Foundations for the Future

Plain English Version of the Executive Summary

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Executive summary

About this executive summary

This executive summary gives you a brief overview of the report of the Commission on Taxation and Welfare.

It tells you:

- why the Commission was set up – and what it examined;
- the principles that guided the work of the Commission;
- the key messages of this report;
- the main parts of the report.

Why was the Commission set up?

Taxation and welfare policies are important ways through which the State can influence our living standards. These policies also affect many aspects of economic and social policy. They are a part of a wider social contract – the set of rights and mutual obligations that come with living in Ireland. For this reason, debates over taxation and spending lie at the heart of our democratic tradition.

The Commission on Taxation and Welfare was set up by the Minister for Finance in April 2021 and began its work in June 2021. The Commission was established as an independent body and was asked to:

- examine whether Ireland's taxation and welfare systems are suitable for the country's medium- and long-term needs; and
- consider a number of specific topics – such as:

- How to promote business, economic activity and employment.
- How taxation and welfare policy can work together to fairly support the most vulnerable in society.
- How the taxation and welfare systems can help Ireland reduce carbon emissions.
- Taxes on property.
- How to modernise tax administration.

The full list of topics the Commission was asked to examine are outlined it its terms of reference which are on page *xvii* of the full report.

The members of the Commission come from a variety of backgrounds and have expertise in areas such as taxation, social policy, economics, public administration, business, enterprise, law and broader civil society. The Commission's role was to stand back from day-to-day concerns and advise the Government and the public on how the taxation and welfare systems should be reformed to meet the country's long-term needs.

Did the Commission examine all aspects of taxation and welfare spending?

No. Our task was to look at the taxation and welfare systems and how they work together. We were asked to take a medium- to long-term view. This meant we had to decide which issues were most relevant to our work. To do this, we were guided by five principles (see page 8 of this summary).

What challenges and context did the Commission take into account when writing the report?

Fiscal sustainability

Fiscal sustainability is the ability of a Government to maintain public finances at a credible and serviceable position over the long-term while being able to withstand shocks without suddenly reducing promised expenditure (plans to spend) or not being able to pay its debts.

The issue of fiscal sustainability, which is set out in Chapter 4 of the report, is so urgent that we have recommended a net revenue-raising approach. This means we need to earn more revenue from taxation to fund public services in the years ahead. This is urgent given Ireland's high level of public debt, the age and make up of its population, and other fiscal risks. To simply meet existing expectations for public services will require additional tax revenues. For this reason, our recommendations on taxation and Pay Related Social Insurance (PRSI) are intended to either:

- directly increase revenues (income from taxes); or
- reform the structures of the taxation and social insurance systems so that more revenue can be raised over time at low cost and in line with the principles set out on page 8 of this summary and contained in Chapter 3 (Objectives and Principles) of the report.

Social cohesion

The issues of social cohesion and intergenerational equity were recurring themes when we were developing our report.

- Social cohesion means that all groups within society feel connected to each other and belong to one society.

- Intergenerational equity is about trying to ensure that both older and younger generations have an equal share in the State's resources.

Over the past 30 years, Ireland has become a richer and somewhat fairer society. However, we cannot take this social progress for granted. Keeping it fairer will depend on:

- adequate social welfare payments,
- high levels of labour force participation,
- a progressive and fair system of taxation, and
- Ireland remaining a competitive location for investment and job creation.

It also, and fundamentally, depends on the Irish taxation and welfare systems including and supporting everyone so that everyone can play their part. This is essential to maintain social cohesion. Reforming the social insurance system and how we pay for it will be vital to this.

Carbon reduction

Ireland must reduce its carbon emissions in a way that also maintains social cohesion. We believe the taxation and welfare systems have an important role to play in achieving a carbon-neutral economy. We also believe that this should be achieved carefully through a 'just transition' where every group in society is supported in making the changes needed. This will mean ongoing implementation of the Carbon Tax and more reductions in fossil fuel subsidies to better align taxes on fossil fuels with the carbon they contain.

Over time, as use of fossil fuel falls, so too will income from fossil fuel taxes. For example, if the target of reducing the sale of diesel-fuelled cars in Ireland by 2030 is met, the tax collected on the sale of diesel will drop. Therefore, we need to begin planning to

replace the revenues from these taxes and introduce alternative revenues in a fair and sustainable way.

Business and investment

In our work, we have been conscious of the need for a supportive environment for enterprise, innovation and investment in Ireland. The Irish economy has been transformed over the past three decades, but again we cannot take its continued success for granted. While it is important to continue to attract international business investment into Ireland (Foreign Direct Investment), it is also important to promote investment and growth in smaller businesses and entrepreneurs in Ireland. Developing this sector requires:

- improved financing for early-stage businesses,
- more support for research and development, and
- help with attracting talent and skills.

It is also critical, both socially and economically, to maintain a high level of employment and this is reflected in Chapter 11 and across a number of our recommendations throughout the report (see Key messages on page 11).

Balanced reform of taxes and welfare needed

Our report includes a balanced package of proposed reforms to address the challenges outlined above. We believe there is a need for reform and change across several taxes. Our taxation policy recommendations are designed to work together. Equally, our welfare policy recommendations are part of a balanced approach which is linked to our proposals for taxation.

Carrying out the report's recommendations

We are aware that our report is being published during a time of rapid inflation which is having a serious effect on living standards in homes across the country. This report, however, is about the medium- and longer-term needs of the Irish economy, and not the current situation. We do not propose or expect that our recommendations, although interconnected, should be put in place at the same time. We know that detailed analysis and planning will be needed as changes are brought in over time. It will also be important to carefully consider how the reforms we recommend might affect individual households and businesses.

By the same token, the cost of the different recommendations will depend on when they are introduced and the circumstances at that time. For this reason, we have set out a clear strategic direction rather than explicit rules and timelines around how these changes should be introduced.

This does not mean that we can postpone action to address fiscal sustainability. Instead, we should take action in a measured way that reduces risk and minimises the costs to society of higher taxes.

What principles guided the Commission's work?

The principles we used to guide us in writing this report are long-standing concepts used in taxation and welfare, and reflect current concerns. They are:

Sustainability | Reciprocity | Adequacy | Equity | Efficiency

Let's look at each of these in turn.

Sustainability

In the 21st century, sustainability is a distinct principle of taxation and welfare design. We must consider all aspects of sustainability including **economic, social and environmental sustainability**. While much of the impact of the taxation and welfare systems is on short-term outcomes, as a society we must consider how the taxation and welfare systems of today, and the behaviour they incentivise, shape the range of opportunities available to future generations. Equally it is important to ensure the long-term sustainability of the State's finances, ensuring that the State can meet the needs of society throughout the ups-and-downs of economic life.

Reciprocity

The taxation and welfare systems have evolved over a long time. They are at the core of the social contract – **what we owe each other**. As taxpayers, we are not just paying for what we may ourselves receive, we are also contributing to a greater good of which we are part.

We pay taxes and social welfare contributions into a common pool and we expect that:

- We can rely on adequate social welfare supports when we need them.
- We will benefit from living in a society that tries to achieve the lowest possible level of poverty.
- Everyone of working age who can work should do so according to their ability.

For these mutual obligations to work, it is important that everyone contributes to our welfare system through taxation and PRSI.

Adequacy

One of the objectives of the taxation and welfare systems is to redistribute pre-tax income, such as from employment or investments, across the economy to achieve greater equality and prevent poverty. This is to:

- protect people against sudden loss of income;
- enable everyone to take part in society; and
- create and maintain social cohesion.

To achieve these objectives, citizens need adequate income supports to have fair and just living standards. However, adequacy is more about setting social welfare rates against a desired target. The taxation and welfare systems must support people to take part in the labour market, improve their lives without facing disincentives, and improve their earning potential by developing their skills and experience.

Equity

Taxes and PRSI contributions should be levied fairly.

- People in the same circumstances should contribute equally. This is known as horizontal equity.
- At the same time, those who can contribute more should do so. This is called vertical equity.

It is unfair to those that contribute to the tax system that large groups, sectors or activities do not have to pay tax (are exempt). This can also damage the State's finances as it places greater reliance on a smaller pool of taxpayers.

Efficiency

An efficient tax system treats similar activities in similar ways. This reduces unintended consequences that are economically and socially costly. An efficient social protection system treats people in similar circumstances the same way.

Well-designed taxation and welfare systems avoid 'traps' (for example, big drops in income supports) that discourage people from entering the labour market or increasing their work hours. In short, simple and well administered systems are more efficient systems.

What are the key messages of this report?

The key messages in this report are set out below. You will find more detail on them throughout the report.

Fiscal sustainability

- Ireland faces major fiscal sustainability challenges. Over time, the overall level of taxation as a share of national income will have to increase.

- **Substantial reforms** – we need substantial reforms to meet the fiscal sustainability challenges and Ireland's broader needs even though the existing taxation and welfare systems have performed well in many areas.

Broaden the tax base

- **The tax base needs to be broadened** to limit the need for increases in tax rates and to protect the taxation system against future challenges. Broadening the tax base means taxing some forms of wealth or income that are not currently being taxed or ensuring that more people are liable to pay tax by, for example, reducing reliefs or limiting or removing exemptions. It means:
    - widening the base within taxes (for example, applying the zero rate of VAT to less goods);
    - increasing the amount of income from taxes which are less harmful from an economic perspective (for example, increasing taxes on property);
    - promoting environmental goals by phasing out subsidies (see page 13); and

- improving the tax system so it is better at collecting taxes from people who can best afford it.

The balance of taxation needs to move away from taxes on labour towards taxes on capital, wealth and consumption. We also need to reduce our over-reliance on Corporation Tax due to the relatively small number of taxpayers who contribute so largely. We cannot use the increase in Corporation Tax receipts as a reason to not reform other taxes, or as a reason to increase public spending.

- **Reform PRSI base** – personal taxes are highly progressive, meaning the more you earn, the more you pay. However, excluding large numbers of people from the personal tax system is becoming increasingly problematic from a fiscal sustainability and reciprocity perspective (explained on page 8). The priority in this area is to reform PRSI to bring more people into the PRSI system and to increase the overall amount of money in the Social Insurance Fund.

Tax reforms

- **Promote equity and sustainability in Income Tax or Universal Social Charge (USC)** – to promote these, the Government should phase out preferential treatment (e.g. exemptions or reduced rates) based on age or personal characteristics. As far as possible, Income Tax and PRSI charges should be based on income only and different types of income should be treated equally.

- **Tax revenues from property and wealth** – these revenues are low and should increase. The Commission

is not recommending a tax on net wealth. However, the income from Capital Gains Tax[1] (CGT) and Capital Acquisitions Tax[2] (CAT) as well as from taxes on land and property should be substantially increased. In addition, assets should be taxed the same way when given as a gift or as an inheritance. Assets transferred as part of an inheritance should be brought within the scope of CGT.

- **A Site Value Tax (SVT)** – a SVT on all land that is not subject to the Local Property Tax (LPT) should be introduced. This would mean, for example, taxing land used for commercial purposes. This would replace the existing system of Commercial Rates. Agricultural land should be taxed differently under SVT due to the unique role of agricultural land in the production process.

- **Local Property Tax** – this is a well-functioning tax that should be increased. Tax incentives should not be used to encourage the construction of more housing.

- **Tax and carbon reduction** – the tax system has an important role to play in promoting carbon reduction. The schedule of Carbon Tax increases to 2030 should be followed. Fossil fuels should be taxed in relation to how much carbon they emit. This will mean phasing out of historic subsidies (where the Government does not

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[1] Capital Gains Tax is a tax on the increase in value between the price that was originally paid for an asset and the price at which it was disposed of (sold or gifted).
[2] Capital Acquisitions Tax is a tax on the value of a gift or an inheritance.

charge tax on a product or charges less tax) such as for diesel.

As the yield from taxes on fossil fuels declines, the Government will need to replace these revenues with new taxes, including road usage charges. In the short-term, the Commission supports the introduction of congestion charging, where vehicles entering areas, such as cities, that have a lot of traffic must pay a charge, similar to what is done in London and other cities.

- **Value Added Tax (VAT)** – VAT should be reformed to increase its yield by merging the existing special reduced rates and increasing them over time. The Government should not use temporary VAT reductions to boost economic activity. VAT administration should be modernised.

- **Ireland's corporate tax strategy** – this strategy has many of the building blocks needed to promote enterprise, innovation and investment. We need to maintain this strategy. Government should make tax-based policies to support productivity and employment growth in small and medium enterprises (SMEs) and ensure they are accessible for early-stage, high-risk, and research and development-intensive businesses.

- **Incentivising savings for retirement** – this is an important part of the tax system. However, reforms are needed to make sure that tax-relieved savings are taxed appropriately when a person receives a payment from their pension. Tax reliefs should only be available up to a specified level of retirement income. A more flexible

approach to encourage greater retirement savings at younger ages should also be adopted, subject to an appropriate lifetime limit.

- **Excise Duties** – these duties should continue to be used to discourage people from consuming alcohol and tobacco and to support public health, and the link between the public health rationale and design of these taxes needs to be strengthened. The Government should have the right to impose taxes on ultra-processed foods ('sugar and fat' taxes) to improve public health.

- **Tax expenditures** – these are decisions by Government not to collect tax, or to collect less tax, from certain categories of taxpayers (for example when someone buys a bicycle on the bike-to-work scheme they can reduce their tax bill). Tax expenditures should only be used in limited circumstances. The should be only be introduced where the market is not delivering the best result for society and direct expenditure options, like grants, have been examined and rejected.

  Better data and more resources for reviewing, and deciding if tax expenditures should be introduced or kept are also required.

Social welfare reforms

- **Specific targeted reforms** – significant improvements to the welfare system should be made through the progressive introduction of reforms to support employment for people in all situations, address child poverty and remove disincentives to someone taking up

work or increasing their earnings over time. We do not support the introduction of a Universal Basic Income (more about this in Chapter 10).

- **Adequate social welfare rates** – these rates are central to reduce poverty. The rate of income support payments for people of working age should be regularly reviewed. These reviews should set targets for increases in rates.

- **Investment** – we recommend that there is more investment in digital transformations of tax administration processes, including increasing the use of automation.

- **A strategic approach and debate** – a strategic approach is needed to address long-term fiscal challenges. There should also be greater debate on these challenges as part of the annual budget cycle. Tax and expenditure policy changes and administrative systems needed to deal with them should be put in place.

What are the main parts of the report?

There are four main parts to the report:
Part 1 – Strategic Approach
Part 2 – Fiscal Sustainability and Taxation
Part 3 – Broad Policy Goals
Part 4 – Better Systems

Below we briefly describe the chapters in each part of our report.

Part 1 – Strategic Approach

Part 1 sets out the approach which the Commission took to its work and the context for its work.

Chapter 1 explains how the Commission's approach involved careful selection of the issues on which to concentrate, standing back from day-to-day controversies to take a medium- to long-term perspective.

Chapter 2 looks at the remarkable changes in Ireland's economy and society over the past 30 years and the role played by the taxation and welfare systems in those changes. It outlines some of the major trends likely to influence policy in coming decades, including technological change, demography and climate change.

Chapter 3 outlines the core policy objectives which the taxation and welfare systems must address. These include fiscal sustainability, income adequacy and equality, promoting enterprise, innovation and employment, and climate action. The chapter also outlines the principles which the Commission used to guide its work – sustainability, reciprocity, adequacy, equity and efficiency.

Part 2 – Fiscal Sustainability and Taxation

Part 2 describes the scale of the fiscal challenge and the Commission's recommendations for how this should be approached.

Chapter 4 sets out some of the major fiscal risks that face Irish society. These include an ageing population, high levels of public debt and growing reliance on Corporation Tax. This chapter explains why the Commission has adopted a net revenue-raising approach. It identifies areas where revenue can be increased. It also points out the reforms to the taxation and welfare systems that will be needed to achieve higher tax revenues while minimising economic, social and environmental costs.

Chapter 5 discusses how the balance of taxation has evolved in recent years. It compares the make-up of tax receipts in Ireland to other European countries, and makes recommendations in relation to how this balance should develop over time. At the core of the Commission's approach is the broadening of the tax base. Government should focus on maintaining the progressivity of Income Tax and the Universal Social Charge (USC). It should make reforms to PRSI and addressing horizontal equity concerns.

Chapter 6 looks at issues in relation to horizontal equity – the idea that people (or businesses) in similar circumstances should pay similar amounts. This chapter looks at how age impacts Income Tax and USC paid by a person. It also looks at the taxation of deposit interest income, and Value Added Tax (VAT).

Chapter 7 sets out the Commission's approach to the taxation of capital and wealth. It includes major reforms to increase the yield from existing capital taxes, such as, applying CGT on

inheritances, reducing reliefs, and introducing a new minimal capital charge.

Chapter 8 addresses the tax treatment of retirement savings and ways to encourage more saving for retirement over a working life.

Part 3 – Broad Policy Goals

Part 3 looks at particular policy issues which were included in the Commission's terms of reference.

Chapter 9 sets out the Commission's recommendations to promote enterprise, including targeted tax incentives to support early-stage start-ups, research and development, and attracting skills. It also addresses international corporate tax matters and Ireland's corporate tax strategy.

Chapter 10 discusses the Commission's approach to how social protection policy should evolve, including recommendations to broaden the PRSI base to support the sustainability of the system.

Chapter 11 sets out recommendations on supporting employment growth. These include avoiding over-reliance on labour taxes, addressing 'traps' in the taxation and social welfare systems, and expanding the role of the Public Employment Service.

Chapter 12 addresses the adequacy of social welfare payments and recommends changes to in-work benefits, a second tier of child income support, and individualisation of social welfare payments – where a portion of the payment goes to each adult in the household.

Chapter 13 sets out the Commission's recommendations on the role of taxation in encouraging carbon emissions reduction. This

includes implementing the scheduled increases in Carbon Tax, reducing fossil fuel subsidies and developing new taxes to replace the revenues from fossil fuel taxes.

Chapter 14 discusses the taxation of land and property and proposes the introduction of a Site Value Tax on all land not subject to the Local Property Tax.

Chapter 15 discusses the Commission's conclusions in relation to public health and taxation.

Part 4 – Better Systems

Part 4 gives recommendations for developing the tax administration system and reforming policy development and evaluation.

Chapter 16 discusses the system for evaluating tax expenditures and makes recommendations about review methodology, peer review (review by other people), and resourcing the evaluation.

Chapter 17 deals with the ongoing modernisation of the system of tax administration and recommends further digital transformations in tax administration.

Chapter 18 comments on the importance of improving debate on medium and long-term fiscal sustainability and adopting a strategic approach to achieve sustainability.