DÁIL ÉIREANN

AN ROGHCHOISTE UM FHORMHAOIRSIÚ BUISÉID

COMMITTEE ON BUDGETARY OVERSIGHT

Dé Céadaoin, 20 Meán Fómhair 2017

Wednesday, 20 September 2017

Tháinig an Roghchoiste le chéile ag 9 a.m.

The Select Committee met at 9 a.m.

Comhaltaí a bhí i láthair/Members present:

Teachtaí Dála/Deputies	
Richard Boyd Barrett,	
Thomas P. Broughan,	
Dara Calleary,	
Lisa Chambers,	
Pearse Doherty,	
John Lahart,	
Michael McGrath,	
Eamon Ryan.	

I láthair/In attendance: Deputy Mattie McGrath.

Teachta/Deputy Josepha Madigan sa Chathaoir/in the Chair.

Business of Select Committee

Chairman: Apologies have been received from Deputies Colm Brophy and Stephen Donnelly. Before we bring in our witnesses, we will go into private session to deal with housekeeping issues.

The select committee went into private session at 9.07 a.m. and resumed in public session at 9.12 a.m.

Ex-ante Scrutiny of Budget 2018: Nevin Economic Research Institute, Irish Congress of Trade Unions, Irish Tax Institute and Chambers Ireland

Chairman: Before we begin, I remind members and witnesses to turn off their mobile phones. The interference from mobile phones affects the sound quality and transmission of the meeting.

I welcome Dr. Tom McDonnell, senior economist from the Nevin Economic Research Institute, NERI. With him is Mr. Liam Berney, who is an industrial officer with the Irish Congress of Trade Unions, ICTU. I thank both witnesses for making themselves available to this committee. Dr. McDonnell has been asked to touch on the themes of income taxation, USC and distribution, labour market participation and demographics in his presentation. Mr. Berney was invited to speak on the issues of labour market participation, the Lansdowne Road agreement and budget impact, VAT and the hospitality sector, income taxation and Brexit.

Before we hear our guests' opening remarks, I draw their attention to the position on privilege. Witnesses are protected by absolute privilege in respect of their evidence to the committee. However, if they are directed by the committee to cease giving evidence on a particular matter and they continue to so do, they are entitled thereafter only to a qualified privilege in respect of their evidence. They are directed that only evidence connected with the subject matter of these proceedings is to be given and they are asked to respect the parliamentary practice to the effect that, where possible, they should not criticise or make charges against any person or entity by name or in such a way as to make him, her or it identifiable. Members are reminded of the long-standing parliamentary practice to the effect that they should not comment on, criticise or make charges against a person outside the Houses or an official either by name or in such a way as to make him or her identifiable.

Dr. McDonnell has been allocated 15 minutes for his opening statement, and we look forward to hearing from him. We will then take questions and answers. He does not need to use the 15 minutes if it is not appropriate.

Dr. Tom McDonnell: I will be as brief as I can. I thank the chairperson for the opportunity to appear before the committee. I will discuss those three issues within the broader context of how the economy is doing. I will also speak about the budget.

The most recent national accounts were published at the end of last week. The headline figures are that there has been real GDP growth of 5.5% in the first half of 2017. Every sector grew on an annual basis in both the first and second quarter with the exception of financial and insurance activities. The construction sector expanded by a fifth in the first half of 2017 compared to the same period last year. Our forecasts are now for GDP to increase by between 4.5%

and 5% in 2017. Perhaps more interesting than GDP is the new measure of modified domestic demand which the Central Statistics Office, CSO, has developed. It gives a more accurate measure of activity in the domestic economy by stripping out intellectual property investment and purchases of aircraft by leasing firms. Modified domestic demand grew by 2.4% in the first half of this year, which is slightly below what my expectations were, given how strong employment growth has been. The relatively strong growth should continue into 2018 as, in our view, the economy continues to approach its potential and, on the back of this, unemployment should fall below 6%. Employment growth should continue at a strong pace in 2018. Clearly, the outlook for 2019 is much more uncertain, not least because of Brexit, but also because of other factors such as the potential for interest rate increases by the European Central Bank, which would dampen domestic demand in the Irish economy.

The public finances are improving. The general Government deficit will be close to zero in 2018 and 2019 on current forecasts, but it must be borne in mind that the gross debt level remains elevated and is greater than 100% if expressed in the new GNI* metric, though that metric is itself problematic. Our view - and this is currently one of the debates between some of the institutions such as the OECD and the ESRI - is that there is limited evidence of overheating in the economy. Total employment and the employment rate are still below pre-crisis peaks. The employment rate is indeed below the EU average, despite the assumption that the Irish economy is rocketing along and doing really well. It is doing really well compared with how it was doing, but its employment rate is below the EU average and significantly below the top performers such as Sweden. The unemployment rate is also still relatively high; it is higher than in such countries as Germany, the UK and the US. The recent growth in consumption that we saw in 2016 follows almost a decade of stagnation and therefore partially reflects a working through of pent-up demand. At the same time, consumer price inflation is only 0.4%, while average hourly earnings are growing at just 1.6% year on year, again after years of stagnation. Underlying investment is admittedly growing strongly but is doing so from a very low base, while consumer credit is less than half its 2009 peak.

Some of the more traditional metrics used to attempt to understand whether an economy is overheating include the current account balance. Unfortunately, it is impossible to measure the real current account balance at present. Technically, it is in surplus. The current account*, which is the new metric, is in deficit but there is a lot going in and out of that which perhaps does not reflect the real economy and its sustainability.

Property prices are growing very quickly but, again, are less than three quarters of their peak value, and the recent price growth should be understood as essentially a market failure in the housing market, with supply running well below projected long-run demand, something that is likely to continue for the foreseeable future.

The committee invited me to comment on income taxation, labour market participation and demographics. Regarding income taxation, according to OECD data, the total employee tax wedge - that is, income tax, USC and employee PRSI - for a single person as a percentage of gross wage earnings is 19.2%. This is the lowest in the EU 15 and less than half that of Belgium and Germany. It is also lower than that of the United States. Ireland is also the lowest tax country if we compare the same person's tax wedge as a percentage of total labour costs. This would include employer PRSI. If we compare *per capita* receipts from taxes on labour in Ireland with *per capita* receipts in the other high-income EU countries - I am talking again about income tax, USC and PRSI - we find that receipts in Ireland are almost €2,000 lower. It is the low level of social contributions, namely, PRSI, that really explains this difference. The OECD also compares earnings from 50% to 250% of average incomes for a range of family types and finds that Ireland is a consistently low-tax jurisdiction. The graphs I have provided in the supplementary materials show that labour taxation in Ireland is very progressive. However, given the high level of gross income inequality - that is, market income inequality - in Ireland, this is only sufficient to move Ireland to the middle of the EU pack in terms of net income inequality. If we were to reduce that progressivity, we would become one of the more unequal countries. Finally, this progressivity is mainly attributable to the structure of the income tax. The USC is only modestly progressive, although it does have the advantage of being immune to almost all tax expenditures, most of which are regressive in nature. Pension tax relief, for example, tends to accrue to the top 20% of earners.

Regarding labour force participation and demographics, the most recent cross-country data from the OECD, which is for 2015, shows that Ireland had a labour force participation rate of 70.1% for persons aged 15 to 64. This was below the EU average of 72.7% and significantly below the UK's 77.6%. Ireland is more than 11 percentage points below Sweden and 17 percentage points below Iceland.

One notable barrier to labour force participation in Ireland is the extremely high cost of child care. This is particularly relevant in the case of second earners and lone parents and mainly effects female labour force participation. The implication for budget 2019 and beyond is clear. It is necessary to increase State spending on child care subsidies and to reduce the cost of child care. Budget 2018 was a very important start, but we are still far from best practice in terms of the quantum of State supports for child care.

Ireland has very favourable demographics compared with most other advanced economies. Our working age ratio of 65.2% is broadly in line with that of the EU as a whole. The important difference is that we have a much larger young person ratio than the EU and a much smaller elderly population. This means the Irish economy has a higher growth potential than that of the EU, which is very positive. On the other hand, Ireland's relatively small elderly population, which at 12% is just two thirds of the EU average of 18%, makes our long-run fiscal position appear stronger than it really is. This position will deteriorate over time as the population ages. Elderly people require additional spending on health and social protection and are generally out of the workforce. Finally, our fertility rate of 1.9 is well above the EU average of 1.5. This is positive in terms of long-term economic growth. However, this fertility rate also implies deteriorating demographics over time in the absence of inward migration, as 2.1 is the replacement rate.

In respect of fiscal policy, the remaining fiscal space available is less than €500 million in 2018. This is concerning given the severity of the housing crisis and the evident need for additional State support in this area. In addition, our analysis shows that Ireland underspends on a *per capita* basis compared with other high-income EU countries - those with a GDP *per capita* of €30,000 or more - in a number of areas. Notably, we estimate that the State underspends in a number of areas fundamental to long-run economic growth, specifically education, infrastructure and research and development, where the cumulative underspend is in the order of €2.5 billion to €3 billion. There is a particularly large underspend on primary education, especially in the area of ancillary supports, and on tertiary education. In this context we argue that long-run economic growth, employment and equity goals can best be achieved by prioritising use of the available fiscal space to increase public capital investment levels, increase spending on education, and increase direct spending and subsidies for research and development. Here, we are going beyond budget 2018 and talking about the period to 2021.

On the other hand, measured on a *per capita* basis, combined taxes and social contributions in Ireland are significantly lower than in comparator high-income EU countries. Taxes and social contributions are combined by the OECD because they are compulsory payments. The OECD sees social contributions as taxes in effect. Ireland is particularly low when it comes to taxing stocks of capital, for example, property taxes, inheritance tax or wealth tax, and when it comes to social contributions from employers. Overall, there is no evidence that the Irish tax system is onerous compared with other high-income European states. In light of this, and in the context of substantial areas of underspend, the case for further tax cuts is extremely weak. Indeed there is a strong argument for increasing taxes in certain areas.

Chairman: I thank Dr. McDonnell. IBEC was before the committee yesterday and its view is that our tax base is too narrow and that we have too high a marginal tax rate. What is NERI's view on that? Dr. McDonnell mentioned that child care is a major barrier to employment and I agree with him. Does he think the Government child care scheme will go some way to improving the situation?

Dr. Tom McDonnell: The budget 2018 measures will be extremely helpful in respect of child care supports. Our view is that it is a start. State spending on child care is well below what it would be in the Nordic countries. In the countries that have such high labour force participation rates, particularly for women, second earners and lone parents, the barriers for entering the labour force and staying in the labour force are much lower. I view that as year one and we gradually ramp that up over time. Clearly there is a capacity issue with the number of people working in the field.

There are also issues with the attractiveness of that as a career. One should consider moving it to being something akin to primary school teachers, who are salaried over a year and it can be a genuine profession, leading to a higher quality workforce in the long run. To give the best bang for buck, the best returns economically are in within education. Within education, the best bang for buck is the earlier the better. Therefore, pre-primary care and pre-primary education are extremely important for the development of human capital. It is a terrible phrase, but it is one used in the economics literature. The biggest barrier to human capital, of course, is poverty, but early childhood care and education are also extremely important. In our view, that should almost be top of the priority list for budget 2019 and beyond.

The marginal tax rate kicks in at quite a low rate when compared internationally. However, the effective tax rate for someone on average earnings is well below what it is elsewhere - the graphs are included in the supplementary materials. Comparing personal average tax rates and labour income for a single earner, for example, we are below the EU 15 all the way up to 250%, which is as far as the OECD does it. The gap is significant enough that one would imagine it goes to at least 300%. Therefore, someone on the average wage is paying less than-----

Deputy Richard Boyd Barrett: On what page is that?

Dr. Tom McDonnell: In the supplementary materials, the graph is on page 12. There is also a table entitled, “Comparison: Income Tax plus Employee Social Security Contributions in 2016 as a Percentage of Gross Wage Earnings”, which looks at the single personal average earnings for Ireland, the other EU 15 countries, the United States and the OECD as a whole. The total payment is 19.2% according to the OECD, which is the lowest in the EU 15. For example, the United Kingdom has 23.3%. The EU 15 average is over 30%. Even countries like the United States have a higher level of tax. It is simply not factually correct to say there is an onerous burden on the average earner. The reason for that is the system of tax credits, which keeps the effective tax rate really low. Even though the marginal rate kicks in quite early, the effective tax rate that people are actually paying is quite low for most of the distribution. The tax wedge as a percentage of labour costs is lower again because employer PRSI is so low in Ireland compared with comparator countries. It is important to bear that in mind.

Ireland has issues relating to costs. We have high costs in a number of areas such as child care, rent, groceries and so on. The focus should be on dealing with those specific issues in a targeted fashion rather than narrowing the tax base further, which I understand may be about to happen in the coming weeks.

Given that we are talking about a fiscal space of about €330 million, the full-year cost of increasing the standard-rate cut-off point by €1,000 would be a little over €200 million. We believe that would be a poor use of the existing fiscal space. It would be better to deal with areas like child care, education, infrastructure and so on.

Chairman: I call Deputy Calleary.

Deputy Dara Calleary: Dr. McDonnell actually answered my question about child care.

Chairman: I call Deputy Boyd Barrett, followed by Deputy Eamon Ryan. I ask Deputy Boyd Barrett to confine his contribution to five minutes because we have many witnesses. We can come back to him again later in the meeting.

Deputy Richard Boyd Barrett: I thank Dr. McDonnell of the Nevin Economic Research Institute. I welcome the focus on increased investment in child care, education, research and development and infrastructure. I welcome the general thrust of what Dr. McDonnell has said. He said that there is a case for more taxes. Could he be more specific about what he is proposing? Would he agree that the amount of fiscal space is miserable, compared to the requirement for investment in the areas he has identified, including housing, child care, research and development and education? What would he propose in that regard?

I take Dr. McDonnell's point about the tax wedge being lower than average. I think we have always had a difference of opinion about property taxes. How would he respond to the popular perception that while our direct labour taxes might be somewhat lower - I believe Dr. McDonnell when he makes that argument - we have a whole range of hidden regressive charges and taxes? I could go through the list of such taxes, including VAT on the consumption of goods, parking charges, high bus fares and the cost of rent. Many people believe property tax is a regressive charge because it does not take income into account. Does Dr. McDonnell accept that people are right to resist things like property tax? Does he agree that there are fairer ways of going after wealth, such as taxes on landlords who have multiple properties, financial transaction taxes, wealth taxes and taxes on people's highest earnings?

I ask Dr. McDonnell to comment on Jeremy Corbyn's approach to tax, which is very popular. It is old-school, left-wing politics. It involves increasing taxes on the richest 5% only. It has received massive traction. It comes from a left-of-centre perspective. Does Dr. McDonnell agree that the left and the trade union movement should be arguing in favour of this kind of approach?

Dr. Tom McDonnell: The Deputy has asked many questions. The easiest question to answer is the one about fiscal space. I agree that it is miserable. It is not nearly sufficient to deal with all the problems that will arise over the next year. Part of the problem with the fiscal space is that the Commission's methodology for calculating it - which is bunkum, as any serious economist knows - is reducing it by over €1 billion in the context of next month's budget. The Commission's view is that we have been overheating ever since we had an unemployment rate of 10.3%. Its model is not designed for Ireland at all. It is essentially taking some of our fiscal space away from us.

The Deputy asked me to be specific about the taxes I am proposing. He spoke about different property taxes and the range of hidden charges. His point about the range of hidden taxes and charges is absolutely correct. The taxes that people rarely notice are VAT and excise duty. Maybe people notice excise duty when they see how much cheaper certain things are in other countries. Ireland over-taxes, and is a high-tax country, in the area of consumption taxes. On average, such taxes are higher in Ireland, on a per-person basis, than they are in the other ten high-income countries. This point does not necessarily apply to VAT, but is particularly relevant to excise duty. Our excise rates are extremely high by comparison with other countries. We have a range of regressive charges. The television licence is a flat charge. That is the most regressive structure one can have. It is probably our most regressive tax or charge. Everyone has to pay it, in effect.

It is true that the property tax is not progressive in the same way as income tax or the USC. I believe this conclusion was reached in research from the ESRI. It is a tax on an asset, not necessarily a wealth tax *per se*, and it has certain problematic elements such as where a person with a very low income pays a high level of property tax. The best way to deal with such situations is to provide relief by way of a charge on the property which would only become due on sale or transfer. It would accrue over time and, when it is being inherited or sold, the State would get what is owed to it first. Over a lifetime, the State would get the same amount of property tax but it would not cause hardship issues for low-income households. The determination of what hardship was could be left to a democratic decision but I have not carried out any research into that point.

The Nevin institute has published papers on a financial transaction tax, FTT, and on a wealth tax. A wealth tax on all assets over €1 million, without reliefs, would generate a yield of around €0.3 billion.

Deputy Richard Boyd Barrett: Is that at 1%?

Dr. Tom McDonnell: Yes. It does not sound like a lot but the current long-term return on capital is approximately 4%, meaning it is tax of 25% of that amount. It would only affect the top 1% or 2% of households. A wealth tax operates from a different base from income tax and wealth inequality is much more pronounced. Many economists take the view that the best way to deal with intergenerational wealth inequality is inheritance and gift tax, which we call capital acquisitions tax. We tax the person who gets the money rather than the inheritance itself and that is a better system than the one in the UK. The problem is the system of reliefs is so inordinately generous for particular types of assets that many people can have an inheritance worth millions without paying a penny in tax.

I was asked whether I could be specific about the different types of taxes. I stated that we have an overall revenue problem and we are not so much a low-tax country as a low-revenue country. The big difference is social security contributions, which in Ireland are PRSI. Employer PRSI makes up 80% of the gap to the high-income EU average and that is the elephant in the room. It is often called a social wage because in many countries it goes towards benefits for workers. If the benefits went towards something such as child care subsidies it would be for the benefit of employers in the long run, as it would increase the size of the labour force. If it went to the retraining and upskilling of workers it would lead to a more productive workforce. Child care subsidies also lead to a more productive workforce by keeping women in the workforce and, as we know, women are more educated than men. Moreover, when they fall out of the workforce they often never fully come back.

Genuine reform will be necessary in regard to the sufficiency of revenue as there is a pensions time bomb, health care is going to increase year on year and we have an infrastructure deficit, which has been well flagged and of which the committee is cognisant. Our research and development deficit, compared to the top performers, is €0.5 billion per year. The literature on economics suggests one has to have a functioning innovation system to develop top companies but we ignore that completely and our spending is two thirds of that in Sweden and elsewhere. Such countries have the idea of the “entrepreneurial state” but we do not have that. We discuss increasing employer PRSI and the property tax - there can be other types of property tax, for example, on stocks – and perhaps reducing consumption taxes. We are not just about increasing taxes - the distributive impact is important; for example, taxes on pollutants could be increased and used to subsidise renewable energies - but also about reforming the taxation and revenue systems and public spending to bring us into line with the best performing countries in the world in terms of policy. We are a long way off that. In our summer and autumn quarterlies and some of our working papers, we have tried to show what those countries do and describe what needs to be done to get us there.

The fiscal space is extremely small this year, but we view this as a five-to-ten-year issue and beyond. Improvements can be made year on year. Unfortunately, we cannot solve everything in one year, but at least we can make a start. Does that answer the question?

Chairman: I thank Dr. McDonnell. I propose that-----

Deputy Eamon Ryan: May I ask a question?

Chairman: If he would not mind, the Deputy might ask that in moment. To be time efficient, I will ask Mr. Berney to make his opening statement after that. Deputies Lahart and Chambers will then be next. Deputy Doherty can ask his questions of both witnesses. Deputy Calleary can also contribute.

Deputy Eamon Ryan: I will be brief. I thank Dr. McDonnell for attending. Regarding the term “human capital”, IBEC said something similar when it appeared before us yesterday. It wants more human capital in business. If I pay someone else to raise my children - I must be careful with my words, but I mean child care - that is developing human capital. If I care for the children myself, is that human capital? Is capital just a monetary thing?

I ask this question because a large number of people make this choice and feel that they were forgotten, and their work undervalued, by last year’s budget. IBEC seems to believe it is a monetary thing. I am worried that the trade unions seem to believe it as well. That is a strong, powerful combination. In our tax system and everything else that we do, we have incentivised the situation because we want there to be more human capital. Should we not leave the choice as to how that human capital is developed to parents?

I agree with Dr. McDonnell, in that this is some of the most important and valuable work that we are doing, but there is a slight dichotomy. On one hand, Dr. McDonnell is saying that child care is too expensive, which is the case for many people. On the other hand, he is saying that this is the most important work that anyone can do and we should be paying child care workers the same that we pay primary school teachers. If Dr. McDonnell does not have the figures, he can revert to me with them, but what is the average pay of a child care worker and what is the average hourly pay of a primary school teacher? If we are to value this work and increase the pay of child care workers to that of primary school teachers, what would it cost and how would we afford it? I am fully supportive of that idea.

How would Dr. McDonnell have voted in Dublin City Council last night if he had had a call on increasing the property tax? It was a “Yes” or “No” vote, so I would love if he could give me a “Yes” or “No” response.

The ESRI appeared before us and, interestingly, pushed for a switch to a site value tax. Has NERI undertaken any work on the merits of switching property tax away from the current model to a site value model?

Dr. Tom McDonnell: “Human capital” is a terrible expression. It is a technical one that we use to fit the matter into an economic model. Sometimes, we use it as a term to encourage policy makers to think of something as being good for the economy in the long run, but what we are really discussing is flourishing individuals and their ability to thrive in the world, which also tends to make them productive workers.

The point of the child care subsidies is not to devalue people who choose to educate their children themselves. Rather, it is that second earners and lone parents should not have barriers preventing them from having a real choice about whether to return to the workplace. For us, it is about choice. It is not about devaluing or demeaning those who stay at home in any way. I have immense respect for that. I would not for a moment underrate it. The single most important thing is the family environment. A child will only spend about 12% of his or her week at school. If we are talking about human capital, the single most important thing we can do is prevent childhood poverty. That means family income supports and other supports. Indeed, our work suggests that the emphasis in terms of education spending would be on disadvantaged groups, preventing people from ever falling behind. I would not want people to get the wrong impression.

My colleague will be able to give the committee a better steer on average rates of pay for child care workers and primary teachers. That is something we could calculate in terms of fiscal space if the committee would like us to. The other question is how we would pay for it. We would do so out of the upcoming fiscal space, which is about €10 billion after 2021, not counting demographics and price pressures which will eat up about half of that. Otherwise, we would increase taxes.

I was asked how I would have voted on the property tax. The Nevin institute does not make explicit political statements such as how we might vote on particular issues.

Deputy Richard Boyd Barrett: That is the easy life. NERI wants the money but we have to vote for unpopular Bills.

Deputy Eamon Ryan: We have the yellow button for that.

Dr. Tom McDonnell: NERI can talk about what the advantages or disadvantages of different policy options might be. We never go as far as to actually say we would vote “Yea” or “Nay” on something.

As to a site valuation tax, that is an excellent concept. I see no reason the two could not be combined or blended without necessarily being merged completely. The classic idea from the 19th century was, of course, the land tax from Henry George. The economics literature is clear that all of those taxes are extremely positive in terms of the economic benefits, particularly compared with some other taxes. They are not necessarily progressive because they are not based on income. When taxes are based on wealth, they generally are progressive. The site valuation tax has the advantage of not necessarily disincentivising development. On the other hand, the property tax perhaps reflects the real value and may be more progressive in terms of its actual effect. Personally, I think both taxes are good ideas. One would not necessarily have both of them in place. To get rid of a property tax and replace it with a site valuation tax would, I suspect, be politically very difficult.

Chairman: I thank Dr. McDonnell and invite Mr. Berney to read his opening statement, after which the remaining members can ask questions of both witnesses.

Mr. Liam Berney: I thank the Chairman and the committee for inviting us here today. While the statement we submitted to the committee touches on the issues we were asked to address, members will notice that it contains no reference to the Lansdowne Road agreement or the proposal for a new public sector pay agreement. There is a very good reason for that. As politicians, the committee members will appreciate that the trade union movement is a democratic organisation and the process of approving the public sector pay agreement only concluded earlier this week. It would have been premature for us to include comments on the agreement in our submission prior to it having been accepted by our affiliate organisations. It was accepted by a large majority of the public services committee on Monday. In accepting the agreement, the public services committee of ICTU notes that there are still some issues that are hangovers from the crisis era and that there are matters to be addressed around the issue of public pay. Most notable in this regard is the question of new entrant pay and pay equalisation. The headlines have focused on teachers, but there are new entrant pay scales in all parts of the public service and there is still pay inequality in many parts of the public service. We should focus on trying to eliminate this over the coming period. There is also, of course, the question of retention and recruitment in critical areas of the public service which need to be addressed as part of the public service pay agreement. However, the agreement has been accepted by a large majority of the public services committee and we are looking forward now to implementing the agreement and making sure that the issues to which I have just referred are addressed within that context because they are very important issues.

My remaining remarks are really in the context of the pre-budget submission that Congress has produced. I understand that all Members of Dáil Éireann and Senators, as well as councillors, have received a copy of our pre-budget submission, so my comments are made within that context. From our perspective, people deserve to see an inclusive, equality-proofed budget that places the welfare and betterment of the majority at its very core. We have a responsibility to make sure budget 2018 is the first in a series of transformative budgets that will prioritise higher living standards and quality of life underpinned by a programme of investment in infrastructure and improvement to services. For budget 2018, Congress has three key priorities. We must begin the process of tackling the housing and homelessness crisis. That must be our absolute priority. We must end the reduced VAT rate for the tourism sector, which has cost some €2.2 billion in lost revenue to date, and invest in public services such as education, health and child care in order to lower living costs. I will come back in a moment to the question Deputy Ryan asked earlier about the cost of privately provided child care as opposed to pay for teachers and so on.

On the question of housing and homelessness, failure to tackle the housing crisis properly in budget 2018 would see Ireland pay a high price in terms of future social cohesion, damage to future growth prospects and increased living costs for working people. Although housing and homelessness are acute problems in themselves, they are very much labour market problems as well because they inhibit people's participation rates in the labour force if they do not have access to affordable housing. Congress proposes that local authorities across the country take the lead in the provision of social housing as the only long-term sustainable response to the crisis. Unfortunately, we abandoned the housing market to private developers and let profit become the key driver of housing provision. However, the market has failed and, as classical economics tells us that government must step in in the case of market failure, the Government must now step in and declare a national housing emergency and act accordingly. Local authorities, as we said, should take the lead in a major house-building programme with funding of at least €1 billion from Government, providing at least 10,000 social housing units a year by late 2018. Given this is an emergency, compulsory purchase orders must be utilised as a matter of urgency - there has been conjecture around the constitutionality of that, but we do not believe the Constitution is an impediment - to ensure available serviced land is put to good use, while the introduction of the vacant site levy should be brought forward from January 2019. We simply cannot afford a return to the developer-led and developer-shaped policies of previous years, despite recent attempts from the private sector to extract more tax breaks and subsidies in order to build houses. I notice Deputy Ryan said that IBEC was here yesterday. There is a subgroup of IBEC that represents property developers. If the committee reads its pre-budget submission, it will be shocked to see what it is seeking. Essentially, it wants a tax-free environment. If that were to be the approach to incentivising developers, it would make the situation far worse. We question the value of the help-to-buy scheme and think that money would be far better used by giving the funding to local authorities for housing construction. In the short and medium term, thousands of lives and life chances are being damaged beyond repair by the housing crisis. This itself is cause enough to act. However, the crisis will also discourage inward investment, drive up living costs for working people and have an adverse impact on the labour market. Budget 2018 is an opportunity to deliver a game-changer on this critical issue.

One of the issues we were asked to talk about is the tourism sector's VAT subsidy. Congress continues to argue for an end to the special reduced rate of VAT enjoyed by the hospitality and tourism sector. This is a *de facto* subsidy that has already cost the State €2.2 billion in taxes forgone. There is no justification for this ongoing subsidy to a highly profitable and predominantly low wage sector. This is a sector that refuses to participate in the joint labour committee system the Government has established for wage setting in sectors. It refuses to participate in the process.

There is no evidence of any significant new job creation or that the consumer has benefited in any way. ICTU regards the subsidy as being used simply to take profits. There is no other use for it that we can see. In fact all the evidence suggests that the reduced rate operates as a subsidy to very profitable corporations, which is a waste of valuable resources when set against areas of obvious need such as homelessness. Ending this unjustified and wasteful subsidy will create additional fiscal space which can then be used for much more urgent priorities in education, child care and infrastructure.

A question was asked earlier about where we can get new taxes. In the last table of our pre-budget submission, congress has set out where new taxes can be raised. This is one of the places where a significant amount of money could be raised without any real risk.

We want to emphasise the importance of investment. Workers deserve a much improved social wage paid for through general taxation or social insurance. Congress is calling for additional investment in public services, including education, health and child care, in a bid to lower living costs and to boost a social wage for working people. We know that Brexit carries huge risks for the Irish economy. The best way to respond to Brexit and other threats to our collective prosperity is to invest in the things we need. We need to invest in skills to retrain and upskill workers especially in sectors most vulnerable to Brexit and to climate change. Deputy Ryan and others are aware of the need to invest in adjustment transition for workers who are affected by vulnerable industries with regard to Ireland's climate change obligations. We need to invest in infrastructure such as public and other transport hubs to meet the challenge of diversifying trade flows. Investment is also needed in the areas of research, innovation, marketing and organisational capacity to develop new products and services and locate new markets and alliances. We also need to invest in core economic and social infrastructure to help make Ireland a country with high levels of well-being, equality and economic efficiency.

Plans for tax cuts in the budget should be abandoned. Ireland has massive infrastructure deficits in housing, transport, broadband, renewable energy and water treatment that require immediate attention. Such investments must take priority over tax cuts.

Public capital investment should be doubled over the next three years and the rainy day fund should be used now rather than later to address vital areas of infrastructure deficit. Ireland has a young and growing population, and bottlenecks will only get worse if we fail to invest now.

The trade union movement stands in solidarity with the most vulnerable people in society, including pensioners, young people and others who are dependent on social welfare, income support and social transfers. Social welfare payments should be restored by more than the expected cost of living increases in 2018. I am happy to take any questions from members on the congress pre-budget submission and I have brought spare copies with me if the committee needs them.

Deputy Ryan asked about the wages of child care workers in the private sector and those of a primary teacher. I cannot be absolutely certain as I do not have exact figures, but I will find them for the Deputy. Congress published a paper on this issue not too long ago. From memory, child care workers in the private sector earn, on average, between €12 and €15 per hour. A primary school teacher would earn somewhere between €25 and €30 per hour, as far as I am aware. The question is that the policy direction has decided to subsidise private child care provision. Money is given to private child care providers, yet there has been no examination of the possibility of providing child care services within the State sector. In Scandinavian countries, for instance, children go to primary school much earlier than children in Ireland. They go into a different setting than a classroom where child care is provided and there is an educational dimension within that setting. There is no reason at all why, with a small infrastructural spend, Ireland could not produce child care settings in the public sector in primary schools. This would not be for the purpose of sending children to school. Obviously their early developmental education would be much different from that which they would encounter when they attend primary school. Directly intervening in the sector with public sector child care provision is one way of dealing with a problem that has been completely ignored and not given proper consideration in this State, as far as I can see.

Chairman: I thank Mr. Berney. Deputy Lahart is next and he may ask his questions to both the witnesses, if that is okay.

Deputy John Lahart: I thank the Chairman. Is that simultaneously? I will talk out of both sides of my mouth.

Chairman: We are trying to confine contributions to five minutes.

Deputy Richard Boyd Barrett: I could make a comment there.

Chairman: I shall resist the urge myself. I ask Deputy Lahart to please continue.

Deputy John Lahart: I will respond to the second speaker first. I thank Mr. Berney for his comments and I thank Deputy Boyd Barrett for his resistance.

I shall make a couple of responses. Budgetary oversight is interesting; we met representatives of IBEC yesterday and have listened to different participants. The meetings have left me with a strong sense of the challenges that politicians face in terms of making decisions because everyone has made valid arguments with some interesting contrasts. First, ICTU made a presentation and mentioned the abolition of the VAT rate. Last Monday, Fianna Fáil held a party think-in at which Professor Alan Ahearne made a presentation. He made the point that the abolition of the VAT rate would double or increase it by 50%. The difficulty with removing a tax is one might have to re-impose it.

I agree with Mr. Berney about the questionable treatment of workers. However, I disagree with his belief that increasing the VAT rate and returning it to its original rate would more than likely be passed on to consumers when they go out for a bite to eat or stay in hotels. I would like to hear his response to that.

I agree with Mr. Berney when he said: "Local authorities should take the lead in a major housebuilding programme with funding of at least €1 billion from government, providing at least 10,000 social housing units a year by late 2018." Does he live in the real world? I would love to see such a development. My own local authority of South Dublin County Council will complete ten social houses this year. Therefore, ICTU's request is unrealistic. I wish it were realistic. I am disappointed with ICTU making such a generalisation. I would like to have seen something more concrete, please pardon the pun, in terms of ways to deal effectively with the housing crisis. The figure is totally impractical. I wish I could wave a magic wand and provide 10,000 social housing units by the end of next year. The figure produced by ICTU is unrealistic and I am disappointed with the organisation.

One of my colleagues has suggested that close to €1 billion for the housing assistance payment, HAP, has been provided in the budget. That is a huge payment but it is one of the prices that we must pay.

Neither of the witnesses has said anything about the vulnerable middle classes. Dr. McDonnell mentioned USC cuts. I represent the constituency of Dublin South-West. It represents a good microcosm of the country because it has middle class, working class, working-middle class people and people who are seriously disadvantaged. The constituency also has a really struggling middle class for whom September is the new Christmas in terms of child care costs and back to school allowances. They are the people who budget from month to month. If there is an unexpected cost in a month, let us say the car, fridge or washing machine breaks down and needs a part that has not been budgeted for, these people are thrown into a financial crisis. Therefore, a targeted tax reduction such as the USC would be welcome.

There is a lack of appreciation for people who must budget on a monthly basis. Recently I tabled parliamentary questions on motor taxation. If one pays one's motor tax monthly one is penalised. That situation may not seem much to people who can afford to pay their motor tax for a year. If one budgets from month to month one can pay up to an extra €100 or €150 per year, which means at least €10 a month. I agree with NERI that the property tax, and Fianna Fáil has said it for years, should reflect a person's ability to pay. I like the idea of the offsetting effect. In other words, the State ends up accruing the same amount of income from the tax.

I reiterate that the struggling middle class must budget from month to month and exist on a financial knife edge. Any little break we can give them would be greatly appreciated. I ask the organisations to factor that into their calculations.

Consumption taxes were mentioned such as excise tax. How can one reduce the excise tax on alcohol? There is a political debate on alcohol at present so a call to reduce the excise tax is completely unrealistic.

I shall conclude by discussing child care. I agree that the State has kept child care at arm's length from preschool for some unknown reason. I would co-locate preschool facilities. In the past few years we have embarked on a massive school building programme. Not including preschool facilities is a missed opportunity. School facilities could have been a one-stop shop for parents. Of course, primary school teachers are qualified to teach preschool children. I suggest that we increase the skills level in the sector. Unfortunately, as preschool education operates in the private sector, it means the cost of preschool will increase. I would appreciate any comments that the witnesses can make on these issues. The increased grant has, anecdotally, led to increased charges being imposed by some child care providers.

Chairman: I urge the Deputy to move on.

Deputy John Lahart: That is okay. I have covered everything.

Chairman: Five minutes have elapsed and we have a lot of business to discuss.

Deputy John Lahart: Clearly, I have not accumulated credits over the week-----

Chairman: No.

Deputy John Lahart: -----having not exhausted anything like my time.

Chairman: I thank the Deputy.

Mr. Liam Berney: I shall make a couple of points. Our proposals were not meant to be fanciful or unachievable. From our perspective, we face a situation where there is a limited amount of fiscal space and, therefore, we must prioritise how best to spend the available money. ICTU has tried to identify priorities in its pre-budget submission. Congress has thousands of members like those described by Deputy Lahart. We have tried to improve their incomes through the collective bargaining process. Hopefully, those who are employed in the public sector will benefit from the increases they will get through the wage increase that forms part of the public service pay agreement. ICTU has launched a campaign to increase pay in the private sector as well. We are trying to ensure, as best we can, that the traditional and most effective way of increasing wealth through collective bargaining is maximised.

ICTU has tried to emphasise that the scale of the problem is so great that we need a new response to address the homelessness and housing crisis. The only way to do this is to present the challenge accurately. That is why we have clearly stated that we need 10,000 new houses per year. I accept that we will not magic them out of nowhere. ICTU emphasised the problem in order to draw attention to finding solutions. That is why I made the point that local authorities must take a lead. There are significant gaps in the capacity of local authorities to do so. That does not mean we cannot look at ways to provide adequate resources to local authorities to meet the challenge. We must tackle the problem in some shape or form. The local authorities are best placed to understand the problem. For example, land that is not currently in use and is lying idle should be used to meet the housing need. ICTU believes that local authorities should take the lead in tackling the housing crisis. The purpose of the pre-budget submission by ICTU is to highlight the extent of the challenge we face. ICTU wants to focus attention on the political and policy-making systems in order to find ways to meet the challenge. Congress, as an organisation, can only point to the challenge and suggest ways to meet the challenge, which is what we have tried to do. Ultimately, the solution comes down to the political choices that are made by the people in these Houses on how to spend the available resources. We believe that the Government, in the 2018 budget, should, instead of cutting taxes, use whatever money is available to invest in the key infrastructural deficits that exist in the economy and our society. It is our view that this is the best way to spend the money. We are not unsympathetic to the point made by Deputy Lahart.

I shall respond to the question of dispensing with the 9% VAT rate in the hospitality sector. The Deputy said that the initiative would lead to the tax being doubled. That cost does not necessarily have to be passed on to consumers. ICTU has seen evidence that suggests that the hospitality sector has increased its profits due to the increased money generated by the reduced rate of VAT. Those in the sector can simply reduce their profits rather than pass the cost on to consumers.

Chairman: I thank Mr. Berney.

Dr. Tom McDonnell: Deputy Lahart made the point that it is difficult to reimpose a tax.

Deputy John Lahart: That is not really my view. I simply reflected a view.

Dr. Tom McDonnell: Yes, Deputy. One of the things that speaks to is that we should be very cautious about engaging in tax cuts, particularly when the economy is on an upswing. Actually the best time to cut taxes is during a recession, provided one has built up a sufficient surplus to be able to do that, to keep demand going in the economy and to keep things on a steady ship. With employment growing and the economy doing well, what one wants to avoid doing is overheating the economy. Given that we all acknowledge that there is a problem in the housing sector, the response to that, whether it is private or public, will be to ramp up house building and construction. We have seen that construction is already starting to expand quite quickly. What one does not do is to supplement it by cutting taxes at the same time because one runs the risk of overheating, such as what has happened in virtually every country in the world at different points. When people think about having all of this money, they suggest spending it and improving things now. Our emphasis is always on investment. What I mean by that is investing in something now to gain something even in 20 years' time when it comes to child care or education or in the near future when it comes to infrastructure and perhaps never at all, as it is a gamble when one invests in research and development. However, one cannot win if one does not try.

One point, that was perhaps taken up incorrectly, was that I did not actually mean to give the impression that we think that excise taxes should be cut necessarily. I agree the bad items should be taxed, whether it is alcohol, cigarettes, sugar, carbon and so on. I was simply making the point that it is actually the one area where we are a high tax country. It might be a good thing that we take those things seriously as problems, betting, of course, being another example.

I agree absolutely that in the longer term it would be better to co-locate and to roll preschool education in with primary education. It will take us a long time to get to that point, but to do it will require fiscal resources and ramping up. It would be wonderful to get a commitment from this Dáil to deal with this preschool issue, as well as housing, by putting in place a plan for it to happen during the next five to ten years.

On the question of the vulnerable middle classes, my first port of call is to say that their tax burden, as it were, is actually quite low compared with other high income countries. Perhaps that may be slightly simplistic. The labour taxes are low, but the employee contribution is not necessarily low. Perhaps reorienting the distribution of who pays labour taxation from the employee to the employer would help the hard pressed worker. We know that the countries that have a high level of employer PRSI do not seem to have a dearth of employed workers but tend to be the countries with the highest employment rates in the world. Of course, it is more complicated than that. Measures, such as reducing child care costs, improved infrastructure, which means lower public transport costs, better roads and rural broadband are all things that will help the economy and will help reduce costs.

Dealing with the housing crisis will push down the cost of rental in the long run and also will push down property prices as well. All of those measures will benefit the younger generation coming through, which of course, is the suffering generation, the people who did not get jobs in their twenties in 2008 and beyond and are now suffering from higher costs in many ways. That is the generation that has really suffered. What we can do for them is ensure that we have strong infrastructure and that we are Brexit-proofed by investing in education infrastructure or in research and development. There are certain sectors to which we will need to provide specific help to assist them, such as agrifood, but overall that would be the strategy that we would employ in terms of helping the hard-pressed middle earner. We are very cognisant of the issue but in our view the strategy we are proposing would help them more in the medium to long term.

Chairman: I thank Dr. McDonnell. Deputy Chambers has five minutes.

Deputy John Lahart took the Chair.

Deputy Lisa Chambers: I thank Dr. Tom McDonnell and Mr. Liam Berney. I wish to address a number of questions to Mr. Berney. In regard to VAT in the hospitality sector, I note that ICTU really seemed to focus on the fact that the lower rate of VAT did not give anything back to workers. Mr. Berney feels that his members have not benefited and are still being paid low wages when the sector is making profits. That seems like quite a hostile approach. It does not appear that ICTU has factored in the impact of Brexit on the hospitality sector, which is unknown. It seems premature to revert to the prior rate and increase it without properly considering the impact of Brexit. We could potentially lose jobs in the hospitality sector if the VAT rate were to go back up. Has ICTU considered that?

In terms of the rainy day fund, Mr. Berney says that we should spend it now and not save, but obviously this is a committee that has oversight of the budget and every household should put aside, if they can, savings in their budget. It seems a prudent thing for a country to put aside some funds to protect itself in the event that the unforeseen happens. I have to disagree with Mr. Berney on that point.

In regard to the housing help to buy scheme, Mr. Berney makes the point that the allocation of money to that scheme should be taken from it and reallocated to the local authorities. The Minister for Housing, Planning and Local Government, Deputy Eoghan Murphy, has stated that money is no object in terms of building homes and that the local authorities have access to as much money as they need. In that vein, the help to buy scheme was not referred to in terms of reducing it, or eliminating it. What are his views on the Minister's suggestion that money for local authority housing is no object?

I will now address questions to Dr. McDonnell on the growth of GDP. Obviously Government and politicians are fixated on the GDP growth rate, but my question is whether the welfare of the country is improving. In the past number of years, we have seen an increasing number of people commuting longer distances to work, having to spend longer times on the train or in the car, resulting in increased stress levels and mental health issues. The number of jobs has increased, but many are low paid or part-time jobs with zero contract hours offering no stability or security. Now we are discussing the reintroduction of bed-sits to deal with our housing crisis. We are very focused on GDP, GNP, GNI* and the measures of how the economy is doing, but there is little focus on the welfare of our people and our country. I would like to hear Dr. McDonnell's views on that point.

Dr. McDonnell stated that we rank 25th in the OECD in terms of public expenditure on research and development. We put money into tax relief for expenditure on research and development in the private sector. Is it Dr. McDonnell's view or the view of the Nevin Economic Research Institute, NERI, that we should redirect that money to public research and development? Would the country and the people be better served if we did that? Does that policy warrant a review?

I am glad that Dr. McDonnell referred to child care. Many child care workers in the country are on the minimum wage and do not earn €12 to €15 an hour. It has to be the only job where one can do a four year higher level degree and then earn the minimum wage. We have major problems. It is not a coincidence that it is a sector and a job that is predominantly done by women. The country needs to get to grips with the fact that women are not treated equally. In the year 2017, we are still moving around the subject of inequality, pay inequality, women's access to the workplace, and the low level of labour force participation predominantly among women, who have to take time out from work.

I am very glad that Dr. McDonnell states that we should invest in child care. I agree wholeheartedly. It should have happened years ago. We are so far behind, and we need to get moving on that. I would like to hear the views of both Dr. McDonnell and Mr. Berney on shared parental leave. We have maternity leave, but only the woman can take that leave. It often makes financial sense for the household to do that, but it can mean six months and more out of the workplace. The woman goes back to work but has very often been passed over by a colleague who has been at work. That is not to say anything against the person who has stayed at work, but we do not attribute enough value to the work in the home and we do not give the family the choice as to who can take time out. It is my strong view that shared parental leave, where the parents make the choice as to who takes the time and when he or she will take it, would go a long way towards addressing the inequality that women face in the workplace today.

When we are talking about housing and homelessness, we very much focus on the acute issues of homelessness, people on the streets or in emergency accommodation. I have a different experience as a person in my 30s. Many of my friends cannot get on the property ladder and have no prospect of getting on the property ladder. First, they cannot save the deposit, particularly if they are living in Dublin, and that is a problem for many people, but also because they are on contracts of six or 12 months' duration and have no job security, the banks will not look at their applications. What can we do? The banking sector is operating on archaic and old regulations and old risk models. They have not come up to speed with the way that work is now organised. A job is not as secure as it once was. Not everybody has a permanent, pensionable job and the days of such jobs are numbered. What can we do for people in their 30s and 40s who are struggling to get access to finance? On the USC, I take Dr. McDonnell's point that we should increase taxes but people want a break.

Vice Chairman: The Deputy's time is up.

Deputy Lisa Chambers: There are conversations about whether we should reduce the USC or widen the tax bands. If we increase the tax bands, those earning less than €33,000 will get nothing back. If we reduce the USC from 5% to 4.5%, it will impact on 1.3 million citizens who are working, though it is not big money. What are the witnesses' views on this? I know they do not agree wholeheartedly with reducing taxes but we have choices to make. Do they think the USC is the best thing to address, rather than tax bands?

My final question is on the sugar tax. Companies have become very smart by using alternatives to sugar to sweeten their drinks. A tax that may have been able to take in €100 million in revenue would now only take €40 million. There is also a cross-Border problem. What can we do to close off any loophole in that respect, to avoid implementing a tax and then being obliged to spend two or three years fixing the problem? As with the rent pressure zones, there are loopholes and people are getting around them. Landlords cannot increase rent by more than 4% so they are kicking tenants out to sell the house or revamp it for a family member to move into. They then do not do that and just get new tenants. Where we can see loopholes happening in advance, should we not close them off?

Deputy Josepha Madigan resumed the Chair.

Mr. Liam Berney: The question on the VAT rate referred to ending a subsidy, and that is what it is. There is no evidence to suggest there would be job losses in the sector. Employment in the sector has increased and will continue to increase significantly, though there is a Brexit risk associated with currency fluctuations. I do not look at the currency markets every day but there has been a slight improvement in the position of sterling recently. We can see no justification whatsoever for continuing the subsidy as it is simply profit-taking.

There was a question on earnings in child care. The €12 which I referenced is the average based on a survey we did and which I can supply to the Deputy. The Deputy is correct that there is an appallingly low level of income in that sector and the trade unions are doing their best to provide the benefits of collective bargaining to workers in the sector. We will continue to do that and through those efforts we can, hopefully, make a difference.

The Deputy is also correct about young people struggling to get onto the property ladder through access to finance and our members talk to us all the time about the issue. I am not sure what the answer is and there is no silver bullet for the problem but, in the past, local authorities provided housing finance to young people and couples who could not get mortgages through the private sector, and maybe we could look at that again. It is all about resources and in the past hour or so we have identified measures which would probably entail spending all the country's income. Unfortunately, we do not have it. We have to prioritise so that we can, in the small fiscal space we have, make a difference. As Dr. McDonnell said, however, there are major things on which we need to make a start, such as child care and the infrastructural deficit. I agree that parental leave should be shared and it should be for a family to decide how to use it, rather than it be given to one parent over the other.

Dr. Tom McDonnell: I completely agree on the point about shared leave. Having to take a career break is one of the most important factors in the gender pay gap. That this is not shared leave is essentially discriminatory and shows a mid-20th century attitude to child care responsibilities.

As has been pointed out, those working in the child care sector, almost all of whom are women, are extremely badly paid. The longer-term solution is to professionalise and systematise and to have the State provide the vast bulk of resources for the sector to ensure it becomes more formalised. The State must deal with child care in the same way that it deals with primary and secondary education, including in terms of budgeting.

On the issue of the research and development tax expenditures versus direct subsidies or funding of higher level institutes to carry out their own research, the OECD examined this issue in the case of Ireland. Among the issues it noted was that public research and development expenditure in Ireland is extremely low, as is research and development expenditure at national level, that is, public and private expenditure combined. It also noted that research and development tax expenditure is very costly and recommended that the direction of fiscal reform in this area be moved towards subsidies. We do not do enough of this in Ireland and we do not provide sufficient support to the fourth level sector in the area of research and development.

The concept of national innovation systems and an entrepreneurial state is all about the triple helix, as it is known, of higher level education, the state and the private sector working together and co-ordinating. Part of this could simply be the State taking equity stakes in high potential startups coming out of universities and research institutes. We spend two thirds of what the top performing countries spend in this area. This will lead to lower levels of productivity growth, a lower quality of life for everyone and less employment growth in the long run.

Another important aspect of this is the regional element because the universities not only in Dublin, but also in Cork, Limerick and Galway, are employment generation and innovation hubs in particular areas. We are obviously aware of the capital plans for the period until 2040. We view research and development as a form of capital. While it is important to keep research and development separate from capital, it achieves the same effects as capital and boosts productivity in the long run. That should be very much part of the plan.

While GDP growth is very high, it is meaningless at the moment. It is an accounting artefact for reasons that are well understood. The concept of modified domestic demand is a little bit better and the rate of growth under this measure has been strong in recent years, although not as strong as GDP growth.

As to whether welfare has been improving, deprivation rates are much higher than they were at the start of the crisis. In 2015, the deprivation rate was 25.5% of households - more than one quarter - and the at-risk of poverty rate stood at 16.9%. Professor John FitzGerald pointed this out.

Chairman: What is the at-risk of poverty rate?

Dr. Tom McDonnell: The latest figure, which was for 2015, is 16.9%. The deprivation rate is particularly stark. All of these figures exploded during the crisis and none of them has declined by much. They have improved a little, however.

Deputy Lisa Chambers: What was the deprivation rate before the recession?

Dr. Tom McDonnell: Deprivation has doubled. The deprivation rate stood at approximately 10% before the crash and now stands at approximately 25%, having peaked at over 30% in 2013. It remains very high, however, and indicates that many households are suffering, particularly those at the bottom of the income distribution scale. The unemployment crisis was the main driver of this. One of the things that will help a great deal will be employment growth. Employment is considerably lower than it was at the height of the boom.

Deputy Chambers is correct that we have not been investing in infrastructure in recent years and investment was disproportionately hit. It means that as employment grows, public transport infrastructure is creaking. Coming on a train from Maynooth into Dublin one finds it difficult to breathe. It is arguably unsafe. Because of house prices in Dublin, people are having to move out to Meath, Louth and Wicklow, which means longer commutes and spending more time away from their families, which is psychologically devastating and corrosive in the long run. These problems can be dealt with but it is the focus on things like infrastructure that will be very important.

I was asked about the great debate on increasing the standard rate versus reducing the USC. Of course, it depends on what reforms one makes to USC. There is only about €333 million. I made the point that increasing the standard rate cut-off point by €1,000 would mean a full-year cost of marginally over €200 million according to the Department of Finance's tax strategy group. One could reduce the 2.5% rate to 1.5% at €164 million, which would be approximately half the fiscal space. With a break-down of 2:1 tax and spend, one is talking about net space of a little over €100 million for taxes with, obviously, more arising from tax increases on excise that are likely to happen. What one can do for households is really about shaving at the edges. In our opinion, it is better to focus on things like child care. From a progressivity point of view, reducing the universal social charge probably would be preferable. As was pointed out, a lot of households will not benefit at all from an increase in the standard rate. Again, in terms of the tax burden *vis-à-vis* other countries, low-income workers in Ireland pay very low effective rates, but middle earners also pay very low effective rates compared with other high-income EU member states. It is kind of a rotten choice as I look at it.

I do not really have any solution in terms of the sugar tax. The soft drinks companies have already changed the sugar content. One cannot even buy some of the drinks that used to exist in 2016. If it is in fact true that aspartame is not as damaging as sugar, the tax is already doing what it is supposed to do. Excise is not technically supposed to bring in revenue, it is technically supposed to reduce bad behaviour and poor choices. If the yield ultimately goes to zero, it will supposedly have done its job. It is the same with alcohol and cigarettes.

Chairman: It is all about moderation.

Dr. Tom McDonnell: It is all about moderation, yes, so the State will always get a cut. If they are getting away with it by changing their behaviour in a way that is positive for human health, I am fine with that.

I do not have a particular macro solution on the issue of affordable housing. One of the things that will lead to more affordable housing in the long run is dealing with the mismatch between demand and supply. Simply building more houses will cause house prices to come down. They will come more into line with earnings for middle earners as that ratio improves, albeit I take the point about short-term contracts, which situation may improve as the labour market tightens. We still have not reached our potential with job vacancy rates remaining poor in Ireland compared with other countries. Workers will be able to negotiate better conditions as the market tightens and that will help. Those policies in terms of building houses and the labour market taking care of itself will both assist in what the member is talking about.

Introducing some fiscal instrument to support those households may or may not be a good idea. It would certainly be difficult to force banks to lend money to those households. Presumably, the banks' models are based on probability of capacity to pay over the next 25 to 30 years. Clearly, if they see a contract of six to 12 months, they would have an issue. I do not necessarily have a solution to that problem other than to say that building houses will drop rental costs as well. Part of the issue is that rental costs are so much higher than mortgage costs. People want to buy houses, which is simply fuelling house prices, which will continue to increase over the next two years at least, unfortunately, and probably at a double digit rate. The solution is getting the public and private sectors to build houses - the Deputy spoke about welfare - in areas close to urban centres, such as Dublin, Cork, Limerick and Galway city centres. That should be the focus in terms of public policy. I am not sure if I addressed every question.

Chairman: We have to move on because we have other witnesses waiting to come in as well. If the answers could be as brief as possible at this point we would be obliged. We have a lot to get through.

Deputy Pearse Doherty: Cuirim fáilte roimh an bheirt chuig an choiste. Sa gcéad dul síos, ó thaobh ICTU de in terms of the 9% VAT rate, after leaving the ploughing championships yesterday I travelled to Monaghan, where I stayed last night. The reason for that was that Dublin was booked out. I looked quickly at where Dublin stands today and it is booked out again. Well, it is not really booked out. If one is happy to pay €605 for the Fitzwilliam Hotel or €300 for Jury's one may get a bed, but those are the last beds available at this point in time. We will not, in our alternative budget, argue for a complete reduction of the 9% VAT rate. However, the portion in terms of hotel beds is not sustainable, given that we have the highest occupancy rates in Europe and that we have seen bed prices increase by around 6% last year. If we look at ICTU's proposal, the idea is to take the €500 million that it brings in. However, approximately €189 million of that relates to hotel beds. Does the witness think that there is more merit in going after the hotel beds as opposed to other parts of the sector, which includes food and beverages and so on? Other parts of that 9% are also not sustainable, for example, newspapers.

Mr. Liam Berney: The problem as we see it is that the VAT reduction has been used to increase profits. That is evidenced by what the Deputy has just said about the cost of hotel rooms today. It has been used to increase profits and has not been used in a way that has seen the development of the sector in any significant way. It was not necessary in order for the sector to develop. In terms of how the State spends its money on the resources it has, we do not believe that it is a necessary subsidy at this point in time and, therefore, we are arguing that the VAT rate should be normalised and the money should be used on the priorities that we have identified in our pre-budget submission around the issues of child care, infrastructure development, housing and homelessness. When one is in an emergency one has to take emergency measures. We have been saying this for a while; this is not the first pre-budget submission where we have talked about a reduction in the VAT rate. We have been saying this since before Brexit was a reality.

To respond to a point raised by Deputy Chambers, it is not as if the workers in the sector have benefitted from a reduced VAT rate. These employers refuse to engage in the joint labour committee system that is established for collective bargaining in that sector. Our approach was described as being aggressive. It is not aggressive. There is no partnership work in this sector at all. It is being used purely to profit take, and we see no justification for its continuance.

Deputy Pearse Doherty: Dr. McDonnell spoke about the small amount of fiscal space that exists and about how the commission is calculating it. I do not want to go into the debate around how the one-size-fits-all approach does not fit Ireland. However, not only have the commission reduced our net fiscal space through their method of calculation, but the Department, through the Government, is reducing it voluntarily through this margin of convergence. There has been some debate on hidden fiscal space, that is, the hidden fiscal space that will undoubtedly present itself on the eve of the budget, in that the €150 million of the margin of convergence will no longer be used and we presumably will be able to spend that money. What is NERI's view on the margin of convergence? Should we be setting aside another €150 million that we will not use despite the crises in certain sectors, not least housing and health?

Dr. Tom McDonnell: The Commission recently made two decisions - one active, one inactive - about reducing our fiscal space. One was on how to calculate the structural position in the economy, which costs us more than €1 billion in fiscal space per year. The other is on not using the 26% growth figure. While changing how that is calculated was probably a good decision, it was a unilateral one.

It would be safe to use the €150 million. Such are the pressures on child care and housing that it would be foolish not to do so. Given the losses in terms of forgoing reduced interest costs versus the gains in terms of child care, education and so on, it speaks to using that money.

A point was made about how it would be better to save the money in the rainy day fund. Presumably, that fund will go into an account somewhere and generate interest. The alternative is to invest it in the economy whereby it will generate jobs, tax revenue and, in the long term, a stronger and more robust society. This is not about the profligate spending of money. Rather, it is about investing. The rainy day fund will be going into a low-interest account somewhere or it will be invested in shares in companies or pension funds around the world. Either way, the money is invested or saved, so I am not sure that using the fund is necessarily the best choice. That said, I agree with counter-cyclical fiscal policy. Hence my points on tax cuts. From a macro or fiscal hawk perspective, I would not be overly concerned if that €150 million was spent.

Deputy Pearse Doherty: The Irish Fiscal Advisory Council, IFAC, has advised the committee that the €150 million is available and we would still be within the fiscal rules if we used it.

I wish to move on to what is something of a fake debate between Fianna Fáil and Fine Gael. Let us leave the party political stuff aside, though, and deal with the policy issue, which is how best to give €200 million in tax cuts. We have learned the lessons of the past about the herd mentality or have we? Newspapers are holding conferences that allow these two to bat it out when there are people dying on our streets and hundreds of people are on hospital trolleys. Fake tears will be shed in sympathy for all of these issues while they continue to decide how best to give €200 million in tax cuts even though they know fine well that the pot is a certain amount of money.

The Irish Tax Institute, which published an excellent report in terms of producing statistics, will appear before us and tell us clearly that our marginal tax rates are a deterrent to employment. I would love to see whether there is any economic evidence to support that. The institute will tell us that the marginal tax rate kicks in too low and we are out of kilter with the rest of Europe. Presumably, it means the 49% rate and not the 52% rate when it refers to marginal tax. Am I correct in presuming that the marginal tax rate is the last tax rate?

Dr. Tom McDonnell: Yes.

Deputy Pearse Doherty: We compare our marginal tax rate, which is the middle tax rate, with other countries' higher tax rates. We can abuse statistics, so I want to delve into NERI's own statistics to see whether it is also guilty of that to present its narrative.

Dr. Tom McDonnell: Sure.

Deputy Pearse Doherty: Let us consider the comparison of the total tax wedge in 2016. Dr. McDonnell can correct me if I am wrong. Is the total tax wedge the cost to an employer of employing an individual?

Dr. Tom McDonnell: Does the Deputy mean the OECD's statistics?

Deputy Pearse Doherty: Yes. It is based on the OECD statistics. I assume that NERI has taken the average earnings in each of the 15 western European EU countries.

Dr. Tom McDonnell: That is what the OECD has done.

Deputy Pearse Doherty: It has converted those figures to dollars.

Dr. Tom McDonnell: On a purchasing power parity, PPP, basis.

Deputy Pearse Doherty: It is all equal. Is that the best way to equalise this?

Dr. Tom McDonnell: According to the OECD.

Deputy Pearse Doherty: If an employer wants to employ an individual in Belgium on the average Belgian wage, how does that compare with the situation in Ireland? According to the data being presented here, how much would an employer have to pay to pay the average?

Dr. Tom McDonnell: According to the OECD, in Belgium the total tax wedge as a percentage of total labour cost for a single person on average earnings is 54%.

Deputy Pearse Doherty: What does that mean in layman's terms?

Dr. Tom McDonnell: What they would call income tax, employee social security contributions and employer social security contributions are added together and calculated as a percentage. Those three as a percentage of labour costs amount to 54%.

Deputy Pearse Doherty: Okay. In Ireland's case, it would be 27%.

Dr. Tom McDonnell: According to the OECD, it is 27.1%. This is for 2015.

Deputy Pearse Doherty: Out of the 15 countries, Ireland would have the lowest tax wedge for the average earnings.

Dr. Tom McDonnell: Evidently.

Deputy Pearse Doherty: For an employer looking at it and saying he or she wants to pay an employee the average wage in the country, he or she will have to pay net pay, tax and the employer PRSI. In Belgium, that would cost him or her €74,000, or €74,913? Is that correct?

Dr. Tom McDonnell: No. They are saying that the total labour costs are €74,000.

Deputy Pearse Doherty: What makes up the labour costs? Is that not employer's PRSI, employee's PRSI, income tax and the wage?

Dr. Tom McDonnell: It is the wage plus employer PRSI, effectively.

Deputy Pearse Doherty: Therefore, the cost to the employer of paying an average wage in Belgium would be that amount.

Dr. Tom McDonnell: On a US dollar purchasing power parity, PPP, basis.

Deputy Pearse Doherty: In Ireland-----

Dr. Tom McDonnell: Obviously, different countries have different costs.

Chairman: I know the Deputy is trying to elucidate information but I would like to move this along.

Deputy Pearse Doherty: I am sorry but I am very interested in these answers.

Chairman: I appreciate that but I ask the Deputy to get to the questions.

Deputy Pearse Doherty: These are the questions. The questions are about how it appears in the data as presented that, in terms of the cost of employing someone on an average wage in the 15 countries, only Greece and Portugal would have lesser costs in terms of labour costs. This is my point. There is a narrative that everyone believes, which is that high marginal tax rates and particularly those we have in Ireland, are a cost on employment, a deterrent and all the rest. However, it appears from the OECD data, if we take average earnings, that Ireland has the second lowest cost in terms of tax wedge on average earnings out of the EU 15.

Dr. Tom McDonnell: The OECD data would suggest that. Given the way income tax systems are structured in all the different countries, however, it is important to note that the data is taking a static person. It is a single person, of course, it is not a family, and it is a person on a particular wage. To get a fuller picture, and we are publishing a paper on this in advance of the budget, one has to look at the entire distribution. That does not necessarily imply that Ireland is bottom across the distribution. It simply refers to that static point, which is the one they use, which is the 100%. However, they also do it for 50%, 250% and 150%. They do it for families versus single persons. They do it to include children. Ireland's position will move up and down based upon that.

Deputy Pearse Doherty: Dr. McDonnell has provided us with graphs on it. If we take the a one-earner married couple with two children, Ireland falls below the UK as well as the EU average in terms of the tax wedge and labour costs. This is not only at 100% but right up to 250%.

Dr. Tom McDonnell: Is this the tax wedge and labour costs for a single earner?

Deputy Pearse Doherty: This is for a one-earner married couple with two children.

Dr. Tom McDonnell: Yes, but partially what is happening there is that there are family supports which the OECD is taking into account in terms of that particular chart, which distorts it.

We will have the paper ready in approximately two weeks' time, which we will disseminate to the committee.

Chairman: In advance of the budget?

Dr. Tom McDonnell: In advance of the budget. It will be the week before it. The arguments and the articulation will flow within that document. The broader point is that the danger with using single graphs is that they are a static point and the arguments around it are important. What the OECD is saying with regard to fiscal costs and the fiscal supports that go to families is that Ireland is quite generous in how it treats families and single people, particularly families, in its budgetary policy. It is clear that when we talk about the tax rate, we are including things like employer PRSI. That would make it look better for the household than it really is. We have said that when it comes to taxes, and when social security contributions are excluded, the picture changes very much. When it is purely about the employee contribution, we move from 11th to seventh among the high-income EU countries. Perhaps the employee contribution is what is relevant in terms of take-home pay.

Deputy Pearse Doherty: I have two final short questions, the first of which relates to the smoothing effect in terms of capital expenditure. We could provide for €200 million in tax cuts through rate increases or a reduction of half a percentage point in the USC rate, which would give someone on an average income approximately €1 a week. However, that figure could be quadrupled if we used capital expenditure for housing.

Dr. Tom McDonnell: If €100 million is spent on capital expenditure in the first year, it will take up €25 million but it will have used up the same amount of fiscal space by the fourth year.

Deputy Pearse Doherty: Yes.

Dr. Tom McDonnell: It increases incrementally, so it is €25 million, €50 million, €75 million-----

Deputy Pearse Doherty: If the Government decided not to pursue €200 million in tax cuts, it could decide to invest €800 million in social housing this year and that would be spread out over four years.

Dr. Tom McDonnell: Yes, essentially. It depends on what the level of capital spending was in previous years. It does not necessarily work out as cleanly as that. As a broad principle, that is a good way to describe it. Essentially, €800 million in tax cuts would have an €800 million fiscal cost in the first full year. A similar approach to capital spending would take up €200 million in the first year. That would be €400 million of fiscal space - €200 million in each year. That would involve a gross figure of €600 million by the third year and €800 million by the fourth year. This would essentially involve taking €200 million out of budget 2018, €200 million out of budget 2019 and-----

Deputy Pearse Doherty: Of course. The fiscal space is a lot bigger in those years.

Dr. Tom McDonnell: It is.

Deputy Pearse Doherty: That is why it would be prudent to-----

Dr. Tom McDonnell: One of the misunderstandings about fiscal space is that it is actually not €500 million or €350 million. The fiscal space is actually the size of one's economy, how much tax one is willing to impose and what one wants to spend. It is actually the entirety. We often think about small increments, but it must be borne in mind that €350 million is 0.5% of public spending.

Deputy Pearse Doherty: I have a final question. If I were to look for evidence that is based on research, what would be the best type of research to show me that marginal tax rates in this State are a deterrent to employment and, in the opinion of policy decision-makers like Dr. McDonnell, should therefore be reduced? I wish to clarify that I disagree completely with this theory. When representatives of the ESRI appeared before this committee last year, they said there was no such evidence at all. They suggested that child care costs were a greater deterrent to employment than marginal tax rates.

Dr. Tom McDonnell: Yes.

Deputy Pearse Doherty: Let us test this. Is there any evidence to suggest that the tax rates we have at this point in time are a deterrent to employment?

Dr. Tom McDonnell: There has been a great deal of research from the United States on this issue. It is probably fruitless to look at cross-country comparisons because the marginal tax rate is one of thousands of factors that affect employment rates within countries. It is more useful to look at a single country over time. In the United States, there have been fairly dramatic increases and decreases in the marginal tax rate over more than a century. Over that time, there has been no relationship between marginal tax rates and economic growth or employment growth. In fact, the golden era of the United States between 1945 and 1973 was the period when marginal tax rates were at their highest. That is a fact, but it does not mean there is a causative relationship. The literature suggests that whether a country has a tax burden of 20%, as it is in the United States, or of 50% to 55%, as it is in Denmark, makes very little overall difference to economic growth in the long run. While the composition is obviously important, other factors, including the productivity of the economy, are much more relevant. Therefore, our emphasis is on things like child care, education, infrastructure and research and development, which are the things that will generate long-run economic growth and the accruals in well-being and quality of life that will follow. The marginal tax rate kicks in at a very low point in Ireland. That is correct. It is just a fact. However, the effective rate is not high. It is low because we have a very generous system of tax credits.

Deputy Pearse Doherty: Dr. O'Donnell might just correct me here. Is the marginal tax rate 49% or is it the 52% rate? Britain, for example, has a number of rates.

Dr. Tom McDonnell: It does but it is different. For an employee, it is 49%.

Deputy Pearse Doherty: If one is over €70,000, one's USC will be 8%.

Dr. Tom McDonnell: Sure, yes. Ultimately, the marginal rate for self-employed above €100,000 is the highest rate. Personally, I find the debate on marginal tax rates to be somewhat problematic. The effective tax rate is much more relevant. From what I have seen, what is more important is effective tax rates at the bottom of the income distribution where there is a choice about labour market entry at all. I have not seen the evidence about whether I will work if my marginal tax rate is 47% or 48% and I am on €80,000 or €90,000. People tend to talk about a guy in a pub who said he would not move back to Ireland because of this. I have not seen econometric evidence that suggests it is relevant although I would be very interested in seeing it.

Again, cross-country comparisons are extremely problematic because even the 28 member states of the EU are very different from each other. The only way one can do any kind of analysis is of a single country over time where the institutional structure and the structure of the labour force are similar. One could do state by state where relevant. We have seen very good research on the minimum wage, for example. That is the level at which one has to do it or one will otherwise fail the like-with-like test required in any scientific analysis. As a final point, I note that while I say the marginal tax rate is not hugely important, it would be wrong to say it is of no relevance at all. Clearly, all taxes have some impact on the economy.

Chairman: Deputy Calleary has five minutes. Does Deputy Broughan want to ask anything before the witnesses for this session leave?

Deputy Thomas P. Broughan: I am okay.

Chairman: I just wanted to check. Deputy Calleary is the last questioner for these witnesses. We will then take a break.

Deputy Dara Calleary: I thank both witnesses. Dr. McDonnell said something in the early stage of his presentation about one of the bigger issues facing the economy, namely, the notion of interest rate increases. In his engagement with Deputy Lahart, Dr. McDonnell spoke about families being under pressure and on the verge of poverty. Deputy Lahart set out the experience we have all had. How significant would a 1% increase in interest rates next year be on the figures Dr. McDonnell quoted for families at risk of poverty and on our general consumption trends and patterns?

I agree absolutely on child care. A child can be four and a half or five when he or she moves to primary school but the education system and the way we value education is entirely different. We need to do a great deal more. If we implement a system of full payment and justify payment for child care workers in recognition of their degrees, will Mr. Berney's ICTU not then lob in a relativity claim for national school teachers to keep them separate? We will then end up in this spiral we always do where we are watching over our shoulders. I do not mean that in a smart aleck way, but when one looks at costings, one must look at all the knock-on effects.

On a similar note, Mr. Berney spoke about the public service pay agreement. We have major difficulties at the moment in our health service in nursing, physiotherapy and speech and language therapy because we cannot fill vacancies. The nature of our agreements are that everyone gets the same increase and we do not have the flexibility required at local management level to redesign contracts. It is not even the pay element of contracts, it is also career breaks and so on. There are entire nursing classes going to the UK after getting a degree here because our system does not allow career breaks or recognition of past work. Is there not a point to be made in this regard? Yes, there is the old-style agreement. However, we need greater flexibility to respond to challenges. Health care is the obvious one at present. There is so much pressure.

On the VAT issue, Deputy Pearse Doherty is correct. We have been forced to spend weekends in Dublin recently and the gouging of Dublin hotel prices that is going on is a disgrace. There has been a drop of 140,000 in the number of UK visitors. The west coast tourism market in particular depends on UK visitors. The fall in numbers cannot just be dismissed as a matter of having to watch sterling or other currencies. It is a very real figure. Many areas depend on that market. Even if it is not profit-taking, it is the market that keeps businesses and employment going. That is the argument on the VAT issue. Perhaps we need to separate it out between accommodation and food, as Deputy Pearse Doherty suggested. There may be time to have a discussion about regionalising tax rates on consumption. Dr. McDonnell pointed out that consumption taxes here are actually incredibly high. Perhaps we should stop looking at the entire island and start looking at regions that need a particular boost. This ties in with the discussion we were having yesterday about the sustainability of regional economies.

ICTU wants a housing emergency declared. We all know what we are dealing with on a daily basis. If we declare a housing emergency in the morning, what will that actually mean? The difficulty is that we need to build houses. What are we going to do in the 18 or so months it will take to build any number of houses to get people off our streets?

Mr. Liam Berney: The Deputy made a point about a so-called habit of the trade union movement of having knock-on claims arising. That is a bit of a myth, frankly. We pioneered reforms in the health service whereby health care assistants were introduced and there were no repercussive claims. If he takes the time to look at the submission ICTU made to the Joint Committee on the Future of Healthcare, he will see that we place major emphasis on the need for reform in the health sector and the need for portability of skills. There are things nurses currently do which other grades could perhaps do. There are things doctors do that may be more appropriate to nurses. There is a whole process of organisational reform that could happen within the health service to address some of the problems to which the Deputy referred. He talked about nurses leaving *en masse* to go to the UK. There is an argument that we are not providing sufficient university places to train nurses. If we are currently providing 1,000 places a year, perhaps what the system needs is 2,000. It might not be simply that there are more attractive health systems abroad.

Deputy Dara Calleary: There are 2,000 nursing vacancies in Ireland at present.

Mr. Liam Berney: My point is that we need to take a holistic approach to this issue. There is a range of solutions, including reforms to the health service such as those I have talked about, to give nurses more responsibility and do some of the things to which the Deputy referred. It is also necessary to look at how we train nurses and to consider whether we are training enough nurses and doctors to respond to the needs of the health service. The public service pay agreement has charged the Public Service Pay Commission with looking at the retention and recruitment issue in the health service in order to identify the bottlenecks and consider how the problems can be resolved. That work is going to be done as a priority and we should have a report on it before the end of the year. That will address some of the issues raised by the Deputy. The unions will make submission in the normal way to the commission. I look forward to that report.

On the question of the VAT rate, the simple point we are trying to make is that we currently provide a very generous VAT rate to the hospitality sector. We have a crisis in other parts of our economy, where that money could be better spent. We strongly believe that the money provided through that subsidy could be better spent elsewhere. We do not necessarily see the risk. If we increased the VAT rate tomorrow, I do not see evidence that hotels and hospitality venues would close down across the west of Ireland. While there has been a drop in visitor numbers from the UK, the numbers from the United States have increased in the same period with one group replacing the other. That is according to statistics from the tourism industry. It was on "Morning Ireland" just the other morning. In the crisis that we are currently facing across a lot of our public services, there are better uses for the money that is being provided to the hospitality sector through the subsidy of the lower VAT rate.

Chairman: Would Mr. Berney not agree that it is an incentive or stimulus, particularly with sterling weakened at the moment and in terms of Brexit?

Mr. Liam Berney: If it were being used to reduce hotel room rates or prices in the sector for potential visitors, it might be possible to make that argument but there is no evidence of that.

Chairman: I thank Mr. Berney. Are there no further questions?

Deputy Dara Calleary: Would Dr. McDonnell address my question about interest rates?

Dr. Tom McDonnell: While I do not have my figures to hand, the Deputy is right to make the point about interest rates. It would have a very damaging effect on the Irish economy. The Department of Finance stability programme update in April or May gave an estimate as to how much a 1% increase would cost in terms of jobs and economic growth. Given our very high private debt levels, an increase in interest rates would be a straight-up negative shock to the Irish economy, in my view, although it would perhaps bring some benefits to the banks. There is nothing we can do about it, unfortunately. The expectation is that interest rates will start to increase in 2019. One thing that might work against this is if Brexit has a more devastating effect than is anticipated. That might dampen growth and employment growth in the euro area, leading the ECB to postpone an interest rate increase. In that case, however, we are wishing for one bad thing in order to avoid another bad thing. Interest rates are going to go up.

There is no doubt that the Irish economy has been benefitting over the last few years from low oil prices and low interest rates. They have supported the Irish economy and that support is going to go away. The high rates of growth we are seeing at the moment should be understood as a temporary phenomenon. We should not get carried away with thinking that we have moved completely past the crisis. We do still have that burden in terms of households and businesses. That is all the more reason to be prudent now. To the extent that we are talking about fiscal policy, we should focus on things that will boost productivity rather than boosting income flows in the short term. That would be my perspective.

Deputy Calleary made an interesting point about regionalisation of VAT. It might then be prudent to have a system of regional authorities, perhaps not the 30 or so local authorities but a smaller number, such as Dublin, Cork, Limerick, Galway and two or three others, with a certain degree of fiscal power over commercial rates, property tax and even VAT. They might be allowed to set their own local economic plans. I suppose it would empower county councillors to have a proper executive and legislature. Without having that structure in place, however, regional VAT rates could be arbitrary. Would we be talking about special zones for particular counties? We could have issues in the adjoining county if, for example, there was a lower VAT rate in Longford than in Westmeath. Would Dublin have one rate and the rest of the country another? That could just push people out into Kildare and Meath for their shopping. We need to be very careful about this. If different parts of the country had different fiscal powers in different areas, that would be one thing, but having regional VAT rates could have unintended consequences. However, I am certainly cognisant that the economy outside the M50 is not performing as strongly as is the case in Dublin. It should be noted that when a recovery happens, it tends to happen in the dominant economic zones first and then tends to spread out. We have not fully seen that yet but we are seeing unemployment rates, for example, falling across the board now. That should continue for another year and a half. It does not fully answer the Deputy's question about regionalising VAT. However, it is an interesting idea and over the next 12 or 18 months we intend looking at regionalisation of fiscal policy, for example, to see if it is viable. However, I do not have the answer yet.

Chairman: I would like to thank the witnesses and-----

Deputy Thomas P. Broughan: May I ask-----

Chairman: I asked the Deputy earlier and he said “No”.

Deputy Thomas P. Broughan: Further to what Dr. McDonnell just said, last week Fingal County Council increased its local property tax by reducing the 15% discount to 10%. That is an example of a local authority that increased a tax.

I apologise for missing Dr. McDonnell’s presentation. He mentioned the huge tax expenditure on the 9% rate of VAT in the hospitality sector. In light of the earlier work NERI has done in this area, do any other tax expenditures scream out for us to close off? My colleagues may have asked this earlier.

Dr. Tom McDonnell: Mr. Liam Berney is pointing me to a few examples. Ireland is particularly generous with some of the reliefs associated with inheritance tax. Obviously, it is not very popular, but there is very different treatment of different assets. Farming and business assets are given much easier treatment than other types of assets. Perhaps blending the reliefs might be a better solution.

We are also concerned that 80% of the pension tax relief goes to the top 20% of income earners. Obviously, it is extremely regressive and it is not necessarily achieving its goal of ensuring that everybody has an adequate pension in old age, which presumably is the official goal at least. To my mind, it would be better to use that money to increase the basic pension for everyone in the long term. That would be one example.

Broadly speaking, we have a fairly jaundiced view of most tax expenditures. Essentially, they are hidden subsidies to particular sectors. Often they outlive their usefulness. We believe that all tax expenditures should have sunset clauses attached and that they should be reviewed automatically every three years at least. This does not mean that they should be abolished. Some tax expenditures serve a very useful function. The research and development tax expenditure was mentioned earlier. I know some people have criticised it, but providing incentives to engage in research and development is a good thing. Other examples could be given of positive tax expenditures. By and large, we see them as leading to misallocation of resources in the economy. They tend to be regressive hidden spending that people do not see. We would like a fundamental review of the entire-----

Deputy Thomas P. Broughan: Is Dr. McDonnell happy with the data? Our staff have prepared an incredible list of different expenditures. Is the €5.5 billion that is talked about the actual figure?

Dr. Tom McDonnell: There are different calculations. Some people consider tax credits to be tax expenditure. I personally do not because I see it as a core part of the income tax system. I regard tax expenditures as things that certain segments of society may have a capacity to exploit or as providing reliefs in respect of certain types of activity. I have not looked at the exact data. A couple of years ago a former colleague of mine on the Commission on Taxation did a lot of good work in that area. Many of the tax expenditures have already been closed off. There are potential gains in that area, but I would take a more surgical approach rather than seeking to get rid of all of them automatically. Again, a core point is that there should always be a sunset clause. When we produce public finance estimates every year for all the different areas of spending such as health and education, the tax expenditures, for example, should automatically be part of that because they are effectively subsidies in the same way that the basic pension or pension tax relief is a transfer to someone.

Chairman: I thank the witnesses, Dr. McDonnell and Mr. Berney, for coming today. We really appreciate the time they have taken to give to the committee and their presentations and thank them for having answered the questions so comprehensively. We will now suspend for a few minutes to allow the next group of witnesses from the Irish Tax Institute to take their seats.

Sitting suspended at 11.16 a.m. and resumed at 11.19 a.m.

Chairman: Before we begin, I ask the witnesses to turn off their mobile phones. The interference from mobile phones affects the sound quality and transmission of the meeting. I welcome Ms Olivia Buckley, communications director of the Irish Tax Institute. With her is Ms Cora O'Brien, policy director. They are listed here as "Mr. Buckley" and "Mr. O'Brien", which is incorrect. It is nice to meet them both. I thank them for coming in and making themselves available. The institute's document, A Future Tax Strategy to Grow Irish Indigenous Exports, has been circulated to the committee in advance of the meeting. We will take that as read but the Irish Tax Institute has been asked to deal in its presentation with Irish tax strategy.

Before we hear the Irish Tax Institute's opening statement, I draw the witnesses' attention to the position on privilege. Witnesses are protected by absolute privilege in respect of their evidence to the committee. However, if they are directed by the committee to cease giving evidence on a particular matter and they continue to do so, they are entitled thereafter only to a qualified privilege in respect of their evidence. They are directed that only evidence connected with the subject matter of these proceedings is to be given and they are asked to respect the parliamentary practice to the effect that, where possible, they should not criticise or make charges against any person or entity by name or in such a way as to make him, her or it identifiable.

Members are reminded of the long-standing parliamentary practice to the effect that they should not comment on, criticise or make charges against a person outside the Houses or an official either by name or in such a way as to make him or her identifiable.

Ms Buckley has been allocated 15 minutes, if she needs it, to make her opening statement.

Ms Olivia Buckley: I will share that time with my colleague, Ms Cora O'Brien, if that is okay. I thank the Chairman and members for the invitation to appear before the committee and the opportunity to outline our views on a future tax strategy for the Irish indigenous sector aimed at strengthening and growing the country's tax base while building resilience into our economic model. There are important factors against which we present this proposal: an increasing demand for expenditure on services to meet the needs of an expanding and ageing population; external political and economic risks that could impact Ireland's small economy, as highlighted by many international bodies as well as the Departments of Finance and the Taoiseach in their national risk assessment report; a highly concentrated tax base with very little buffering in the face of any unforeseen global or domestic disruptions; and a significant reliance on foreign-owned multinationals.

Foreign-owned multinationals account for 80% of Ireland's corporate tax base, and US multinationals account for 70% of employment in IDA-supported companies. The foreign-dominated pharmaceutical sector on its own accounts for almost 40% of the value of manufacturing production in Ireland. We have an Irish economy that is approximately one third smaller when the main effects of multinational activity are removed, using the new GNI* economic measurement as opposed to GDP. Our debt ratio, using the GNI* measurement, is the fourth highest in the OECD, according to the Irish Fiscal Advisory Council last week.

To deal with this backdrop of risks and vulnerabilities we need a diversified and resilient tax base that is capable of withstanding shocks. However, our current base has become increasingly reliant on taxes on labour and on corporation tax paid by foreign multinationals, as the committee can see in the diagram we have provided. Several international bodies have highlighted these dependencies to us. The European Commission country report on Ireland this year said, "The stability of tax revenues in the medium term is a concern for public finances ... [T]he increasing reliance on buoyant corporate tax receipts to finance permanent increases in current expenditure is a concern." It stressed that "Ireland is a small and ... open economy [and] its public finances remain vulnerable to external shocks and changes in economic outlook". The IMF has also been instructive regarding what Ireland must do. It recommends that our policies focus on rebuilding fiscal buffers and strengthening resilience. It said measures to strengthen human capital and reinforce competitiveness, particularly for domestic enterprises, are key to supporting sustained growth and reducing regional disparities.

While Ireland cannot control external shocks, what it can control, it must. The Government's report on Irish trade, Ireland Connected, stresses that the key to sustaining jobs and incomes is Ireland's ability to succeed in international markets. Our national plans have placed a firm focus on exports as key to our economic growth. New EU free trade agreements, an expanding eurozone economy and rapid growth in services as a share of world trade represent real opportunities for Ireland. However, we need tax policy and tax administration changes if we are to realise the plan. While Ireland's exporting story has been one of success, there is an acceptance that it is highly dependent on exports from foreign companies and that our indigenous export model is skewed in many respects. Although there are "superstar" Irish performers that are globally focused, Irish manufacturing companies remain narrowly concentrated.

In parallel with our high-performing FDI sector, Ireland now needs an innovative, export-led indigenous sector. We rightly have a comprehensive roadmap for FDI. However, a detailed and long-term roadmap is also urgently needed for the indigenous sector. The thorough and strategic approach that we have adopted on FDI must be applied for the benefit of Irish indigenous companies and entrepreneurs if we are not just to protect our tax base but to grow it.

Ms Cora O'Brien: Before I commence I wish to say that this is the piece of work we did and it is effectively the strategy we are proposing for the indigenous sector. This is the Government's strategy for tax and foreign direct investment, FDI. Fundamentally, we are saying that we want to see an equivalent of that for the Irish indigenous sector and this is our suggestion for what that might look like.

Detailed analysis from the Irish Tax Institute's new report highlights a range of mismatches in tax policy that are hindering efforts to grasp global trade opportunities and meet the challenges Ireland faces. While our 12.5% corporation tax rate is valued by many Irish businesses, we have a pattern of sustained high rates across a range of other taxes that are critical for growth and we have some tax reliefs that are either not available or not accessible to Irish SMEs. The right tools, supported by the right policies are essential. This urgent need to change tax policy is reflected in independent research we did with Behaviour & Attitudes where 84% of the companies to whom it spoke believe that tax policies relating to the future of the Irish indigenous sector need to be addressed in this year's budget. We must take a strategically-focused approach to Irish business and address barriers in the tax environment. Policies that focus on the country's access to highly-skilled talent, expertise, innovation and research and development, as well as capital investment and finance, are critical to the plan.

The first challenge for releasing the necessary dynamism that the IMF has stressed as critical, is the high capital tax environment. We know that Irish SMEs are more reliant on bank finance than those in other EU member states and that they need to diversify into other equity sources of finance. The Government has recognised the need to develop appropriate alternative funding mechanisms to support companies over the coming years. This makes the capital gains tax environment critical. However, the high capital gains tax rate is restricting external investment in Irish businesses and creating "reluctant" business owners who may hold onto businesses beyond the point where they have the capacity to grow them to the scale required in a new global exporting environment. Unless addressed, that will hinder the structural changes needed for a new and more resilient export model, including the national ambition to "increase the number of our Irish-owned companies of scale by 30%". In fact, the 33% CGT rate is the fourth highest rate in the OECD and ten percentage points above the median OECD CGT rate. It is also high when one compares it with Germany, which has a rate of 25%, and also an excellent record of business investment.

We do have a targeted "entrepreneur relief" which reduces the high CGT burden on business sales to a limited degree and is especially important given the serious competition from the UK regime, as highlighted earlier this month by the UK Institute for Fiscal Studies. Ireland's CGT regime is not competitive when compared with the UK and the entrepreneur relief which should mitigate our high rates locks out important angel investors, who are willing to invest money, experience and industry expertise in ambitious young companies. Business angel investment in Ireland is low compared with other countries such as the UK, Spain, France, Germany and Sweden, which are doing this well.

There has been much talk about our personal tax regime in the context of an export strategy. We need the best human capital and talent to build management expertise, innovation and research and development capability and to drive export-led expansion. However, challenges abound here too. In addition to having high personal tax rates, Ireland does not currently have a workable share option scheme that allows SMEs to attract and reward highly skilled and hard-found talented employees. SMEs must compete with larger companies for talent and 38% of them do not believe they can compete with the larger companies when recruiting for the best candidate. A new share option scheme would help them attract the talent they need.

On research and development and innovation, which is the second pillar, in the work and research carried out, especially post-Brexit, innovation and new product development are deemed essential to export growth. Only 1% of small firms and 16% of medium firms consider themselves to be research and development active, which is a low number in the context of our national ambitions. Innovation in younger companies has flat-lined since 2009. The 1% figure is a concern in the context of IMF findings which show that SMEs are the drivers of change in innovation. Ireland has an attractive R&D tax credit regime, but some administration barriers are weighing on its success in terms of the low take-up among SMEs. Irish Tax Institute research shows that 75% of companies are aware of the R&D tax credit and 20% have availed of it. However, of those who availed of it, almost half said that the process was difficult to prepare for and administer and only 35% of companies surveyed said that they intend to use it in the next 18 months, although that would rise to 62% if there was more clarity around the criteria for qualification.

In summary, we appreciate that fiscal constraints limit the funds available in this year's budget and that not all the essential policy changes can be addressed this year. In light of the urgency of Brexit and the need to capture markets we would like to see some changes that might assist in the talent and innovation area. These include a less punitive capital tax environment; a workable share options regime; some reduction in the personal tax burden and; and, an improvement to the foreign earnings deduction regime.

In the longer term, which in some ways is almost more important, we would like to see the announcement of a new tax roadmap for the Irish indigenous sector, alongside the roadmap for FDI so that we give Ireland the best possible growth opportunity into the future.

Chairman: I thank Ms O'Brien and Ms Buckley for their presentations. I have just one question. We should bear in mind that Ireland is a small open economy and, as was outlined in their opening statement, it has vulnerabilities because of that. It was also mentioned that in order to maximise our economic output, in effect, this country must be involved globally in an integrative way. How can this country insulate itself if there is a hard Brexit and a resultant reduction in our integration with the UK?

Ms Cora O'Brien: We see Brexit as everybody does, namely, as one of the challenges and in large part it is why we decided to undertake the research for this report because it is about trying to address vulnerabilities and create a sustainable tax base. That will not happen overnight. Some parts of the indigenous Irish sector are very exposed to Brexit which means they need to expand the markets they are selling into and it also means that they need help in terms of innovating with new products so that they can expand the range of products they have. We are trying to get a bit more balance between the 80% corporate tax from the FDI sector and 20% corporate tax from the indigenous sector with a medium to longer term plan that drives the sector that is most exposed to Brexit and gives it some support. We think that is the priority for the next few years.

Chairman: The first questioner is Deputy Lisa Chambers. She has five minutes. Then we will have Deputy Calleary, Deputy Broughan, Deputy Eamon Ryan and Deputy Pearse Doherty.

Deputy Lisa Chambers: I thank Ms O'Brien and Ms Buckley for their presentations. I am pleased they are focusing on the SME sector because it is our largest employer and very often it gets left behind because we tend to focus on and go after the bigger multinationals as though they are a fix-all for everything. We have left indigenous businesses behind and to fend for themselves for the most part, which they have done very successfully. Reference was made to a share option scheme. Could the witnesses expand on that a little further in terms of how it would work and the costing of it? It will always be difficult for the SME sector to compete with the large multinationals in attracting the best talent. Do they believe a share option scheme would do a lot to assist in that regard or is there is something else we could do to help the SME sector?

A debate is ongoing currently in terms of personal taxation. On the one hand there is the suggestion that we should not lower taxes at all because we have increasing pressures in terms of spending on public services and the question is whether it is the right time to do that. What is the view of the witnesses on that? If we are going to reduce personal taxation, the question is whether we look at the USC or the tax bands. What do the witnesses consider to be the fairest and most progressive way of doing that? I am conscious that if we reduce, for example, the 5% rate of USC to 4.5% we will hit 1.3 million people. If we address the tax bands and leave the threshold for the higher rate at €33,000 and one is earning €33,500 or less there is no impact. What is the fairest way to level those reductions? The Irish Tax Institute appears to be arguing that the tax base is not broad enough. Is that correct? If it is not broad enough, how can it be broadened? A broader tax base would be a safer option as it would enable us to be more prepared for potential shocks.

What is the Irish Tax Institute's view on the corporate tax rate? Is it economically and fiscally sustainable to be so dependent on receipts from a small number of multinational companies? What recommendations would the institute make to manage volatility in this area?

What is the Irish Tax Institute's view on the proposal to merge the universal social charge with PRSI?

Ms Olivia Buckley: I will address the Deputy's question on the tax base as it provided the backdrop to our research in which we focused strongly on the sources of tax. In budget after budget, we have debate and conflict surrounding the small amount of money available to respond to major demands for increases in expenditure on capital, social services, housing and health. We also have a small amount available for tax cuts to relieve people of the burden of taxation on labour. We need to focus on a plan for growing the tax base. In a country with a population of 4.7 million, there is only limited scope for broadening the tax base from domestic sources. Some 40% of Exchequer returns come from labour, while a further €10 billion is collected from PRSI, although technically PRSI does not qualify as a tax. These are significant sums which are collected on the back of labour and work. VAT generates another substantial amount of State income.

Unless we want to increase taxes, which is a very difficult decision, the only way to broaden the tax base is to achieve growth outside the country by taking advantage of external opportunities. One of the areas on which our study focused was services, the largest area of growth in world trade and an area in which Ireland is particularly good. Trade in services is growing at 10%. While we have the potential to take advantage of this growth, we also have significant skill shortages in this area. For example, one State-owned website, *TechlifeIreland.com*, currently features 3,000 job vacancies. We must avail of the advantages that present themselves. Growing the tax base means asking what we can do outside our population of 4.7 million people.

In the context of the Brexit debate, one of the questions being asked is why a country would remove itself from the European market and the seamless transit it offers for goods, services and people. We can take advantage of the value this market offers. On the economic front, recent positive figures show growth returning to the eurozone economy. The question is how we can take advantage of this and grow our tax base. The way to do this is through exports but this requires us to have entrepreneur and business friendly tax policies as we face into a budget with tight constraints.

Ms Cora O'Brien: I will address some of the other questions Deputy Chambers asked. On the share options scheme, the main difficulty with share options is that income tax is charged on options when they are exercised, which is likely to be before the person has sold the shares. As such, the person will not have money to pay the tax. A capital gains tax also applies. Both these taxes are high.

Share options are generally provided in small companies. For example, a person may wish to forgo a high salary in a large company to take a chance on an innovative company achieving growth. Offering such persons share options to work for the company is an important way of attracting talent to small and innovative companies. While share options must be taxed, in other countries, for example, Sweden, they are taxed at the point at which the person sells the shares and has cash to pay the tax. In such circumstances, the sale is subject to capital gains tax. We would like to see a share options scheme as small companies, in particular, need one.

On personal tax, a debate is taking place on whether to use the €200 million available to reduce the universal social charge or widen tax bands. We are trying to move forward from the budget to budget approach. There are different proposals on the table, all of which are intended to relieve the tax burden but only by a little as there is not much fiscal space available. Our focus is on growing the fiscal space to ensure we have more money to play with in future as we seek to make the necessary reforms to the personal tax regime.

The decision to reduce the corporate tax rate to 12.5% was one of the best things we have ever done in terms of tax strategy and in providing certainty and assurance. The current rate is generating corporate tax receipts at equivalent ratios to countries with much higher rates. It is also the right thing to do for a small and open economy. The debate about corporate, personal and capital tax must take place against the backdrop of the type of economy we have. Our message is very much that we should start with the overall economic objectives and needs and work back to tax policy, rather than taking each tax head in isolation and arguing it should be set at this or that rate. I agree the corporate tax rate is very sustainable and certain.

Corporate tax is volatile in all countries. While Ireland has a high dependency on foreign multinational companies - these companies are very welcome and the money they provide helped us through the crisis - one of the reasons we produced the report was to seek to achieve greater balance and sustainability by generating more revenue from the domestic sector.

Deputy Lisa Chambers: I also asked a question about combining the universal social charge with PRSI.

Ms Cora O'Brien: That would be a substantial undertaking and one which would certainly simplify the tax system. The personal tax system, with USC, income tax and PRSI, is highly complex. Merging USC and PRSI could be done in many different ways and would depend on whether one wanted to fully integrate the two systems. Would one put all of the USC into the PRSI system? Would one start at the bottom or top? Would it involve putting income tax into PRSI or *vice versa*? Members may be interested to note that the United Kingdom has been examining this issue for five or six years. Its office of tax simplification has produced some good reports on some of the challenges. We have different bases, rates and bands in the various categories, all of which would have to be amalgamated. The process would be done taking a year-by-year approach. If members are interested, the British office to which I referred has done some good work on the issue.

Deputy Dara Calleary: What would be the total cost of the Irish Tax Institute's proposals in respect of capital gains tax and general taxation? Does the institute foresee tax increases in any areas? For instance, what is it views on the introduction of a sugar tax? What is its position on the 9% VAT rate for the hospitality sector? Its members were present for the debate on the issue.

On a more general issue, what are members of the Irish Tax Institute saying about their clients' preparedness for Brexit? The witnesses made a number of interesting proposals related to Brexit. How prepared for Brexit are the companies served by the institute's members? Which presents the greater threat - Brexit or the changes to corporation tax discussed recently by President Juncker?

Ms Cora O'Brien: I will discuss first the 9% VAT rate as I listened to the debate on the issue. There are two aspects to the debate, namely, the 9% rate and the idea of having regionalised VAT rates. It is interesting to note that between nine and 12 items are currently covered by the 9% rate. Hotel rooms have been the subject of much discussion. They are not the only thing that are subject to VAT at 9%. Up until now the tendency has been towards an all or nothing debate, so it would be interesting to look at some of the other areas at 9% because they could be different. We do not measure their economic sensitivity. We can, however, say that this is what one can or cannot do in this area. One could change one part of the list and not change another. There are hotels, for example, tour guides, meals, cinemas, open farms and green fields; there is a lot in there and one could have a debate over some of the other issues. We do not have to change 9% back to 13.5%; we could go for something in between. This is something that the committee might find worth exploring but we have no evidence and we have done no economic analysis on it.

I will now address the issue of regional VAT. While I fully understand the difficulty between Dublin and outside of Dublin for the sectors involved, the problem is that one cannot apply regional VAT because of the European system we have. Although one could take certain items in and out of the list, one cannot apply lower VAT in one part of the country and not in another. That is because of the rules within which we have to operate.

Deputy Dara Calleary: Are we not allowed to have city taxes within the European Union as opposed to areas that are not cities? There are cities across Europe such as Rome and Paris which have city taxes.

Ms Cora O'Brien: Yes, there are. When we go to hotels overseas we sometimes pay those taxes. One could look at that separately but that is not a form of VAT. It is not the 9% value added tax applied under European rules, but it is a possibility that could be considered.

Deputy Dara Calleary: What would be the cost of the package?

Ms Cora O'Brien: We have not definitively said what, for example, the capital gains tax rate should be, but a 1% reduction in that particular rate would amount to approximately €25 million per year. I understand the constraints imposed on the Government by the European rules. One cannot, for example, counterbalance what might result from increases in activity, one can only look at what the blunt cost of the tax reduction amounts to. This, then, is a longer-term model. It is not something we should think can happen overnight. We are starting from a different point, however, starting from where the Government is trying to get with its export strategy and working back down to what the best tax policy might be to try to arrive at that point.

Ms Olivia Buckley: There was also the sugar tax question.

Ms Cora O'Brien: Yes, how can I help the Deputy with regard to the sugar tax?

Deputy Dara Calleary: Is the Irish Tax Institute advocating any increases in tax? The introduction of a sugar tax was already signalled in last year's budget. Are there any other areas in which the witnesses feel we should consider tax increases?

Ms Cora O'Brien: I have outlined some areas there with regard to possibly broadening the VAT base. That could be looked at. The sugar tax is going to happen anyway. We are also going to see a small increase in the training levy for employers, currently part of employers' PRSI. There will be some changes there. There may perhaps be changes in climate and carbon tax - these are always worth looking at. What we are doing as much as anything else is putting out the options that could be looked at.

Ms Olivia Buckley: I will deal with the question of whether Irish companies are Brexit-ready and what is happening on that particular front. There are a number of angles to this. A lot of work is going on in terms of the feedback from our membership. There has been a huge amount of Brexit briefings and advisory work. Companies are seeking advice on what sort of plans they need to be make for customs union arrangements, what this implies and what it costs. Much of the research has been done in the vacuum of not knowing the final details but our companies and their advisers are certainly very focused on it. We will be in London next week to meet our sister institute, the Chartered Institute of Taxation, CIOT, along with its Belfast members. We had meetings in Belfast and Dublin earlier in the summer. There is no doubt that the focus is on the mechanics, namely, on what may happen and how.

The broader issue of whether companies are Brexit-ready goes back perhaps to our export strategy. A number of worrying statistics came out in the past couple of months. When we conducted our research into behaviour and attitudes, we looked at export-prone companies, that is, companies in export-driven sectors. There are three worrying statistics here. Most companies are still focused on the domestic market as their real priority. Over half of the companies we looked at were exporting to the UK. However, those that are not already doing so do not, for obvious reasons relating to Brexit, see huge potential to do so in the next 18 months. Fewer than half are exporting beyond the UK market and do not see themselves doing so in the next 18 months. There is an underlying cautiousness, fear and lack of confidence, a sense of constrained circumstances - whether they involve finance, capacity or sales staff - and a sense of an inability to enter export markets in the eurozone in particular. We know that the eurozone has been prioritised by Enterprise Ireland as one of the areas in which we can really take advantage. The Tánaiste and Minister for Business, Enterprise and Innovation is also looking at Europe's free trade agreements with countries such as Japan and Canada to see what advantage we can take from these. There is, however, an underlying sense of worry.

Diversification is the real answer to Brexit. Quite apart from dealing with the mechanics of Brexit, I am not so sure that we are Brexit-ready when it comes to diversification to markets in other countries. The chief executive of Enterprise Ireland spoke on "Morning Ireland" recently from the latter's showcase event. I do not have the statistics from the Enterprise Ireland survey to hand, but one of the areas she highlighted was the research showing that companies were not as Brexit-ready as they might like in the broader terms of looking at the world. Our export figures show that most of our exports in both services and goods, that is, approximately 85% to 90%, are carried out by multinational companies. This means that only 10% of our overall exports are driven by the indigenous sector. We do not have the same level of statistics for services, but looking at goods and products we can see that we have some really good superstars, companies that have conquered the world, and we are very proud of them. However, only 11% of them are exporting more than 20 products to more than 20 countries and they account for almost 50% of the value. The fact that our indigenous sector is reduced down to 10%, with 11% of those accounting for 50% of our exports, shows how limited we really are. The median number of countries our companies export to is actually five and the median number of products exported is four. Nine out of ten products exported by our indigenous companies are food products and one of these - chilled boned beef - accounts for 23% of our exports.

Ms O'Brien has already dealt with the area of innovation, diversification and research and development, which has flatlined in small companies. Very small and medium-sized companies consider themselves to be innovation-active. We have a great deal going for us but we also have much work to do. No stone must be left unturned.

In the context of our tax policies as supported by our tax administration system - which will Ms O'Brien might want to expand upon - if the members wish to be Brexit-proofed as policy-makers, they will have to look at every line of possibility in terms of what we can do for SMEs and how we might - with the relevant policies in place to support this - transform Ireland into a really ambitious country.

Ms Cora O'Brien: The tax administration issue is really about support services for small businesses. It relates to matters such as research and development, companies obtaining assistance in respect of the employment investment incentive scheme, trans-border activities, education, information and the need for dedicated staff. I know that last year, or perhaps this year, the Revenue Commissioners got some dedicated resources for audits, which are very important in a self-assessment system. We do, however, need some dedicated customer service support people. Our survey revealed that small businesses are having difficulty claiming some of the reliefs that are available and that they are having difficulty understanding whether they are entitled to such reliefs. They are worried about the uncertainty of claiming the relief and perhaps having to repay it if they are audited. It is something we can control and let us try to do that.

Deputy Thomas P. Broughan: I want to go back to the cost of the CGT change and the witness spoke of the €25 million per point deduction of the rate. Would the Irish Tax Institute favour going back to the Charlie McCreevy era? While the witness talks of just a couple of points, it is a significant tax. In my submission to the Minister last year, I suggested that it should actually be increased to 38% to give us an additional €178 million. One could argue that it is a very important element of tax and that we should perhaps leave it alone. The Scandinavian countries, all of which have very dynamic economies, are all clustered around our rate.

Ms Cora O'Brien: The basic principal of a capital gains tax is that one will collect more capital gains the more activity there is in the economy. We would very much welcome an economic analysis of this but the people we spoke to, business and our members, were unanimously of the view that there is activity that is not happening in this economy because of high capital gains tax rates. To be ten points above the OECD median is making Ireland an outlier; we are the fourth highest in the OECD. We would say, "Do not look at the rate of capital gains tax in isolation, look at what we are trying to do". We are trying to diversify the funding sources for small businesses, many of which cannot get bank finance. Many of them need angel investment, equity investment and help in that area.

Deputy Thomas P. Broughan: Would we be better to emulate the UK in that area with some sort of seed investment programme? There has been some criticism of angel-type investors in the UK in the context of some foreign investment and the way it is concentrated in certain areas such as the south east and so on. Are there different approaches we could take such as a dynamic tax policy, particularly for start-ups?

Ms Cora O'Brien: I absolutely agree. The UK has a very good and rounded tax policy for SMEs and it encompasses the seed investment fund to which the Deputy referred. It would be a good idea to have something on the seed investment side. That might be done as part of an overall review of the current employment investment incentive that is currently in place. The UK has a 20% capital gains tax rate so the authorities there know that if they want to generate this activity, more money will accrue to Exchequer not by having a high rate but by having a low rate.

Deputy Thomas P. Broughan: What does Ms O'Brien call a workable share option scheme? Is this not the problem? We have share option schemes. Do we introduce discrimination between different employees if some people have access to part ownership of the company and the rest do not? If one wants to have a good team approach in the company does this present a problem?

Ms Cora O'Brien: Again, the UK has a very good, workable enterprise management incentive whereby it is recognised that there are certain types of companies where there is a real need for a particular type of talent. The UK has a share option regime that is targeted at those individuals so those small businesses can compete. That would be a really good model for Ireland to have. That is part of their overall strategy for dealing with small businesses, so there are a lot of moving parts within that. We need a share option scheme that is going to work for small businesses.

Deputy Thomas P. Broughan: I shall now turn to the issue of excise that is obviously very important to business. Ireland has some of the highest excise rates in the world. Is the Irish Tax Institute in favour of gradually or immediately equalising the rates on diesel and petrol?

Ms Cora O'Brien: We have not looked at excise. We look at the key taxes around capital, labour and VAT. We do not examine excise and those sort of levies.

Deputy Thomas P. Broughan: Could this have an impact on business and small business?

Ms Cora O'Brien: Yes and we have certainly heard how this is a real cost of doing business. Maybe the overall point is if one is going to look at trying to help that sector in general. Our tax policies are part of that and the Deputy is correct that excise would have to be a part of that also. There are lots of different bits underlying it and people with expertise in different areas should all be part of that conversation.

Deputy Eamon Ryan: I thank the witnesses for coming to the committee. I could not agree with them more on their joint thesis that we need to develop our indigenous economy. I am old enough to remember the Telesis report saying that. The Culliton report said it and the Enterprise Strategy Group report said it and during our own time in government the smarter Building Ireland's Smart Economy report said it. While the attention was all on banking at the time, the underlying issue was that we have to move to a new sustainable, indigenous economy. In the past 35 to 40 years they were the times we went to look at what Ireland's economic strategy was. I absolutely agree with the argument that we need to become less reliant on foreign direct investment, FDI.

I have a concern, however, around the mechanisms the witnesses have presented for that. First I have a query for Ms Buckley and wonder if I heard her right. I was stunned that the figure for chilled, boned beef accounts for one quarter of our indigenous exports.

Ms Olivia Buckley: In the economics that does not take account of services

Deputy Eamon Ryan: Is that for manufacture?

Ms Olivia Buckley: It is for manufacture.

Deputy Eamon Ryan: Okay. So one quarter of our manufacturing material exports are chilled, boned beef.

Ms Olivia Buckley: Yes. That figure came from an excellent report that was produced by the ESRI earlier this year. It looked at the exports of Irish indigenous services and the exports of indigenous products. We have a lot more detail on products because of the revenue system in Customs and Excise. The number one product exported by Irish owned companies is meat of bovine animals, fresh or chilled. It accounted for 23% in 2015.

Deputy Eamon Ryan: We have come a long way from the 1930s when we were sending live exports; now we are sending it chilled and boned. It is not just that it is the number one export, the fact that it accounts for one quarter of our product is a startling figure.

Ms Olivia Buckley: Sorry can I correct the Deputy? That figure is for the indigenous sector.

Deputy Eamon Ryan: Yes. We live in a world where I believe capital has too much power. In the negotiated position of the various factors of production, and because capital can move so fast and is so transferable, it has huge power over labour. Natural capital does not move so it is completely undermined in the current economic system that we have. Everything is designed to support the interests of capital and we forget about the labour and natural capital or costs. A lot of the political problems currently happening around the world are, I believe, because labour rates are not increasing. The share of income going to capital versus labour is historically completely out of kilter, not just in Ireland but across the board. Would the witnesses agree with that view as a broader macroeconomic assessment? Any time, therefore, we have people coming in to say we have to reduce the burden on capital I believe that this is not the world we are in with regard to the big challenge. Let us say we went from 33% down to 25%, which makes rational sense to promote the indigenous economy, where would we get that €200 million from? From what I heard Ms Buckley saying, a rising tide will lift all boats and we would be exporting more. That is the problem, though. Every country has been saying that for the past 40 years. Since the late 1970s, the ideology has in a sense been that the market knows best. If it is satisfied and freed up, it will deliver. With every country beggaring its neighbour on this front, all it means is that capital generates more profits and labour and natural capital are undermined. This is a broad point. I am uncomfortable with the current imbalance between the power of capital and the power of labour and natural resources.

Before I ask my two questions, I believe that the State-----

Chairman: The Deputy is on his last question.

Deputy Eamon Ryan: I will cut them down to one question.

Chairman: I thank the Deputy.

Deputy Eamon Ryan: Can measures be targeted? If the capital tax rules are reduced in line with what the witnesses are suggesting and I buy shares in IBM that subsequently increase in value, I will pay a lower capital gains tax on them. Similar to Deputy Broughan's point, could there not be targeted measures for Irish exporting companies in terms of funding and so on? It would be a more specific model. I would be concerned about a general across-the-board cut in capital tax at a time when my income tax is 52% and my capital tax is 25% in a world where capital holds all of the power. While I understand the institute's intention, I am concerned about the means.

Ms Olivia Buckley: I thank the Deputy for his interesting remarks. I will make some general comments on why we have focused on this area and Ms O'Brien might wish to add something on the technicalities.

There are a number of reasons for this focus in our report. As Ms O'Brien outlined, we find ourselves with the fourth highest rate of capital gains tax in the OECD with a median percentage of 23%. Countries like Germany and the UK have much lower rates. We view ourselves as an open economy where a cold wind has a significant economic effect, given the nature and scale of our economy.

An issue was raised acutely by the Institute for Fiscal Studies in the UK last week. It outlined that the mobility of capital and people is a risk for Ireland, given that we are a small country neighbouring the UK with Newry less than one hour up the road from here.

Ms O'Brien has researched another issue relating to capital taxes, so I will let her pick up on this point after I have finished. We have a national ambition. Multiple extensive and thorough reports on Brexit were commissioned and well written by many people. There were reports from the then Department of Jobs, Enterprise and Innovation, Enterprise Ireland and Ireland Connected on the Brexit challenges facing Ireland. One of the major elements that these reports examined was the need to scale up our companies. If one is going to expand and drive into export markets, one needs to scale up. The figures set out in one of those reports - I believe it was Ireland Connected's report - indicated that we needed to scale up our companies by 30%. That requires investment at a time when as a country we have a greater dependency on bank finance than anyone else. Interest rates have been raised as an issue in this regard.

Other countries have far more competitive regimes than ours in terms of attracting angel and third-party investors to companies. We are low compared with the UK, Spain, France, Germany and Sweden.

In terms of the debate on capital or labour, we consider what strategic direction is required, what other countries have used, how competitively we stand on capital taxation and what we need to grow our companies, not just for the sake of growing them but to give our people the best chance economically. Going back to the beginning of our argument, this is all about people having world class services and giving children the best chance at education. We need the best hospitals and health services and we want housing, but we must look to Exchequer returns and see what can be accumulated that will allow us to do all of that for our people. This debate is not for the sake of the accumulation of capital and wealth, rather it is about how to give a country of just 4.7 million people the best chance and deciding what role the capital environment will play in that. It plays an important part in other people's strategies and in the scaling of their companies. As a country, we must ask ourselves what a competitive environment is.

Ms Cora O'Brien: We are considering this matter from two points of view, namely, what will help small businesses to grow and become more dynamic and what will generate more tax for the Exchequer. Capital gains tax is only returning 1% of total tax yield. As such, we have high rates, but we are not getting tax yield from them. In 2008, we were getting twice as much from capital gains tax when the rate was lower. That is the point - high rates are only good if they can match-----

Chairman: When was that?

Ms Cora O'Brien: It was 2008. High rates are not going to work if they are not going to generate yield.

Deputy Eamon Ryan: Was our rate at the time approximately 20%?

Ms Cora O'Brien: Yes.

Deputy Eamon Ryan: But it did not develop our foreign direct investment sector. I have a related question. If I earned profit on an IBM share, would I benefit just as much under this measure?

Ms Cora O'Brien: Yes. That is a valid question. It is something that we need to examine because the Deputy is right. There are state aid rules and some restrictions on what one can do, but it should be possible to develop a capital gains tax measure that is targeted at a particular group or focused cohort. The entrepreneur relief is a form of targeted measure for active trading businesses, allowing shares in them to be taxed at a lower rate. One could do something in that regard without including speculative gains or-----

Deputy Eamon Ryan: What did Ms O'Brien say the measure was?

Ms Cora O'Brien: The entrepreneur relief.

Deputy Eamon Ryan: Could we not expand it?

Ms Cora O'Brien: We could. That would be one way of going about it.

Chairman: Deputy Doherty has five minutes.

Deputy Pearse Doherty: Fáilte roimh. We know from the Coffey report and the tax strategy papers that claims for capital allowances for intangible assets increased from €2.7 billion in 2014 to €28.9 billion in 2015, which was an enormous jump. Obviously, intangible assets include intellectual property. This coincides with the onshoring of IPs by some multinationals. The Coffey report has suggested a limit of 80% on the quantum of relevant income that could be set against capital allowances for which intangible assets or any other related interest-related deductions could be made in a given tax year. What is the Irish Tax Institute's position on this suggestion?

Ms Cora O'Brien: I understand why Mr. Seamus Coffey has made that suggestion. When the cap was moved from 80% to 100%, it was at a time when a great deal of change was forecast in light of the OECD's base erosion and profit shifting, BEPS, proposal and positioning Ireland to deal with what would happen as a result. It is good that there has been a review of what happened. Many intangible assets have come onshore. In many ways, that is good. Under the new regime, IP and substance must be matched. The fact that we have IP is crystallising substance in Ireland in the rest of the business and protecting that for the medium term.

The number of claims is large. A cap of 80% would have a smoothing effect, so it is a reasonable recommendation to make, given the size of the IP that we now enjoy.

Deputy Pearse Doherty: Could the cap be placed in this year's budget?

Ms Cora O'Brien: I imagine that it will be examined in the budget. That is probably one of the areas that would be considered.

Deputy Pearse Doherty: The Irish Government has become known for kicking the can down the road, so I expect that a process of consultation will be embarked upon to consult on a report that took quite a period of time to be drafted. We do not tend to do things fast, particularly when it comes to raising taxes on multinationals.

Ms Cora O'Brien: Seamus Coffey has recommended that we do a consultation. The consultation he recommends is more on the longer-term European changes, the anti-tax avoidance directive and BEPS. He has not put the 80% into the consultation list-----

Deputy Pearse Doherty: No, it is the other wider part of it that requires consultation, and there is merit in that. Does Ms O'Brien have any indication of the revenue there would be if we were to give effect to the Coffey recommendation, which obviously stems from last year's budget announcement on examining these issues? Has the Irish Tax Institute any estimates of what going to 80% would mean?

Ms Cora O'Brien: No, I do not have an estimate.

Deputy Pearse Doherty: Would she agree that it could be significant?

Ms Cora O'Brien: We would need more visibility of the revenue data. Anybody who was examining that as an exercise would have to see the underlying individual companies and what the IP was. There is top-line data here, but the exercise on how much would be saved is difficult to carry out with only top-line data.

Deputy Pearse Doherty: Ms O'Brien mentioned that the discussion on income tax rates must be framed within the discussion on the type of economy we wish to have. Not to nitpick, but I argue that it should be framed within the type of society we wish to have. Indeed, the type of debate we have is extremely frustrating for me. Perhaps we are all at fault. Perhaps I am not making my voice loud enough or we are not getting other players to make their voices loud enough, but the herd has left the field already with the tax cuts agenda. However, let us put it into the context of what type of society we want. We know the fiscal space is €470 million after allowing for the pay agreement. We can raise it by additional discretionary tax measures, but let us take it as €470 million. The argument is how to cut €200 million in taxes. How do we do that and where does the Irish Tax Institute stand on it? As we sit here discussing issues such as what is the best way to cut €200 million in personal income taxes, as Fianna Fáil members have asked a number of people, there are 456 patients lying on trolleys. Many of them are in pain, some of them are extremely elderly and some are very vulnerable. As we came here this morning 3,000 children woke up in emergency accommodation, accompanied by 5,000 adults. Rough sleepers were moved along from doorways. We use feeble words such as, "We need to challenge or address the crisis in health or housing", yet the debate is completely occupied by reduction in personal income tax rates. I must be unique among the other political parties because nobody comes to my office to ask for a reduction in personal income tax rates, although many people tell me they are under pressure because of the costs of child care, education, health and so forth. The institute has also been a party to that debate. That is its role. How can the institute suggest that we should reduce the tax rates or marginal tax rates at a point when it is so familiar with the other crises that exist and with the fact that the pot is not bottomless?

Ms Cora O'Brien: I will try to step back a little from that. The starting point with identifying the right tax policy is how much expenditure we need to raise as a society for the types of things we need to pay for. That is the first question. The second question is, given that amount of expenditure and the type of small open economy we have, because that is what we have to work with, how will we devise our tax policy to get the most tax to fund all the services? When we in the institute say that capital taxes and marginal tax rates are high, it is not because we wish to take from somebody and give to somebody else or that we think a tax cut is more important than hospital trolleys. It is not about that. It is about trying to raise the most tax. We believe the best way to raise the most tax is by having the most appropriate tax policy for this type of country. In our view, the way we will generate more tax to pay for more services is by examining our personal tax regime, which is impeding our talent. By all means we would welcome a piece of work on marginal tax rates-----

Deputy Pearse Doherty: Has the institute any such work? I asked Dr. McDonnell a question earlier about evidence and he suggested that there is none and that we need to look at the long-term in a country. We dispute and disagree with some of what the ESRI produces, but its representatives told this committee last year that there is no evidence to suggest that marginal tax rates are a deterrent to employment. Indeed, they pointed out that investment in child care would be a larger enabler in terms of economic activity and job creation.

Ms Cora O'Brien: Obviously, child care is a massive issue. As the previous contributor said, the research that has been done on marginal tax rates has largely been carried out in the US. The analysis there is that it did not have a huge impact, but the US economy is massively different from Ireland's. In the US economy there is not nearly as much cross-border movement in labour. What is driving ours and where we need to get our money is exports. There is also foreign direct investment, which we cannot forget in the debate. There is huge movement in and out of the country by a very mobile labour market. There has not been enough research carried out on what is the right income tax policy for a very small open economy. I would welcome some economic analysis. We cannot do that as we are not an economic body, but we would definitely support the right income tax policy for Ireland for the next five years. All we can go on is where we are in terms of other countries - and we are certainly out of line with other countries at that upper talent end - on what our members tell us about the dealings they have with businesses and things such as the PwC pulse survey and so forth. That is the evidence we have, but we would welcome some economic analysis of it. However, it has to be for the type of economy we have.

Deputy Pearse Doherty: We have seen-----

Chairman: Deputy, I appreciate the points you have raised but it is over ten minutes.

Deputy Pearse Doherty: I have a tiny question.

Chairman: A tiny question and a tiny response.

Deputy Pearse Doherty: The Chair might give the witness more latitude than she has given me, but she has been very generous in terms of time.

Chairman: I am strict with the witnesses as well.

Deputy Pearse Doherty: On the 9% VAT rate, I heard the comments about not looking at it in its totality. I argued that earlier in terms of hotel beds. Ms O'Brien commented that perhaps we could consider not going directly from 9% to 13.5%. That is interesting because my understanding is that this is not possible. Under the EU VAT directive we only have two reduced VAT rates which are 13.5% and 9%. There is no option to have further reduced VAT rates. The other reduced VAT rates we had - zero, 4.5% or 5.4% - were historical so we could have them because they were in place before 1991. There has been comment in the media and the Minister has been flying kites about it possibly going up to 10%, but it is my understanding that this is not possible. It is either 9% or 13.5%. Is my understanding wrong and is it possible to increase incrementally one of the two lower VAT rates that are permitted under the directive?

Ms Cora O'Brien: I will double check it for the Deputy but my understanding is that we can have two lower VAT rates but we cannot have another one. We could change it to another rate but we could not introduce a third one.

Deputy Pearse Doherty: The 9% would have to move to 10%.

Ms Cora O'Brien: I think that is the case, but I will check it.

Chairman: Does Ms Buckley wish to say something?

Ms Olivia Buckley: I have a brief comment on the budget debate. We have been at pains in the institute this year to concentrate on the export strategy piece of work more than a budget document. This is a longer-term journey and there is much pressure on the system. It was not an exercise in clamouring and calling but rather a reflection on where we felt the strategy of the country needed to go, supported by tax policy. The tone and approach of the institute has very much been geared towards the medium to long term, given what is going on.

Chairman: I thank Ms Buckley and Ms O'Brien for their presentations and for answering our questions so comprehensively. I thank the members also. We will now suspend for a few minutes to allow the next group of witnesses to take their seats.

Sitting suspended at 12.26 p.m. and resumed at 12.28 p.m.

Chairman: Before we begin, I ask witnesses to turn off their mobile phones as interference from them affects the sound quality and transmission of the meeting. I welcome Mr. Ian Talbot, chief executive of Chambers Ireland. With him is Ms Sarah Freeman, director of policy and communications. I thank them for making themselves available to the committee. A copy of their pre-budget submission has already been circulated and we will take it as read. The witnesses have been asked to touch on the following themes in their presentation: VAT in the hospitality sector; the vacant site levy; local property tax, LPT; and their pre-budget submission.

I draw the attention of witnesses to the fact that by virtue of section 17(2)(*l*) of the Defamation Act 2009, witnesses are protected by absolute privilege in respect of their evidence to the committee. However, if they are directed by the committee to cease giving evidence on a particular matter and they continue to so do, they are entitled thereafter only to a qualified privilege in respect of their evidence. They are directed that only evidence connected with the subject matter of these proceedings is to be given and they are asked to respect the parliamentary practice to the effect that, where possible, they should not criticise or make charges against any person, persons or entity by name or in such a way as to make him, her or it identifiable.

Members are reminded of the long-standing parliamentary practice to the effect that they should not comment on, criticise or make charges against a person outside the House or an official either by name or in such a way as to make him or her identifiable.

Mr. Talbot has been allotted 15 minutes to make his opening statement. He does not have to use all of that time and may share time with Ms Freeman.

Mr. Ian Talbot: I thank the Chairman. Ms Freeman has just recently joined the organisation and is still coming to terms with the volume of paperwork, so I will do most of the talking. I thank the committee for inviting us here today and for taking the time to look at these very important matters.

As the committee members will know, Chambers Ireland is the largest business organisation in the State. With over 45 member chambers in our network, we represent businesses in every region and economic sector in Ireland. We are very much generalist and represent all types of business without breaking them down into specific sub-sectors. This geographic representation gives us a unique understanding of the challenges facing businesses throughout Ireland. In particular, we know and understand the threats to those doing business and providing much-needed jobs in towns and villages. We also understand the opportunities and believe Government can play a major role in minimising the threats and turning the opportunities into realities.

Moving straight on to the first area we were asked to address, the 9% rate of VAT in the hospitality sector has contributed significantly to the growth of tourism and jobs in the last few years. Tourists are also arriving from increasingly diversified markets. We welcome recent announcements about new direct air links and affordable fares, which will undoubtedly contribute to this area. However, in spite of 4.2% growth in arrivals in the first six months of 2017, there was a concerning fall of 6.4% in visitor numbers from Great Britain during that period. The tourism and hospitality sector has particular regional importance, providing much-needed employment in rural Ireland and Border areas. The fall in tourist numbers from Great Britain was predicted following Brexit. The fall in the value of sterling has made Ireland less attractive financially while also potentially improving the competitiveness of UK tourist offerings for Irish and other eurozone visitors. There is also a competitiveness aspect this debate. Some 17 out of 19 eurozone countries have tourism VAT rates of 10% or less, making our current rate competitive against that cohort. Taking those matters into consideration, together with the uncertainty surrounding the nature of and timeframes for Brexit, we believe that the 9% VAT rate should remain in place. To increase it to our standard rate of 13.5% would be detrimental to the sector.

On the vacant site levy and local property tax, Chambers Ireland has long called for a broad-based system of property taxation. The chief attributes required for such a system to be acceptable would include a local tax to fund local services and local development needs; fairly applied taxation, in that everyone should contribute something; taxation that is structured to broaden the revenue base of local government leading, in turn, to a reduction in the pressure on the business community via rates and other charges; and that the tax should be equitable. Having established the local property tax and a high compliance ratio, we are concerned that the objectives above are being watered down with property values still locked at 2013 levels and many exemptions now in place.

We appreciate the difficulties significant increases in house prices cause when computing liabilities. However the bands and rates of taxation applied could, for example, be adapted. In addition, local authorities have flexibility to vary LPT payable through the local adjustment factor by an amount of plus or minus 15%. While it falls within the remit of local councils to determine the use of this factor, there is an opportunity for appropriate use of this flexibility to raise funds for local services and development which otherwise could not be delivered or would have to be funded by increases in business rates. We have called on councils to assess the opportunity in each of their areas to raise additional funds. In the long term, Government should consider the development of a land tax that is based on the value of a parcel of land as a replacement for LPT. As the value of a piece of land increases, the rate of tax increases. Such an approach to land management would encourage improved use of land and not penalise improvements in the way LPT does. With regard to the vacant site levy which is due to be levied from January 2019, we have recommended that it be brought forward to January 2018 as one of several measures that could be employed to encourage housing development.

Turning to our pre-budget submission, we conducted an extensive consultation process with our network about the concerns of the business community, feedback from which forms the basis of our submission. We recognise that there is limited fiscal space and we strongly encourage Government to continue to urge the EU to review and update the fiscal space calculations to reflect economic circumstances, the nature of investments proposed and relative borrowing costs. There has been a very strong message from our network that investment in infrastructure needs to be the absolute priority in budget 2018 with a preference that other matters such as small business focus and tax reform are addressed by making commitments under the multi-annual framework model for future budgets. A significant component of the rationale for this was the importance of maximising our competitiveness in light of Brexit uncertainty. Our submission is fully laid out on our website.

The key elements are in three separate areas: infrastructure, small business focus and tax reform. The feedback was that investment in infrastructure should take precedence. The Minister, Deputy Donohoe's commitment to an additional €4.1 billion in capital spending between 2018 and 2021 is welcome as is the commitment to link capital plans to the national planning framework, NPF. We believe the NPF is hugely important.

One of the key areas we need that investment to target is housing. Our current issues in housing are a huge threat to Ireland's competitiveness. We welcome the attention it is receiving but it is vitally important to implement the latest plans with a huge sense of urgency. Transport is a crucial area for investment. Greater connectivity between our regions and improving inter-city transport should be prioritised. The Government must deliver the national planning framework, the next draft of which is due at the end of September, and we need to ensure that spending on infrastructure ties in strategically with that. A recent Indecon Cork and Limerick Chambers research report found an M20 motorway would create over 5,000 jobs, help create a seamless Atlantic corridor and enable much greater connectivity between the regions. Our ports infrastructure and connectivity to those ports also needs to be upgraded particularly to help open up more direct access to EU markets in light of Brexit.

It is essential to roll out the national broadband plan as soon as possible. Businesses cannot function without quality high speed broadband. It affects a company's ability to do business, hampers access to new markets and renders it increasingly difficult to do business with the Government, for example, applying for Government tenders, dealing with Revenue and filing annual returns with the Companies Registration Office. Download and upload speeds also need to be future-proofed to ensure competitiveness with other jurisdictions.

In the area of energy, our priority is ensuring a dependable and sustainable supply. We also have to be ready for a welcome increase in population of 1 million people over the next 25 years as the CSO has predicted. We need to prioritise continual investment in our grid infrastructure and address climate change issues. We have more detailed information in our full pre-budget submission. We need to know how it is proposed to fund a sustainable water supply across the country from general taxation, to ensure reliable funding and to open up the opportunity to raise external funding for vital projects.

In the area of education, Ireland continues to have the youngest population in Europe with one-third of the population under the age of 25. We must aspire to be the best there is with a best practice education system encompassing everything from early child care to college education and beyond. In the area of adult education and upskilling in business, with unemployment heading for 6% and below, which is a great story, there is a need to reallocate funding from unemployment programmes to schemes specifically geared at upskilling those already in employment. This will increase our competitive capability internationally and augment the ability of existing businesses to grow.

We need to continue investment in accessible, affordable, high quality child care services and to meet our commitments outlined in the national women's strategy.

I will now turn to the other two sections. Recognising that we would like to see the concept of the multi-annual framework model being used here and limiting the surprises in a budget, the small business focus should continue to be the retention of the 9% VAT rate, the implementation of an employee share ownership scheme tailored to the needs of SMEs and establishing grant support for SMEs undertaking innovative research and development. In addition, there should be Brexit supports including financial commitment to back up announced proposals to expand our networks overseas and additional supports for a wide range of businesses to expand our export horizons with the necessary training and skills.

On tax reform, we need to reduce the marginal rate of tax below 50%. We need a competitive capital gains tax regime with the UK. We need to continue commitments we have made in the past to supporting the self-employed, entrepreneurs and small businesses in areas such as the USC surcharge, income tax credit, parity for the self-employed in maternity and paternity benefits and a tax credit on employers PRSI for micro-enterprises

We greatly welcome the committee's interest in these areas and are happy to respond to its questions.

Chairman: I thank Mr. Talbot for his opening statement. I have two quick questions. A representative from the Irish Congress of Trade Unions, ICTU, was here earlier. Mr. Talbot is advocating retention of the 9% VAT rate but ICTU is saying it is a loss to Revenue. How does Mr. Talbot counter that argument?

Representatives of the Irish Tax Institute were also here. I think Mr. Talbot heard some of their evidence here today. The representatives talked about a lack of diversification as one of the main struggles facing the SME sector and small businesses in terms of Brexit. The impression I got is it is their main underlining worry. Does Mr. Talbot agree with that?

Mr. Ian Talbot: On the VAT rate, if one simply takes the amount of income earned, which is taxed at 9%, and tax it at 13.5%, one gets a big number. The question for us is what will happen if we are even 4.5% less competitive? We must also consider that depreciation in the value of sterling might potentially put people off coming to eurozone areas. It is not just an Irish problem. There is a risk of Irish consumers heading to the UK. There are several risks that could undermine the amount of revenue we collect that would be taxed, whether the rate is 9% or 13.5%.

The other issue that came through very strongly from our network was the regional-rural impacts that could arise from this. Our geographic mandate means we are very focused on towns, villages and communities across the country. We have some way to go before we get the tourism and the recovery fully out to all those areas. I mentioned things such as the national planning framework. It is really important to ensure we target investment so people can understand where they fit into the national planning framework. Are they one of the cities that will be developed or are they a rural area that needs to link into it? We feel the retention of the 9% rate is important to retain jobs particularly in regional and rural areas.

On the other question about the lack of diversification, there are several ways of looking at it. There is diversification in what they do and diversification in the markets in which they sell. We are all hoping to see further supports and hopefully EU support for further supports to assist companies to diversify the markets into which they are selling. We focus on things such as the need to upgrade ports infrastructures to facilitate Irish exporters with more direct access into EU markets from our ports rather than having to, for example, go across the UK. With regard to the diversification of the products and services companies, we are a very innovative nation and we have lots of things going on. The challenge for us is to get more of those companies exporting.

We have a huge amount of stuff going on. We all have recommendations for how we might help promote research and development.

Chairman: Deputy Chambers has five minutes.

Deputy Lisa Chambers: I thank Mr. Talbot for his presentation. The Chairman talked about the presentation from ICTU and its very strong proposal that the VAT rate should be increased. Part of that is coming from the fact that it is still perceived as a very low paying sector and that the benefit in the reduction of VAT has not been passed on to employees or, if it has, it is marginal. I would like to hear Mr. Talbot's views on that. It is very difficult to maintain the VAT rate at 9% when there are hoteliers in Dublin charging €600 for a room without breakfast. There is a regional aspect to it. In the west of Ireland, which I represent, it is vastly different to Dublin. How do we deal with that? It seems as though there are huge profits being made in some urban centres, with the benefit not being passed on to the employees and the price reductions not being passed on to the consumer.

In terms of preparedness for Brexit, how prepared does Mr. Talbot think his members are? Are there any things we should be taking into consideration for the budget for next year and for the committee's work into the future in terms of helping Chambers Ireland members?

Mr. Talbot spoke about the need for investment in transport, broadband and infrastructure. In the west of Ireland, there is a massive infrastructure deficit and broadband is a huge issue. It appears that lots of the resources available are being pumped into infrastructure projects in urban areas. While we need that because we have populations migrating east - if they are not emigrating - it is creating huge problems for us in the west of Ireland. What are Mr. Talbot's thoughts in terms of regional balance for this budget? Are we in the west of Ireland getting our fair share of the investment in infrastructure as opposed to the rest of the country? In terms of job creation, there are now people commuting exceptionally long distances. They are spending a lot of time in their cars and on trains, increasing the time away from their families. It is having a devastating impact on family life, on mental health and on all those other factors. What are the members of Chambers Ireland saying about that? From where are they getting their pool of people? Obviously the housing issue is definitely having an impact on that, but the fact that our investment in infrastructure and capital is so weighted towards the urban centres means that we are not giving the regions a fair chance at providing that employment and assisting them to keep people in those areas.

My final question is on climate change. I know Mr. Talbot has touched on this and on the need to address these issues. This country is looking at substantial fines. How prepared is the business community to adapt to any budgetary measures which might be introduced in order to meet emissions targets? Has Mr. Talbot's organisation done any work on how industry and businesses might cope with the huge fines we may face? How receptive are they to doing their fair share in terms of reducing emissions?

Mr. Ian Talbot: I thank the Deputy. As I am sure she knows, we have four affiliated chambers in her area.

Deputy Lisa Chambers: I know very well.

Mr. Ian Talbot: They now also operate as a County Mayo chamber group and they are also members of the Atlantic economic corridor group of chambers. As an organisation we are doing everything we can to support those businesses working together across our entire island to achieve things. If one looks back ten years, our chambers tended to work very independently. They are now working much more closely together and are seeing the value of getting together to get higher levels of investment into an area.

To address the Deputy's specific queries, on the low-pay sector there is a question mark between when the rate of unemployment was at 15% and now, when it is down to 6%. We certainly now need to be looking at the quality of jobs that are coming through. If we go back to looking at the 9% rate of tax and when it should be changed, we continue to believe that now is not the right time. I did not really mention it earlier but I specifically mentioned international competitiveness in my presentation. Approximately 10% seems to be the normal rate for tourism businesses in Europe. We feel that 9% is right in that sector at the moment. It is creating employment and with the unemployment level coming to 6% other challenges in the economy will be created. We may start to see wage pressure coming through for example. I think we are seeing that because we are reaching full employment. We believe that is positive.

On the issue of Dublin hotels being able to charge the rates they can charge at the moment, we have spoken to tour operators and and such businesses. They say that if one is trying to get a tour coming into Ireland and visiting the east and west coasts, it is still important to get people into Dublin, but it is vitally important that they come to Ireland and we get them over the far side. It is also vitally important that when cruise ships come calling to ports other than Dublin that there are attractions which can get people off the boat and spending money locally. There are a whole lot of areas in which we need to remain competitive in the tourism sector. I am not sure how the obvious shortage of supply that is facilitating hotel prices in Dublin can be dealt with.

I keep coming back to two things. First, our focus as an organisation this year is that infrastructure must be the priority. We have said that we are prepared to forgo some of our other typically standard projects, such as tax reform, small business supports and so on, to make sure that we are spending money on infrastructure around the country. I know it is a little bit further south than the Deputy's constituency, but I specifically mentioned the Cork to Limerick motorway and that then joins up all the way up to Gort, Tuam and Galway. It is really opening up the Deputy's area. We are pushing very hard for that sort of infrastructure building. I also specifically mentioned how important we believe the national planning framework is in order for us to have a proper debate about how we support regional and rural development and not just to allow Dublin to keep growing at the rate at which it has traditionally grown. We really believe that national planning framework is vitally important in starting to address some of the many issues. We do not feel that it will be too easy to address them in budget 2018.

Deputy Lisa Chambers: Before Mr. Talbot moves off that point, he has spoken about the motorway from Gort into Tuam and then on to Dublin. One could draw a line from Tuam up to Mullingar and one would cut off the entire north west. We just do not have the road infrastructure. We are doing well to keep the businesses, the multinationals that we have, there. They tell us all the time that they are losing money because goods that are being transported on those roads are being damaged *en route* to the various ports and different areas. It is vitally important that Chambers Ireland advocates for proper infrastructure - for a good road network in the north west and for proper rail links, because Mayo is one of the counties making the greatest use of freight rail. We only have one line, however, which goes straight to Dublin. If that gets cut off for any reason it has a huge impact on our companies such as Hollister, Baxter and Allergan. These are major employers in that area. We feel that the north west is consistently left off the map in every planning framework and in all of the investments in infrastructure which we speak about. It is so important that organisations such as Chambers Ireland fight for us in that regard.

Mr. Ian Talbot: Yes, and I think we do. There is always more we can do but, again, we have the Atlantic corridor chambers, the Mayo chambers group, and there is also a grouping that has put papers together, the N6-N7 chambers. We are very conscious of all of those. We very actively try to support them in the work they try to do. We are also very focused on the far north west, the Letterkenny and Donegal area, for example. We also engage with the Northern Ireland Chamber of Commerce and Industry, for example on the road link between Monaghan and Strabane in Northern Ireland, which is not a particular focus of the authorities in Northern Ireland which are more focused on the links from Belfast laterally rather than those cutting across. We are very focused on these things but I thank the Deputy for pointing out that there is more we can do and we would love to do more in that regard.

If the Deputy is happy for me to move on to other points, on the whole area of climate change, we have not looked overly closely at the impact of fines and how the business community will deal with them. We believe our members are very open to dealing with climate change. There is a sense of frustration among our members at times at the length of time it can take to get really important planning approvals in respect of energy, the national grid and those sorts of things. Our members would be very supportive of efforts by organisations to put in proper infrastructure which would help us meet our climate change targets. To go into the detail of our pre-budget submission again, we have many recommendations on areas such as electric vehicles, the electrification of the public transport fleet and the Government using Government procurement and the e-tender platform to facilitate and encourage more environmentally friendly purchasing by Government itself. There are many things which we are trying to introduce to the debate to try to improve things.

Deputy Thomas P. Broughan: I welcome the delegation and its comments on the site levy. Moving on to where the witnesses have spoken about land tax, what is their thinking in that regard? Do they think that the local property tax is not a just system in the sense that major property across the country is not taxed? On that issue, there is a planned re-evaluation, possibly for 2019, which will lead to major increases for households in urban areas, certainly in parts of Dublin. I note the views of some commentators, including our colleague, Senator McDowell, for example, who sent us a briefing recently. It is probably related to the next election. He is hoping that some of us may be able to vote for him as a Senator. He made the proposal that perhaps there should be some kind of regional valuations system.

To be fair we have been trying to broaden the tax base as much as possible and this committee is very interested in doing so but the property tax is becoming the local government tax, as other people have said. Obviously Mr. Talbot’s organisation has a heavy involvement in this area in the context of rates and it members have a huge interest as business people, as well as as householders, in respect of what happens with them. Has Chambers Ireland given any attention to the efficiency of councils? Many people have been taken aback by how lethargic local councils sometimes are in respect of moving on the housing crisis, for example, or moving on other major issues. Councils are very often involved in many kinds of local development issues, but sometimes people think they should stick to the knitting, which is providing the basic essential services for households and businesses. I wonder whether Mr. Talbot can see trouble ahead with regard to the local property tax, which was not the subject of huge political campaigns when it was introduced. I suppose it went straight to Revenue and the Department of Social Protection. That is one of the major things I want to ask about.

Reference has been made to the 9% rate. A rate of 23% is imposed on a range of businesses. We are fixated on this, to some extent. Many people feel that the Irish Congress of Trade Unions is making a very valid point. The key point that was made earlier by the witnesses from the Nevin Economic Research Institute, whom Mr. Talbot may have heard, was that tax expenditure should be the subject of an absolute timeframe. They referred to sunset clauses etc. Are we going to have this debate about VAT *ad infinitum* into the future?

I noted what Mr. Talbot had to say about the situation with regard to water. Does he have any ideas about how we might pay for water infrastructure from general taxation?

Mr. Ian Talbot: I thank the Deputy for his interesting questions, which are very much in our space. As we have at least one chamber per local authority, we have a very clear focus on what local authorities are doing. When we talk about the efficiency of local authorities, we need to consider the executive process and the councillor process. We are constantly wonderfully impressed by the great work that is being done by executive operations in local authorities around the country to encourage business, tourism and everything else.

Deputy Thomas P. Broughan: I would prefer if we had an elected mayor for the Dublin region. It appears from examples like Manchester, Liverpool and, particularly, London that directly elected mayors seem to work as very good focal points for local development. I apologise for interrupting.

Mr. Ian Talbot: That is fine. At national level, we have not focused particularly on the proposal to have a directly elected Dublin mayor. We have allowed the four main chambers in the Dublin area to have that debate. I do not feel I am sufficiently well briefed to go into that issue.

I would like to return to the issue of a land tax. We feel that the taxation of land is a very efficient way to go about raising tax and broadening the tax base. It is also about the efficient use of land, which ties back into the national planning framework. It is great to see factories in deeply residential areas like Baldoyle Industrial Park, which is close to the Deputy's constituency, being rebuilt and regenerated. As my son goes to school in Kilbarrack, I am aware that it is a hugely residential area. We need to make sure we have the right mix of accessible jobs and accessible public transport in order that people do not have to travel too far. We need to make sure we make the best use of the DART, the Luas lines that are being built and, in due course, the metro north system.

The point I would like to make about how land is taxed is that there is a danger that the property tax will start to look like how the residential property tax looked at the end of the 1980s and in the early 1990s. As valuations increased, it became politically difficult and something had to change. We ended up giving up on property tax. It took several years to get something back on the table. We need to consider whether we should look at how a commercial site value tax and a residential site value tax might integrate together. Would such an integrated tax act as a substitute for commercial rates as well? As I said in my presentation, we are concerned that the current local property tax system has stagnated. In 2018 or 2019, a big decision will have to be made on whether to let the existing rules go through or, as I suggested in my presentation, to change the 0.18% and 0.25% bands to make the figures a little more acceptable to ordinary taxpayers who are working hard to pay their bills and do not expect huge increases in these taxes.

We suggest there is still a great deal of work to be done here. We believe the introduction of a land tax would be a better way of taxing than the current system of commercial rates based on the historical valuation system and on the striking of rates by councils. Ultimately, the rate that is struck by a council is a balancing figure after it has added up all the other income it is not getting. In the intervening period, there is an opportunity to increase the valuation in 2019, to adapt the rates or to look at the effective use of the 15% variation system, or all three. I know that last week, for example, Fingal County Council moved back from the full 15% reduction and pulled it back to 10%. At a time when there is a housing crisis and many other things are going on, often specific to certain areas, there is an opportunity for councillors to realise they are not taking full advantage of a pool of funding that is available. We believe an opportunity exists in that regard. At its core, we would rather see an efficient land tax introduced. Not only would that create a broad base of taxation, but it would also lead to more efficient use of land. We would then be able to return to issues like the density of population in areas where infrastructure has been developed. Our network's view is that in the interests of the efficient use of infrastructure, there needs to be more carefully managed and controlled high rise development.

I would like to respond to a couple of other questions. As I listened to the commentary of the Nevin Economic Research Institute, I felt there was a lot of stuff we agreed on. We are not particularly keen for the debate on the 9% rate to continue forever and a day. When it was brought in, it was meant to be a timebound thing. We have come through the financial crisis and our own fiscal stability issues. Now we have the Brexit crisis. The strong word coming through from our network - we have four chambers in Dublin and 42 chambers outside Dublin - is that this rate is having a significant impact on regional and rural jobs. The members of our network are asking us to continue to call strongly for the 9% rate to be maintained. I think people recognise that this debate will continue. Perhaps, in due course, we should consider whether the 23% and 13.5% VAT rates are the right rates to have as we seek to get a more balanced and broader tax base. Are those rates competitive from a global perspective? Irish people pay many other taxes. If one wants to buy a car, one has to pay VRT, which rarely gets a mention these days. When other parties and stakeholders look at our excise duties, they say they are too high. We have not really focused on any of that. I think there is a general acceptance that the rate will need to be balanced at some point. It is a question of timing. We do not believe it should happen now.

Chairman: I thank Mr. Talbot and Ms Freeman for attending today's meeting, making their presentations, engaging with the committee and providing their pre-budget submissions. We very much appreciate it.

Mr. Ian Talbot: I wish the Chair good luck with her role. It is not easy to juggle all these things and get them to add up.

Chairman: I appreciate that.

The select committee adjourned at 1.05 p.m. until 2 p.m. on Wednesday, 27 September 2017.