

Irish Congress of Trade Unions

**Rewarding Productivity and Promoting
Social Equity – Tax Reform to underpin a
New National Agreement**

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Some Principles and the Philosophy underlying Taxation

The Irish Congress of Trade Unions believes that Taxation policy should be grounded in the concept of equity.

The government and the social partners now fully accept that economic and social concerns must have parity in policy decisions. This means that tax equity should have parity with the economic/incentive objectives of taxation policy.

Therefore income from all sources should be taxed in the same way, in so far as is feasible. Unfortunately the current system taxes income from work and enterprise at much higher levels than gains from speculation, inheritances, capital etc.

Taxation should encourage preferred economic activity, but many tax incentives have become diffused, ineffective, costly and outlived their usefulness. In contrast money used to pay for public services is referred to by Ministers as “a burden”, demonstrating a strong ideological perspective. Congress rejects this paradigm. We regard taxation as the legitimate way of funding public services. If some public spending is ineffective, that is a different matter from ensuring adequate funding of public services.

There could be difficulty maintaining public services in a slower growing economy unless the tax base is broadened by the elimination of tax breaks and exemptions that are regressive, disproportionately benefit the rich and allow high earners to minimise their tax bill. The principle of simplicity should be applied to exemptions and allowances in order to close off abuses.

The Changing Economic Climate

Ireland reduced its public spending as a percentage of GDP from the average of the EU15 in the 1980s and early 1990s to much lower levels, due to spectacular economic growth. Now it is rising again. Yet many Irish citizens and citizens' groups, including Congress, believe that calls for increased public services are strongly justified, despite the end of the prolonged economic boom during the latter half of 2007.

This can be done by achieving greater equity in a system that has undermined the objective of rewarding work in recent years, as opposed to rewarding speculation, inheritance and capital gains. For instance, the lower taxes on capital and inheritances have led to a situation where someone inheriting €1,000,000 from a parent only pays an effective tax of 10.1 per cent, while many wage earners pay tax at 41 per cent plus PRSI.

In the wake of the international banking crisis, the ‘light’ regulation of this sector by Central Banks and governments is no longer sustainable. German President Horst Köhler – a former head of the International Monetary Fund – told *Stern* magazine on May 15 that: “We need more and efficient regulation, higher capital requirements to underpin financial trades, more transparency...”

Congress does not favour heavy or unresponsive regulation, but we need structures that monitor practices effectively and adapt quickly to changing circumstances. We believe the Government's *Better Regulation* guidelines are useful in this regard.

Policy choices can match economic competitiveness with social equity

Contrary to the myth that 'high taxes discourage investment because profits are taxed at a high rate' the National Competitiveness Council publishes benchmarking reports annually (based on the World Economic Forum and other sources) showing that high-tax Nordic countries are consistently ranked among the most competitive in the world. In 2007/2008 competitive league tables three Nordic countries are listed in the top six.

Congress is not advocating high taxes, but rather a broader tax base, based on fairness, that achieves a European level of public services. For instance, in addressing the need to reduce carbon emissions, we must also address the issue of fuel poverty in a time of rapidly rising fuel prices that impact most on the poor.

Congress has long been an advocate of evidence-based taxation policy in the public interest, as opposed to myriad tax breaks for property investment, which cost the taxpayer around €2 billion to mid 2007. The government has finally moved on property tax breaks, but has not curbed all of them and has allowed very long termination periods.

We understand that it can take time to unwind tax breaks/incentives for business but the extended time span is costing the Exchequer substantial lost revenue. Indeed newly-released figures show that one group, stallion owners, received tax exemption of some €91m in 2006, at a cost of €22.5m to the Exchequer.

Gain sharing

In contrast workers are still awaiting implementation of proposals agreed under *Towards 2016* on the tax treatment of earnings from approved Gain sharing Schemes.

Indirect & Direct Taxes

The shift in taxation from direct income to consumption through indirect taxes and user charges is more regressive than income tax and the Government must examine this imbalance with a view to equity and to Ireland's high price levels.

Ironically inflation is partly due to high indirect taxes and user charges. No government subsidy should be introduced for Biofuels, which would further push up the price of food, and VAT rates should be reduced below the very high 21 per cent rate.

Philanthropy & Charities

Congress recognises the valuable work carried-out by many charitable organisations in the areas of poverty reduction, social inclusion, human rights, health, care, international development and across a range of community, cultural and arts areas. It believes such work should be supported through tax relief and the threshold for tax relief granted on donations should be reduced from €250 to €0.

The cap on tax efficient giving at 10 percent of income should also be reconsidered for those within the PAYE system who choose to give more.

But within the area of philanthropy and high-level gifts, we are concerned that many tax exiles regard charitable giving as their 'voluntary tax'. Charitable tax exemption should not contribute to the creation of a more inequitable society by endowments to elite, fee-paying schools, cram colleges and other enterprises, including in the health sector.

Similarly S103 of the Taxes Act 1997 is overgenerous in allowing a total write-off of the estimated value of a donated work of art against a wealthy person's tax bill, instead of a cash tax payment. Tax breaks for charities, schools and religions should be strictly monitored and controlled.

Charities & VAT

There should be a VAT compensation scheme for expenditure on equipment and services, funded from donations under the Revenue Scheme for Donations to Eligible Charities. The principle is already recognised in the treatment of VAT on charitable expenditure for exported humanitarian goods, some medical and research equipment, aids and appliances for people with disabilities and on the purchase of rescue crafts.

Corporation Tax

Forward thinking is now required on Corporation Tax. Congress recognises the value of the 12.5 per cent rate and many companies pay effective rates far below this. For example Ryanair only paid 3.4 per cent tax on €451m in 2007. This low rate of Corporation Tax gave Ireland first-mover advantage and revenue grew with the sector grew, but it is a temporary advantage.

Revenue also grew partly from Transfer Pricing (TFP) by multinationals which located profits here that were generated elsewhere to avail of our lower taxes. Congress trusts that the Commission on Taxation will deal with this sensitive issue in its forthcoming report and not pretend like Forfas and other state agencies that it does not exist.

TFP has played to our advantage to date, but it is artificial and not a real competitive advantage. As other countries reduce their tax rates, the benefit of low Corporation Tax rates is being eroded and a change in the US or other countries could eliminate its benefits overnight. Over-reliance on low Corporation Tax does not provide good long-term competitive advantage.

If the EU Single Market is to work effectively, the same rules have to apply for all companies. Tax competition has a finite life and the Commission on Taxation would do Ireland a service if it recognised this and made its recommendations accordingly.

Our position is deeply annoying to other EU member states as we are no longer poor and the Union has to formulate workable rules on taxing companies, especially mobile corporations, within a European framework. However Congress believes that broad ranges within which tax rates can to be set by member states are preferable to total harmonisation. We would be opposed to a Common Consolidated Corporation Tax regime based on point of sales, as it would be unfair to a small open economy which could face a major loss of revenue.

There is also a wider global issue. Tax avoidance/evasion costs the developing world at least US\$160billion annually, more than the total global overseas aid budget. Effective taxation policies are the key to raising the revenues necessary to achieve Millennium Development Goals. To ensure policy coherence between Ireland's overseas aid objectives and our taxation policies, Congress would like to see the Commission on Taxation recommend that the Irish government usher in a new financial climate of accountability, by taking an international lead in helping end tax abuses that are having a devastating effect on developing countries. One specific effort in this regard would be to actively support the OECD's efforts to regulate tax havens.

The Bank Levy

The government abolished the bank levy in spite of the banks being major beneficiaries from the reduction in Corporation Tax from 50 per cent to 12.5 percent. Many had expected that the bank levy would continue with the new maximum 12.5 percent rate. The levy should be re-introduced as a way of broadening the tax base.

Tax Advantages for Private Equity Firms

While private equity firms are no longer riding high, they will do so again on the economic upturn. These firms have no allegiance to regions, countries or the employees of firms they take over. These firms should not enjoy any tax advantages over normal commercial firms. Congress supports the tax deductibility of loan interest as a normal business cost, but when a private equity firm takes over a commercial firm and loads it with debt, then the state should not subsidise the takeover by allowing tax deductions on the debt interest. The UK and Denmark have already moved on this.

Taxes and Royalties on Oil and Gas

The Government decision in August 2007 to impose an additional tax on profits from oil and gas fields was welcome. However, Congress believes that a Royalty Tax on production, rather than on profits, is more transparent and easier to determine. It gives a definite return to the owners of the resources, the Irish people. Provided there is a reasonable threshold for production, this tax on output would not discourage exploration and exploitation.

Capital Taxes

Major flaws remain in a system that allows large amounts of income and wealth to remain untouched or only lightly touched by taxation, while income from work, especially by workers as employees, is taxed at the marginal or higher rate. Reform of capital taxes is essential to a fair tax system. At present inherited wealth is virtually untaxed while incomes are taxed by nearly 50 per cent for middle income workers. This grossly distorts our system of reward for effort and work.

The taxation of capital gains favours speculation and unearned income over that earned through work and enterprise. In last year's Budget statement under the heading *Rewarding Work*, the then Minister for Finance, Mr Cowen, said that Irish "economic success is driven by the hard work and the collective effort of the people." In the Programme for Government, the section on taxation entitled *A Fair Tax System* begins by stating that 'our first priority remains low and middle income earners.' The best way to assist these people is to ensure that income from all sources is taxed in the same way. This principle of taxation is the key to a fair tax system.

Tax Exiles

Revenue must act firmly against tax exiles. Time limits should be reduced especially for those who have huge trophy homes, in which they purport not to live. They are in effect stealing from the state.

Income Taxation & Excessive Remuneration

People on the minimum wages should continue not having to pay income tax and the system should be progressive. However, due to our many tax exemptions we also have

many millionaires who do not pay tax. While we welcome the new minimum income tax rate, we are still at a loss as to why those on very high incomes still will pay effective rates below those on average incomes.

Pay curbs for High Earners

It is not feasible to call for wage moderation when those at the top in the public and particularly the private sector are awarding themselves excessive pay rises. All remuneration in excess of €640,000 i.e. excessive pay, should not be deductible as a cost for companies and thus we should end the tax subsidy for making such excessive payments. This is already the case in the US and Germany is looking at a similar proposal. Taxation is a key policy instrument for reducing income disparity.

Savings and Pensions

The Government must develop a strategy for older people covering all areas of policy relevant to their quality of life, such as pensions, care, health care, housing, employment and pensions. Congress is calling for an increase and reform of the State pension, but in ways that no longer subsidise employers with integrated schemes. More needs to be done to protect defined benefit occupational schemes; and incentives created to improve pension take-up by regular workers. All of this could be part-funded by curbing tax incentives for wealthy private pension investors.

Instead Congress favours a mandatory pension scheme for all employees. Recognising the failure of the private annuity market, we hold that a State Annuity Scheme should be introduced as a matter of urgency.

PRSI Reform & Social Insurance Fund

The Programme for Government commits to abolition of the ceiling on PRSI. Congress welcomes this move, which will improve the progressiveness of the income tax system. However, it appears that the proposed reduction will also reduce the size of the Social Insurance Fund.

While Congress supports a comprehensive welfare system and retirement benefits, we are concerned that the reduction of 33 per cent in the rate of contributions for the self-employed is over-generous. There must be a full assessment of the cost and benefits to ensure the reforms are equitable.

The government promised that 'the Fund will be reimbursed by the Exchequer for the cost of this reform'. The governance of this massive Fund is very poor by modern criteria. The best way to protect the hundreds of millions of contributions from workers is the establishment of modern governance structures, perhaps with a Board of Trustees for the Social Insurance Fund with a majority of employee representatives from within the NTMA.

Any removal or upward shift in the PRSI ceiling must be simultaneously accompanied by a commensurate reduction in the rate, particularly in regard to middle income workers. The current high ceiling on pension contributions should be substantially reduced for reasons of equity and to reduce tax avoidance by high income earners.

Local Government Funding

The system of local authority funding must seek to protect local democracy. An effective system of local funding should link accountability between revenue raising and the

decisions of local councillors on funding and services. The abolition of domestic rates in 1977 weakened this link and any new proposal should bear this in mind.

Congress is strongly of the view that the privatisation of local services is not an acceptable response to the challenges of local government funding and has tended to result in weaker democratic control of the range and quality of services, higher charges, and worse pay, pensions and working conditions for staff delivering those services. T

Local government is the product of centuries of local political culture and the services provided by local authorities differ widely across countries. In most European countries, local authority funding systems are characterised by an almost universal acceptance of property-based domestic rates, business and domestic service charges, or some combination of both.

The present system of taxation on property in Ireland is fairly regressive and distorts the market, as the recent OECD report showed, but fixing it would require considerable political skill and commitment.

Congress supports the 'polluter pays' principle, but within parameters that include:

- 'Polluters' should be adequately identified at every stage in the generation of waste. Penalties should include economic disincentives on producers and distributors of unnecessary packaging and waste;
- The system must take account of ability to pay;
- The system must take account of other social and economic policy objectives;
- Any charges or penalties must be genuinely aimed at changing behaviour.
- Benefits should accrue to those who produce fewer waste products just as penalties accrue to those who produce more;
- The system should reward those who reuse and recycle waste products.

With Ireland's very low overall business tax regime, there is scope to increase central business taxes and divert resources to the local government fund and other public services. However, a better balance between central and locally generated local authority funding is also desirable.

Consideration should be given to:

- Taxing beneficiaries of local authority rezoning decisions.
- Development levies should be reviewed to ensure they raise funds from builders and speculators, rather than home buyers. Levies could be part paid by building social housing.
- The introduction of local sales taxes (for example on fuel or bed nights in hotels), which are a feature of local authority funding in some countries.
- The standardisation of waivers for domestic charges across all local authorities.
- Increases in central funding should reflect the real burdens on local authorities, rather than the CPI, including costs imposed because of central government policy decisions.
- Local authorities should have increased powers to raise funds through initiatives such as tourism taxes.

Addressing the downside of Tax Expenditures

As far back as May 2005 we made the following points:

1. Tax expenditures are difficult to quantify in advance.

2. They are subsidies and have anti-competitive effects.
3. Some property based schemes have caused urban and rural blight.
4. They can have unintended consequences
5. They have boosted construction inflation.
6. They should have a limited time span because of the adverse 'diffusion effect' which increases demand for tax breaks and makes them difficult to terminate, even when they have a negative effect.
7. Tax expenditures can be very regressive.

BES Schemes

The huge expansion of the so-called Business Expansion Scheme (BES), allowing high earners to increase their income tax write-off from €31,000 to €150,000 and to prolong the scheme for 7 years flew in the face of equity and evidence-based taxation. Congress objected to this ill-considered move, which was even contrary to the advice of government's own consultants.

The expansion of the BES was decided without an independent evaluation. Yet the government is not found wanting when it comes to talking about 'Value for Money' in health or education spending. We call for consistent and evidence-based policy making.

Future tax breaks should be reviewed prior to their establishment by the Department of Finance. If the Department does not have the expertise to do undertake this important work, then it should hire it in-house, as a matter of priority.

Emissions Trading and Carbon Tax

The EU's emissions trading scheme is largely a subsidy to industry. Congress recognises that many of the industries covered by it are large employers that provide good jobs. However, in Ireland's case, this subsidy to business comes on top of a long list of business-friendly fiscal policies including:

- Corporation Tax reduced from 50 percent to 12.5 percent;

- Capital Gains Tax halved to 20 percent;

- Employers' PRSI is the lowest in OECD;

- Introduction of R&D tax credits;

- Maintenance of an extensive list of tax shelters - although there have been moves to terminate many of them over a long time span.

While we recognise that capital is mobile and has no loyalties there must be some controls, otherwise the implications for social cohesion are severe. The issue of climate change is one which has to be addressed and taxation must be part of the solution, but it must be framed in a way which is equitable.

Evasion & Avoidance

While progress has been made in tackling tax evasion, Revenue should undertake many more tax audits. These audits generate excellent results and their wide sweep leads to further evasion being uncovered, generating a strong deterrent. The levels of evasion in the construction sector are still high and while Revenue has focused on this area, more needs to be done, particularly in dealing with bogus self employment.

The virtue of a relatively simple tax system means less room for tax avoidance. Congress would like to see the day when many of the best brains in Ireland move from tax avoidance planning to more productive employment.

Conclusion: Greater Equity Equals Greater Productivity

The growing income and wealth gap cannot continue if Ireland is to become a more meritocratic society, based on reasonably equal opportunities for all. What has been happening in recent years is dangerous for society and for the economy. The modern knowledge-based economy cannot be based on small rich elite around whom society is organized to simply to maximize their profits.

Political legitimacy in Ireland and internationally is being undermined by this new breed of super rich who want tax breaks everywhere but do not want to pay tax anywhere.

The above recommendations are in line with the ICTU submission to the Commission on Taxation. This is available on request. Below are appendices containing recent statements by ICTU on Tackling Inflation and Narrowing the Pay Gap

Appendix One: Tackling Inflation and High Prices

1. As food price rises impact disproportionately on the lower paid and families dependent on social welfare, food and fuel poverty programmes must be immediately enhanced.
2. Massive price rises for electricity and gas must be mitigated by government
3. Public transport fares and user charges must be frozen for 2009.
4. The Orwellian attempt by the government to underplay inflation by ordering to use the HICP instead of the Consumer Price Index should cease forthwith.
5. The falling value of wages, combined with slowing employment growth, has hit retailers and other businesses hard, underlining the case for real wage increases above the rate of inflation.
5. There has to be Government recognition that Irish consumer price levels are far too high. For consumer goods, Irish prices are 14 percent higher than the average in the 27 EU states, but for consumer services, they are a staggering 31.2 percent above the average. This must be addressed.
6. An immediate reduction in VAT by 2 percentage points. This would reduce inflation by almost 1 percent i.e. from 4.7 percent today to 3.7 percent. It could be paid for by a rise in income tax for those earning over €120,000 a year and ending all the many property and other tax breaks, especially those for private hospitals and clinics.
7. The remit of the National Consumer Agency should be immediately strengthened to enable it to police the passing on of the reduction to all consumers. It needs to a) investigate price fixing and, b) take vigorous action against excess profit-making by wholesalers or retailers, especially for food including groceries and petrol and diesel.
8. The government should not continue to make major gains from soaring fuel costs. It should eschew any further rise in taxes on fuel while oil remains at over say, \$125 a barrel, for a specified period of time.
9. There must be publication of the accounts of all Irish supermarkets and other 'public interest companies' to assist transparency in assessing their prices and profits.
10. Move to address the growing pay gap, in both the private and public sectors.

Appendix Two: How to Narrow the Pay Gap

1. Terminate tax subsidies for executives big salaries, like the US has since 1992. In the US, senior all executives of publicly held corporations have to declare if their total remuneration exceeds \$1,000,000 a year (c. €640,000) and profits.

This practice should be immediately introduced in Ireland for all companies, public and private. The limit should be set where executives are paid more than 15 times the average industrial earnings.

The excess over that sum would no longer be deductible against tax as a cost. This would mean that any excess executive remuneration payment would not be subsidised by the ordinary taxpayer.

It should include *all* remuneration such as share options (whether exercised or not), deferred compensation, all forms of bonuses and benefits of all kinds, with the exception of pension contributions and tax subsidies. In short, if board of a company wants to pay executives huge salaries, bonuses and share options, then the company should pay excessive remuneration from profits.

2. Reduce the ceiling on the amount of tax subsidies top executives can claim by limiting the ceiling on annual pension investment to three times industrial wage as per Congress' Budget Submission of November 2007. There is a strong case to limit this more with the subsequent revelations on the gap between top executive remuneration and ordinary workers. Why should the rest of us subsidise their pensions though overgenerous tax breaks?

3. Place a cap on executive pay by not allowing bonuses to exceed one-third to one half of salary.

4. Reform company law on transparency of executive remuneration with tighter legislation for all large companies in Ireland. It should be similar to the SEC in the US, where there is a clear statement of annual remuneration for top executives with *a single total figure* for the year, with simple disclosure rules covering all top executive remuneration, including pensions, share options, chauffeured company cars, use of helicopters, aeroplanes and other benefits. This should apply to all senior positions in the public sector too.

5. A law should be introduced to set broad parameters under which top executive pay is set by company boards which will establish objective criteria, including financial performance, employee welfare, consumer satisfaction, environmental protection, etc.

6. Consideration must now be given to the appointment of real outsiders as non-executive directors appointed to boards of major companies, either by a government appointments body or an investor grouping, or by a pension fund, or even by worker representatives. This is needed in the light of the excessive remuneration and poor performances by many of those at the top of the corporate world.

7. There should be an oversight group (of independent persons including employee/union representatives, pension funds, consumers, government nominees, citizens, etc.) which ensures that top executive pay packages of all large Irish companies annually comply with the criteria set out in this section.

8. Reform Irish Company law to make it more transparent, by removing the option for all large companies to avoid disclosure by:
- a) going unlimited or
 - b) by merging Irish businesses into European consortia or
 - c) by any other means.

All public interest companies should have to disclose the full accounts of individual subsidiaries deemed to be of interest to the public. Congress holds that the Irish subsidiaries of European companies which are public interest companies should no longer be able to lump all their assets and sales into one big company.

9. Companies should no longer be allowed to operate in Ireland by profiting from activities here if they are registered in tax havens such as Liechtenstein or the Bahamas, without also having an Irish registered base and disclosing all information in accordance with Irish law.

10. There is a strong case for imposing a higher tax rate on very large incomes, when we recognise that there are many who 'earn' a million a year or more.

11. A systematic and vigorous pursuit of Irish tax exiles must begin now, to ensure that they are tax compliant on residence and domicile grounds.

The net impact of these reforms will be to:

- a) Reverse and reduce the widening pay gap in Ireland;
- b) Reduce tax subsidies to excessively paid top executives in the private sector;
- c) Help rebalance the relationship between executive performance and corporate performance;
- d) Greatly improve transparency;
- e) Boost productivity by improving workers' attitudes in a fairer workplace / society.