The Irish Economy and its Tax System: Implications for Northern Ireland

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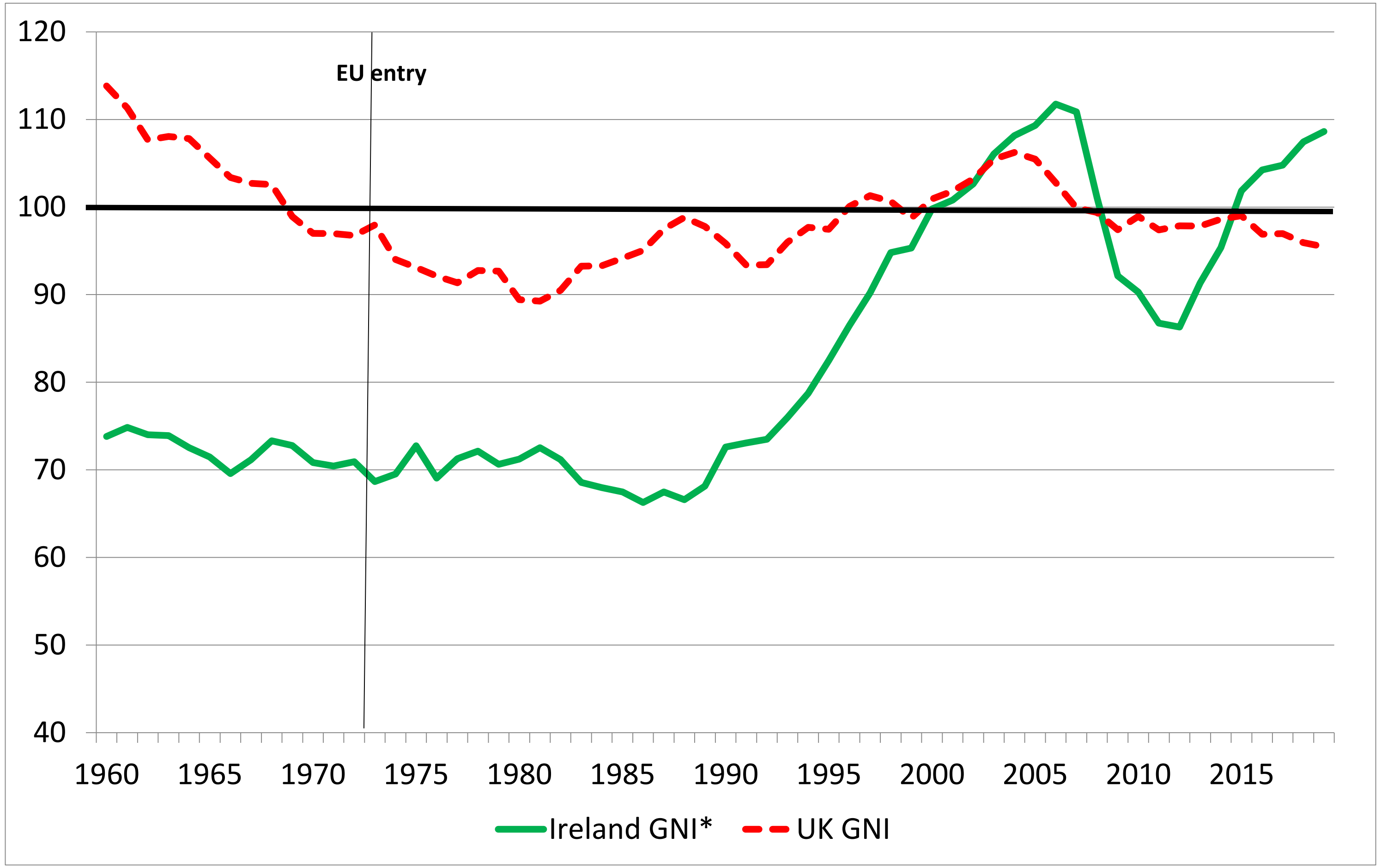
Outline

- The Structure of the Irish Economy
- Corporation Tax
- Indirect Tax
- Direct taxation and the Labour Market

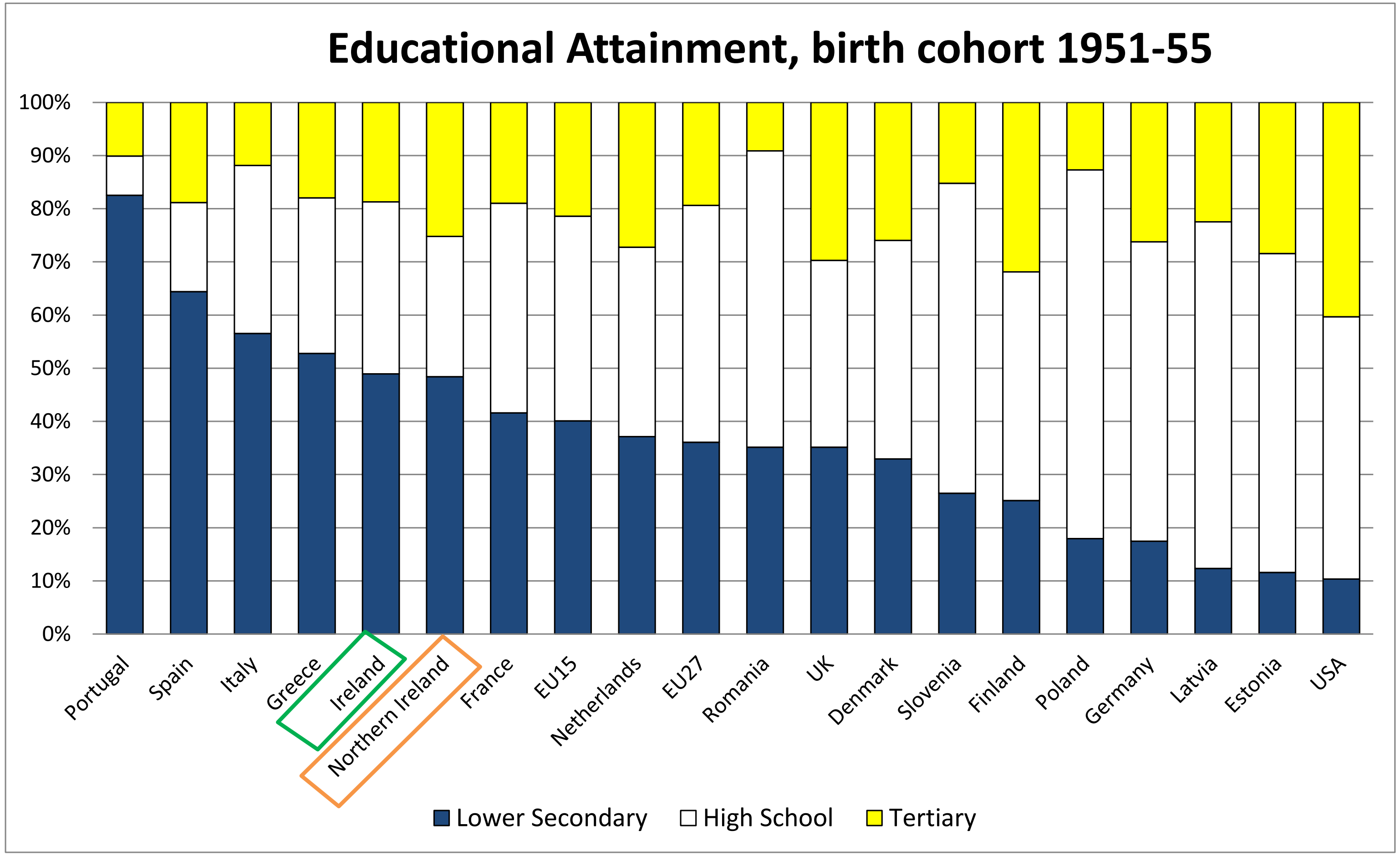
Irish Economic Convergence, GNI per head, PPS EU15=100



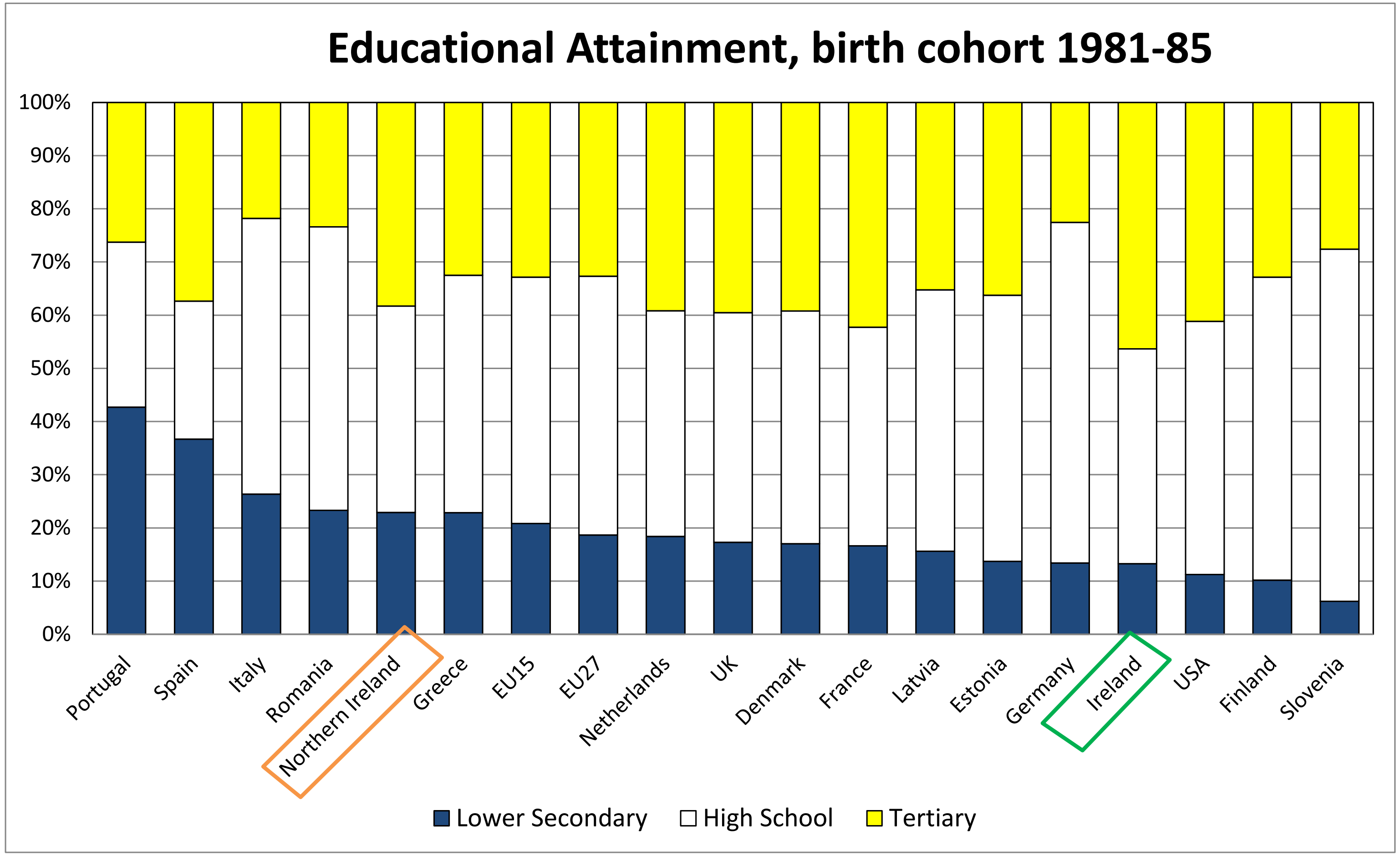
Convergence story

- The surprise was Ireland's failure to converge post-War
- Rapid convergence post-1990 because changed failed polices
  - Failed to adopt free trade in 1945. EU entry 1973
  - Failed to invest in education like rest of Northern Europe
- Benefitted from globalisation within the EU
  - FDI – Corporation tax important in 1970s and 1980s
  - EU Single Market 1993 very important
- Today Labour Force skills vital. Specialised into tradable goods and services with a high income elasticity of demand

Education – cohort of 1951-5



Education – cohort of 1981-5



Measuring national output and income

- GDP: from that deduct profits of MNEs
- GNI: problem it includes the depreciation of the MNEs
  - Huge depreciation on IP of MNEs and aircraft (of aircraft leasing companies)
- GNI* Adjusted GNI – after deducting much of depreciation of MNEs
  - Broadly comparable to GNI for other countries
- NNP deducts all depreciation – probably a better measure but not widely used internationally. Thus usable for understanding the economy but not for measuring relative performance

Measures of Growth

	2014	2015	2016	2017	2018	2019	Average Annual 2013-2019
NNP adjusted for redomiciled PLCs	**8.0**	**3.7**	**5.5**	**2.3**	**7.1**	**3.9**	**5.1**
NNP	7.8	1.5	6.2	1.3	7.3	3.2	4.5
GNI* from NIE	**8.8**	**-0.3**	**5.9**	**4.6**	**6.8**	**1.7**	**4.6**
GNI from NIE	8.8	13.7	7.5	6.3	7.3	3.4	7.8
GDP from NIE	8.6	25.2	2.0	9.1	8.5	5.6	9.6
Modified Domestic Demand	6.2	5.4	6.1	3.0	2.5	3.5	4.4
Employment	**2.6**	**3.4**	**3.6**	**2.9**	**2.9**	**2.9**	**3.1**

Contribution to Growth, by industrial sector, constant prices 2013-2019, %

	Total	Foreign	Domestic
Agriculture, forestry and fishing	3.2	0.0	3.2
Industry	8.4	3.8	4.5
Construction	9.0	0.0	9.1
Distribution, transport, hotels and restaurants	18.3	6.1	12.2
Information and communication	14.3	6.6	7.7
Financial and insurance activities	3.6	0.3	3.3
Real estate activities	6.0	-0.1	6.1
Professional, admin and support services	19.2	5.8	13.4
Public Admin, Education and Health	9.8	0.1	9.7
Arts, entertainment and other services	2.5	0.0	2.6
NNP after profit repatriations	94.4	22.5	71.8
Factor Income - other, excluding Redomiciled PLCs	-5.6	1.1	-6.8
NNP adjusted for redomiciled PLCs	100.0	21.4	78.6

Government Revenue, % of GNI*

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Direct taxes	**22.6**	**25.1**	**26.0**	**24.8**	**24.6**	**24.7**	**24.1**	**23.9**	**24.8**	**24.6**
of which										
Income Tax	7.1	7.8	8.3	8.1	10.9	10.5	10.6	10.3	10.4	10.4
Corporation Tax	3.1	2.8	3.3	3.1	3.1	4.2	4.2	4.4	5.2	5.1
Social Insuramce contributions	7.4	8.6	8.4	8.1	7.9	7.6	7.5	7.5	7.5	7.4
Indirect Taxes	**14.0**	**14.1**	**14.5**	**14.1**	**14.3**	**13.8**	**13.4**	**13.2**	**12.9**	**12.8**
of which:										
VAT	7.8	7.7	8.0	7.5	7.5	7.3	7.1	7.1	7.1	7.1
Excise	3.8	3.9	3.8	3.6	3.4	3.4	3.3	3.2	2.7	2.7
Total Taxes	**36.6**	**39.2**	**40.5**	**38.9**	**38.9**	**38.5**	**37.5**	**37.1**	**37.7**	**37.4**
Total Revenue	**42.9**	**46.0**	**47.6**	**45.4**	**44.9**	**44.2**	**42.7**	**41.8**	**42.2**	**41.7**

Profits share and Corporation Tax

	Profits as % of GVA		Share of Corporation Tax
	2008-2012	2014-2018	2017
Germany	40.3	50.5	2.5
France	54.0	59.3	2.3
Other EU		63.8	9.4
UK	39.0	50.1	4.0
US	81.3	91.6	56.8
Japan	68.0	83.5	1.9
Domestic	32.5	45.4	20.2
Total	71.6	84.5	100.0

Corporation Tax

- Originally low corporation tax attracted FDI employment to Ireland
- Non-US firms not permitted to exploit opportunity by domestic tax authorities
- Bulk of corporation tax is paid by small number of US firms
- Exceptional profit margins because location of IP in Ireland
- In individual companies, such as Apple, IP held by separate subsidiary from company employing large numbers in Ireland
- Employment decision separable from where IP is held and tax paid (or not paid)
- Trump tax reform may have benefited Ireland because GILTI rate 10.5%
- Very vulnerable to changes in US tax law – e.g. proposed Biden reforms?
- OECD process would have impact. Department of Finance estimate up to €2bn
- With US tax reforms total of €6bn could be at risk: c. 3% of GNI*, but direct employment impact likely to be low

Indirect Taxes

- Undue dependence on stamp duties on property before 2008 crisis
  - Since then greatly reduced
- Two major tax heads – VAT and Excise – c. 10% of GNI*
  - Carbon tax of €33.5 a tonne rising to €100 a tonne by 2030
  - Revenue hypothecated for tackling climate change and compensating losers
- Carbon price floor not applied in Northern Ireland.
  - If it had been it would have forced the Republic to follow suit which would have been good for climate change
- Periodic concerns about revenue loss across border
  - Concerns also about "fuel tourism" adding to Irish emissions
  - Studied in 1980s and 1990s North and South of border

Cross-Border Shopping

Table 1: Extent of Cross-Border Shopping

Country	Border Region	Year	Proportion of Expenditure Regional %	National %
Ireland	Border Counties	1986	10	2
Denmark	<50 kms	1985	3	1
Denmark	Sonderjylland	1991	5.7	0.9
Netherlands	Zuid-Limburg	1991	8.5	0.6

Cross-Border Shopping

Table 3: Maximum Distance Irish Shoppers Will Travel, Kilometres

	Price Difference, %			
Size of Shopping Bundle, ECU's	2.5	5	7.5	10
100				
125				5
150			5	10
175			5	20
200			10	20
225		5	10	30
250		5	20	30
275		10	20	40
300		10	30	50

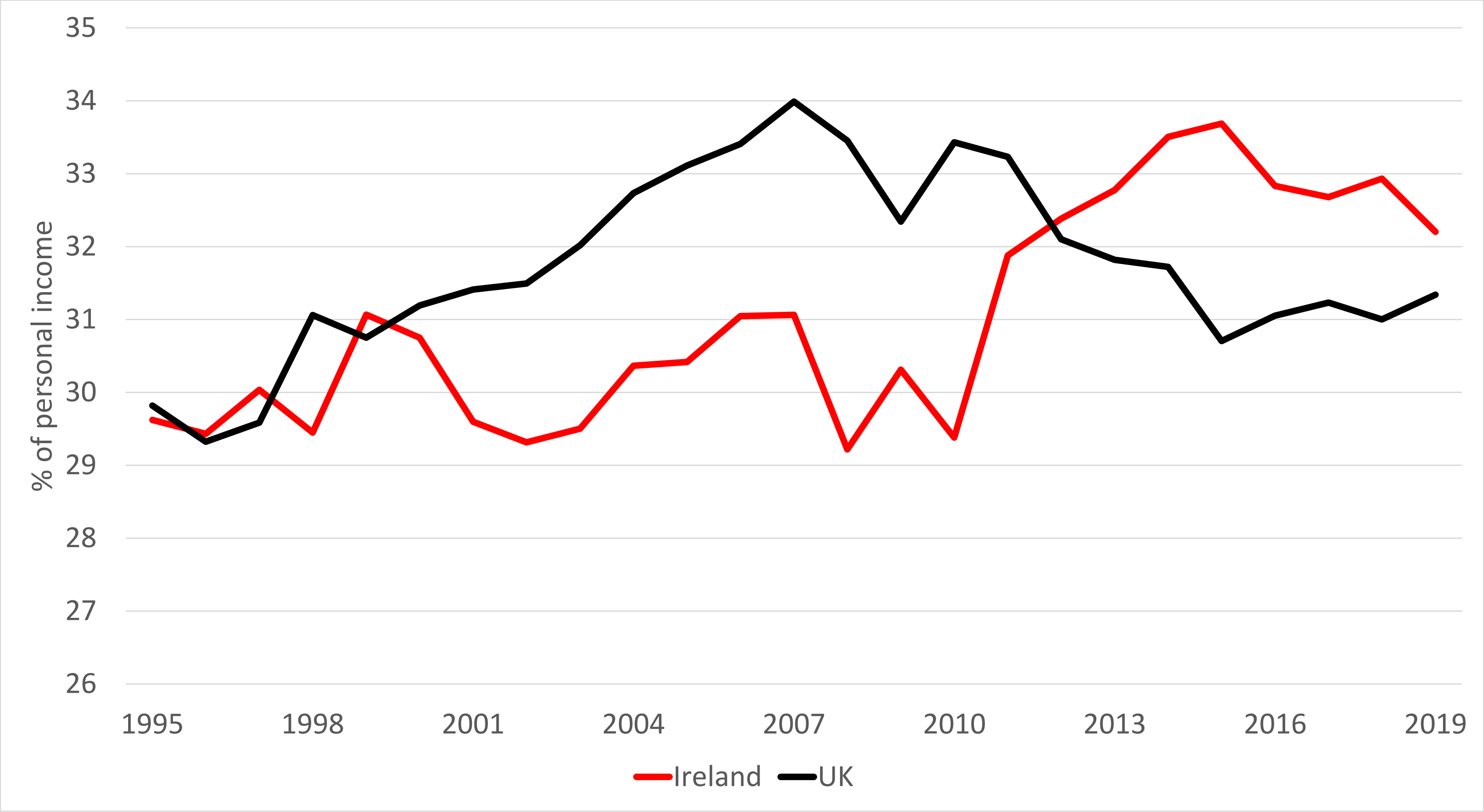
Conclusions: Not a major constraint on independent action

However, fuel "laundering" on the border has been a serious trigger for crime

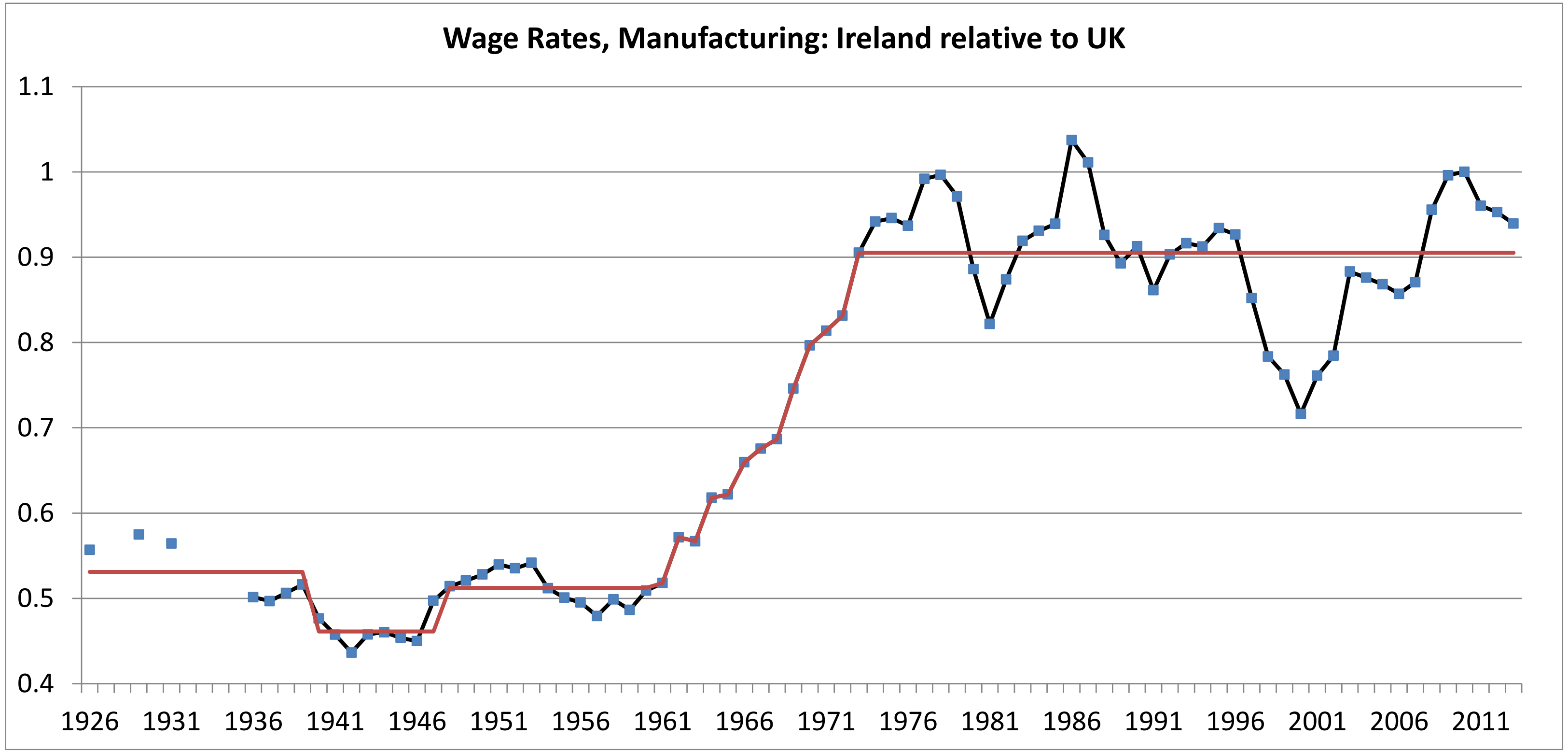
Direct taxation and the labour market

- Ireland had low average tax rate up to financial crisis. Rose substantially post 2009
- Most of direct tax is paid by those in top half of income distribution – very progressive
- Ireland has been part of British Isles labour market for 150 years
- Over a long period Irish wage rates were determined on that market
- Up to 1960 Irish wage rates were 60% of UK
- Between 1970 and 2010 similar wage rates
- Modelling suggested that over that period Irish people would work in Ireland for c. 90% of the real after tax GB wage. This drove migration in both directions
- Pushed government to cut marginal rates of income tax in late 1980s to avoid brain drain
- Since late 1990s Ireland has attracted major immigration of skilled labour

Average personal tax rate



Ireland v UK, Wage Rates



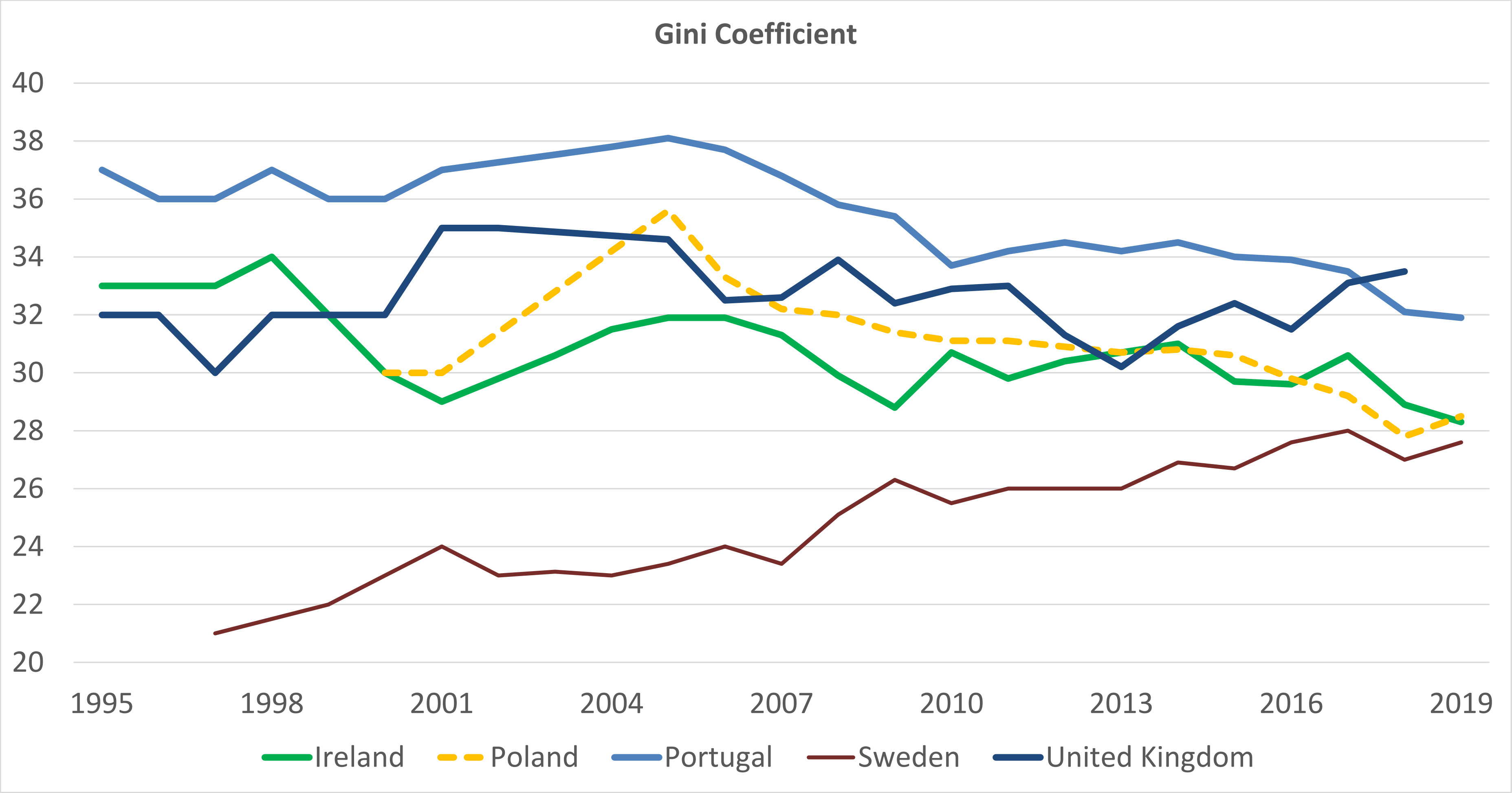
Relative average earnings by education

Ireland relative to UK, %

	2002	2018
All Employees	94	115
Lower Secondary	99	97
Upper Secondary	98	101
Third level	80	114

Northern Ireland average earnings are, in turn, 90% of UK average earnings
However, in spite of the difference in earnings, there is very little cross-border Labour movement from North to South

Income distribution – after tax and welfare



Implications

- Corporation tax – if there was ever an opportunity for Northern Ireland it is over
  - Research for DETI shows that educational attainment is a major driver of FDI
- Surprisingly the Northern Ireland labour market seems less part of the British Isles labour market than the Republic. The effects of direct taxation on labour mobility is probably low
- Indirect taxes – cross border effects limited. However, in tackling climate change, lack of co-ordination within UK and on the island could be problematic. Need to price carbon across the UK. Could Northern Ireland go it alone?
- Other possible fiscal instruments
  - Water charges, public service obligations , local property taxes
  - Can provide some additional fiscal space but first two are regressive and Northern Ireland cannot offset this with changes in welfare
- Obviously on expenditure side Northern Ireland has some scope to make better use of its resources