SUBMISSION TO THE MINISTER OF FINANCE ON THE 'JOBS INITIATIVE'

15 April 2011

Key Recommendations:

- Extend the use of the cash accounting scheme for VAT purposes, which would improve the cash flow of SMEs;
- Enhance the Employer Job (PRSI) Incentive Scheme to reduce the number on the Live Register by extending its application to all persons on the Live Register and doubling the limit on the number of employees to 10% of a company's workforce;
- Maintain the corporation tax rate at 12.5%;
- Maintain the current higher VAT rate at 21%;
- Implement the decisions of the European Court of Justice in terms of unfair competition by local authorities and other VAT exempt public bodies;
- Consider lowering the VAT rate applied to labour-intensive services;
- Reduce stamp duty on commercial transactions from 6% to 2%; and
- Complete the reform of the Business Expansion Scheme (BES) announced in Budget 2011, and increasing the number of qualifying trades in particular.

Dublin Chamber of Commerce

Dublin Chamber of Commerce represents 1,300 companies, both large and small, across a wide range of sectors in the Greater Dublin Area.

The Economic Environment

Ireland faces a severe crisis. The problems of high sovereign and bank debt, low growth, doubts about fiscal sustainability, and a fragile credit environment have undermined the confidence of businesses and consumers. The Live Register has risen to over 440,000 and emigration has increased markedly. Recent Exchequer figures published illustrate a major increase in the Exchequer deficit since last year.[1] This is largely due to payments to Anglo Irish Bank and Irish Nationwide and is broadly in line with expectations. However, there are growing concerns at the decline in VAT receipts.[2]

Ireland faces the challenge of generating growth, against a backdrop of continuing fiscal difficulties. At the top of the agenda for a stable and sustainable economic recovery is the fostering of enterprise and the creation of jobs. Small and medium sized enterprises (SMEs) are a central component of any such strategy. These businesses can be helped to survive and grow by tax changes which improve credit flow – changes that will increase Exchequer receipts as these firms expand and generate employment.

1. Department of Finance figures illustrate an Exchequer Deficit of €7,066m in Q1 2011, compared to €3,942m in Q1 2010.
2. VAT receipts have fallen from €3,216m in Q1 2010 to €3,110m in Q1 2011 and are running €179m below forecast.

A Jobs Initiative
Dublin Chamber appreciates that it has been necessary to turn to our international partners for assistance and supports the new Government in its renegotiation of the IMF/EU Programme of Financial Support for Ireland. In advance of the General Election, Dublin Chamber set out its members' priorities for the next Government in our 'Business Needs…' document. We believe that the arguments set out in this document continue to be pertinent. In this context, we **commend the Government's clearly stated policy** that the current **corporation tax rate of 12.5% will be maintained**. Dublin Chamber welcomes the new Government's commitment to implement a strategy for job growth and sustainable enterprise and in particular, the introduction of a Jobs Fund, as outlined in the Programme for Government.

This submission sets out a number of specific measures which the Chamber believes, if introduced in the forthcoming Jobs Initiative, would stimulate business activity and job creation. These measures are outlined under the following headings:

1 VAT MEASURES TO IMPROVE CASH FLOWS FOR SMES
2 HIGHER & LOWER VAT RATES AND CONSUMER CONFIDENCE
3 AN ENHANCED PRSI REBATE SCHEME
4 DECREASING STAMP DUTY
5 GROWTH OF THE BUSINESS EXPANSION SCHEME

1. VAT MEASURES TO IMPROVE CASH FLOW FOR SMES
Dublin Chamber believes that it is important to improve the cash flow of SMEs by implementing EU law to allow SMEs to utilise a cash accounting system. Article 66(b) of Directive 2006/112/EC permits Member States to use cash accounting. Directive 2010/45/EU of 13 July 2010 states in the recitals that Member States should provide for cash accounting:

> "*to help small and medium-sized enterprises that encounter difficulties in paying VAT to the competent authority before they have received payment from their customers, Member States should have the option of allowing VAT to be accounted using a cash accounting scheme which allows the supplier to pay VAT to the competent authority when he receives payment for a supply and which establishes his right of deduction when he pays for a supply. This should allow Member States to introduce an optional cash accounting scheme that does not have a negative effect on cash flow relating to their VAT receipts*."

The Revenue Commissioners have implemented a cash accounting scheme, allowing companies to account for VAT on sale on the basis of payments received, rather than tax invoices issued. This improves cash flow for qualifying businesses. Certain conditions are currently imposed on businesses to avail of this treatment. The annual turnover of the business must not exceed €1 million. This threshold is low in international comparison, being approximately two-thirds of the thresholds that apply under the cash accounting schemes in the UK and Australia (see Appendix 1). Where a VAT-registered trader has an annual turnover exceeding €1 million, it can only apply the cash accounting scheme where its supplies goods or services that are almost exclusively (at least 90%) made to unregistered persons. This limits its application in practice to retailers and others business that sell to consumers.

This does not seem to meet the statement set out in Directive 2010/45/EU that such **cash accounting scheme** should assist SMEs with cash flow. It does not assist the large number of SMEs with a turnover of over €1 million that carry out mainly business-to-business sales. We recommend the **extension of the scheme to businesses with a turnover less than €2.5 million**.

Consideration of Unfair Competition by VAT-exempt bodies
The ramifications of the decisions of the European Court of Justice in *HMRC v Isle of Wight Council and others* (Case C-288/07) and *European Commission v Ireland* (C-554/07) need to be considered in the context of unfair competition by local authorities and other VAT exempt public bodies. This is an issue which is particularly acute in the leisure industry, where the failure to charge VAT on non-core activities results in predatory pricing by VAT-exempt bodies. Urgent attention should be given to the creation of a level playing field between public and private sector bodies competing for the same market. This should be done, not only in order to engender fair competition, but also to ensure that Ireland is fully in compliance with its obligations under EU law.

2. HIGHER & LOWER VAT RATES AND CONSUMER CONFIDENCE

The Programme for Government has indicated a limit in the rise of the higher rate of VAT to 23%. Dublin Chamber is **concerned that any VAT rate increase would further dampen consumer confidence**. Businesses will not be in a position to carry the burden of the increase in VAT and it will drive up the rate of inflation. Dublin Chamber believes that a period of stability is required. Indeed, if the Exchequer deficit were not what it is, we would be calling on Government to reduce the higher rate significantly. Based on 2009 data, the expected revenue from a 2% increase in VAT is in the order to €800 million. Given the ongoing decline in consumption, we believe that any expected increase must be weighed carefully against the impact on domestic consumption and its impact on indirect, and indeed direct tax revenue, through reduced employment.

Dublin Chamber believes that **consideration should be given to ensuring that labour-intensive services prone to operating in the 'informal economy' are brought within the lower rate of VAT**. In addition, bringing these types of services within a lower rate of VAT should stimulate consumption by consumers. There is precedent for such treatment in other EU member states. Directives 2006/112/EC and 2009/47/EC permit a reduced rate of VAT for certain labour-intensive services. A reduced VAT rate is permitted in labour-intensive services such as domestic care services (including home help and care of young, elderly, sick or disabled) and repairing and renovation of private dwellings. Dublin Chamber appreciates that if the overall lower VAT rate is decreased by 1% it would cost in the order of €250 million; therefore, we believe that a more targeted approach would be more cost effective.

3. AN ENHANCED PRSI REBATE SCHEME

Since 2010, the Employer Job (PRSI) Incentive Scheme has exempted employers from their liability to pay the employer PRSI contribution for certain employees for 12 months. In order to qualify:

(a) The employee must be on the FAS Work Placement Programme for at least 3 months or in receipt of certain social welfare benefits such as jobseekers allowance/benefit for at least 6 months.

(b) The job must be new and additional and must be for at least 30 hours per week. If the job lasts for less than 6 months the contribution for that employee must be paid.

Employers may only receive the exemption for up to 5% of their workforce or a maximum of five jobs. Since coming into effect the scheme has had a very limited impact in that there have only been claims in respect of 1247 employees to date.[3]

3. Answer to Dail Question 25 January 2011 - http://debates.oireachtas.ie/dail/2011/01/25/00172.asp

We believe that the reason for the poor take up of the scheme is that the conditions are excessively restrictive, particularly in relation to who can qualify and the maximum number of employees. Dublin Chamber recommends that the scheme be amended such that:

(a) The **qualifying period that a person must be a FAS Work Placement Programme or in receipt of Jobseeker benefit/allowance be eliminated**; and

(b) The **company employment limit be increased to an overall ceiling of 10% or 10 employees**, whichever is greater.

We acknowledge that there will be a deadweight element to this measure, but believe that this will be mitigated by retaining the requirement that there must be a net increase in employment. Dublin Chamber believes that this change would have a very real impact on increasing employment and would have an even greater impact if the PRSI exemption was increased to two years.

4. DECREASING STAMP DUTY

The **Chamber proposes the reduction of stamp duty on commercial transactions from 6% to 2%**. Despite the 2008 reduction from 9%, Ireland's rate of stamp duty is above well above the UK's Stamp Duty Land Tax, which applies to transfers of interests in land and immovable property located in the UK and varies from 0% to 4%. The Stamp Duty represents the highest proportion of the transaction cost for commercial property, creating a very considerable bid/offer spread on investing in Irish real estate. Such high bid/offer spreads serve as a significant deterrent to property transaction activity and directly affects the valuation of commercial property. Under typical property valuation methodologies the underlying rent is grossed up by an appropriate yield and reduced by transaction costs.

A four percentage point reduction in the rate of stamp duty would nominally cost the Exchequer between €70m to €125m annually. Lowering the bid/offer spread is likely to significantly increase transaction activity. Transaction activity in the Irish commercial property sector has remained extremely low with, for example, 2010 investment property volume totalling only €242 million (reflecting 29 transactions). Recent Exchequer figures indicate illustrate a continued decline in stamp duty revenue.[4]

5. GROWTH OF THE BUSINESS EXPANSION SCHEME

Dublin Chamber welcomed the reform of the Business Expansion Scheme (BES), announced in Budget 2011, as it provides much needed financial support for small business. Dublin Chamber supports the revised Employment and Investment Incentive (EII) scheme, as we believe it will support jobs and enhance SMEs' export potential. To this end, we would be delighted to assist the Department of Finance and the Revenue Commissioners in finalising the development of and promoting use of the EII.

Department of Finance ex-ante economic analysis indicates that if the number of companies using the EII doubles from 2009 figures, approximately 2,400 new jobs will be created over a two-year period. In addition to the benefit in employment, the growth of these companies will benefit the economy. Market failure in equity capital investment is inhibiting the ability of many SMEs to invest in product and/or process innovation.

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4. Stamp Duty revenue has fallen from €142m recorded for the first quarter in 2010 to €124m recorded for the first quarter in 2011. This illustrates a decrease of 12.6%. Furthermore, stamp duty revenue for the first quarter in 2011 is 8.2% below target.

Service sector companies that are innovating are about twice as likely to export as non-innovating companies.[5]

In 2009, the take up of the BES dropped significantly. It was, of course, largely due to the economic down-turn and the tightening of equity investment. However, there were a number of operational barriers to the BES that prevented companies from taking part that would have benefitted from it. The Chamber in its Pre-Budget 2011 Submission and subsequent meetings identified the limitation on qualifying trades, the high administrative burden and a failure to communicate the scheme to SMEs.

The **removal of the limitation on qualifying trades contained in the EII and the Revenue Commissioners proposal to allow companies to qualify** - where they meet the requirements for company size provided they are not on the list of excluded trades - is a positive step forward, as this will mean that the revised scheme will be accessible to the majority of SMEs, which was not the case under the BES.

5. Central Statistic Office, "Community Innovation Survey 2006-2008", Table 13.4: Percentage of innovative and non-innovative enterprises engaged in exporting by sector (2006).

APPENDIX 1

UK cash accounting scheme

The UK scheme allows companies to account for VAT (output tax) on sales on the basis of payments received, rather than on tax invoices issued. It follows that if a company opts to use the scheme, it can only reclaim the VAT incurred on purchases (input tax) once the supplier is paid.

The eligibility conditions are as follows:

(a) The company has an expected value of taxable supplies in the next year will be £1,350,000 or less.

(b) The company has no VAT returns outstanding, has not been convicted of a VAT offence in the last year and does not owe any VAT, or if so, arrangements have been made to clear the total amount of outstanding VAT payments.

Australian cash accounting scheme

A person or entity is eligible to account for GST on a cash basis if it meets any of the following criteria:

(a) It is a small business with an annual turnover (including the turnover of its related entities) of less than $2 million

(b) The person is not operating a business, but is carrying on an enterprise with a GST turnover of $2 million or less

(c) It accounts for income tax on a cash basis

(d) It carries on a kind of enterprise the commissioner has determined is able to account for GST on a cash basis regardless of GST turnover or, is an endorsed charitable institution, trustee of an endorsed charitable fund, gift-deductible entity or government school, regardless of GST turnover.

If a person is eligible and accounts for GST on a cash basis, it will:

(a) account for the GST payable on sales in the tax period for which payment is received. If the person receives only part payment for a sale in a tax period, its account only for the part of the GST payment that relates to that part of the sale in that tax period.

(b) claim GST credits for business purchases in the tax period for which they are paid. If only part of the cost of a business purchase is paid in a tax period, and the person has a valid tax invoice, it can claim only the GST credit for that part of the cost in that tax period.