**Remarks to the Oireachtas Select Committee on Budgetary Oversight on the topic of Tax Expenditures**

9:30am on Thursday 24 June 2021 – online session

By Dr Micheál Collins, Assistant Professor of Social Policy, University College Dublin.

Chairman, I thank yourself and the committee for the invitation to make a presentation on this topic. My name is Dr Micheál Collins, I am an Economist and Assistant Professor of Social Policy, at the School of Social Policy, Social Work and Social Justice at University College Dublin. I was also a member of the 2008-2009 Commission on Taxation, and within the Commission chaired the subgroup which examined Tax Expenditure. As a researcher, I am also part of an international research group focused on the links between taxation and social policy and within that I focus on the often 'hidden' role of the state in using the taxation system to encourage and support certain activities among individuals and corporates via tax expenditure.

I also want to welcome the decision of the Select Committee to return once again to the topic of tax expenditure. The Committees report on the topic from 2019 was most welcome and reflected the relevance of giving this area increase attention as part of the annual budgetary oversight process.

It might be useful to put the scale of tax expenditure in some context. Budget 2021 outlined an expectation that the state will collect €77.6 billion in tax and social insurance contributions this year.[1] Data from the Revenue Commissioners for 2018 show approximately 85 'discretionary' tax expenditure measures costing a total of €15.8 billion in revenue forgone; these are measures which are not structural to the taxation system but rather have been put in place to incentivise certain activities or as a means of pursuing certain policy objectives. Many of these are well targeted and worthwhile, although for the most part we assume this rather than have any hard evidence to support it, while others have a less robust basis for defending their cost and effectiveness. Overall, put simply, for every €5 collected in taxation and social insurance, the state currently decides

[1] Calculated from Department of Finance data from: *Budget 2021*; see Collins (2021 – forthcoming) Taxation: Measures and Policy Issues in O'Toole, F. and C. Whelan (eds.) *The Economy of Ireland 14th edition*, Palgrave.

not to collect an additional €1 which is forgone through the provision of various tax breaks and reliefs.

## Tax Expenditure: evidence and parliamentary oversight

The information available to this Select Committee, and to Irish society in general, regarding tax expenditure measures has increased dramatically over the last decade or so. When the Commission on Taxation commenced its work in 2008 there was limited information on the annual costs but this has transformed following the work of the Commission, revisions to the scale of information on tax expenditures published by the Revenue Commissioners, annual reports from the Department of Finance and requirements at a European level that all countries report on the nature and scale of the tax resources they decide not to collect each year via tax expenditure.

While this increase in information is very welcome, there remains a deficit in parliamentary scrutiny of tax expenditure measures – both new proposals and existing provisions. I would encourage the committee to consider these measures as equivalent to direct expenditure by Government departments or agencies and to approach them in this way. In particular, I would encourage the committee:

- to select a theme each year and review the merits of each of the tax expenditure measures currently in existence under that scheme. Approaching the long list of tax expenditures in this way will make them more accessible and the exploration more intuitive; and
- to review the case made in the Budget and Finance Bills, and in associated documentation, for the introduction of each new tax expenditure. Both the Commission on Taxation and the Department of Finance have provided a useful set of criteria to assess the appropriateness of new measures and it would be worthwhile for a committee such as this to consider if the measures as proposed and designed adhere to these criteria.

Overall, if we treated tax expenditure more like new and recurring departmental expenditure it would represent a more comprehensive assessment of the taxation collection and resource allocation decisions of the state.

**Tax Expenditure: current context and some suggested reforms**

Chairman, while my main message to the committee is about the merit of establishing recurring and structured assessments of tax expenditure as part of the process of budgetary oversight, I am conscious of the discussions the committee has had over recent months and the forthcoming post-pandemic fiscal context. The pandemic has reminded us of the often hidden role that welfare states, such as ours, play in providing a safety net for all members of society. No doubt, that experience will frame much of the policy response in the years to come and points to at least a greater recognition of the role of the state and most likely a more enhance role for the state. Coupled with the impact of higher public debt, higher than anticipated debt financing costs, and the long-overdue reform of the international corporate taxation system, it seems inevitable that the state will have to raise more taxation on a recurring basis once the pandemic has subsided. In the absence of large-scale reductions in public services and redistributive supports, an increase in total taxation and social insurance contributions is a matter of how not if.

Within the context of broadening the tax base, and ensuring a progressive overall taxation system, I believe that reforms to tax expenditure have an important role to play in the period ahead. The following is a short list of five such reform which I would encourage the committee to consider in the context of the Budgets in the years to come. The measures are a mixture of those enhancing fairness and those likely to generate significant additional taxation income; some do both:

1. ***Broaden the high-income individuals' restriction to cover all tax relief measures***

Currently this measure, which ensure a minimum income taxation contribution from higher earners (those above €125,000 per annum), applies to 'specified reliefs' rather than all tax reliefs. As a consequence some tax expenditure measures, such as relief on pension savings, are excluded from the restriction. It makes a lot of sense to have a minimum income taxation contribution, there was none prior to this measure first emerging in 2006/07, but it should cover the use of all tax relief measures.

The committee should also note that the minimum rates are low when benchmarked against the rates paid by others down the earnings distribution. Currently, the minimum rate gradually rises from 20 per cent at €125,000 to 30 per cent at €250,000 and to 40 per cent at €400,000 and above – a 20 per cent rate is equivalent to the tax level faced by a single PAYE worker earning €39,000.

### 2. *Phase-out tax credits for earners above €100,000 per annum*

The provision of tax credits to workers, the self-employed and families is an important part of the tax system. These measures are in strict-terms tax expenditures although I did not include them in my calculation of discretionary tax expenditures mentioned earlier. While these measures serve important objectives in terms of work incentivisation and income support for many earners, particularly those on lower income, they have less relevance to those on the highest incomes in our society. Revenue data from 2016 showed about 85,000 earners with income above €100,000 per annum; less than 3 per cent of all earners in the state. Phasing out the personal tax credits from these earners would have almost no disincentive effects and generate approximately €70m per annum in additional income taxation.[2]

### 3. *Reform tax reliefs associated with pension savings*

The largest area of personal tax expenditure is related to pensions. Overall, pension reliefs amount to €2.7 billion per annum in revenue forgone. Reform to this area sits in the context of other proposed reform to pension savings supports, including the introduction of auto-enrolment, which may carry significant additional costs in state subsidies and tax expenditures.

Within the area of pension savings, three tax expenditure measures are worth reforming:

(i) *Limiting all pension contributions to tax relief at a single rate of income taxation.* Currently this is offered at the marginal rate meaning the state supports the savings of higher income earners more than those on lower incomes. Depending on whether the adjustment was to the standard rate for all or to a hybrid rate, say 31%, the annual savings would be between €200 and €400m per annum.[3]

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[2] See Collins, M.L. (2013) *Modelling the Withdrawal of Personal Income Tax Credits from High Income Earners*, NERI Paper 2013/4. Dublin, NERI.

[3] See: Collins, M. and Hughes, G. (2017). Supporting Pension Contributions through the Tax System: Outcomes, Costs and Examining Reform, *The Economic and Social Review,* Vol. 48, No. 4, pp. 489 – 514; Doorley, K., Callan, T., Regan, M. and Walsh, J.R. (2018). *The Tax Treatment of Pension Contributions in Ireland*. Dublin:

(ii) *Restricting the tax-free lump-sum payment to a value equivalent to two-thirds of average earnings.* Currently, the first €200,000 of pension savings (or 25% of total pension savings) can be drawn down tax free. This is an abnormally high level in international contexts, where many countries do not facilitate any tax free drawdown. The benefit is much greater to those with the highest incomes and the largest pensions savings. While there is a case to abolish the tax-free lump sum in its entirety, the provision of a smaller tax-free lump-sum to all retiring workers has some merits; a value set at two-third of average earning would correspond to approximately €30,000. The Revenue Commissioners have not provided a costing of this tax expenditure since 2014; it then cost €134m.

(iii) *Reducing the standard fund threshold (SFT) to €1 million.* The SFT is a limit or ceiling on the total capital value of pension benefits that an individual can draw from tax-relieved pension arrangements. It is currently set at €2 million (since 2014) having been €5m when introduced in 2005, and reaching a peak of €5.4m in 2010; prior to 2005 there were no tax-supported pension savings limits. In effect, the threshold represents the point at which the state will step aside from using tax reliefs to support pension savings. Judged from that perspective, it is difficult to justify why the state should continue to subsidise savings beyond a threshold of, say, €1 million. It is not that individuals should be impeded from saving resources at more that this level; rather that the state has done its jobs supporting savings when they reach this point and there are better uses for the states resources beyond that.

### *4. Abolish the Special Assignee Relief Programme (SARP)*

The SARP provides a tax break to high earners, those working for international companies in Ireland who relocate to Ireland and have earnings more than €75,000 per annum; according to Revenue Commissioner's data individuals earning above €75,000 are in the top 6 per cent of earners in the state. The scheme provides for full income tax relief on 30 per cent of income over the €75,000 threshold, subject to an upper limit of

ESRI; and Government of Ireland (2020), Report of the Interdepartmental Pensions Reform and Taxation Group 2020, Dublin, Stationery Office.

€1 million per annum. The scheme also allows tax free employer provided benefit-in-kind of €5,000 per child per annum in school fees and one trip home per year for the individual and his/her family. In 2018 the scheme cost €42.4m, was availed of by 1,481 individuals at an average benefit of €28,629.[4] Based on the Revenue Commissioners numbers, this suggests the average recipient has an income of €313,000. This would put them in the top half per cent of the earnings distribution. While there are economic benefits to a schemes such as this, one could make similar arguments for many other jobs and roles. However, do earners at this level of income need a tax reduction? On the grounds of fairness, I think the scheme is hard to justify; there are better uses for these resources.

### *5. Standard rating of other tax reliefs*

As a general point of principal, where Government supports are provided through the taxation system they should be worth the same to all income tax payers irrespective of whether they are fortunate enough to have a high income or not. As well as the aforementioned tax relief on pension contributions, there are a number of other tax expenditures granted at the marginal rate i.e. worth 40 per cent to some and 20 per cent to others. A recent reply to a parliamentary question identified that making this reform, for those tax expenditures costing more than €5 million per annum, would yield €147.7 million in additional taxation revenue each year.[5] Again, on the grounds of fairness such a reform seems appropriate.

## Final Observations

Chairman, to conclude, I wish to thank the committee for the opportunity to engage with you this morning. I strongly encourage the committee to adopt a recurring and systematic approach to the oversight of these budgetary choices; tax expenditures are a hidden but important part of the decisions we make on the allocation of the state's resources. Thank you.

[4] From PQ 44567/20
[5] See PQ 10516/20