



Overview of Department of Finance Tax Expenditure Evaluation Guidelines

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Outline of presentation

- 1. What are Tax Expenditures?**
- 2. Purpose of Guidelines and approach**
- 3. Ex ante evaluation**
- 4. Ex post evaluation**
- 5. Implementing the guidelines – a proportionate approach**



What are tax expenditures?

- **Term first coined by Surrey (1973)**
 - **Equivalent to direct expenditures**, except this spending takes place through the tax system (Surrey, 1973)

- **Definition in Irish legislation draws on OECD definition**
 - Transfer of public resources, targeted at a narrow group or activity
 - Reduces tax obligations with respect to a benchmark tax



What are tax expenditures?

As identified by the Commission on Taxation (2009)

- Exemption of foster care payments from income tax (DCYA)
- Rent-a-room relief (DECLG)
- Reliefs for health expenses and medical insurance (DH)
- Relief for gifts made to the Minister of Finance (DoF)
- Relief for expenditure on heritage buildings and gardens (DAHG)
- Accelerated capital allowances for energy efficient equipment (DCENR)
- Jobseeker's Benefit to short-time workers (DSP)
- Stamp duty relief for young trained farmers (DAFM)
- Income tax exemption for scholarships (DES)
- Relief on public transport travel passes (DTTaS)
- Tax exemption for Start-up Companies (DJEI)



Overall purpose and approach

“Though evaluation of tax expenditures may be difficult, a more serious problem may be the failure to try”. (OECD, 2010)

■ Objectives

- Promote high standards, consistency and rigour
- Transparency
- A tax-equivalent to the Public Spending Code

■ Approach

- Distinguish between ex ante and ex post evaluation
- A set of “plain English” questions for evaluation at each stage
- Proportionality
 - the higher the cost the more detailed the analysis required
 - and the shorter the review timeframe



Building blocks

- **Builds on evaluations carried out by Department over recent years**
- **Informed by the Public Spending Code**
 - And reports from Commissions on Taxation
- **And by international practice in tax expenditure evaluation**
- **Draws on the economic literature**
 - Principles of neutrality
 - Risk of tax capitalisation



Tax expenditure evaluations

2006/2007	Property Incentives, Film Incentives	Department of Finance
2011	Property Incentives	Department of Finance
2012	Film Incentives	Department of Finance
2013	R&D Tax Credit	Department of Finance
2013	Living City (property)	Department of Finance
2014	Agri-Taxation	Finance, Agriculture, Revenue



Key Evaluation Questions

Ex Ante Evaluations	Ex Post Evaluations
1. What objective does the tax expenditure aim to achieve?	1. Is the tax expenditure still relevant?
2. What market failure is being addressed?	2. How much did the tax expenditure cost?
3. Is a tax expenditure the best approach to address the market failure?	3. What was the impact of the tax expenditure?
4. What economic impact is the tax expenditure likely to have?	4. Was it efficient?
5. How much is it expected to cost?	



Ex ante - What's the objective?

- **Essential for evaluation purposes to have clear statement of what intervention is intended to achieve**
 - Facilitates analysis of alternatives

- **Ex ante evaluation should interrogate this**
 - Clarity of objective
 - Consistency with Government policy
 - Does it lend itself to monitoring?



What's the market failure?

- **Rationale for intervention via tax expenditure or other intervention hinges on existence of a market failure**
- **Market failure: a situation where, for one reason or other, the market mechanism alone cannot achieve economic efficiency**
- **Examples include**
 - Externalities
 - Public goods
 - Imperfect information
 - Market power
- **Ex ante evaluation needs to identify the market failure**



Is a tax expenditure the best approach?

- **Once the market failure is identified, the issue is one of identifying the most efficient intervention**
- **Option analysis**
- **Tax expenditure vs. direct subsidy vs. other intervention**
- **Important to take account of existing instruments and how a new tax intervention would interact with these**



Distinction between Tax Expenditures and Direct Expenditures

	Tax expenditures	Direct subsidies
Cost control	Cost uncertain – depends on taxpayer participation (nature of market led intervention)	Cost capped by expenditure ceiling.
Accessibility for beneficiaries	Simple, due to their automatic (market-led) nature. Can facilitate a greater range of taxpayer choice	More complex, requiring selection/targeting
Effectiveness	Make use of market knowledge. Additionality cannot be guaranteed – may finance activity that would have happened anyway	Risk of displacement of private sector.



What economic impact will the tax expenditure have?

- **Even if we establish that a market failure exists and that a tax expenditure is a better option need to think about whether it will work**

- **Is the design right?**

- **Intervention logic: is there a plausible link between the tax expenditure and the objective?**
 - Incidence (who benefits?) a key issue in tax expenditure analysis
 - Need to think about how impact will be evaluated at ex post stage and collection of data to facilitate this



How much will it cost?

- **Need to form some estimate of likely cost**
- **Essential if a CBA is required**
- **Most feasible approach likely to involve development of scenarios based on assumptions as to size of target population, take-up etc.**
- **Revenue forgone method likely to be the practical method**
- **Important to put arrangements in place to collect cost data for later monitoring and evaluation purposes**



Ex post evaluation

- **Ex post evaluation serves important for accountability purposes whereas ex ante evaluation is associated more with resource allocation and design of intervention**
- **A focus on “value for money”**
- **Some tax expenditures may have time limits or sunset clauses**
- **Important links between ex ante and ex post**
 - Clarity of objectives
 - Data collection



Is the tax expenditure still relevant?

- **Is the objective still valid given changes since scheme inception?**
- **Need to think about**
 - Developments in external environment, sectoral or market conditions
 - Policy changes, e.g., new programmes, regulations etc.
- **Analyse what these mean for the tax expenditure**



How much did it cost?

- **Need to establish estimates of outturn costs**
- **As at ex ante stage revenue forgone method likely to be the most applicable**
- **For CBA need estimate of “economic cost”**
 - Incorporate opportunity cost of public funds
 - Also need to account for legacy and other costs



What impact did it have?

- **Critical issue for ex post evaluation - what difference did the tax expenditure make?**
 - To behaviour, performance, economic activity etc.

- **Difficult because counterfactual is unknown, options include**
 - Surveys of beneficiaries
 - Control groups
 - Randomised control trials

- **Some of these may not be feasible**

- **At a minimum need to examine participation levels and coverage**
- **And consider possible deadweight and displacement effects**



Was it efficient?

- **Efficiency = value for money**
- **Scheme may be effective and have met its objectives but at what cost?**
- **Examine unit costs e.g., cost per job created and compare with other interventions including for public expenditure programmes**
- **Leading to consideration of possible alternatives**
- **For costly tax expenditures address through a CBA**



Implementing the Guidelines- Proportionate Approach

Estimated Annual Cost	Level	Ex Ante	Ex Post	Time Limit/ Review
Between €1m and €10m	Level 1	Ex ante assessment and identification of criteria for ex post evaluation	Application of ex post criteria	Five years to review
Between €10m and €50m	Level 2	Detailed assessment – scenario based analysis or similar and statement of proposed methods and data requirements for full ex post cost-benefit analysis (CBA)	Full ex post CBA	Five years to trigger review Interim review after three years if annual costs exceed €25m
Greater than €50m	Level 3	Full ex ante CBA and statement of methods and data requirements for full ex post CBA Use of pilot scheme if possible	Full ex post CBA	Interim review after three years