NICVA and UUEPC SUBMISSION

NICVA UPDATE

Fiscal Powers: A review of the fiscal powers of the Northern Ireland Assembly
NICVA PwC report 2013

NICVA commissioned PwC to carry out this ***review*** which was published in 2013. It was part of a body of work carried out by NICVA through our Centre for Economic Empowerment. The focus of the work was twofold. The first was to help voluntary and community organisations to become better informed about economic issues and to take part more effectively in economic policy debates. In support of this we ran a series of training courses and masterclasses on a wide range of economic issues.

The second aspect centred on researching issues that might improve the lives of people in Northern Ireland if policies were adapted or new policies developed that might improve the economy of Northern Ireland. NICVA believed in informing the debate and much of the research was commissioned to explore the options rather than to find evidence to support a position.

That was the basis for commissioning this research report. We wanted to explore the possible benefits, or not, of devolving more fiscal powers to Northern Ireland. We wanted to shed light on which powers may be useful to have or not but mostly we wanted an informed debate.

NICVA tried to have an open mind on all the issues believing they were worth exploring and examining before we should take a view for or against any change in policy.

NICVA had taken part, over a 10-year period, in the Government's Economic Development Forum which advised the economy Minister. The EDF focus was trying to find the policy changes that might improve the trajectory of Northern Ireland's economy. NICVA's research was also driven by that goal and in all ***18 reports*** are available on the NICVA website under the work of the Centre for Economic Empowerment.

Seamus McAleavey
NICVA

Fiscal Powers:
A Review of the Fiscal Powers of the Northern Ireland Assembly
April 2013

NICVA commissioned PwC to produce this report in 2013. It was part of a project, the Centre for Economic Empowerment, that NICVA established over a number of years. The purpose of the CEE was to enhance the voluntary and community sectors economic skill and build its capacity to contribute to the economic debate.

In all 18 research reports were commissioned and published by NICVA and are available on NICVA's web site at ***https://www.nicva.org/programmes/centre-for-economic-empowerment***

The main purpose in commissioning the research was to explore and try and find evidence to support beneficial policy change in Northern Ireland. NICVA recognised that Northern Ireland's economy chronically underperformed and was searching for policy initiatives that might change Northern Ireland's 'flatline' development.

With regard to devolution and fiscal powers by 2013 Northern Ireland was the only devolved region that had not been subject to a comprehensive review of fiscal policy and legislation/proposals to devolve a variety of fiscal powers.

Executive Summary of the report

The success of previous attempts to agree and implement a vision for the Northern Ireland economy has been limited.

A number of studies, including the Strategy 2010 in 1999, the most recent Programme for Government and the Northern Ireland Economic Strategy have all identified and articulated a vision of a more prosperous Northern Ireland. This is summarised in Strategy 2010 as, "A fast growing, competitive, innovative, knowledge-based economy where there are potential opportunities and a population equipped to grasp them." Of course, without a single, cohesive and generally agreed economic objective, policy making, and objective setting will remain challenging. Hitherto, successful implementation has remained elusive.

There has been little progress towards closing the prosperity gap between Northern Ireland and the rest of the UK.

At least, 15 major reports on the state of the Northern Ireland economy, since the 1957 Isles and Cuthbert's report have reached broadly similar conclusions about the region's shortcomings. Successive strategies and reviews have collectively failed to close the productivity, innovation and earnings gaps between Northern Ireland and the UK average.

Maintaining the status quo in economic strategy is unlikely to significantly improve Northern Ireland's economic performance, relative to the rest of the UK.

So, it is reasonable to suppose that a continuation of previous performance is unlikely to substantially narrow or close the existing gaps between Northern Ireland and the UK average in terms of performance.

The current macroeconomic climate and the absence of public spending growth is likely to further disadvantage the region for the foreseeable future.

Given that an improvement in economic performance towards a defined vision is desirable and can be assumed to be feasible it is worth considering how policy might be adjusted to promote such an outcome. This is particularly appropriate in the current climate of austerity where pressures on public expenditure are likely to be continued well into the next Spending Review period beginning in 2015.

Northern Ireland is the only devolved region that has not been subject to a comprehensive review of fiscal policy and legislation/proposals to devolve a variety of fiscal powers.

Recent developments in terms of comprehensive reviews of the fiscal powers available to the devolved administrations in both Scotland (the Scotland Act 2012), potentially in Wales (the Silk Commission) and in the English regions (the Heseltine Growth Review), suggest there is a real opportunity to begin a similar debate in Northern Ireland as to the further devolution of fiscal powers that could assist in rebalancing the economy.

Northern Ireland's current position in terms of funding the devolved administration could be characterised as one of:

• Very limited fiscal variation, where only a few taxes, the Regional Rate and Air Passenger Duty (APD) direct long haul, are under devolved control and where there are limited powers to borrow and gain extra resources from, for example, the EU.

• Overwhelming dependency on the block grant from HM Treasury.

• Being the recipient of a longstanding and sizeable net transfer from the UK Exchequer.

In considering which taxes might be devolved it is important to quantify the revenue generating potential of those taxes.

Drawing upon the deliberations of the Calman, Holtham and Silk Commissions in determining which taxes might be devolved, it is helpful to define taxes as “major” and “minor” in terms of the size of the revenues raised. Devolving a major tax will potentially make a greater contribution to increasing the revenue stream, autonomy and accountability of a devolved assembly. Having said that, it might still be decided to devolve certain minor taxes because of their potential contribution to particular economic, social or environmental policy agendas.

In terms of the scale of revenues collected three taxes stand out as major: Income Tax, National Insurance Contributions and VAT. In practice, only Income Tax is a strong candidate for devolution, as has been identified in both Scotland and Wales. Devolving and thus potentially varying the rate of National Insurance Contributions from that of the rest of the UK would in practical terms be hard to reconcile with welfare and benefits policy commitments. EU law appears to prohibit regional variations in VAT rates.

Corporation Tax is not a major tax, although the revenue raised is greater than some of the minor taxes. There has been a prolonged debate about, and campaign for, devolving Corporation Tax varying powers to Northern Ireland. The Prime Minister has indicated that any decision about this will not happen until after the Scottish independence referendum in September 2014. In addition, devolving Corporation Tax is subject to the strict Azores Judgement and would have a direct and substantially detrimental impact on the block grant for many years.

In identifying potential taxes for fiscal devolution in Northern Ireland, we should make allowance for:

• Developments in Scotland (additional Income Tax variation powers, Stamp Duty and Land Tax, and Landfill Tax) and proposals in Wales (Silk proposed Income Tax variation, Stamp Duty and Land Tax, Landfill Tax, Aggregates Levy and APD);

• Developments in England under the Heseltine Growth Review proposals where, while the majority of the proposals to decentralise powers to the English regions/cities seem to have been accepted, the magnitude of financial transfers have yet to be determined.

• In addition, a number of criteria will influence the suitability of a tax for devolution:

1. Would devolution improve accountability?

2. Is devolution possible without creating significant economic distortions?

3. Is devolution possible without imposing significant costs (either administrative or compliance)?

4. Could devolution promote various policy objectives; economic, social, health or environmental?

5. Would devolution be compatible with EU law?

6. Is devolution possible without a major negative effect on the tax base in the rest of the UK?

• Further reform of the tax base across the UK, whereby fiscal incentives will add to the attractiveness of Northern Ireland for foreign direct investment (FDI) and indigenous investment, even without specific regional devolution. The recent progressive reduction of Corporation Tax rates, introduction of the Patent Box regime and increased tax incentives for R&D are examples where UK wide policy has had a potential benefit to Northern Ireland. Regardless of what happens in terms of enhanced powers it is important to make the most of the incentives Northern Ireland already has.[i]

Given these considerations and the experience of Scotland and Wales, the following taxes would theoretically become candidates for full or partial devolution in NI:

• Income Tax;

• Stamp Duties;

• APD;

• Landfill Tax. **Of the so-called "major taxes", only Income Tax is a major tax in terms of revenues raised.**

The size of the revenues raised and the fact that devolution has already occurred in Scotland and is proposed for Wales is an argument in favour of considering Income Tax devolution for Northern Ireland. At the same time, there are some other significant considerations relevant to whether Income Tax should in fact be devolved. There is considerable uncertainty about the extent of responsiveness on the part of employees to tax rates and the elasticity of labour supply. This is both in general terms and amongst Basic and Higher Rate[ii] taxpayers but there are indications from the external evidence that if the Assembly wished to maximise revenue it would increase the Basic Rate by a small amount and hold the Higher Rate at current levels.3 [iii]

Care must be taken in choosing the method to index deductions from the Northern Ireland spending block if any of the taxes were to be devolved.

This would especially be the case in terms of Income Tax as a large source of revenue (such deductions are a requirement under EU law). Indexing to the growth of UK revenues for that tax (the method favoured by Holtham for Wales) has the advantage of insulating the block deduction from the general UK economic cycle and UK policy risk (things that would have a general impact on the amount of Income Tax revenue collected but are not under the control of the devolved administration). However, it is much less clear, based on the past performance of the Northern Ireland economy, that Northern Ireland would be able to grow its regional Income Tax base above the UK average.

So, it is uncertain whether the gains to revenues could outgrow the deduction from the spending block. This creates the risk that Income Tax devolution would lead to the Assembly having less resources in the future. Such a risk has to be weighed against any benefits (e.g. economic or political accountability) from such devolution.

If Income Tax was devolved policy makers must balance the respective priorities of revenue maximisation, the promotion of entrepreneurship amongst high earners and distributional objectives.

Trade-offs are likely and it is very unlikely the Assembly could use Income Tax variation to pursue all three of these goals at once. This reinforces the point that the question of whether the power to vary a tax should be devolved (the subject of this report) is in principle separate from the question of how such a power might be used. Greater tax powers might require the Assembly to clarify or define its policy position, e.g. on the relative priority to be given to economic efficiency or distributional considerations.

Defence of the Northern Ireland funding block is understandable but not the only consideration.

Especially during a period of austerity, it would be entirely understandable if the Executive gave strong emphasis to defending the extent of the block grant to Northern Ireland (hence producing a concern about possible off-setting reductions in the block grant which arise from fiscal devolution given the need to ensure compatibility with the Azores Judgement). This reinforces the point that devolution of a tax may require confidence that it could produce sufficient compensating growth in the private sector to set against any reduction in the block grant. This confidence will be reinforced if the induced gains in other tax receipts relate to tax streams which are also under devolved control. Even if the other tax streams are not devolved such a policy might be justified if the aim were to contribute to rebalancing the Northern Ireland economy, i.e. the % share of the private sector and social enterprise sector compared to the public sector.

Fiscal variation should be seen as a supplement to other policy emphases and not as a solution in its own right.

Northern Ireland has hitherto not engaged in the level of debate about wider fiscal powers which has been going on in Scotland and Wales. While it may be useful to initiate that debate, it does not mean that enhanced fiscal powers would, in themselves, become a game changer to transform the economy.

Other, previously identified objectives should still be pursued; these would include improving the quality of management across the private, public and third sectors whilst having a single-minded emphasis on raising productivity and exporting performance through gains to R&D and management capabilities. Indeed, regardless of what happens in terms of enhanced fiscal powers, the scope to use the UK's existing business tax package (e.g. Corporation Tax falling to 20% in 2015, and Patent Box now in place) should be maximised as a selling point for Northern Ireland as a destination for international investment.

NICVA
February 2020

[1] Of course, none of these characteristics of the UK business tax system mark Northern Ireland out relative to other UK regions. Our point, however, is that we suspect more could be done to sell these attractions to potential international investors given that it is undoubtedly the case that the UK overall has a relatively attractive offering compared to many other Western economies.

[1] Strictly speaking, "Rates" as both the 40p and 45p rates are relevant.

[1] It remains unclear how far an elasticity taken from US or UK experience would accurately predict how the Northern Ireland labour market would respond to, say, a 2p increase in the Basic Rate or a 3p decrease in the Higher Rate. The revenue maximising argument for actually cutting the Higher Rate becomes stronger if we assume a very strong behavioural response (i.e. considerable increase in labour supply) and/or strong in-migration by high earners from, say, GB and the Republic of Ireland.

Written Statement to Department of Finance Committee: The Fiscal Powers of the Northern Ireland Assembly

Dr Esmond Birnie, Senior Economist Ulster University Business School

Context: Limited fiscal powers

- At the establishment of the State of Northern Ireland (NI) back in 1921, again in 1998, and now in 2021 the extent of fiscal powers was limited. Currently, NI's tax varying powers are restricted to the Regional Rate and Air Passenger Duty for long haul trips. Also, a few new very small (in terms of the revenue raised) taxes were introduced during the 2007-16 period of devolution: the levy on plastic bags and the Large Retail Levy. The power to vary Corporation Tax has existed since 2016 but remains unused. Stormont does have discretion over a range of charges.
- Three arguments for greater powers and greater use of those powers (including greater use of existing powers): (1.) to improve accountability (decisions to spend more would be linked to an extent to the decisions about how to fund that spending), (2.) to either discourage or encourage certain economic behaviours or sectors (e.g. higher taxes on environmental damage) by either raising or lowering certain tax rates, (3.) if we wish to fund a higher level of spending we may have to look to our own resources given the extent to which post-Covid UK fiscal policy is likely to be constrained with more limited growth of the Block Grant and Barnett consequentials.
- None of this implies that greater tax varying powers is a miracle cure for all the ills of the NI economy (or of NI society). The under-performance of the NI economy over the last 100 years has been a long run trend arising from a range of explanations.
- Fiscal devolution isn't just about cutting taxes or just about increasing taxes. Different circumstances imply that certain taxes should increase and certain should decrease. Tax varying powers give the Stormont Executive greater choice as to what to do.
- Fiscal devolution is not in conflict with the pursuit of greater efficiency and effectiveness in terms of public spending and public sector delivery. In fact, the knowledge that some decisions to spend more would be accompanied by a necessity to raise taxes or charges could incentivise public sector reform. I do see it as an antidote (albeit a partial one) to the mindset of "free money" which helped to create the RHI crisis.
- Unlike Scotland (Calman and Smith Commissions) or Wales (Holtham and Silk), NI has *hitherto never had a full scale, independent inquiry* re. the extent of fiscal powers. Now, of course- in the shape of Paul Johnson's Fiscal Commission- it does.

The position in Scotland and Wales

- Back in 1998-99 NI had more fiscal powers than the other 2 devolved administrations. That is no longer the case. In 2020-21 31% of total tax revenues collected in Scotland were devolved (including assigned VAT), 20% in Wales but only 9% in NI (Institute for Government website, "Tax and devolution", accessed 21 April 2021).
- SCOTLAND: Has devolved the former Stamp Tax on property sales (SDLT, now LBTT), Landfill Tax and Income Tax on earned income in terms of rates and bands (though not the Personal Allowance). To be devolved, Air Passenger Duty (APD) and Aggregates Tax (subject to some legal issues relating to state aid). VAT, half of its revenue to be assigned to Scottish Government (subject to both the UK and Scottish Governments working out and agreeing that amount).
- WALES: Now devolved SDLT (now LTT), Landfill Tax, and part of Income Tax (can vary by up to 10p in each band).
- It may be worth anticipating the implications for NI if in a few years Scotland does head to "Devo Max" (possibly following a majority vote for such a "third option" in a second independence referendum).

Importance of this Committee

- The NI public/electorate/taxpayers/service users deserve an informed debate re. fiscal powers. This Committee is well-placed to contribute to such a debate.

- And that debate could happen alongside and be informed by the analysis and recommendations of the Fiscal Commission.

Fiscal devolution: Broad principles

Here are some important considerations:

- Keep the tax base, i.e. the areas of economic activity which are taxed, as broad as possible in order to keep rates of tax as low as possible. Ironically, the tendency under devolution has been for scale of reliefs from non-domestic Rates to be widened (in 2018-19 totalling £237.5m). This is not a good approach to taxation policy in so far as greater burden has to be applied to those who are defined within the tax base.
- It is sometimes argued that the acceptability of a tax or charge increases if it is known that revenues raised are ring-fenced to a dedicated area of public spending. This situation is called a hypothecated tax. People might be happier to pay Vehicle Excise Duty or the duty on petrol or diesel if they knew the money raised would be used to eliminate pot holes etc. Or, it is argued, people do want more spending on the health service and so would pay a an additional NHS tax etc. etc. Traditionally, there has been resistance within the UK fiscal system to hypothecation, the Treasury disliking its "inflexibility". Designing a NHS tax for NI would be very challenging- not least because total health department spending exceeds the sum of the two biggest regional taxes combined, i.e. Income and VAT.[Note 1.]
- If you think a potential benefit of fiscal devolution is greater accountability you will be most concerned to devolve some of the bigger taxes (those with larger amounts of revenue raised). In NI the three largest taxes are: Income (about £2.9bn in 2018-19), National Insurance Contributions (NICs) (c. £2.7bn in 2018-19) and VAT (c. £3.4bn in 2018-19)- source: HMRC 20 December 2019, *A Disaggregation of HMRC Tax Receipts for England etc.*. However, see below re. specific comments about the desirability of devolving Income Tax and the feasibility of devolving VAT or NICs. In practice, the range of taxes in Northern Ireland where the feasibility of devolution is greatest tends to represent the smaller ones.
- Increasing accountability re. public expenditure decisions and the ability to raise additional revenues to fund plans for increased public spending are two arguments for increased tax varying powers. An increased ability to use tax variation to incentivize "good" behaviour or disincentivize "bad" behaviour is other important possible reason. Just as such tax policy can be pursued at a UK-wide level, it could also be operated at a devolved level. The public (and politicians) have become familiar with the concept of "sin taxes", e.g. the excises or duties or taxes on alcohol, cigarettes, disposable plastic bags and sugary drinks. Notwithstanding the important moral and philosophical debate about how far the state should making such paternalistic interventions to influence individuals behaviour ("nanny state"?) there is some statistical evidence that such taxes do work in the sense that higher sales prices lead to less consumption, less alcohol abuse etc. etc.

  We are likely to see even more taxation of behaviour which leads to environmental harm: production of greenhouse gases, congestion, production of waste. There are already some environmental taxes in place which are under-used at the UK level because of lack of political will, e.g. the provision to increase duties on petrol and diesel which has been unused for a decade as the rate has remained frozen at 57.95p per litre. There are also cases of taxes which have been billed as "green", but are not well designed from an environmental point of view: notably, the APD (because it is not strongly related to the amount of carbon being produced and does not necessarily incentivize airlines to operate well-filled and highly fuel efficient aircraft: see ***www.parliament.uk*** "Select Committee on Treasury Fourth Report, "environmental taxes"", accessed 21 April 2021).

Fiscal devolution: Which taxes and charges

- Domestic water charges. Placed at "the top of list" not because it necessarily the best piece of taxing and charging which could take place but because it is something that Stormont certainly has the power do and is **probably the one single change which could make the greatest impact in terms of extra revenue raised- over £200m** p.a. From an equity/fairness point of view it is worth reflecting that the *absence of that £200m+* from NI public spending probably impacts most on lower income groups (if one was concerned about the distributional effects of charging for water this could probably be addressed in various ways, e.g. an allowance of an amount of free water for lower income households). It is sometimes argued that it would be wrong to introduce such charges given that households “already pay for their water through their Rates”. The evidence suggests this argument is not as convincing as it might seem given that the sum of Council Tax+ Water charges in GB far exceeds the Rates payments. For example, in 2018-19 the average Rates payment per household in NI was £970 but that contrasted to total household charges of £1826 in Wales, £1742 in England and £1516 in Scotland: Richard Ramsey 28 January 2020, “New approach isn’t just for January”, *Irish News*. Earlier but similar figures were produced by Department of Finance (November 2017, “Budgetary Outlook 2018-20”).

- <u>The Regional Rate</u>. Stormont could raise **additional revenues by, for example, uplifting the annual increase above the inflation rate**. In 2017, for example, the Department of Finance estimated an increase of 5% in real terms for domestic Rates and constant real terms non-domestic Rates could raise £35m annually.
- <u>Other Charges</u>. Some commentators have suggested the total loss of revenue (annually) given so-called **“super parity” (i.e. the extent to which, on average households in NI are charged less for services than their counterparts in GB) amounts to £500m annually** (see Richard Ramsey 11 November 2014, “Next generation will pay for our “super parity” party”, *Irish News*). Examples include the relatively low level of Tuition Fees and prescription charges (zero) as compared to England. Particularly, question begging is the free public transport for those aged 60-64.
- <u>Income Tax</u>. Of the big three taxes (in terms of revenue), i.e. Income, NIC and VAT, this is the one which is **most feasible to devolve**. This is indicated by the experience in Scotland and Wales. It would be very hard to devolve NICs whilst preserving parity in the UK welfare system and as regards VAT, EU law probably prohibits variations by region. NI probably remains subject to the EU rules. Careful thought needs to be given to any devolution of Income Tax. For many years the Scottish Parliament had some Income Tax powers and they remained unused. Even now, the extent to which Scotland’s Income Tax schedule differs from that in the rest of the UK is still limited.[Note 2] Just under half of Scottish Income Tax payers now pay more (for most a little more), just over half pay less (for most a little less) and the net gain in terms of extra revenue raised has been small.

  Stormont needs to ask itself whether it would really wish to set its own Income Tax policy and if it does for what purposes. Answering the latter question may not be straightforward especially given likely policy conflicts or trade offs. For example, a redistributive policy might focus on cutting tax rates for lower incomes whilst raising those much further up the income schedule but that policy may not much increase the total amount of tax revenue collected. In theory, total revenue could even decrease. At the UK-wide level there has been the experience of the introduction of the 50% Additional Rate in April 2010 on incomes greater than £150,000. That rate was reduced to 45% in 2013. The additional yield from the 50% was much less than projected although there is dispute about how much of this was caused by “longer term” behavioural change and how much was the result of a one-off adjustment whereby £16b-£18bn of income was brought forward into the 2009-10 tax year. [Note 3.]

  If the priority was **to secure an increase in revenue raised that is most likely to come about by increasing the rate paid by many Basic Rate taxpayers** in NI to a level above the current 20%.

  The basis for these assertions is partly that the number of Higher (i.e. 40p) and Additional (i.e. 45p) taxpayers is very small compared to the number of Basic Rate payers: for 2020-21 62,000 and 5,000 compared to 714,000 (HMRC 26 June 2020, “Number of taxpayers by country”).

- APD. Important to note this has already been *partially* devolved, i.e. for the long haul (such as trans-Atlantic). There **may be a case to go the whole way**. APD is not a large source of revenue in NI (about £70m p.a. in total prior to the Covid crisis) but there is likely to be some disincentive effect to air travel and growth of the tourism (and other) sectors from the implied higher cost of air tickets. To the extent that cutting APD led to increased air traffic there would be some environmental costs notwithstanding that APD was not optimally designed from the point of view of discouraging carbon production.
- SDLT and Landfill. Devolution is certainly doable (again, Scotland and Wales show this). “Small taxes” in terms of amount of revenue raised. **Possibly not very large policy gains from varying the NI rate from the UK one.** [Note 4.]
- Corporation Tax. The power to vary has been in place in 2016 but remains unused. A precondition of use is that the NI Budget is able to bear the strain of a reduction in the Block Grant. Two recent changes (Chancellor Sunak’s increase in the UK rate back to 25% in 2023 and Biden’s tax increase proposals for the USA) imply **there *is a case* in terms of improving business competitiveness for NI sticking at the current 19%** as rates increase elsewhere In the UK but the “price” of so doing would be a substantial reduction in the Block Grant. [Note 5.]
- Summary In terms of both feasibility and ability to improve the competitiveness and growth of the economy there is a case for using the Corporation Tax powers and devolving the rest of APD although the former has to be weighed against the loss of Block Grant and for the latter against any adverse environmental impacts. Stamp Duty and Landfill are feasible but that has to be weighed against the administrative cost and it is unclear whether there is scope for very dramatic outcome gains from varying rates from those in rUK. [Note 4.] In principle, the Assembly/Executive should **re-assess whether the current reliefs from Rates are fit for purpose. Also, there is scope to raise revenue through charging- notably but not only domestic Water charges.**

How much has changed since the 2013 NICVA Report on Fiscal Powers?

In broad terms, the arguments in this Written Statement are the same as those set out eight years ago in the NICVA/PwC Report *Fiscal Powers: A Review of the Fiscal Powers of the Northern Ireland Assembly.* If anything, the case for further fiscal devolution, and certainly for **more discerning use of existing powers, especially regarding charges**, has increased:

- Post-Covid increases in the **Block Grant (and Barnett consequentials) may be more limited**.
- The UK government (HM **Treasury) may be “maxed out”** in terms of scope for further (relatively generous) financial packages to NI.
- The experience of the NI Executive during 2013-21 might suggest there would be benefits from **increased fiscal self-responsibility and the associated fiscal discipline**.
- During the 2007-17 period devolution leant towards reducing taxes/charges relative to GB (hence creating a “super parity”), it may now be **necessary to lean in the opposite direction**.
- The external policy environment may be moving towards a situation which would imply the **benefits of creating a lower rate of Corporation Tax** in NI compared to rUK. The “pain” related to such a policy would probably be a reduction in the Block Grant- hence confirming the previous point about **the necessity to raise some other charges**.

Note 1

In the 2021-22 draft Budget the allocation to the Health Department for Resource (i.e. current) spending was £6451.9m and the capital allocation £326.5m, i.e. a total of about £6.8bn. The total revenue collected from the Income Tax and VAT in NI is unlikely to much exceed £6.5bn (the amounts in 2018-19 were £2.9bn and £3.4bn respectively and since then the 2020 recession will have reduced the amount of tax receipts).

Note 2

The Scottish Government has “bent” the tax schedule to make it a bit more “progressive” (i.e. higher rates on higher incomes, lower rates on lower incomes) than its “rUK” (i.e. England, Wales and Northern Ireland) counterpart. The first two thousand pounds above the Personal Allowance are taxed at 19% rather than the rUK’s 20%. A rate of 21% kicks in at £25.3k. The higher rate (41% rather than 40% applies from about 44k rather than 50k (in both Scotland and rUK and additional rate applies from £150,000 onwards but that rate is 46% in Scotland and 45% in rUK). Fraser of Allander (FoA) Institute estimated that in 2020 anyone living in Scotland earning about £27,000 or less would be paying less Income Tax than his/her rUK counterpart. The converse was true for incomes above £27,200. The Scotland “penalty” in tax terms being about £125 on earnings of about £40,000 and £1540 for earnings of £50,000.

The Scottish Government estimated that the Scottish Income Tax differentials would have led to £591m of extra revenue collected (compared to using rUK rates etc.) all other things being equal but once behavioural changes were allowed for (less labour supply by the higher income, avoidance, migration) that gain was £456m in 2020-21. FoA also make the point that the true net gain to Scottish tax revenues through tax devolution was probably much less than £456m given that the Scottish income tax base was growing more slowly than rUK (i.e. England). Fraser of Allander Institute website 11 March 2020, “Higher income taxes and public spending in Scotland?”, accessed 21 April 2021.

Note 3

There is great uncertainty about the impact on total revenue collected of various tax scenarios and that uncertainty may be even greater at the NI regional level.

It has been suggested at the UK level that the positive responsiveness of tax revenues to increased tax rates is low for very high rate Income Tax payers (see M. Brewer and J. Browne, “Can more revenue be raised by increasing Income Tax rates for the very rich?”, *Institute for Fiscal Studies Briefing Note BN84*). This is because the very rich may engage in various behavioural responses which act to reduce the amount of Income Tax paid (e.g. work less, avoidance, emigration). Note 2 shows how in the case of Scotland a negative effect from behavioural change has been indicated as a result of raising Income Tax on above average incomes. At the NI level it might be asked how far an increase in the tax rate for high income individuals may lead to some of those individuals shifting their tax residence to GB or the Republic of Ireland?

Note 4

In terms of Landfill and waste there is an interesting question as to what might happen to the incentive to divert NI waste from landfill to exports (whether legal or illegal) to the Republic of Ireland. In the early 2000s a large increase in landfill charges in the Republic of Ireland contributed to 250,000 tonnes of waste being illegally dumped in NI.

Regarding Stamp Duty, at least before the current 2020 and 2021 “holiday” during the Covid recession, the existing £125,000 threshold is already quite high compared to the average level of house prices in NI. According to the official measure of prices (Department of Finance’s for Quarter 4 2020) nearly half of transactions in NI would not be required to pay Stamp Duty in any case at the existing threshold: in Quarter 4 2020 the median house price was £146,000 and it was only in 2017 that the median price recovered sufficiently to rise above the £125,000 level.

Note 5

Interestingly, both the (never used) “2017-19 option” in terms of creating a NI-rUK Corporation Tax rate differential (i.e. going from the UK’s 19% to the Republic of Ireland’s 12.5%) and the “2023 option” (i.e. sticking at 19% rather than going up to 25%) are about (roughly) the same % point difference. However, as economists might put it, the effects may be “non-linear”- diminishing returns to the policy of cutting Corporation Tax may set in as rates get lower and lower (many countries and not just the Republic of Ireland now have low nominal and effective rates) but the relative “damage/harm” (e.g. in terms of discouraging inward investment) may increase disproportionally as rates start to go up again.