the incidence of bogus self-employment. Aligning the rates also implies that the self-employed should have access to the same benefits as employees. This would reduce the consequences of business failure for households thereby increasing the desirability of taking a risk to start a new business.
Marginal effective tax rates (METRs) should be maintained at low rates for low paid workers. The low tax rates should be considered a positive feature rather than a bug. Low rates minimise employment disincentives as well as the risk of in-work poverty. In order to minimise METRs, welfare payments should never be subjected to cliff edges but instead should always be tapered away at a low rate as income increases. The step-effects in the PRSI system should be removed as these create a disincentive to work and a disincentive for employers to increase hours.
The tax system should phase in full individualisation (individual taxation) in order to reduce the potentially significant employment disincentives that can exist for second earners within couples. The current system (along with lack of access to low cost child and elder care) may be contributing to Ireland's relatively poor participation rates for women. The higher SRCO for married households with one income should be aligned with the SRCO for non-married one earner households.
Incentivising businesses to enable their workers to work from home could help ameliorate weak employments rates for cohorts experiencing particular barriers to labour force participation such as a disability or a caring responsibility. In addition, consideration should be given to introducing a partial six-month employer PRSI relief for businesses hiring long-term unemployed workers.
Supporting the vulnerable can also be achieved by increasing wages. The COTW should therefore consider how Ireland can transition to a Northern

European style high value added and high pay model. Useful steps for consideration in this regard include benchmarking the national minimum wage to the living wage and/or establishing the legislative machinery to enable and support collective agreements for each economic sector.

2 Does Ireland's taxation and welfare system strike the right balance between maintaining the incentive to increase earnings and alleviating some of the risks of low income (poverty and deprivation)?

Yes

Please explain your view::

The taxation and welfare systems perform reasonably well as a system of income redistribution. The combined system also succeeds in significantly reducing the incidence of poverty and deprivation. Ireland is one of the best performing countries in Europe in terms of reducing poverty rates through its welfare system. However, the strongly progressive structure of labour taxation also plays an important role. Tax rates are low for most low paid workers relative to other OECD countries and this helps maintain strong incentives to engage with the labour market while reducing the propensity of in-work poverty. The vast majority of people have a financial incentive to work although care should be given that in-work benefits for low paid workers are always tapered away slowly. The withdrawal of means-tested benefits can create poverty traps if it pushes the METR high enough. Consideration should be given to enhancing the Working Family Payment to further reduce replacement rates for families.
Finally, it is important to note that the incentive to take-up work can also be increased by increasing wages for low income workers. The sufficiency and reliability of wages and solutions to the issue of low pay ought to form part of the COTW's deliberations when considering employment disincentives and the risk of in-work poverty. It is not reasonable to expect the state to be responsible for effectively subsidising low wage enterprises via the welfare system

3 Are income supports equitable in terms of how they treat people of working age?

Yes

How is this balanced with the requirement to meet differing needs?:

The income supports are broadly equitable in terms of how they treat people of working age. The medical card is somewhat more difficult to assess as it is a non-cash benefit. Fear of losing the medical card may be a disincentive to take-up work or increase hours. Moving to a free universal health care service would of course eliminate the potential employment disincentives. In the shorter term, it should be possible to design a system that effectively tapers the benefits of the medical card with income by providing subsidies that reduce the gross cost to the household on a declining basis along with income.
Our view is that the use of secondary benefits is appropriate in principle. Households have different needs and circumstances and an increased complexity in the system is justified in order to accommodate these heterogeneous needs.

4 What changes to the social insurance system should be considered to ensure sustainability into the medium to longer term? (Please note the recommendations of the Pensions Commission and NESC Report 151 on the future of the Irish social welfare system)

Please specify changes to be considered?:

Our proposed reforms to social insurance benefits are discussed in an earlier section. Social insurance rates will need to increase even in the absence of those reforms, and PRSI increases should be the COTW's main focus with regard to increasing the net revenue yield from labour taxation.
There is significant scope to gradually increase employer PRSI given its low rate relative to other EU countries. Our view is that the proposals of the Pensions Commission do not go far enough in terms of the increased size of the contribution from employers. Self-employed PSRI contributions should be aligned with combined employer and employee contributions and the benefits aligned with those of employees. Reforms to employee PRSI should be considered in the context of Ireland's relatively high average ITR on employee income, although an increase in employee PRSI and an expansion of the PRSI base would be reasonable in conjunction with any extension of the benefits. We agree with the Pensions Commission that the earnings threshold should not be increased as this will unduly and disproportionately impact vulnerable groups of workers.

Chapter 4 - Climate

1 As Ireland moves to a low carbon economy, what should be the role of the taxation and welfare system in:

a) taking advantage of opportunities? :

The Irish state must utilise every fiscal tool at its disposal to realise our climate goals. The State's approach should attempt to maximise "win-wins" which advance both environmental and social sustainability. This isn't simply desirable but necessary if climate targets are to be feasible. The taxation and welfare systems are crucial to the state's capacity to achieve such a Just Transition. The sustainability of the Just Transition will depend upon the availability of technological alternatives

However, wider state policy must be attentive to the potential differential impacts of these changes across groups. The tax and welfare system must address the potential regressive impacts of measures such as carbon taxes. The state must also encourage greener activities so costs are not simply imposed in the absence of alternatives. Inducements – such as rebates for electric vehicle use – should be accompanied by a wider programme of state investment in areas like public transport, energy infrastructures and R&D to make green options more feasible.

b) mitigating the risks? :

Tax policy should also be attentive to the differences in environmental impact across the income distribution. Evidence suggests that wealthier groups contribute disproportionately to emissions, primarily through consumption tied to luxury items (Ivanova and Wood, 2020). This suggests a potential role

for sliding taxes on carbon and other pollutants relative to necessary items. Policy should be sensitive to whether alternatives are available for necessities as sequencing is important in terms of fairness and public acceptance of the transition. Taxes on luxury items like air travel, larger cars and tourism would disproportionately impact richer households and could also promote sustainability in their own right.
On the welfare side, new supports introduced during the Covid pandemic could offer a template for new transition supports which reduce harm to individuals and encourage upskilling needed for high quality green jobs. Recent research from the New Economics Foundation (2021) pointed to the potential for short-time work scheme supports to facilitate in job upskilling in affected areas. These schemes could remove barriers to upskilling – which are often financial – and redress Ireland's low in-job training rates.

c) in meeting Ireland's emissions targets?:

On the tax side, policy must encourage sustainable production and consumption activity. This entails both an end to all direct and implied supports for damaging activities as well as increased environmental taxes. All environmentally harmful tax expenditures and fossil fuel subsidies should be abolished or phased out. Eliminating the diesel excise gap should be done as soon as possible. Consideration should be given to supplementing the carbon tax with a levy on methane emissions with the revenue then used to help the agriculture sector shift to a more sustainable model.

2 Are there existing taxation and welfare measures that are counter-productive to Ireland's climate change commitments?

Yes

If yes, please specify::

According to the CSO, direct and indirect subsidies to fossil fuel use reached record levels in 2019, at €2,356 million. These subsidies cannot be sustained if policy is to be guided by ecological science.

However, some of these direct and indirect subsidies support necessary items and mitigate deprivation such as fuel poverty. As mentioned, in the absence of policy supporting alternatives, reforms could simply impose additional costs while doing little to mitigate emissions. Certain reliefs should therefore be phased out alongside accompanying enhancements to income supports and the roll-out of technological alternatives.

To what extent are these justified in the Irish context and are any reforms necessary?:

Welfare supports for example, could do more to significantly support home retrofitting in conjunction with other state programmes, which could reduce the need for fuel allowances. Despite a widespread consensus on the desirability of home retrofits, policy to date has been insufficient to redress the significant financial barriers which face most households. The tax system could also encourage take up of new greener technologies in sectors like haulage in tandem with the necessary removal of supports for fuels like diesel.
The distributional implications of various supports could also imply a certain staggered approach. Reforms which initially target reliefs to sectors such as aviation may have more progressive distributional implications than changes which affect road transport or home heating.

3 What changes should be made to the taxation system to ensure longer term fiscal sustainability given the expected impact of the continued decarbonisation of the Irish economy, in particular the impact of reducing tax revenues from energy, carbon and motor taxes?

Please detail the changes::

A short to medium term increase in environmental taxes should be pursued but not relied upon as a long-term source of funding. As the tax take in these areas declines with policy successes in reducing fossil fuel use, government could pursue taxes on these new assets, or new levies such as congestion charges, taxes on air travel, waste taxes and car park levies. The green transition represents an opportunity to rethink transport policy with the tax system utilised to incentivise public transport via new forms of disincentivising private car usage.
However, our view is that the revenues from environmental taxes be ring-fenced for the once-off costs associated with the green transition. As the transition is achieved and the revenue yield declines the commensurate need for the green investments will also decline.
NERI research also points to significant relative shortfalls in Irish revenues relative to other comparable European states which are unrelated to environmental taxes. This relative shortfall is primarily a function of lower revenues from labour, especially in the area of social contributions. This is particularly pronounced on the employer side, with potential additional revenues in the billions. New taxes on capital assets and wealth could raise additional revenues. Medium term reforms along these lines could offset revenue losses from carbon intensive activity

Chapter 5 - Housing

1 Taking into account previous taxation related interventions in the housing market, what role do you think the taxation and welfare systems have to play in contributing to the long-term supply of housing?

Please outline your views::

The appropriate role of the tax system in the housing market is limited. In particular, the disastrous history of the provision of tax breaks for property should prompt caution. The legacy of bad planning and distortion of market prices as a result of tax incentives provided an incentive for imbalanced and disjointed housing developments, inflated house prices, and precipitated a highly damaging boom bust economic cycle. These measures were also highly regressive. Our view is that the State should not use the tax system to respond to short-term supply issues in the provision of housing
The government should cease or phase out all tax expenditures that encourage demand for housing, for example the help-to-buy-scheme. The CGT PPR exemption should be phased out or capped as it makes housing assets more attractive and leads to a misallocation of investment resources. On the other hand, abolishing Stamp Duty on residential property and replacing the yield with recurrent taxes on property (LPT, SVT) would be a beneficial reform. Transaction taxes unlike recurrent asset taxes are likely to contribute to market distortions and are more volatile.
A higher LPT on all residential property combined with a tax on all other land (e.g. through an SVT) would put downward pressure on house prices. This could be supplemented by a surcharge on non-principal residences and vacant properties. Taxes on immovable property are also highly efficient from an

economic perspective. There is a strong case for a significant increase in the LPT.
There are certain tax measures that government could take to increase the supply of houses at the margin. For example, a tax on commercial property might disincentivise demand for new commercial property, thereby reducing prices for commercial property and redirecting construction resources to invest in residential property. The introduction of a site value tax would disincentivise owners to hold on to unused land or keep property vacant. This would have a downward impact on land prices and should ultimately lead to an increase in housing supply. However, neither of these measures is likely to have a particularly large effect.

2 Should the taxation system have a role in supporting or promoting any specific form of housing tenure (e.g. home ownership, rental), or should it remain neutral?

No, taxation should be neutral

Please elaborate further::

Our view is that the state should not promote any specific form of housing. Instead, it should focus on ensuring that everyone has access to affordable, secure and good quality housing regardless of type.
The core issue is affordability not housing tenure. In practice, given the market dysfunction that has been ongoing for close to 20 years, it seems likely that a greater role for the state in direct housing provision is likely to be necessary to achieve this goal.

3 What in your view is the role that taxation should play in housing affordability?

Please outline your views::

Tax policy should seek to avoid measures that stimulate demand as these will ultimately increase house prices and lead to further distortions. Taxes on land and property can be helpful at the margins in reducing land and property prices. The long-term solution to housing affordability is to increase supply, but government should avoid intervening through the taxation system. Our view is that the State should return to its historical role of direct housing provision. The Austrian cost-rental model as proposed by NESC and NERI describes a way to do this.

4 Following the introduction and recent amendments to the Local Property Tax (LPT) and the commitment in Housing for All to introduce a new taxation measure to activate vacant land for residential purposes, do you consider there is a role for a Site Value Tax in Ireland?

Yes, Site Value Tax has a role

Please elaborate further::

We agree that there is a role for a Site Value Tax as a complement to the Local Property Tax. Land taxes tend to be highly efficient and non-distortive relative to other forms of taxation. In addition, as they are a tax on wealth they tend to be positive from a distributive perspective. An SVT would disincentivise the hoarding of unused land and contribute to housing supply. It would also be a sustainable source of revenue that is difficult to avoid and would be relatively straightforward to administer once the initial challenge of determining land values has been surmounted.

Chapter 6 - Supporting Economic Activity

1 How can Ireland maintain a clear, competitive, sustainable, and stable taxation policy with regard to its attractiveness to Foreign Direct Investment (FDI) in light of the rapidly changing global environment?

Please outline your views::

The situation in relationship to FDI policy is obviously fluid given the likelihood of some form of international agreement on corporation tax policy. While welcome from an international tax justice perspective and ultimately from a reputational perspective, these developments do pose questions for the future success of Ireland's current FDI policy. It is unclear whether the surge in corporation tax receipts can be maintained and Ireland's focus on FDI will need to be increasingly complemented with a greater emphasis on developing our national innovative capacity via enhanced investments in human capital, physical capital, R&D, and supports for indigenous start-ups.
The common justification for Ireland's 12.5% corporation tax rate was its attractiveness to FDI and in particular to large multinationals with significant IP assets. Therefore, it's not entirely clear why the new 15% rate should not also apply to smaller non-internationally trading companies. Our view is that the COTW should commission an independent review of the benefits and revenue and reputational costs of retaining the 12.5% rate for smaller firms. Given that Ireland can no longer be 'undercut' in terms of its corporation tax rate, it may be that the negative FDI impact of increasing the rate is not sufficiently significant to justify retaining the lower rate. Other factors such as quality of life and cost of living (e.g. housing and childcare) may be more important for FDI decisions in the future. More independent research is needed.
It's also not clear that there would be any FDI benefit arising from alignment of corporation tax rates for investment income and passive income. For example, aligning the rates might have a negative economic impact by channeling investment into property assets and away from start-ups. Rewarding entrepreneurship suggests that a lower rate should continue to apply to investment income.

2 How can the taxation environment support indigenous enterprise, particularly small and medium sized enterprises (SMEs) to be productive, to innovate and be competitive internationally?

Please specify::

Ireland is not a world leader when it comes to innovation according to most metrics with much innovative activity confined to multinational firms. Overall, the OECD (2013) find that investment intensity in knowledge-based capital is in the bottom half of OECD countries for which data are available, and that while the Ireland is making progress in building up its scientific capabilities, its innovative capacity remains weaker than in other small advanced

economies.
Knowledge production and innovation are fundamental to long-run economic growth. Productivity is ultimately an output of applied knowledge, whether embodied in human capital or in new technology. The non-rivalrous nature of knowledge production opens up the potential for positive externalities in the economy in the form of spill-overs. However, the characteristics of knowledge (only partial excludability, uncertainty in the cost of production) means that it tends to be underproduced from the perspective of society as a whole. The economy-wide benefits outweigh the private benefits so that the market structurally invests less than the optimum amount.
Where there is a structural reason for private underproduction of a good or service that generates positive externalities, then there is a justification for government intervention to remedy the market failure. In other words, there is a strong justification for tax reliefs and government subsidies designed to encourage investment in knowledge production and in the diffusion of innovation. This is also a justification for tax reliefs and subsidies to encourage people to invest in their human capital. These types of supports should be the focus of enterprise policy.
Tax expenditures such as the R&D tax credit are therefore justified in principle although direct subsidies may be more impactful in practice for SMEs. Its notable that almost three quarters of the benefit of this measure goes to large firms. In addition, the R&D tax credit is likely to have a large element of deadweight with greater additionality from direct R&D subsidies.
On the other hand, CAT reliefs for business continuation by blood successors (CAT business and agriculture reliefs) are difficult to justify if the goal is support productivity and innovation. Inherited family firms tend to be poorly managed on average. Our view is that the revenue lost each year on CAT reliefs for business and agriculture provide little benefit in terms of increased entrepreneurship, productivity or innovation.
The resources used on CAT and CGT reliefs would be better targeted at providing enhanced supports to encourage the development, survival and scale-up of new start-ups and SMEs including equity capital investments in those companies. The Start-up Corporation Tax Relief, the Employment Investment Incentive (EII) and Start-Up Refunds for Entrepreneurs (SURE) are conceptually moving in the right direction, albeit the COTW should examine how best to reform the existing schemes. These types of intervention, alongside direct subsidies from state agencies should be the direction of travel in terms of enterprise policy.
The government should examine options for establishing a fund to make equity capital investments in risky high potential start-ups spinning out of higher-level institutions.

3 With regard to starting, scaling or growing a business in Ireland:

a) what features of the current taxation system work well?:

See above

b) what features do not work well and how can these be improved?:

We do not believe that the CAT reliefs and CGT reliefs provide meaningful benefits in terms of starting, scaling or growing a business. The resources used on these schemes would be better utilised on schemes designed to provide new businesses with the necessary early-stage administrative and bureaucratic support and advice, alongside schemes (including tax reliefs) designed to channel equity capital investments to new businesses, as well as direct subsidies for new businesses interested in engaging in R&D or looking to invest in new machinery and equipment that will improve productivity.

Chapter 7 - Tax Expenditures

1 How do you think the process of reviewing taxation measures and taxation expenditures is currently functioning?

Please outline your views::

We do not believe the process of reviewing taxation measures and taxation expenditures is working well.

How well defined do you think the benchmark taxation system is in Ireland?:

The benchmark taxation system is not well defined. A definitive description of the benchmark system including all existing tax expenditures should be published alongside the Finance Bill each year. The Department of Finance could seek assistance from the OECD to ensure best practice in clarifying the benchmark system and appropriate categorisation of tax expenditures.
Tax expenditures are analogous to government-spending programmes and they should be accounted for as part of voted expenditure by topic (e.g. housing, pensions) on budget day as well as in publically available documents updated every year. Tax expenditures are a type of public spending that benefits particular interest groups by treating certain activities or groups in a preferential way. Public spending on tax expenditures tends to deliver larger benefits to higher income households. In particular, reliefs available at the marginal rate will disproportionately benefit high earners. A key challenge for policy analysts is to regularly review these expenditures and ask is there a justification for these exemptions and deductions.

2 How do you think the process of taxation expenditure review could be improved?

Please specify::

Each tax relief will have its own costs and benefits, and these will not be uniform across the population. A specialist unit should be established to review tax expenditures on an ongoing basis. This unit should consider issues of efficiency, equity, sustainability and opportunity cost. The unit should be based within IGEES or within the Parliamentary Budget Office and should report to the Committee on Budgetary Oversight without any interference from the government of the day. Work should not be outsourced to the private sector. The unit's work should be subject to external academic peer review.
The impact of tax expenditures should also be incorporated into annual equality budgets, gender budgets and carbon budgets. Even when there is a clear public policy case for supporting a particular group, or activity, there still needs to be a rigorous social cost benefit analysis of the overall effect of the proposed expenditure including the impact of the need for higher taxes or lower public spending elsewhere to pay for the tax expenditure. The results of the social cost benefit exercise should be transparent with the winners and losers clearly identified months in advance of the proposed tax break becoming law. Policymakers should also measure the social cost benefit ratio for the tax break against the cost benefit ratio for direct public subsidy for the group or activity.

Finally, all tax breaks with a cost in excess of €10 million should have a built-in sunset clause of five years, which automatically triggers unless the Dáil actively renews the tax break. An updated and transparent cost benefit analysis should form part of the process of review in advance of the tax break's expiration with continuation of the measure made contingent upon the results of the analysis.

3 Please give examples of taxation expenditures that you believe run counter to public policy/are badly designed?

Please specify::

Specific examples of poorly designed or inherently flawed tax expenditures include:
• The help-to-buy scheme
• The CAT agriculture and business reliefs
• The CGT retirement, entrepreneur and PPR reliefs
• The excise rates on kerosene and auto-diesel
• The tax-free retirement lump-sum relief
• Medical insurance relief and health expenses relief
• The Special Assignee Relief Programme

Please explain your rationale? :

Tax breaks on capital stocks and stock-generated income are likely to be regressive given the unequal distribution of wealth. Tax breaks such as those related to CAT or the exemption of the principal private residence from CGT are particularly difficult to justify from an equity perspective. Our view is that all of the reliefs identified above should either be abolished (e.g. help-to-buy), or significantly lessened (e.g. the CAT reliefs). Life time ceilings should also be imposed for all reliefs. Finally, the value of the Standard Fund Threshold should be reduced from its current level.

4 Please provide examples of taxation expenditures that you believe work well, either in Ireland or internationally?

Please specify::

It is difficult to identify successful examples of tax expenditures in theory or in practice due to their inherent flaws (e.g. market distortion, regressive). One reason why such reliefs might be justified is where the market can be expected to under-produce a good or service that generates a positive externality or spillover through the economy and society. The traditional example is a tax relief for R&D as the social benefits to new knowledge will generally outweigh the private benefits to the business. A well-designed tax relief aimed at adoption of green technologies or conversion of land-use to facilitate biodiversity or carbon reduction could also be justified in theory as could reliefs that incentivise the hiring of the long-term unemployed.

Chapter 8 - Public Health

1 How well do the taxation and welfare systems support good public health outcomes, addressing health challenges including but not limited to those caused by or related to tobacco and alcohol use, obesity, poverty and/or environmental issues?

Please outline your views::

Tax policy supports good health outcomes via the high excise rates on alcohol and tobacco. The sugar tax was a positive innovation notwithstanding concerns over regressivity. There is a strong case for introducing higher taxes on other unhealthy foods, for example salt. The revenue from taxing unhealthy food could be ringfenced to provide subsidised healthy food targeted at disadvantaged schools.
The introduction of motor tax, carbon tax and the nitrous oxide surcharge on VRT can also be seen as positive from a health perspective. However, the range of environmentally harmful tax expenditures are a concern as they run counter to good public health as well as Ireland's environmental commitments.
Even so, the range of welfare programmes that ameliorate poverty and deprivation are perhaps the most important healthcare interventions arising from the combined tax and welfare system. Poverty and deprivation are strongly associated with negative outcomes in terms of both physical and mental health. Policymakers should ensure that the total elimination of poverty and deprivation in Irish society remains the number one public policy goal.

2 What changes would you like to see to better promote the goal of good public health?

Please specify::

Tax and welfare policy should be consistent with full implementation of Sláintecare, in order to achieve the goal of a publicly funded, universal, single tier healthcare system. Healthcare is a merit good and should be available based on need and regardless of ability to pay. Healthcare should be funded through general taxation. No one should be able to use their financial resources to skip the queue or receive preferential treatment.
This implies that tax reliefs for medical insurance and health expenses should be phased out over time. It also implies that direct subventions to private healthcare provision and private facilities (e.g. nursing homes) should be discontinued over the medium-term as the system transitions to a free and universal single tier model.

Chapter 9 - Administration

1 How can modernisation of the taxation and/or welfare administrations evolve to best meet customer needs in a satisfactory manner while respecting data rights and ensuring secure and reliable tax collection?

Please outline your views::

Administration should move over time towards a real-time whole of government approach to administration. This process should ensure user data rights. For example, users should themselves have access to the tax and welfare information held by the central administration in order that they can query and potentially correct pertinent information.

What do you see as the implications of modernisation for taxpayers either positive or negative?:

2 What improvements in service quality and delivery could be achieved by integrating (elements of) the taxation and welfare administrations?

Please specify::

A whole of government approach to administration would reduce compliance and administration burdens for users as well as reduce unnecessary interactions with state bodies. Means testing could be calculated automatically under a centralised whole of government approach while users could automatically be informed of benefits to which they are entitled. Such an approach would also make it more difficult for taxpayers to avoid paying taxes owed. It would also facilitate valuation of wealth assets such as land as the central administration would be building up a database of purchases. This would make it easier to introduce a hedonic model of asset valuation which would be fairer than a self-assessed model.

Are there any risks arising from such integration? :

Chapter 10 - Submit Your Ideas

1 Taking into account the Terms of Reference, submit any other thoughts, ideas or feedback on taxation and welfare in Ireland:

Please outline your views::