



Submission to Commission on Taxation

By the Irish Exporters Association 2008

Introduction

The Irish Exporters Association (IEA) welcomes the opportunity to submit the views of export industry, which includes both manufactured goods exporters, as well as services exports, and the industry sectors that support international traders. This latter category includes shipping and logistics services providers.

The Commission has requested structured responses to its specific questions on the structure, efficiency and appropriateness of the Irish taxation system. The IEA note that the work of the Commission will set out the framework within which tax policy will be set for the next decade at least.

The IEA has addressed these questions in the sections below.

Section. 1. Consider How best the tax system can support the economic activity and promote increased employment and prosperity , while providing the resources necessary to meet the cost of public services and other Government outlays in the medium and long term?

Irish exports peaked in 2002. In the years since, Irish exporters have faced major challenges in many key markets. Some challenges were as a result of extreme fluctuations of the US Dollar and the Japanese Yen, the continued link of the Chinese Yuan to the falling US Dollar, and the continual appreciation of the Euro.

Some challenges were as a result of rampant home-based cost increases. Average hourly earnings in Irish manufacturing industry were 18% above our major trading partners in 2003. By 2007, Irish industrial earnings had increased by 22% whereas our main trading partners were still paying out at below the Irish level for 2003. Electricity and gas costs have equally risen much faster than in our main European competitor countries.

Further challenges have arisen as a consequence of the success of our export growth in the decade up to 2003, such as congestion on the roads and into the sea ports and airports. These have added supply chain stock costs to the rising production costs.

In the past 12 months the extraordinary boom in demand from Asia for a wide range of commodities and the switching of agricultural output into alternative energy fodder have pushed many basic commodities such as milk powder, whey and lactose, upwards by 44%. This has affected many added-value food producers and exporters in Ireland.

Services exporters who now account for 43% of total exports are amongst the most aggressive of the firms building new export business from Ireland. They equally face the challenges arising from rapid inflation in labour costs, rent and the creaking infrastructure.

- **Hence, the first message from Irish exports to the Commission on Taxation is;**
 - **Don't introduce any additional taxes or indirect charges which will inflate the cost of labour, electricity, gas, fuel or rent and rates in Ireland.**
 - **As business people, exporters are only too well aware of the pressures the Government will come under to balance the budget as revenue returns from a declining property sector impact in 2008/2009. However, we would strongly urge the Commission to look at consumption taxation (VAT) rather than direct taxation increases to balance any budget deficit.**
 - **Competitiveness of the economy and, in particular, the export sector will depend heavily on keeping labour costs down.**
- NOTE: The IEA submission is not addressing certain issues which are not core mission concerns to members, such as the Commission request for inputs on Pension.

Section .2. Examine the balance achieved between the taxes collected on income, capital and spending?

The IEA notes that the Commission is not looking for views on Corporation tax, and that the Commission's contextual framework carries a guarantee that the 12.5% corporation tax rate will be maintained.

The IEA is strongly of the view that Ireland's taxation system is a very important competitive advantage for Irish export industry, however, we are not alone in offering an attractive taxation regime and that we must continue to develop and build on the existing system. The IEA recommendations below are provided in this context.

2.A . Income tax and skilled labour attraction.

With workers and companies becoming increasingly internationally mobile, it is essential that the existing policy of keeping a low income tax regime in place must not only continue, but also be adjusted to facilitate the attraction of the higher skilled workers needed for the knowledge intensive industries we are now attempting to build in Ireland.

Irish industry faces strong competition internationally for highly skilled staff that are required in our services industry sectors and our advanced manufacturing sectors.

There is a need to attract Irish people to continue to work out of Ireland on export activity, and also attract Irish people living abroad to return to Ireland and participate in export activity. This was identified in various Government sponsored studies, including 'Ahead of the Curve' report by Forfas.

- **The IEA recommends to the Commission to assist the retention of Irish nationals, and the focus on working for regular periods of 5 days working out of Ireland in pursuit of export sales, that they be given a tax incentive to compensate for the unsocial-able requirement to spend continuous periods abroad. The tax incentive that was in place was removed in 2003, was seen as a retrograde move. The IEA recommend that a scheme similar to that in operation in the US would be a good model to adopt. Hence, the first 80,000 euro of earnings should be allowed tax free, if more than 50% of the working year is abroad, regardless of the length of individual periods abroad.**

The remittance basis of taxation was a highly attractive proposition to enable Irish based companies to bring in skilled workers to Ireland. Under the scheme, an individual resident, not domiciled in Ireland (e.g. a citizen of Germany, working and regarded as a tax resident in Ireland), was liable for Irish income tax on his Irish remitted income, but not on his "foreign" income.

This scheme was abolished in January 2006 and has had a negative impact of the ability of MNCs and Irish indigenous companies to attract key staff required in areas such as financial services, hi-tech manufacturing and engineering services.

If we want high-value jobs in Ireland we have to attract in high skilled professionals. These people are used to imbue their skills through working with and mentoring other local staff. In this way, knowledge is passed on to create the knowledge economy we are now moving into.

- **The IEA recommends to the Commission the re-introduction of the Remittance Taxation scheme for foreign professionals. We fully accept that the enabling legislation should have safeguards, such as maximum tenure and definition skill types allowable, to avoid abuse.**

2.B. With-Holding tax Legislation is not Competitive

The benefits of placing high added-value and strategically important business functions in Ireland such as head quarters or R&D centres and regional head offices are well known. However, the international competition to attract foreign multinational corporations' strategic business functions has increased. But so also has the nature of fast-growing indigenous Irish companies who primarily trade internationally, and these companies are also faced with competitive pressures to locate HQ activities abroad.

Holding international operations from Ireland currently has attractive features such as:

Exemption from capital gains on the sale of shares by the Irish company

Where 5% or more share ownership participation is held in a company, profits realised from the sale of that company can be re-invested or used to acquire new business without any Irish tax cost

Access by the Irish holding company to EU tax directive incentives, such as elimination of tax on dividends received in Ireland

In this submission the IEA wishes to draw to the attention of the Commission, the need to extend the advantages to countries other than the EU countries and countries with whom we currently have double taxation agreements with.

Currently Ireland has double taxation agreements with approximately 44 territories.

However, the UK has agreements with 112 territories approximately, and the USA 120 territories approximately.

Hence, a company locating its HQ in Ireland has to pay 12.5% on profits in a wide range of territories, compared to locating the HQ in London, for example.

This situation will come to a head for a range of companies currently on 10% corporation tax, but due to lose this in 2010.

- **The IEA recommends to the Commission to introduce a tax exemption regime for a list of territories (a "White List"), agreed with industry as key trading countries, other than those currently covered by the double taxation agreements.**
- **The IEA recommends to the Commission to introduce a "Pooling" arrangement for royalties so that they can be paid in territories not included in the Double Taxation agreements. This would benefit particularly pharmaceutical and software corporations. The idea is to pool all overseas territories and their income as one, and tax would apply only on Irish profits.**

2.C. Intellectual Property (IP)

The stimulation of innovation is widely accepted as critical in the development of a competitive economy, and business investment, and business investment in R & D, and the acquisition of Intellectual Property by industry plays an important role in this context.

The Government has substantially improved the treatment of IP from a tax point of view in recent budgets, reflecting IEA submissions on behalf of the export industry. However, there remains an anomaly which the industry requests the Commission to address as follows;

- **Many businesses find that the current regime provides incentives for them to acquire technology licences, but does not incentivize them to actually acquire outright the intellectual property being targeted for their company.**
- **As a long-term investment, purchasing high quality new IP outright offers Irish industry a stronger Irish base for new product development and sales**

exploitation. Hence, we ask the Commission to exempt the acquisition of IP as an outright function from taxation.

2.D. Business Expansion Scheme – Fine Tuning

The government has made significant steps in reducing the range of incentives in place that supported investment in property. The IEA recommends to the Commission that this trend should be continued, as property investment has taken away the incentive to invest in productive industry over the past decade. The IEA commends the success of the Department of Finance in the recent clearing of the expansion of the BES scheme with Brussels.

However, we are concerned that the EC negotiation has had the effect of dramatically reducing the usefulness of the scheme for the productive sector of business.

Most productive businesses that have availed of the BES scheme have been export oriented and have received early stage grant aiding from the State agencies. They then proceed to seek second stage funding from the private sector through BES schemes.

- **The IEA recommends to the Commission action to ensure that the extended BES scheme does not exclude companies on the basis of having prior receipt of State grant aid.**

Section .3. Reviewing all tax expenditures with a view to assessing the economic and social benefits they deliver and to recommend the discontinuation of those that are unjustifiable?

The business community, as a user, and a funding source for the Public Services, has a strong stake in the cost and efficiency of government. There is strong concern amongst exporters that the benchmarking payments to the public sector are not being matched by efficiency gains. And in the case of retired civil servants, payment of benchmarking increases obviously cannot be justified on the basis of efficiency gains and therefore should be removed from all future reviews. For those at work in the Public sector, the level of detail provided in terms of efficiency targets set and achieved varies significantly between government departments. These benchmarking payments with clear efficiency plans, with milestones and timeframes as to how each department will seek to achieve its targets should uniformly be in the public domain, if the public and business community are to have confidence in the robustness and attainment of return for pay increases are to be accepted.

The available statistics show that public sector growth in employment was 6.4%, an increase of 25,000 over last year. It is clear that the commitment to control public sector employment has not been kept.

Exporters find themselves in competition with the public sector for skilled staff who are being attracted by rapidly increasing average earnings. There is not doubt among exporters that the state sector is pushing up the wage rates in the open market and adding to the private sector's difficulties in curtailing wage cost increases. The Taoiseach in his role as Minister for Finance has stated in the past

'Our approach must balance the wide range of competing priorities and focus on developing efficient and cost effective public services that are consistent with sustainable economic growth'

In this regard, the IEA urges the Commission look at measures to improve the business

climate by reducing the total administrative burden, simplifying and improving the quality of legislation and creating an environment more supportive to business.

Section .4. Investigate fiscal measures to protect and enhance the environment including the introduction of a carbon tax.

There is a real concern amongst exporters that the Programme for Government, driven by a Green agenda and EU policies to reduce carbon emissions are likely to lead to significant increases in costs to vulnerable manufacturing industry, and to generally lead to increases in road, sea and air transport cost. The Irish Exporters Association strongly advises the Commission that it will be necessary to take into account the competitive position of manufacturing industry in relation to non EU competitors such as China and the US, as well as the peripheral nature of the island, when implementing any of the EU Directives, as carbon taxes will inevitably bear most heavily on older manufacturing industry and longest distance road movements.

4.A Manufacturing Industry

The IEA wishes to bring to the attention of the Commission that businesses are already facing increasingly higher energy costs, both because of global fuel price increases, as well as the particular lack of nuclear options in the Irish electricity cost make up. Many industry sectors cannot take any further cost increases that put them at a competitive disadvantage to other country locations with which they are competing.

- **The IEA recommends to the Commission that they take into account the Forfas research in this context and proceed with any introduction of Carbon taxes at a very low level, but also offset this with incentives to introduce newer equipment with lower carbon emissions.**

Companies already engaged in Carbon trading should be exempted from any new taxes and again incentives to participate in binding energy agreements should go hand in hand with any new legislation.

4.B. Transport and Logistics Sector

The Irish Exporters Association also wish to state at the outset that an all island approach to sustainable transport will be essential, to avoid an environmental divide arising in transport of goods across the island.

The IEA restate a long held view that efficient transport infrastructure is central to our export competitiveness and the economic well-being of the country. The IEA also accept that environmental issues must now be addressed to ensure a sustainable, efficient transport system for the future.

However, to ensure a sustainable infrastructure for the foreseeable future, there is a need to fully understand

- Freight trends
- Drivers of emissions from the transport sectors
- Impact of new technology investment, and
- Impact on competitiveness of merchandise exports and imports.

>Freight Trends

There are a number of issues which affect demand for transport. Official statistics gathering exercises have regularly failed to fully grasp the key drivers of transport demand and hence continuous infrastructure planning below requirement takes place. For example actual

growth rates for unitised traffic in Ireland in 2005 and 2006 ran at double those predicted in the Fisher report commissioned by the Dept of Transport.

The shift in industry demand for supplies from the Far East and the need to replace empty containers back into the supplying country has major implications for volumes of traffic movements.

Size of ships internationally are growing, this brings in it's wake larger peak demand volumes for transport in and out of ports, but also restricts the ship service to fewer ports with large ship capability.

These are but three areas impacting the industry demands but there many others which need full research.

>Drivers of emissions from the transport sector

The freight trends stated above drive much of the emissions from transport industry.

But age of the fleet and engine types also impact. So also does simpler things such as air pressure in tyres, and truck overloading.

>Impact of Technology investment

There has been an established utilisation of low emission ethanol fuelled vehicles in wide-spread use in Brazil for over a decade .This involves new technologies which Irish industry is not familiar with, nor able to access. Solutions of this kind should be promoted and made available, in line with any drive to tax higher emission transport.

Concluding on this point, efficient transport is essential to the competitiveness of Irish merchandise exports. It is particularly important to an island nation which reaches the bulk of it's market by roll-on roll-off transport through seaports.

Any actions to improve the emissions record of the transport sector must be based of better studies of the real trends in freight and what is driving.

The NDP 2007-2013 and Transport 21 are intended to support the National Spatial Strategy.

However, they fail to address many of the sustainable transport issues now facing us, as the focus is almost exclusively on people movement. The NDP has no capital investment earmarked for ports and Transport 21 almost totally focuses on people movement, ignoring the needs of freight transport.

- The IEA submit that many of the congestion issues which are a constant feature of the greater Dublin area are brought about by lack of:
- Rail freight connections to the main sea port
- Poor port connectivity to the road network
- Lack of quality, priority freight routes

The issues affect rural as well as urban route congestion, with the consequent emissions problems.

Freight transport is a derived demand and, as such, must be studied by the sectors that cause the demand.

The changing nature of our economy has seen import volumes of finished furniture, clothing, household goods and packaged foods increase greater than export volumes. Import volume is now over one third higher than export volumes. Exports have grown most rapidly in the chemical, pharmaceutical, medical devices, electronic and computer sectors, where higher values and lower volumes typically apply. Sophisticated logistics linked to production systems are more important to the sector than minimisation of transport cost.

However, other sectors such as the added value consumer foods (pizza, for example) rely on high volume, low cost transport to the UK and European markets to stay competitive.

The construction sector has grown to a very significant volume of total tonnage carried on Irish roads in the past decade. The impact and requirement of the sector need separate analysis.

The type of vehicle used for freight transportation has also changed over the decade, with larger vehicles with more axles growing at the fastest rate. Tonnes lifted by 4+ axle rigid vehicles has tripled in volume, compared to 74% growth of smaller rigid vehicles. The same trend occurs for articulated vehicles, with the largest growth of 6+ axles.

All these issues must be taken into account when determining any environmental policy initiatives.

The IEA summarises the key points of it's recommendations to the Commission on the introduction of any environmental taxes for the transport and logistics sector as follows;

Irish industry has show itself to be very responsive to fiscal incentives to achieve change. Hence, the IEA recommends to the Commission that it adopt an incentives approach to engendering a spirit of adoption of Climate Change in the Transport and Logistics sector along the following lines:

- Emissions trading schemes, to encourage each company along the supply chain to enter into voluntary programmes to reach zero emissions by 2020, inclusive of clear advice on how to enter into an emissions trading scheme.
- Continue rebalancing of vehicle registration tax and motor tax towards more fuel efficient vehicles with less CO2 emissions.
- Introduce Tax incentives to encourage the purchase of vehicles capable of using bio fuels.
- Congestion charges if introduced should also have "free time" where there is low traffic volume, to encourage change to outside peak traffic periods for freight vehicles.
- Introduce Tax incentives for rail freight use
- Tax incentives for short sea shipping use, as opposed to inland road haulage to major ports with larger ships.

These recommendations can be elaborated upon below, if the Commission require more information.

END.

For further information contact:

John Whelan, Chief Executive, Irish Exporters Association
Tel: (01) 6612182
Email: jfwhelan@irishexporters.ie