TOWARDS AN *EQUALITY BUDGET*

TASC's Proposals for Budget 2012

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Introduction and Summary

TASC is an independent, progressive think-tank. We carry out research across issues of public policy, politics, economics, culture, the environment and other related fields; and we make our findings available to the public. Our goal is to stimulate new ideas about how we can bring about a more equal society with a stronger democracy.

The national budget represents a crucial set of political choices that affects our economy and society. Budgetary decisions are about who pays and who benefits in terms of taxation and public services. TASC's goal in presenting our Equality Budget is to show how it is possible to balance the goal of equality with economic progress.

Ireland has a high level of economic inequality compared to many other European countries. Compelling research, such *The Spirit Level* by Richard Wilkinson and Kate Pickett, have provided evidence that more equal societies tend to do better economically, but also socially, with lower crime and people enjoying better health. The Nordic countries are among the most equal societies in the world, yet they are also among the most economically competitive. They are not without their problems, but they have been among the most resilient economies in Europe during the global crisis.

The global financial crisis, combined with Ireland's home-grown property crash, is the context in which crucial decisions are being made about how to balance the deficit, reverse mass unemployment and achieve sustainable economic recovery. (A technical analysis of the economic context is given in Section 3).

Three goals for economic recovery

We know that the Irish state has a deficit in its public finances; that is, the state's income (mostly from tax) is much lower than the amount it is spending. Some of this is 'cyclical' or tied to the economic cycle. It is normal when the economy slows down that the state gets less tax money coming in but spends more on welfare due to higher unemployment. A cyclical deficit can be worked through, although a prolonged recession can add a lot to the overall national debt. The more serious problem is that much of the Irish state's deficit is 'structural'. It is a real gap between taxes and spending that can only be closed by a combination of three measures: raising tax, lowering spending and growing the economy.

The IMF estimates that Ireland's structural deficit is 6.8 per cent of national economic output (measured in GDP); that's approximately €10.7 billion.

Austerity measures do not simply equal savings.

Almost all tax increases and spending cuts will *shrink* the economy. While reducing the deficit on one hand, a shrinking economy means fewer jobs, less tax coming in and more welfare spending; which increases the deficit again. Austerity on its own is self-defeating. For example,

despite nearly €6 billion in tax and cuts in the Budget for 2011, the IMF estimates that the structural deficit will only close by 1.4 per cent of GDP or c. €2.2 billion (IMF 2011, p. 24).

Although we must close the deficit, too much attention has been paid to this goal in isolation, as if the rest of the economy will magically recover once the government's finances are in order. In fact, the austerity measures of recent years have done unnecessary harm to the economy and society. There is a need to balance the goal of closing the deficit with two equally important goals: job creation and a new model of economic development.

The key to increasing employment is the supply of jobs – and creating jobs is partially a result of the demand for goods and services those jobs provide. Most people want to work, and recent ESRI and NESC studies have shown that the vast majority of people would be financially much better off if they had a job. The problem is there are far too few job opportunities.

TASC has been pointing to the issue of demand in the economy (also called 'aggregate demand') from the outset of the crisis. Recent IMF papers and others have recognised the need to increase demand in the domestic economy. Not every country can succeed in growing its economy through boosting exports in isolation from developing the domestic economy. This is because for some countries to have net exports, other countries have to have net imports, which few countries want to do right now. Also, the Irish export sector is not as labour intensive as the domestic sector.

One way to increase demand is to increase the spending power of people who are on the lowest incomes. People on welfare or in low-paid jobs spend practically all of their money to meet their essential needs. We can use the tax and benefit system to increase the incomes of the low paid and those on welfare. That will lead to job creation. In the short-term, the Government can also boost demand in the economy by spending money in job-rich areas, like home insulation schemes, road maintenance, etc.

But closing the deficit and creating jobs is not enough. We need to seriously look at what went wrong in the Irish economy. Our model of development was wrong. We built too many houses and apartments, some of poor quality and many in the wrong locations. The property boom and other aspects of the economy were all built on debt; the massive private debt burden which still strangles many businesses and weighs down heavily on many households. We must not go back to debt-driven consumption that creates only unstable and unsustainable growth. What is required is a national debate about what we really value, like education, health and wellbeing. We need to imagine Ireland as a flourishing society, and then adopt the economic model that is best suited to bring this about.

The national budget plays an important role every year in shaping our model of social and economic development. TASC's budget proposals are written with this in mind. In summary form, there are two important facts and three specific proposals for Budget 2012.

Two important facts related to Budget 2012

Every budget affects different groups in society to a greater or lesser extent. Yet the Government does not carry out systematic tests to see what those impacts are, and whether some groups have been unfairly affected.

TASC recently carried out an analysis of Budget 2011 in terms of how it affected different household types and, in particular, how it affected men and women differently. We looked at the evidence, in terms of the distribution of income across different households and the effect of the main tax and welfare changes in Budget 2011. The evidence shows that people on lower incomes lost a greater proportion of their incomes than people on higher incomes. We also found that single people with children lost nearly five per cent of their income from changes to direct taxation and benefit cuts. This compared with a reduction of income of less than three per cent income for most other households. Because higher numbers of women earn lower incomes and/or are single with children, women were significantly worse affected than men. (More detail is presented in Section 4). But even this analysis of tax and benefit changes masks further inequality, because cuts to direct public services have a bigger impact on lower income households who are more reliant on them.

What this shows is that there is a need for every budget to be carefully analysed before and after, to see how it changes the distribution of income and wealth in society, and how it affects different household types and impacts upon men and women differently. TASC advocates a full distributional analysis of budget measures, including equality-proofing and gender-proofing.

A second fact that must be considered at budget time is that Ireland remains a low tax economy. The IMF estimates that tax in 2011 will amount to nearly 35 per cent of GDP, whereas spending will be 46 per cent of GDP. Spending of 46 per cent of GDP is close to the EU average. Some of that increase is due to cyclical effects, such as the higher welfare bill for more people who are unemployed. This extra welfare spending will go down when jobs are created. It is also the case that tax revenue collapsed by a third in the first two years of the crisis. For these reasons, it makes sense for the budget to focus much more on rebuilding the tax system rather than cutting back on services.

In the years leading up to the crisis, the state was able to provide more services of higher quality, even though we had not reached West European standards or efficiency in many cases. If we go back to being a low tax-low spend economy, we will see the removal of many social supports and services, which will harm social cohesion and reduce the quality of life for us all. There are also economic arguments for raising tax rather than lowering spending: Ireland is at such an extreme of low spending that judicious tax increases will do less harm than cutting spending.

Many people would be better off despite paying more tax. Take for example childcare. If everyone paid a little more tax, the state could provide a national system of pre-school education and childcare, which would be cheaper though economies of scale. Many families would be better off from not paying for expensive crèches. With extra money, those families would spend more in the economy, which would lead to job creation. Women who want to

pursue a career would be free to do so, which would also benefit the economy. And it is not just parents who benefit: pre-school education has been shown through countless studies to lead children to achieve more in life, which in turn would benefit all of us, when we are old and they are the main taxpayers and innovators for the future. Of course, this requires careful public policy and good management – but many European countries have a lot of experience in doing this well.

Three budget proposals

TASC's proposals are designed to work within the reality of Ireland's current economic context, and the need to close the structural deficit while promoting job creation. Based on what we know about distribution and taxation, our budget proposals are designed to lead to economic recovery with equality.

Our first proposal is for tax measures that are least damaging to the economy, which are taxes on wealth rather than taxes on labour. International studies have shown that taxing immovable property does the least damage to economic growth and job creation, whereas other taxes, like income tax on low-paid workers, have a more damaging impact on growth and employment, through reducing people's ability to buy goods and services (i.e. demand). These taxes would also help redress the inequality of recent budgets, so that those who have a larger share of wealth pay more.

TASC proposes €3 billion in tax increases, spread across four areas. We have worked out an equality-proofed model of residential property tax. Those whose housing and childcare costs are too high, or whose incomes are too low, would be able to defer payment. Combined with other property-related measures, a total of €1.6 billion could be raised. A further €413 million of taxation on different forms of wealth are proposed, through changes to capital taxation rates and exemptions. TASC has called for the standard-rating of pension tax breaks and other reforms of pension tax law, which would raise €590 million in this budget, and which should be a first step in comprehensive pension reform. Finally, we propose certain targeted taxes on consumption, including excise, carbon taxes and a special tax on sweets/sugar-sweetened drinks, to raise €324 million. Some of this money should be used to counter fuel poverty and for health promotion in schools. (The outline of these taxation proposals is given in Table 1.1 in Section 1. Further detail about these proposals is in Section 2 and tax reform is addressed in Section 5).

Our second major proposal is for the remaining money in the National Pension Reserve Fund (NPRF) to be invested productively in targeted areas that will generate jobs and boost people's skills and training to find work. The pension fund is a national savings account that belongs to the Irish people. That money is best invested now, in order to recover the economy sooner, which will allow us to restore these savings. There is about €4.7 billion left in the NPRF. We propose spending €1.2 billion per year, for four years, to speed up economic recovery.

Our third proposal is to reschedule that part of the national debt incurred mostly due to Anglo Irish Bank, reducing our payment on that debt by €2 billion each year from 2012 for the next number of years. It is important to note that this debt is not covered by the agreement made with the IMF and European institutions, so it is open to renegotiation.

Many of Anglo's bondholders were paid off with money that we borrowed from the European Central Bank by issuing special IOUs (so-called 'promissory notes'). We are now borrowing money from the IMF/EU, paying interest on those debts, and using some of that money to pay back the European Central Bank for the Anglo promissory notes. We are scheduled to pay over €3 billion in 2012, and every year until 2023; and further, smaller payments until 2031. In other words, the Anglo debt burden is still a very real drain on national resources, which will require at least €48 billion in public spending in the next two decades, and up to €85 billion if financed at a higher interest rate (see Appendix A).

TASC suggests that the Government robustly renegotiate the repayment of the promissory notes, by seeking to convert them into a low-interest, long-term government bond (sometimes called a 'bullet bond'). It is not a magic bullet, as we would still have to repay the debt. But repayments would be over a longer period, such as 50 or 100 years. Through this proposal, we could reduce our spending on the Anglo promissory notes by €2 billion in 2012 (as we would still pay €1 billion towards them) and a further saving of €2 billion every year to 2023. (See Appendix A for more details). This money would be much better spent on increasing welfare payments to reduce some of the hardship of recent years, along with investment in childcare and pre-school education. It could also be used for investing in the development of Ireland's long-term productive capacity, in terms of infrastructure and people's education, training and skills.

It is time for a change in direction in the Budget and national economic policy, as a first step towards a new model of development that is environmentally sustainable and which will make Ireland a more equal, flourishing society with an economy designed to enhance people's wellbeing.

Nat O' Connor

Director, TASC

1 TASC's Budget Proposals (overview)

Overview of Proposed Fiscal Adjustments

1. The Irish Government is running a primary structural deficit of 6.8 per cent of GDP (IMF 2011). Discretionary fiscal consolidation over the short- to medium-term period to eliminate this structural deficit is required. However, the proposed speed and composition of the fiscal adjustments set out in the National Recovery Plan and the Memorandum of Understanding are damaging to Ireland's future economic potential and to society.

2. TASC notes that the Government has broadly adopted the budgetary parameters set by the previous administration, most particularly the adjustment of €3.6 billion, prioritising spending cuts over tax increases in Budget 2012, in line with the previous Government's National Recovery Plan. TASC proposes a quite different package of discretionary fiscal adjustments in Budget 2012, focused on revenue-raising measures, which cumulatively add up to approximately €3 billion. These adjustments are targeted at areas that will minimise damage to employment and output. The adjustments proposed by TASC are also designed to protect the public services on which vulnerable groups, in particular, depend and minimising the impact on the incomes and living standards of low and middle income groups.

3. In addition to suggesting revenue raising-adjustments, TASC recommends that the Government robustly push for a renegotiation of the repayment schedule for the promissory notes for Anglo Irish Bank, Irish Nationwide Building Society and the Educational Building Society, which are not covered by the Memorandum of Understanding with the International Monetary Fund, European Commission and European Central Bank. Exchanging the current repayment structure for a long-term bullet bond[1] could reduce Ireland's debt repayments by over €2 billion annually over the next few years. See Appendix A for a fuller discussion of TASC's proposals in this area.

4. TASC's suggested cumulative adjustment on the revenue side is approximately €3 billion. The yields to the exchequer of these adjustments are in many cases conservative estimates, based on best and most recent data, and it is probable the full year yield could exceed €3 billion. TASC is not proposing any tax increases on labour in Budget

[1] A bullet bond is redeemed on a fixed maturity date and pays a fixed rate of interest.

2012, although increases in the implicit tax rate on labour are inevitable in the short to medium term as the current rates are unsustainable. This is discussed further in Section 3. TASC's proposed fiscal adjustments on the revenue side are outlined in brief in Table 1.1. There are a large number of other minor revenue raising measures that should be considered by Government for Budget 2012. However individual measures with an estimated yield below €10 million have not been shown in Table 1.1.

5. TASC's taxation principles are outlined at the end of this section, and explain the economic and equality rationale for the following specific proposals.

6. TASC's proposed adjustments on the revenue side are focused on measures that will cause least damage to economic output and employment while minimising hardship for the most vulnerable. The academic evidence suggests that a recurrent (annual) tax on immovable property is the single most growth-friendly form of taxation. The empirical evidence also suggests that taxes on intergenerational wealth, and taxes on passive income, are amongst the least damaging to growth. In terms of specific budgetary recommendations, TASC is proposing the introduction of a residential property tax and a number of other reforms to the taxation of property. These include guillotining the legacy property-based reliefs and curtailing the ability of landlords to use interest repayments on residential rental property as relief against tax. The precise details of TASC's residential property tax proposal are set out in Appendix B.

7. The goal of putting the tax system on a sustainable and stable trajectory is fundamentally constrained by the excessively high level of personal and private indebtedness resulting from the boom-bust cycle; and in particular the excessive leveraging by households and businesses in relation to buying property. This is likely to require some form of exceptional measures by Government to assist a substantial proportion of the population in deleveraging more rapidly than is possible under existing bankruptcy and other legislation.

8. TASC also proposes significant reform in the treatment of both Capital Acquisitions Tax (CAT) and Capital Gains Tax (CGT). In particular, TASC is proposing that the Universal Social Charge be applied to all income from inheritances, gifts, and capital gains in the same way that it is currently charged on labour income. The existing thresholds for payment of CAT are excessively generous, and TASC proposes a substantial reduction in these thresholds. TASC also recommends amalgamating the agriculture and business

reliefs for CAT and curtailing of those reliefs. Finally, TASC suggests curtailing the CGT exemption for the disposal of a site to a child and abolishing the exemption from CAT of the residual value of Approved Retirement Funds (ARFs).

9. Privileging pensions over other types of investment is damaging to long-run economic growth because it distorts the allocation of investment and creates opportunities for tax avoidance. TASC proposes that the Government reduce the relief on pension contributions to the standard rate of income tax, and in addition reduce the tax exemption for lump-sum payments to the average industrial wage with the balance taxable at the marginal income tax rate and subject to the USC. For equity reasons, TASC suggests that the Government increase the rate of tax on imputed withdrawals from ARFs exceeding €1,500,000.

10. TASC is proposing a number of excise taxes. Specific proposals include an increase in the carbon tax to the market rate of €22 per tonne of CO_2 and implementation of the commencement order on coal and turf. TASC suggests that the €200 tax on car parking spaces, which was announced initially in Budget 2009, be implemented, and also recommends increases in the excises on petrol, cigarettes, beer, cider, spirits and wine. Finally, TASC proposes the introduction of a new excise on sweets and on sugar-sweetened soft drinks.

11. There is a need for fundamental reform of public services. This reform process should include greater transparency and full personal accountability for all decisions made within the civil and public service. All private submissions related to any aspect of public policy should be made publically available, and the rationales for all major decisions made should be explicitly set out, within the budgetary cycle (i.e. twelve month period). See Appendix F for further proposals relating to transparency, equality auditing of budgets, etc.

12. TASC proposes the introduction of annual efficiency and equality audits of all public expenditure programmes, and urges the Government to immediately publish the findings of the Comprehensive Review of Expenditure (CRE). The purpose of an equality audit is to ensure that budgetary changes are not regressive by undertaking a distributional analysis of proposed changes to taxation and social welfare to assess the effects of such measures on all income groups.

13. TASC does not suggest a reduction in net expenditure in Budget 2012 beyond those savings achieved through the ongoing implementation of the Croke Park agreement and through savings on waste identified by the Comptroller and Auditor General's Report. TASC proposes a reallocation of spending between expenditure headers. A number of proposed expenditure increases are identified in Appendix C. TASC proposes that these additional spending measures be paid for through specific measures to be identified following the publication of the Government's CRE.

14. TASC is proposing that the Government deploy the remaining value of the National Pension Reserve Fund to support a temporary programme of investment costing €1.2 billion annually for four years. European Commission data shows that, in 2011, gross fixed capital formation (i.e. investment) in Ireland will be the lowest in the EU as a proportion of GDP[2]. This implies a high level of capacity in the Irish economy to absorb investment. The proposed €1.2 billion Economic Recovery Fund should principally be allocated toward measures to address the structural problem in the labour force. However, consideration should also be given to measures to improve the liquidity of small and medium enterprises as well as to specific labour-intensive projects designed to upgrade the stock of productive capital in the economy. TASC welcomes the European Commission's new project bonds initiative which makes €50 billion available across the EU for infrastructure projects. Any viable strategy for economic recovery must contain measures to enhance growth. TASC's proposal of €1.2 billion per annum in additional strategic investment spending could be used to leverage private sector investment and/or European Investment Bank (EIB) project funding. A strategy focused merely on debt reduction will simply embed structural unemployment and move Ireland permanently to a reduced long-term growth equilibrium (that is, negatively impinging upon Ireland's long-term growth potential). See Appendix D for a discussion on investment multipliers in small open economies.

15. TASC also supports the introduction of a Financial Transaction Tax, or alternatively a Financial Acquisitions Tax, at the European level. This money should be used to create a European wealth fund to pay for future financial crises and to fund countercyclical investment.

[2] European Commission (Spring 2011) *Statistical Annex of European Economy*. p. 66. http://ec.europa.eu/economy_finance/publications/european_economy/2011/pdf/2011-05-13-stat-annex_en.pdf

16. Despite the crisis in the public finances, the Government has reduced the rate of Social Security Contributions (SSCs) for employers in the interim. In the long term, Ireland's public finances will only be fixed in a way that is compatible with Western economy level public services through fundamental reform of the social security system. Currently, SSCs as a proportion of GDP are the second-lowest in the European Union, and are less than half the European average. If Ireland's level of social contributions, when measured as a proportion of GDP, were equivalent to the European Union's weighted average level of contributions, total Government revenue (including SSCs) would have been €11.24 billion higher than it actually was in 2009.

Table 1.1 Proposed Fiscal Adjustments[3]

Area	Proposal	Yield (Cost) 2012
Immovable Property		**€ millions**
1a.	*Residential Property Tax:* *Introduce a 0.30% tax on residential property*[4]	1,050
1b.	*Abolish €200 levy on rented properties; second homes and holiday homes and reduce residential stamp duty on residential properties to 0.03%*	(200)
2.	*Abolition of property based 'Legacy Reliefs on non-residential property. Any unused capital allowances carried forward beyond 2012 to be lost.*	450[5]
3.	*Reduce the level at which individuals and companies can claim interest repayments against tax for residential rental properties from 75% to 40%*	350+[6]
Subtotal		***1,650+***
Capital/ Wealth		**€ millions**
4.	*CGT and CAT Extension:* *Extension of the Universal Social Charge to all gifts and inheritances and also to all capital gains, whether liable to Capital Gains Tax or not. The charge would be levied on the gross amount and not just the taxable amount, i.e. the gift or inheritance or gross gain.*	200[7]
5.	*CAT Tax Free Thresholds:* *Reduce the threshold for Category A to €250,000 and reduce threshold to €25,000 for all other existing Categories*	75[8]

[3] Unless otherwise stated all estimates are from the 2010 Tax Strategy Group, the 2010 National Recovery Plan, the Report of the Commission on Taxation, or from Ministerial responses to parliamentary questions.
[4] Yield assumes a 25% deferral rate.
[5] This figure is likely to be conservative. Case V losses forward stood at €2,365M, based on 2009 returns. Assumed maximum tax cost for 2008 was estimated at €455 million by Minister Noonan (7 July, 2011). Available at: http://www.kildarestreet.com/wrans/?id=2011-07-07.470.0&s=tax+exemptions+for+pension+lump+sum+payments#g472.0.r
[6] This figure is likely to be conservative. Minister Noonan (14 September, 2011) stated the estimated cost of providing interest relief in 2009 for individuals was estimated at €1,150M by the Revenue Commissioners. Available at: http://www.kildarestreet.com/wrans/?id=2011-09-14.800.0&s=%2222016%2F11%22+section%3Awrans#g804.0.r . No figure was provided in relation to property companies. Also see: http://www.kildarestreet.com/wrans/?id=2011-07-21.908.0&s=relief+interest+repayments#g910.0.r
[7] Figure is extrapolated from current CAT and CGT yields. The adoption of this measure would of course increase the yield from the other CAT proposals. These increased yields have not been included in the specific given estimates.
[8] TASC estimate

Area	Proposal	Yield (Cost) 2012
6.	*CAT Reliefs:* *Limit the business and agricultural reliefs for CAT by reducing the level of discount on market value before tax is calculated from 90% to 60% and by introducing a €3 million ceiling on the qualifying amount. Amalgamate into a single relief.*	94[9]
7.	*CAT Reliefs:* *Eliminate the exemption to CAT of the residual value of Approved Retirement Funds*	25
8.	*CGT Exemption:* *Reduce exemption for disposal of a site to a child from 100% to 50%*	19
Subtotal		***413+***
Pension Reform		**€ millions**
9.	*Reduce income tax relief on pension contributions to the standard income tax rate*	500[10]
10.	*Reduce tax exemption for lump-sum pension payments with immediate effect to the level of the average industrial wage. The balance should be taxed at the marginal rate of income tax and should be subject to the USC*	65[11]
11.	*Increase the rate of imputed withdrawal on ARFs with assets in excess of €1,500,000 as follows:* *Value of Fund* *€1,500,001 to €3,000,000 – imputed withdrawal rate of 7.5%* *€3,000,001 to €5,000,000 – imputed withdrawal rate of 10%* *In excess of €5,000,001 – imputed withdrawal rate of 12.5%*	25+[12]
Subtotal		***590+***

[9] Extrapolated from Tax Strategy Group estimates

[10] Response to parliamentary question (October 4, 2011) http://www.kildarestreet.com/wrans/?id=2011-10-04.727.0&s=pension+tax+relief#g728.0.q . See also, TASC's revised pensions policy, *Making Pensions Work for People.* There would likely be an additional windfall tax in 2012 to reflect the increased number of civil/public servants retiring in advance of February because of the superior pension arrangements being offered to this group before February 2012.

[11] There would likely be an additional windfall tax in 2012 to reflect the increased number of individuals retiring in advance of February 2012 because of the superior pension arrangements being offered to public sector workers retiring before February 2012.

[12] Estimate

Area	Proposal	Yield (Cost) 2012
Consumption		**€ millions**
12.	*Environmental:* *Increase the existing carbon tax rate to €22 per tonne of CO_2 and make commencement order on coal and turf, with compensating measures such as fuel allowance.*	176[13]
13.	*Environmental:* *Implementation of €200 car park tax originally introduced in Budget 2009 but never enacted*	10
14.	*Excises:* *Increase the excise on petrol by +2 cent per litre* *Increase the excise on beer and cider by +5 cent per pint* *Increase the excise on spirits by +5 cent per half glass* *Increase the excise on wine by +75c per bottle* *Increase the excise on cigarettes by +10 cent per packet*	138
15.	*Health Promotion:* *Introduction of a 20% tax on sweets and sugar-sweetened drinks[14]. Use the yield to partially fund health promotion measures, including the provision of healthy school meals in primary schools.*	n/a
Subtotal		***324***
Additional Measures		**€ millions**
16.	*The 'number of days' test for determining the tax residence of an Irish citizen should be reduced from 183/280 days to 90/183 days*	Unknown
17.	*Increase the domicile levy from €200,000 to €400,000*	Unknown
18.	*Abolition of certain other minor tax reliefs and exemptions e.g., relief for expenditure on heritage buildings and gardens and exemption from BIK charge on professional subscriptions*	25+
Subtotal		***25+***
		€ millions
Total		3,002 +

[13] Estimates from the National Recovery Plan suggest a €1 increase per tonne will generate €22 million. The addition €22 million revenue reflects the commencement order being made on coal and turf. Compensating measures such as fuel allowance should be prioritised within expenditure.

[14] By way of comparison, Social Justice Ireland have estimated a 2% tax on 'non-nutritious' food would yield €15 million.

Investing in Recovery

17. Based on the weight of empirical evidence (detailed in Appendix D), TASC rejects the argument that Ireland's small open economy status will render fiscal stimulus ineffective. Establishing economic growth is a prerequisite to restoring Ireland's debt dynamics to a sustainable equilibrium. TASC does not accept the Department of Finance's forecasts for economic growth under the parameters set by the National Recovery Plan, because they are too optimistic. The weakening global economy, the low levels of lending to the private sector, the continued deleveraging by the private sector and the Government's fiscal stance will all combine to drag on economic growth and employment levels in the short to medium term

18. TASC is proposing that €1.2 billion per year (0.75 per cent of GDP), for each of the next four years, be taken from the National Pension Reserve Fund for targeted investment in projects that will contribute to the economy's ability to generate long-term Schumpeterian growth[15] and contribute to the reduction of long-term structural unemployment. Typical schemes might include the construction of a next generation broadband network over a number of years in collaboration with the private sector, as well as investment in human capital through the funding of re-training and up-skilling schemes targeted at the long term unemployed. This €1.2 billion could be combined with funds from the European Investment Bank and with the European Commission's new project bonds.

Taxation Principles

19. While all taxes impact upon economic efficiency and income distribution, these impacts differ sharply depending on the type of tax. For example, the distortionary effect on the allocation of resources in the economy is likely to be less severe for taxes on immovable property than it is for taxes on income or consumption. Numerous empirical results, for example Johansson et al. (2008) and Heady et al. (2009), have consistently shown recurrent taxes on immovable property to have the smallest negative impact on long-run economic growth. This is followed by other property taxes and then by consumption taxes such as VAT, excises and certain environmental taxes. Labour taxes and corporate

[15] Schumpeterian growth is 'intensive' growth that is growth that occurs as a result of technological progress and innovation.

taxes tend to have the most distortionary effect on economic activity. The impact on economic growth of a change in tax policy will also vary depending on the country's starting point. There are diminishing returns to adjusting taxes upwards, and tax increases tend to have smaller effects on growth when they are starting from a low base. Thus, low tax countries such as Ireland have a higher potential net benefit from tax increases than high tax countries. Changing the balance of taxation between different tax sources, e.g., by moving from taxes on labour to taxes on property, should be considered a complement to improving the design of individual taxes.

20. In general, consumption taxes tend to be less progressive than personal income taxes, and consequently shifting the composition of the tax take from taxing personal income to taxing consumption is likely to be regressive overall. Likewise, a heavy reliance on consumption taxes as opposed to other taxes such as capital taxes, as is currently the case in Ireland, leads to greater wealth inequality by increasing the value of assets and by shifting the burden of taxation to low earners.
21. Recurrent taxes on net wealth are generally less distortionary than taxes on financial and capital transactions. They are also a mechanism for redistributing income. Wealth taxes also help assist tax authorities in fighting tax evasion and criminal activity by revealing inconsistencies between income flows and wealth. When taxing net wealth an important principal is to ensure that all classes of asset are treated the same way and that no assets, e.g. pensions, are made exempt from the tax. Exempting or giving favourable treatment, such as reduced rates, to certain asset categories distorts private investment decisions and provides a mechanism for tax avoidance. A common strategy is for an individual to borrow money to reduce his or her net wealth, and then use these borrowings to purchase tax-exempt assets.
22. More generous exemptions and reduced tax rates for housing assets, relative to those available for other forms of investment, are likely to be particularly damaging to long-term growth because they distort capital flows away from productive sectors and toward housing. Housing assets have long been given favourable treatment in Ireland. This has undoubtedly harmed long-term growth and negatively impinged on the accumulation of productive capital by the private sector. It certainly contributed to the boom-bust cycle that produced the current economic crisis.

23. Finally, inheritance taxes are an important complement to net wealth taxes. These taxes have a minimal impact on economic growth and play an important redistributive role in the economy. Gift taxes are a necessary supplement to inheritance taxes, as otherwise it is straightforward to avoid the inheritance tax.

2 TASC Taxation Proposals for Budget 2012

Proposals for the Taxation of Immovable Property

24. Overview: The arguments for a recurrent tax on immovable property are overwhelming on both efficiency and equality grounds. In particular, recurrent taxes on residential property have been shown to have a minimal negative impact on growth, are hard to avoid or evade, are stable throughout the economic cycle, do not penalise productive activity and do not create barriers to labour mobility. Tax breaks for non-productive assets such as houses and hotels distort economic activity away from more productive uses, and for this reason are generally damaging to economic growth. Such tax breaks are also regressive as they principally benefit the very well off. Taxing property is particularly appropriate in the context of increasing globalisation, where the other factors of production (labour and capital) are increasingly mobile.
25. TASC is proposing the introduction of an annual Residential Property Tax (RPT) which would be set initially at 0.30 per cent of the gross value of the home. To prevent hardship, a mechanism should be introduced to enable those on low incomes to defer payment. TASC's proposal is outlined in greater detail in Appendix B.
26. In the event of a universal residential property tax being introduced, TASC proposes that the current €200 levy on rented properties, second homes and holiday homes be abolished and that the stamp duty on residential properties be reduced to 0.03 per cent of the value of the home.
27. TASC is proposing that the level at which individuals and companies can claim against tax for interest repayments for residential rental properties be reduced from 75 per cent to 40 per cent.
28. TASC is proposing that all property-based 'Legacy Reliefs' on non-residential property be abolished. Any unused capital allowances carried forward beyond 31 December 2012 should be lost.

Proposals for Reform of Capital Gains Tax and Capital Acquisitions Tax

29. Overview: Taxes on property tend to be less damaging to economic growth and employment than most other taxes. In addition, intergenerational wealth transfer runs counter to the principal of equity as it perpetuates economic inequality.
30. TASC is proposing that the tax free thresholds for Capital Acquisitions Tax (CAT) be reduced to €250,000 for Category A and to €25,000 for all other categories
31. TASC is proposing that the Universal Social Charge be extended to all gifts and inheritances and also to all capital gains, whether liable to Capital Gains Tax (CGT) or not.
32. TASC is proposing that the business and agricultural reliefs for CAT be amalgamated and that the reliefs for CAT be limited by reducing the level of discount on market value before tax is calculated from 90 per cent to 60 per cent, and by introducing a €3 million ceiling on the qualifying amount.
33. TASC is proposing that the exemption from CAT of the residual value of Approved Retirement Funds be abolished.
34. TASC is proposing that the 100 per cent CGT and stamp duty exemptions on the disposal of a site to a child should be replaced with a relief set at 50 per cent of the value that would otherwise be charged.

Proposals for the Reform of Pension Taxation

35. Overview: The Irish taxation system is characterised by a number of very generous pension related tax reliefs. These reliefs tend to principally benefit higher groups. The economic argument for privileging investments in pensions as opposed to other forms of investment is theoretically and empirically very weak. TASC's policy argues for the standard-rating of the tax relief and the use of these funds to provide an increased universal State pension over a five year period, from 2013, based on the assumption that the state pensions will not be cut in 2012 and are increased in line with inflation. TASC's pension policy also makes the case for a establishing a new Social Insurance Retirement Fund that is a mandatory defined benefit pension scheme (TASC 2010a).
36. TASC proposes that income tax relief on pension contributions be reduced to the standard rate.
37. TASC proposes that the tax exemption for lump-sum pension payments be reduced to the level of the average industrial wage. The remainder should be taxable at the

marginal rate of income tax and should be subject to the Universal Social Charge. This change should take effect from midnight of Budget day.

38. TASC proposes that the rate of imputed withdrawal on ARFs with assets in excess of €1,500,000 be increased as follows: 7.5 per cent for funds valued between €1,500,001 and €3,000,000, ten per cent for funds valued between €3,000,001 and €5,000,000 and 12.5 per cent for funds valued in excess of €5,000,000.

Proposals for Carbon Tax and Excise Taxes

39. Overview: TASC's proposals in this section are targeted at disincentivising certain types of activities on environmental and health grounds. Consumption taxes are less damaging to economic growth than taxes on production and while consumption taxes tend to be regressive, the TASC proposals for consumption taxes comprise just over ten per cent of the total value of measures proposed.
40. TASC proposes that the carbon tax rate be increased to €22 per tonne. TASC also proposes that the commencement order be made on coal and turf. See Appendix E for a fuller discussion.
41. TASC proposes that the €200 car park tax outlined in Budget 2009 be implemented.
42. TASC proposes a two cent per litre increase in the excise on petrol, a five cent per pint increase in the excise on beer and cider, a five cent per half glass increase in the excise on spirits, a 75 cent per bottle increase in the excise on wine and a ten cent per packet increase in the excise on cigarettes.
43. As a health promotion measure TASC proposes the introduction of a new excise, equivalent to a 20 per cent tax, on sweets and sugar-sweetened drinks.

Proposals for Social Solidarity and the Treatment of Tax Fugitives

44. Overview: The process of fiscal consolidation will entail great hardship and distress for many people. The last thirty to forty years have increasingly been characterised by the ultra-wealthy exploiting tax havens to avoid paying tax. In the interests of social justice, solidarity and cohesion it is imperative that tax fugitives contribute to the process of fiscal adjustment.

45. TASC proposes that the ‘number of days’ test for determining the tax residence of an Irish citizen should be reduced from 183/280 days to 90/183 days. TASC also proposes an increase in the domicile levy from €200,000 to €400,000.

3 Economic Context

46. The aftershocks of the property-driven boom-bust cycle continue to reverberate through the economy. The inevitable sharp decline in property prices and in construction activity from their respective peaks devastated the construction sector and seriously undermined the Irish banking system. The catastrophic losses in the banking sector have resulted in a freeze in credit to the economy, which has amplified the crisis and the rate of business collapse. The Irish economy is now characterised by a severe debt overhang. Private household debt, private corporate debt and public debt are now all at very high levels. Nominal GDP collapsed by just under a fifth between the fourth quarter of 2007 and the middle of 2010, and the large debt overhang has negative implications for short- and medium-term growth potential. The unemployment rate has more than trebled between 2007 and 2011 and employment levels are continuing to fall, albeit at a reduced rate.
47. Double-digit deficits in the public finances, combined with the spiralling costs associated with the banking collapse, led to Ireland being increasingly shut out of the international credit markets in late 2010. The original bank guarantee of September 2008 had been for two years and the largest amount of the banks' bond funding was scheduled to mature at the end of September 2010, in advance of the expiration of the guarantee; this was equivalent to €30 billion of government-guaranteed bank debt. Critically, however, the banks were unable to obtain new funding on the market and became almost totally reliant on the willingness of the European Central Bank (ECB) and the Irish Central Bank to provide liquidity. This in turn damaged the market perception of Ireland, and the sovereign temporarily withdrew from the bond markets as bond spreads worsened. By the beginning of November 2010, the ECB's exposure to Irish banks had reached almost €130 billion and ultimately Ireland was pushed into a €67.5 billion programme of assistance from the 'troika' of the IMF, the ECB and the European Commission in late November 2010.
48. It is certainly true that the institutional design flaws associated with monetary union have not only contributed to the Irish crisis but impeded its successful resolution. Five particularly damaging examples of European policy failures which contributed to the crisis are: (A) the attempt to shoehorn a homogeneous interest rate onto seventeen heterogeneous economies operating at different points of the economic cycle; (B) the absence of an EU-wide mechanism, and set of protocols and conditions, for writing

down debt; (C) the absence of an EU-wide special resolution regime for dealing with insolvent financial institutions; (D) the absence of a lender of last resort for sovereign debt within the Eurozone; and (E) the failure to construct a banking union and centralised financial regulation to accompany monetary union.

49. Nevertheless, Ireland's crisis is primarily home-grown in nature. The capital stock of the Irish economy soared by 157 per cent in real terms in 2000-2008, yet non-productive stock (housing) accounted for almost two-thirds of the increase (Davy, 2010). Sufficiently prudent domestic decision making in both fiscal and regulatory policy would have prevented a crisis of the severity experienced in Ireland. The Irish crisis is primarily attributable to a failure of regulation and a failure of macroeconomic policy. Policy failure is at the root of the crisis. Certain systemic institutional failings, including weak decision making processes, aversion to transparency, general lack of accountability and oversight, propensity to group-think, and an insufficient institutional architecture for strategic economic planning, were all contributory factors.

50. Official forecasts of Ireland's growth trajectory have been notably unreliable in recent years. The unknown future evolution of the European debt crisis adds an additional layer of uncertainty to Irish growth prospects. International historical experience suggests it usually takes between five and seven years for a country experiencing a severe banking crisis to work its way through the crisis and return to long-term trend growth rates[16]. Output growth is typically very low or non-existent during the recovery period. Ireland's domestic economy is likely to remain anaemic next year as continued deleveraging by heavily indebted households and businesses, combined with the Government's ongoing programme of austerity, will continue to impede a significant pickup in domestic demand. The extremely large magnitude of the private sector debt overhang will continue to weigh on consumption and investment in the domestic economy for the foreseeable future[17]. Recent improvements in GDP growth are attributable to net exports, which have held up well during the crisis. However, the growth of net exports can be expected to fall in 2012. This is due to the ramping up of the budgetary consolidation process in most of Ireland's main trading partners, and to the general weakness of the major European economies.

[16] See Reinhart and Rogoff (2010) for an overview of the impacts of banking and debt crises on output and employment.

[17] Cecchetti, Mohanty and Zampolli (2011) find that sovereign debt levels above 85 per cent of GDP, corporate debt levels above 90 per cent of GDP, and household debt levels above 85 of GDP are all bad for growth. Ireland exceeds the threshold for all three types of indebtedness.

51. Recent IMF research by Leigh et al. (2010) has provided useful estimates of the impact of austerity measures on both output and employment. They find a fiscal consolidation package equivalent in scale to one per cent of GDP will typically reduce GDP growth by approximately 0.5 per cent within two years and raise the unemployment rate by about 0.3 percentage points. However budget deficit cuts are found to be more painful in cases, such as the present one, when these adjustments occur simultaneously across many countries. The reason is straightforward, in that not every country can increase their net exports at the same time. Budget cuts are also found to be more damaging when monetary policy is not in a position to offset them. If interest rates are at, or just above, zero, as is currently the case, the effect of the fiscal consolidation will ultimately be more costly in terms of lost output. The pro-cyclical austerity measures have heightened the severity of economic collapse.

Table 3.1 Selected macroeconomic indicators for Ireland (Annual Percentage Change)

	2010	2011	2012
IMF World Economic Outlook:			
Real GDP	*-0.4*	*0.4*	*1.5*
Consumer Prices	*-1.6*	*1.1*	*0.6*
Balance of Trade	*0.5*	*1.8*	*1.9*
European Commission:			
Real GDP	*-0.4*	*0.6*	*1.9*
GDP Deflator	*-2.4*	*0.5*	*0.9*
Current Account[18] *(% of GDP)*	*0.5*	*1.8*	*2.7*
Nominal GDP (€bn)	*156.0*	*157.7*	*162.1*

Sources: IMF World Economic Outlook, September 2011; European Commission Economic Adjustment Programme for Ireland, September 2011 (July forecast).

52. The labour market continued to deteriorate between the second quarter of 2010 and the second quarter of 2011. The unemployment rate in Ireland now stands at 14.3 per cent of the labour force or 304,500 people (CSO, 2011). The male unemployment rate is now 17.5 per cent while the female unemployment rate is 10.4 per cent. Total employment fell by a total of 37,800 over the course of the year. The employment rate has now fallen from a peak in 2007 of 69.2 per cent of those aged between 15 and 64, to a rate of just 59.6 per cent in 2011. Total employment fell by 292,600 between the second quarter of 2007 and the second quarter of 2011.The male employment rate has fallen from over 77 per cent in 2007 to 63.3 per cent in 2011, while the female

[18] The current account is the sum of the balance of trade, net factor income (such as interest payments and repatriated profits) and net transfer payments (such as foreign aid).

employment rate has fallen from over 60 per cent in 2007 to 56 per cent in 2011. Long-term unemployment, which typically develops into structural unemployment, now exceeds 50 per cent of total unemployment for the first time since the late 1990s. The South-East region has the highest unemployment rate in the State at 18.2 per cent.

Table 3.2 Selected labour force indicators (pp = percentage point) – Annual changes are Q2 to Q2

	2009 (Q2)	2010 (Q2)	2011 (Q2)	2010-2011
Persons Aged 15 and Over ('000s)	3,523.8	3,512.4	3,502.7	-0.3%
In Labour Force ('000s)	2,203.1	2,152.7	2,125.9	-1.2%
Persons in Employment ('000s)	1,938.5	1,859.1	1,821.3	-37.8
Annual Change in Employment ('000s)				
All Economic Sectors	-174.3	-79.4	-37.8	
Selected Sectors:				
Construction	*-86.0*	*-30.1*	*-19.6*	
Industry	*-29.0*	*-18.2*	*-6.4*	
Wholesale and Retail Trade	*-29.6*	*-8.6*	*-3.5*	
Accommodation and Food Services	*-5.6*	*+0.0*	*-12.6*	
Other	*-24.1*	*-22.5*	*+4.3*	
Unemployment Rates				
All Persons	12.0%	13.6%	14.3%	+0.7pp
Male	15.1%	16.7%	17.5%	+0.8pp
Female	8.1%	9.8%	10.4%	+0.6pp
Youth Unemployment:				
15-19	36.4%	40.6%	40.1%	-0.5pp
20-24	23.0%	25.8%	27.7%	+1.9pp
25-34	13.4%	14.6%	16.5%	+1.9pp
Numbers Unemployed ('000s)				
All Persons	264.6	293.6	304.5	+3.7%
Male	186.9	200.1	205.7	+2.8%
Female	77.7	93.6	98.8	+5.6%
Employment Rate (persons aged 15-64)				
All Persons	62.5%	60.4%	59.6%	-0.8pp
Male	67.3%	64.5%	63.3%	-1.2pp
Female	57.8%	56.4%	56.0%	-0.4pp
Labour Force Participation				
All Persons	62.5%	61.3%	60.7%	-0.6pp
Male	71.3%	69.4%	68.4%	-0.6pp
Female	54.0%	53.5%	53.3%	-0.2pp

Source: CSO (September, 2011), Quarterly National Household Survey: Quarter 2 2011

53. IMF estimates for Ireland's deficit and debt profile are shown in Table 1.4. The sustainability of Ireland's debts is contingent upon the restoration of nominal GDP growth. Ireland's baseline deficit exceeded ten per cent of GDP during 2009 to 2011, and is forecast to be 8.9 per cent in 2012. The Memorandum of Understanding, which sets out the terms of the agreement with the troika, requires the Irish Government to reach the target of an 8.6 per cent deficit in 2012.
54. Negative shocks to the baseline average growth rate will result in a higher debt-to-GDP level, and potentially undermine the medium-term sustainability of Ireland's debt burden. The occurrence of such a negative shock is highly plausible in the short term, given the uncertainties surrounding the resolution of the Eurozone debt crisis. The short-run growth prospects of Ireland's main trading partners in Europe look increasingly weak, and austerity measures in the Eurozone and the United Kingdom can be expected to reduce demand for Irish goods. The debt crisis is spreading through the Eurozone, and the ongoing failure to credibly tackle the Eurozone debt crisis now risks major disruption to global financial stability. It is now evident that the Eurozone contains a number of serious institutional design flaws[19] which, if not repaired, will provoke periodic crises. Worryingly, the responses to the crisis by many national leaders, and by the ECB, have been persistently insufficient and occasionally counterproductive. Although a number of viable technical solutions to the debt crisis have been proposed, it is unclear whether there is sufficient political will or capacity to take the necessary steps to resolve the crisis in the short-term. A significant increase in the interest rates on new market borrowing would similarly undermine Ireland's debt sustainability, and would be likely to necessitate a continuation of official lender financing beyond the end of the current program in 2013.

[19] See De Grauwe (2011); Varoufakis and Holland (2011) and McDonnell (2011) for overviews of these design flaws.

Table 3.3 Public Finances – IMF Forecasts

	2010	2011	2012	2013	2014	2015
General Government Balance *(% of GDP)*	*-32.0*	*-10.4*	*-8.9*	*-7.3*	*-4.9*	*-4.6*
General Government Balance (€bn)	*-44.9*	*-16.5*	*-14.5*	*-12.2*	*-8.7*	*-8.5*
Primary Government Structural Balance[20] *(% of Potential Output)*	*-9.0*	*-7.0*	*-6.0*	*-5.0*	*-3.2*	*-3.4*
General Government Gross Debt *(% of GDP)*	*94.9*	*109.2*	*115.2*	*118.3*	*118.1*	*117.0*
Nominal GDP (€bn)	*156.0*	*157.7*	*162.2*	*168.4*	*176.0*	*185.0*
General Government Gross Debt (€bn)	*148.0*	*172.2*	*186.9*	*199.2*	*207.9*	*216.5*

Sources: IMF Country Report, September 2011, and Derived Estimates

55. Ireland's fiscal policy options are now constrained by the Government's reliance on the IMF and the European Union for external financing. The schedule of financing from these institutions is shown in Table 3.4. This official lender financing is conditional on Ireland adhering to a strict programme of fiscal consolidation and a number of other economic reforms. The pace and scale of this consolidation is outlined in the Memorandum of Understanding signed last year by the Irish Government and the troika. Current policy is now framed by the National Recovery Programme (NRP), which provides for at least €15 billion of budgetary adjustments over the period from 2011 to 2014. This €15 billion is composed of €5 billion in revenue-raising measures and €10 billion in expenditure cuts. The NRP provides for €3.6 billion of consolidation measures in Budget 2012 including €1.5 billion of revenue increases and €2.1 billion of expenditure cuts.

Table 3.4 Annual Schedule of Programme Financing from the Troika (€ billions)

	2011	2012	2013
Program Financing	**38.2**	**19.0**	**10.3**
IMF	*12.5*	*6.3*	*3.6*
EU	*25.6*	*12.7*	*6.6*

[20] The structural balance is the non-cyclical component of the budget balance. The structural balance ignores one-off revenues (such as the sale of state assets) and expenditures (such as bank supports).When the economy is operating below potential output the budget balance will be worse than the structural balance while the opposite is true if the economy is operating above potential output.

4 Budgeting for Equality

Measures of Economic Inequality

56. Economists and social scientists use a number of measures of inequality. The most commonly used of these measures is the Gini coefficient, which varies between zero and one. A Gini of 0.0 indicates that everyone in the population has the same income and a Gini of 1.0 indicates that a single person in the population controls all of the income.

57. Gini coefficients vary within the EU15 group of advanced Western European economies. The high income countries of Sweden (0.24), Denmark (0.25) Austria (0.26) and Finland (0.26) are the most equal societies within this group, while the more fiscally troubled periphery of Portugal (0.36), the United Kingdom (0.34) and Greece (0.33) comprises the most unequal societies. With a Gini of 0.30 Ireland is close to the EU average (CSO, November 2010). The prevailing Gini coefficients among the world's wealthiest nations range from below 0.25 in parts of northern and central Europe to over 0.40 in countries characterised by weaker social supports and lower tax ratios such as the United States. The more equal countries in the OECD have in general weathered the global economic crisis with far greater success than the more unequal countries. For example, Latvia (the country with the highest Gini coefficient in the European Union) also experienced the largest collapse in economic output of all European Union economies.

Inequality and the Crisis

58. IMF researchers Kumhof and Ranciere (2010) have recently identified the key role played by increasing levels of income inequality in the global crisis. Their research show how the periods 1920-1929 and 1982-2007 were characterised by similarly large increases in the income share of the richest five per cent of the population. At the same time, there was a large increase in leverage (indebtedness) for the remainder of the population. The ratio of household debt to GNP/GDP doubled over both time periods. The additional income gains of the high income households were recycled through the financial sector and back to the rest of the population by way of loans. This enabled the rest of the population to temporarily maintain their existing consumption levels. As the income distribution became more unequal over time, the loans continued to grow and

eventually became unsustainably high with negative implications for the financial system.

Table 4.1 Historical share of total income commanded by the top 5% of the income distribution in the United States

1920	1928	1983	2007
24%	34%	22%	34%

Sources: Piketty and Saez (2003); Kumhof and Ranciere (2010)

59. The empirical results of the IMF model show how rising inequality increasingly drives economic instability and eventually produces a financial and economic crisis. Kumhof and Ranciere argue that any success in reducing income inequality would be very useful in reducing the likelihood of future crises and in safeguarding long-term macroeconomic stability. Their findings suggest that an increase in workers' earnings would offer a better long-term solution to the problem of historically chronic overleveraging (high household debt) than would a reduction in the actual stock of debt. They argue this could be achieved by moving away from taxing the labour of low-income workers, and instead increasing taxes on economic rents, including land, natural resources and financial sector rents.

Inequality and Long-Term Development

60. Empirical research strongly suggests that growing inequality reduces social cohesion and increases political instability (Alesina and Perotti, 1996). This instability leads to decreased investment and slows economic development. Government spending can propel economic development, not only through investments in human and physical capital but also through investments in the social cohesion required for a healthy economic and social environment. Guarantees of a basic and sufficient minimum income, of quality housing, and of free healthcare and education are all important pillars supporting this social cohesion. Redistributive tax policies and the social programmes underpinning the welfare state mitigate the inequalities of risk and wealth generated by the market. Finally, every new investment project and almost all innovative activity involves a certain degree of risk-taking, and the potential costs of failure act as powerful

barriers to entrepreneurial activities. The consequences of failed investments can be reduced by ensuring there is an adequate social safety net to fall back on. In this way, entrepreneurial activity and an adequate safety net reinforce each other.

61. More recent empirical work from the IMF's research department (Berg and Ostry, 2011, and Berg, Ostry and Zettelmeyer, 2011) has shown that, when growth is looked at over the long term, a trade-off between efficiency and equality does not exist. Berg et al note that: "*In fact equality appears to be an important ingredient in promoting and sustaining growth. The difference between countries that can sustain rapid growth for many years or even decades and the many others that see growth spurts fade quickly may be the level of inequality. Countries may find that improving equality may also improve efficiency, understood as more sustainable long-run growth.*"

Illustrative Examples of Equality Auditing

62. TASC received support from the EU PROGRESS Fund and the Equality Authority to undertake an analysis of two groups under the nine grounds in the equality legislation. TASC undertook a gender-impact assessment of Budget 2011 to quantify the effect of changes to taxation and social welfare provisions on the income of women and men. TASC also undertook a comparative analysis of the tax treatment of same sex couples and that of married couples following the introduction of Civil Partnership.

63. TASC's gender-impact analysis uses Survey of Income and Living Conditions (SILC) data to examine the impact of changes in Budget 2011 on men and women. Changes to the system of social contributions and taxation may disproportionately impinge on one gender because of systemically differing characteristics such as income, time use and family structure. TASC's gender-impact assessment examines the changes to income tax and benefit changes announced in Budget 2011. We consider the impact of these changes to the earning bands and standard tax reliefs to which all employees are entitled. We only consider earned income that is subject to the Pay as You Earn (PAYE) system of taxation in this example.

64. In Budget 2011 the government signaled its intention to abolish the Income Levy and introduce a new Universal Social Charge (USC). This change brought a significant number of low-paid workers into the tax net. Individuals are liable to pay the USC if their gross

income exceeds €4,004 per annum, whereas previously an employee could earn up to €15, 028 before becoming liable for the Income Levy.

65. In addition to these changes, the personal tax credit and the PAYE tax credit were both reduced by approximately ten per cent. Under the new system, employees exhaust their tax credits upon earning €16,500 per annum and will begin to pay the standard 20 per cent rate of income tax on earnings above this amount. Finally, the entry point for the higher rate of income tax was reduced by between eight and ten per cent, depending on an individual's familial circumstances. For unmarried persons the income threshold marking entry to the higher rate of tax was reduced by 9.9 per cent.

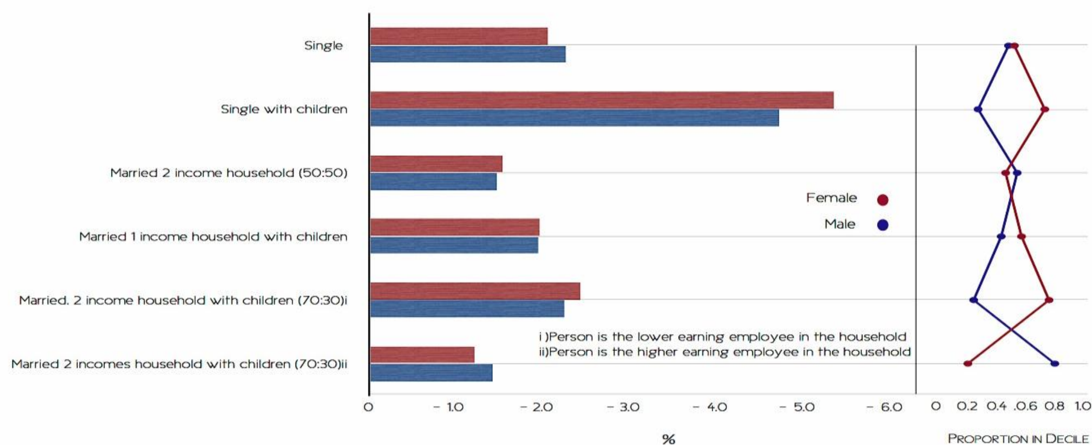
66. The most significant alteration in Budget 2011 to the system of social contributions, from an employee's perspective, was the decision to abolish the Health Contribution Levy. This measure partially offset some of the additional charges incurred as a result of the introduction of the USC and the reduction in the tax bands and tax credits. However, because only those individuals earning in excess of €26,000 per annum were liable to pay this levy, the decision to remove it only benefits middle-to-high income employees. Pay Related Social Insurance (PRSI) rates for employees remained unchanged in Budget 2011, although the annual earnings ceiling – above which no PRSI was paid – was abolished. This change means that high-earning employees will now continue to pay PRSI on annual earnings in excess of €75,036.

67. There were substantial cuts made to many of the most costly welfare schemes in Budget 2011. Not all benefits were treated equally. While some areas did remain untouched (for example, there was no reduction in the state pension), other benefits such as child benefit suffered cuts in excess of 5 per cent. Child benefit was reduced by €10 per child with an additional €10 reduction for a third child.

68. The combined impacts of the changes to the system of direct taxation (which include the changes to social security contributions), and the changes to the system of primary social benefits, are shown in Figure 2.1 for each of the main groups. The group most negatively affected by the Budget 2011 policy changes is the *'single with children'* group. This group has by far the lowest average income of all the groups studied, and has a very high ratio of females (73 per cent) to males (27 per cent). Individuals within the *'single with children'* group saw their net incomes fall by an average of five per cent as a result of the Budget 2011 policy changes. Children (0-17) and adults living in lone parent

households have been identified as the two most vulnerable groups in Irish society, with an 'at risk of poverty' rate of 18.6 per cent and 35.5 per cent respectively. Therefore, the analysis shows that the impact of Budget 2011 may further exacerbate the 'at risk of poverty' levels for these two groups. The least negatively affected group as a consequence of the budgetary changes was the *'married two incomes 70/30 – high'* group i.e. the group representing the higher earner within two earner households. This was the group with the highest male (80 per cent) to female (20 per cent) ratio. From this analysis, it appears that the budgetary changes relating to taxation and social welfare were not progressive and would not pass an equality audit. This demonstrates the need for an equality audit that is based on a distributional analysis of the effects of proposed changes to taxation and social welfare on all income groups. Such analysis should inform budgetary decisions to ensure that the budget does not have a disproportionate impact on low income or vulnerable groups.

Figure 4.1 Budgetary Impacts by Group



69. Nevertheless there have been important moves, in some areas, towards greater economic equality. One example of this was the Civil Partnership legislation which came into effect in 2011. Finance Act (No. 3) 2011 provided for changes to existing tax legislation following the Civil Partnership Act, to provide for the same tax treatment for registered civil partners as that provided for married couples under all tax categories. Broadly speaking, the Act does achieve this aim and civil partners are now treated the

same way as spouses in most areas of taxation. Significantly, the Finance Act also provides for the same tax treatment of a child whose parents are in a civil partnership as that of a child of a married couple, except in relation to maintenance payments. However, Marriage Equality[21] has identified twelve provisions where full equivalence has not been achieved, specifically in relation to the breakdown of civil partnerships, maintenance payments for children, and the definition of relatives. Marriage Equality (p.17) concludes that "…*tax legislation can only operate within the confines of general law, which means where the Civil Partnership Act does not achieve equivalence, tax changes are subject to these limitations also. Therefore without equal access to civil marriage, the consequence for same sex couples appears to be that civil partnership has created a structural barrier to achieving full equality in the area of taxation."*

[21] Marriage Equality (2011) *Missing Pieces – A comparison of the rights and responsibilities gained from civil partnership compared to the rights and responsibilities gained through civil marriage in Ireland.*

5 Tax Reform

International Comparisons

70. A comprehensive review of European Union (EU) tax structures is undertaken each year by the European Commission. The most recent year for which complete data is presently available is 2009[22]. Ireland's overall tax-to-GDP ratio[23] was the third lowest in the European Union at 28.2 per cent in 2009. This ratio was the second lowest in the Eurozone. By comparison the weighted EU average was 38.4 per cent in that year. The difference in the ratios is primarily attributable to the relatively low levels of Social Security Contributions (SSCs) and to the relatively low levels of local government taxation in Ireland. Ireland was the third most fiscally centralised country in the European Union in 2009, with 80 per cent of tax revenue accruing to central Government. This level was well in excess of the weighted EU average of 48.7 per cent. Ireland's taxation structure is characterised by a disproportionate reliance on taxes compared to SSCs. Irish SSC levels were the second lowest in the European Union in 2009 at just 5.8 per cent of GDP. This compares to a weighted EU average of 12.8 per cent. The low levels of SSCs are the most important reason why Ireland had one of the lowest levels of taxes on labour in the EU at 11.8 per cent of GDP. The weighted EU average level of tax on labour was 20.0 per cent in 2009.

71. One school of thought peculiar to Ireland has argued that measuring Ireland's tax ratio as a proportion of GNP, rather than as a proportion of GDP, is a more appropriate method of comparison between Ireland and other countries. This is because a significant portion of Ireland's GDP is repatriated out of the country by multinationals in the form of profits. Ireland's tax ratio as a proportion of GNP was 34.6 per cent in 2009. However using GNP instead of GDP as a measure of the implicit tax rate is inherently problematic. GDP measures all the income generated in Ireland, and all of this generated income is theoretically available to be taxed by the Irish government. Profits intended for repatriation are not immune to taxation. If all of the income repatriated abroad is excluded from cross-country comparisons of tax ratios, then it can be argued for the sake of consistency that all taxation revenue coming from the corporate profits of these multinationals should also be excluded from cross-country comparisons of tax ratios.

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[22] Eurostat (2011) "*Taxation Trends in the European Union: Data for the EU Member States, Iceland and Norway*", 2011 Edition

[23] Including Social Security Contributions

Government revenue obtained from corporate income amounted to 2.5 per cent of GDP in 2009 (3.1 per cent of GNP), though of course not all of this will have come from multinationals.

Table 5.1 Structure of Tax Revenues (including SSCs) as % of GDP – GDP Weighted Averages for the EU27

		2005	2006	2007	2008	2009	Rank[24]
Total							
	Ireland	**30.7**	**32.2**	**31.4**	**29.7**	**28.2**	**25**
	EU27	**39.1**	**39.6**	**39.6**	**39.3**	**38.4**	**-**
Cyclically Adjusted Total							
	Ireland	*29.3*	*29.9*	*28.0*	*28.2*	*29.8*	-
Total as % of GNP							
	Ireland	*36.0*	*37.0*	*36.5*	*34.6*	*34.5*	-
Consumption							
	Ireland	11.4	11.5	11.2	10.9	10.0	**25**
	EU27	11.1	11.0	11.0	10.8	10.6	**-**
Labour							
	Ireland	10.4	10.4	10.8	11.3	11.8	**25**
	EU27	19.6	19.4	19.3	19.7	20.0	**-**
Capital Income							
	Ireland	6.2	7.1	6.6	5.2	4.4	**17**
	EU27	5.8	6.3	6.5	6.1	5.3	**-**
Capital Stock/Wealth							
	Ireland	2.7	3.2	2.9	2.2	2.1	**9**
	EU27	2.8	2.9	2.9	2.8	2.6	**-**
GDP (€bn)							
	Ireland	163.5	178.3	189.9	180.0	160.6	-

Source: Eurostat, Taxation Trends in Europe Annual Report 2011, p. 202.

72. Ireland's extremely low levels of SSCs mean that Ireland has one of the lowest levels of taxes on labour in the EU. This level stood at 11.8 per cent of GDP in 2009, a figure that was just over half the weighted EU average of 20.0 per cent. Ireland's Implicit Tax Rate (ITR[25]) on labour was 25.5 per cent in 2009 compared to an average of 36.0 per cent overall in the European Union. Increases in labour taxation in the 2011 budget have since closed part of this differential. The implicit tax rate on capital was 14.9 per cent in 2009, which was just over half the weighted average of 28.6 per cent for the Eurozone as a whole. Ireland's ITR on corporate income, which was 7.5 per cent in 2009, was just

[24] Rankings are out of 27. A ranking of 1 indicates the largest proportional tax take and a ranking of 27 indicates the smallest proportional tax take.

[25] The average or effective tax rate, sometimes also referred to as the implicit tax rate (ITR), is calculated by dividing the revenues from taxes on a special activity or good by an appropriate corresponding aggregate tax base from national accounts statistics.

one third of the European Union's weighted average of 21.7 per cent. On the other hand Ireland's ITR on consumption was 21.6 per cent in 2009, which was above the weighted European Union average.

Table 5.2 Implicit Tax Rates – Figures for EU27 and Euro Area 17 are GDP Weighted Averages

		2005	2006	2007	2008	2009	Ranking
Consumption							
	Ireland	26.1	26.3	25.1	23.3	21.6	**10**
	EU27	19.6	19.7	19.9	19.4	18.9	-
Labour Employed							
	Ireland	25.3	25.3	25.7	25.3	25.5	**22**
	EU27	36.2	36.3	36.4	36.7	36.0	-
Capital							
	Ireland	19.6	21.2	19.1	16.3	14.9	-
	Euro Area 17[26]	28.8	30.8	31.2	29.4	28.6	-

Source: Eurostat, Taxation Trends in Europe Annual Report 2011.

Table 5.3 Irish ITRs in 2009 as Proportions of Weighted EU Average – (Euro Area in the Case of Capital)

Consumption	Labour	Capital
1.14	0.71	0.52

73. The tax take for environmental taxes was broadly in line with European Union averages in 2009, although taxation on energy was the fifth lowest in the EU.

Table 5.4 Environmental Taxes (% of GDP) – Figures for EU are the Weighted Averages

		2005	2006	2007	2008	2009	Ranking
Total							
	Ireland	2.5	2.5	2.5	2.5	2.4	**18**
	EU	2.6	2.5	2.4	2.4	2.4	-
Energy							
	Ireland	1.3	1.3	1.2	1.3	1.5	**23**
	EU	1.9	1.9	1.8	1.7	1.8	-
Transport (excluding fuel)							
	Ireland	1.2	1.2	1.3	1.2	0.9	**5**
	EU	0.6	0.6	0.6	0.5	0.5	-
Pollution							
	Ireland	0.0	0.0	0.0	0.0	0.0	**22=**
	EU	0.1	0.1	0.1	0.1	0.1	

[26] No figure available for the EU-27.

74. The only large-scale change introduced in Budget 2010 on the revenue side of the public finances was the introduction of a carbon tax charged at €15 per tonne. There were more substantial changes introduced in Budget 2011. These changes included reductions in the income tax rate band, the reduction of tax credits and the replacement of the income and health levies with the new Universal Social Charge. There were also increases in excises for mineral oil, and increases in employer and employee pension contributions. In addition, a number of tax expenditures were abolished.
75. There are two statutory Personal Income Tax (PIT) rates. The standard rate is 20 per cent and the top rate is 41 per cent. The threshold for the top rate is €32,800 for a single person with no dependents, with this threshold increasing for married persons and for persons with dependents. There is also a system of tax credits that reduce the amount of income tax payable by an individual. The personal tax credit is granted to all taxpayers and is €1,650 for a single person while a Pay As You Earn (PAYE) tax credit of €1,650 is granted to employees who are paid most of their money under the PAYE system. A Universal Social Charge (USC) was introduced in Budget 2011 which replaced the pre-existing income levy. Those on incomes below €4,004 are exempt from the USC. Otherwise the USC is charged at two per cent for income from €0 to €10,036; four per cent on income from €10,037 to €16,016 and seven per cent on income above €16,016. In relation to social security contributions, the first €127 of income per week is exempt from employee Pay-Related Social Insurance (PRSI) with the balance charged at four per cent. Employer PRSI is 10.75 per cent for employees earning over €356 per week and 4.25 per cent for employees earning €356 or less per week.

Table 5.5 Rates and bands under the USC and the Income Levy

Rates & bands under the USC (Budget 2011)		Rates and bands under the Income Levy (Budget 2010)	
Income per Annum	*Rate*	*Income per Annum*	*Rate*
Up to €10,036	2%	Up to €75,036	2%
From €10,036 to €16,016	4%	From €75,037 to €174,980	4%
In excess of €16,017	7%	In excess of €174,980	6%

76. Capital gains are taxed at 25 per cent and there is an annual exemption of €1,270. There is a 25 per cent tax, which in Ireland is called Capital Acquisitions Tax (CAT), on gifts and inheritance over a certain value. This value is determined by the relationship of the beneficiary to the donor. The basic corporation tax rate is 12.5 per cent, although the

effective tax rate is often much lower due to tax reliefs. Ireland is characterised by widespread transfer pricing and the exploitation by multinationals of international tax schemes such as the ‘Double Irish’ tax avoidance strategy that allows them to pay extremely low rates of corporation tax. The standard Value Added Tax (VAT) rate is 21 per cent and applies to the majority of goods. There are reduced VAT rates of 13.5 per cent for certain labour-intensive items and nine per cent for certain goods related to the tourism sector. Unusually for an advanced economy, there is no annual tax on the principal primary residence, although the Government has announced its intention to introduce one.

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Appendix A: The Eurozone Crisis and the Promissory Note Question

1. TASC urges the Government to prepare for the likely impending Greek default by putting in place a mechanism for the renegotiation and write-down of the promissory note liabilities undertaken as part of the bailout of Anglo Irish Bank and Irish Nationwide Building Society.

2. If we assume a fairly benign 4.7 per cent interest rate on Government borrowings after the country has exited the external programme of assistance, we can estimate that the total cost of these notes, including the interest costs on borrowings, between 2011 and 2031 will be in the region of €85 billion. According to this scenario, the annual cost would peak at over €5.3 billion in 2023. Under this scenario there will also be continuing debt interest costs on payments beyond 2031.

3. The burden of the promissory notes will act as a drag on growth and employment for years to come. It is unfortunate that the horrendous losses incurred by private sector financial institutions have been imposed on the people of Ireland, particularly as it is abundantly clear that the causes of the Eurozone debt crisis are in fact ultimately attributable to flaws inherent to the design of the Eurozone itself.

4. If it is deemed necessary by supranational institutions such as the European Central Bank and the European Commission that the entirety of the losses to the financial sector be socialised, then, given the mutual responsibility of European leaders and policymakers for constructing a currency union with systemic and foreseeable flaws, it is appropriate for these losses to be socialised at the level of the Eurozone.

5. In the event of Greece defaulting on its sovereign debt obligations, Ireland will have a strong case for receiving relief on some of its own debt obligations. This would be best achieved by seeking a renegotiation or write-down of its promissory note obligations. The promissory notes are not part of the Memorandum of Understanding (MOU) agreed with the EU/IMF, and future repayments under the programme of assistance are not contingent upon maintaining the current promissory note schedule. The relevant institutions are also, for the most part, detached from the European financial system and consequently the risk of contagion is limited.

6. TASC proposes that a viable solution to the promissory note burden would be to have the promissory note liabilities transferred to the EFSF, with Ireland then agreeing a

negotiated repayment schedule which could, for example, be in the form of a bullet bond at a favourable interest rate. Ideally, this would also include an element of write-down. This could reduce payments by over €2 billion annually over the course of the next few years and would go some way towards stabilising Ireland's debt dynamics.

7. In the medium-term TASC suggests that a number of reforms are required to make European monetary union viable in the long-run. The design flaws of the Eurozone are discussed in McDonnell (2011), and include the absence of a lender of last resort for sovereigns, the lack of a centralised countercyclical fiscal mechanism to combat recessions, the instability and inefficiency caused by imposing a homogeneous interest rate on heterogeneous economies, and the lack of an EU-wide special resolution regime for dealing with insolvent financial institutions.

Appendix B: Residential Property Tax Design

1. The broad parameters of TASC's preferred model for a Residential Property Tax (RPT) were outlined in TASC's budgetary proposals for 2011 (TASC, 2010)[27]. TASC is proposing that a 0.30 per cent levy be imposed on all residential property. There should be a deferral system to prevent incidences of hardship. As Callan (2010) argues, RPTs can be equitable if correctly designed. The most inequitable type of RPT is a flat charge.

2. The broad principles for TASC's recurrent residential property tax proposal are as follows:

    a. A recurrent (annual) Residential Property Tax (RPT) should be introduced in Budget 2012.

    b. It should apply to **all** residential property, with the exception of social housing and communal residential facilities, and should be borne by the property owner.

    c. It should replace the existing levy on rented properties, second homes and holiday homes. The existing transaction-based RPT (stamp duty) should be reduced to 0.03 per cent of the transaction price.

    d. Deferrals should be made available to property owners on low incomes, with the precise level of deferral available being dependent on the exact income of the property owner, and their housing and childcare costs relative to their income. The deferral should only apply to the principal private residence.

    e. The deferral should be implemented by creating a defined cap on the maximum property tax charge in a single year which would be set at a proportion of the property owner's gross imputed income for that year. Any property tax charge beyond this capped amount would be payable upon decease, or upon sale or transfer of the property and should attract interest. The amount payable at that time would not exceed ten per cent of the value of the property.

    f. Those individuals with a proven inability to pay should have access to a 100 per cent deferral. This includes households where combined housing and childcare

[27] Although there is a strong economic rationale for a site valuation tax it is unlikely such a tax could be implemented fully in 2012. In the medium term TASC supports the eventual replacement of the residential property tax with a tax based on site valuation, on a cost neutral basis.

costs are over 50 per cent of net household income. See TASC (2010b) for a fuller discussion of how the inability to pay system would work.

g. The recurrent RPT should be a defined percentage of the gross market value of the property.

h. In the short term, the market valuation of the property should be undertaken on an owner-assessment basis to minimise the administrative burden. To facilitate this valuation process, all properties would be categorised as belonging to one of a set of wide and mutually-exclusive bands, for example the €150,001 to €300,000 band or the €300,001 to €450,000 band.

i. TASC recommends that the tax rate set in Budget 2012 should be 0.30 per cent of the value of the property. For the first year of payment, the value of the property for the purpose of this charge should be the mid-point of the valuation band.

3. The Programme for Government commits to examining the introduction of Site Value Taxation. A site value tax is applied to the value of the land rather than the value of the land and the buildings found on it. The economic rationale behind the arguments for a site value tax is that it encourages the efficient use of land. That is, unlike other forms of property tax, it penalises the under-use of valuable land, thus discouraging land hoarding and the retention of derelict sites in urban areas. Equally, it does not discourage improvements to buildings on the land (such as structural improvements to houses), which can bring positive economic benefits.

4. Applied in tandem with a robust planning system, site value tax can be a valuable tool in ensuring the optimal use of land and preventing the kind of bad and unnecessary development which occurred during the Celtic Tiger years. Another advantage which marks it out from other property taxes is that it can recoup for the state some of the rising value of land which is due to improvements made by state investment, such as the building of schools and public transport.

5. It has been argued that site value tax would be too complex to introduce in Ireland in the short to medium term. The complexity of the system will depend to some extent on the method of valuation chosen. In Northern Ireland it took five years to construct a valuation system which valued property not on the basis of the current market, but on

the basis of various factors including age and size of house, location, presence of central heating etc[28]. However, part of the delay in setting up the system can be attributed to the political problems concerning the Assembly which prevailed at that time. A similar system, including elements such as proximity to public transport and environmental amenities and quality, could be set up here over the next eighteen months to two years. Like other forms of property tax, the Government will need to ensure that the system takes account of issues such as ability to pay, and incorporates a transparent, free and easily accessed appeals procedure.

[28] This is technically known as a hedonic regression appraisal system.

Appendix C: Additional Expenditure Measures within the Envelope of Spending

1. TASC is not proposing a reduction in net expenditure in Budget 2012 beyond those savings identified through implementation of the Croke Park agreement and the Comptroller and Auditor General's Report.

2. TASC proposes a reallocation of spending between expenditure headers. An annual re-evaluation and reallocation of spending is best practice.

3. Within the envelope of spending, TASC suggests additional spending in the following areas should be prioritised:

    a. Introduce a series of health promotion initiatives in schools and communities aimed at promoting healthy eating habits. This should include supporting initiatives aimed at providing healthy school meals at primary level. It is envisaged the yield to the exchequer from the proposed 20 per cent tax on sweets and sugar-sweetened drinks would contribute to the cost of this programme.

    b. Abolition of direct provision for asylum seekers and replacement with Social Welfare and Rent Allowance. The 2010 report by the Free Legal Advice Centres (FLAC), *One Size Doesn't Fit All*, highlights the human rights issues involved in direct provision as well as the poor conditions in which many of those affected live. In particular, the report highlights the negative impact of Direct Provision on children[29].

    c. A 25 per cent increase in funding for the National Adult Literacy Agency and associated literacy programmes[30].

    d. Fuel allowances and other measures to counteract fuel poverty.

[29] FLAC, One Size Doesn't Fit All, 2010, available at: http://www.flac.ie/download/pdf/one_size_doesnt_fit_all_full_report_final.pdf (accessed 08.10.11)
[30] Available at: http://www.kildarestreet.com/debates/?id=2010-11-11.935.0&s=nala+funding#g937.9.

Appendix D: Economic Recovery and Investment Multipliers

1. While the key role played by capital accumulation in the generation of growth is widely accepted, the actual size of investment multipliers is a source of deep contention amongst economists. This is partially because of the multiplicity of confounding effects in a complex adaptive system which make constructing plausible fiscal multipliers notoriously difficult. The official response in Ireland has been to reject stimulus out of hand because it is argued that much of the benefit of an investment stimulus in a small open economy like Ireland will leak out of the country, thereby rendering the stimulus ineffective.

2. To examine this claim by reference to the empirical literature, and to estimate the size of an investment multiplier in a country as open as Ireland, it is arguably most appropriate to compare Ireland with sub-national regions in federations such as the United States or Germany. Doing so would also help to address the criticism that Ireland is somehow 'different' to other European countries and that fiscal policy will be ineffective in Ireland.

3. A recent study by Nakamura and Steinsson (2011) is useful to illustrate the applicability of investment multipliers, even in extremely open small economies. They identified a relatively high fiscal multiplier of 1.5 for individual states within the United States. The individual states within the union are analogous to small open economies, and this result suggests that appropriately targeted investment can be an effective countercyclical mechanism in small open economies. Nakamura and Steinsson used regional variation associated with military build-ups[31] to estimate the effect of a relative increase in spending on relative output. The United States example is illustrative for Ireland, because individual states within the United States are even more open to the rest of the United States economy than Ireland is to the global economy. In addition, most of the economies of individual US states are either as small, or smaller, than Ireland's economy. The findings are also of interest because the United States is a monetary union. This means interest rates cannot be raised in one state and held

[31] Military spending makes up varying proportions of total spending in US states. When the US embarks upon a military build-up, there is a systematic tendency for spending to increase more in some states than others. For example, when aggregate military spending in the US rises by 1 per cent of GDP, military spending in California on average rises by about 3 per cent of California GDP, while military spending in Illinois rises by only about 0.5 per cent of Illinois GDP. Nakamura and Steinsson find that when relative spending in a state increases by 1 per cent of GDP, relative state GDP rises by 1.5 per cent.

constant in another as a response to the stimulus. This, in turn, implies there is no confounding effect on the results caused by the loosening or tightening of monetary policy. The Nakamura and Steinsson findings also suggest that aggregate fiscal stimulus will have large output multipliers when the economy is at the zero lower bound.

4. The economic crisis appears to have stimulated an increase in research on using sub-national variation in spending to estimate investment multipliers. For example, Shoag (2011) finds that each dollar of government spending generates $2.12 of personal income, and that $35,000 of additional spending generates another job in the state where the spending occurs. The effects are stronger when employment and labour force participation are low. Acconcia, Corsetti and Simonelli (2011) looked at the local effect of the law mandating the interruption of public work where there is evidence of corruption, and they estimate fiscal multipliers as high as 1.4 on impact and two when dynamic effects are counted. Most of the post-crisis empirical work on sub-national fiscal multipliers has found multipliers of between 1.5 and 2.5.

5. Nakamura and Steinsson (2011) argue that their estimates are: *"much more consistent with New Keynesian models in which 'aggregate demand' shocks – such as government spending shocks – have large effects on output when monetary policy is sufficiently accommodative than they are with the plain-vanilla Neoclassical model"*.

6. Based on the weight of empirical evidence, TASC rejects the argument that Ireland's small open economy status will render fiscal stimulus ineffective. Establishing economic growth is a prerequisite to restoring Ireland's debt dynamics to a sustainable equilibrium. TASC does not agree with the Department of Finance's forecasts for economic growth under the parameters set by the National Recovery Plan, because they are too optimistic. The weakening global economy, the low levels of lending to the private sector, the continued deleveraging by the private sector and the Government's fiscal stance will all combine to drag on economic growth and employment levels in the short-to-medium term.

7. TASC is proposing that €1.2 billion per year (0.75 per cent of GDP), for each of the next four years, be taken from the National Pension Reserve Fund for investment in projects targeted at enhancing the economy's long-term productive capacity and addressing the growing crisis of long-term structural unemployment. This €1.2 billion could be combined with matching funds from the European Investment Bank and also with the

European Commission's new project bonds. Typical schemes might include the development of a next generation broadband network over a number of years in collaboration with the private sector, as well as investment in human capital through the funding of re-training and up-skilling schemes specifically targeted at the long term unemployed.

Appendix E: Carbon Tax

1. Ireland is committed to 20 per cent reduction in greenhouse gas emissions in the non-ETS (Emission Trading Scheme) sectors by 2020. On its own, a modest carbon tax will not lead to a large reduction in CO_2 emissions; however, it provides an indication to the public, businesses and international audience that Ireland is serious in tackling its high emissions. International evidence for the relative effectiveness of carbon taxes is mixed, and depends on factors such as the elasticity of energy demand and the design of the tax itself. Where tax reliefs and exemptions were granted to energy-intensive industries, the tax was much less effective (ESRI, September 2011). However, it is generally agreed that if well-designed, and as part of a range of policy measures, a carbon tax can be a cost-effective way of decreasing emissions.

2. Concerns about the distributional effects of a carbon tax and its effect on economic growth have been addressed in a number of ESRI studies. As a consumption tax, carbon tax is regressive in nature; however, the effects can be mitigated by measures such as increasing fuel allowance. Carbon taxes are less harmful to economic growth and employment than taxes on labour.

3. Budget 2010 saw the introduction of a carbon tax in Ireland. The tax was to be initially applied to petrol, diesel and home heating oils and extended to coal and turf when a suitable mechanism for countering the possible supply of coal and turf from Northern Ireland was designed. The carbon tax is not applied to electricity as it falls under the ETS. The application of the tax to coal and peat was subject to a commencement order, once it could be ensured that coal and oil would not be directly imported from Northern Ireland, where the carbon tax did not apply. The commencement order has not been made. The carbon tax was introduced at €15 per tonne. The National Recovery Plan commits to an increase of €10 per tonne in 2012 to €25 per tonne followed by a further rise of €5 per tonne in 2013 to €30 per tonne. This would bring the carbon tax above the current ETS level of €21.50. Maintaining the carbon tax at the level of the ETS would ensure a level playing field for those sectors of the economy outside and inside the ETS. On current predictions, if the carbon tax were to shadow the ETS level, it would rise to €21.50 per tonne in 2012 and €26 per tonne in 2015 (ESRI, September 2011).

Appendix F: Budgetary Transparency

1. TASC argues that reform of the budgetary process through increased transparency is required. An annual equality statement should be included with the budget and all major budgetary decisions should be informed by an equality audit that is based on a full distributional analysis. A distributional analysis of budgetary impacts on all income groups should be published annually within three months of the budget. This should allow for an equality audit/equality-proofing of the effects of budget measures.
2. The Department of Finance and the Government should ensure the main set of assumptions and algorithms underlying the Department of Finance's macroeconomic projections are included in each Budget statement.
3. The Government should ensure that all future Finance Bills and Budgetary statements clearly state the full cost to the State in revenue foregone of all existing and new tax expenditures.
4. The Government should ensure all tax expenditures are subject to a periodic cost benefit analysis as well as a periodic distributional analysis. The results of these analyses should be published.
5. The Government should ensure that all new and existing tax expenditure is subject to an economic efficiency audit and equality audit, to compare proposed and existing tax expenditures with a range of alternative options, including direct expenditure.
6. The Government and Department of Finance should compile a single database of all state assets and liabilities, make it publicly available, and update it at least twice a year.
7. Parliamentary questions should be permitted on a year round basis.
8. TASC welcomes the introduction of a fiscal council. The independence of the fiscal council from the Government and the Department of Finance should be rigorously safeguarded. The fiscal council should publish the assumptions and algorithms underlying its macroeconomic projections as well as the rationales for their assumptions. The fiscal council should report periodically to the Oireachtas Finance Committee and its members should be available to the public. All advice given by the fiscal council to Government should be published within 12 months.

9. The Government should not have the power to remove members of the fiscal council before their term of office is completed.

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The information contained in this publication does not necessarily reflect the position or opinion of the European Commission. The information contained in this publication does not necessarily reflect the position or opinion of the Equality Authority.