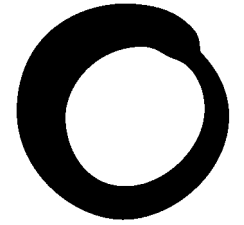


June 2011



**Friends of
the Earth**
Northern Ireland

Consultation response

Rebalancing the economy

Introduction

The consultation by the UK Government on 'Rebalancing the Economy' has focused attention on the question of lowering corporation tax in Northern Ireland. The issue is not just whether the benefits or costs associated with the proposal will be positive to the Northern Irish economy. The fundamental issue for Friends of the Earth is that we are asking the wrong question. The question is not whether we should lower corporation tax but to ask, 'in what ways do we want to rebalance our economy and what are fiscal and tax measures that need to be put in place to meet that goal?'

Friends of the Earth fully supports the need to rebalance the economy

More than ever we need a new economic vision to create a sustainable economy for Northern Ireland. Friends of the Earth believes we should develop a model of consumption, investment and development that is fair, works within ecological limits and creates long term stability. The debate should start by asking what is the economy for, how will it be sustained and for whom should it benefit? Re-thinking the economy is the first task. To begin this task we should be debating the preferred

Friends of the Earth inspires solutions to environmental problems, which make life better for people.

Friends of the Earth is:

- dedicated to protecting the environment and promoting a sustainable future for Northern Ireland**
- the UK and Ireland's most influential environmental campaigning organisation**
- the most extensive environmental network in the world, with over 60 national organisations across five continents**
- a unique network of campaigning local groups working in over 200 communities throughout the UK and Ireland**
- dependent upon individuals for over 90 per cent of its income.**

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economic model and discuss options for development and prosperity including GDP, competitiveness and growth but not excluding other models.

Most importantly we need to develop a model that addresses the massive switch required in this decade to renewable energy to reduce our greenhouse gas emissions and to make our economy safe and resilient. It is illogical that we are one of the most oil dependent countries in the world yet we have some of the most abundant reserves of free, clean, safe and stable energy [1].

We must 'rebalance the economy' but at the right speed and in the right direction. In Friends of the Earth we call this direction the low carbon economy.

Rebalancing for the low carbon economy - some principles

The debate on 'rebalancing the economy' should be realigned from merely pushing the scales further in the direction of increasing short term corporate opportunism to addressing real job opportunities through principles of equality, energy security and increased economic self reliance and security. Friends of the Earth believes the following principles should frame this debate:

1. *Supporting local business*

We should intelligently rebalance by supporting more indigenous industry and commerce as this investment is most likely to stay in Northern Ireland, create a more entrepreneurial culture and have a stronger multiplier effect on other jobs. We must re-think the practices of Invest NI subsidising multinational companies and prioritise instead more indigenous industry and local firms;

2. *Targeting low carbon industries for support*

We should strategically rebalance in favour of low carbon projects and industries. For example, at least 24,000 jobs could be created if the government grasps the diverse opportunities across all business sectors in the Green New Deal. The first phase of the Green New Deal was to cost the public purse £72 million and demonstrated how a home energy efficiency programme could lever £230 million of other funding, dramatically reduce winter deaths and illness by alleviating fuel poverty, tackle climate change by reducing carbon emission and secure 2,000 jobs;

3. *Planning for a new energy future*

More renewable energies and smarter grids will give us the twin prizes of price security and energy security in the future. This means developing tidal and off-shore wind energy, a strategic approach to conventional wind farms and a huge boost to farm-scale anaerobic digestion.

The crisis caused by over dependency on finite reserves of fossil fuels has already started. As one of the most highly dependent countries in Europe on oil and gas, we are more than vulnerable to inevitable increases in prices due to volatile world politics and 'peak oil'. This dependency will ultimately cripple Northern Ireland's economy unless a radical change in direction is put in motion by this new Assembly. With renewables we will keep energy prices stable, have a consistent long term supply and reduce atmospheric pollution. Infrastructure development, research and supply chain investment could be

centred in Northern Ireland.

This is a unique investment challenge and the Government must show leadership in making this investment happen.

- *Creating more resilience and stability*
We are now entering politically stable times yet economic uncertainty remains with growing unemployment, unskilled young people, bankruptcies, mortgage foreclosures and cuts to public expenditure. Resilience does not just mean energy security. Developing food security and banking security are two areas in which we could support more jobs and promote stability through promoting mutualised and cooperative forms of governance.
- *Rebalancing must deliver economic justice*
Vulnerable citizens, and those in disadvantaged areas, must be allowed to benefit from our investments and economic policies. This should start by rebalancing transport investment away from new roads to bus, cycling and rail. In the banking world the 'culture of greed' has returned, if it ever went away. A fairer and more consistent planning system should explicitly serve the public interest and not narrow private interests. A transparent system of planning with much more weight given to agreed local plans would give both consistency and speed to decision making.
- *Measuring prosperity*
A principle of rebalancing is to measure economic progress through an understanding that real wealth comes from working within the finite limits of the earth and by having a more equal and contented population. It is absurd that activities that add to GDP include accidents, divorce, deforestation, crime, pollution and natural disasters. An economy should not be measured in GDP but judged by how it affects the social, environmental and cultural life of an area it serves. It is not tenable to use GDP as a measure of economic, social or environmental progress. Numerous reports have indicated that the rising tide does not lift all boats. Furthermore, growth in GDP does not always translate into increases in living standards [2].
- *More effective regulation*
Robust economies such as Sweden and Germany are characterised by effective and consistently applied environmental regulation. The Aldersgate group, supported by some of the UK's largest companies, argues that regulation is an essential tool to stimulate growth and that crude deregulation damages competitiveness [3]. The report questions whether de-regulation makes sense to address pressing environmental challenges such as climate change. Recent market failure and a reduction in business confidence requires more, and not less, regulation to safeguard the environment and drive growth in new industries.
- *Rebalance the debate by listening to others*
Some have cogently argued in Northern Ireland that it is not that the public sector is too big but that the private sector is too small. However their voices are not given appropriate weight. Numerous models of rebalancing should consider the thinking of policy initiatives such as FEASTA, The New

Economics Foundation, the Sustainable Development Commission and the Ecumenical Council for Corporate Responsibility. Analysis by Government is limited by the powerful influence of vested interests advocating business-as-usual solutions that tend to reinforce the structural deficiencies that cause the original problems.

Reasons to oppose the lowering of corporation tax

Friends of the Earth is strongly opposed to a lowering of corporation tax for the following reasons:

1. *Profiteering will increase*

Only a few public companies registered in Northern Ireland pay the full rate of corporation tax and their profits tend to leach out of Northern Ireland. Other companies will simply use Northern Ireland as their registered address, thereby paying the lower rate. Creative accounting will be used to shift profits from where they arise to Northern Ireland. A displacement of investment from Great Britain, potentially from deprived areas, will result generally in less economic activity and tax revenue.

2. *Unfairness will be created within the private sector*

A major problem will result in affecting trade between Northern Ireland and Great Britain if differential tax rates are applied. To stop companies falsely pricing goods as a means of transferring profits to a lower tax regime, HM Treasury would have to impose the significant administrative and financial burden of transfer pricing rules.

Within Northern Ireland the SME sector will not necessarily benefit from the measure and will probably be put at a disadvantage. In any event, corporation tax is not a major determinant for business investment especially for SME's, which make up the vast majority of Northern Ireland's economy. SME's employ over 65% of the private sector workforce and 95% of businesses employ fewer than 10 people. The determinants of domestic investment are complex and varied but in a survey carried out by the Federation of Small Business in 2009 lowering corporation tax came joint fifth in a ranking of factors that would stimulate the economy.

3. *Too Risky a Strategy*

Around £300 million will have to be found out of the public purse to offset the cost to the economy as a result of less tax revenue and this will dramatically affect public services. (The Minister for Finance and Personnel has recently stated that this could be as high as £385 million). Richard Murphy says we are "playing roulette with public funds and hoping for a win". The Varney report [4] argues that the case for a 12.5 % rate of corporation tax cannot be made: "It is clear from this initial assessment there would be an upfront cost of near £300 million per annum in lost corporation tax receipts with no cost recovery in terms of tax receipts in a reasonable period of time".

Losing a significant resource (around £300million) from the public purse for the benefit of the shareholders in these companies does not seem to be in Northern Ireland's interests.

It is highly unlikely that extra business activity will be generated to offset the cost of reduced government caused by the falling off in corporation tax. Indeed, a major risk is that competitors in Scotland and Wales who will have as strong a case to lower their own taxes would erode any advantage Northern Ireland may have gained. Indeed, Income per capita in Northern Ireland is £1,000 higher than in Wales so any justification to lower tax on the grounds of economic deprivation should be applied in a more compelling way to Wales.

4. *Parity between North and South is not desirable*

We should not try and compete with the Republic of Ireland's regime as it facilitates tax avoidance, allows for the 'brass plating' of companies, is effectively a tax haven to avoid all taxes, has ineffective foreign company laws, invites easily achieved corporate secrecy and is in the Eurozone. Lord Oakeshott referred to Dublin as "Liechtenstein on the Liffey" and "Cayman Islands in a cold climate" and warned that when you attract mobile money from around the world you run greater risks when things go wrong [5].

The loopholes and exemptions that exist in the Republic could never be matched in the UK. Moreover, in terms of the EU as a whole the UK is already the sixth lowest tax economy and is considered very favourable to business.

5. *There is no evidence that it will assist FDI, even if more FDI is considered desirable*

The debate on corporation tax has ignored the fact that the strongest economies in the world have corporation taxes higher than 25%. Furthermore, there are no guarantees that extra jobs will be created as argued in the Wilberforce Society's report [6] and ICTU's report, *Pot of Gold or Fools Gold* [7]. These reports have never been challenged. Pricewaterhouse Coopers have written "in our research...we could not find any clear evidence of a simple correlation between low Corporation Tax per se and high levels of FDI" [8]. Those arguing for a reduction in corporation tax have made sweeping predictions of guaranteed investment returns to 2030 when predictions to 2013 cannot be made with any accuracy.

There is compelling evidence of the problems that will arise if an FDI approach 'at any cost' were to be adopted. A lower rate of corporation tax may attract some inward investment but the experience from the Republic of Ireland and elsewhere is of communities being devastated when the inward investment is withdrawn and business is transferred to Eastern Europe or South East Asia. The experience of communities in the Republic of Ireland such as Youghal demonstrate the economic failures that can so quickly result by pursuing indiscriminate support for all FDI [9].

Recruiting more FDI has been relentlessly pursued in NI since the 1960s. This is not new and we have seen the effect that it can have when companies close and relocate.

6. *More than a hint of unlawfulness*

The implications of the Azores judgment [10] is that in order to be legal under

EU law any costs or benefits from reducing corporation tax must accrue solely to Northern Ireland. Demonstrating open tax accrual will require significant administrative challenges and costs. Furthermore, the paper by the Wilberforce Society suggests that to be compliant with EU law all tax power would have to be devolved to Northern Ireland.

The implication of this is that the entire Barnett Formula (which determines the size of the Stormont Block Grant to Northern Ireland) would have to be overhauled to accommodate the Azores judgement.

Another issue is the lack of an Impact Assessment being carried out with this consultation. This should have been the mechanism to tease out this and many other issues and the fact it appears this has not been carried out is not only against HM Treasury's own guidelines but is potentially challengeable on legal grounds.

Reasons to support devolving certain tax powers

Friends of the Earth would generally support the devolution of new revenue streams whether they are charges, rates or tax varying powers and whether they are tax relief or impositions. What is clear from the above is that all tax powers would have to be devolved and this has major constitutional implications for the integrity of the United Kingdom.

That said, revenue streams should either be progressive (with those earning more paying more relative to income) or should have an agreed social or environmental objective. For example, water charges and congestion charges could be introduced. A congestion charge on retail centres and town/city centres can provide both revenue streams and relieve congestions. Charging can deter parents from taking their children to school by car and encourage the benefits of walking and cycling.

Friends of the Earth would also welcome powers being devolved to close down the mechanisms by which tax avoidance takes place. This could significantly increase the revenues available for desirable public benefits such as health, housing and tackling climate change.

Conclusion

Friends of the Earth believes that a tax reduction for a limited number of already profitable companies is a red herring driven by dogma and self interest. It is not in Northern Ireland's interest to cut corporation tax unless it is targeted to specific initiatives to drive the low carbon economy or to develop a fairer tax regime to assist SME's, the mainstay of our economy. It may not be in the interests of the UK as a whole.

Proposed business investment is too uncertain, the costs are too severe by forcing reduced government spending and the proposal is potentially unlawful. There are many other more targeted ways to improve the local economy such as the Green New Deal, with far fewer risks and which can guarantee success.

Cutting corporation tax is an irrational proposition devoid of any process of deductive

reasoning. A valid question is asked – how do we rebalance the economy? A fallacious syllogism is reached, namely lowering corporation tax. It is a syllogism based on two false and absurd premises – firstly the belief that FDI is necessary and will bring economic prosperity and secondly that, in the words of Owen Patterson, there is no Plan B.

The priorities for economic policy in Northern Ireland must be to create a new low carbon economy that provides for energy and food security, as well as dealing with social exclusion, poverty and unemployment. We should pose that scenario first and deal with the real question: "How do we get there - fast?".

[1] The Foundation for the Economics of Sustainability's most recent book, *Fleeing Vesuvius*, attributes the cause of the global 2008 market failure to the over exploitation of the world's resources driven by our reliance on declining oil and gas. Our addiction to what is described as a "grotesquely unsustainable energy system" also means the problems of peak oil will be compounded by accelerating climate change and the destruction of ecosystems.

[2] Report by the Commission on the Measurement of Economic Performance and Social Progress. <http://www.stiglitz-sen-fitoussi.fr>

[3] The report launched in June 2011 is called 'Dealing with deficits : best value regulation to reduce our environmental and financial debts'. <http://www.aldersgategroup.org.uk/reports/>. Peter Young, Chairman of the Aldersgate Group, said: "It is a myth that all businesses want less regulation. Effective green laws create a level playing field which drives efficiency, early action and the innovation in UK companies that will be the engine for future growth and jobs."

[4] The Varney Report (2007) 'Review of Tax Policy in Northern Ireland'.

[5] House of Lords debates 8 December 2008

[6] http://thewilberforcesociety.co.uk/wpcontent/uploads/2011/05/TWS_Corporation_Tax_NI.pdf

[7] Murphy, R. (2010) Lowering Northern Ireland's Corporation Tax: Pot of Gold or Fool's Gold.

[8] PricewaterhouseCoopers (2011) 'Corporation Tax: Game Changer or Game Over?' p. 6.

[9] "All the town's big factories are now closed. Elba, Couristan Carpets, Technicolor Home Entertainment, Artesyn Technologies. They have all shut down over the past decade, leaving at least 2,000 people without jobs. The last employees in the only remaining factory, Tytex, a Danish medical-textiles manufacturer, were let go a year ago. Tytex, which employed up to 150 people, said it was pulling out of Ireland because it couldn't afford the high labour costs; it relocated the factory to eastern Europe. When a town loses between 2,000 and 2,500 manufacturing jobs in a few years the shock waves reverberate through the lives of former employees and shake the commercial heart of the town. While other towns were bustling, the

manufacturing industries here were beginning to relocate to Asia and eastern Europe, for their cheaper labour. Political leaders insisted that new multinationals with higher-skilled work would take their place. But none did.” This article is taken from the Irish Times referring to Youghal

<http://www.irishtimes.com/newspaper/weekend/2011/0402/1224293621909.html>

[10] Summaries of Important Judgments: Case C-88/ 03 Portugal v. Commission, judgment of 6.9.2006 State aid – Tax scheme in the Azores, European Commission Legal Service.