Ibec Budget 2020 Priorities

BUDGET
2020

An Ibec campaign

About us

Ibec is Ireland's largest lobby group representing business both domestically and internationally. Its membership is home grown, multinational, big and small representing every sector of the economy. Together they employ over 70 % of the private sector workforce in Ireland. Ibec and it's trade associations lobby government, policy makers and other key stakeholders to share business conditions and drive economic growth. It has over 230 professional services staff in seven locations including Brussels and has 38 trade associations.

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We need to build on our progress by nurturing indigenous business and reinventing our offering to multinational firms. By addressing the demands of a rapidly changing labour market we can attract and retain the best talent through improving quality of life. And, deal or no deal, we must get ready for Brexit. So make Budget day your business.

Priorities for Budget 2020

Budget 2020 could be the most strategically important Budget faced by the Irish State in a generation. This year's Budget day should set the sails of Ireland's economy determining a more sustainable course. Windfall corporate taxes and strong growth in household incomes have given us the opportunity to address a unique set of challenges to our business model from the OECD/G20 Base Erosion and Profit Shifting (BEPS) process, Brexit, and a rapidly expanding population from a position of strength. We have a once in a generation opportunity to deliver on nurturing and scaling Irish indigenous business with the objective of growing an ecosystem that is both broader and smarter. This can only be achieved by using our resources and investing in innovation, education and world class infrastructure.

Ibec is Ireland's largest lobby group representing Irish business both domestically and internationally. Its membership is home grown, multinational, big and small, spanning every sector of the economy. Together they employ over 70% of the private sector workforce in Ireland. The following priorities for Budget 2020 have been developed in conjunction with the Ibec Economic and Taxation Committee which has a membership reflective of Ireland's highly globalised business model. We have also consulted through Ibec's 38 trade associations and broader membership.

These headline priorities aim to distil Ibec's overall submission into succinct messages for business and other stakeholders.

1 Indigenous business

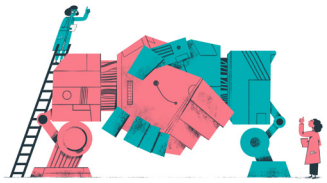
If Ireland is to follow through on the economic promise of the last six decades, then it is evident that Government must go further by investing more ambitiously in indigenous business. Tax policy – including reform of Capital Gains Tax (CGT), the Employment Incentive and Investment Scheme (EIIS), Key Employee Engagement Programme (KEEP), and the R&D tax credit – must be part of a coherent overall policy for growing indigenous business.

2 Foreign Direct Investment

The Irish FDI growth model has never been in a position of greater challenge because of pending global tax reform. The best way to combat unease is to provide certainty and innovative improvements (such as capital allowances for advanced robotics) to the current offering.

3 The future of work

Globalisation, rapid digitalisation, changing lifestyles and new consumer preferences are transforming jobs and careers. Budget 2020 must begin the process of responding to these trends by addressing key labour market issues such as childcare, funding of education, and the taxation of share-options.



4 Quality of life

Feedback from business is consistent –the high cost of housing, long commutes, and challenges to the environment are amongst the top barriers in achieving better quality of life. Budget 2020 must be bold in dealing with core issues such as the cost of land, carbon pricing, and the delivery of key infrastructure projects.

5 Brexit preparations

A no-deal Brexit would fundamentally re-frame the economic outlook of the country. This must be borne in mind when setting the parameters of Budget 2020. Business will continue to make key decisions over the coming months and the Government can play a greater role in supporting them. There must be a stronger delivery on Brexit preparation and mitigation domestically.

Preparing for a changing world

Ireland's current economic prosperity has been decades in the making. The First Programme for Economic Expansion laid before the Dáil in 1958 ultimately formed the backbone of Irish industrial policy for over half a century. Ireland's FDI driven industrial policy over the last six decades was incredibly successful and transformed us from the 'sick man of Europe' to become one of the continent's richer countries. Industrial policy has evolved over the period but further and potentially very significant policy changes may be required over the next decade. The Irish economy needs a proactive Budget 2020 which helps the country prepare for that change.

The change experienced is driven by three fundamental shifts in our business environment:

Firstly, there is great change underway in the global tax environment. Recent developments under the OECD/G20 Base Erosion and Profit Shifting (BEPS) initiative will have a major impact on how our FDI driven growth model evolves into the future. Those proposals, if implemented, would represent the most fundamental change in global corporate tax policy in a century. Some of the proposals, in particular those seeking a minimum effective global corporate tax rate, could pose significant challenges for Ireland's FDI model over the coming decade.

Secondly, the global trading environment is becoming more difficult for small open economies like Ireland. Outside of Brexit, there are signs of a slowdown coming soon in many of our other key trading partners. Germany has flirted with recession over recent months, Chinese growth last year was its lowest since 1990, and US financial markets are beginning to show signs of strain. The negative impact of mounting global trade tensions, whilst not targeted at us directly, will inevitably wash up on our shores. How long these global trade tensions last, and their ongoing reverberations will have a big say in the future of open economies such as Ireland's.

Finally, Ireland's relationship with our nearest neighbour is changing irrevocably. Brexit has left business to manage rolling and costly uncertainty. Despite making up a little over one-tenth of overall goods exports, the UK remains a major market for our indigenous business. Indigenous business, in turn, makes up a significant proportion of the net benefits of exports which trickles down to Irish households. Almost €4 in every €10 in net foreign earnings come from Ireland's food sector. More broadly, our indigenous exporters, which are most reliant on UK trade, account for as much employment and spending on suppliers in the domestic economy as multinational companies.

These three trends together mean that the Irish State will need to be much more strategic into the coming years. The decisions Government makes in coming budgets will be the most important for Irish industrial policy for decades. For the moment, our FDI driven growth regime continues to deliver the resources to make this step. Cumulatively the State has collected over €14.3 billion since 2015 in unexpected corporate tax receipts. The significant resources and investment that this trend has brought and continues to bring to our country is a once in a generation opportunity to prepare for a future when, ironically, other parts of our business investment toolkit will become relatively more important.

Managed well the State could use the resources which have accrued unexpectedly to ensure sustainable growth in Ireland by improved public infrastructure, a thriving indigenous sector and improved standard of living for households. Thus far, however, the Government has used the majority of the cumulative €14.3 billion in unexpected corporate tax which business has paid, to fund unplanned and unbudgeted supplementary estimates. Finding money 'down the back of the couch' before Budget day may seem like harmless politics in isolation, but these unexpected expenditures must be provided for in future years too. The Government must be much more prudent and strategic in how it uses our resources over the coming years

During previous downturns important national projects in infrastructure, innovation, and education were the first to suffer from cutbacks. This long-held pattern cannot be repeated in a post-BEPS world. Any additional unexpected windfall corporate tax returns over the coming years should be set aside in a designated 'strategic investments' fund which would then be used to guarantee the delivery of the National Development Plan, key areas of our innovation infrastructure, and to bring much needed funding to our starved third-level education sector into the future, no matter what the economic circumstances.

The impact of BEPS2

BEPS represents the biggest change in the global corporate tax system in a century. It seeks at its core to ensure that the companies' profits are aligned with the substance of their activities.

Fundamentally the need for the BEPS process arose because the global tax regime for companies was designed for an old Fordist mass-production model. With the rise of global supply chains, new business models and the digital economy it became necessary to reflect these changes in the international tax infrastructure.

The BEPS process began in 2013 with the first BEPS package agreed in 2015. Over 115 countries and jurisdictions have now joined the BEPS process. So far changes have been implemented in 83 countries and 1,400 tax treaties through a multilateral instrument. Many of the measures at a European and Irish level are part of the EU's Anti-Tax Avoidance Directive and will take effect from 2019 onward into the early 2020s.

The work at OECD/G20 level is not complete, however. There is now clear renewed political momentum behind global multilateral tax reform through the process known colloquially as BEPS2. The recent publication of the BEPS2 roadmap from the OECD/G20 is a significant step. The second BEPS package (BEPS2) will concern both the allocation of tax bases between countries and a potential for a global minimum effective corporate tax rate. Both will be significant for Ireland from an industrial policy standpoint. These proposals, if adopted, would take effect over the course of the next decade. Agreement will require a majority and countries will implement the proposals unilaterally if there is no agreement in Paris. In contrast to previous efforts at global tax reform these most recent proposals have strong political backing from all major countries including the US, Germany, and China. Ireland has no veto.

Proposals under Pillar 1 will mean some re-allocation of taxing rights to larger importing countries and, as a small exporting country, may mean the Irish exchequer will lose a proportion of its corporate tax base. Irish business, however, is more concerned about proposals under Pillar 2 which would introduce a minimum effective corporate tax rate globally. It is crucial for small open economies that this rate, if introduced, is set at a level which focuses on addressing actual profit shifting concerns and does not infringe on our right to set competitive tax rates. These proposals are gaining significant momentum amongst the G20 and many of our traditional allies on tax issues.

Ibec will continue to represent Irish business interests as the only Irish representative at BIAC (Business at the OECD) and on its working groups on these issues. Although we are early in the process, it is now highly likely that significant change is coming to how companies are taxed globally. The Irish Government will need to react proactively by significantly strengthening other areas of our FDI regime. This will require significant investments in areas such as education, innovation, and quality of life which we have failed to make over recent years.

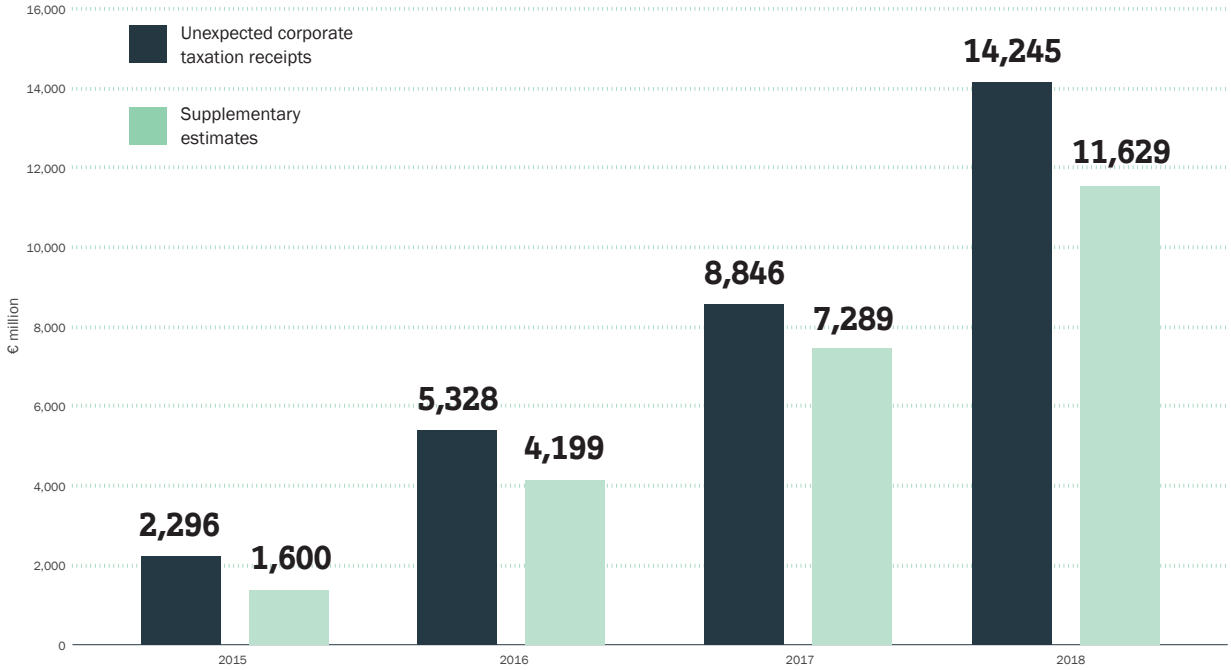


Figure 1: Cumulative unexpected corporate tax take and supplementary estimates since 2015 [€ million]

Fiscal risks

In 2018, the Government ran a surplus for the first time since 2007. This happened despite significant increases in spending over recent years. Unexpected corporation tax revenues played a significant role in achieving this. If corporation tax receipts came in as forecast from 2015 to 2018, and everything else remained equal, the State would still be running a deficit of almost 2% of GDP at the top of the business cycle. Based on the current plans from the Government it would be 2023 before Ireland ran a surplus had it not been for the unexpected upswing in corporate taxation revenues. To date, much of the volatility in corporation tax receipts was positive but were it to move in the other direction, public finances would be left very exposed. As we head into the next decade the possibility of this reverse scenario is real.

Because the State's revenue is 'fungible' (i.e. part of a central pot rather than specifically earmarked) it would in ordinary circumstances be difficult to link one source of unexpected revenue to one expenditure line. However, we have a good idea of where the major overruns were spent due to the timing of the revenue and their unexpected nature. In each of the years, the scale of the corporate tax overrun was not known until close to year-end. As such it was not included in that year's budget. However, the unexpected increases in each year once-known were accompanied by end of year 'supplementary estimates' of a strikingly similar scale. Both revenues and those expenditures are then built into the base of revenue and expenditure for the following year.

Figure 1 shows the scale of the end-of-year corporate tax overrun and that year's end-of-year supplementary estimate (decided around the same time) in cumulative form. The average annual unexpected corporate tax take in each of the years between 2015 and 2018 has amounted to €1.2 billion, while the average supplementary estimate has run at €1 billion. In our view, the evidence suggests that most of the unexpected corporate tax boon thus far has been used to finance budgetary overruns, to extend services in a way which has not been planned for at the time of the previous budget, or to give once-off discretionary payments (such as the Christmas Bonus). More than half of that additional spend has gone to cost overruns in the health sector.

These are all political choices with knock-on impacts on fiscal sustainability. Any potential under-delivery of corporate taxation in future years will require either a reduction in spending elsewhere, an increase in taxation or an expansion of the deficit. Even if the corporate tax take remains on target future overruns in spending will result in the same outcome. Our fear is that in the event of a loss of corporate taxation, the deficit will be made up by cutting projects from the 10-year capital plan, as has been the case in every previous downturn, or by increasing the deficit to fund current spending on services at a time when that fiscal firepower may be needed to deal with the fallout from Brexit.

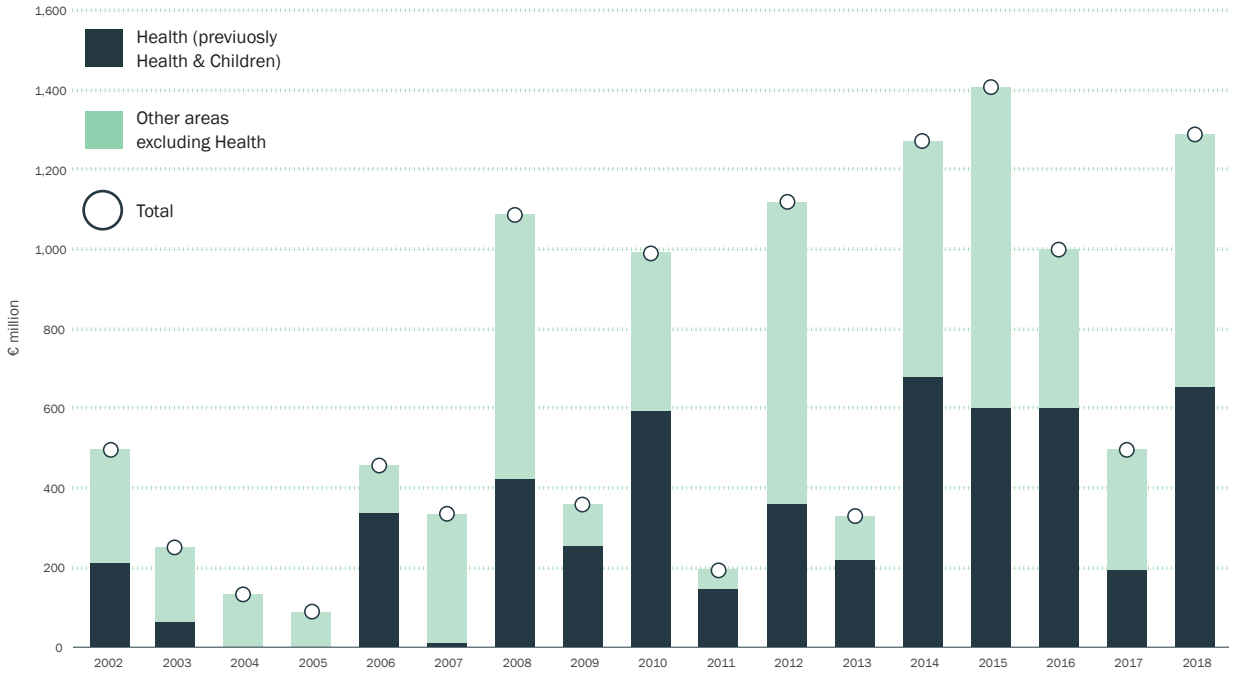


Figure 2: Supplementary estimates needed at year end, 2002 to 2018 [€ million]

The expiration of capital allowances on IP, the end of the double-Irish, and further onshoring could potentially boost tax revenues substantially in the short-term. However, Brexit and the prospect of a transatlantic trade war also pose significant risks to Ireland in the immediate future. In addition, consistent feedback from business makes it clear that firms are beginning to review their options regarding corporate investment because of US tax reform and after the transposition of the anti-tax-avoidance directive (ATAD) by January 2019. In the medium-term, there are reasons to believe that tax reforms suggested under BEPS2 could cost Ireland up to 20% or more of its corporate tax base and significantly blunt the attractiveness of our 12.5% corporation tax regime and reliefs (for things like R&D) for investors in the future. Growing corporate tax revenues are not a given and should not be treated as such.

Ireland's business model in a post-BEPS world

Ireland must begin to prepare for a world, after BEPS, where non-tax elements of our business model will play a much more significant role in the location of investment. The US corporate tax rate was a baseline globally for the attractiveness of tax rates on new marginal investments. In a global context, the recent US rate cut is part of a wider trend toward lower marginal rates of corporate taxation.

Our 12.5% tax rate has been a significant advantage over the past two decades, but it remains a fact that the average corporate income tax rate across the developed world has dropped from 32.5% in 2000 to 23.9% in 2018. By comparison to other Northern European countries our advantage in terms of effective tax rates is now down to only 7 percentage points and shrinking. We are still in a period of global flux, but the trend is that average corporate tax rates across our competitors are quickly converging in a race to the middle. Tax is important but alone it is no longer enough.

Table 1 ranks Ireland to similar Northern European countries across several indicators which are of importance for the mobile business community. Our relative strengths lie in the tax regime and our labour market openness. It is important that we think strategically about our future. The Government must take this opportunity to radically improve the non-tax elements of our regime if Ireland is to continue to compete in the post-BEPS2 world. Even in a benign scenario these investments would pay dividends for the State as our indigenous companies seek to improve productivity and move up the value-chain into ever more complex areas of production and services.

Table 1: Top-level benchmarks of Ireland's FDI regime

	Netherlands	Sweden	Finland	Denmark	UK	Ireland	Germany	Ireland rank
Skills and Innovation								
Higher education spend per student, $ PPP	19,286	24,417	17,591	15,626	26,320	13,229	17,036	7th
Primary education spend per student, $ PPP	8,478	10,853	9,305	12,199	11,630	8,228	8,619	7th
State innovation spend per capita, $ PPP	1,084	1,710	1,278	1,660	747	808	1,589	6th
25 to 49-year-old employees with 3rd level education, %	47.2	52.3	51.5	48.9	51.9	59.1	32.0	1st
Tax support								
Composite Effective Average Corporate Tax Rate, %	23.0	19.8	19	19.5	19	11.8	27.3	1st
Government tax subsidy for R&D, % of total BERD	14.7	0.5	-	1.0	13.8	29.2	-	1st
Quality of life								
OECD better life ranking	10	4	9	2	16	15	13	6th
Price level index relative to EU average (EU avg. = 100)	114.6	134.5	123.3	139.0	117.6	129.1	103.7	5th
Public capital stock per capita, $ PPP	32,277	31,048	30,247	38,386	18,925	25,593	20,075	5th

Despite the downside risks, trends in business investment continue to be strong particularly in the FDI sectors of the economy. In total, business has invested around €1 billion per month since 2015 in capital equipment and buildings. There are clear benefits to this additional investment, but this scale of growth may also pose risks if it is not managed properly. Rising competitiveness pressures will intensify both in product and labour markets should investment continue without clear efforts to invest in public infrastructure. In areas from transport to housing, the failure to match this surge in private investment with investment in public capital in areas like transport, housing and education will push up operating costs directly for business by making trade more difficult or expensive. They will also mean higher costs and longer commutes for workers.

If the fruits of continued private investment are not managed correctly Ireland risks the fate of other poorly planned resource economies who have discovered the 'paradox of plenty'. Our failure to capitalise on a once in a generation opportunity – by failing to use additional resources to improve public investment – will reinforce a two-tier economy with high costs, lower productivity and continuing challenges to living standards in areas like transport and housing. On the other hand, if changes over the next decade blunt the attractiveness of our tax regime, both households and business will be left with significant deficits in other areas of our investment offering – in innovation, talent, and quality of life – which need to be addressed.

From this point of view the business sector which is investing and paying tax in record numbers urges Government to use these resources, over time, to provide the funding needed to deliver on the National Development Plan, to give a funding boost to much-needed education and innovation projects, and to help us deliver a strong indigenous enterprise sector. At the same time, we advocate that the Government should convene a new Commission on Taxation to try and provide consensus on the best ways to structure a sustainable and competitive tax system which can provide adequate resources for the State into the future.

Table 2: Budget costings

	Budget 2020	Strategic investments' fund	No-Deal Brexit provisions
Tax reform for indigenous business	135	0	0
Corporation tax & R&D tax credit	60	0	0
Technological and Innovation supports	35	50	0
Income tax and share options	330	0	0
Education, childcare, and wellbeing	135	400	0
Housing, sustainability, and infrastructure	€70 million with other measures funded by tax increases or through existing provisions for capital expenditure		
Brexit diversification and competitiveness measures	90	0	0
Stabilisation measures in the event of no-deal Brexit	0	0	500
Total	855	450	500

Key takeaways for Budget 2020

- **Non-tax offering**: There are potentially significant implications for Ireland, from global corporate tax reform, over the coming decade. When it comes to our international competition our relative strengths lie in the tax regime and our labour market openness. The Government must take steps to radically improve the non-tax elements of our regime if we are to continue to compete in the post-BEPS world. These changes will mean that Ireland will need to significantly step-up non-tax elements of its business model such as infrastructure, innovation, education, and quality of life.

- **Commission on Taxation**: Ireland is threatened by shifts in global economic conditions and the extreme concentration of the Irish economy. Starting in Budget 2020 the State will have no choice but to follow through on the promises of previous decades and finally make a concrete effort to grow our indigenous enterprise base. This includes an intense focus on productivity, innovation, skills, and exporting early. In our view, it also means a new Commission on Taxation should be convened to address many of these issues. The prospect of a no-deal Brexit adds significant urgency to this need and must provide a moment of clarity for policymakers.

- **Long-term investment**: Ireland has a history of focusing cuts on productive spending during any downturn. The Government has an opportunity to break this cycle and guarantee significantly improve quality of life into the future. Any additional unexpected windfall corporate tax returns, over the coming years, should be set aside in a designated 'strategic investments' fund which would then be used to guarantee the funding capital projects in the National Development Plan, key areas of our innovation infrastructure, and to bring much needed funding to our starved third-level education sector throughout the economic cycle and guarantee significantly improved quality of life.

We need to build on our progress by nurturing indigenous business

1

Some notable successes aside, there is a strong argument that we have not done enough over the past 60 years to fulfil the promise of the First Programme for Economic Expansion to 'foster in every way' the development of Irish indigenous business. If we are to follow through on the economic promise of the last six decades, then it is evident we must go further by developing our indigenous enterprise base.

Recent years have seen dramatic changes in the business tax environment in Ireland. In one sense the impact of BEPS has been dramatic, in another we have yet to see its true impact. It has massively boosted both capital investment in Irish based MNEs and led to a sharp increase in our corporate tax returns.

All available evidence shows that Irish indigenous firms are well below 'best in class' when it comes to management, innovation and exporting

However, the measures underpinning the BEPS process are only now being translated into concrete action, companies are still changing their structures to manage this new framework. BEPS2 is also underway and will, in our view, have significant implications for Irish industrial policy going forward. We are entering a world where the impact of our headline rate of corporate tax alone will be more muted than in the past, and companies are increasingly looking at the broader context. To guard against the risk of relying on too few firms for our exports and tax receipts Ireland will necessarily need to strengthen its indigenous base.

Indigenous business has made some progress over recent years. To survive the downturn firms have invested in new product, engaged in capital deepening, and become leaner. The impact of this and better price competitiveness in the Irish economy can be seen in the fact that Irish exports over the eight years to 2017 were between five and six times more responsive to growth in global demand than they had been between 2001 and 2008. As a result, for the first time in 2015 agency figures showed Irish-owned exporters accounting for a greater share of agency supported employment than foreign MNEs. In a post-BEPs environment, it is inevitable that continued strong investment by large firms will increase costs across the economy, particularly if public infrastructure cannot bear the strain. We must focus on increasing productivity in indigenous firms to deal with this.

While Ireland does not produce enough start-ups, equally worryingly is not enough small companies make it big. Finance, access to export markets and the ease and cost of doing business all remain significant hurdles. We need a business environment that supports entrepreneurship and rewards innovation and risk taking. Enterprise policy must focus on helping companies scale up by improving investment supports such as the EIIS and CGT. We must also encourage firms to invest in innovative activities by making the R&D tax credit more accessible for firms seeking to scale.

Ireland must go further, however. All available evidence shows that Irish indigenous firms are well below 'best in class' when it comes to management, innovation and exporting — three of the main drivers of business growth and productivity. Improving management practices, helping firms innovate or export earlier will increase the productivity and growth of Irish indigenous firms. We also have low start-up rates compared to the majority of our European neighbours – the second lowest in the EU15 and one-quarter that of the UK. We must do more to help people starting out in building high-skilled teams when growing a business in Ireland. Given the constraints on cash in start-ups, this can only be done within a sensible tax environment for share-options.

Irish businesses face several ongoing challenges to their growth. These include high legacy debts and costs, a small domestic market, a lack of diversified funding options, barriers to innovation, and challenges accessing and competing for the right skills to help them grow. These issues are not unique to the Irish market but the challenges to growth from the funding environment, market size, and peripherality are far more acute in Ireland than most developed countries. Tax policy must be part of a coherent overall policy for growing our indigenous base and must be cognisant of the broader context. There are several levers within the tax system which can be used to help overcome some of the broader systemic disadvantages facing our indigenous business community. Below we set out some of the key tax policy levers which we believe can help Irish business to grow.

Recommendations for Budget 2020 to broaden the indigenous enterprise base and support SMEs

Issue	Recommendations	Cost [m: million]
Capital gains tax	— Send a signal of intent to serial entrepreneurs by radically improving the CGT entrepreneurs' relief by introducing a 12.5% rate with no lifetime limit on capital gains. — Expand CGT entrepreneurs' relief to passive investors in high-potential and high-risk areas (Tech, Med-Tech, Food, Biopharma, or other high-tech/creative industries) to increase the supply of equity for Irish companies. — Charge CGT for earn-out and similar arrangements only on receipt of earnings. As it stands, the current system ties up cash to re-invest for several years and can lead to high levels of debt for entrepreneurs without access to cash.	€100m
EIIS	— Increase the €150,000 limit on EIIS investments to €2 million. The current level is severely restricting the flow of capital to firms. — Remove the current system of split relief based on employment levels or R&D expenditure. This introduces a level of uncertainty for the investor over which they have very little control. Full relief should be given in the investment year. — In line, with the recommendations of the Indecon review losses on EII investment should be allowed for CGT purposes and any capital gains on the sale of shares should be taxed as capital gains rather than as income, as is currently the case.	€20m
KEEP	— Increase to €10 million the limit on the market value of issued but unexercised KEEP shares. This remains overly restrictive for truly high-potential firms where early rounds of investment may place the companies' valuations at many multiples of this level. — Remove the restrictions on employer share buy-backs under KEEP. Given the low liquidity in the market for equity in Ireland, this is unreasonably onerous and can render the scheme unusable for many workers. — Ensure better guidance is given for firms around the definition of holding companies and excluded activities (i.e. Fintech) under KEEP. If necessary, amend regulations in this area. These challenges create significant issues for several sectors. — Introduce an agreed 'safe harbour' approach to share valuation. As it stands it is difficult for many early-stage companies to value their companies. The cost of doing this for the operation of KEEP alone is disproportionate and a major impediment for many early-stage companies.	€5m
R&D tax credit for SMEs	— Introduce a pro-forma R&D tax credit to help smaller firms overcome administrative costs and engage with the credit. The existing limit should be in line with UK's R&D tax relief for SMEs with more generous tax treatment, reduced additional recordkeeping requirements, cash repayments upfront, and 'advanced assurance' for the first three times you claim it. — Introduce pro-forma templates for R&D project management, recording R&D activity and calculation of eligible costs and revenue benefit associated with the credit for SMEs. — Increase the limit for non-audit under the science test to €100,000 for SMEs if they have already received similar clearance from other state or EU agencies.	€10m

Foreign Direct Investment

Reinvent our offering to multinational firms

2

As outlined in the introduction, Ireland's FDI growth model has never been in a position of greater challenge. The trend over the past decade is for countries to reduce their headline corporate tax rates in response to base broadening globally. This will accelerate in response to the implementation of BEPS and the lowering of the US corporate tax rate.

Ireland's 12.5% tax rate has been a significant advantage over the past two decades, but it remains a fact that the average corporate income tax rate across the developed world has dropped from 32.5% in 2000 to 23.9% in 2018.

In other Northern European countries like the UK, Sweden, Denmark, Finland the gap in effective tax rates is now down to only 7 percentage points and on a downward trend. This is not a significant gap when bases are broadly the same.

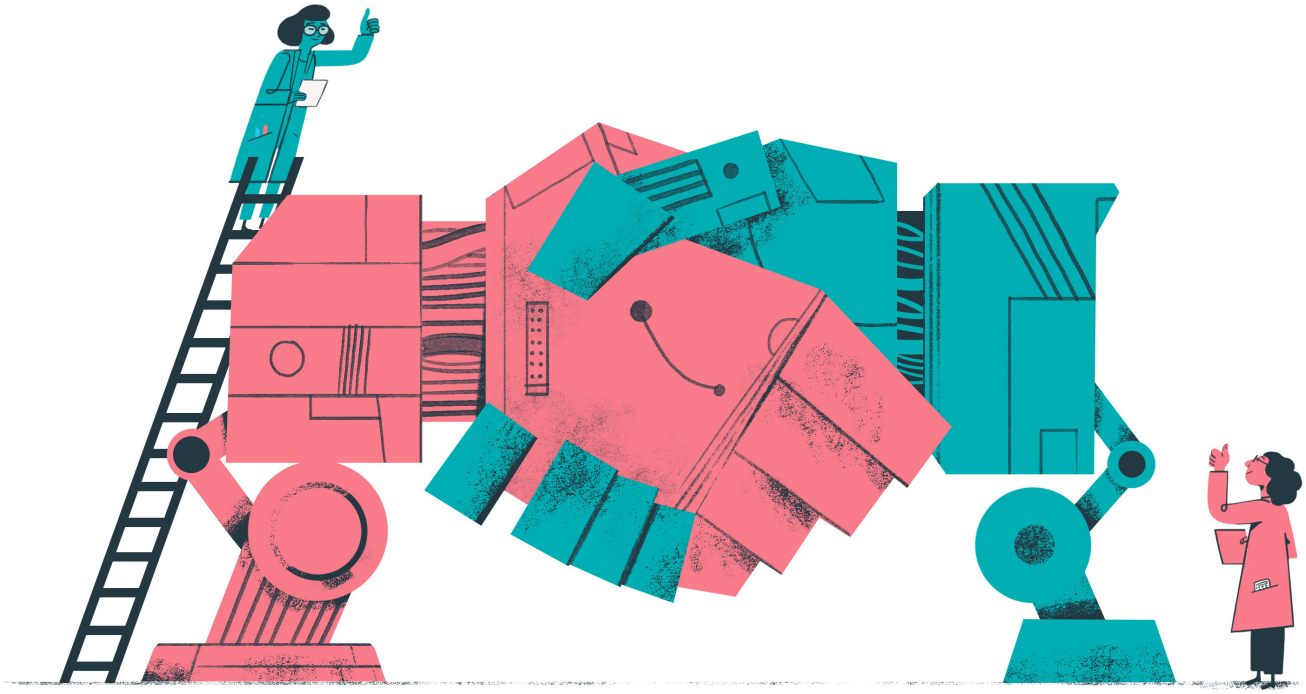
Both taken together these issues are resulting in serious uncertainty amongst companies both investing in and out of Ireland. But tax remains an important tool. The best way to combat unease is to take concrete measures to provide certainty and innovative improvements to the regime we have. Administrative issues are causing continued concern for companies interacting with the R&D tax credit and must be addressed.

Outside of the tax regime, it is important that we up our game in areas of our offering where we traditionally have had a weakness. Recent years have seen us slip further behind in Government funding of innovation. Our traditional strength in advanced manufacturing is one which will not last into future decades if we stand idly by while large developing countries attempt the next step up the value chain. Ambitious plans like 'Made in China 2025' are targeting our domains of expertise. We have lost industries before to foreign competition. The key to rising living standards is our ability to step into more complex products and services industries immediately up the value chain. This requires forethought and investment.

It is important the Government embrace this change by introducing accelerated capital allowances for advanced manufacturing technologies and robotics which will help us advance technically and improve productivity. As it stands Ireland has one of the lowest densities of industrial robots in the European Union.

Recommendations for Budget 2020 to bring certainty to a challenged FDI model

Issue	Recommendations	Cost [m: million]
Corporation tax	— Provide certainty to the regime by re-committing to an FDI driven growth model, the 12.5% corporate tax rate and the importance of the R&D tax credit. — Prepare for a post BEPS2 world by ringfencing any future overruns in CT revenues for spending on innovation, education, or capital projects alone. — Investigate the feasibility of a model which would allow companies to 'roll-over' their capital allowances on expiry in exchange for investment in public goods through an approved skills, infrastructure, and innovation vehicle (SIIV) or body (for example an educational institution).	No cost in 2019
R&D tax credit	— Remove the 5% limit on qualifying outsourced expenditure to Third Level Institutions, under the R&D tax credit, and the restrictions on outsourcing to related parties should be removed. This would be consistent with the treatment under the Knowledge Development Box and in line with other jurisdictions. — Improve the administration of the R&D tax credit by working with industry to resolve issues around timesheets — Improve consistency of decision-making amongst technical experts	€60m
Technological supports	— Introduce accelerated capital allowances for a number of areas of advanced manufacturing (including computerised/computer aided machinery and robotic machines). Ireland has the second lowest density of industrial robots in the EU15, despite them being strongly linked with increased productivity. — Extend the industrial buildings allowance to include the construction of data centres to encourage the sector to continue its growth despite recent setbacks — Ensure the National Cyber Security Centre (NCSC) continues to have the resources and expertise adequate to its role as Ireland's lead authority for cyber security in the State	€35m
Innovation supports	— In advance of developing a successor to Innovation 2020, set out an ambitious ten-year funding framework for innovation in consultation with business and academic stakeholders. In 2020, establish a new approach to funding innovation capacity and infrastructure at third-level that builds on the progress made under PRTLI with funding of €30 million. — Increase the Innovation Voucher value to €10,000 to encourage higher levels of research, development and innovation activity within business. — Enhance Ireland's capacity from frontier research system to target highly competitive EU funding opportunities via an additional €11 million funding for Laureate awards	€50m



Address the demands of a rapidly changing labour market

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Globalisation, rapid digitalisation, changing lifestyles and new consumer preferences mean jobs and careers are being transformed. And the pace of change is accelerating. This brings great opportunities, but also risks.

As Ibec has outlined in our 'Smarter World, Smarter Work' campaign, the archetypal worker used to be a person on a production line or a salaried employee in an office. This will not be the case in the future. The needs of businesses and individuals are shifting, and so too are career paths.

How organisations, government, and individuals respond to these trends will fundamentally affect the quality of our jobs and our lives in the future. It will determine the ability of businesses to prosper and, more fundamentally, it will shape our society and living standards for generations to come.

To address this, public policy must focus on investing in an individual's employability. It must prioritise an inclusive and lifelong approach to skills development. At present, Ireland's lifelong learning rate is less than half the benchmark set by the EU and significantly below what is required by a knowledge-based economy.

Failure to address the provision and affordability of childcare (among the highest of the 36 OECD countries) further has the potential to force more women out of the labour market.

Indeed, across the education system underfunding is clear. Nowhere is this more acute than in the third level sector. Ireland is currently spending significantly less, per student, than competitor countries. Feedback from our members on this has been extraordinarily strong - it is having an impact on our reputation internationally.

As it stands Ireland's prime age labour market participation is at record levels, but still below most of the rest of Northern Europe. Significant parts of this trend can be linked back to childcare costs which are amongst the highest in the OECD. This issue too will need to be solved if it is not to continue to provide structural barriers to second-earners in the workforce. While many positive initiatives have been undertaken in the area of Early Childhood Care and Education, we are still one of the lowest spenders on Early Childhood Education in the entire OECD, while at the same time having the highest fertility rates in the EU. Despite having increased Government spending by 117% in budgets since 2015 our starting position was from a very low base.

To stand still and just provide the services already committed to for 2020 will require €50 million, yet we are still struggling with a lack of places for babies and toddlers, a lack of affordability for not just lower but also middle-income families and there are challenges for providers too in terms of commercial rents, rates, and regulations.

Failure to address the provision and affordability of childcare (among the highest of the 36 OECD countries) further has the potential to force more women out of the labour market. While we have had the third largest increase in prime age (25-54 years) female participation rates in the last two years with 78,000 more women at work than in 2014, we still lag our EU counterparts as the fifth lowest country for the proportion of women at work.

Employers have also been encountering numerous barriers in accessing the disability supports provided by the Department of Employment Affairs and Social Protection and report their lack of relevance for the modern workplace. Many grants provide assistance to new recruits only instead of existing employees such as those returning to work with reduced productivity levels. All grants have been reported as being administratively burdensome, time-consuming and resulting in delays of six to eight weeks for individuals and employers alike.

Finally, Ireland's labour market is tightening rapidly. This is now leading to strong wage growth across almost all sectors. The extreme progressivity of our tax system has its virtues, but it is also increasingly putting pressure on take-home pay for people earning modest wages. It is important workers earning around the average wage do not see increasing amounts of their income fall under our extremely high marginal rate of tax.

In most countries this is achieved by automatically indexing tax bands to wages, but this practice has been abandoned in Ireland. Non-indexation of income tax bands and reliefs is resulting in real tax increases each year of around €600 million. A significant portion of that revenue must be recycled into making sure working households do not experience further pressure from these stealth tax increases.

Recommendations for Budget 2020 to prepare for the future of work

Issue	Recommendations	Cost [m: million]
Income tax and share options	— Increase the entry point to the 40% rate of income tax by €1,000 to keep ahead of wage growth. — Reduce the higher marginal rate of tax for those earning over €70,000 by 1%. — Reform the operational and reward constraints in Revenue approved schemes to be more flexible to companies' reward structures. In particular, these schemes must be allowed to be linked to performance. — Increase the €12,700 limit on Revenue approved share options schemes to €20,000 and index it to wages. — Explore a new SSIA-type scheme to encourage households benefiting from economic growth to save more in the good times. Further incentives could also be built into these schemes to encourage a future staggered withdrawal of these savings or to provide a bridge to pension provision.	€330m
Childcare	— Budget 2020 should provide for an additional €50 million on top of existing needs to fund the carryover costs of existing services. — Use additional funding to introduce direct subsidies for childcare providers to offer more places to the Under 1's to enable parents to make real choices about the care of their children and their ability to work. — Increase the flexibility in child-adult ratios where more highly qualified staff can respond to higher numbers of children, enabling wages to be increased and subsidies to stretch further. — Means test Child Benefit payments so that they remain the same for low income households but taper off gradually for higher income households. This has the potential to save the Government €200 million - €500 million, depending on the cut in point for tapering, which should be redirected into services. — Explore the feasibility and possible benefits of a tax saver childcare voucher model to encourage the retention of parents in the labour market.	€50m
Education	— Commit to a rebuilding a sustainable higher education funding model that allows for core funding, programmatic funding, infrastructure investment, and industry-academic collaboration. Increase funding by €400 million in 2020. — Use funding from the increase in the National Training Fund levy to develop, a voucher-style, cost reimbursement scheme to enable employers to choose suitable training services from accredited education and training providers. — Allocate €20 million under the Human Capital Initiative in 2020 to build digital capacity in education and training institutions for online and blended learning programmes. — Develop a scheme for business to offset the cost of training against corporation tax to build long-term sustainability of Generation Apprenticeship programmes. — Introduce an institutional borrowing framework to address capital investment constraints in technological universities and institutes of technology.	€480m
Disability supports	— Amalgamate all the current disability supports into one grant that will cover an employee's need as achieved by the UK's Access to Work scheme. — Remove the onus from employers to apply for grant support and empower the job seeker with a disability to seek work with their supports already in place automatically. — Increase the Wage Subsidy Scheme for persons with a disability from its current level at 55% of the minimum wage to 70% of the minimum wage level. The Government should give a commitment to index it at that level over time as part of the Low Pay Commission process. — Extend personal assistant supports available for persons with a physical disability who work on certain schemes (e.g. CE schemes) to persons in other forms of employment.	€15m

Attract and retain the best talent by improving quality of life

4

The world of business and work globally is changing. When it comes to the affordability of accommodation and a good quality of life there are obvious social reasons why these are desirable. There are also strong reasons why these issues are having a growing impact on business.

The traditional industrial model of the 20th century typically saw capital locate close to raw materials and transport routes. Workers and businesses serving them were then attracted to these towns and cities. That model is no longer dominant in the 21st century. The move toward a digitised intangible economy means companies are now more reliant on intellectual rather than physical capital. Ireland is at the vanguard of this trend.

Ibec recommends a redesign of the carbon tax. The tax should follow the model of the National Training Levy where revenue is ringfenced to support investment in emissions reduction, energy efficiency and the deployment of renewable and low carbon technologies.

In addition, both Irish and non-Irish workers are much more mobile than in the past. The cost of accommodation, strong public infrastructure, quality of life and workplace attractiveness is a key factor in the decision of workers to locate in Ireland. The highest value firms are often choosing to locate where talented workers (and in some cases superstar workers) want to live rather than the other way around. Feedback from business is consistent; the high cost of housing, childcare, allied to high marginal tax rates on second earners and long commutes is the number one issue in getting more workers into the labour force or indeed to continue living and working in the country. As the labour market tightens this issue will only become more acute.

Last year 18,000 new houses were built, but this is only half of what is needed to accommodate our growing population. Ireland's housing market is not functioning at present. Early signs of a slowdown in house price growth are, in our view, a function of affordability being out of reach of too many. This continued shortage of affordable housing has clear knock-on implications for households, employers, and the economy.

Quality of life is a broader consideration than just housing. We are already witnessing the effects of climate change. Global average temperatures have increased by almost 1˚C since pre-industrial times. The atmosphere and oceans have warmed, snow and ice cover has diminished, sea levels have risen, and entire species are on the brink of extinction due to habitat destruction. Failure to address climate change and its main driver - increasing greenhouse gas emissions - will place our environmental, social and economic well-being at great risk.

Ireland is committed to delivering a low carbon economy by the year 2050 as part of the EU's collective efforts to mitigate climate change. Ibec supports this ambition. It makes good business sense to have a sustainable, resilient economy. Businesses throughout the country are reducing their environmental footprint and investing in low carbon technologies, renewables, energy efficiency, and waste reduction.

Additional State support is needed to make these investments more cost-effective and attractive for business. Increased State support is also needed to drive an extensive energy efficiency retrofitting programme of our built environment, and to decarbonise the transport sector.

Ibec recommends a redesign of the carbon tax. The tax should follow the model of the National Training Levy where revenue is ringfenced to support investment in emissions reduction, energy efficiency and the deployment of renewable and low carbon technologies. The tax should be set at €30 per tonne in 2020 with a commitment to increase the tax annually by €5 per tonne until it reaches €80 in 2030. A full review of outcomes and impact should be held in 2025.

Gradual, predictable increases in the tax will give greater investment certainty. A portion of the revenue should be used to support fuel poor households and vulnerable business sectors with no practical alternatives to fossil fuels. This includes businesses at high risk of carbon leakage, where production might move to another country where no such tax exists, causing job losses without reducing global emissions.

Recommendations for Budget 2020 to improve quality of life

Issue	Recommendations	Cost [m: million]
Housing	– Ringfence any major upturn in construction-related tax revenues to invest in infrastructure that opens more land for residential development and invest in direct build social housing where the need may arise. – Renew the Help to Buy scheme for a period of 5 years. While we recognise the need for the scheme to be time-limited, committing now to a 5-year term provides industry with the certainty to supply new homes with greater certainty about realisable demand. – Replace recurring commercial property taxation (e.g. commercial rates, vacant site levy, etc) with a land value tax.	€70m
Sustainability	– Set the carbon tax at €30 per tonne in 2020 with a commitment to increase the tax annually by €5 per tonne until it reaches €80 in 2030. A full review of outcomes and impact should be held in 2025. – Introduce a new cost-effective exchequer support scheme for microgeneration and develop a pilot "green mortgage" scheme to support deep building retrofitting. – Extend the 0% Benefit in Kind rate for electric vehicles out to 2025, maintain existing grant supports for electric vehicles, and amend existing VRT rates to drive greater uptake in low and zero emissions private cars – Introduce a compressed natural gas (CNG) vehicle grant to encourage fuel switching in the freight and HGV sector. – Reduce the VAT for renewable technologies and energy efficiency equipment and material to 4.8%.	Cost neutral
Infrastructure	– Deliver on the capital plan as set out in Ireland 2040. Improve resourcing for procurement specialisms in order to ensure the majority of the €21 billion in projects currently in train are brought in on time and on budget – Introduce dedicated budgets for local authorities to develop segregated cycle routes and greenways. – Increase funding to the Support Scheme Renewable Heat and allow Emissions Trading Scheme installations to participate. – The European Commission rules on state supports to Airports specifies that airports under 3 million passengers are eligible for capital expenditure support for investment. Ibec recommends that the Government implement the EU Guidelines on State Aid to Airports in a manner which allows all airports under 3 million passengers to avail of funding under the Regional Airports Programme for eligible safety and security investment	Cost covered in existing provisions.
Wellbeing	– Remove support by employers for employee health and fitness from BIK. – Make initiatives which relate to programmes which raise health awareness or promote employee participation in wellness programmes creditable against companies' corporate tax bills.	€5m

Brexit Preparations

Deal or no deal, we must get ready for Brexit

5

While the extension of the Brexit deadline until the end of October, agreed by EU leaders in Brussels, avoids a catastrophic 'no deal' UK exit for the short-term, it does nothing to guarantee a long-run solution. Business has already spent millions on contingency planning and has been left dealing with costly uncertainty.

In the absence of some political movement over the summer, this uncertainty will only intensify and the risks of a no-deal Brexit will increase dramatically. While massive uncertainty remains, the right outcome is the most important thing for business. If the worst occurs in October it will fundamentally reframe the economic outlook of the country. This must be borne in mind when setting the parameters of Budget 2020.

No matter what the outcome of Brexit, companies will need support to diversify, innovate and re-align their business models.

If there is a no-deal exit, growth will still be positive, but it will be half what it would have been as there will be negative movements in sterling, investment and prices, and trade disruptions. For many of our regions and indigenous industries, this will feel like a deep and scarring structural break. The main avenue of impact, however, will be through the labour market. For this year, Ibec forecasts that employment growth will slow to 2% as the increase in the number of workers in the country struggles to keep pace with demand. Ibec's expectation is that employment would still grow out to the end of 2020 in every Brexit scenario. However, the pace of growth would slow significantly in 2020 to less than 0.5%.

No matter what the outcome of Brexit, companies will need support to diversify, innovate and re-align their business models. The education system will need support to provide the capacity for up-skilling. Supporting our indigenous industries will mitigate the worst impacts of Brexit domestically.

Previous Ibec work has shown that employment in the most Brexit exposed sectors was mainly focused on rural areas, rather than urban ones. Up to 30% of workers in Cavan/Monaghan work in the most Brexit exposed sectors, whilst fewer than 8% do in any of our cities. New research undertaken by Ibec has also shown that workers in the most Brexit exposed sectors also finished school younger than the average across the economy. For example, only 17% have a third-level qualification. These workers are also much older than average - one-in three workers in the most Brexit exposed sectors are over the age of 50.

Ibec members will continue to make key decisions over the coming months and the Government can play a greater role in supporting them. This does not just extend to the agri-food sector but also to the wider domestic economy with tourism, forestry, traditional manufacturing, retail and energy, transport, utilities, and telecoms all impacted either directly through the loss of trade or otherwise through disruption of their supply chain. It is worth remembering that the need for diversification not only applies to exporting companies but also to those importing.

There must be a stronger delivery on Brexit preparation and mitigation domestically. Yes, there are still major uncertainties which make it difficult to plan ahead for Government but the time for preparation is now.

Recommendations for Budget 2020

Issue	Recommendations	Cost [m: million]
Diversification for Brexit	— Put in place a multi-annual framework for funding Brexit mitigation beginning in Budget 2020. The resources required will be in the region of 5% of the value of current annual indigenous export sales to the UK. — Accelerate the current SME credit guarantee scheme's coverage of invoice discounting and factoring arrangements in Brexit impacted firms, in-line with state aid rules. — Introduce a new scheme covering export credit insurance. This would necessitate temporary changes to the EU's "Short-term Export Credit-insurance Communication" allowing exemptions for schemes which are aimed at companies impacted by Brexit and diversifying away from the UK. This could include some private risk (up to 20%). — Loosen the criteria for the existing loan schemes. These criteria and their overt focus on technological innovation are completely inappropriate for firms in sectors most impacted by Brexit. — Introduce additional innovation, marketing and trade promotion supports for companies developing new product lines for international export markets	Exchequer cost €40m, Partly cost financed by ISIF.
Stabilisation in the event of no-deal	— Continue work to put in place a broader temporary state aid framework to help Governments provide short-term assistance to companies. — Introduce a Compatible Limited Amount of Aid Scheme of up to €5 million over three years for investment or working capital as part of a European temporary State-Aid framework. This was introduced in most countries in 2009. This should take the form of direct grants through an enterprise stabilisation fund, but also include guarantees, interest rate subsidies, and rescheduled debt for companies in distress. — Prepare a short-time work subsidy scheme (for two years initially) for vulnerable workers in the event of a no-deal Brexit. This would mean a subsidy to the worker of up to 60% of the worker's reduced net wage, for up to 12 months. This would allow workers to go part-time into training/ re-training for a temporary period where hours are reduced and would give companies greater flexibility in the case of a demand shock. It would be available only to impacted firms. — Introduce an employment Subsidy Scheme with subsidies up to €10,000 over 24 months for employees in firms in distress.	In the event of no-deal: €500m
Cross-border shopping	— Ensure further price differentials do not emerge between the Republic and Northern Ireland due to increases in taxes or excises which have the potential to drive cross-border/ unlicensed activity and reduce excise on alcohol by 7% in 2020. — Do not increase other areas of VAT or duties on potentially mobile products or services.	€50m

Gerard Brady is Ibec's Chief Economist. His role involves regular analysis of economic issues for a business audience, and policy engagement on economic policy issues, along with advising companies and sectoral organisations. He is a current board member on the National Statistics Board (the Governing body of the CSO) as well as a member of the economic and tax policy committees at both Business at the OECD (BIAC) and Business Europe. Prior to joining Ibec in 2013, Gerard worked as a lecturer in economics in University College Cork. He is a previous winner of the Miriam Hederman O'Brien prize, awarded by the Foundation for Fiscal Studies.

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