Opening Statement to Oireachtas Budgetary Oversight Committee
Dr. Barra Roantree & Dr. Theano Kakoulidou, ESRI
24/06/21

Cathaoirleach,

I am joined by my Economic and Social Research Institute (ESRI) colleague Dr. Theano Kakoulidou. We thank you for the invitation to appear before the Committee on foot of our report published through the ESRI Tax, Welfare and Pensions Research Programme examining options for raising tax revenue, including by restricting tax expenditures.[1] The views expressed in the report and by us both here today are our own and should not be taken to represent those of the Commission on Taxation and Welfare, to which I was recently appointed.

Context

As set out in our report, we believe that there will be a need for tax increases in the coming years to pay for planned and promised spending increases: for example, to implement Sláintecare and maintain existing levels of public services in the face of an ageing population. Such increases are unrelated to ongoing COVID-19 spending and above-and-beyond the additional level of borrowing that our ESRI colleague Prof. Kieran McQuinn has shown could be sustainably financed given the current low level of interest rates.[2] This need for future tax increases is made more pressing by structural deficiencies in the existing revenue base, including a potential over-reliance on volatile and highly concentrated corporation tax receipts and an inevitable decline in motor tax revenues as part of our planned transition to electric vehicles.

Our report provides a range of options that a future government seeking to raise or replace tax revenues might consider. In doing so, it does not seek to advocate any particular tax raising measure as ultimately those are political decisions which depend on distributional goals, value judgements and wider priorities. Rather, it seeks to provide evidence for those of you in the Houses of the Oireachtas who have the responsibility for making these decisions.

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[1] Kakoulidou, T. and B. Roantree. (2021). 'Options for raising tax revenue in Ireland'. Budget Perspectives 2022, Paper 1. ESRI, Dublin. https://doi.org/10.26504/bp202201.
[2] McQuinn, Kieran. (2021). 'With 'g' greater than 'r', should we be borrowing to increase Irish housing supply?'. QEC Special Article. ESRI, Dublin. https://doi.org/10.26504/QEC2021SUM_SA_McQuinn.

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We argue that the most straightforward way of raising substantial tax revenue is through increases to the main rates of income tax, the USC, PRSI, VAT and the Local Property Tax. Even small increases to any of these broad-based taxes could generate considerable revenue, precisely because they affect almost all households. Such tax rises can be designed to meet a range of distributional objectives, with – for example – increases to higher rates of income tax and USC the most progressive, and increases to rates of VAT the least progressive options. The report also considers measures more targeted at the better-off as well as options for raising revenue by restricting tax expenditures: a topic to which I now turn to.

Raising revenue by restricting tax expenditures

While many tax expenditures are well targeted at achieving clear and coherent policy objectives, we draw attention in our report to around a dozen which are less well targeted or have a questionable underlying economic rationale. Three reliefs we highlight that are particularly poorly targeted are:

1. Business and Agricultural Relief from Capital Acquisitions Tax, which cost €360 million in 2019: an average of almost €175,000 per claim. While intended to support the growth of and succession within small family farms and businesses, this relief as currently structured primarily benefits those inheriting substantial rather than small family farms and businesses.
2. A reduced 10% rate of Capital Gains Tax (CGT) on certain assets called "Entrepreneur Relief", which cost €92.4 million in 2018: an average cost per claim of more than €100,000. Such blanket reduced rates of tax are poorly targeted at encouraging start-ups, with evidence on a similar UK scheme suggesting the relief is more likely to generate efforts to avoid tax on retirement than spur entrepreneurship or investment.
3. Allowing those retiring to draw down €200,000 from their pension as a tax-free lump-sum, which cost €134 million in 2014: the latest year for which data is available. This primarily benefits those with substantial pension wealth (especially in the form of Defined Benefit pensions) and encourages the withdrawal of large lump-sums on retirement, something hard to reconcile with the government's goal of encouraging individuals to ensure a regular stream of income in retirement.

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Evaluating tax expenditures

That the latest available information on the cost of the tax-free pension lump sum dates from 2014 raises a broader issue with the availability and transparency of information on tax expenditures. This is something that both the Committee and the Parliamentary Budget Office have highlighted previously. While there have been some welcome steps towards the greater availability of information in recent years, there is still room for improvement. This is especially true in terms of CGT and pension reliefs, where many previously available costings are no longer provided by either Revenue or the Department of Finance

There is also room for improvement in the way in which we review and evaluate tax expenditures more generally. Evaluations are routinely based almost exclusively on responses to surveys of beneficiaries gathered through a non-representative public consultation process, a methodology which cannot deliver rigorous or credible evidence on their impact. One way in which this could be addressed is the development of expertise within the Irish Government Economic and Evaluation Service (IGEES), perhaps through the establishment of a dedicated tax expenditure evaluation unit. Another is by ensuring reviews of tax expenditures are published in advance of (instead of on) Budget Day to allow for sufficient scrutiny, perhaps alongside the Department of Finance Tax Strategy Group papers.

Conclusion

As we conclude in our report, the likely need for significant tax increases in the years ahead provides an opportunity to reassess how effective various parts of the tax system – including tax expenditures – are at achieving their objectives. Doing so could result in a tax system that not only raises the revenue necessary to fund desired levels of public spending in the years ahead, but one that is better designed to meet the challenges of the coming decades.