

**ADDENDUM TO THE  
IRISH HOTELS FEDERATION  
MAY 2008 SUBMISSION TO THE COMMISSION ON TAXATION**

**FEBRUARY 2009**

## **Introduction**

The Irish Hotels Federation made a submission to the Commission on Taxation in May 2008. Since then the tax revenue generating capacity of the Irish economy has been greatly reduced, While some of this reduction is due to the recession stage of the business cycle, a large part is due to a fundamental structural reduction in the tax revenue capacity of the economy because of the decline in construction activity. This decline will not be reversed in the medium to long term. Consequently the economy faces many years of substantially lower tax revenues than were envisaged at the time when the Commission was established.

While the terms of reference of the Commission are unchanged the reality of the changed taxation revenue could lead to the expectation that increasing the tax yield may be a more important element of its deliberations than originally envisaged. Originally the Commission may have been mainly focused on the structure and internal consistency of the tax system within the context of keeping the “ overall tax burden low”.

In light of that changed tax revenue situation the IHF would like to submit this addendum to its original submission. The thrust remains the same but the addendum takes account of the greatly changed economic and fiscal circumstances.

## **Changed Tax Revenue since 2007**

The Commission was established in February 2008. In December 2007 the Government’s 2008 budget projected a tax revenue of €51.8B in 2009. Currently the Government’s expectation(as of January) for 2009 is €37B. This is a decline of 29%. Independent commentators expect that the eventual tax take will be less than €35B in 2009. The Government expects that the 2013 tax take on current rates will be €42.9B even after three years of economic growth. This is substantially less than the 2006 outturn of €45B.

## **Guiding Principles**

There are two alternative principles for deciding on the appropriate national tax burden. One could identify the desired level of public services and design the tax system to finance that level of services. Alternatively the emphasis could be on the maximum tax burden which would sustain and increase economic activity and employment. The level of expenditure would be determined by the tax resources available under this expectation. The Commission’s terms of reference are not clear on which principle is to be adopted. They refer to the commitment to “keep the overall tax burden low” and to consider “how best the tax system can support economic activity and promote increased employment”. But they also refer to “providing the resources necessary to meet the cost of public services and other Government outlays in the medium and longer term”.

The IHF recommends that the Commission’s deliberations should be governed by the principle of keeping the overall tax burden low and supporting economic activity and employment. In light of the reduction in tax revenues and the high levels of borrowing

the IHF recognises that keeping tax low will require substantial reductions in public expenditure.

The IHF recognises that the scale of the public financial adjustment required over the period to 2013 can not be borne by expenditure reductions alone and that there will have to be tax increases which may not have been expected when the Commission was established. However, the bulk of the adjustment should be through expenditure reductions.

As is generally recognised unemployment will reach 15% in 2010 and employment will decline in 2009 and 2010. Consequently there will be a substantial need to foster economic activity and employment creation over the next few years. The tax recommendations and tax structure should support that requirement.

The Commission should identify the maximum level of national tax burden which supports the scale of economic renewal needed by the Irish economy over the next few years. The Commission should recommend that this level should not be exceeded. This level will be substantially below the levels of many other EU economies because of Ireland's need to attract foreign direct investment, the lack of a strong indigenous international industrial sector, the mobility of the labour force, the role of international tourism and the land frontier with the low VAT UK.

The IHF is concerned that the Commission may recommend that the reduction in tax revenues should be reversed by increases in rates of tax and new taxes to support the current level of public services. In the IHF view this would have very serious negative consequences for enterprise development and employment generation and would be disastrous in the current and future Irish economic circumstances.

### **New Tax Revenues**

The IHF recommends that new tax revenue should be collected through a universal property tax but this revenue should be used to reduce borrowing and should not be an addition resource for extra spending by local authorities. Until such time that the government's target of eliminating the current budget is achieved, income tax rates should be altered to collect additional revenue and to bring about a greater degree of progressivity in the income tax system. At salaries above €250K the marginal tax rates could exceed 50%.

### **Profits tax**

As argued in the May submission the IHF agrees with the guarantee in the terms of reference that the 12.5% rate should remain. It is critical for the attraction of foreign direct investment and domestic enterprise development.

### **VAT**

The May submission argued against any increase in the current rates of VAT. In light of changed circumstances including the decrease in the UK rate, the decline in the value of Sterling, the decline in consumer expenditure and the need to stimulate employment the

IHF believes that there is a need for a substantial reduction in the VAT rates at least for a fixed period.

### **Local Authority Funding**

The May submission stated that an equitable local tax applicable to all sectors was acceptable. It also recommended that a system of revenue sharing between central and local government should be adopted. Given the already likely upward trend in tax rates and the state of the public finances it will be more difficult to achieve a diversion of funds from central government or to introduce an equitable new local tax based on sales or incomes. This problem is reinforced if a universal property tax is introduced. The IHF recommends the introduction of a universal property tax. The tax revenue is to be retained by local authorities but the grants from central government should be reduced to match the increased revenues. Therefore the effect of the new property tax should to reduce Government spending and also reduce Government borrowing.

### **Specific sectoral taxes**

The May submission argued that specific sectoral taxes such as hotel bedroom taxes were unfair and reduced competitiveness. Since then the Government has introduced an air passenger tax. Such taxes should not be part of the reformed tax system.

### **Compliance and Regulation**

The regulatory environment should be “flexible and proportionate” relative to the temporary cash flow situation being experienced by many enterprises in light of the sudden and substantial decline in economic activity. Revenue should adopt a supportive approach to enterprises which are in temporary cash flow difficulties and are behind schedule with tax payments. VAT exemption levels should be greatly increased to at least €150K to reduce the compliance costs of small firms and improve competitiveness.

The May submission views on the other issues raised are unchanged. These apply to pensions and carbon taxes. The point about carbon taxes not damaging air travel is even more critical now in light of the high unemployment and the need to generate more economic activity from tourism in the weak international economic environment.