HM TREASURY

Rebalancing the Northern Ireland economy:

a summary of consultation responses

December 2011

HM TREASURY

Rebalancing the Northern Ireland economy:

a summary of consultation responses

December 2011

ISBN 978-1-84532-918-1
PU1222

Contents

1 Introduction

Overview

1.1 On 24 March 2011, the Government published its consultation paper *Rebalancing the Northern Ireland Economy.*[1] Rebalancing the Northern Ireland economy is a shared objective of the Government and the Northern Ireland Executive (NIE).

1.2 The consultation document described the policies of the UK Government and NIE for rebalancing the Northern Ireland economy and considered among other options, the issues involved in the devolution of corporation tax setting powers, in order to allow the Northern Ireland Assembly to reduce the corporation tax rate in Northern Ireland.

1.3 Over 700 responses were received to the consultation. Most of these focused on corporation tax, while also recognising the importance of non tax policies. There was a large amount of support for the devolution of corporation tax, with around three quarters of respondents in favour, given the positive impact they felt it could have in the shared objective of rebalancing the Northern Ireland economy. However, support has not been universal and a number of respondents pointed to the complex issues inherent in devolving these powers, many of which were identified in the consultation document as requiring extra work and consideration.

1.4 The Government has established a joint ministerial working group on rebalancing the Northern Ireland economy, comprising of ministers of the UK Government and the NIE, to consider issues raised by the consultation. This group met for the first time on 15 December 2011. The NIE, in its recently published draft Programme for Government, have indicated that they will press for the devolution of corporation tax.

1.5 No decision has yet been made on whether to devolve corporation tax. A decision will be taken following the conclusion of work developed by the joint ministerial working group, which is expected in summer next year.

Summary of the consultation document

1.6 The issue of rebalancing the economy, while particularly relevant in Northern Ireland, is also applicable to the UK as a whole. The Budget, the Spending Review, the Autumn Statement and the Growth Review set out the Government's overall strategy for rebalancing the UK economy. The consultation document surveyed the current state of the Northern Ireland economy, and concluded that there is a particular case for additional measures to support rebalancing in Northern Ireland bearing in mind its strong dependence on the public sector, the legacy of the Troubles and its land border with Ireland.

1.7 The consultation considered, among other issues, the case for devolution of corporation tax rate setting powers to Northern Ireland. The aim of the consultation was to gain a fuller understanding of the costs and benefits that a separate rate would involve for Northern Ireland and for the rest of the UK, and to consider potential mechanisms for introducing a separate

[1] Rebalancing the Northern Ireland Economy, HM Treasury, March 2011

rate. It sought views on the policy principles of whether to devolve corporate tax rate setting powers to the NIE, rather than on the details of the policy design.

1.8 The document discussed the potential for a reduction in corporation tax rates to have a positive impact on the Northern Ireland economy and the effect it could have on attracting investment to the region. Under the European Court of Justice's "Azores Judgement", the NIE would have to meet the costs of a corporation tax rate reduction from a reduction in the block grant. Estimates of this cost were provided in the consultation document.

1.9 The paper set out in high level terms the issues involved in setting up and administering a separate corporation tax system for Northern Ireland and invited initial views on the possible administrative costs for business. The document also discussed ways in which the costs of introducing a corporation tax rate reduction could be managed.

1.10 Other tax options were also considered, including R&D tax credits, an enhanced annual investment allowance, training credits and an employers' NICs holiday.

1.11 The consultation document outlined the approach and scope being taken by the UK Government and the NIE for a wide range of non-tax reforms which are aimed at rebalancing the Northern Ireland economy.

Responses to the consultation

1.12 The Government recognises the importance of engaging fully with individuals, practitioners, businesses and other organisations in the development of tax policy. The best public engagement allows the Government to explore, develop and test new ideas to improve the tax system, and to build an evidence base to support policy decisions.

1.13 Consistent with the Government's general approach to tax consultation, the consultation document considered the devolution of corporation tax in high-level and principled terms.

1.14 The Government is grateful for the large number of responses received on the issue of rebalancing the Northern Ireland economy. These responses will be used to inform the work developed by the joint ministerial working group.

1.15 Over 700 responses to the consultation were received from a wide range of groups, including Northern Ireland businesses, business and sector representative bodies, accountancy firms, individuals, trade unions, political parties, local councils, think tanks and charities. Responses varied in style, from simple statements in favour or opposition to more detailed responses giving thorough answers to all questions asked. The large number of responses indicates a widespread recognition of the need to consider additional measures to address the particular circumstances facing the Northern Ireland economy.

1.16 Responses showed strong support for the rebalancing agenda. Around three quarters of responses were in favour of corporation tax devolution, of which around two thirds were from Northern Ireland businesses or business owners. Businesses responding to the consultation came from a wide variety of sectors, including construction, tourism, retail, manufacturing, services and agriculture. The majority of businesses responding were small and medium sized enterprises, in part reflecting the makeup of the Northern Ireland business population.

1.17 Support for corporation tax devolution also came from Northern Ireland business representative bodies, Northern Ireland accountants and accountancy firms, and some individuals who did not identify themselves as business owners. The main Northern Ireland political parties supported corporation tax devolution and there was also support from some think tanks.

1.18 The main arguments cited in favour of corporation tax devolution focused on potential investment impacts, growth impacts and employment benefits. Arguments were also made for creating a more 'level playing field' with the Republic of Ireland. These arguments are discussed in more detail in Chapter 2.

1.19 Opposition to corporation tax devolution was seen most strongly from trade unions and individuals not identifying themselves as business owners. Concerns were also raised by some UK-wide business and professional organisations, some think tanks and charities and some of the smaller political parties.

1.20 The main arguments opposing corporation tax devolution focused on the uncertainty of the impact and the costs of a reduction in the corporation tax rate, and on opposition to redistribution from the public sector to the private sector as a means of growing the Northern Ireland economy. Several respondents also focused on the potential risks, from a UK perspective, of breaking up the UK's unitary corporation tax regime. These arguments are discussed in more detail in Chapter 2.

1.21 In responses both for and against devolution, greater clarity on a number of issues was sought. In many cases these were issues already identified in the consultation document as requiring additional analysis, for example on expected costs and benefits of a corporation tax reduction, the design of a corporation tax regime, its impact on business and how a corporation tax reduction would be funded.

Government's approach to devolution

1.22 The Government is committed to strengthening the fiscal accountability of devolved administrations across the UK. To this end, it has introduced the Scotland Bill to strengthen and deepen the Scottish devolution settlement. It has established the Silk Commission, to review the powers of the National Assembly for Wales and examine the arguments for devolution of fiscal powers.

1.23 The consultation on rebalancing the Northern Ireland economy forms part of this broad agenda. Here, as in the other devolved administrations, the Government is seeking a balance. It wants to ensure the empowerment of all devolved institutions. At the same time, it must maintain the success of the shared economy on which all countries of the UK depend.

1.24 In particular, the Government must ensure proposals maintain incentives for business to trade, invest and be headquartered in the UK, that they do not impose unreasonable administrative burdens and that they support the competitiveness of the UK as a whole.

1.25 This balance will require careful analysis and close dialogue. The Government is committed to engagement with all administrations, to ensure this balance is achieved. Consideration needs to be given to how to best improve accountability through devolution of tax powers.

Next steps

1.26 Corporation tax devolution would be a significant change to the UK's corporate tax system, involving difficult issues which must be carefully considered before a decision is reached. Responses to the consultation showed that there are a range of views on the likely impacts of corporation tax devolution to Northern Ireland and that further clarity is needed on a number of issues, including over the fiscal and economic impact and over how this will be managed, the possible impact on business, the difficulty in designing a suitable corporation tax ringfence and the need for other policies such as supply side reforms to promote the private sector. The Government will also need to consider further the potential impact on the rest of the UK of devolving corporation tax powers.

1.27 The Government has not made a final decision about whether to devolve corporation tax to Northern Ireland. It has established a joint ministerial working group with the NIE to undertake further work to help inform this decision. Details of the joint ministerial working group are in chapter 3.

1.28 A decision on whether to devolve corporation tax to Northern Ireland will be taken following completion of this further work, which is expected to be in summer next year.

2 Summary of responses

Rebalancing the Northern Ireland Economy

2.1 In general responses showed strong support for rebalancing the Northern Ireland economy, which was viewed by many as vital for the region's economic future. As identified in the consultation paper Northern Ireland has a strong dependence on the public sector, the lowest wages and one of the lowest labour productivity rates in the UK. Additionally, rebalancing was seen by some as an important step to cement the peace process.

2.2 The nature of 'rebalancing' was not defined consistently across responses and respondents highlighted different aspects of rebalancing that they considered important. While most felt the focus should be on attracting high value foreign direct investment (FDI), creating associated skilled jobs and benefiting Northern Ireland growth, others considered the growth of indigenous businesses more important than attracting foreign investment. Some respondents felt that reforming the public sector and improving the productivity of public service delivery was vital to achieve a rebalanced Northern Ireland economy. Others felt that while the private sector needs to grow, this should not be at the expense of the public sector. Other aspects of rebalancing highlighted included an increased focus on achieving a low carbon economy and taking steps to ensure rural areas, as well as urban centres, benefit from growth.

Devolving corporation tax

2.3 Chapter 4 of *Rebalancing the Northern Ireland economy*, sought views on the potential impact of devolving corporation tax powers to Northern Ireland, in particular looking at the potential consequences of a reduction in the rate of corporation tax within Northern Ireland. This was the main subject of the majority of responses. Questions asked in the consultation document focused on the economic impact, costs and administrative impact of devolving corporation tax rate setting powers to Northern Ireland.

2.4 A high level summary of responses is given in Chapter 1. The majority of responses supported devolution of corporation tax rates, though most responses, including those fully in support, agreed that corporation tax is not a 'silver bullet' and would not alone transform the fortunes of the Northern Ireland economy. Other tax and non-tax measures, including skills, infrastructure and the planning system, were also highlighted as important in themselves, and also as a means of ensuring the maximum possible benefits from lower corporation tax.

Impact on the Northern Ireland Economy

2.5 There was strong support for the proposition that reductions in corporation tax would lead to additional growth in the Northern Ireland economy.

2.6 Where respondents identified the reasons why reduced corporation tax rates would stimulate activity, they tended to identify the impact lower rates could have on FDI, in driving greater internal investment and the effect a reduction would have on confidence in the Northern Ireland economy.

2.7 While there was widespread agreement that a reduced corporation tax rate would have a positive impact on the Northern Ireland economy, there was also uncertainty over the scale of this impact and, in some cases, concern that the benefits would not outweigh the costs.

The impact on domestic Northern Ireland businesses

2.8 The consultation received a large number of responses from Northern Ireland businesses and business representative groups. With very few exceptions these were in favour of reducing corporation tax within Northern Ireland. Businesses argued strongly for the growth benefits of a tax cut in Northern Ireland, many saying that lower rates of tax would improve the viability of their business or allow them to undertake additional activity. Businesses from a variety of sectors and of a variety of sizes felt a reduction in corporation tax rates could allow them to increase investment in their businesses or take on more employees.

Box 2.A: Comments made by domestic Northern Ireland businesses

"A reduced rate of corporation tax would make a difference to our business, by giving us the means for more capital investment, with capital investment comes growth, and with growth comes more employment which means more disposable income for the population."

"It is important for businesses in Northern Ireland to be able to compete on a level playing field as much as possible with our neighbour ROI."

"[Lower corporation tax rates] would allow me to invest for the future by hiring some suitable graduates and training them up as business consultants"

2.9 The main effects identified were the impact lower tax rates would have on the level of retained profits and on the post-tax return on capital investment. Some also argued that a lower corporation tax rate would increase general business confidence to invest, for example, on product or premises development or on increasing employment. It was argued that this would provide an alternative mechanism to fund investment in the light of potentially limited access to finance for some businesses.

2.10 There was some concern from trades union and other respondents that there is no guarantee businesses would reinvest increased post-tax profits, which could instead be distributed to shareholders in the form of dividend payments. Some were also concerned that all profitable businesses would benefit from a corporation tax rate reduction, including those that do not "need" a windfall.

2.11 The issue of Northern Ireland competitiveness was also raised. Several businesses, particularly those located close to the border, noted that competition from firms operating in the Republic of Ireland was having a detrimental impact on their business. It was argued that a lower corporation tax rate would 'level the playing field' with the Republic, and also allow Northern Ireland to compete more effectively with other low cost economies.

2.12 Reflecting the composition of the Northern Ireland economy, the majority of responses were from small or medium sized businesses. However, several large business representatives, for example at a consultation meeting in Belfast, expressed strong support for the devolution of corporation tax to Northern Ireland. Many of these saw the measure as vital for the Northern Ireland economy going forward.

2.13 While it was clear from responses that indigenous Northern Ireland businesses supported a corporation tax cut, with many viewing this as an opportunity to increase investment in their own business, many responses, particularly from organisations such as business and accountancy bodies, focused on FDI as the main channel through which rebalancing could be achieved.

Impact on Foreign Direct Investment (FDI)

2.14 A large number of responses proposed that a key benefit of lower corporation tax rates would be the positive impact this would have on the quantity and quality of FDI in Northern Ireland, in particular improving Northern Ireland's ability to attract high value-added activities, HQs and core business functions, as well as operational functions. In addition, several responses highlighted that possible reductions in Selective Financial Assistance in 2013, as a result of changes in EU State aid rules, mean that Northern Ireland may require other drivers to attract FDI.

2.15 Many responses discussed the potential benefits to the local economy from the associated spillover and supply chain effects of greater levels of FDI, with opportunities for indigenous companies to supply products or services to new companies locating in Northern Ireland. For example, one respondent said their businesses would benefit from lower corporation tax rates because they would "create more opportunities to sell my products to other businesses - new companies locating here and other local companies which supply them". Similarly, some responses noted the positive benefits of technology and knowledge transfer if certain types of businesses chose to set up operations in Northern Ireland.

2.16 Some respondents argued that the magnitude and quality of the FDI impact was not guaranteed. For example, rather than productive FDI which has wider benefits, a lower corporation tax rate could create an incentive for 'brass plating' or profit shifting, in which no or little associated activity would accompany the location of companies in Northern Ireland. This is discussed further in the 'Cost' section below.

2.17 The consultation sought views on the extent to which headline corporation tax rates impact FDI decisions. At the London consultation meeting, it was generally agreed that headline corporation tax rates have a useful signalling impact and could attract more international attention to Northern Ireland as a potential location for investment. Attendees argued that final investment decisions will depend on effective tax rates, as well as the wide range of factors that influence investment decisions including labour costs, proximity to markets, infrastructure, energy costs and political stability. Attendees additionally stressed that the level of administrative burden for businesses would be dependent on the complexity of the tax system put in place, especially the level of anti-avoidance rules, to ensure access to any lower Northern Ireland rate was limited to genuine economic activity.

2.18 Responses were divided on the importance of the corporation tax headline rate in explaining the high levels and quality of FDI in the Republic of Ireland. Some respondents believed this has been a fundamental determinant of Republic's attractiveness to foreign investors and its subsequent economic growth. Others noted that the Republic's more generous business tax regime, particularly the treatment of foreign profits and intellectual property, creates in some circumstances a significantly lower effective rate than the headline rate alone implies.

2.19 A number of respondents also pointed to the wide variety of explanations for the Republic's growth, including EU investment in Irish infrastructure, strong supply side skills policies, an effective inward investment strategy, the availability of non-tax related grants and incentives, Euro membership, as well as a different global economic and FDI environment during the period of strong Irish growth.

2.20 Building on Northern Ireland's existing strengths, many respondents suggested that non-tax policies such as skills development and marketing of 'NI plc' would also encourage increased levels of FDI, particularly high value-add FDI. (Non-tax policies are discussed below).

Estimates of the impact

2.21 The consultation document estimated that reducing corporation tax rates to 12.5% in Northern Ireland would lead to an increase in domestic investment of around £110m by year 10 and an increase in gross FDI of around £310m by year 10.

2.22 Alternative estimates of the impact were given by the Economic Advisory Group[1] (EAG), for example they estimated that the Northern Ireland economy would be 13.8% larger by 2030 following a reduction in the corporation tax rate. These estimates were quoted by some respondents in favour of corporation tax devolution; others had concerns about the assumptions and methodology underpinning them. The EAG estimates are not directly comparable to the numbers published in the consultation document as they published estimations of different measures of the impact.

2.23 Respondents who compared estimates felt they were unable to draw firm conclusions due to the lack of clarity on expected benefits, for example noting that "there are considerably different opinions as to the potential impact on economic growth and employment of reducing the rate of corporation tax in Northern Ireland. These different opinions on the potential benefits of a reduced rate have to also be weighed against the different estimations of the potential costs to the Northern Ireland Executive." A number of responses expressed concerns about the uncertainty of the benefits, viewing corporation tax devolution as a 'gamble'.

2.24 There was widespread support in responses for pro-employment policies. Many responses cited increased employment, potentially in high value-add FDI companies, as a significant benefit of lower corporation tax rates, particularly as this may have the additional benefit of improving opportunities for young graduates and other skilled workers in Northern Ireland. While the consultation document did not include estimates of the expected impact on employment, estimates of very significant levels of job creation published by the EAG were endorsed by several respondents; others believed these estimates were optimistic.

2.25 Conversely, several responses expressed concern that there is no guarantee additional jobs would be created, particularly if businesses distributed increased post tax profits as dividends rather than using them to increase investment. Some respondents were also concerned that a reduction in corporation tax may be funded by a reduction in public sector employment, potentially resulting in an ambiguous impact on overall employment.

Corporation tax devolution and impact on the rest of the UK

2.26 Several responses expressed concern about the risk of breaking up the UK's unitary corporate tax system. Respondents argued this is seen as a competitive advantage for the UK, providing the simplest environment for UK and foreign businesses to operate in. The unitary system also minimises the potential for distortion of economic activity through artificial diversion of profits.

2.27 Some believed that economic inefficiencies could arise as firms react to considerations other than commercial factors when making location and investment decisions within the UK. There could also be risks for deprived regions elsewhere in the UK. Another consideration was the potential damage to the UK's commitment to provide stability and certainty in the corporation tax regime, and to the Government's tax simplification agenda.

2.28 Some commented on the potential for pressure to devolve corporation tax powers to Scotland and Wales (and England) and warned this could create a 'race to the bottom' scenario, negating much of the competitive impact of a lower rate in Northern Ireland but with a

[1] *The Impact of reducing corporation tax on the Northern Ireland economy*, EAG, May 2011

substantial Exchequer cost. It was argued that this scenario would also cause an 'economic drag' for the UK as a result of increase compliance costs for all affected UK businesses. It was also argued that UK growth could be hampered by external perceptions of the complexity of operating in such a multiple rate corporation tax regime, reducing the attractiveness of the UK as a location for foreign investment.

Cost

2.29 Devolving any tax rate varying power must satisfy the European Court of Justice judgment on the "Azores Criteria", which set out the conditions that would need to be met for regional differences in direct taxation not to involve State aid and to be compliant with EU law. One of these criteria states that the full fiscal consequences of a regional reduction in the national tax rate must be borne by that region.

2.30 The annual costs to Northern Ireland of a reduction in corporation tax rates to 12.5% were estimated in the consultation document to be in the region of £300-£350m. The cost estimates in the consultation document did not include the cost of reducing corporation tax rates on Northern Ireland branches of GB resident companies, which make a significant contribution to the NIE economy, as this analysis was not available. Further work is underway on these estimates and it is an issue which we expect to cover in the ongoing work plan with the NIE.

2.31 There was widespread agreement that further clarity is needed on the costs of a corporation tax reduction. Some respondents argued that the estimates presented in the consultation document were too high, based on growth assumptions that are too conservative and over-estimates of the likely behavioural impact; others felt the behavioural cost estimates for profit shifting and tax motivated incorporation (TMI) were too low.

2.32 Profit shifting arises where companies artificially manipulate transactions so that their taxable profits arise in low tax jurisdictions, while the activities generating those profits remain in a high tax jurisdiction. Some respondents felt the costs in the consultation paper were too high and that existing anti-avoidance legislation could adequately prevent substantial profit shifting. Others argued that the estimates in the consultation document were conservative, and unlikely to reflect the full potential for restructuring of corporate groups and their operations to benefit from the lower rate in Northern Ireland. It was also requested by some respondents that the Government avoids imposing overly onerous anti-avoidance legislation to minimise profit shifting, as this would have a negative impact on the attractiveness of Northern Ireland as a location to invest.

2.33 TMI arises when an individual incorporates with the primary reason of reducing their overall tax bill. Some responses suggested TMI costs in the consultation document were overestimates; others acknowledged that a 12.5% corporation tax rate could significantly incentivise TMI, which would have a significant cost.

2.34 Some responses noted that additional revenues from non-devolved taxes would improve the value for money of a corporation tax reduction to Northern Ireland and argued for their inclusion in the block grant adjustment, were corporation tax devolved.

2.35 A clear message from responses was that while the estimated costs presented in the consultation document are useful for informing the debate, more detail is needed to enhance the debate on the cost-benefit trade off.

Impact on public spending

2.36 In addition to uncertainty about the likely scale of costs, some respondents who opposed corporation tax rate reductions were concerned about the associated reductions in public spending. Concern over the impact on public spending in Northern Ireland tended to be combined with uncertainty over the potential benefits of the policy.

2.37 Concern was expressed by some respondents about the impact a reduction in the block grant could have on disadvantaged members of the community and on those employed in low paid public sector jobs.

2.38 Conversely, those in favour felt the cost of a corporation tax rate reduction was small compared to potential long run benefits, and that some elements of public spending would decline as a result of increased growth and employment following a rate cut. A few respondents argued that improvements in the efficiency of public service delivery could cover the cost.

2.39 It was requested in some responses that the NIE set out plans on how they would propose to fund a corporation tax rate cut. Several argued that the benefits of a corporation tax cut would be undermined if it were funded by increasing other taxes on businesses; others that cuts to education spending, funding of bodies such as Invest Northern Ireland or local authorities would also be inconsistent with the overall rebalancing aim. Reassurance was sought that measures to encourage FDI would not be at the expense of measures to support indigenous companies.

Implementation

Administration

2.40 Amongst respondents who commented in detail on administrative burdens of a separate corporate tax rate in Northern Ireland, there was widespread recognition that rules would be required to ensure a Northern Ireland corporation tax rate was available only to genuine economic activity in Northern Ireland. However, there was a split of views expressed as to whether this could be achieved with existing rules or whether new rules were necessary and also the extent of the burden these rules would impose.

2.41 Some respondents felt that extra admin burdens would be minimal since rules, including those for transfer pricing, already exist for situations where business activity goes outside of the UK and that many companies already have systems in place to manage this. In particular some argued that the business admin burden figures shown were overstated and that a separate regime could be managed with minimal additions to current rules.

2.42 However others felt not only that current rules would be insufficient and that additional rules would be required, but also that the cost to business of administering these rules would be significant. For example, some highlighted concerns around identifying when a Northern Ireland presence existed and how profits might be allocated, others suggested that new rules tackling anti-avoidance and tax motivated incorporation would be required. It was argued that the additional administrative burden may affect the international competitiveness of the UK and potentially even UK growth.

2.43 Some businesses did not comment in detail, but did say that they believed additional administration would be minimal. A large number of businesses that responded to the consultation operate solely in Northern Ireland and so would be largely unaffected by new tax rules setting out how to separate Northern Ireland activity from activity elsewhere in the UK or world.

Block grant adjustment

2.44 The consultation document outlined the main principles of that would underpin the block grant adjustment in the event of corporation tax devolution, though some responses sought greater clarity on this issue. For example it was suggested that a monitoring arrangement could be set up in advance of devolving corporation tax to ascertain with greater certainty the block grant implications of corporation tax devolution.

2.45 A small number of responses recognised the volatility of corporation tax receipts, and suggested the NIE may need extended borrowing powers to cope with this volatility.

Cost management approaches

2.46 Of those that commented, a majority supported cost management approaches such as phasing in or deferring a corporation tax reduction, or applying a lower rate only to trading profits.

2.47 Some argued that deferring the rate cut could mean that the Northern Ireland economy would benefit from increased investment activity in advance of block grant reductions, though others felt the impact of the rate cut may be lessened if its introduction were deferred and that action should be taken immediately

2.48 While many of the responses that commented supported a phased introduction in order to manage costs, there was also concern that a phased approach would dilute the signalling impact of a significant corporation tax rate reduction.

2.49 In the cases of both deferred and phased implementation, it was viewed as vital that certainty for businesses would be maintained.

2.50 Most who commented supported a restriction of the lower rate to trading profits only, seeing it as a means to reduce the cost of the policy and encourage activity that is more likely to generate growth. However it was acknowledged that this approach would be associated with a greater admin burden and suggested that small companies may lack the resource to manage differential rates.

Other tax options

2.51 Other tax options, in particular capital allowances, R&D tax credits and an employers' National Insurance holiday, received support from some respondents although a few voiced concern about State aid and the capacity of some measures to have a transformative impact on their own. Several suggestions were made on the administration of individual measures, which the Treasury and HMRC will consider alongside other submissions on these policy areas. The joint ministerial working group programme will include work on alternative tax measures alongside its main focus on corporation tax.

2.52 The suitability of alternative tax measures to support the rebalancing of the Northern Ireland economy was questioned in some instances. For example, while R&D tax credits would enhance Northern Ireland's historic strengths in science and engineering, it was suggested that the comparability in practical terms of the UK's R&D tax credit scheme to that of Ireland means there is potentially less imperative to consider this in Northern Ireland.

2.53 Other tax measures suggested included a reduction in local business rates, a review of tax related investment schemes and reliefs and extending the current film tax credit to cover television production. It was also suggested that the NIE reconsider the Large Retailer Levy.

Other options for rebalancing the Northern Ireland economy

2.54 The consultation document recognised the importance of policies other than taxation for rebalancing the Northern Ireland economy and set out the plans of the Government and NIE in this regard.

2.55 The responses to the consultation document confirmed that these policy areas are vital in achieving the rebalancing objective, with many respondents citing non-tax areas as equally important as tax measures for achieving rebalancing. In particular responses referred to a range of issues including:

- the need to improve educational performance of schools and tertiary education, and the skills and training of the workforce;
- improving infrastructure including transport, IT and communications;
- reform of the planning system;
- improving the science base and R&D, and making the most of research by Northern Ireland's universities;
- increasing investment and exports, including the role of Invest Northern Ireland, and improving competition;
- increasing deregulation and reducing red tape for business;
- increasing the pace of public service reform, efficiency, and public sector asset disposal;
- the importance of welfare reform including to help more people into work;
- the importance of increasing bank lending, particularly to business; and
- the potential to develop the all island economy further.

2.56 The UK Government has set out its plans for promoting economic growth and rebalancing the economy in the Budget. In the Autumn Statement the Government announced further measures which will help to rebalance the economy, across the UK. Among other things, these measures included investment in infrastructure, skills and employment, and housing; reduced business rates; enhanced capital allowances for Enterprise Zones; and deregulation. While these measures fall in devolved areas, the funding made available to the NIE as a result of these measures by the Barnett formula will enable the NIE to take forward similar measures in Northern Ireland if they wish. The Autumn Statement also announced that Belfast will be one of 10 new 'super-connected' cities across the UK, as a result of investment by a new urban broadband fund.

2.57 The NIE also welcomes these responses and has taken them into account in its draft Programme for Government, draft Investment Strategy and draft Economic Strategy which were published on 17 November 2011. These set out the NIE's priorities of rebalancing and rebuilding including through: stimulating innovation, research and development and creativity; improving skills; encouraging business growth; competing in a global economy; and developing economic infrastructure. It is recognised that many of the issues raised as part of the consultation process have been taken forward as priority areas for action within the draft Programme for Government. This contains a key commitment to press for the devolution of corporation tax and reduce its level; in the case of the draft Economic Strategy it now outlines how the NIE would ensure that the wider actions necessary to support rebalancing of the Northern Ireland economy would be taken. The NIE have also welcomed the reduction of APD on long haul flights.

2.58 The Government and NIE will also consider these responses further as part of their joint work programme, which will report next year.

3 Next steps

3.1 The Government and the NIE accept that a particular need exists to rebalance the Northern Ireland economy by strengthening the private sector over the long term. Rebalancing the Northern Ireland economy is a shared objective of the Government and the NIE.

3.2 On 17 November 2011, the First Minister and deputy First Minister published the draft Programme for Government 2011-2015 for consultation and this contains a key commitment to press for the devolution of corporation tax and reduce its level. The draft Economic Strategy was also published for consultation which includes complementary measures to be taken by the NIE to rebalance the Northern Ireland economy.

3.3 Considerable support has been seen, particularly from the Northern Ireland business community, for lowering corporation tax, with around three quarters of respondents in favour. However support has not been universal and a number of respondents pointed to the complex issues inherent in devolving these powers, including over the fiscal and economic impact and over how this will be managed, the possible impact on business, the difficulty in designing a suitable corporation tax ringfence and the need for other policies such as supply side reforms to promote the private sector. Some of these issues were identified in the consultation document as requiring extra work and consideration.

3.4 Consistent with the Government's general approach to tax consultation, the consultation document considered devolution in high-level and principled terms. It was also largely focused on the impact on Northern Ireland. However in light of the issues raised and the potential for impacts on the rest of the UK, the Government wishes to examine the case for devolution in greater detail before coming to a decision.

3.5 As part of this it will work with the NIE to seek to establish with greater clarity the costs and benefits, administrative changes and potential legislative vehicle for transferring corporation tax powers to the NIE, as well as considering other options to support private sector growth highlighted during the course of the consultation. This work will recognise the importance of complying with the relevant EU criteria and HM Government's wider fiscal policy.

3.6 This work will be overseen by a joint ministerial working group comprising of Ministers from HM Treasury, the Northern Ireland Office and the NIE. This group met for the first time on 15 December where the Government and the NIE have agreed a work plan to examine these issues. The group is expected to produce a report to the UK Government in summer 2012 and a decision will be taken following this.

3.7 Alongside this work the NIE is currently consulting on its draft Programme for Government, Investment Strategy and Economic Strategy. This work is addressing some of the non-tax options available to the NIE to rebalance the Northern Ireland economy.

A Consultation questions

A.1 The consultation document welcomed views on the following:

- Whether there is a need to rebalance the Northern Ireland economy by strengthening the private sector over the longer term and to increase economic growth and promote significant new investment;
- Where there is most scope for increasing productivity, reducing labour market inactivity and increasing growth;
- The Government would welcome views, in the context of this report, on devolving corporation tax rate varying powers to Northern Ireland. In particular, the Government would welcome views on the following:
  - The importance of the headline corporation tax rate in encouraging investment;
  - The extent to which a reduction in the rate of corporation tax in Northern Ireland could support additional investment, higher growth rates and increased employment in the Northern Ireland economy;
  - The estimated costs arising from a lower corporation tax rate in Northern Ireland;
  - The dynamic impacts on tax receipts arising from a lower corporation tax rate in Northern Ireland;
  - The risks to the NIE arising from a devolved corporation tax rate in Northern Ireland;
  - Potential compliance costs and administrative burdens for business arising from a devolved corporation tax rate in Northern Ireland;
  - The approach that would be taken to adjust the block grant arising from a devolved corporation tax rate in Northern Ireland;
  - The balance of potential costs and benefits of a reduced corporation tax rate in Northern Ireland;
  - The merits of a deferred implementation of a rate reduction in Northern Ireland and its potential impact on investment decisions;
  - The extent to which a phased reduction in the rate of corporation tax in Northern Ireland could support a rebalancing of the economy while allowing the costs of the reduction to be more effectively managed;
  - The impact that restricting any reduction in corporation tax receipts to trading income only would have on the aim of rebalancing the Northern Ireland economy and the value for money of a corporation tax reduction;

    - Whether there are other options to offset the cost to the NIE of a reduction in the rate of corporation tax that would be consistent with the overall aim of rebalancing the Northern Ireland economy; and

    - The extent to which changes to R&D tax credits, annual investment allowances, training credits or a national insurance holiday could provide feasible, effective, affordable and value for money support for the rebalancing of the Northern Ireland economy.

- In relation to other economic reforms in Northern Ireland discussed in this report, bearing in mind the devolved nature of many of these policies, the Government would welcome views on how far:

    - Welfare reform has the potential to reduce economic inactivity in Northern Ireland and increase economic growth;

    - There are lessons to be learned and policy proposals from the recent Sub-national Growth White Paper that are transferable to Northern Ireland. If so which ones?

    - Devolved policies have an important role in rebalancing the Northern Ireland economy.

B Consultation respondents

B.1 Responses were received from:

- 377 business or individuals identifying themselves as business owners
- 192 individuals not identifying themselves as business owners
- 50 accountancy firms or individual identifying themselves as accountants

B.2 In addition responses were received from the following organisations:

- Queen's University Belfast
- Association of Chartered Certified Accountants
- Institute of Chartered Accountants Scotland
- NI Tax committee of chartered accountants Ireland and chartered accountants Ulster society
- Institute of Chartered Accountants in England and Wales
- Chartered Institute of Taxation / Association of Tax Technicians
- Larne Traders Forum
- InterTradeIreland
- Roe Valley Chamber of Commerce
- Causeway Chamber of Commerce
- Newry Chamber of Commerce and Trade
- NI Tourist Board
- Institute of Directors NI
- Confederation of British Industry NI
- Federation of Small Businesses NI
- Centre for Competitiveness
- Londonderry Chamber of Commerce
- NI Chamber of Commerce
- NI Environment Link
- Green Party Northern Ireland
- Ulster Unionist Party
- Traditional Unionist Voice
- NI Conservatives
- Alliance Party
- Democratic Unionist Party
- Social Democratic and Labour Party
- Workers' Party
- NI Human Rights Commission
- Dungannon & South Tyrone Borough Council
- Fermanagh District Council
- Belfast City Council
- Committee for Enterprise, Trade and Investment
- Committee for Finance and Personnel
- Committee for the Office of the First Minister and Deputy First Minister
- Larne Borough Council
- Limavady Borough Council
- Larne Enterprise Development Company

- Confederation of British Industry
- NI Retail Consortium
- Young Enterprise
- Warrens Children Centre
- The Community Foundation for NI
- Friends of the Earth
- Save the Children
- Arts and Business NI
- Ulster GAA
- Women's Resource and Development Agency
- Unite the Union Retired Members Association NI
- NI Independent Retail Trade Association
- Construction Employers Federation
- Portadown Chamber of Commerce
- Community Arts Forum
- ADS NI Council
- NI Polymers Association
- Institute of Civil Engineers NI
- Institute of Physics
- Dairy UK (NI)
- Royal Town Planning Institute
- NI Council for Voluntary Action
- Ulster Chemists' Association
- NI Meat Exporters Association
- Invest NI
- Strabane District Council
- NI Local Economic Development Forum
- Enterprise NI
- Coleraine Borough Council
- Derry City Council
- Quarry Product Association NI
- Irish Congress of Trade Unions
- Glentoran Community Trust
- NI Bakery Council
- Pubs of Ulster
- Royal Institute of Chartered Surveyors
- Ulster Farmers Union
- NI Food and Drink Association
- Manufacturing NI
- NI Hotels Federation
- Procapitalism party
- Wilberforce Society
- NI Economic Advisory Group
- NI Economic Reform Group
- Future UK
- The Bow Group
- UNITE Lisnafillan
- NI Public Service Alliance
- Belfast and District Trade Union Council
- Law Society of NI

B.3 Representatives from the following attended a consultation meeting in Belfast:

- NI Economic Advisory Group
- NI Economic Reform Group
- Confederation of British Industry NI
- Institute of Directors NI
- Invest NI
- Enterprise NI
- Manufacturing NI
- NI Chamber of Commerce
- Centre for Competitiveness
- NI Food and Drink Association
- Federation of Small Businesses NI
- NI Independent Retail Trade Association
- South Eastern Regional College
- BDO
- Ulster Society of Chartered Accountants Ireland
- KMPG
- Ernst&Young
- NI Council for Voluntary Action
- Irish Congress of Trade Unions
- Ulster University
- Momentum
- Committee on the Administration of Justice
- Manufacturing NI

B.4 Representatives from the following attended a consultation meeting in London:

- Confederation of British Industry
- British Retail Consortium
- Federation of Small Business
- Institute of Chartered Accountants of England and Wales
- Tesco
- Barclays
- Shell
- ALMAC
- Bombardier
- Allstate Northern Ireland
- Sony
- Nomura
- Canon Europe

HM Treasury contacts

This document can be found in full on our website: http://www.hm-treasury.gov.uk

If you require this information in another language, format or have general enquiries about HM Treasury and its work, contact:

Correspondence Team
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

Tel: 020 7270 5000
Fax: 020 7270 4861

E-mail: public.enquiries@hm-treasury.gov.uk

ISBN 978-1-84532-918-1