

**COSTS OF DOING
BUSINESS IN
IRELAND 2012**

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Executive Summary

Background

Action 1.27 in the Action Plan for Jobs 2012 requires Forfás to ‘benchmark and develop actions to systematically reduce excessive key business costs or delays’.

This report includes detailed cost profiles to assess the importance of various costs to 17 manufacturing and services sectors. It includes a wide range of benchmarks which measure Ireland’s cost performance vis-à-vis our key competitors for trade and investment. Finally, it assesses progress made to date and sets out further actions to reduce excessive business costs. These are dealt with in seven different cost components:

1. Labour	2. Property	3. Utilities	4. Transport
5. Credit	6. Professional Services	7. General Cost Environment	

Key Messages

In the absence of a currency devaluation policy lever to manage short term cost competitiveness pressures, the policy focus needs to be on achieving enhanced competitiveness through a combination of cost reductions in key business inputs and enhanced productivity growth¹.

Reductions in costs have been achieved across a range of business inputs and Irish cost competitiveness has improved markedly over the last 3 years or so. The pace of correction is a reflection of the open and flexible nature of the Irish economy, the depth of the recession, the weak performance of the euro and policy reforms implemented. Reforms that enable markets to work more efficiently are the key mechanism to achieve long term improvements in cost competitiveness.

Much of Ireland’s recent cost competitiveness story can be told through Ireland’s Harmonised Competitiveness Indicator (HCI) (see Figure 1.1). During the property boom, costs in Ireland rose dramatically. This is reflected in a 22.5 per cent loss in competitiveness recorded between January 2000 and April 2008. Since then Ireland has regained some of its cost competitiveness as a result of falls in relative prices and favourable exchange rate movements. From April 2008 to July 2012, Irish cost competitiveness improved by almost 19 per cent according to the real HCI measure (and 10.6 per cent in nominal HCI terms). Prices have now fallen back to levels last seen in 2002.

The role played by exchange rates, both in terms of the initial deterioration in Irish cost competitiveness and the more recent competitiveness gains, is important to note. Over half of the improvement in Ireland’s cost competitiveness since 2008 is accounted for by favourable exchange rate movements (i.e. a weak euro, making Irish exports cheaper in non-euro markets). At the same time, one must be cognisant that national data masks significant differences in the pace of sectoral adjustments.

The importance of the various costs differs significantly across firms. While a high share of total manufacturing costs are determined internationally, the cost base of internationally trading services companies is highly dependent on the local cost environment. Similarly, Irish owned firms tend to

¹ Productivity growth is the preferred long term mechanism to improve competitiveness as it can support cost competitiveness in tandem with high and increasing wage levels.

be highly dependent on the local cost environment². The cost of labour is the most significant driver of business costs for most firms – particularly for services firms. However, across manufacturing, a range of other inputs also play an important role – in particular, transport, utilities and property costs.

Table 1 looks at the individual cost components for enterprise in Ireland by summarising the key trends. As noted above and as illustrated in Chapter 2, the importance of the various cost components varies by sub-sector.

Table 1: Summary of Enterprise Cost Component Trends in Ireland

Labour Costs	Labour costs have fallen marginally since 2008 (Figure 3.1). After a number of years of declining wage levels, the data suggests that wage growth has resumed of late – albeit at a lower level than elsewhere in the euro area, meaning that labour cost competitiveness continues to improve (Figure 3.2). While Irish unit labour costs have improved significantly, the figures are dominated by the performance of exporting sectors. The tax wedge in Ireland has been increasing (Figures 3.6-3.9).
Property Costs	Construction costs and rental costs for both office and industrial space have fallen dramatically for new businesses since the collapse of the property bubble and the onset of recession – rental costs for office space, for example have declined by 45 per cent between 2007 and 2011 (Figures 4.2-4.5). Of course, many existing businesses are tied into higher property costs having purchased or leased property with upward only rent review clauses during the property boom. Labour costs in construction have reduced over the course of the recession, but perhaps not by as much as might have been expected. Other property related costs such as stamp duty on transactions have recently been reduced. Local Authority rates have fallen marginally in the past three years but significant regional differences remain (Figure 4.6).
Transport Costs	In terms of diesel costs, Ireland is the fourth most expensive country in the euro area (Figure 5.1). Prices for transport related services (e.g. road freight, sea transport, warehousing) have generally remained relatively stable since 2006 – the exception being the cost of air transport which has increased significantly since 2010 (Figure 5.3). In terms of the administrative cost to import and export goods to and from Ireland, Ireland is relatively expensive (Figures 5.4-5.5).
Utility Costs	Electricity costs for large energy users and SMEs are the seventh and fourth highest amongst the euro area 15 countries (Figure 6.1-6.2) respectively. Ireland has the sixth highest industrial gas prices although Irish prices are 3 per cent below the euro area average (Figure 6.3). While Ireland is the sixth most expensive location from 15 countries benchmarked, the cost of water for industrial users remained relatively static since 2007 (Figure 6.4). Water costs also vary significantly by region (Figure 6.5). Waste costs in Ireland remain high, particularly in relation to landfill fees, reflecting in part the limited availability of other waste treatment options (Figure 6.6-6.7). While the cost of a basket of telephone calls is relatively competitive, Ireland is expensive in terms of broadband costs – particularly when broadband quality is considered (Figures 6.8-6.12).

² The Forfás Annual Business Survey of Economic Impact shows that indigenous firms (both manufacturing and service firms) source a much greater proportion of their materials locally than their foreign owned counterparts. See Forfás, Annual Business Survey of Economic Impact, June 2012

Credit Costs	The cost of credit (i.e. interest rates) for new loans to enterprise in Ireland exceeds the cost in the euro area for a range of loan types and sizes. Loans of up to 1 million (which are often used as a proxy for the rate for loans to SMEs) are over 10 per cent more expensive in Ireland while loans of over 1 million are almost 15 per cent more expensive. Irish interest rates for the stock of outstanding loans are lower than the euro area average (Figures 7.1-7.4).
Business Service Costs	The cost of the majority of business and professional services (e.g. computer programming and consultancy; architecture, engineering and technical testing; and advertising, media representation and market research) in Ireland has fallen since 2006 (Figure 8.1). The cost of legal services (for solicitor services), however, is the exception, with legal costs reported by the CSO ³ to be 12 per cent above 2006 levels (Figure 8.2).

As evident in the table above, progress is being made in addressing Ireland's cost competitiveness. Despite this progress, it is important that we do not become complacent, as:

- Ireland remains an expensive location - Chapter 9 which examines the broader cost environment - primarily using consumer price data - shows that Ireland is the third most expensive country in the euro area, with consumer prices 12 per cent above the euro area average. These price levels do not appear to be justified by our income levels (GDP/GNP). This has an impact upon wage demands, and ultimately on the cost base for enterprise.
- Improvements in cost performance have been strongly related to the weak performance of the euro - a factor outside of our control, which is subject to change. A significant proportion of the recorded gains could be quickly eroded if the euro strengthens.
- The pace of cost improvement has slowed considerably in recent months - perhaps related to the fact that the economy returned to modest growth. Upward price pressures are already emerging (i.e. rising consumer price inflation, a return to positive, albeit weak, wage growth).
- Rigidities within the economy persist. High levels of spare capacity (e.g. high unemployment, excess property, etc.) suggest that costs remain too high and that adjustment is occurring too slowly.

In terms of domestically driven costs, we are concerned that recent price falls in Ireland are largely a cyclical response to the Irish and international recession (i.e. reduced demand, spare capacity), rather than a response to structural changes in the Irish economy. While weak economic growth continues to moderate inflation in Ireland, structural or policy induced changes are necessary to ensure that prices do not escalate and erode competitiveness when the Irish economy returns to stronger growth.

Progress to Date and On-going Initiatives

A range of policy initiatives are in train, which have the potential to support continued improvement in cost competitiveness. These arise from commitments made in the Action Plan for Jobs 2012, from the EU-IMF Programme of Financial Support, and from a range of other key policy documents (e.g. Pathways to Work, etc.). The section below summarises the key policy actions

³ Source: CSO's experimental services producer price index.

currently underway. It is vital that we progress these actions (some with proposed amendments) and that we monitor their impact to ensure that they have the desired effect:

Labour

- The transfer of housing entitlements out of the social welfare system (i.e. linking housing benefits to income rather than employment status), as proposed would substantially reduce replacement rates (i.e. the proportion of out-of-work benefits received when unemployed against take home pay if in work) for those concerned.
- The recent enactment of the Industrial Relations Act (reforming the system of sectoral agreements governing labour market conditions in a range of sectors) when combined with the expected conclusion of on-going discussions on overtime and Sunday working should contribute to labour market flexibility and also eliminate barriers to employment creation.
- On-going development of up-skilling and retraining solutions to help the unemployed, particularly focusing on the long term unemployed and other vulnerable groups will improve labour supply, which in turn will help to maintain labour cost competitiveness.

Property

- It is anticipated by the Property Services Regulatory Authority that the commercial leases database will be in place by early 2013, which will provide important market information to potential investors.
- The enactment and implementation of the Valuations Bill is a critical step in addressing the costs of commercial rates.
- The introduction of an annual broadly based and equitable residential property tax and water charges for households will broaden the tax base, facilitate the sustainable funding of Local Authorities and will reduce the need for more economically damaging increases in (for example) income tax.
- The on-going implementation of the recommendations from the Report of the Local Government Efficiency Review Group should continue to reduce the cost of local government and deliver further efficiency savings.

Transport

- The recently announced additional €2.25 billion domestic infrastructure stimulus package is welcomed.
- There has been significant investment in national transport routes over the past decade and this has led to significant improvements in connectivity for Irish enterprise (notably the completion in 2010 of the motorway network from Dublin to Waterford, Cork, Limerick, Galway and Belfast). However a number of bottlenecks remain⁴.
- Given the limited capital resources available in the short to medium term, it is critical that we prioritise investment that will support economic recovery and sustainable growth by contributing to a more effective transport network and reduce transport costs for enterprise.
- Once completed, the Department of Transport's review of ports policy should help to ensure that Irish firms continue to have good sea access. Similarly, the completion of the port

⁴ Forfás, Infrastructure Briefs: Overview of the Main Infrastructure Issues for Enterprise, May 2012

competition study being undertaken by the Competition Authority is important in ensuring that sufficient levels of competition exist within and between Irish ports.

Utilities

- In terms of utilities, as part of the Action Plan for Jobs 2012, Forfás are currently examining the manner in which a range of services are regulated. This project is focused on identifying changes in the regulatory environment which could lead to reduced costs for enterprise.
- The recently unveiled National Broadband Plan, which envisages up to €175 million of State investment, recognises that access to high speed broadband is essential for national competitiveness. A range of actions are to be implemented to reduce the costs of broadband rollout.

Credit and Professional Services

- Significant reforms and restructuring are underway in the banking sector.
- In the area of professional services, the Legal Services Bill is nearing completion and it is anticipated that this will address many of the existing concerns.

Outstanding Issues

While the progress outlined above is welcome, further action is required to restore Ireland's cost competitiveness. The priority outstanding issues are summarised briefly below.

Labour

- Ireland needs to enhance wage cost competitiveness across all sectors of the economy - to achieve this, however, we must relentlessly pursue policies to improve cost competitiveness and address the continuing high cost of living (see section 9).
- We must continue to ensure that replacement rates do not exceed 70 per cent. If changes are made to personal taxation, social contributions or other social welfare payments, policy makers must be cognisant of their interaction with and impact upon replacement rates.
- To reduce replacement rates there is a need to reform the social welfare system so that benefits decline in line with the length of time a person is out of work - this would bring Ireland into line with European approaches to social welfare.
- It is important that the impact of the new Industrial Relations Act in terms of promoting labour cost competitiveness in sectors covered by sectoral wage agreements be assessed in due course as provided for in the Act 2012.
- As more immediately required reforms (relating to social welfare and to sectoral wage agreements) are completed, consideration should be given to examining the level of the national minimum wage in relation to younger age cohorts where the unemployment crisis is greatest.
- To encourage employment creation and take-up, there should be no further increases in the labour tax wedge and when feasible, the marginal labour tax rate should be reduced to below 50 per cent. The introduction of further costs on employment (e.g. changes to sick pay policy, pension's policy, etc.) should be considered carefully from a labour cost competitiveness perspective given the scale of our unemployment crisis.

Property

- A range of initiatives are underway including the development of the commercial lease database, the enactment of the Valuations Bill, and the introduction of the residential property tax. It is important that these initiatives are progressed quickly - in particular, the revaluation process for business rates where the process could be outsourced or self-assessment used. In order to avoid more economically damaging increases in (for example) income tax, it will be necessary to achieve a significant revenue stream from annual property taxes.

Transport

- Planning reform is required to reduce planning delays and to enhance the coordination of infrastructure delivery in a manner that supports the development of a sustainable property sector. At the same time, local authorities should develop more robust and transparent charging mechanisms for Local Authority charges that match levies with the economic cost of providing development.
- Taxes and duties on fuel should not be adjusted in response to changes in global fuel prices (or capped) as this would create further fiscal uncertainty for the State, would adversely impact upon the revenue collected, and would blunt market signals that encourage efficiency.

Utilities

- There has been a substantial increase in the Public Service Obligation (PSO) levy for peat and renewable energy in 2012/13; it has increased by 30 per cent from €92.1 million to €132 million. Unless there is a clear economic rationale for maintaining them, subsidies for peat generated electricity should be discontinued. Prior to potentially converting peat plants to biomass, a full cost benefit analysis should be undertaken. As a maturing technology, the price support scheme for onshore wind should be revised so that the price support levels for new onshore wind projects are phased out over time. While there are potentially significant enterprise opportunities in emerging energy technologies (e.g. offshore wind/ocean energy), they should be supported through funding mechanisms for R&D, if deemed competitive.
- The recent publication of the new waste policy is welcome. Arising out of this document, we must proceed rapidly with the proposed reduction in regional formations from 10 to no more than three for the purpose of developing waste management plans. The development of waste infrastructure other than landfill (e.g. waste to energy) is a priority for enterprise.
- As with waste, the recent publication of a National Broadband Plan is welcome but is not an end in itself. Rather it sets out a list of actions (including actions relating to planning, the use of State assets to enhance rollout, actions to reduce broadband rollout costs etc.) which must now be progressed.

Credit and Professional Services

- Looking at the domestic financial market and the current high cost and limited availability of credit, we must find ways to encourage existing foreign banks to retain lending operations in Ireland and to attract new entrants in the medium term. In this context, the Competition Authority should consider the merits of undertaking a review of the barriers to entry, expansion and exit in retail banking. We must also continue to support the bank's efforts to lower their cost structures.

- In the realm of legal services, a number of actions (in addition to the Legal Services Bill) should be considered - including the creation of a single tier counsel system, and the opening up of conveyancing to suitably qualified professionals other than solicitors. Reform of court procedures also offers significant potential to reduce costs.

Broader Consumer Costs and Public Service Costs

- While consumer prices in Ireland have adjusted downward in recent years, Figure 9.1 shows that prices remain high relative to most other euro area countries. In 2011 Ireland was the 3rd most expensive location in the euro area for consumer goods and services and Irish prices were 12 per cent above the euro area average. Housing costs - both to buy and to rent - are significant determinants of wage demands. Since the bursting of the property bubble, house prices have adjusted downwards and consequently have become more affordable when expressed as a ratio of average earnings.
- Health and education consumer costs, where the public sector dominates supply, have increased at a significantly faster rate than overall consumer costs since 2000. In 2011, education costs were 93 per cent above what they were in 2000 while health costs were approximately 76 per cent above 2000 prices. There is a need to maximise value for money, ensuring that public services are delivered as efficiently and effectively as possible. Available international data suggests significant potential for improvements. Where cost data is available, public sector salaries in Ireland are generally higher than in most comparator countries. Given the need to achieve further reductions in exchequer spending, and the tough choices confronting policy makers in terms of where cuts can be made, public sector pay rates, allowances and increments must be examined. Furthermore, government departments and agencies should be provided with reduced pay budgets within which they must control headcount, rather than the current assigned headcount target approach.

Conclusion

While Ireland has already regained some cost competitiveness, further progress is required if Ireland is to return to strong economic and employment growth. To achieve a greater restoration in cost competitiveness, further price adjustment is required relative to our main competitors.

It is difficult for small open economies, particularly those that share a currency with larger regions, to control their rate of price inflation, as this is, to a significant degree, determined by events outside domestic control. Nonetheless, as noted throughout this report, there are a number of policy levers available to Government which can be used to restore Ireland's cost competitiveness.

Continued reductions in costs for labour, property, transport, utilities, credit, professional services and public services would exert downward pressure on overall costs and prices across the economy. Implementation of these recommendations would represent a major step in ensuring Ireland's future competitiveness and prosperity.

1. Introduction

Action 1.27 in the Action Plan for Jobs 2012 requires Forfás to ‘benchmark and develop actions to systematically reduce excessive key business costs or delays’. Forfás, having the lead role, was required to complete this task by the end of Quarter 3, 2012. In delivering on this task, this paper largely adopts a methodology that Forfás have previously used in their work on assessing the costs of doing business in Ireland.

Generating sustainable broad based export-led growth is essential to rebuilding our economy. In order to deliver growth, Ireland’s international competitiveness needs to continue to improve. Competitiveness is a complex concept and encompasses many different drivers. However, cost competitiveness is a critical foundation. In the longer term, productivity growth is the preferred mechanism to improve competitiveness as it can support cost competitiveness in tandem with high and increasing wage levels⁵.

A high cost environment weakens competitiveness in a number of ways.

- High costs make Ireland less attractive in terms of foreign direct investment;
- High costs can make firms which rely on domestically sourced inputs less competitive when they are selling into foreign markets - this is a particular concern for large indigenous exporting sectors such as the food and drink sector;
- A high cost environment can impact on firms which may not export, but which rely on the domestic market - their customers (consumers and other firms) may source cheaper inputs from abroad, rather than from within Ireland, leading to a loss of market share for Irish based enterprises; and
- More broadly, high costs have implications for the costs of living with knock on implications for wage demands.

In the absence of a currency devaluation policy lever to manage short term cost competitiveness pressures, the policy focus needs to be on achieving enhanced competitiveness through cost reductions in key business inputs and enhanced productivity growth⁶. The focus of this paper, as the title suggests, is primarily on direct costs to enterprise. Acknowledging the interlinked nature of all sectors and elements of the economy, however, reference is made to the wider costs environment and account is taken of a range of consumer costs.

Finally, it is necessary to note that other Forfás studies will address issues relating to delays in service provision (e.g. Action 1.28 of the Action Plan for Jobs 2012 relating to actions designed to improve Ireland’s international competitiveness ranking; Action 1.49 relating to the streamlining of the various licences required by enterprises in order to conduct their business).

⁵ National Competitiveness Council, Ireland’s Productivity Performance, 1980-2011, Forfás, May 2012.

⁶ Productivity growth is the preferred mechanism to improve competitiveness as it can support cost competitiveness in tandem with high and increasing wage levels. Many firms, however, may have limited opportunities to increase value added significantly in the short term. The more productive the labour force and the capital stock are, the higher the level of wages that is consistent with a state of “price and wage” competitiveness. This illustrates the importance of skills development, innovation, infrastructure, etc. in the longer term.

1.1 Overview of Ireland's Cost Competitiveness

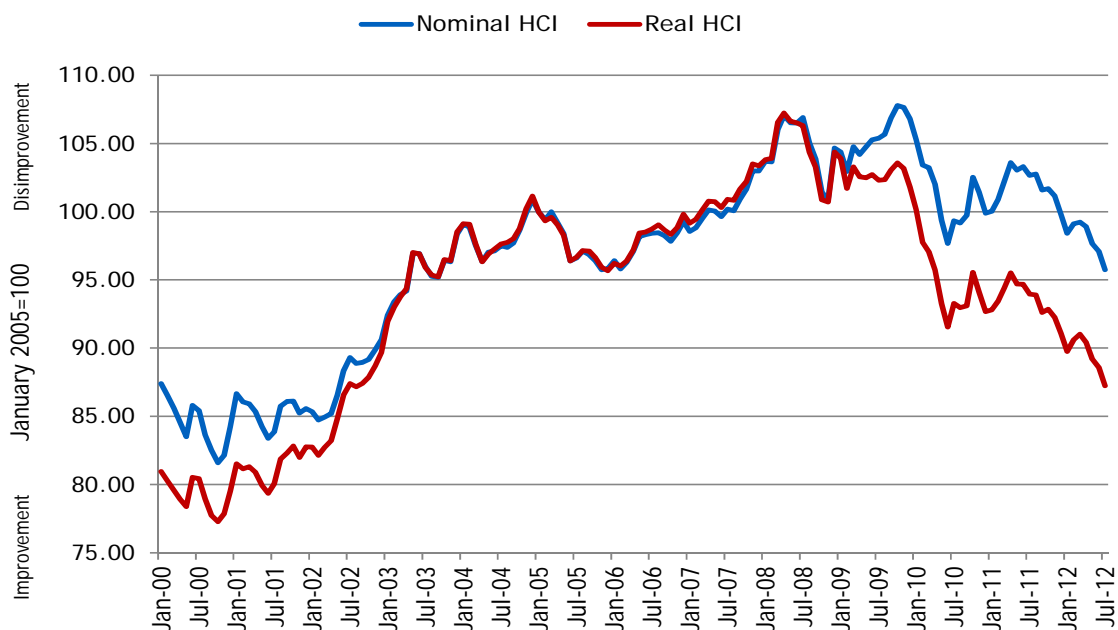
In the late 1990s and early 2000s, the Irish economy benefited from favourable cost competitiveness relative to our key competitors. Allied to an advantageous skills and demographic profile, a pro-enterprise policy regime and a range of other factors, exports and investment boomed, leading to record rates of economic growth. All of this was supported by relatively high levels of productivity growth.

In the middle of the last decade, domestic policies combined with cheap international credit to fuel a consumption and property boom. As a result, costs in Ireland rose dramatically for a range of inputs and international competitiveness declined.

With the onset of the global economic recession, the weaknesses inherent in the Irish economy were laid bare, and the effects of the world-wide downturn compounded domestic mistakes. Since 2008, the Irish economy has undergone significant adjustment. Most obviously, incomes and living standards have declined sharply as we confront a new economic reality. However, unwinding the excessive price increases built up during the boom years is challenging.

Much of this narrative is illustrated in Figure 1.1 below, which examines a number of Harmonised Competitiveness Indicators⁷. The nominal Harmonised Competitiveness Index (HCI) is a nominal effective exchange rate for the Irish economy that reflects, on a trade weighted basis, movements in the exchange rate vis-à-vis 56 trading partners. The real HCI (deflated by consumer prices) takes into account relative price changes along with exchange rate movements.

Figure 1.1 Harmonised Competitiveness Indicators, 2000-2012 (January 2005=100)



Source: Central Bank of Ireland, Forfás calculations

Ireland experienced a 7.7 per cent loss in cost competitiveness (real HCI) between January 2005 and April 2008 reflecting an appreciation of the euro against the currencies of our trading partners

⁷ The Central Bank provides a good assessment of the strengths and weakness of various competitiveness indicators. See O'Brien, D., & Scally, J., Cost Competitiveness and Export Performance of the Irish Economy in Central Bank of Ireland, Quarterly Bulletin, Q3 2012, July 2012.

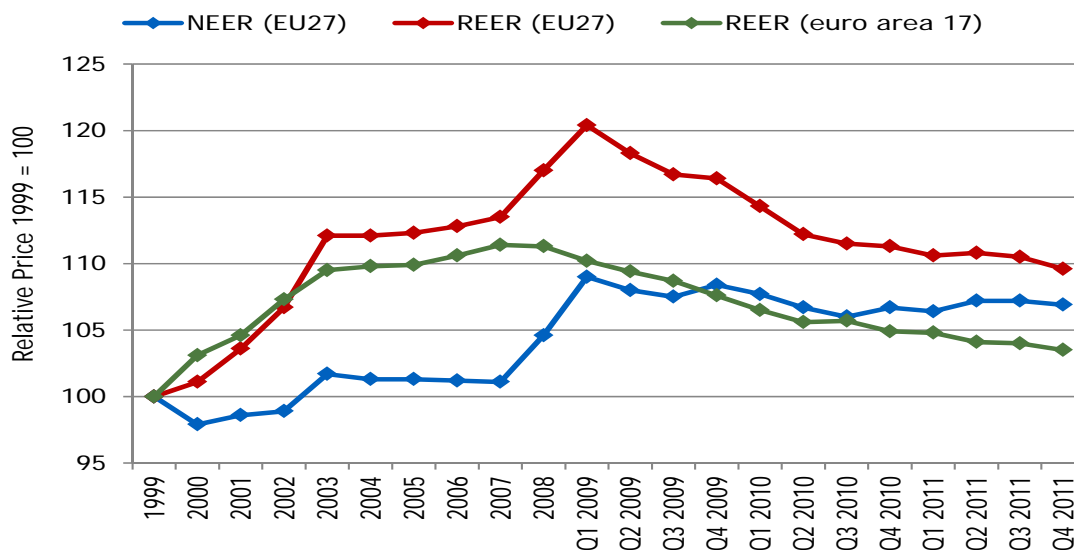
(nominal HCI) and higher price inflation. Since the peak, Ireland has regained some of its competitiveness because of falls in relative prices and favourable exchange rate movements: from April 2008 to July 2012, the nominal HCI fell by 10.6 per cent. The real HCI fell by almost 19 per cent. These recent gains could be quickly eroded if the euro strengthens or if prices increase more rapidly than in our competitors.

The European Commission also calculates a series of economy-wide price and competitiveness indices⁸:

- The nominal effective exchange rate (NEER) or “trade-weighted currency index” tracks changes in the value of a given country’s currency relative to the currencies of its principal trading partners⁹.
- Changes in cost and price competitiveness depend not only on exchange rate movements but also on cost and price trends. The real effective exchange rate (REER) “relative price and cost indicator”, aims to assess a country’s price or cost competitiveness relative to its principal competitors in international markets. It corresponds to the NEER deflated by selected relative price or cost deflators¹⁰.

The results of the Commission’s analysis are illustrated in Figure 1.2 below. Mirroring Figure 1.1, it is clear that price levels in Ireland increased rapidly throughout the middle years of the last decade, peaking in 2008/early 2009. Since then, Ireland’s relative cost competitiveness has improved.

Figure 1.2 Relative Price Indicators for Ireland, 1999-2011



Source: European Commission¹¹

8 European Commission, Director-General for Economic and Financial Affairs, Price and Cost Competitiveness, Fourth Quarter 2011, February 2012.

9 The NEER is calculated as a weighted average of the bilateral exchange rates of the relevant currencies.

10 Deflators used in DG ECFIN reports are consumer price indices (CPI and HICP where available), the GDP deflator, the price deflator of exports of goods and services, and unit labour costs in the economy as a whole and in the manufacturing sector.

11 Note that within the euro area, there are no currency effects and so there is no need to include data on the NEER (EU17).

Against the wider EU27, Ireland REER has declined from 120.4 per cent in Q1 2009 to 109.6 per cent in Q4 2011 (1999=100), representing an improvement in cost competitiveness. This is primarily a result of lower rates of inflation than is the case in most other EU member states. Ireland's REER vis-à-vis the euro area 17 has also declined over the same period (from 110.2 per cent to 103.5 per cent).

In summary, following a long period of weakening cost competitiveness, Irish cost competitiveness has improved since the onset of the recession.

1.2 What Drives Costs?¹²

During a boom such as Ireland experienced, it is to be expected that prices and costs will increase. Wealthy countries are generally expensive countries. The high rate of domestic price inflation in Ireland in recent years partly relates to convergence in Irish and European price levels due to faster economic growth in Ireland.

Higher inflation due to this 'convergence effect' is not, in itself, a major concern, reflecting a natural rise in the cost of domestic services justified by higher incomes and living standards¹³. Analysis by the European Commission, however, has found that even allowing for Ireland's relatively high level of GDP per capita, the price level in Ireland prior to the current crisis had been relatively high in comparison with other euro area economies (see Figure 9.1)¹⁴. In GNP per capita terms - a more realistic measure of income levels (where net factor incomes from the rest of the world are excluded), Irish price levels were even more out of line compared with the benchmarked countries.

In the past (i.e. during the boom years of the Celtic Tiger), a number of factors contributed to the rise in costs including:

- Economic overheating caused by pro-cyclical fiscal policy (fast growth in public spending and tax cuts) while euro area interest rates were low;
- Rapid credit growth and the unsustainable boom in the construction industry;
- The circular impact of rapid house price inflation on wage growth; and
- Regulatory and other restrictions to competition as outlined in various Competition Authority reports.

With the onset of recession, many of these cost drivers dissipated and Irish cost competitiveness is back at levels experienced about a decade ago. However, further enhancements in costs competitiveness are still required. A range of factors persist which threaten to undermine Ireland's international cost competitiveness, including:

¹² This section is largely based on research conducted by Philip Lane, Trinity College Dublin for the National Competitiveness Council in 2004.

¹³ In an economy catching up with its richer neighbours, labour productivity tends to rise faster in sectors producing internationally tradable goods (particularly in capital intensive manufacturing industry) than in those involved in the more labour intensive and generally non-traded service sector. Increases in labour productivity growth in traded manufacturing industries are usually followed by wage growth throughout the economy. Thus, a combination of wage growth across both traded and non-traded sectors, but lower labour productivity gains in the services sector, leads to more rapid increases in the cost of services. In this way, services inflation is often higher in those regions of a monetary union enjoying the most rapid growth in productivity and incomes. This is known as the 'Balassa-Samuelson effect'.

¹⁴ Directorate-General for Economic and Financial Affairs, The Economic Adjustment Programme for Ireland, European Economy, Occasional Papers 76, February 2011, page 14.

- Rigidities within the economy persist. High levels of spare capacity (e.g. high unemployment, excess property, etc.) suggest that costs remain too high and that adjustment is occurring too slowly.
- The pace of improvement in cost competitiveness has slowed and upward pressures are emerging (i.e. rising consumer price inflation, positive, albeit weak, growth in wages).
- Exchange rates account for a significant share of the improvements in Ireland's competitiveness to date¹⁵. A significant proportion of the gains achieved could be quickly eroded if the euro strengthens - particularly given Ireland's high levels of non-eurozone trade. On the other hand, the weakness of the euro has resulted in higher import prices for goods and services sourced from outside the euro area.
- It is not clear that cost gains are being driven across the broad economy - i.e. the relatively small internationally trading manufacturing sector has recorded significant gains¹⁶. Costs in large domestically trading services sectors (e.g. health, education) remain high.

In summary, we are concerned that recent price falls in Ireland are largely a cyclical response to the Irish and international recession (i.e. reduced demand, spare capacity), rather than a response to structural changes in the Irish economy. While weak economic growth continues to moderate inflation in Ireland, structural or policy induced changes are necessary to ensure that prices do not escalate and erode competitiveness when the Irish economy returns to stronger rates of growth.

1.3 Structure of this Paper

Chapter 2 uses sectoral cost profiles to assess the importance of various costs to 17 sectors. The cost profiles have been developed using KPMG's Competitive Alternatives 2012 report. The following cost components are captured:

- Labour Costs;
- Property (leased facility);
- Utilities;
- Transport;
- Interest and Depreciation;
- Total Taxes (net of grants); and
- Location Insensitive Costs.

Using the Competitive Alternatives study, we have created indicative cost profiles for a number of sectors, which are of importance to the Irish economy. The profiles provide an indication of the varying importance of the different cost components to individual sectors. However, it should be noted that the cost structures of individual firms are likely to vary significantly within sectors.

¹⁵ See 'Regaining Competitiveness' by Brendan Walsh, 24th July 2012 at <http://www.irisheconomy.ie/index.php/2012/07/24/regaining-competitiveness/>

¹⁶ O'Brien and Scally have found that aggregate competitiveness data masks significant differences in sectoral adjustments. Indigenous firms, for example, are much more exposed to the domestic and UK markets and were quite adversely affected by the sharp depreciation of sterling during the early phase of the crisis. Foreign-owned firms, which account for a very large proportion of total exports, tend to be more acyclical in nature. However, given that the foreign-owned firms are generally less labour intensive, the overall employment performance in the exporting sector was much weaker. For more detail see O'Brien, D., and Scally, J., Cost Competitiveness and Export Performance of the Irish Economy in Central Bank of Ireland, Quarterly Bulletin Q3 2012, July 2012.

Chapter's 3 to 7 focus on each of the individual location sensitive cost components (excluding taxation¹⁷). Chapter 8 examines data on professional and business services - a cost category not captured in the profiles referred to above.

In each of these chapters, a range of internationally comparable cost indicators are collected for Ireland and a number of key trading partners. Given that the prices of internationally traded business inputs are set on world markets (e.g. industrial equipment or commodity raw materials), this report concentrates on the costs that are largely domestically determined such as labour, property, energy, water, waste, communications and business services. Where comparable data is available, costs are compared over time. Where possible, Ireland's cost levels are compared to a relevant peer group average, the OECD and euro area average or else compared to as wide a group of countries as possible. The report uses the most up to date internationally comparative cost data. As much of the data is collected on an annual basis, there may be a time lag in capturing recent changes in cost levels. Recent changes in Ireland's cost environment, which are not captured in the international data, are reflected in the text where applicable.

Finally, Chapter 9 considers the general cost environment - using data from the Consumer Price Index and the Harmonised Index of Consumer Prices - to provide a broader overview of Ireland's cost competitiveness.

¹⁷ Taxation priorities are captured in the Development Agencies Pre-Budget Submission.

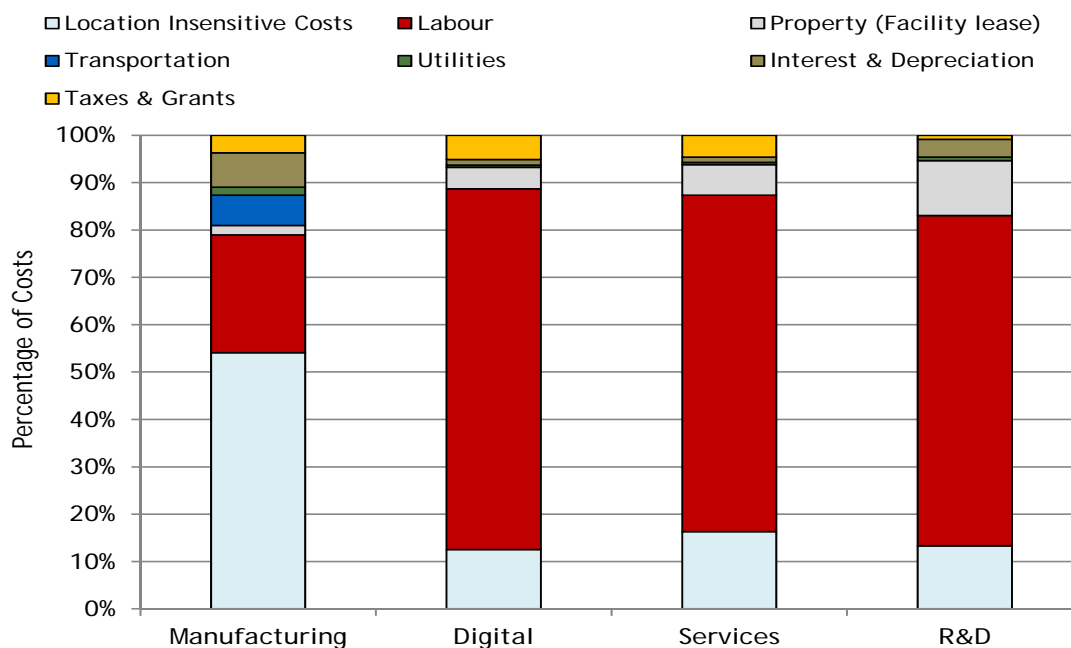
2. Cost Profiles

This chapter assesses the relative importance of key business inputs across the main exporting sectors. From a competitiveness perspective, it is essential that the Action Plan for Jobs 2013 focuses on reducing costs that comprise a significant percentage of business costs (as set out in this chapter) and that are out of line with those in competitor countries (chapters three to eight).

2.1 Summary¹⁸

The summary cost profiles present a breakdown of the cost components for four sectors - manufacturing, digital services, broader business services, and research and development (R&D) services. They illustrate the relative importance of location sensitive and location insensitive costs (i.e. goods and services produced on international markets where the price is determined by global supply and demand conditions). A striking, though not unexpected, feature of the comparison is that relative to manufacturing, location insensitive costs form a smaller component of total costs for digital (12.5%), services (16.3%) and R&D (13.3%) operations. Over half of the total costs in manufacturing (54.1%) comprise location insensitive costs. There are, however, significant differences within manufacturing; 37.1% of total costs in the medical devices sector are location insensitive compared to 66.6% in the chemicals sector.

Figure 2.1 Summary Cost Profiles for Manufacturing, Digital, Services and R&D Operations



Source: KPMG, Competitive Alternatives 2012, Forfás Calculations

¹⁸ The cost profiles discussed below have been developed using KPMG's Competitive Alternatives 2012 report, which uses case study business operations for 19 different sectors and benchmarks the cost of doing business for these model firms in a range of countries. Ireland is not included in the study. The benchmarked countries used to calculate the cost profiles are Australia, Canada, France, Germany, Italy, Japan, Netherlands, the UK and the US. As the profiles are based on a single case study firm in each sector, the profiles should be regarded as indicative rather than representative of the cost structure across sectors.

While not discounting the importance of location insensitive costs, it is nonetheless notable that Irish-owned companies are generally much more integrated into the domestic economy and therefore are more sensitive to locally influenced, location sensitive costs. Differences in sectoral specialisation will also influence spend in the local economy. Forfás data on development agency assisted exporters¹⁹ shows that:

- In overall terms, foreign-owned industry spent €20.74 billion on raw materials in 2010, of which €2.2 billion or 10.6 per cent relates to materials sourced in Ireland (by either indigenous suppliers or other foreign-owned multinationals in the country). In contrast, Irish-owned firms spent €11.25 billion on raw materials. In this case, however, 68.4 per cent of these materials were sourced locally.
- A similar story emerges in terms of services inputs - in 2010 foreign owned firms purchased over €45.4 billion worth of services. 18 per cent of this was sourced in Ireland. While the value of services purchased by Irish-owned firms is much lower (€4.75 billion), almost 83 per cent of these services were sourced in Ireland.
- In 2010, the total payroll bill of foreign-owned firms amounted to almost €7.58 billion with manufacturing accounting for €4.74 billion (63 per cent) and services contributing the remaining balance (37 per cent). Irish-owned companies spent €5.38 billion in 2010 on payroll costs - €3.48 billion (65 per cent) of which was accounted for by manufacturing firms.

In general, location insensitive costs include inputs for which the price is set in international markets, such as materials and equipment. As location insensitive costs do not influence decisions on where to invest, these cost elements have been excluded from the detailed sectoral cost profiles discussed below²⁰.

¹⁹ Forfás, Annual Business Survey of Economic Impact 2010, June 2012.

²⁰ It should be noted that the assumption that location insensitive costs do not influence decisions on where to invest may not hold in all cases. For example, peripheral locations may face additional transportation costs on commodity products. Domestic policies such as taxes and tariffs may also impose additional costs on 'location insensitive costs'.

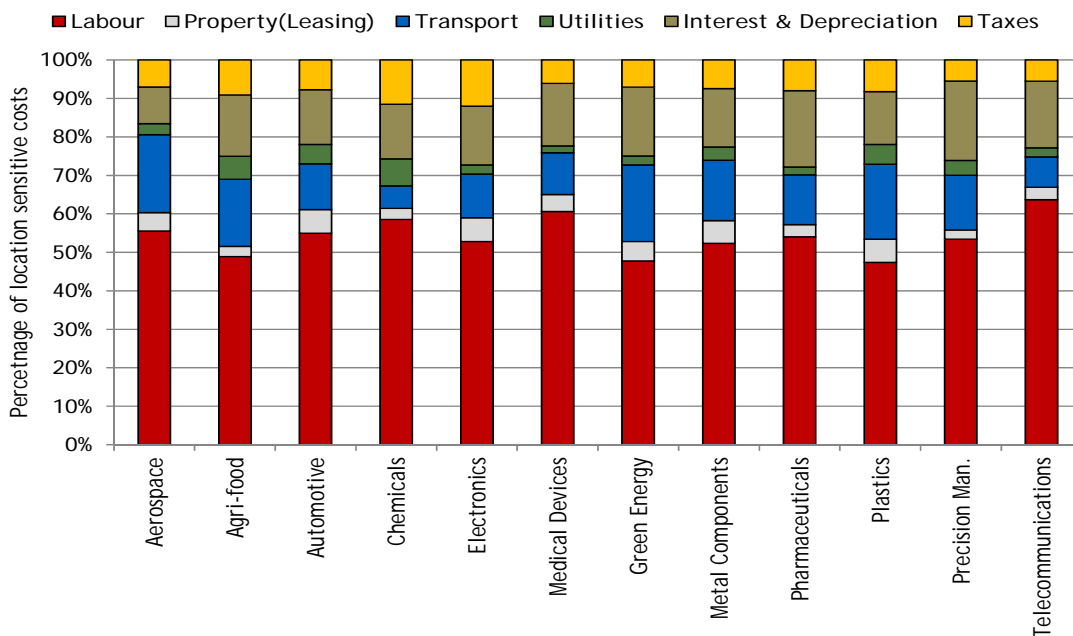
2.2 Sectoral Cost Profiles

The following sectoral cost profiles provide an indication of the contribution of various location sensitive cost components to total costs in a number of key sectors. As the profiles are based on a single case study firm in each sector, the profiles should be regarded as indicative.

2.2.1 Manufacturing Sector Cost Profiles

The contribution of labour costs to total location sensitive costs varies from 47 per cent in the case study plastics firm to 61 per cent in the case study medical devices firm and 64 per cent in the telecommunications case study. Transport costs are a major component of locally determined costs in the aerospace (20%), plastics (19%) and agri-food operations (17%) case studies. Utilities (e.g. energy, waste, etc.) are also an important cost input for the chemicals (7%) and agri-food (6%) case studies.

Figure 2.2 Manufacturing Sectors' Cost Profiles (Location sensitive costs only)



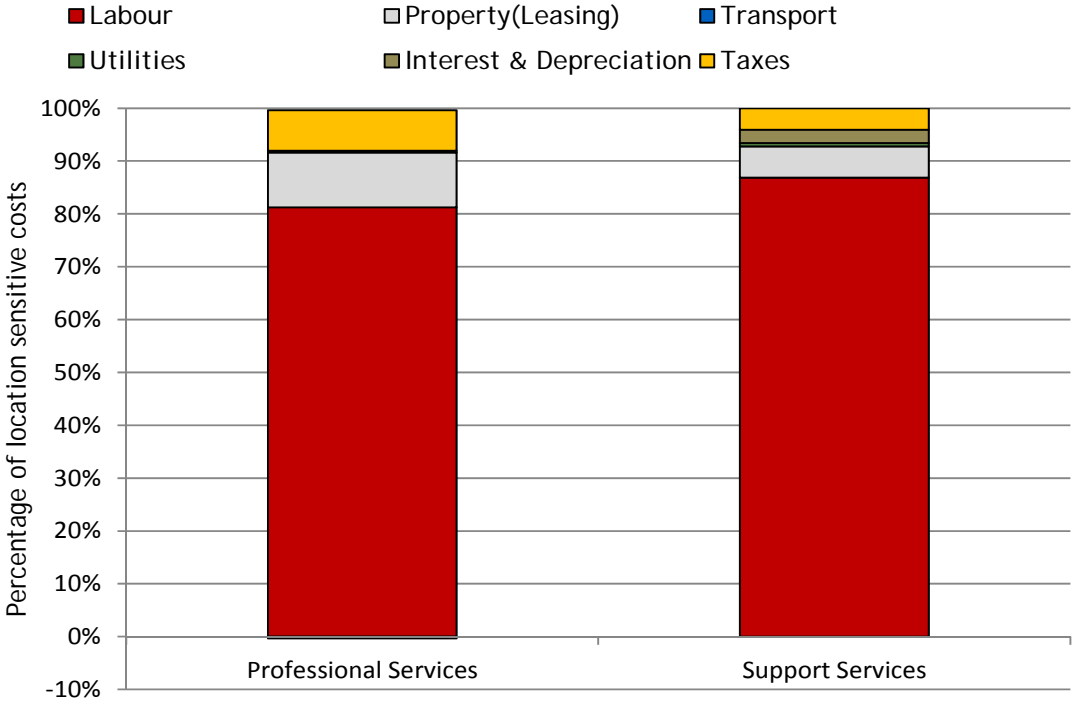
Source: KPMG, Competitive Alternatives 2012, Forfás Calculations

2.2.2 Service Sector Cost Profiles

On average, location insensitive costs account for just 16.3 per cent of total cost for the case study services firms, making services operations highly sensitive to locally determined costs and the value they offer. In 2011, services exports accounted for 50.9 per cent of total Irish exports compared to 25 per cent in 2001²¹. Location insensitive costs have been eliminated from Figure 2.3.

Unsurprisingly, labour costs are the main component of costs in services sectors, accounting for 81.9 per cent of location sensitive costs for professional services and 86.9 per cent of location sensitive costs for support services (e.g. a shared services centre). Property leasing costs are particularly significant for professional services operations (10.4%).

Figure 2.3 Services Sectors’ Cost Profiles (Location sensitive costs only)



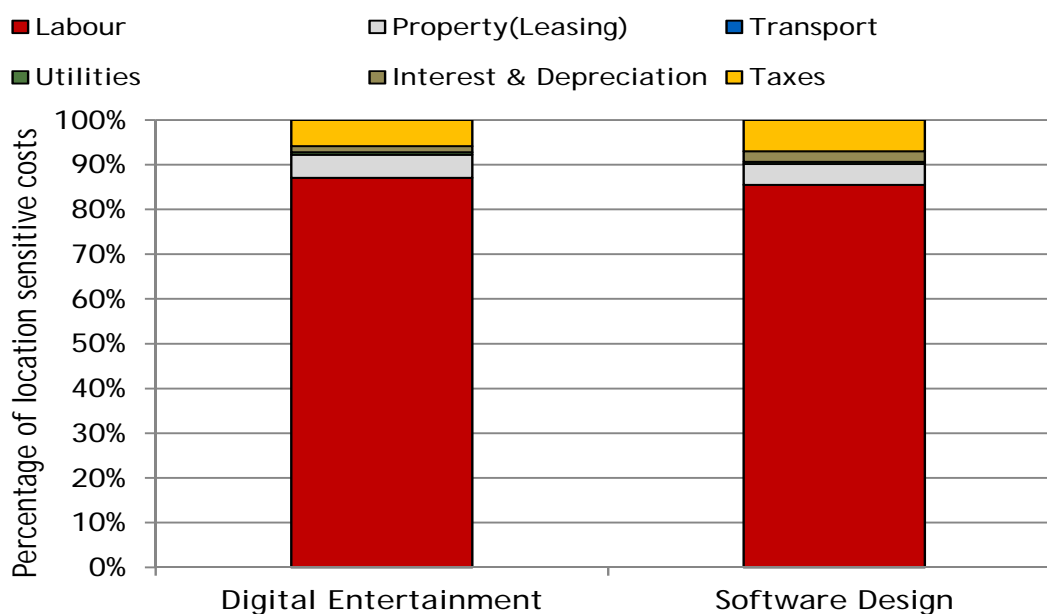
Source: KPMG, Competitive Alternatives 2012, Forfás Calculations

²¹ CSO, Balance of Payment March, 2012.

2.2.3 Digital Sector Cost Profiles

For the first time, the 2012 KPMG cost profiles examine the digital sector in isolation. The digital sector includes both digital entertainment and software design - two key sectors in Ireland's economy. As with the services sector, location insensitive costs account for a small proportion of overall costs - 12.5 per cent in this case. Figure 2.4 looks in more detail at the breakdown of location sensitive costs. Once again, labour represents the largest cost element for firms, accounting for over 75 per cent of total costs for both digital entertainment and software design. Tax and property costs are the next two most important costs for the sector.

Figure 2.4 Digital Sectors' Cost Profiles (Location sensitive costs only)

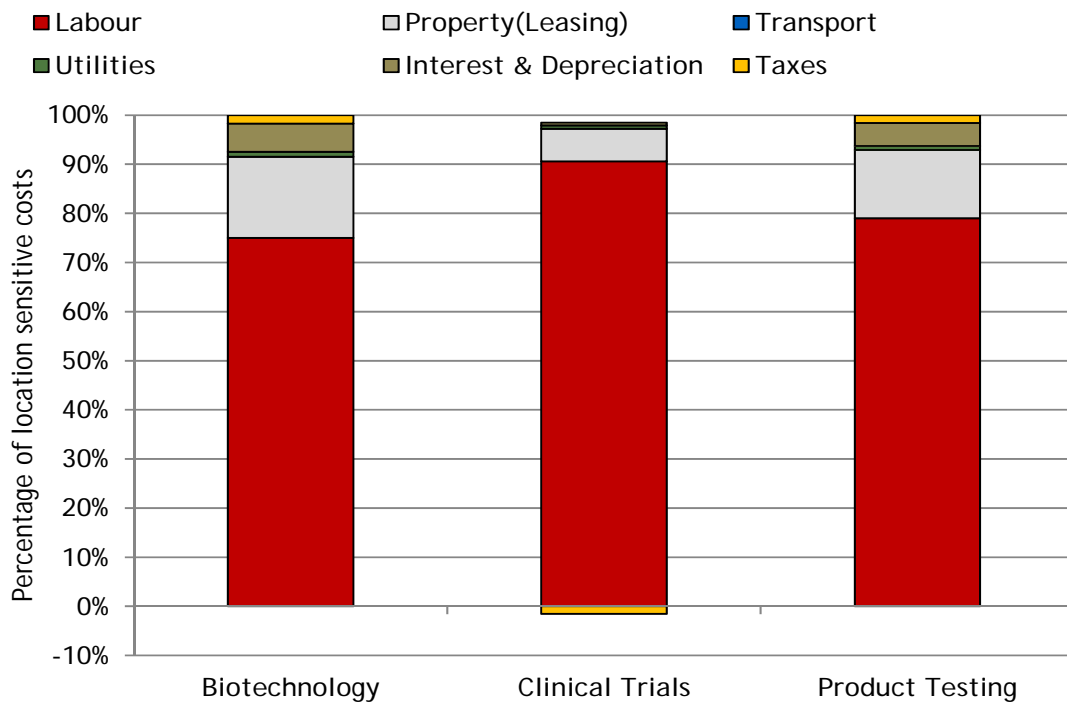


Source: KPMG, Competitive Alternatives 2012, Forfás Calculations

2.2.4 R&D Sector Cost Profiles

Labour costs comprise a large component of location sensitive costs for the case study R&D operations. They account for 93 per cent of costs within the clinical trials firm, 79 per cent within the product testing operation and 75 per cent within the biotechnology firm. The leasing of property is a major cost element for these firms also (16.5 per cent for biotechnology, 14 per cent for product testing). Interest and depreciation charges are also significant for biotechnology and product testing facilities.

Figure 2.5: R&D Sectors' Cost Profiles (Location sensitive costs only) ²²



Source: KPMG, Competitive Alternatives 2012, Forfás Calculations

In summary:

- While a high share of total manufacturing costs are determined internationally, the cost base of services companies is highly dependent on the local cost environment.
- The cost of labour is the most significant driver of business costs for most firms - particularly for services firms.
- Across manufacturing, a range of other inputs also play an important role - in particular, transport, utilities and property costs.

²² On average, 13.3 per cent of costs for R&D operations are determined on global markets. Of the three R&D sectors benchmarked in this report, clinical trials operations are the most sensitive to locally determined costs (88%).

3. Labour Costs

3.1 Summary

Labour costs are the most significant location sensitive cost for all sectors. This section examines trends in relative labour costs, unit wage costs, and labour tax wedges across a range of countries.

Labour Cost Growth Rates and Unit Labour Costs

Labour cost growth rates show the change over time in the cost of employing workers. Ireland's growth rates exceeded the EU-15 average between 2004 and 2007. However, growth rates in Irish labour costs slowed significantly since 2008: annual growth of 4.5 per cent was recorded in 2008; in 2011 wages declined annually by 1.7 per cent. From 2009, Irish labour cost growth rates have been lower than the EU-27 and euro area-16 average (Figure 3.1).

Figure 3.2 examines total compensation levels for a range of economies²³. At €35,856 per annum, average compensation levels in Ireland in 2011 were higher than average levels in Germany and the UK. Between 2000 and 2008, the average annual increase in total compensation per employee was significantly higher in Ireland (5.8%) than the euro area (3.6%). Between 2008 and 2011, while average employee compensation continued to grow in the euro area (+4.6%) compensation levels fell in Ireland (-0.9%). Annual data for 2011 suggests that wage growth in Ireland has turned positive. The UK, our largest individual trading partner, experienced a sharper drop in compensation costs in 2008 and 2009 although costs have rebounded somewhat since then.

Total labour costs include wages, taxes on income and employer and employee social security contributions. Ireland has the fourteenth highest total labour costs level in the OECD-28 (Figure 3.3). Ireland has the tenth highest net wage level in the OECD-28, almost 13 per cent above the OECD-28 average. This is a result, in part, from Ireland's lower tax wedge on labour.

Unit labour costs (ULC) measure the average cost of labour per unit of output. In 2005, Irish ULCs grew by 6.15 per cent (a loss of cost competitiveness), well ahead of both the euro area and OECD averages (2.16 and 2.09 per cent). Up to and including 2009, significant annual increases in Irish ULCs were recorded compared with EU and euro area averages. In 2010, however, real Irish ULCs fell by 4.6 per cent - a substantially larger fall than was recorded for either the EU or euro area, and representing a competitiveness gain for Ireland (Figure 3.4). The European Commission expects this trend to continue out to 2013.

At an economy wide level, therefore, Irish labour wage rates adjusted for productivity are becoming more competitive. It is important to note, however, that ULCs are heavily influenced by composition effects, reflecting changes in both productivity and costs. Recent improvements in Ireland's ULCs are a result of a reduction in output from low productivity sectors, an upturn in high value added export oriented sectors, and a reduction in compensation per employee²⁴.

²³ Data on total compensation includes remuneration in cash and in kind, but excludes the cost of employers' social contributions.

²⁴ According to the Central Bank, much of the improvement in unit labour costs is set to come increasingly from the productivity side rather than the compensation side, as many firms have completed their rounds of wage reductions; the Central Bank forecasts includes modest compensation increases this year and next. See Central Bank of Ireland, Quarterly Bulletin Q2 2012, April 2012.

Finally, Figure 3.5 measures statutory monthly minimum wages and minimum wage as a percentage of the average wage. Ireland has the second highest statutory monthly minimum wage (€1,461.85) of the 14 countries benchmarked. A number of EU member states operate non-statutory minimum wage rates on a sectoral basis and have rates, which are significantly higher than Ireland. The minimum wage is more prevalent in certain locally traded sectors, notably in hotels and restaurants, wholesale and retail and other locally traded service industries. When measured as a percentage of the average wage, the minimum wage in Ireland is ranked eighth highest amongst the 14 countries benchmarked.

Social Security Contributions and Labour Taxation

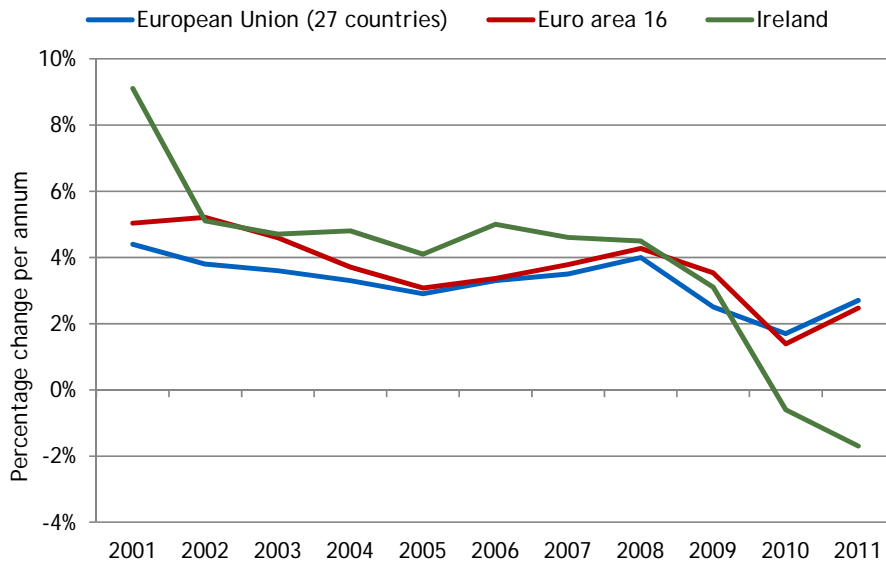
There are significant disparities across locations in relation to the levels of social security contributions and labour taxation. Ireland has one of the lowest levels of employers' social welfare contributions (Figure 3.10). The Irish rate (9.7%) is significantly lower than the OECD average (14.8%) and the euro area average (18.8%), which reduces the total cost of employing workers in Ireland. In many countries, however there is either a cap on employer social security costs or a reduced rate above a certain income threshold²⁵. In Ireland, a flat rate is charged on the full salary, therefore as salaries increase, Ireland's competitiveness position is quickly eroded.

Ireland's tax wedge on labour (i.e. the gap between what the employer pays and what the employee receives) for a married couple (with two children) with a combined salary of 167 per cent of the average wage rose from 16.2 per cent in 2010 to 19 per cent in 2011 (Figure 3.9). The tax wedge is significantly higher for higher income earners - a financial disincentive for highly skilled internationally mobile workers (Figure 3.8). For a single worker (with no children) on 167 per cent of the average wage, the tax wedge has increased from 36.4 per cent in 2010 to 38.7 per cent in 2011 (Figure 3.7). The tax wedge is important from a competitiveness perspective for a number of reasons - it affects the cost of labour for the employer, it partly determines labour supply, and it can impact on Ireland's ability to attract high skilled labour.

²⁵ There are also examples of caps on employee social security contributions. In Germany for example, employee contributions are capped at a monthly income of €5,500 (in relation to pensions and unemployment benefit) and at €3,712.50 per month in relation to health and long term care.

3.2 Labour Cost Indices and Unit Labour Costs

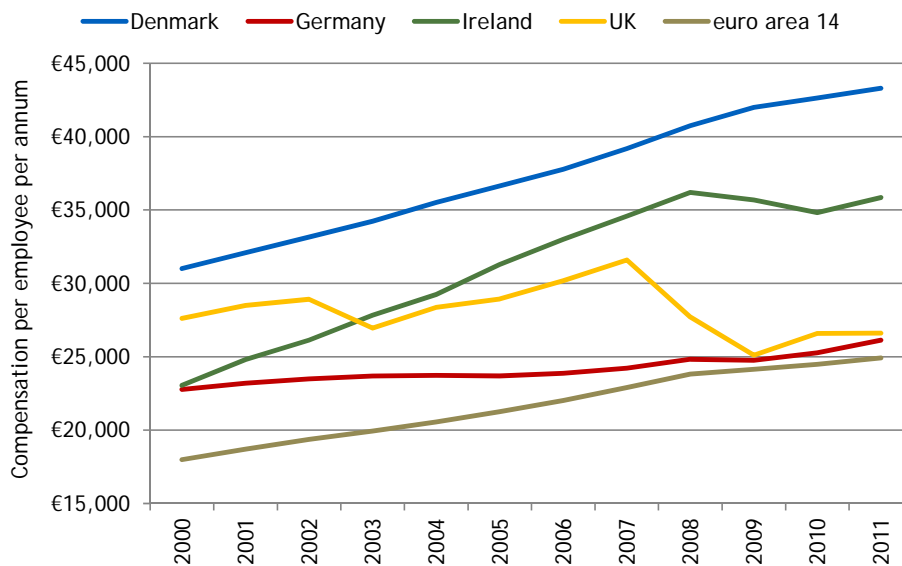
Figure 3.1: Growth in Labour Cost, 2001-2011



This indicator shows the trend in labour cost growth in Ireland compared with the euro area-16 and EU-27. From a high of 9.1% growth in 2001, Irish labour costs have fallen in both 2010 (-0.6%) and 2011 (-1.7%). This represents a gain in cost competitiveness as labour costs continue to rise in the EU and euro area.

Source: Eurostat, Population and Social Conditions, CSO, Labour Cost Index

Figure 3.2: Total Compensation per Employee Across the Entire Economy, 2000-2011

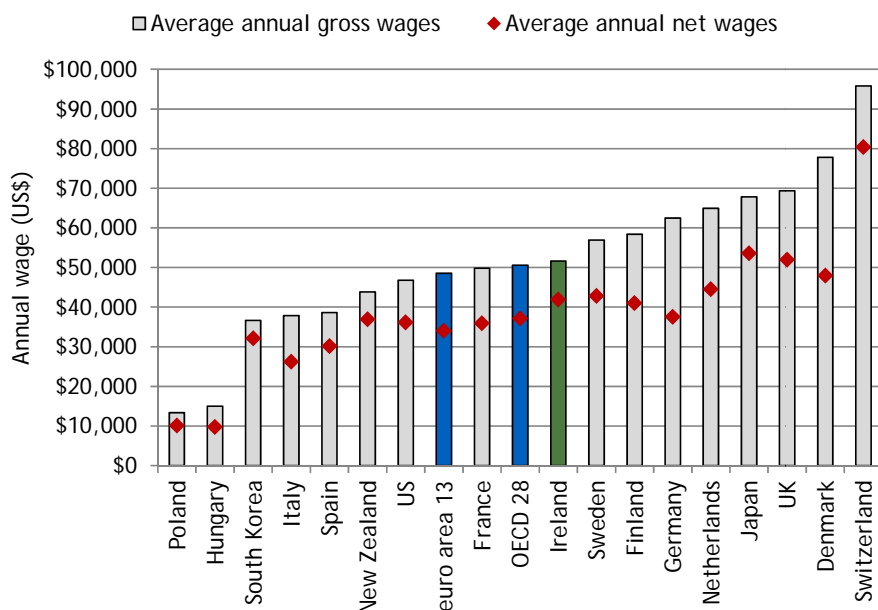


Between 2000 and 2008, compensation per employee rose rapidly in Ireland (5.8%) compared to the euro area (3.6%). Between 2008 and 2011, average employee compensation continued to grow in the euro area (+4.6% p.a.) while it fell in Ireland (-0.9% p.a.). Annual data for 2011 suggests that wage growth in Ireland has turned positive following a couple of years of decline²⁶.

Source: Eurostat, National Accounts, Groningen, Total Economy Database

26 Euro area 14 excludes Cyprus, Estonia and Malta.

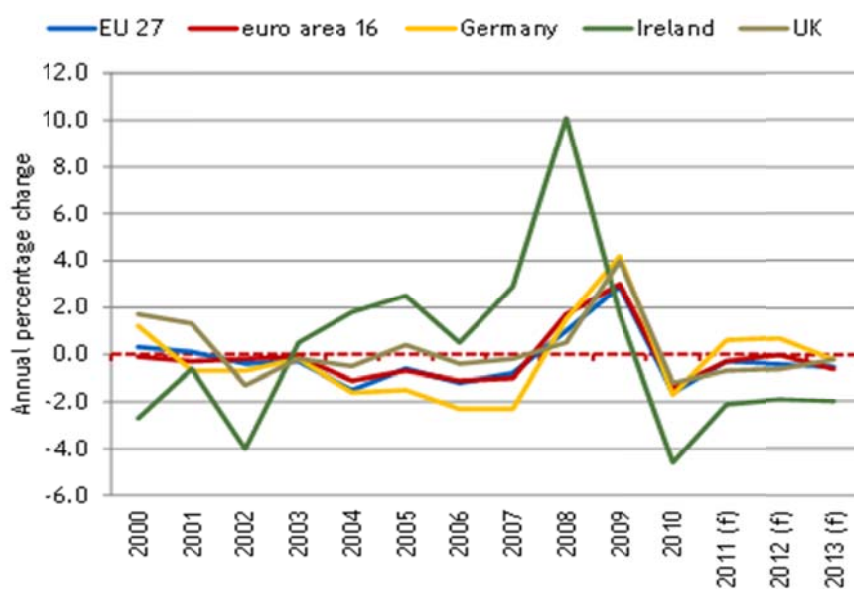
Figure 3.3: Average Total Labour Costs and Net Wages, 2011



Total labour costs include wages, taxes on income and employer and employee social security contributions. Ireland has the 14th highest total labour costs level in the OECD-28²⁷. The chart also shows average net wage levels. Ireland has the 10th highest net wage level in the OECD-28 (13% above the OECD average), partly a result of the relatively small gap between before and after-tax wages in Ireland.

Source: OECD, Taxing Wages 2011, OECD Comparative Price Levels 2012, Forfás Calculations

Figure 3.4: Annual Change in Real Unit Labour Cost, 2005 - 2013(f)



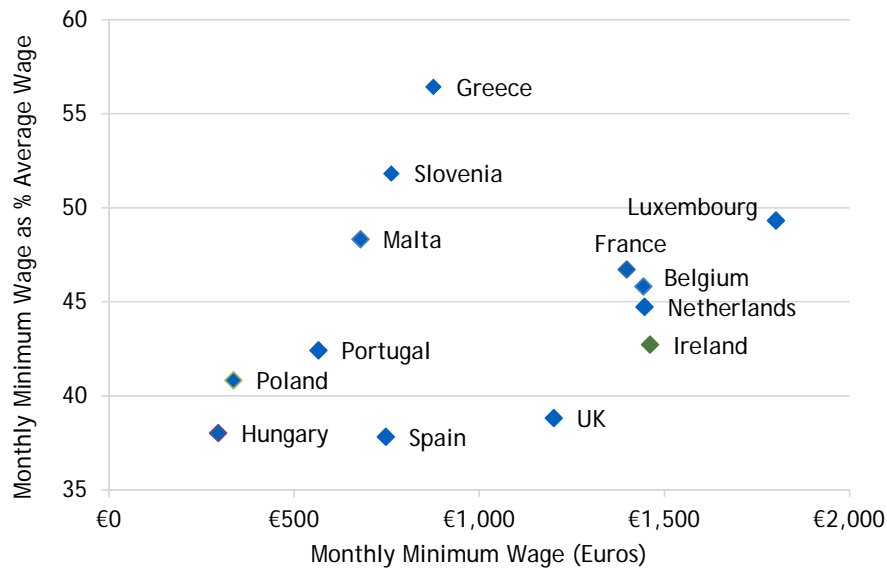
Unit labour costs (ULC) measure the average cost of labour per unit of output. Prior to 2009, higher annual increases in ULC's were recorded in Ireland than in the EU and euro area. Conversely, real Irish ULC's (-4.6%) fell by more than the EU (-1.6%) and euro area (-1.4%) averages in 2010. The European Commission expects Irish ULCs to continue to fall out to 2013²⁸.

Source: Eurostat, Unit Labour Costs Annual Data

27 The Universal Social Charge which came into effect on 1st January 2011 is captured in the Irish data.

28 According to the European Commission, the largest declines in relative ULCs were seen in Spain, Ireland and Greece. Further reductions in ULCs are expected in all three countries in 2012-13. See European Commission, European Economic Forecast, Spring 2012, European Economy 1/2012.

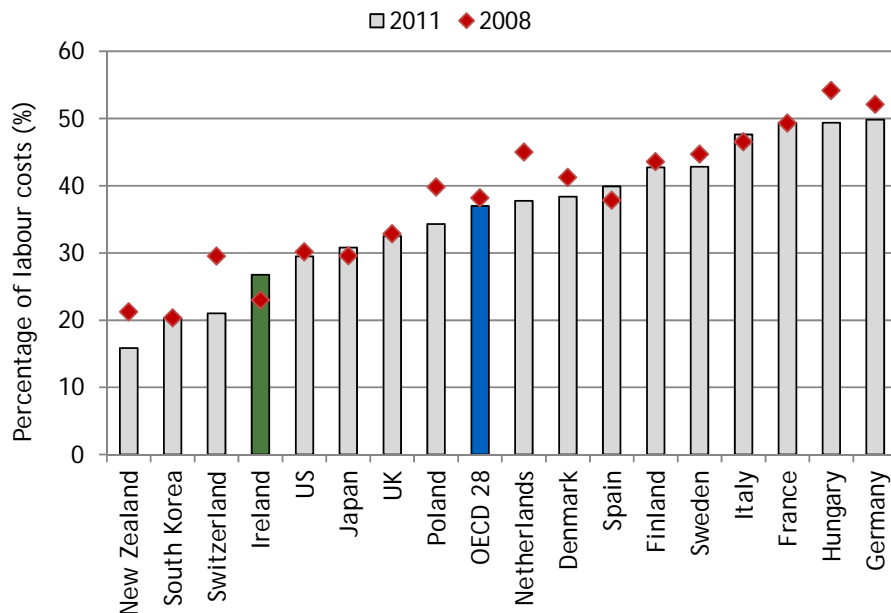
Figure 3.5: Monthly Minimum Wage and Minimum Wage as a % of Average Wage, 2012²⁹



This indicator measures the statutory monthly minimum wage levels and also as a percentage of average wage. Of these 13 countries, Ireland has the second highest monthly minimum wage. When expressed as a percentage of average wages, Ireland has the eighth highest minimum wage.

Source: Eurostat, Minimum Wages

Figure 3.6: Average Income, tax plus employees' and employers' social security contributions: Single individual without children, 100% of average earnings, 2011

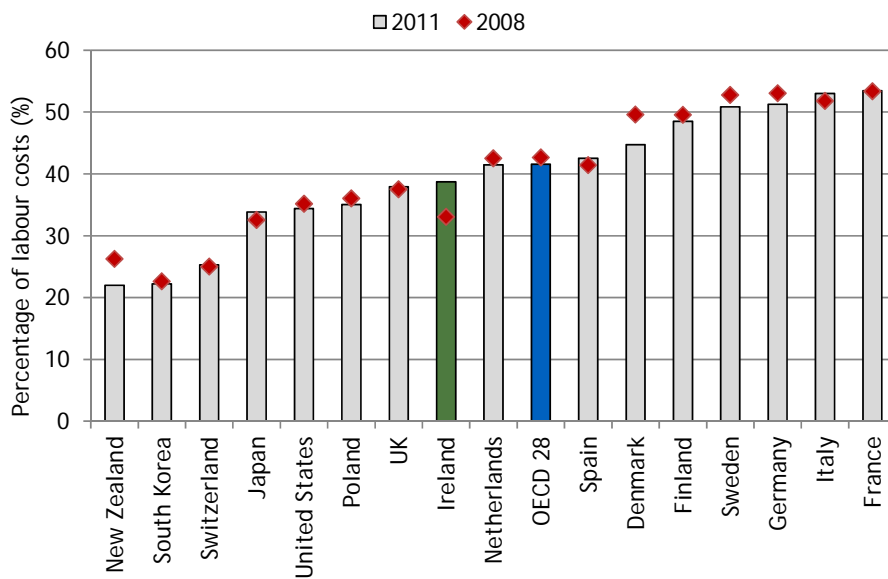


For a single person with no children on 100 per cent of the average wage, the total tax on labour (the gap between what the employer pays and what the employee receives) is the fifth lowest in the OECD and well below the OECD average of 37 per cent.

Source: OECD, Taxing Wages, 2011

²⁹ Data relating to the minimum wage as a percentage of average wages is based on the latest year available between 2009 and 2011. While the minimum wage level for Ireland relates to 2012, the minimum wage as a percentage of average wages relates to 2010.

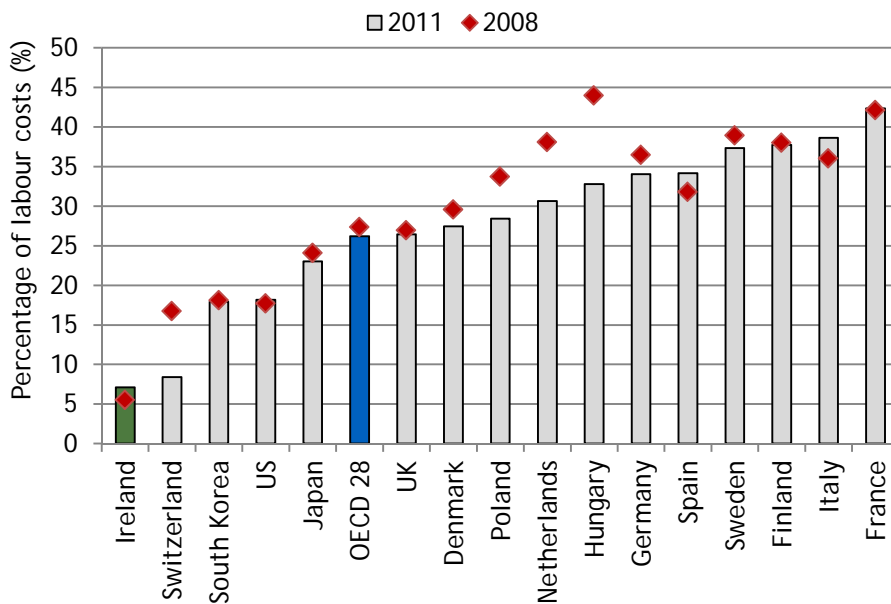
Figure 3.7: Average Income, tax plus employees' and employers' social security contributions: Single individual without children, 167% of average earnings, 2011



The total tax on labour is the 11th lowest in the OECD for single individuals with no children earning 167% of average earnings, down from 8th lowest in 2008. For this higher income cohort, the total tax on labour in Ireland (37.8%) is much closer to the OECD average.

Source: OECD, Taxing Wages, 2011

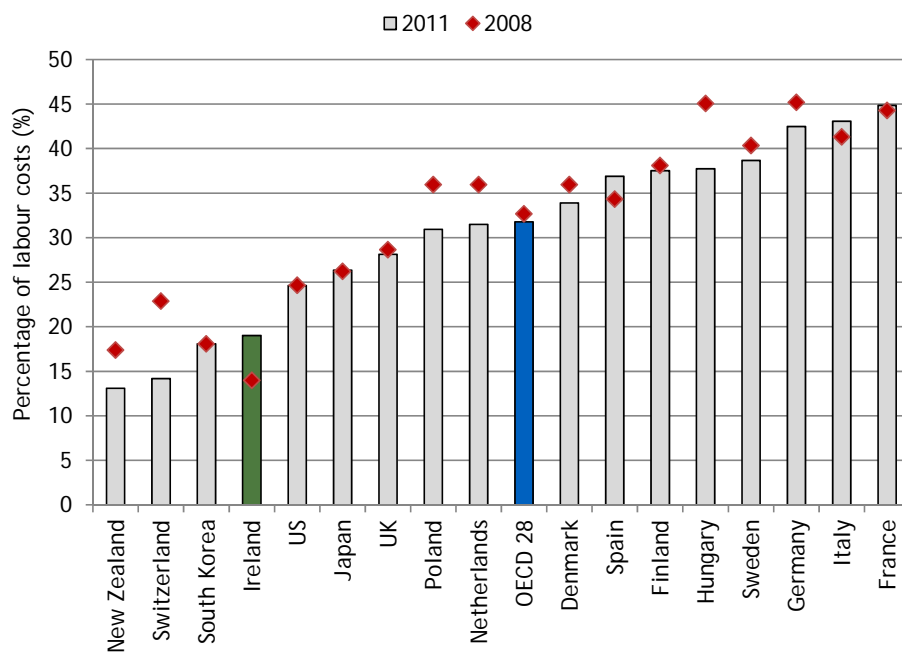
Figure 3.8: Average Income, tax plus employees' and employers' social security contributions: Married Couple with two children, 100% of average earnings, 2011



For married couples with two children, the total tax on labour is much less pronounced at 7.1 per cent. At this level, Ireland had the second lowest tax imposition on labour in the OECD for this family cohort. This ranking remained unchanged relative to 2008.

Source: OECD, Taxing Wages, 2011

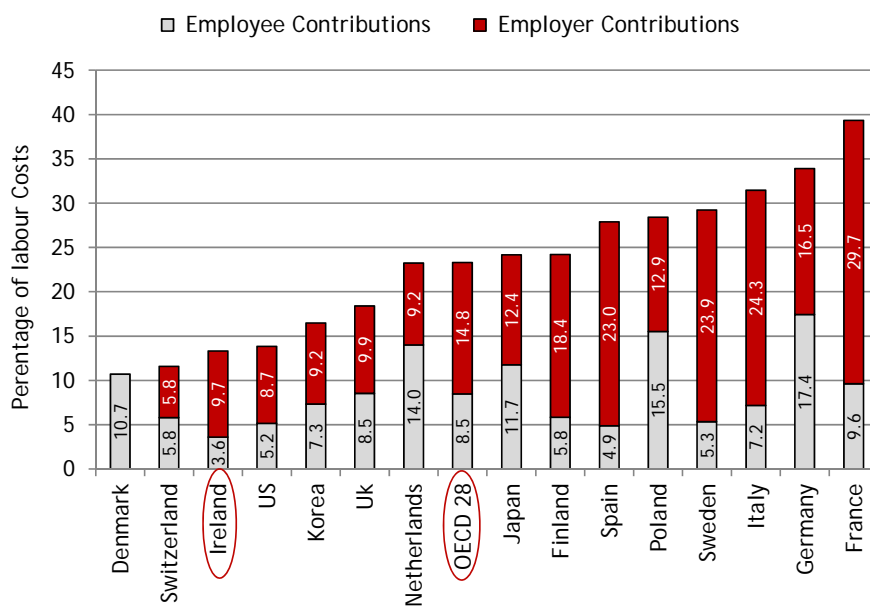
Figure 3.9: Average Income, tax plus employees' and employers' social security contributions: Married Couple with two children, 100-67% of average earnings, 2011



19% of total labour costs for a married couple with two children earning 167% average earnings went towards tax, up from 14% in 2008. This is below the OECD average of 31.8%.

Source: OECD, Taxing Wages, 2011

Figure 3.10: Employer and Employee Social Security Contributions, 2011



Ireland has the fourth lowest rate of total social contributions in the OECD 28. Employer's social security contribution is the 7th lowest, while employee contributions are the 2nd lowest. In many countries, however there is either a cap on employer social security costs or a reduced rate above a certain income threshold. In Ireland, a flat rate is charged on the full salary, therefore as salaries increase, Ireland's competitiveness position is quickly eroded.

Source: OECD, Taxing Wages 2011

3.3 Policy Focus on Labour Costs

Despite some evidence of reductions in Irish labour costs being recorded over recent years, wage rates have proven relatively sticky³⁰. The purpose of this section is to examine the operation of the Irish labour market and to identify actions, which can improve its operation – encouraging employment creation and maximising labour supply.

OECD research finds that labour market reform can support labour cost competitiveness and employment growth. For example, Germany, having implemented significant labour market reforms in the years preceding the current crisis, has weathered the unemployment crisis relatively well³¹. Cross-country evidence suggests that strong growth in unit labour costs in the years leading up to the crisis is related to employment losses during the crisis. German unit labour costs fell from 2000 to 2007, compared to an increase of over 4 per cent per annum in Ireland³². See Appendix 1 for more details of German labour market reforms.

In 2010, Forfás conducted a review of labour cost competitiveness³³. The paper provided an analysis of labour market costs and their drivers and policy recommendations to improve labour market efficiency. The paper highlighted that the complex relationship between the various drivers of wage levels means that coordinated and complementary action is required. To the greatest extent possible, the market should set wage levels, as opposed to State interventions determining pay rates, and interventions should be designed with this in mind³⁴. Building on that research, this paper focuses on three issues, which are presented below in order of priority:

- Reductions in high replacement rates;
- Reform of the sectoral employment agreements;
- Modifications to the national minimum wage (NMW).

In addition, other issues such as activation and training policies are briefly considered.

3.3.1 Replacement Rates

Jobseekers' Benefit is designed to offer income maintenance during periods of frictional or cyclical unemployment, not to serve as an alternative long term source of income³⁵. The replacement rate measures the proportion of out-of-work benefits received when unemployed against take home pay if in work. As such, it sets a de facto rather than legal minimum wage.

30 The ESRI, analysing Irish data from 2006-2009 based on the National Employment Survey, have found that despite an unprecedented fall in output and rise in unemployment, both average earnings and average labour costs increased marginally over the period. Their analysis suggests that a good deal of the downward wage rigidity observed within Irish private sector employment has been driven by factors consistent with continued productivity growth. See Bergin, A., Kelly, E., & McGuinness, S., Explaining Changes in Earnings and Labour Costs During the Recession, Renewal Series Paper 9, ESRI, April 2012

31 Hüfner, F. and C. Klein, The German Labour Market: Preparing for the Future, OECD Economics Department Working Papers, No. 983, 2012 <http://dx.doi.org/10.1787/5k92sn01tzzv-en>

32 Boysen-Hogrefe, J. and D. Groll, The German labour market miracle, National Institute Economic Review, Vol. 214, pp. 38-50, 2010

33 Forfás, Review of Labour Cost Competitiveness, October 2010.

34 Potential exists to use the social protection system to achieve important income policy goals.

35 Jobseekers' Allowance (and other assistance payments) may serve as income support on a long-term basis – subject to satisfying scheme conditions.

In general, a replacement rate in excess of 70 per cent is considered to act as a disincentive to work (i.e. if an individual can receive more than 70 per cent of in-work income in benefits, they will demand a higher wage in the market to retain a monetary incentive to work³⁶).

Forfás has previously highlighted the need to ensure that the social welfare system does not create poverty traps and has emphasised the need to ensure that unemployed persons do not become disengaged from the workforce.

A range of actions have been taken in recent budgets to reduce replacement rates, for example: reductions of at least 4.1 per cent in all social welfare payments made to those of working age and larger reductions in jobseeker allowance rates for claimants under the age of 25 (2010)³⁷; changes to tax credits and tax bands along with the introduction of the universal social charge (2011); entitlement to jobseekers benefit based on a five day rather than a six day week where a person is working for part of a week (2012).

A report from the ESRI illustrates that approximately 18-19 per cent of unemployed persons currently in receipt of jobseeker's benefit or allowance have a replacement rate of 70 per cent or over³⁸. Secondary benefits, and specifically housing entitlements, are a major influencing factor on replacement rates. The IMF has also noted that the flat structure of unemployment payments over time results in replacement rates for the long-term unemployed that are high by international standards, contributing to low exit rates from the Live Register³⁹. Continued action on ensuring that replacement rates do not create impediments to the take up of employment must occur in tandem with improved activation and up-skilling.

Recommendation: Continuing from measures included in recent budgets, replacement rates should be addressed, ensuring that all replacement rates move below the 100 per cent mark and ultimately move towards the 70 per cent benchmark. Policymakers must also be cognisant of the impact of various policy changes on replacement rates (in particular the impact of changes to personal tax, social contributions and social welfare payments on replacement rates).

Responsibility: Department of Social Protection / Department of Finance / Department of Public Expenditure and Reform

Significant moves have already been taken to address the impact of housing entitlements upon replacement rates⁴⁰. Arising out of commitments in the Programme for Government to review the operation of the Rent Supplement Scheme, proposals to integrate the systems for

36 While there is no pre-determined level of replacement rate which would influence every individual's decision to work, clearly the higher the replacement rate, the lower the incentive to work. A replacement rate in excess of 70 per cent is considered excessive. It should also be noted that standard measures of replacement rates exclude a number of factors. For more information see: Department of Finance, Replacement Rates and Unemployment, 2009 and Department of Finance, Tax Strategy Group 11/14, Replacement Rates 2011, September 2012.

37 See Department of Finance, Financial Statement of the Minister for Finance, 9th December 2009

38 Callan, T., et al, Tax, Welfare and Work Incentives, published in Budget Perspectives 2012, Dublin: ESRI, 2011

39 IMF, 2012 Article IV Consultation with Ireland - Concluding Statement of the IMF Mission, 18 July 2012

40 It was announced in Budget 2012 that the minimum contribution an individual in receipt of Rent Supplement must pay towards rent would increase.

providing rent supplement and social housing support have been advanced⁴¹. The Government has decided, in principle, to transfer responsibility for the provision of rental assistance to persons with a long term housing need from the Department of Social Protection (currently provided through Rent Supplement) to housing authorities using a new Housing Assistance Payment (HAP)⁴².

The effect of this transfer and the introduction of a new form of Housing Assistance Payment will be to remove a barrier to accessing full-time employment that exists under the Rent Supplement scheme. Under the new Housing Assistance Payment, the contribution that the tenant makes towards the rent is based on a means test that links the level of contribution to the household income, rather than employment status.

Recommendation: The rollout of the Housing Assistance Payment (i.e. decoupling housing support from social welfare payments) is an essential element in removing barriers to employment and reducing replacement rates. Once implemented (due to occur by January 2013), the impact of HAP on replacement rates should be monitored to ensure that the payment successfully reduces barriers to employment, whilst protecting living standards.

Responsibility: Department of Social Protection / Department of Environment, Community and Local Government

In their September 2012 report, the IMF has noted that in Ireland (in contrast to most other EU members), unemployment benefits do not vary with the duration of unemployment⁴³. It was further noted that such a structure can lead to disincentives for a minority of job seekers (e.g. through the creation of poverty traps). Reform of the social welfare, however, should be considered in the context of the level of employment opportunities available.

Recommendation: There is a need to reform the social welfare system so that benefits decline in line with the length of time a person is out of work⁴⁴ - this would be in line with European approaches to social welfare. The retention of secondary benefits for a period of time after take up of full time employment (depending on income levels) can reduce the impact from the loss of social welfare entitlements upon taking up employment. A comprehensive review of Secondary Benefits Retention arrangements, however, should be conducted with a view to establishing whether or not they are effective in the long term in removing barriers to the take up of employment.

Responsibility: Department of Social Protection

41 Rent Supplement is paid to people living in private rented accommodation who cannot provide for the cost of their accommodation from their own resources. In general, individuals qualify for a Rent Supplement, if their only income is a social welfare payment and they satisfy a range of other conditions.

42 At present there are around 70 rent schemes in the country operated by individual housing authorities. Under the Housing (Miscellaneous Provisions) Act, 2009, a new regulatory framework will be put in place that will set national parameters for local rent schemes. This new model will be progressive and will allow for a gradual increase in rent contribution as the household income rises.

43 International Monetary Fund, IMF Country Report No. 12265, Ireland: Selected Issues, September 2012.

44 Greater conditionality is being developed. As of August 2012, it has been reported that some 1,275 jobseekers' payments have been reduced. The reduction is for people who refuse to take up training offers, job interviews or employment opportunities.

3.3.2 Sectoral Employment Agreements

It is estimated that between 212,000 and 284,000 workers⁴⁵ are covered by either Employment Regulation Orders (ERO's) or Regulated Employment Agreements (REA's) regarding the terms and conditions of their employment⁴⁶. An examination of the hourly rates guaranteed by ERO's suggests that these agreements are offering a premium of approximately nine per cent over the NMW rate⁴⁷. Current REAs provide for a wage rate well in excess of the hourly minimum wage.

In 2010, Forfás concluded that elements of the Employment Regulation Orders (EROs) were resulting in higher wage costs than might be expected given labour market conditions. Specifically, it was found that clauses contained in EROs, which determine working conditions, may be imposing more serious costs on employers than the hourly rate prescribed in such agreements. While much of the power in relation to EROs and REAs rests with employer and employee representatives, reform of the various collective agreements was recommended.

Following a High Court Ruling, all Employment Regulation Orders ceased to have statutory effect from 7 July 2011⁴⁸. As a result, the pay and conditions of employees who start work after 7 July 2011 was governed by employment legislation such as the minimum wage. Existing employees who were covered by an ERO have existing contracts of employment, which govern their pay and conditions of work.

In response, in December 2011, the Minister for Jobs, Enterprise and Innovation published the Industrial Relations (Amendment) (No. 3) Bill 2011. The purpose of the Bill was to reform the Joint Labour Committee (JLC)/REA system with the goals of making it more responsive to changing economic circumstances and labour market conditions and reinstating a system of protection for workers in these sectors in the aftermath of the High Court ruling. The principal measures in the legislation provided for:

- JLCs will have the power to set a basic adult rate and two additional higher rates, based on length of service in the sector or enterprise concerned as well as the standards and skills recognised for the sector concerned.
- JLCs will no longer set Sunday premium rates. In order to recognise the special status of Sunday working a statutory Code of Practice will be prepared by the Labour Relations Commission (LRC) following submissions from employers and trade unions.
- Companies will be able to derogate from EROs and REAs in cases of financial difficulty. Such derogation will be granted, for a limited period, in cases of proven economic difficulty, following consultation with the employees.

45 Duffy, K. & Walsh, F., Report of Independent Review of Employment Regulation Orders and Registered Employment Agreement Wage Setting Mechanisms, April 2011.

46 The various agreements on pay and conditions made by Joint Labour Committees (JLCs) are known as Employment Regulation Orders (EROs). Agreements which result from negotiations between trade unions and employers are called Collective Agreements. If a Collective Agreement has been registered with the Labour Court, it is known as a Registered Employment Agreement (REA). These agreements are reached by employers and unions, independently of Government.

47 The difference between the employment weighted average of the JLC minimum wages and the national minimum wage suggests a positive differential of about 10 per cent for the average JLC rates. For further details, see Department of Jobs, Enterprise and Innovation, Report of Independent Review of Employment Regulation Orders and Registered Employment Agreement Wage Setting Mechanisms, April 2011

48 In *John Grace Fried Chicken and others v The Catering Joint Labour Committee*, The Labour Court, Ireland and the Attorney General

- The constitutionality of EROs and REAs would be restored through inclusion of robust principles and policies.

The Industrial Relations (Amendment) (No. 3) Bill was enacted on 24th July 2012 and commenced on 1st August. It is not yet clear what the impact of the Act will be in terms of improving labour cost competitiveness. In part, this will be determined by the conclusion of on-going discussions on overtime and Sunday working and uptake of the derogation in cases of financial difficulty⁴⁹.

The Minister has also moved to implement a number of additional reforms:

- The Minister has requested the Labour Court to put in train the necessary steps for the abolition of the three JLCs (the Aerated Waters and Wholesale Bottling; Provender Milling and Clothing JLCs), on the basis that these sectors have declined considerably in terms of numbers employed, or have effectively ceased to function as wage fixing bodies.
- The Minister has also asked the LRC to begin work on the formulation of two Codes of Practice. The first, on Sunday Working, will provide guidance to employers, employees and their representatives in sectors covered by Employment Regulation Orders, on arrangements that may be put in place to comply with the options specified at section 14 of the Organisation of Working Time Act, 1997. The second will address the standardisation of benefits in the nature of pay - including overtime and the conditions under which it becomes payable - across sectors covered by JLCs.

The Act provides that the Labour Court will carry reviews of the JLCs, as soon as practicable after the commencement of the Act. The outcome of these reviews will inform the Labour Court as to whether any JLC should be maintained in its current form, amalgamated with another JLC or its establishment order amended.

Recommendation: It is important that impact of the Industrial Relations (Amendment) Act 2012) in terms of promoting labour cost competitiveness be assessed in due course as provided for in the Industrial Relations (Amendment) Act 2012⁵⁰. Likewise, the formulation of the Codes of Practice relating to Sunday Working and standardisation of benefits (i.e. overtime) should be completed as quickly as practicable while seeking to enhance labour cost competitiveness.

Responsibility: Department of Jobs, Enterprise and Innovation / Labour Court / Labour Relations Commission

3.3.3 National Minimum Wage (NMW)

At first glance, relatively few workers in Ireland are earning the NMW rate - based on data from the CSO's National Employment Survey, in October 2007, 4.9 per cent of employees in Ireland (83,700) were earning €8.65 per hour or less. It is likely that the minimum wage

49 Use of derogation will not occur until after new Employment Regulation Orders are made and Collective Agreements are registered.

50 By the end of the second quarter of 2013, the Government is required to report to the Troika on the impact on the labour market of reforms to the sectoral wage mechanisms. For further detail see <http://www.finance.gov.ie/documents/publications/other/2012/EU-IMFprog.pdf>

influences wage levels of those who earn close to the NMW rate. For example, the earnings of another 26 per cent of the labour force are within 1.5 times the NMW.

The NMW impacts on sectors in different ways - sectors such as wholesale and retail, hotels and restaurants, and other services sectors tend to have significantly more NMW workers than internationally trading sectors. While the sectors and occupations where the greatest job losses have occurred generally coincide with the sectors where the NMW is most prevalent (excluding construction), these sectors have also experienced a major collapse in demand for their output.

A majority of international studies surveyed by Neumark and Wascher (2007) give a relatively consistent (although not always statistically significant) indication of negative employment effects of minimum wages. Of the studies which find a negative relationship between minimum wages and employment, a 10 per cent increase in the minimum wage typically reduces employment in the cohort studied by between zero and five per cent⁵¹. However, there is broad agreement that a moderate national minimum wage (e.g., 30-40% of median wages) can have a positive effect on equality and will have a limited effect on lowering employment rates for low skilled workers.

Forfás' earlier work argued that replacement rates and sectoral agreements represent the primary barriers to labour cost adjustments⁵². Thereafter, other measures such as changes to the National Minimum Wage should be considered. The NMW was reduced from €8.65 per hour to €7.65 per hour as of 1st February 2011 and was subsequently changed back to €8.65 from 1st July 2011. In this context, Forfás believes that consideration should be given to amending the NMW rate for younger cohorts, given the high levels of youth unemployment.

Recommendation: Consideration should be given to extending the lower NMW rate for younger workers^{53&54}. Currently a rate of €6.06 exists for workers less than 18 years of age. Recognising high levels of youth unemployment, consideration might be given to introducing a rate lower than €8.65 for all workers aged under 21 or 25 years of age.

Responsibility: Department of Jobs, Enterprise and Innovation

51 Neumark, D. and Wascher, W., Minimum Wages and Employment, Institute for the Study of Labor, Discussion Paper Series IZA DP No. 2570, January 2007.

52 Forfás, Review of Labour Cost Competitiveness, October 2010.

53 As noted in the 2010 Forfás Review of Labour Costs Competitiveness, firm level actions may limit the impact of any such reductions. Firms generally do not favour wage reductions that just take advantage of labour market conditions; they usually prefer layoffs to pay cuts because they are less harmful to morale. Although layoffs also hurt morale, their effects are less severe and long-lasting than those of wage reductions. Firms also remain reluctant to hire overqualified people at lower rates than existing staff, as perceptions of internal wage equity are important for morale. For a more detailed discussion on firm level behaviour, see Bewley, Truman F., *Why Wages Don't Fall during a Recession*, 1999, Harvard University Press.

54 In analysing Irish earnings data, the ESRI have identified a similar trend in Ireland and noted a general reluctance of firms to cut wages in order to avoid productivity losses associated with worker dissatisfaction or higher rates of labour turnover. In support of this view, the study demonstrates that firms will adopt strategies such as reducing staff numbers, hours worked and bonus payments, in preference to reducing wages. See Bergin, A., Kelly, E., & McGuinness, S., *Explaining Changes in Earnings and Labour Costs During the Recession*, Renewal Series Paper 9, ESRI, April 2012.

3.3.4 Activation and Up-skilling

The high levels of unemployment, youth unemployment and long-term unemployment pose a significant challenge to society, to policymakers, as well as imposing costs on enterprise. Structural imbalances in the labour market arising from the past dominance of the construction sector remain.

At the same time, concerns persist about the availability of enterprise relevant skills despite the unemployment crisis. At present, skills shortages are currently limited to specialised positions in the information and communications sector (e.g. designers and developers with specific skill sets such as sophisticated database architecture, JAVA related applications etc.), in high tech manufacturing (mostly in the biopharma sector), in the financial services sector (e.g. risk analysts, credit specialists, actuaries), and in the health sector (e.g. medical doctors, radiographers, and advanced nursing practitioners)⁵⁵.

However, the reality is that many unemployed workers are ill-equipped to work in those sectors most likely to experience employment growth. A major programme of up-skilling and re-skilling is essential to support growth in employment and to manage labour costs.

In the longer term, Ireland must address long standing participation bottlenecks - historically, Ireland has had relatively low rates of labour market participation and employment among certain groups (e.g. females; lone parents; persons with a disability; older workers and people dependent on welfare).

A number of programmes have been introduced recently, designed to up-skill unemployed workers, and provide them with practical work based experience. The greater emphasis on evaluation, targeting, and accreditation which has accompanied the development of recent programmes (e.g. Jobbridge⁵⁶ and Springboard⁵⁷) is to be welcomed.

Activation measures should primarily aim to improve employability and should be characterised by:

- Identifiable labour market/ enterprise needs;
- Ability to target candidates appropriately to programmes based on their abilities, skills and learning requirements;
- Emphasis on quality assurance and demonstrated progression pathways for the learner - to employment/self-employment, further/higher education and training;
- Structured internship / opportunities providing work experience opportunities within enterprise.

There has been some progress in this regard through the rollout of the Springboard programme and to an even greater extent, with the development of a Higher Diploma Level 8 Conversion Programme in Computing. Such programmes directly link higher education places with identified enterprise needs and have significant employer engagement in course development. In the case of the Conversion Programme, companies were involved in the

⁵⁵ A skills shortage refers to a situation whereby there are an insufficient number of individuals who have the required qualifications, skills set and/or experience to fill a particular post. For further detail, see Expert Group on Future Skills Needs, National Skills Bulletin 2012, July 2012

⁵⁶ Jobbridge is a national internship scheme, which provides up to 5,000 work experience placements for interns for a 6 or 9 month period.

⁵⁷ Springboard is a series of educational courses aimed at areas where there are current or future opportunities (e.g. in finance, green energy, ICT, science and environment, sales and marketing).

selection of candidates for entry to the courses, delivery of aspects of the programme and the provision of internship placements during the programme. This close education/ industry engagement increases the prospects of progression to employment on completion of such programmes and also encourages better engagement of jobseekers in up-skilling and conversion where the progress paths are clearer. Wider adoption of models such as this should be considered where evaluations have found positive outcomes. There is also more scope to align broader education and training provision with the needs of the labour market.

Recommendation: There should be wider adoption of activation programmes which are linked directly to identified enterprise needs, have significant employer engagement in course development, selection of candidates, and programme delivery, and which offer internships to participants.

Responsibility: Department of Social Protection / Department of Education and Skills

3.3.5 Labour Costs: Maintain a Competitive Tax Regime for Labour

A competitive tax regime is essential in attracting and retaining individuals in Ireland and more generally in terms of encouraging people to remain in or return to the labour market. In general, the Irish taxation system has been broadly supportive of labour market efficiency. While Budget 2012 did not increase taxes on labour, increases in personal taxation in 2010 and 2011, however, have eroded cost competitiveness and the incentive to work. Budget 2013 has abolished the weekly PRSI allowance for employees. Higher labour taxes raise the costs of labour, raise replacement rates (i.e. make work less attractive vis-à-vis social welfare), reduce take home pay and domestic demand and risk stimulating the informal economy.

In Ireland, the difference between the employers' cost of hiring an individual and the individual's actual take home pay, has widened for all income categories (in particular, as a result of changes to tax bands and credits and the introduction of the Universal Social Charge) while the tax wedge in most OECD countries is unchanged or falling⁵⁸. The difference is wider for higher paid workers in Ireland, which is of concern as Ireland competes internationally for mobile talent.

Another concern is that the level at which individuals start paying the higher rate of tax (€32,800 for single individuals) is low relative to other countries⁵⁹. The higher rate of tax actually impacts on individuals earning less than the average wage⁶⁰. Marginal tax rates (i.e. the tax paid on an individual's last euro of income) are now in excess of 50 per cent for single individuals earning €32,800 per annum⁶¹. It is also important that expenditure changes in

58 For a single person with no children on 167 per cent of the average wage (€66,000 p.a.), the difference between what the employer pays and the employee receives has increased as a result of increased labour taxes. The difference in 2010 was 39.9 per cent up from 34 per cent in 2008. This differs from the trend reflected in the OECD 28, which experienced an average decrease in taxes on labour. Importantly the downward decrease on taxes on labour was evident amongst a number of our key competitors e.g. Poland, the Netherlands, and Switzerland.

59 For instance, in the case of the US, the threshold at which the marginal rate takes effect is at a much higher earnings level (approximately €310,000). In the case of Germany the marginal rate is lower than Ireland's at 47.5 per cent and takes effect at a much higher wage level of approximately €253,000. All rates refer to 2009, OECD taxing wages 2009, Forfás calculations

60 The CSO, Earnings and Labour Costs Survey for Q1 2012 show that average weekly earnings are €691.29. The average annual salary in the economy, therefore, is approximately €36,000.

61 The following example illustrates the effect of recent changes in taxation on individuals. For a single worker earning €40,000 per annum the average rate of tax has increased from 18.6 per cent in 2008 to 24.2 per cent in

Budgets do not increase the costs of employment - for example, proposals to introduce a statutory sick pay scheme.

Recommendation: It is recommended that there are no further increases in the labour tax wedge. There is a need to flag when it will be feasible to reduce marginal labour rates below 50 per cent. The introduction of further costs on employment (e.g. changes to sick pay policy, pension's policy, etc.) should be considered carefully from a labour cost competitiveness perspective given the scale of our unemployment crises.

Responsibility: Department of Finance/ Department of Social Protection

2012, while the marginal rate has increased from 47 per cent to 52 per cent. At the higher income levels, a single worker earning €100,000 per annum, the average rate of tax has increased from 33.8 per cent in 2008 to 40.9 per cent in 2012, while the marginal income tax has increased 43.5 per cent in 2008 to 52 per cent in 2011. Department of Finance, Budget 2012, Annex

4. Property Costs

4.1 Summary

While labour costs dominate business costs, property costs form a significant share of costs – particularly in service sectors. As outlined in Chapter 2, property costs (as measured by lease costs) are particularly significant for professional services operations (10.4% of location sensitive costs).

Construction costs and rental costs for both office and industrial space have fallen dramatically for new businesses since the collapse of the property bubble and the onset of recession. Of course, many existing businesses are tied into higher property costs having purchased or leased property with upward only rent review clauses during the property boom.

Figure 4.1 illustrates the change in capital values for commercial property between 2009 and 2012. With commercial property values approximately 65 per cent below their 2007 peak, there is some evidence of stabilisation.

The next series of charts consider the costs of both constructing and renting commercial property. Not surprisingly, construction costs in Ireland have declined markedly over recent years. The cost of constructing a prime office unit in Ireland has fallen by approximately 32 per cent since the peak of the property boom in 2007 (Figure 4.2), while the costs of constructing a prime industrial unit (Figure 4.3) have fallen by over 23 per cent between 2007 and 2011.

Looking at Gardiner and Theobald data on building tender price inflation for Ireland, the impact of the recession is clear to see – tender prices in Ireland fell by 10.4 per cent in 2008, 17.1 per cent in 2009 and 5.8 per cent in 2010 before stabilising. Of the 13 locations benchmarked, Ireland now is sixth and seventh most expensive in terms of office and industrial construction costs, respectively.

Looking at Irish earnings data for the construction sector, labour costs have reduced over the course of the recession, but perhaps not by as much as might have been expected, given the dramatic reduction in activity. According to CSO data, weekly earnings in construction declined by almost 11.3 per cent between Q1 2008 and Q1 2012; hourly wages, however, declined by just 6.7 per cent over the same period – similar to the reduction agreed in the construction sector REA⁶². In November 2012, the Labour Court recommended increasing the previously agreed 7.5 per cent pay cut to 10 per cent⁶³.

In terms of how rents have evolved, Figure 4.4 finds that office rents in Ireland have fallen substantially over the 2007-2011 period (this figure relates to new contracts only). Office rents on new leases in Dublin have fallen over 45 per cent. The rate of decline, however, has stabilised between 2010 and 2011. Dublin is now the sixth cheapest location amongst the 16 locations benchmarked, and is now cheaper than both Frankfurt and Madrid. In terms of renting a prime industrial site, in 2010 Ireland was the sixth most expensive location out of the 14 locations benchmarked (Figure 4.5). Cumulatively, industrial rental costs on new leases fell by almost 37 per cent between their peak in 2007 and 2010.

Commercial rates are a property-based source of income that is levied by local authorities throughout Ireland on the occupiers of commercial and industrial properties. The annual commercial rate for each property is calculated by multiplying the annual rate of valuation (ARV) by the rateable valuation for the property which is determined by the Valuation Office.

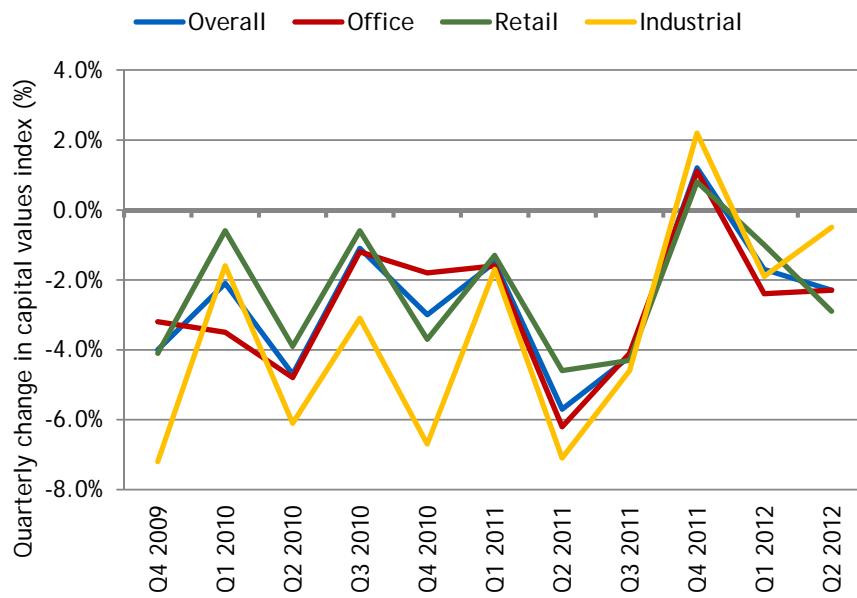
62 See CSO, EHECS Earnings Hours and Employment Costs Survey, Q1 2012, June 2012.

63 <http://www.labourcourt.ie/labour/labour.nsf/LookupPageLink/HomeRecommendations>

Based on data from the Department of Environment, Community and Local Government, in 2012 the national average ARV declined for the third year in a row (Figure 4.6)

4.2 Property Cost Indicators

Figure 4.1: Quarterly Change in Capital Values in Ireland, 2009-2012

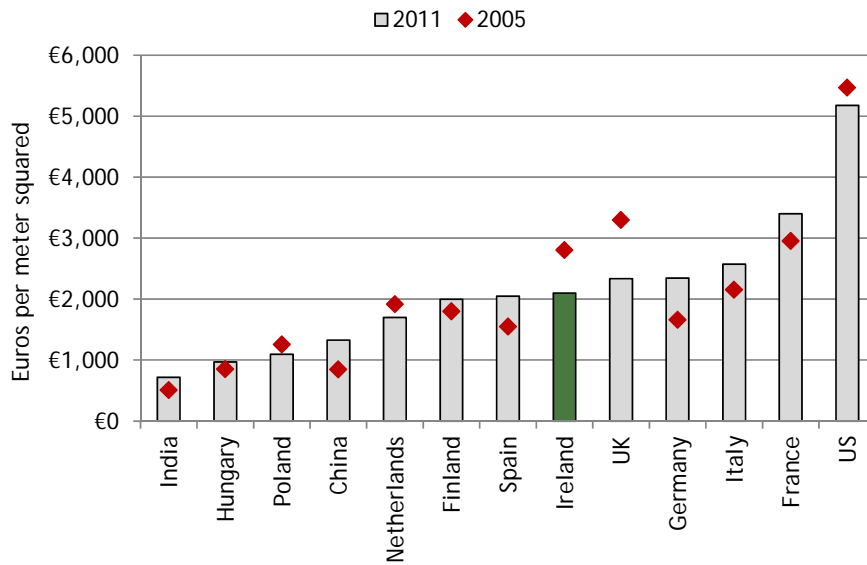


This indicator illustrates the change in capital values in Ireland for a range of commercial property classes over the last number of years. While negative growth has been recorded across all sectors since the beginning of the recession (in total capital values are approximately 65% below their 2007 peak), there is some evidence of stabilisation⁶⁴.

Source: Jones Lang LaSalle, Irish Property Index

⁶⁴ The positive change recorded in Q4 2011 reflects the reduction in stamp duty in Budget 2011 – a change which technically moved values up by 3.8 per cent, all other things being equal. In fact, property values increased by 1.2 per cent overall, suggesting that the underlying fall in values would have been -2.6 per cent without the stamp duty reduction.

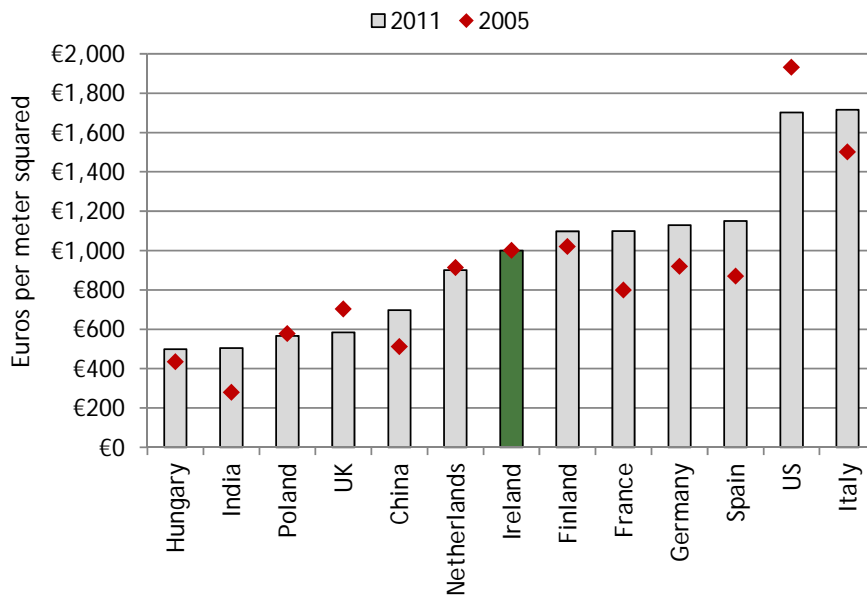
Figure 4.2: Cost of Constructing a Prime Office Unit⁶⁵, 2011



Construction costs data takes account of building, labour and material costs. The cost of constructing a prime office unit in Ireland has fallen by 32% since costs peaked in 2007 (and down 25% from 2005). Amongst the locations surveyed, Ireland was the 6th most expensive location to construct a prime office unit in 2011.

Source: Gardiner and Theobald, International Construction Cost Survey

Figure 4.3: Cost of Constructing a Prime Industrial Unit⁶⁶, 2011



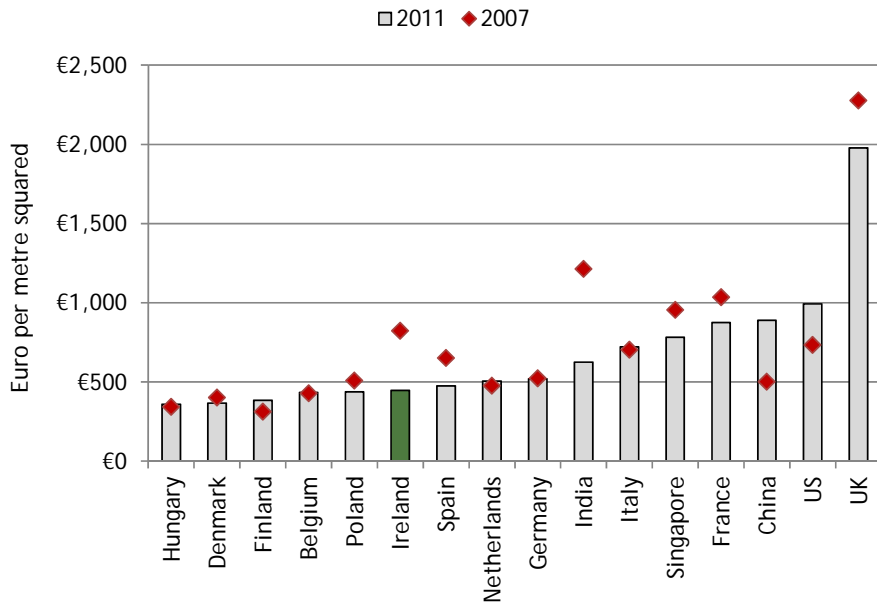
The cost of constructing a prime industrial unit in Ireland has also fallen significantly over recent years. Costs in 2011 had fallen back to levels last seen in 2005. Relative to the cost peak recorded in 2007, costs have fallen by over 23 per cent, and Ireland is now the 7th most expensive location amongst the 13 countries benchmarked.

Source: Gardiner and Theobald, International Construction Cost Survey

65 Prices quoted are the upper boundary of the cost of the constructing a prime office unit. Prices quoted for the US reflect the upper boundary cost of constructing a price office unit in New York.

66 Prices quoted are the upper boundary of the cost of the constructing a prime industrial unit. Prices quoted for the US reflect the upper boundary cost of constructing an industrial unit in New York.

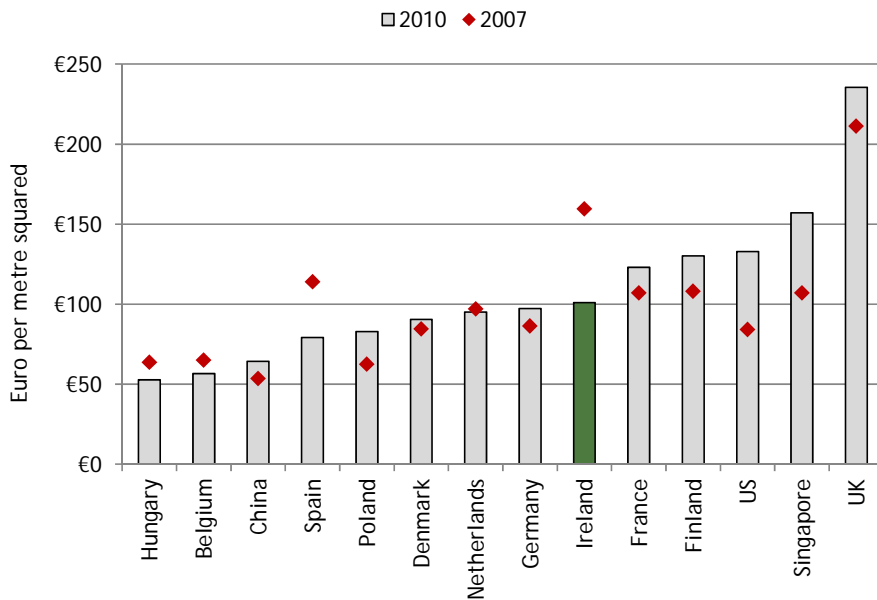
Figure 4.4: Cost of Renting a Prime Office Unit, 2011



Office rents in Dublin on new leases have fallen by 45% between 2007 and 2011. The pace of decline seems to have stabilised in 2010 and 2011, with rents falling by less than 1% year on year. Dublin is now the sixth cheapest rental location amongst the 16 locations benchmarked, and is now cheaper than both Frankfurt and Madrid.

Source: Cushman and Wakefield, Office Space Across the World, 2007 - 2012

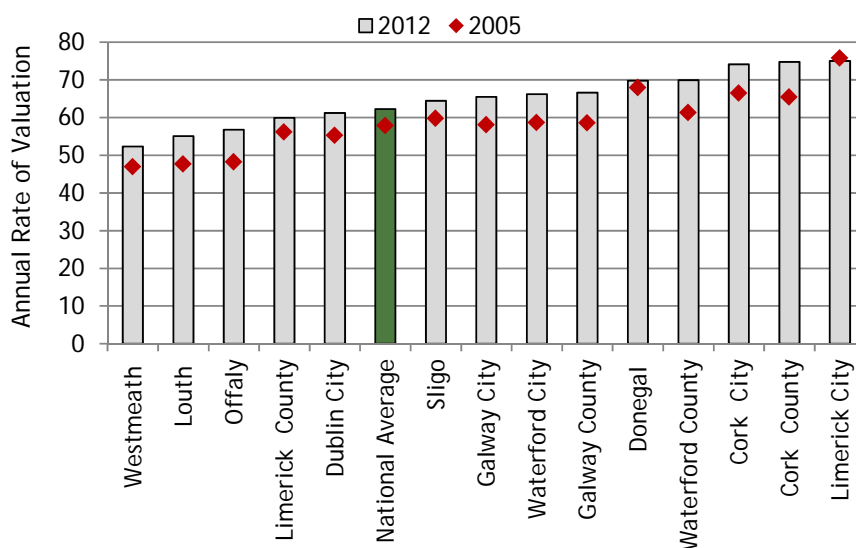
Figure 4.5: Cost of Renting a Prime Industrial Unit, 2010



In terms of industrial rental costs on new leases, Dublin was the 6th most expensive location out of the 14 locations benchmarked. Rental costs in Ireland have fallen in recent years and cumulatively have declined by almost 37% since their peak in 2007, improving Ireland's competitiveness ranking by 4 places.

Source: Cushman and Wakefield, Industrial Space Across the World, 2007 - 2011

Figure 4.6: Annual Rate of Valuation (ARV) by selected Local Authority⁶⁷, 2012



The annual commercial rate for commercial property in Ireland is calculated by multiplying the annual rate of valuation (ARV) by the rateable valuation for the property (determined by the Valuation Office). In 2012 the national average ARV declined for the third year in a row to a rate of 62.25 - but this remains above the 2005 average rate.

Source: Department of Environment, Community and Local Government

4.3 Policy Focus on Property Costs

A properly functioning property market is an essential element of a healthy economy. It is essential that property related costs faced by enterprises already operating in Ireland are internationally competitive and that potential new entrants are not dissuaded from establishing in Ireland because of excessive property prices.

Reinvigorating the property market to a sustainable level is also important. Firstly, it offers the potential to create employment. Secondly, it is clear that the availability of high quality office space in key locations is starting to fall with implications for attracting new enterprises⁶⁸ and for property costs as prices are bid up. In this regard, the lower rate of stamp duty (2 per cent rather than 6 per cent) for non-residential property transactions is welcome⁶⁹. Similarly, the introduction of a valuation based residential property tax in 2013 will also represent a move away from transaction based property taxes.

The analysis and recommendations set out below are intended to improve the efficiency of the Irish property market in order to reduce the costs of doing business in Ireland whilst simultaneously reducing the potential for future boom-bust cycles by smoothing cycles. The analysis is divided into a number of categories:

⁶⁷ Data is included for all local authorities with a designated Gateway town. Data on Fingal, Dun Laoghaire-Rathdown and South County Dublin are excluded from the chart as their values are not comparable due to revaluation of all commercial and industrial property in these areas by the Valuation Office.

⁶⁸ See "Lack of office space may thwart multinationals, warns IDA" in Irish Times, 13th July 2012

⁶⁹ As a result of changes introduced in Budget 2012, a new lower rate of 2 per cent applies to instruments relating to non-residential property. In conjunction with the introduction of the single rate of 2 per cent, which applies to the entire amount of the consideration attributable to non-residential property, the current exempt threshold of €10,000 has also been abolished.

- Promoting market certainty through better information;
- Managing business property taxes (rates);
- Supporting the sustainable development of the property market over a longer time horizon.

4.3.1 Market Certainty

Imperfect information can restrict the ability of buyers and sellers to make rational decisions: unless businesses and consumers feel that they have adequate information to make informed decisions (e.g. confident that they have up-to-date and accurate information relating to prevailing market conditions) they will be reluctant to engage with the market. International experience (e.g. Finland) suggests the provision of detailed, relevant and timely data is a key element in ensuring an efficiently functioning commercial property market. In the case of commercial property, the only fairly comprehensive and widely available data is on the Dublin office market.

The Property Services Regulatory Authority (PSRA) was established on a statutory basis by Ministerial order under the Property Services (Regulation) Act 2011, which came into effect on 3rd April 2012. As well as being responsible for the licencing of property services providers (PSPs), investigating complaints against PSPs and imposing sanctions in respect of improper conduct, and setting various other property related standards, the PSRA is also tasked with:

- The publication of residential property sales prices; and
- The establishment and maintenance of a public database containing relevant details of letting arrangements and rent reviews in the commercial property market (Section 87)⁷⁰.

These measures are designed to help restore confidence in the property market.

Recommendation: It is anticipated by the PRSA that the commercial leases database will be put in place during the early part of 2013 and that it will contain data relating to leases entered into after 3 April 2012⁷¹. Given the dearth of property related data in Ireland, it is essential that this target is adhered to. There may be merit in extending the database to cover the purchase of commercial property.

Responsibility: Property Services Regulatory Authority

4.3.2 Managing Business Property Taxes (Rates)

Commercial rates are a form of property tax levied by local authorities on tenants of commercial properties. These revenues enable Local Authorities to provide services to both businesses and households. Rates generally account for a relatively small proportion of total business costs for many businesses⁷².

70 Section 87 of the Property Services (Regulation) Act 2011 provides for the Property Services Regulatory Authority (PSRA) to establish and maintain "The Commercial Leases Database" which it shall make available for inspection on the payment of a fee.

71 PQ Response by the Minister of Justice, Equality and Law Reform [33354/12], 10 July 2012

72 The Advisory Group on Small Business, The Voice of Small Business – A Plan for Action, November 2011

The dependence of local authorities on commercial rates has increased sharply in recent years due to reduced central government funding and development charges. Despite a moderation in rates in the last two to three years, the cumulative increase in commercial rates has been almost double the rate of inflation over the last decade. In absolute terms, commercial rate revenues grew sharply (7%) in 2012, and as a result of falling rents, rates as a proportion of rents have increased.

The commercial rates system should be simple, transparent and easy to administer. A broad based system with a lower nominal rate is preferable to one with a higher rate and a range of exemptions. In terms of potential reforms, the commercial rates regime should not discriminate between firms based on ownership, country of origin, sector or performance, etc. - other taxes are more appropriately designed to account for business performance (e.g. corporation tax, capital gains, etc.).

Rates are calculated on the basis of property valuations. While a process of revaluation of all commercial and industrial property started in 2005, this will not be completed until at least 2015. This process is too slow. Significant, expedited reform of the valuations process is required to ensure that rates valuations are appropriate to current market conditions. In this regard, the recent publication of the Valuation (Amendment) Bill 2012 is welcome⁷³.

In the long term, the Government should provide local authorities with sustainable sources of income from an annual recurring residential property tax and user charges (e.g. water, etc.).

The implementation of the Local Government Efficiency Review Group report is also vitally important. The report sets out 106 recommendations that could achieve efficiencies and savings amounting to €500 million, which could be passed on in savings to businesses, citizens and Central Government⁷⁴. In response to the report, an implementation group has been established⁷⁵ and the first Report of the Local Government Efficiency Review (LGER) Implementation Group was recently published⁷⁶. According to the Group's report, savings from the local government sector attributed to efficiency measures (as opposed to reduction in activity) amounted to €195 million in the years 2010 and 2011. The on-going focus of the Group is on achieving further efficiency gains.

Recommendation: The enactment and implementation of the Valuations Bill is critical as the revaluation process needs to be expedited. The process could be accelerated through the

73 This purpose of the Bill, published in August 2012, is to amend the provisions of the Valuation Act 2001 to provide for the introduction of a property valuation self-assessment mechanism, an ability to pay clause and related matters including the abolition of liability on a subsequent occupier to pay property rates incurred by a previous occupier.

74 While most of the recommendations concern efficiency savings, a number of recommendations also extend to cost recovery and revenue rising, with an emphasis on a more equitable distribution of the revenue burden. Of the €511 million total, €346 million comprises efficiency savings, and €165 million is accounted for through improved cost recovery and revenue raising. Advances have already been made on some of the recommendations with announcements that Limerick city/county and North and South Tipperary councils are to merge. See Report of the Local Government Efficiency Review Group, 2010

75 The Implementation Group, chaired by Pat McLoughlin was established by Minister Hogan in April 2011 and is tasked with overseeing and advising on the implementation of the Report of the Local Government Efficiency Review Group. The Terms of Reference for the Group can be accessed at:

<http://www.environ.ie/en/LocalGovernment/LocalGovernmentEfficiencyReviewGroup/>

76 The Implementation Group has prioritised the implementation of key recommendations relating to procurement, ICT, human resources/staffing and shared services as areas with potential for short-term and significant savings. This is the first in a series of reports to the Minister and outlines the Group's assessment of progress to date and the next steps necessary.

introduction of self-assessment (as is the case for many other taxes) or the outsourcing of valuations. Where properties are revalued, it is important that ARV's are not allowed to increase to offset business savings. To ensure that recorded valuations reflect changes in market value relatively quickly, property values should be updated on a 3-5 year cycle.

Responsibility: Commissioner for Valuations / Department of Public Expenditure and Reform

Recommendation: Progress the decisions to introduce an annual residential property tax and water charges for households. The speedy introduction of such taxes and charges will assist in rebalancing Local Authority revenue sources and would help to ensure Local Authorities are adequately funded in a sustainable manner. In order to avoid more economically damaging increases in (for example) income tax, and mirroring practices in other advanced economies, it will be necessary to achieve a significant revenue stream from property taxes.

Responsibility: Department of Finance/ Department of the Environment, Community and Local Government

Recommendation: Continue to implement the recommendations from the Report of the Local Government Efficiency Review Group. As efficiency savings are achieved, some of these should be used to achieve a broad based reduction in rates by directing Local Authorities to lower their Annual Rate on Valuation.

Responsibility: Department of the Environment, Community and Local Government / Local Authorities

4.3.3 Rent and Rent Reviews

Commercial leases in Ireland have typically been long-term in nature; often up to 25 years. The Land Conveyancing and Law Reform Act 2009 was introduced in Ireland to ensure that all new leases signed from March 2010 contain a provision that rents can be reviewed both upwards and downwards on review⁷⁷. Previously, rents could only normally be reviewed on an 'upwards only' basis at review under the terms of lease. While this legislation is welcome, it cannot assist existing enterprises, tied into long term leases at rates significantly above current market rates. However, the Government has noted that despite extensive consideration⁷⁸, it has not proved possible to develop a targeted scheme to tackle upward only rent reviews in existing business leases which would not be vulnerable to a legal challenge or require compensation to be paid to landlords. It remains in the interests of landlords, however, to renegotiate rents given the risk of losing tenants.

NAMA has also developed a guidance note for dealing with tenants' difficulties arising from upward-only rent reviews in relation to its own portfolio of property⁷⁹. This provides an opportunity for NAMA to approve rent reductions where it can be shown that rents are in excess of current market levels and a tenant's viability is threatened. The guidance note is designed to facilitate a mutually agreeable process between the landlord owning the property (albeit as security for a NAMA loan) and the tenant, and also provides for the appointment of an independent valuation of market rent where necessary. NAMA had received 114

77 Land and Conveyancing Law Reform Act, 2009

78 See PQ [34262/12].

79 National Asset Management Agency, NAMA Portfolio Management Internal Guidance Note: Assessment of a debtor/receiver proposal for a reduction in rent on an upward-only commercial lease, December 2011.

applications for rent abatements prior to issuing the Guidance Note, of which 113 applications were approved and one was refused. Between 6th December 2011 and 27th March 2012, NAMA had received a further 40 applications for rent abatements under the terms of the Guidance Note. By 27th March 2012, 5 of these applications were approved; another 2 were ineligible; and the remaining 33 applications were still under review⁸⁰.

Separately, the Department of Justice and Law Reform has continued to progress the recommendations of the Working Group on Transparency in Commercial Rent Reviews since it reported in July 2010. Businesses can make use of the Rent Review Arbitration Code, which was drawn up by the Working Group to help to resolve issues at a lower cost, in considerably less time, and in a less adversarial way for the parties concerned. Parties to a rental agreement are free to specify that the code should apply in relation to rent review arbitrations, and use of the code has been endorsed by a number of significant players. The Working Group recommended that the code be reviewed no later than July 2013.

Recommendation: As per the recommendation of the Working Group on Transparency in Commercial Rent Reviews, the Rent Review Arbitration Code should be reviewed no later than July 2013. This review should consider the effectiveness of the code in resolving disputes over rent reviews, and the degree to which stakeholders are making use of the code.

Responsibility: Department of Justice and Equality

4.3.4 Supporting the Sustainable Development of the Property Market

It is important that policies are put in place now that facilitate investment in and development of new commercial properties that meet the needs of enterprise. One of the key issues in terms of sustainable development relates to the manner in which Local Authorities calculate and implement levies on development.

Firstly, Local Authorities require more prioritised and integrated plans based on realistic estimates of future development requirements - this would reduce the cost of providing essential infrastructure. Reductions in construction costs have already reduced these costs. A move to a more coordinated planning system (as well as the downturn in property values) may mean that development will no longer take place where there is not already a suitable level of infrastructure, meaning that levies could be reduced. Reductions in levies may also help areas to attract inward investment.

In June 2012, draft guidelines for planning authorities on development contributions were published⁸¹. The aim of these draft guidelines is to provide updated guidance on the drawing up of development contribution schemes to reflect the radical economic changes that have impacted across all sectors since guidance was last issued 2007. While it is recognised that the adoption of development contribution schemes is a reserved function of the elected members of each planning authority, one of the outcomes of the new guidance should be to achieve a level of consistency in development contribution schemes on a national basis providing enhanced clarity to inform investment decisions across different Local Authority areas. It is important that the final set of guidelines which emerge from this process provide all planning authorities with a consistent step-by-step methodology for the calculation of

⁸⁰ See PQ [16622/12], Written Answers, Tuesday, 27 March 2012.

⁸¹ Final guidelines will be issued under section 28 of the Planning and Development Acts 2000 – 2010. For further details see Department of Environment, Community and Local Government, Development Contributions - Draft Guidelines for Planning Authorities, June 2012

development contributions. Furthermore, development contributions should promote enterprise, support sustainable development and encourage jobs and growth.

Recommendation: Arising from the new draft guidelines on development contributions, Local Authorities should develop more robust and transparent charging mechanisms for Local Authority charges that match levies with the economic cost of providing development⁸².

Responsibility: Local Authorities

Finally, the issue of planning reform is a recurring theme in any discussion about the commercial property market. The NCC's *Costs of Doing Business 2011* report contains a range of actions designed to reduce planning delays and enhance the coordination of infrastructure delivery. These actions remain relevant and if implemented could have a positive impact upon construction costs in Ireland.

82 Note that the recently published National Broadband Strategy states that the Department of the Environment, Community and Local Government is undertaking a consultation on guidelines in relation to development contributions which suggests the introduction of waivers in respect of broadband infrastructure. See Department of Communications, Energy and Natural Resources, *Delivering a Connected Society*, August 2012

5. Transport Costs

5.1 Summary

As noted in Chapter 2, transport costs are a greater concern for the manufacturing sector (who need to move large quantities of goods in and out of the country – both as inputs and as finished outputs) than service based sectors. The indicators in this section focus primarily on the costs of moving freight, rather than the costs of passenger transport. However, we also review international air transport costs given their importance to services and manufacturing companies. See Chapter 9 for a broader assessment of costs including consumer costs.

Figure 5.1 examines fuel costs – a particularly vital input cost for the haulage sector and for firms that rely on them. The cost of 1,000 litres of diesel in Ireland (€1,561) was just above the average euro area 17 price in August 2012. On this basis, Ireland is the 4th most expensive country amongst the 17 euro area countries. The average price of petrol in Ireland was €1,647 per 1,000 litres, making Ireland the 9th most expensive in the euro area.

Figure 5.2 illustrates historic trends for both diesel and unleaded petrol prices in Ireland (including taxes). European Commission data shows that in August 2012 Government taxes and duties accounted for 56 per cent of final consumer petrol prices and 51 per cent of diesel prices.

The CSO's experimental services producer price index tracks the evolution in prices for a range of services⁸³. Figure 5.3 focuses on a range of transport and storage indicators⁸⁴. Since 2006, prices for the majority of these services (e.g. road freight, sea transport, warehousing) have remained stable or have fallen. The cost of air transport is the exception, with significant increases recorded, notably since 2010.

The World Bank's *Doing Business* report measures the administrative time and cost (excluding customs tariffs and duties or costs related to ocean transport) associated with exporting and importing a standardized cargo of goods by ocean transport.

- Figure 5.4 shows that it is more expensive to export a 20-foot container from Ireland (\$1,109) than the euro area 17 average (\$1,104). In terms of the time taken to complete the required procedures to export, Ireland (7 days) performs better than the euro area 17 average (10 days).
- It is also more expensive to import a 20-foot container into Ireland (\$1,121) than the euro area 17 average (\$1,066) (Figure 5.5). At 12 days, the time taken to complete all of the necessary import procedures also exceeds the euro area average (11 days).

The World Bank also produces export and import cost data which takes account of both administrative and shipping costs.

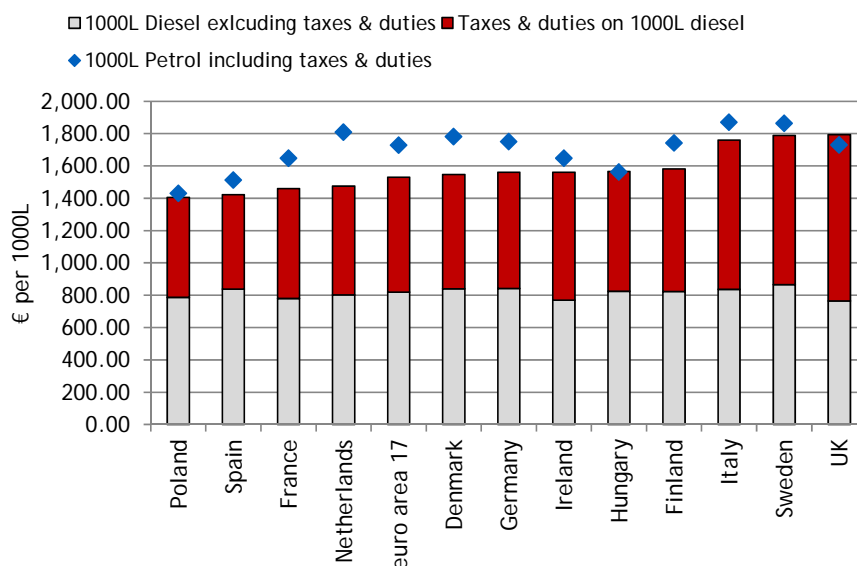
83 The Services Producer Price Index (SPPI) measures changes in the average prices charged by domestic service producers to other businesses for a selected range of services. In most cases these services are provided to business customers only and so individual price indices should not be considered indicative of more general price trends in the economy. The index covers transaction costs from business to business and excludes consumers who are covered in the Consumer Price Index (CPI).

84 Based on the Nace Rev 2 Classification, the following industries are included in (H) – Transportation & Storage: 49.4 Freight transport by road and removal services; 50.1/50.2 Sea and coastal transport; 51 Air transport; 52.1/52.24 Warehousing, storage and cargo handling; and 53.1/53.2 Postal and courier activities.

- As shown in Figure 5.6, because Ireland is a small country with the majority of exporters located close to ports and airports, the internal supply chain is short - and the cost of moving export goods internally as a result is the cheapest in the euro area. Ireland's island status, however, makes it more expensive to export when the distance to the customer is factored in. The cost of moving a 40 foot dry container from its origin to the buyer was the second most expensive in the euro area.
- Figure 5.7 assesses the administrative and shipping costs of importing. The cost of getting a 40 foot dry container from the port/airport of discharge (in this case Dublin) to the buyer's warehouse in Ireland was the joint cheapest in the euro area in 2012. Once again, the total cost of getting a 40 foot container from the seller's factory to the buyer was more expensive - reflecting our geographic location. Ireland was the second most expensive amongst euro area countries for which data was available.

5.2 Transport Cost Indicators

Figure 5.1 Average Diesel and Petrol Costs per Litre, August 2012



Some sectors are more sensitive to fluctuations in fuels costs than other sectors (e.g. the haulage industry). The cost of 1,000 litres of diesel in Ireland (€1,561) was just above the average euro area 17 price in August 2012. On this basis, Ireland is the 4th most expensive country amongst the 17 euro area countries. The average price of petrol in Ireland was €1,647 per 1,000 litres, making Ireland the 9th most expensive in the euro area.

Source: European Commission, Energy Statistics & Market Observatory

Figure 5.2 Average Diesel and Petrol Costs per Litre, Ireland, 2007-2012

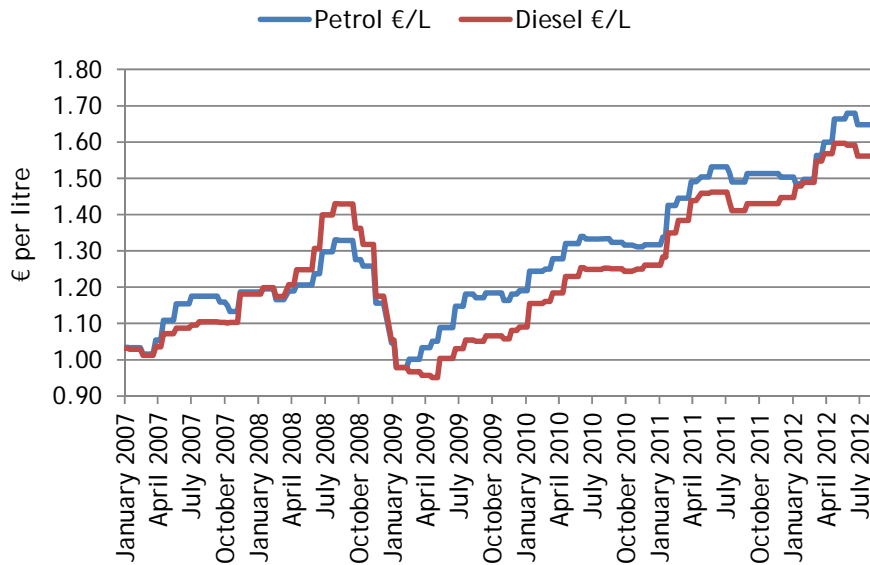
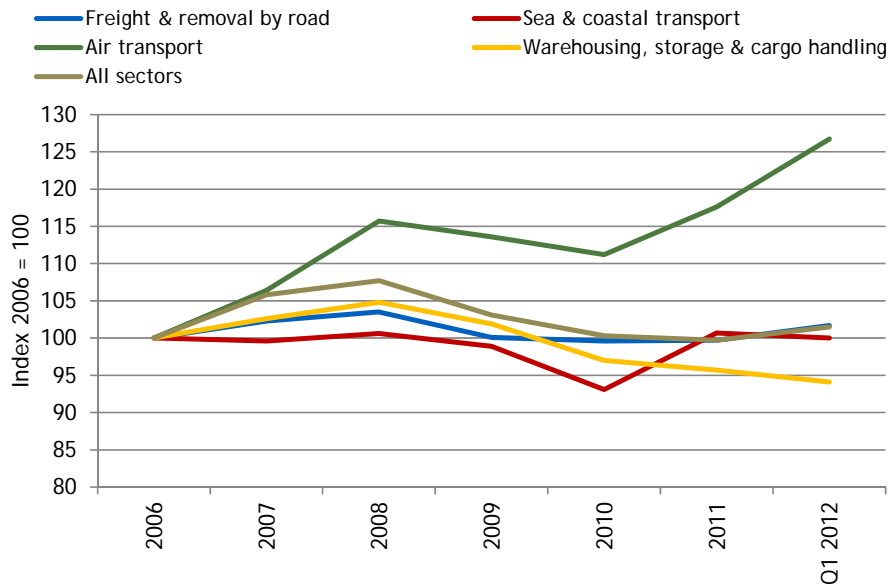


Figure 5.2 illustrates historic trends for both diesel and unleaded petrol prices in Ireland (including taxes and duties). As of August 2012, European Commission data suggests that Government taxes account for almost 56% of petrol prices and 51% of diesel prices, compared with EU averages of 55% and 48% respectively.

Source: European Commission, Energy Statistics & Market Observatory

Figure 5.3 Trends in Transport Related Prices in Ireland, 2006-Q1 2012

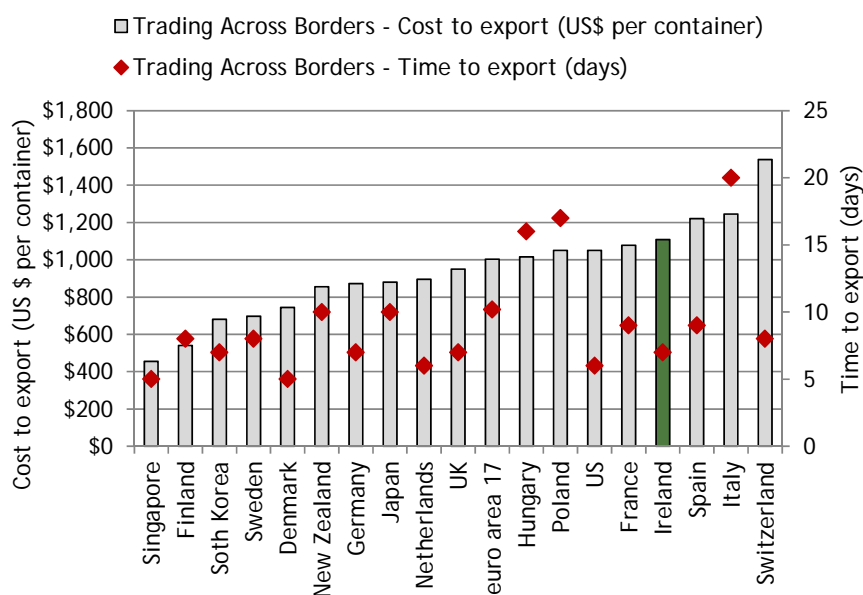


The CSO's experimental services producer price index tracks the evolution in prices for a range of services. This chart focuses on a range of transport and storage indicators. Since 2006, prices for the majority of these services have remained stable or have fallen. The cost of air transport is the exception, with significant increases recorded, notably since 2010⁸⁵.

Source: CSO, Services Producer Price Index

⁸⁵ Air transport data is based on data compiled from the CSO's Consumer Price Index.

Figure 5.4 Administrative Costs and Time to Export, 2012⁸⁶



It is more expensive to export a 20-foot container from Ireland (\$1,109) than the euro area 17 average (\$1,104)⁸⁷. This metric relates to the typical fees associated with completing the procedures to export and does not include customs tariffs and duties or costs related to ocean transport. In terms of the time taken to complete the required procedures to export, Ireland (7 days) performs better than the euro area 17 average (10 days).

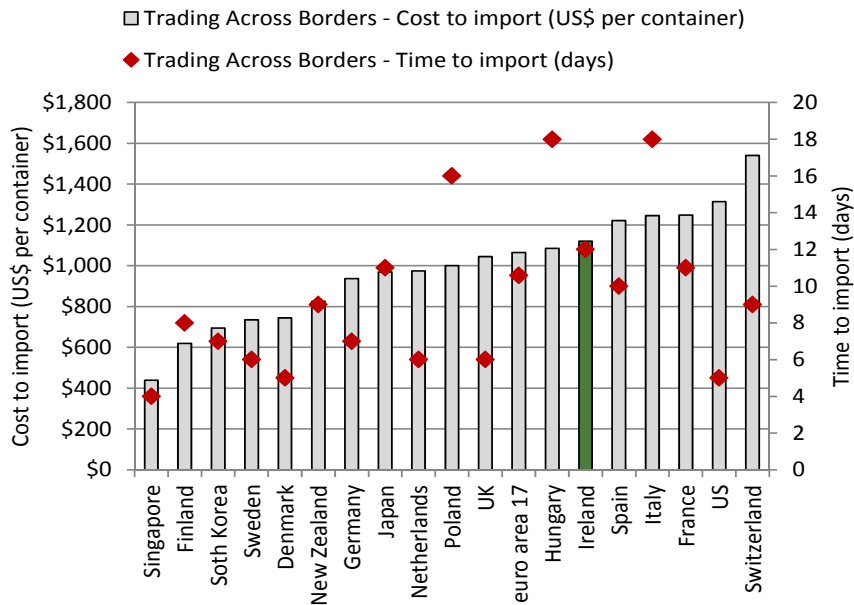
Source: World Bank, Doing Business 2012

86 The World Bank’s cost indicator shows the typical fees levied on a 20-foot container in U.S. dollars. All the fees associated with completing the procedures to export or import the goods are included. These include costs for documents; administrative fees for customs clearance and technical control; customs broker fees; terminal handling charges; and inland transport. The cost does not include customs tariffs and duties or costs related to ocean transport. Only official costs are recorded.

The time for exporting and importing is recorded in calendar days. The time calculation for a procedure starts from the moment it is initiated and runs until it is completed. If a procedure can be accelerated for an additional cost and is available to all trading companies, the fastest legal procedure is chosen. Fast-track procedures applying to firms located in an export processing zone are not taken into account because they are not available to all trading companies. Ocean transport time is not included.

87 The World Bank methodology assumes that the traded product travels in a dry-cargo, 20-foot, full container, weighing 10 tons and valued at \$20,000. It is further assumed that the product in question does not require refrigeration or any other special environment and does not require additional safety standards other than accepted international standards.

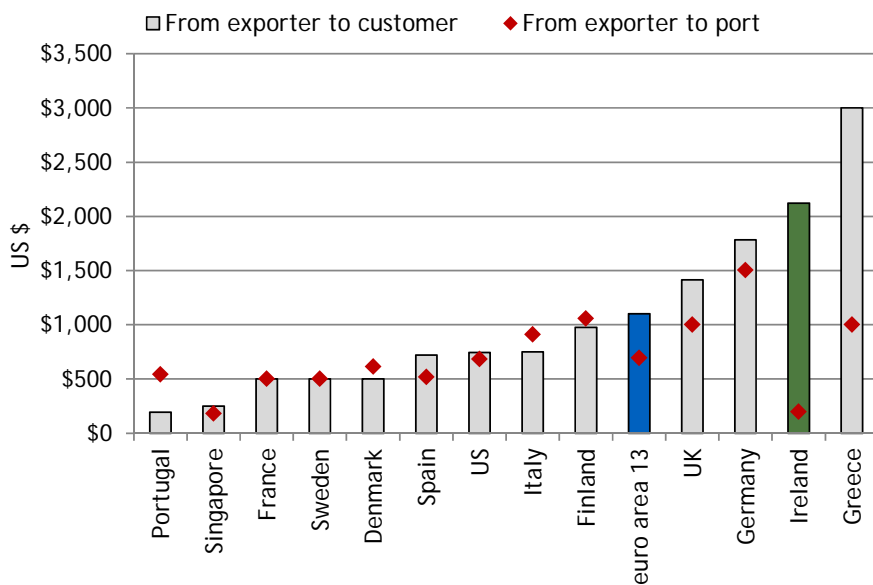
Figure 5.5: Administrative Costs and Time to Import, 2012



It is more expensive to comply with the required procedures to import a 20-foot container into Ireland (\$1,121) than the euro area 17 average (\$1,066). At 12 days, the time taken to complete all of the necessary import procedures also exceeds the euro area average (11 days).

Source: World Bank, Doing Business 2012

Figure 5.6 Cost of Exporting (administrative and some transport costs)⁸⁸, 2012

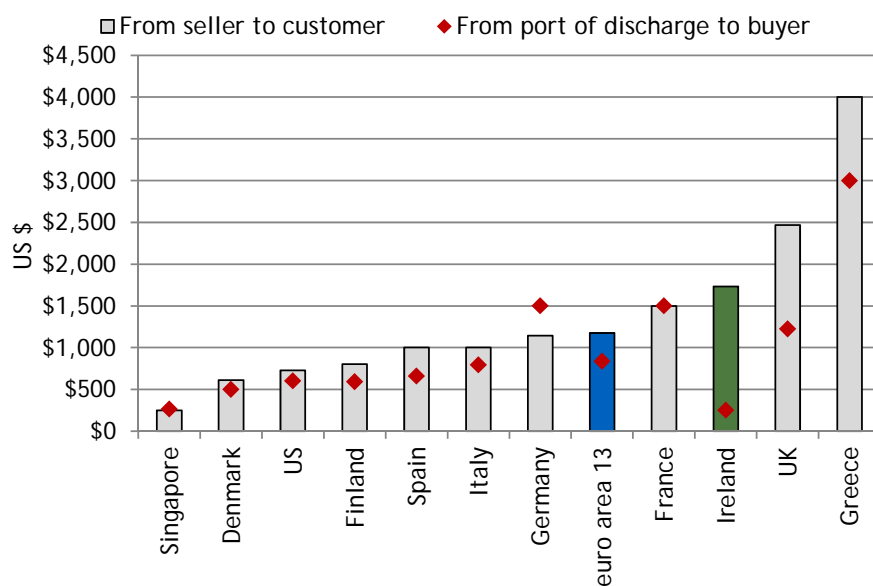


Because Ireland is a small country, the internal supply chain is short - and the cost of moving export goods internally as a result - are the cheapest in the euro area. Ireland's island status, however, makes it more expensive to export when the total distance to the customer is factored in. The cost of moving a 40 foot dry container from its origin to the buyer was the second most expensive in the euro area.

Source: World Bank, Logistics Performance Index

⁸⁸ The costs shown for 'exporter to port' reflect typical charges for a 40-foot dry container or a semi-trailer (total freight including agent fees, port, airport, and other charges). The costs reflect the cost from the point of origin (the seller's factory, typically located either in the capital city or in the largest commercial centre) to the port of loading or equivalent (port/airport), and excluding international shipping. The costs shown for 'exporter to customer' (i.e. the land supply chain) reflect the typical charge for a 40-foot dry container or a semi-trailer (total freight including agent fees and other charges). Euro area 13 is euro area 16 minus Austria, Luxembourg, and Slovenia.

Figure 5.7 Cost of Importing, 2012



The cost of getting a 40 foot dry container from the port/airport of discharge to the buyer’s warehouse in Ireland was the joint cheapest in the euro area in 2012, again reflecting the relatively short distances to be travelled. The total cost of getting a 40 foot container from the sellers factory to the buyer, however, was more expensive - Ireland was the second most expensive amongst euro area countries for which data was available.

Source: World Bank, Logistics Performance Index

5.3 Policy Focus on Transport Costs

5.3.1 Reducing Exporting Costs

Ensuring that goods and services can be exported in a cost competitive manner is critical to indigenous exports, both manufacturing and internationally traded services. As part of the Action Plan for Jobs 2012 (Action 1.29), Forfás has been tasked with reviewing the costs of exporting for Irish firms and to develop an action plan to address these costs. The analysis below builds upon the preliminary analysis conducted for this study.

Specific Costs Identified

Transport costs are the most significant export cost for firms in the food, manufacturing and engineering sectors. Ireland operates at a significant cost disadvantage in relation to all freight transport modes compared to firms located in UK or Continental Europe. Table 2 provides an overview of the cost differential in transport costs, while Table 3 summarises a range of possible factors, which may explain why Irish transport costs are higher than UK or Continental costs for all three categories of transportation.

Table 2: Summary of Cost Differentials between Ireland and the UK/Europe for Shipping⁸⁹

Road Freight	Sea Freight	Air Freight
Typical journey to the continent is circa 50% cheaper for a UK exporter and circa 80% cheaper for a continental exporter than an Irish exporter.	For firms based in both the UK and Belgium, it is almost 20% cheaper to ship a 40ft container to New York and around 30% cheaper to Shanghai or Hong Kong than to ship from Ireland.	The cost is at least 10% less from the UK or continental Europe to global business destinations (such as New York, Hong Kong and Shanghai) when compared to Ireland.

Table 3: Possible Factors Resulting in Relatively Higher Irish Transportation Costs

Road Freight	Sea Freight	Air Freight
Ireland is further from export markets than firms located in UK and Continental Europe.	Many containers from Ireland must first travel to Rotterdam to connect with worldwide sea freight routes. This adds to the cost of the total journey.	There is a wider selection of direct flights at lower cost to key business destinations from UK and Continental Europe, mainly because the volume of freight traffic justifies the service.
Ireland has higher vehicle operating costs compared to UK and Continental Europe.	Reduced competition on Irish Sea routes resulting in higher sea freight costs.	
The opportunity for backloads to Ireland is more limited than backloads to the UK or within Continental Europe.	A shortage of containers on Irish Sea routes.	
Diesel costs are higher in Ireland than in some parts of Continental Europe e.g. Spain, Germany, although not the UK. ⁹⁰		

Fuel Taxes

As the international price of oil increases, this exerts pressure on the price of fuels in Ireland. As illustrated in Figures 5.1 and 5.2, a large proportion of retail fuel prices are accounted for by taxes. As a result, pressures have grown to reduce fuel taxes in order to moderate international prices increases. While reducing taxes could provide temporary relief, such a move would have a number of negative long term impacts:

⁸⁹ More detailed benchmarking data will be available in Q4 2012 when Action 1.29 from the Action Plan for Jobs 2012 (Analyse the Costs Associated with Exporting and set out an Action Plan to reduce these Costs) is completed.

⁹⁰ Increases in fuel prices were found to not commensurately increase the total journey costs due to other costs such as ferry prices and running costs. A 10 per cent increase in fuel was found to increase total road transport journey costs by 2.3 per cent.

- It would reduce State revenues - requiring revenues to be raised elsewhere - potentially through other taxes which may have a more distortionary effect on enterprise development (e.g. labour taxes).
- It would make State revenues from fuel taxes more uncertain as they would be dependent on international fuel price developments. It would also make tax policy more uncertain.
- It would blunt market signals which incentivise the efficient use of scarce resources and the development of alternative fuel sources.

Carbon taxes on certain fossil fuels (excluding peat, coal or agricultural fuels) were introduced in Budget 2010. Budget 2012 increased the carbon tax from the equivalent of €15 per tonne to €20 per tonne. The primary impact of the carbon tax is on the household sector, but it also has direct (increased fuel costs⁹¹) and indirect (use of third party transport providers⁹²) costs for enterprise. The Commission on Taxation recommended that the carbon tax should be based on a standardised measure of CO₂ content of the energy product, and that in general there should not be preferential rates of carbon tax. Broadening the tax base would be preferable to increasing rates further.

Recommendation: The carbon tax should be based on a standardised measure of CO₂ content of the energy product. A broad tax base is preferable to a higher rate which includes preferable, differentiated rates for designated fuels⁹³.

Responsibility: Department of Finance

Finally, in the UK the Office of Fair Trading (OFT) is currently looking into concerns raised about unfair competition at petrol stations. This investigation follows similar ones in both Spain and Germany, both of which found evidence of a lack of competition⁹⁴. There is merit in the Competition Authority reviewing the outcome of this investigation, which is due to be completed in January 2013, to see if the OFT's findings have any relevance for Ireland.

Recommendation: The Competition Authority should review the outcome of the UK's Office of Fair Trading investigation into unfair competition at petrol stations, which is due to be

91 Increases in gas prices for non-exempted industrial consumers of €0.85 per gigajoule of gas in 2014

92 Indirectly, the enterprise sector will face additional costs, particularly through increases in the cost of road freight of €25 million in 2012, €25 million in 2013 and €37 million in 2014.

93 A recent report from the IMF found that "the level of the domestic carbon tax for emissions outside of the EU cap-and-trade system seems reasonable, but the current price for ETS emissions is only about a third of this level. A possible reform (to equalize emissions prices across the economy) would be to bring ETS emissions under the carbon tax, and provide refunds to covered sources for ETS allowance purchases. See International Monetary Fund, IMF Country Report No. 12265, Ireland: Selected Issues, September 2012.

94 The OFT will explore a number of claims about how the road fuels sector in the UK is functioning, including: whether reductions in the price of crude oil are being reflected in falling pump prices; whether supermarkets' and major oil companies' practices may be making it more difficult for independent retailers to compete with them; whether there is a lack of competition between fuel retailers in some remote communities in the UK; and whether concerns about price co-ordination and the structure of road fuels markets identified by other national competition authorities are relevant in the UK. For further information see <http://www.offt.gov.uk/OFTwork/markets-work/othermarketswork/road-fuel-CFI/#named2>

completed in January 2013, in order to see if the OFT's findings have any relevance for Ireland.

Responsibility: Competition Authority

5.3.2 Investment in Critical Transport Infrastructure

Access to markets is one of the key factors for companies in deciding where to locate. An efficient and integrated national transport system with adequate capacity, and with levels of service comparable to other countries with which we compete for investment and trade, plays an essential role in Ireland's ability to compete successfully in international markets. Good transport infrastructure is also essential to supporting labour mobility.

For exporters and importers, good quality international air and sea access coupled with effective internal connectivity is a key factor in mitigating the impact of Ireland's peripheral location in the eyes of potential investors and overseas customers. The key issue for enterprise is ensuring that we have good international access by air and sea in terms of locations served, frequency and costs⁹⁵.

Given the limited capital resources available in the short to medium term, it is critical that Ireland prioritises investment that will support economic recovery and sustainable growth. The following sections summarise the key infrastructural investments required to support Irish enterprise. These investments are broken out into domestic, sea and air transport requirements⁹⁶.

Domestic Transport Infrastructure

In terms of domestic transport infrastructure, Forfás has identified a range of priority road and rail projects⁹⁷:

- The completion of the Cork and Galway ring roads and two sections of the Atlantic Corridor (Gort - Tuam and Croom - Mallow) which will improve mobility of people and goods in and between Ireland's main regional cities. They would also improve access to Cork and Shannon airports and Shannon - Foynes and Cork ports for the south west, mid-west and west regions;
- Other enterprise road priorities include the N28 Cork to Ringaskiddy upgrade and the N22 Macroom/Ballyvourney by-pass.
- Completing the Atlantic corridor from Galway to Waterford remains an important medium term priority to support sustained economic growth and job creation.
- Improving public transport in the key urban centres is critical to improve mobility for all transport users. A selective continued investment in the options (as between bus and rail) with the highest economic and social returns, based on a full cost benefit analysis, to improve public transport in the key urban centres is required.

95 For instance, the development of new direct air links with key existing markets (e.g. the US West Coast), and high growth markets (e.g. India and China), as well as maintaining air links with key European markets is critical to support export growth and job creation.

96 While air and sea access infrastructure is generally not funded directly from public capital expenditure budgets, public policy has a key role to play in ensuring that the private sector (i.e. commercial semi-states and others) invests in a timely manner to ensure the current and future needs of enterprise are met.

97 For a detailed discussion on infrastructure priorities see Forfás, Overview of the Main Infrastructure Issues for Enterprise, May 2012.

- Reform of the regulatory framework for public transport, particularly in urban bus services, to promote competition for routes and ensure quality services in terms of routes served and frequency of service is required.
- Greater clarity is needed on Ireland's rail freight policy objectives, including rail freight's role as part of an integrated transport system across all modes of transport.

Reducing Sea Transport Costs

As an island nation, we are hugely dependent on ports and shipping to transport goods to and from the country. Approximately 99 per cent of Irish merchandise exports and imports (by weight) are transported by sea which highlights the economic significance of Irish ports. Ports play a vital role in the exporting of goods produced in Ireland and as such represent a key cost and infrastructure for our exporting companies⁹⁸. If port services are inefficient, the cost of using them will be higher than it would otherwise be.

Recommendation: The review of ports policy from the Department of Transport is of paramount importance. In particular, the strategy which emerges from this review must (i) ensure that Irish ports are market focused; (ii) encourage and facilitate investment; and (iii) promote competition⁹⁹.

Responsibility: Department of Transport

The increasing international shipping trend toward larger vessels has clear potential to impact on the ability of Irish ports to continue to offer the current range and frequency of services unless adequate deeper water facilities are provided. If deeper water facilities are not provided in the medium term, this will lead to a reduction in the number of routes and services to and from ports on the island of Ireland, and an increase in costs because of the reduced capacity. A number of Irish ports, including Dublin, do have the potential to provide deeper water services.

Recommendation: In the long term, we need to develop deep water facilities at Irish ports to accommodate the international trend toward larger shipping vessels and ensure that Irish importers and exporters continue to have access to a wide range and frequency of port services at competitive prices. Consideration should also be given to creating the regulatory environment to develop Ireland's potential as an entrepot port (e.g. setting out a clear framework ensuring port companies are autonomous and commercial companies).

Responsibility: Department of Transport

98 There are approximately 21 ports in the Republic of Ireland. Ten of these are operated as a self-financing, State-owned limited liability port companies (Drogheda, Dublin, Dundalk, Dun Laoghaire, Galway, New Ross, Cork, Waterford, Shannon Foynes, and Wicklow). Rosslare Europort is operated by the State-owned company Iarnród Éireann, while Greenore in Co. Louth is the only fully privately owned port in the Republic. The remaining smaller ports are run by Local Authorities.

99 The Minister for Jobs, Enterprise and Innovation has requested that the Competition Authority carry out a study of the ports sector in Ireland. Amongst the objectives of the study, the Competition Authority has been tasked with examining: the level of competition between ports in the State and the effect of specialisation; the impact of competition from ports in Northern Ireland; how competition works within the State's major ports; the impact of competition of developments in other transport modes in Ireland and developments in shipping internationally; and the likely impact of changes in port ownership and structures.

Reducing Air Transport Costs

As noted earlier, air transport costs in Ireland have increased significantly over recent years. While much of this increase has arisen as a result of the increase in international fuel prices, opportunity exists to address cost factors arising elsewhere¹⁰⁰.

Ireland's aviation policy supports the liberalisation of international aviation markets to the fullest extent possible. A key component of this policy is to pursue the conclusion of liberal air transport agreements, at both the national and EU levels, to remove regulatory impediments to the inauguration of new air services and to improve connectivity and services and to ensure competitive pricing.

Driven by the recession, the number of flights in and out of Ireland has fallen in recent years. Convery has noted that the two airlines now dominate Europe-based traffic into and out of Ireland¹⁰¹. They account for over 80 per cent of traffic out of Dublin. In addition, he notes that on 24th July 2012, out of 66 routes operated by Aer Lingus from Dublin, 31 are also contested by Ryanair; the average price for a contested flight is €125.75, compared to €145.76 for an uncontested flight. Ryanair is currently endeavouring to buy Aer Lingus outright. The European Commission opened an in-depth investigation into proposed acquisition. The Commission's initial assessment indicates 'potential competition concerns'. The Commission will now investigate the proposed merger in greater depth to determine whether these initial concerns are confirmed or not. From an enterprise development perspective, it is essential that privatisation policy protects and promotes competition in the market, ensures that investment and regional development is promoted and that regulatory capabilities are sufficiently advanced to achieve public policy goals.

Recommendation: It is essential that we maintain competition in the airline market. Should the State share of Aer Lingus be sold, maintaining and developing competition, and expanding the network of routes should be a key criterion in the sale process.

Responsibility: Department of Transport / Department of Finance

100 The regulatory aspects of air travel are being addressed in a separate Forfás study under Action 1.31 of the Action Plan for Jobs 2012.

101 Convery, F., Airline Competition in Ireland – Back To Monopoly?, July 10, 2012, Publicpolicy.ie.

6. Utility Costs

6.1 Summary

This section focuses on a range of utility costs - notably energy, environmental services (waste and water) and communication costs.

Energy costs are a particularly important cost factor for some manufacturing sectors such as chemicals and agri-food. Figure 6.1 shows that electricity costs for large energy users in Ireland are the 7th highest amongst the euro area 15 countries. Electricity costs for SMEs in Ireland are now amongst the highest in the euro area - 4th most expensive in the euro area behind prices in Cyprus, Malta and Italy (Figure 6.2).

Gas also provides a substantial proportion of the energy needs of enterprise. In 2011, Ireland had the sixth highest industrial gas prices (€10.96 per gigajoule) although Irish prices are 3 per cent below the euro area average (€11.33).

Moving onto the indicators measuring the cost of environmental utilities (i.e. waste and water services), Figure 6.4 examines the price paid by enterprise for water. The data examines water costs for industrial users but does not include the cost of waste water services. While Ireland is the 6th most expensive location from 15 countries benchmarked, the cost of water for industrial users in Ireland remained relatively static since 2007. In 2010, the average cost of water per meter cubed for industrial users in Ireland was €1.14. Figure 6.5 displays water cost data for Ireland by Local Authority region. There is considerable variation in costs across the country.

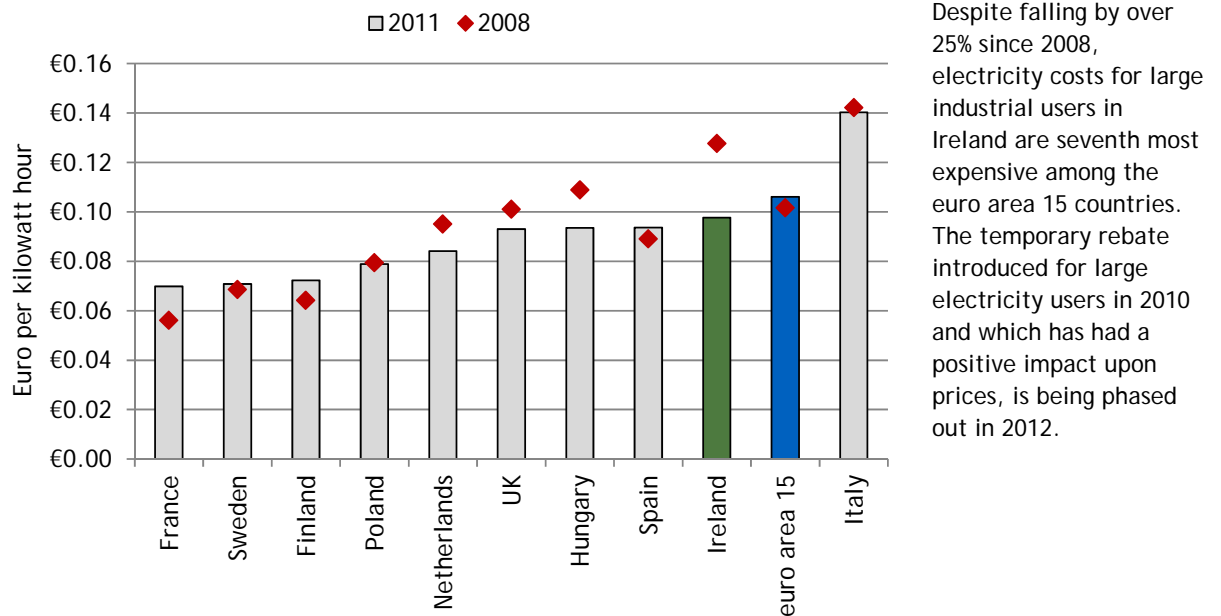
Figure 6.6 looks at the cost of landfill. In 2012, the average market rate for non-hazardous landfill was €35-45 per tonne (excluding the levy) compared to €112 in 2010. However, the landfill levy in Ireland has increased significantly in recent years, from €30 in 2010 to €65 in July 2012. Further increases in the levy are planned - from €65 to €75 per tonne from July 2013. Of the benchmarked countries, Ireland had the fifth highest landfill costs (including levies) in 2012. Figure 6.7 presents data on the average cost of thermal treatment for non-hazardous industrial waste. Ireland had the third highest non-hazardous thermal treatment gate fees (including levies) in 2012.

Finally, looking at range of communications cost indicators, Figure 6.8 measures the average broadband monthly price per advertised megabit for each country. The average price in Ireland is US\$ 3.88 per advertised megabit which is 7 per cent higher than the OECD average. Of the benchmarked countries Ireland is the third most expensive. Figure 6.9 shows the fastest download speed available to business, the accompanying upload speed provided and the annual cost per package (excluding VAT). In Ireland, the cost of the fastest broadband connection available to business was the second highest among countries benchmarked, while the corresponding download speed with this connection was the 6th highest.

The final three indicators examine the cost of various baskets of telephone calls. Figure 6.10 measures the cost of a business basket of 260 calls excluding VAT in February 2012. Ireland is the third cheapest location in the euro area for a business basket of calls. When international call are included (Figure 6.11), Ireland slips down the rankings slightly to become the fourth cheapest location. Finally, Figure 6.12 looks at the cost of mobile calls. The monthly cost of a high usage mobile package (300 calls) in Ireland was seventh highest among the euro area countries benchmarked and above the euro area average in 2012.

6.2 Energy Cost Indicators

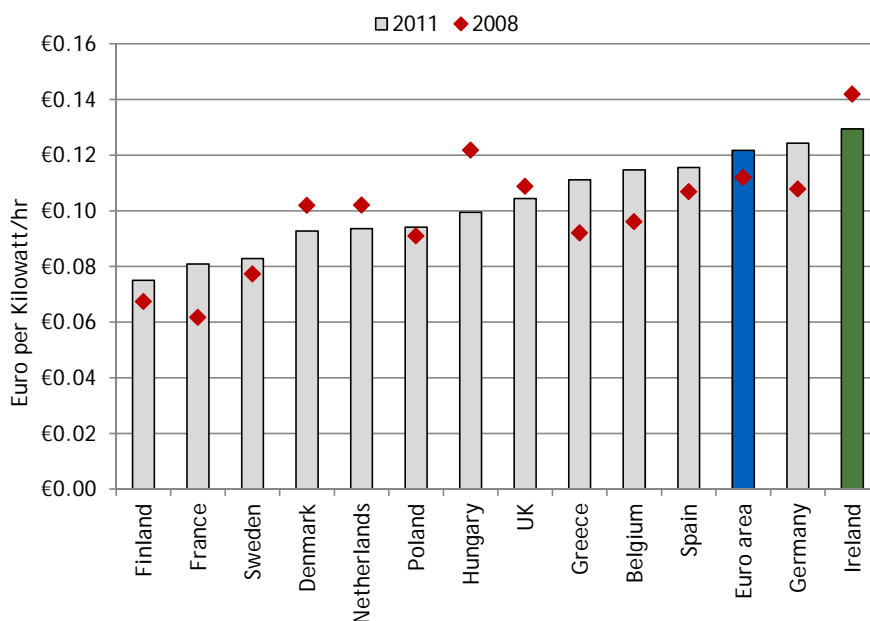
Figure 6.1: Industrial Electricity Prices for Large Energy Users (excluding VAT), 2011¹⁰²



Source: Eurostat - Environment and Energy

¹⁰² Electricity prices for large users are based on an annual consumption of 2,000 to 20,000 MWh. Data refer to half-yearly prices for H2 each year. Euro area 15 excludes Luxembourg for H2 2008, and excludes Austria for H2 2011.

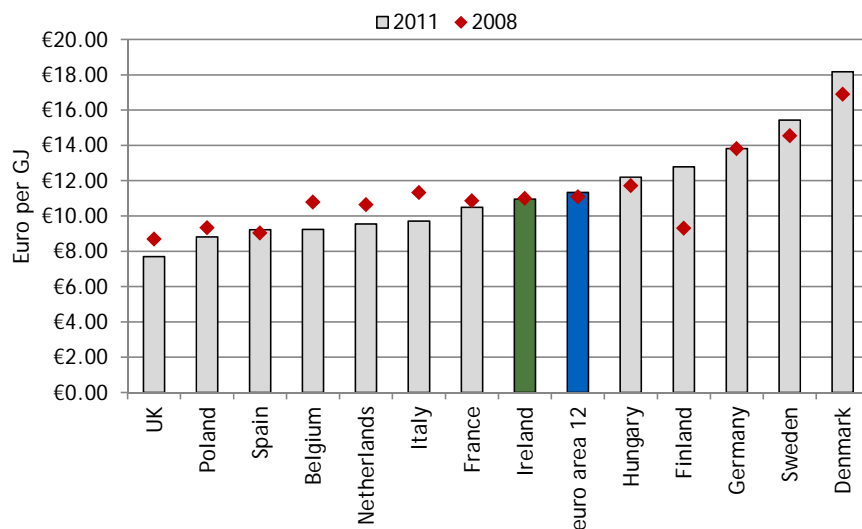
Figure 6.2: Industrial Electricity Prices for SMEs (excluding VAT), 2011¹⁰³



Electricity costs for SMEs in Ireland rose by 14 per cent between 2010 and 2011, eroding some of the competitiveness gains achieved since 2009. Electricity costs for SMEs in Ireland are the 4th most expensive in the euro area behind prices in Cyprus, Malta and Italy.

Source: Eurostat - Environment and Energy

Figure 6.3: Industrial Gas Prices (excluding VAT), 2011¹⁰⁴



Between 2008 and 2009 the cost of industrial gas fell significantly across most benchmarked locations, reflecting the decline in international gas prices. Since then however there has been an increase in world prices. In 2011 Ireland had the sixth highest industrial gas prices (€10.96 per gigajoule). Irish prices are 3 per cent below the euro area average of €11.33.

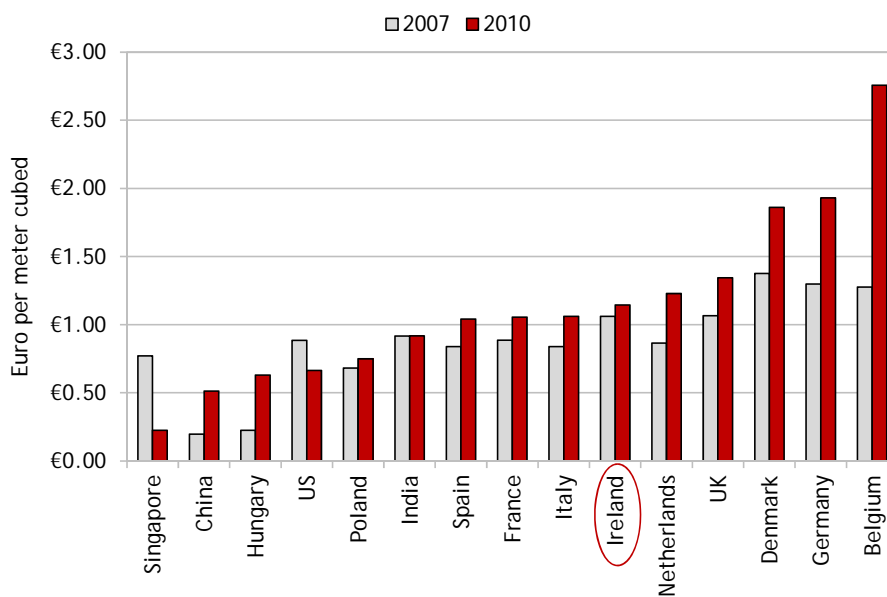
Source: Eurostat - Environment and Energy

103 Electricity prices for SMEs are based on an annual consumption of 500 to 2,000 MWh. Data refer to half-yearly prices for H2 each year. Euro area 15 excludes Italy in H2 2008 and Austria in H2 2011.

104 Based on band I3: 10 000 GJ < Consumption < 100 000 GJ.

6.3 Environmental Utility Cost Indicators

Figure 6.4 Water Costs, 2010¹⁰⁵



This chart examines water costs for industrial users but does not include the cost of waste water services. While Ireland is the 6th most expensive location, the cost of water for industrial users in Ireland remained relatively static since 2007. In 2010, the average cost of water per meter cubed for industrial users in Ireland was €1.14.

Source: EIU World Investment Service, D/Environment, Community and Local Government

Figure 6.5 Water Costs in Ireland by Local Authority, 2010

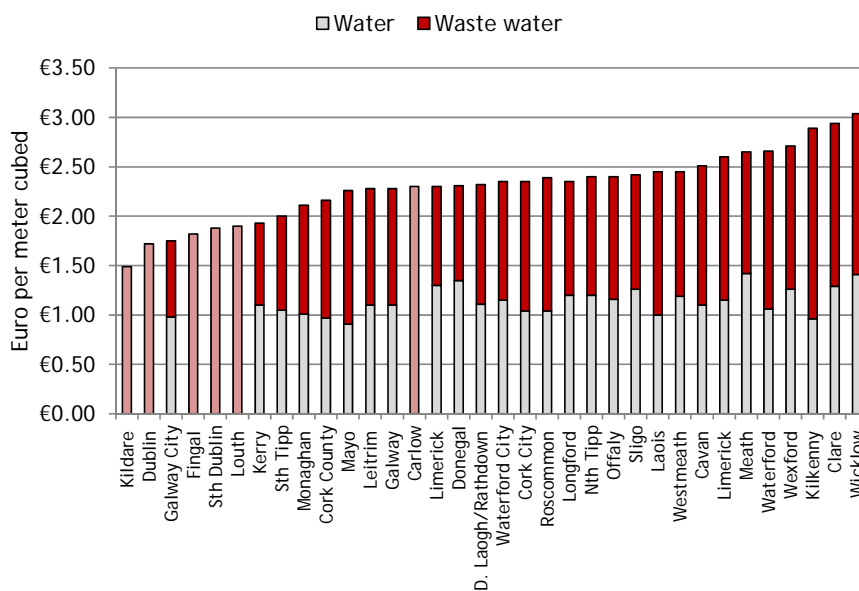
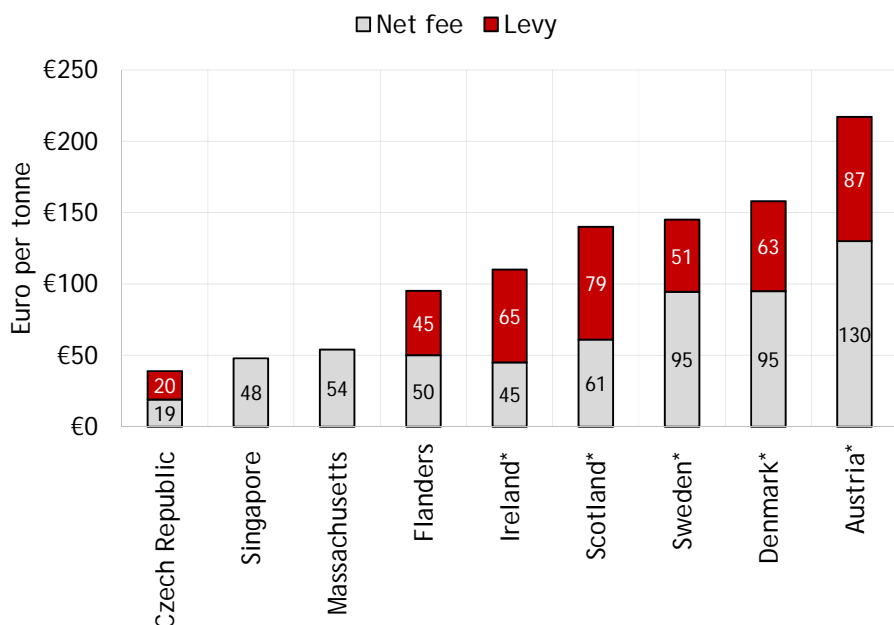


Figure 6.5 displays water cost data for Ireland by Local Authority region. Data is broken out according to water and waste water charges. In the case of a number of local authorities (Kildare, Dublin City, Fingal, South Dublin, Louth and Carlow) only consolidated cost data was available. It is noticeable that there are significant variations in charges across the country.

Source: Local Authority Budgets 2011

¹⁰⁵ Economist Intelligence Unit data on water contains a consolidated figure for both water and waste water costs. For methodological reasons, Irish data sourced from the Department of the Environment for 2007, and from the Office for Local Authority Management for 2010, has been substituted for EIU data. The average cost of waste water services (not included in figure 4.37) in Ireland in 2010 was €1.24 in 2010, bringing the average consolidated water services charge per metre cubed to €2.37.

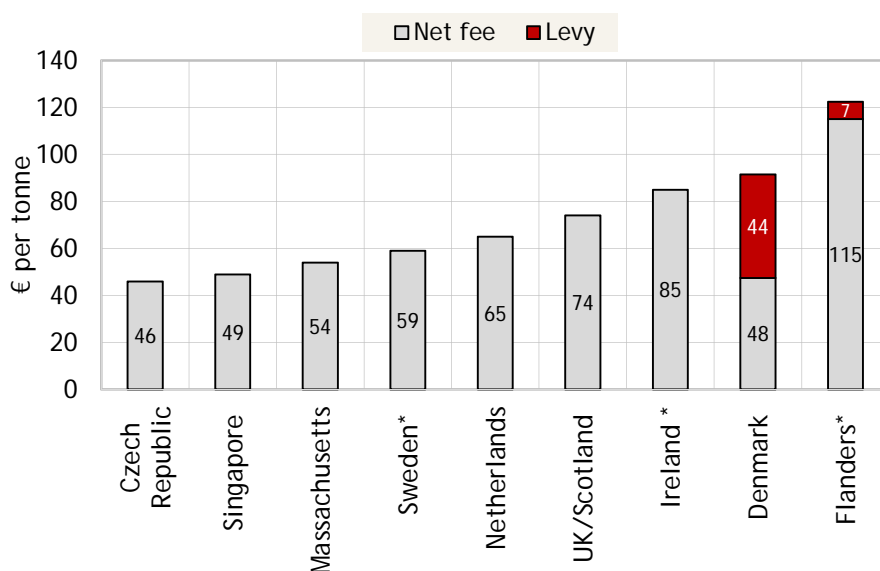
Figure 6.6: Landfill Gate Fees (incl. levy) for Non-hazardous Waste (€ per tonne), 2012¹⁰⁶



Since 2010, Irish landfill gate fees have fallen sharply. In 2012, the average market rate for non-hazardous landfill was €35-45 per tonne (excluding the levy) compared to €112 in 2010. The landfill levy in Ireland has increased significantly in recent years, from €30 in 2010 to €65 in July 2012. Of the benchmarked countries, Ireland had the fifth highest landfill costs (including levies) in 2012.

Source: Forfás Calculations, 2012

Figure 6.7: Non Hazardous Thermal Treatment Gate Fees (incl. Levy) in € per tonne, 2011/2012¹⁰⁷



Ireland had the third highest non-hazardous thermal treatment gate fees (including levies) in 2012. Gate fees differ in some countries for the biological treatment of food and green waste). In Ireland in 2012, gate fees for the biological treatment of food waste were €76 per tonne compared to €15.60 per tonne in Flanders and €50 per tonne in the Netherlands. Irish gate fees for green waste were €31 per tonne in 2012.

Source: Forfás Calculations, 2012

106 In countries marked with *, a range of landfill fees exist. The upper limit is used in Figure 6.6. Net landfill fees in Ireland ranged from €35-45 per tonne and from €60-€130 in Sweden. The landfill levy in Flanders differs depending on whether it's private or public landfill - the public landfill levy is used. The private landfill levy is €32 per tonne.

107 In countries marked with *, there is a range of thermal treatment fees. The upper limit is used in Figure 6.7.

6.4 Communications Cost Indicators

Figure 6.8: Average Price of Mbit per Second, US\$ PPP, September 2011

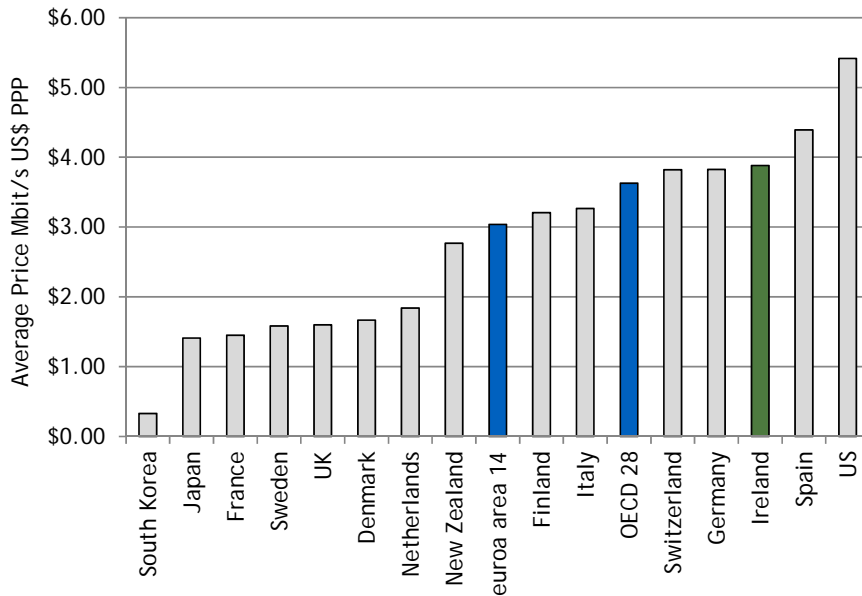
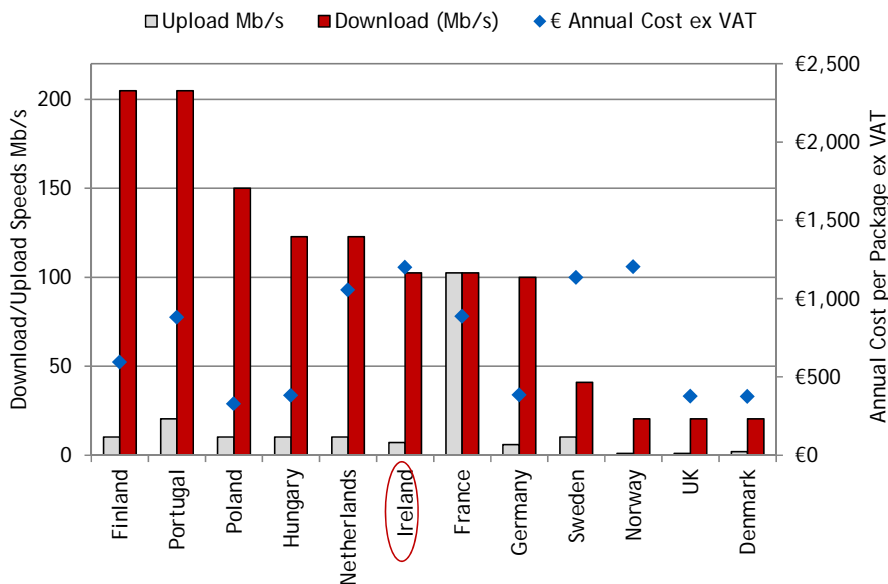


Figure 6.8 measures the average broadband monthly price per advertised megabit for each country. The average price in Ireland is US\$3.88 which is 7% higher than the OECD average and 27% higher than the euro area-14 average¹⁰⁸. Of the benchmarked countries Ireland is the third most expensive.

Source: OECD Broadband Statistics, March 2012

Figure 6.9: Fastest Advertised Broadband Connection¹⁰⁹ and Annual Cost (excluding VAT), 2012



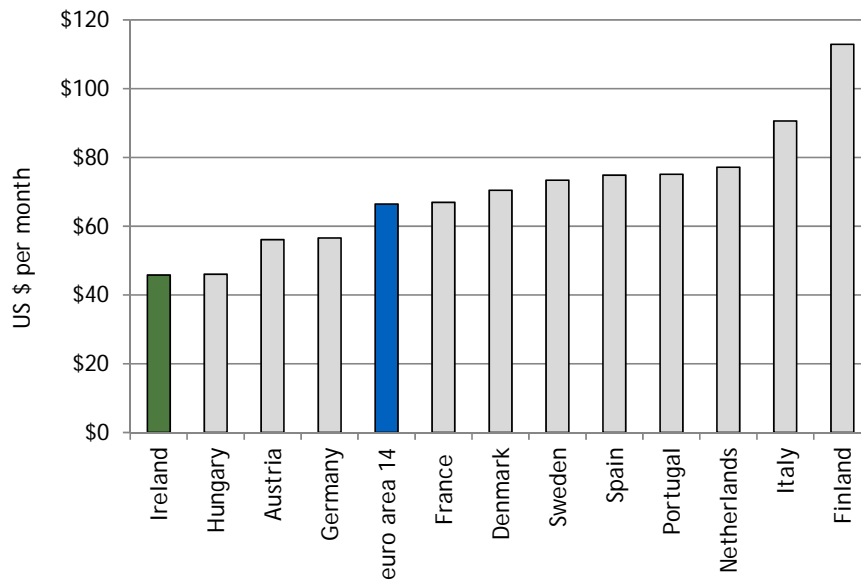
This indicator shows the fastest download speed available to business, the accompanying upload speed provided and the annual cost per package (excluding VAT). The cost of the fastest broadband connection available to business in Ireland was the second highest among countries benchmarked, while the corresponding download speed with this connection was the 6th highest.

Source: Teligen

108 Euro area 14 excludes Cyprus, Greece and Malta.

109 This data reflects advertised business connections only. They do not take into account connections which may be provided to business arising from direct negotiations with service providers.

Figure 6.10: Business Basket of Calls (260 calls excluding VAT), US\$, 2012¹¹⁰



This indicator measures the cost of a business basket of calls excluding VAT in February 2012. According to this metric Ireland is the third cheapest location in the euro area for a business basket of calls.

Source: Teligen

Figure 6.11: Business Basket of Calls including International Calls (260 calls excluding VAT), US \$, 2012¹¹¹

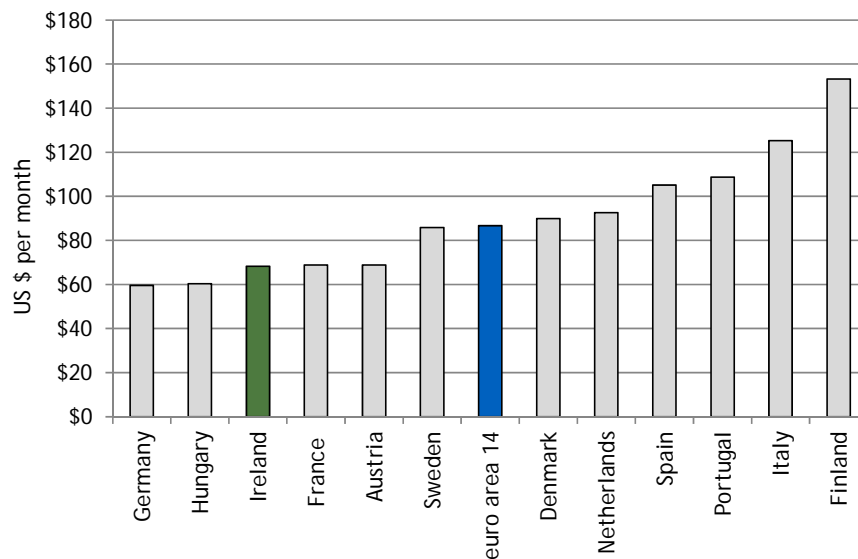


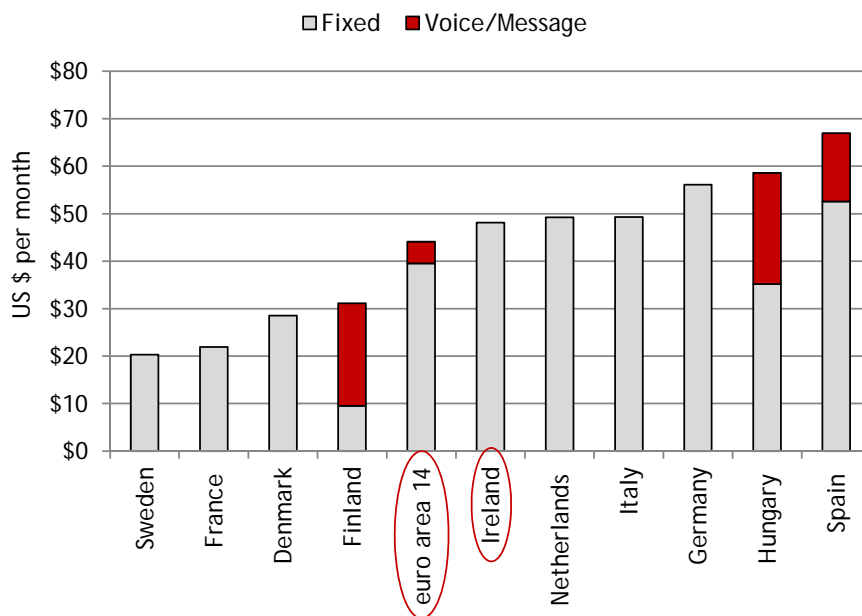
Figure 6.11 measures the cost of a business basket of calls, including international calls in February 2012. When the international element is included, Ireland slips down the rankings slightly to become the fourth cheapest location in the euro area for business calls.

Source: Teligen

110 Euro area 14 is the euro area 16 minus Cyprus and Malta. To allow for comparability with figure 6.10 countries, this figure does not contain the international element of the PSTN basket.

111 Euro area 14 excludes Cyprus, Estonia and Malta.

Figure 6.12: Monthly Mobile Telephone Costs, High Usage Post Paid Basket (300 calls¹¹² excluding VAT), US \$, 2012



The monthly cost of a high usage mobile package (300 calls) in Ireland was seventh highest among the euro area countries benchmarked and above the euro area average in 2012. Mobile voice traffic accounted for 63 per cent of total voice minutes in the first quarter of 2012¹¹³.

Source: Teligen

6.5 Focus on Regulation of Utilities

Regulation by or on behalf of the State plays an essential role in ensuring that economic activity by individual economic actors is consistent with wider national policy objectives, including consumer protection, environmental quality, provision of essential services, competition and health and safety. Whether expressed through primary or secondary legislation, or through the activities and determinations of sectoral regulators, regulation is the means by which society's priorities can be safeguarded in the operation of economic markets.

A range of utilities are already regulated to some degree by the State - others are due to be regulated in the near future. As a result, the State can to a degree affect the cost of the delivery of these business services. In order to enhance cost competitiveness, under action 1.31 in the Action Plan for Jobs 2012, Forfás has undertaken a study to:

- Identify the regulated sectors that are important input costs for enterprise;
- Benchmark the relevant Irish costs vis-à-vis our key competitors and suitable comparator countries;
- Assess the drivers of costs (including the role of sectoral regulation) in the benchmarked sectors, particularly in cases where Irish costs have been found to be out of line with competitor norms;

¹¹² The basket also includes 225 SMS per month. Euro area 14 excludes Cyprus, Estonia and Malta.

¹¹³ ComReg, Quarterly Data Report, Q1 2012

- Examine the functions and structures of the sectoral regulators and their impact on cost competitiveness; and
- Develop recommendations to improve sectoral cost competitiveness.

There are a number of areas where reforms to the manner in which the regulators operate could deliver improvements in Ireland's cost competitiveness. For example:

- Mandates - it is worth considering whether attaching greater importance to consumer interests (both business and individuals) and/or competitiveness would have a positive impact upon price.
- Efficiency - consider whether the regulators are optimally empowered to drive efficiencies in the utilities and services they are regulating.
- Benchmarking can play a key role in driving efficiencies - in particular, international benchmarks relating to key metrics such as prices, quality (as assessed by customer), and environmental performance would lead to more informed decision making.
- Transparency - it is important that regulators are seen to operate in a transparent manner at all times and that decisions are reached in a manner free from inappropriate external influence.
- Enforcement - ensure that the regulators are equipped with appropriate tools to pursue their objectives.
- Consultation - enhanced levels of consultation prior to decisions being made - to improve all parties understanding of the issues, particularly business and domestic users.
- Appeals - reform of the appeals process in relation to decisions by the regulator - to reduce time delays which add to uncertainty and increase capital costs.

6.6 Energy Policy

A reliable and competitively priced supply of energy is vital for business and its ability to compete successfully in international markets. From a national competitiveness perspective, the challenge facing Ireland is to reduce energy costs while delivering on our security of supply and environmental sustainability objectives. While the previous section dealt with the regulation of various utilities - including energy - this section considers those aspects of energy pricing that can be influenced through domestic policy. Many of these issues have been considered in detail previously in Forfás and National Competitiveness Council papers.

The EU-IMF Programme for Financial Support for Ireland required an assessment of the efficiency of the Irish electricity and gas markets, which was completed by the International Energy Agency (IEA) as part of its recent review of Irish energy policy¹¹⁴. The IEA recommended that Ireland should continue to review the electricity market both in terms of the depth of State involvement in the sector and also the unbundling of the incumbent's vertically integrated assets. The 2011 OECD Economic Survey of Ireland made similar recommendations, in particular it recommended that some of ESB's price setting generation plant should be divested to reduce ESB's dominance and increase competition¹¹⁵.

114 IEA, Energy Policies of IEA Countries – Ireland 2012 Review, July 2012.

115 OECD, OECD Economic Survey: Ireland, October 2011.

Forfás notes that the Government decided in July 2011 that the ownership of the electricity transmission assets is to remain with ESB Networks while the operation and development of the transmission system will continue to be the responsibility of EirGrid. This decision has been considered by the SEM Committee and is now with the European Commission¹¹⁶. Further, on the sale of State assets, the Government decided in 2012 to pursue an asset disposal strategy that includes some of ESB's non-strategic power generation capacity.

There has been a substantial increase in the Public Service Obligation (PSO) levy for 2012/13¹¹⁷; it has increased by 30 per cent from €92.1 million to €132 million¹¹⁸. The subsidies to peat generation have increased from €40.4 million in 2011/2012 to €52 million while the renewable supports (mainly wind) are up from €35.8 million to €56 million¹¹⁹. The Action Plan for Jobs 2012 required DCENR to undertake a review of the peat public service obligation to reduce costs while ensuring security of supply and meeting any legal commitments (Action 1.14). The review has been completed and is being considered by DCENR.

Recommendation: In the context of the significant additional costs for consumers arising from the peat PSO, unless there is a clear economic rationale for maintaining them, subsidies for peat generated electricity should be discontinued.

Responsibility: Department of Communications, Energy and Natural Resources

Recommendation: Prior to potentially converting peat plants to biomass, a full cost benefit analysis of the implications for Irish electricity prices and energy security and sustainability should be undertaken.

Responsibility: Department of Communications, Energy and Natural Resources

Recommendation: As a maturing technology, the price support scheme for onshore wind should be revised so that the price support levels for new onshore wind projects are phased out over time. While there are potentially significant enterprise opportunities in emerging energy technologies (e.g. offshore wind/ocean energy), they should be funded through funding mechanisms for R&D, if deemed competitive, rather than by energy customers through expensive guaranteed price supports¹²⁰.

116 The decision will have to be certified by the SEM Committee (see the Guidance Paper on TSO Certification Ireland - SEM-12-005) and the European Commission (see Commission Staff Working Paper on certification of TSO of networks for electricity and natural gas in the EU – SEC (2011) 1095 final).

117 The PSO levy is designed to recoup the additional costs incurred in meeting obligations to purchase electricity from sustainable, renewable, and indigenous sources such as wind and peat.

118 When the subsidy per MWh is greater than the wholesale price per MWh, the cost of the subsidies is passed through to electricity customers. The Commission for Energy Regulation (CER) attributes the significant increases to the rise in the quantity of electricity generation subject to PSO support and a slightly lower than expected wholesale electricity cost in SEM in 2012/13.

119 For more detail, see CER, Public Service Obligation (PSO) Levy for 2012/13 – Decision Paper - (CER/12/121), August 2012.

120 Government recently decided not to introduce guaranteed price supports for offshore wind capacity. The REFIT 2 scheme (onshore wind, small hydro and landfill gas) was opened in March 2012 and the REFIT 3 (biomass technologies) scheme opened in February 2012. Both schemes are for projects built and operational between 1st

Responsibility: Department of Communications, Energy and Natural Resources

Recommendation: Review the objectives and operation of the capacity payment mechanism: Since the existing mechanism was introduced, the capacity payment model has evolved internationally. Potential exists to learn from recent international developments (e.g. New England), and revise the capacity payment mechanism in the all island market to encourage investment and to deal with intermittency. We need to ensure that the capacity mechanism provides certainty for investors, offers electricity customers value for money and delivers the flexible generation capacity required to support an increasing amount of wind on the system.

Responsibility: Department of Communications, Energy and Natural Resources

Recommendation: Assess the effectiveness of the Government statement on the strategic importance of energy infrastructure in delivering key projects in a timely fashion. Delays in completing the North-South electricity interconnector are negatively affecting the efficient functioning of the SEM and are estimated to be costing approximately €20-30 million per annum, which means higher costs for Irish electricity consumers¹²¹. Placing high-tension transmission lines overhead, as opposed to underground, provides a technically superior solution at a fraction of the cost to all energy users¹²².

Following much debate on whether high tension cables should be placed underground or overhead, Government recently issued a policy statement which reiterates the strategic importance of energy infrastructure investment to meet future economic and social goals¹²³.

The policy statement provides clarity for planning authorities to ensure the timely delivery of that infrastructure while also addressing social acceptance issues. It is critical that the effectiveness of the provisions set out in the Government statement are assessed in due course to ensure that the significant energy infrastructure investment (e.g. north-south interconnector, proposed Grid Link project) needed to support future growth and competitiveness is being delivered in a timely and cost allocative fashion.

Responsibility: Department of Communications, Energy and Natural Resources

In spite of Ireland's ambitious plans to increase the use of renewable energy sources, Ireland's reliance on gas as a primary fuel source for electricity generation is likely to continue in the medium to longer term.

January 2010 and 31st December 2015. For more information, see <http://www.dcenr.gov.ie/Energy/Sustainable+and+Renewable+Energy+Division/REFIT.htm>

121 The Action Plan for Jobs required Government to develop an awareness campaign by Q2 2012 to highlight the implications of delays in rolling out infrastructure for regional development and local job creation. According to the progress report for Q2, this has been completed. In July, the Government published a statement communicating the vital importance of the timely delivery of network investment and other energy infrastructure for national energy security, economic competitiveness, regional development and job creation. The awareness campaign will be largely based on the public confidence building measures already devised by EirGrid in relation to progressing GridLink and GridWest.

122 See Section 3.1 of Forfás, Review of Energy Competitiveness Issues and Priorities for Enterprise, December 2011.

123 Department of Communications, Energy and Natural Resources, Government Policy Statement on the Strategic Importance of Transmission and Other Energy Infrastructure, July 2012.

Recommendation: It is critical that the new energy policy framework to be developed by the Department of Communications, Energy and Natural Resources facilitates the development of gas storage and new and diverse sources of gas (e.g. fracking) to ensure that Ireland has a cost-effective, secure and diverse electricity fuel mix in the future.

Responsibility: Department of Communications, Energy and Natural Resources

Finally, reducing energy use is one of the most effective ways for companies to reduce their energy costs.

Recommendation: Continued and enhanced efforts are required by Government departments, enterprise agencies and business representative associations to ensure that businesses are fully aware of how best to reduce their energy use. Actions to improve domestic energy efficiency (e.g. smart metering, retrofitting of homes) also need to be progressed as reducing peak domestic electricity use will lead to benefits for all users.

Responsibilities: Government departments, enterprise agencies, business representative associations, Sustainable Energy Authority of Ireland

6.7 Communications Policy

Ireland's small and dispersed population does not make the economics of broadband rollout attractive relative to many other countries. The National Broadband Strategy commits the Government to a range of actions that will facilitate the more efficient rollout of infrastructure and maximise the use of existing State assets.

In considering the broadband needs of enterprise, it is important to note cost is not the only factor that concerns enterprise - access to high speed broadband is also essential. The best solution for delivering competitively priced advanced broadband services, which are critical for enterprise development and job creation, is that the market invests but in the event the market does not deliver, the State will need to intervene.

Recommendation: It is critical that the State investments committed to in the new national broadband strategy for Ireland (€175 million) are delivered according to the timelines set out¹²⁴. One of the most pressing actions will be the national mapping exercise, which will determine where State intervention is required.

Responsibility: Department of Communications, Energy and Natural Resources

As well as providing details on the Government's funding commitments, the National Broadband Strategy outlines a range of actions designed to reduce cost and to remove barriers to commercial investment, including:

- The establishment of a working group within the Department of Transport, Tourism and Sport to address the policy aspects of any barriers that impact on the deployment of telecommunications infrastructure by agencies under its remit. The group will consider

124 Department of Communications, Energy and Natural Resources, Delivering a Connected Society - A National Broadband Strategy for Ireland, August 2012

timely and standardised processing of permit applications for telecommunications infrastructure as well as applications for street infrastructure such as street cabinets and the installation of underground telecommunications infrastructure;

- The Department of Communications, Energy and Natural Resources (DCENR) will establish a working group comprising of industry representatives, the Department of the Environment, Community and Local Government (DECLG) and local authorities with a view to agreeing a code of enhanced communication between industry, local authorities and communities aimed at addressing public concerns in relation to broadband infrastructure.

In order to maximise the use of existing State assets, the National Broadband Strategy requests that:

- NewERA will assess the relevant assets owned and operated by State entities, both commercial and non-commercial, with a view to determining the extent to which the opportunities exist to enhance the rollout of high speed broadband on a commercial basis. Industry is also being asked to identify what gaps exist in relation to infrastructure provision.
- Government Departments consider the property and other assets owned by the State, which have the potential to assist in the rollout of broadband services. Models for the deployment of key assets owned by non-commercial entities will be explored over the coming months, in consultation with the entities and industry with a view to optimising access for telecoms infrastructure.

Recommendation: Progress on the actions outlined in the National Broadband Strategy must be carefully monitored to ensure that timely implementation is achieved and to ensure that the actions have the desired outcomes.

Responsibility: Department of Communications, Energy and Natural Resources

6.8 Waste Policy

Ireland has long needed to develop a new waste policy that delivers sustainable, cost effective waste treatment options to meet the needs of enterprise and the residential sector and promotes waste prevention. In light of this, the recent publication of the Government's new waste management policy is particularly timely¹²⁵. *A Resource Opportunity* sets out a number of guiding principles which will shape policy henceforth - placing prevention and waste minimisation at the forefront of waste policy; ensuring that Ireland extracts the maximum value from waste (whether through reuse, recycling or recovery); and using landfill only as a last resource.

The policy document provides certainty in relation to the regulation of the household waste market and in an especially welcome move, provides for the streamlining of waste management planning - the reduction in regional formations from 10 to no more than three will deliver a more cost effective and efficient system. The re-commitment to the

¹²⁵ Department of the Environment, Community and Local Government, *A Resource Opportunity – Waste Management Policy in Ireland*, July 2012.

implementation of the waste hierarchy and the prioritisation of waste prevention and minimisation are also positive developments.

Recommendation: Achieving the objectives and measures outlined in the Government's Waste Management Policy document is of paramount importance. In particular, the reduction in regional formations from 10 to no more than three should be prioritised in order to generate the economies of scale necessary to incentivise private investment in waste infrastructure.

Responsibilities: Local Authorities / Department of the Environment, Community and Local Government

From an enterprise perspective, however, concerns remain. Firstly, Ireland has limited waste management infrastructure options compared with international competitors, which is leading to an on-going heavy reliance on landfill. Irish enterprise needs a range of waste treatment options across the waste management hierarchy and delivering such infrastructure is a key priority. While the policy is explicitly predicated on the EU's waste hierarchy, it will take time to deliver the necessary investment to provide a sufficient stock of alternate waste infrastructure to minimise Ireland's reliance on landfill.

As a result, waste management costs remain an issue for Irish businesses, particularly when increased regulations such as those requiring separation of waste and increased recycling are impacting on their bottom line. Although landfill costs in Ireland have moderated significantly, advertised prices and prices which can be negotiated in the market remain comparatively high, and gate fees in Ireland for food waste remain amongst the highest of the benchmarked countries and regions.

Recommendation: Reflecting the currently limited options available in Ireland, future increases in the landfill levy should be cognisant of their impact on cost competitiveness and should be set at a level that reflects the pricing of externalities (environmental and other damage caused by landfill such as remedial treatment costs and emissions).

Responsibility: Department of the Environment, Community and Local Government

A second key concern relates to developments at EU level - EU legislation continues to be a major driver of waste policy through, for example, the Waste Framework Directive, the Landfill Directive, and the producer responsibility initiative etc. The new national waste policy, however, makes no reference to the fact that the European Commission (EC) plans to have new, more ambitious EU waste targets agreed by 2014. It is essential that Ireland takes a proactive approach to shaping EU legislation and that it transposes such legislation in a manner that supports competitiveness.

Recommendation: Given that new waste targets are to be put in place at EU level by 2014, we need to ensure that Ireland's negotiating position is informed by national competitiveness as well as environmental considerations.

Responsibility: Department of the Environment, Community and Local Government

Finally, in order to achieve the goals set out in *A Resource Opportunity* a range of infrastructures are required along the waste hierarchy. The new policy addresses many of the barriers to private sector investment such as the regulatory uncertainty and the lack of national coordination to facilitate economies of scale. Moving forward, we need to prioritise the development of specific infrastructures including:

- Thermal treatment capacity to recover energy from municipal and industrial waste;
- Thermal treatment or landfill capacity for hazardous waste in light of increasingly strict rules on the export of waste;
- Biological treatment capacity (composting, anaerobic digestion); and
- Reprocessing capacity for recovered materials.

7 Credit Costs

7.1 Summary

Access to finance and its cost are critical issues for enterprise. The availability of a flow of affordable capital is essential for the day to day operations of enterprise and to allow firms to undertake productivity enhancing investments. At this point in time, access to credit is the dominant concern. The Deloitte CFO Survey¹²⁶ (Quarter 2, 2012 survey results) notes that the *'perception that the cost of credit is high has grown this quarter with net 81% of respondents stating that the overall cost of new credit is high, despite the continued record low ECB interest rates. Comparing Irish results with selected EU countries for the same questions, Ireland ranked worst in class, with Irish based CFOs perceiving cost of credit to be the highest and credit the hardest to get'*.

Ireland's entry into the eurozone and financial sector deregulation internationally supported a rapid increase in the availability of inappropriately low priced credit prior to the financial sector crises in 2007. Business and consumer debt grew rapidly - according to the National Competitiveness Council, corporate indebtedness in Ireland reached 194 per cent of GDP in Q2, 2011¹²⁷. The preponderance of debt should make Irish business more sensitive to increases in interest rates - especially when euro area interest rates are likely to start increasing from current historic lows.

Loose monetary policy in response to the current financial crises has supported a continuation of low interest rates. However, the difference between the interest rates charged for new loans and base rates has widened. This is driven by a number of factors, which are largely outside of domestic control, including:

- Banks are paying higher funding costs. The cost of raising funds is the dominant driver of the price at which loans are offered. Irish Banks are funding themselves through a combination of central banking funding, deposits, wholesale funding and other sources. The financial crisis and particularly the challenges faced by the Irish banks have put upward pressure on bank funding costs. Relevant Irish banks are also paying fees on the temporary Eligible Liabilities Guarantee scheme.
- More accurate pricing of borrower risk combined with increases in actual borrower risk. The banks under-priced risk prior to the financial crises and are now reassessing this. Higher levels of risk require higher rates of return. In tandem, the economic crisis has also resulted in higher borrower risks as evidenced by increasing business loan default rates.
- Efforts to increase banking profit margins in order to repair damaged balance sheets.

Irish businesses continue to pay more for new lending than their euro area counterparts for new loans and overdrafts:

- In June 2012, Irish interest rates were higher than the euro area average for new loans (Figure 7.1). Loans of up to 1 million (which are often used as a proxy for the rate applying to SME loans) are over 10 per cent more expensive in Ireland while loans of over 1 million are almost 15 per cent more expensive. Interest rates on new loans to

¹²⁶ The Deloitte CFO Survey: Sustainability and the CFO, Quarter 2 2012 Survey Results

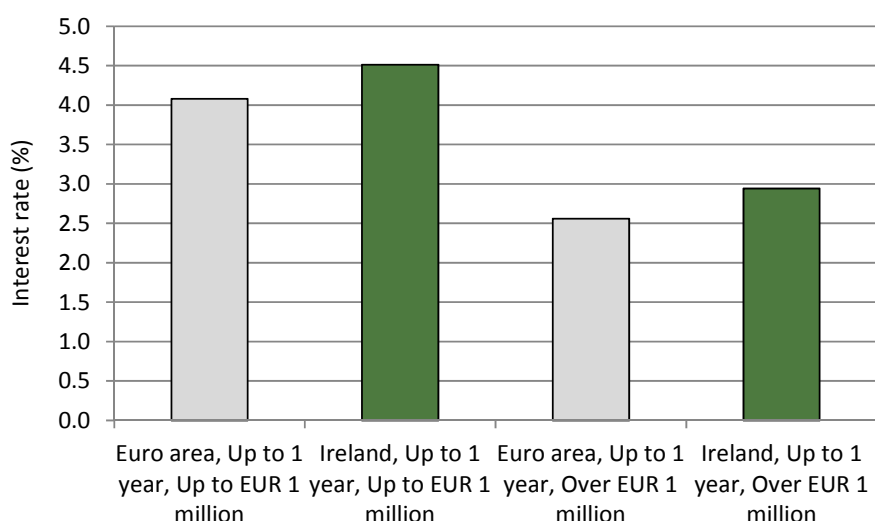
¹²⁷ See Figure 3.8 in National Competitiveness Council, Ireland's Competitiveness Scorecard 2012, Forfás, July 2012

non-financial corporations (NFCs), applied by resident credit institutions, have generally been increasing since 2009 (Figure 7.4).

- Revolving loans and overdrafts also provide an important source of short term finance (Figure 7.2). In June 2012, interest rates in Ireland for overdraft facilities were almost 19 per cent above the euro area average.
- As interest rates on the outstanding stock of loans began to drop across the euro area in mid-2009, interest rates in Ireland began to converge with the euro area and were lower than the euro area average in June 2012 (Figure 7.3).
- Comparing Figures 7.3 and 7.4, the data suggests that Irish interest rates for new loans are generally higher than the euro area average, while the Irish rate for outstanding loans is lower than the euro area average. This is primarily a result of the composition of the stock versus the flow.

7.2 Credit Costs Indicators

Figure 7.1: Interest Rates for Non-Financial Corporations (New Business) by Loan Size Q1 2012¹²⁸



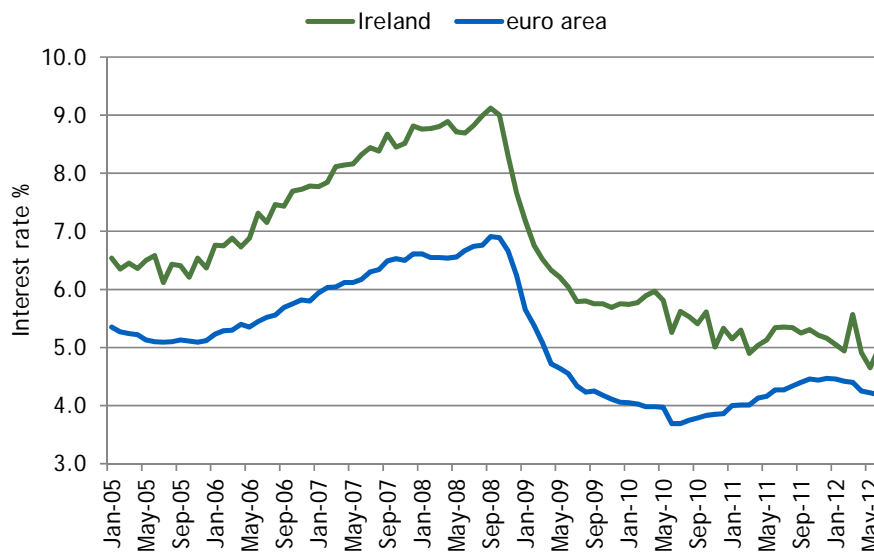
In June 2012, Irish interest rates were higher than the euro area average for both loan categories examined. Loans of up to €1 million (which is often used as a proxy for the rate applying to SME loans¹²⁹) are over 10% more expensive in Ireland while loans of over €1 million are almost 15% more expensive.

Source: European Central Bank

¹²⁸ Loans under €1 million and up to one year refer to loans up to €1 million at floating rate and up to 1 year initial rate fixation. Loans over €1 million and up to one year refer to loans over €1 million at floating rate and up to 1 year initial rate fixation.

¹²⁹ Central Bank, Retail Interest Rate Statistics, Information Release, April 2012

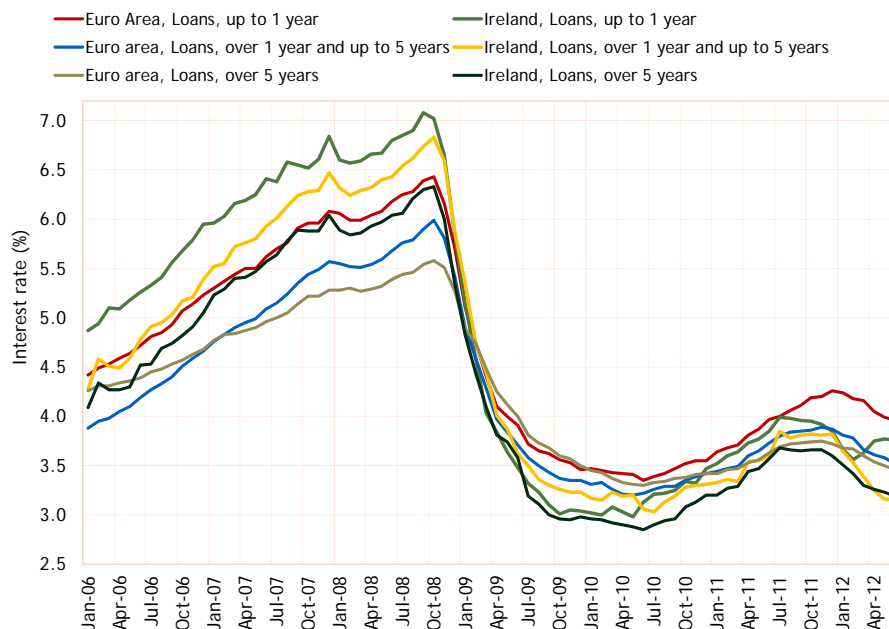
Figure 7.2: Revolving Loans and Overdraft Interest Rates for Non-Financial Companies, April 2012¹³⁰



Interest rates for revolving loans and overdrafts in Ireland have remained elevated above that of the euro area average but the gap has narrowed in the past two years. However, in June 2012, interest rates in Ireland for revolving loans and overdraft facilities were almost 19 per cent above the euro area average.

Source: European Central Bank

Figure 7.3: Retail Interest Rates (%) - Loans, Outstanding Amounts by Loan Size January 2006 - June 2012

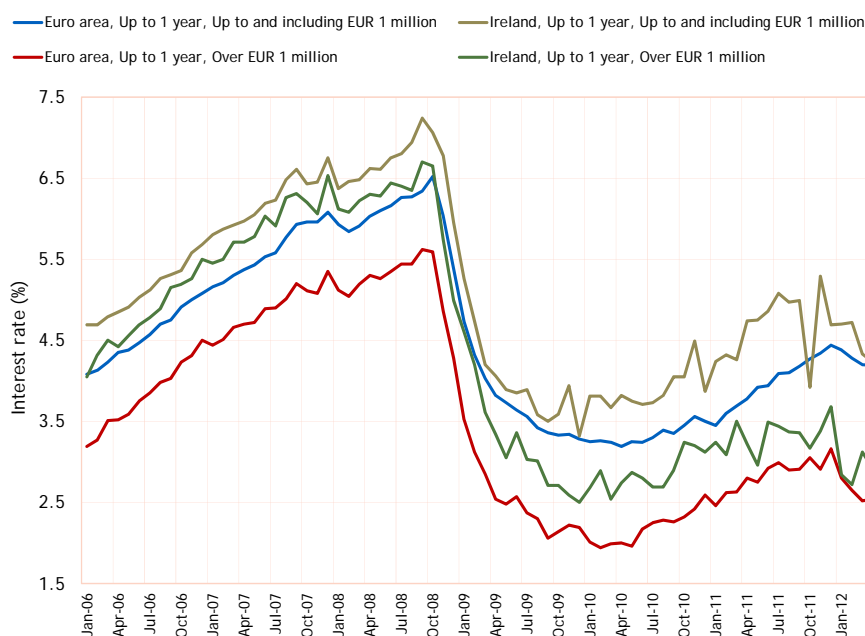


As interest rates on outstanding loans began to drop across the euro area in mid-2009, interest rates in Ireland began to converge with the euro area and were lower than the euro area average across the three groups in June 2012. These three categories of loans accounted for €88.7 billion in outstanding loans in December 2011.

Source: ECB (2012) Euro area and national MFI interest rates (MIR)

¹³⁰ The rate shown reflects those for revolving loans and overdrafts, convenience and extended credit card debt. Data as of June 2010 may not be fully comparable with those prior to that date owing to some minor methodological changes. The impact of the change in methodology, however, is not so drastic to make them completely incompatible.

Figure 7.4: Retail Interest Rates - New Business by Loan Size and Rate Fixation January 2006 - June 2012



Interest rates on new loans to NFCs, applied by resident credit institutions, have generally been increasing since 2009. While the margin between Irish and euro area rates has narrowed for larger loans, the margin for smaller loan has not narrowed significantly since 2006. These two categories of new lending accounted for €1.4 billion of new business loans in Ireland in December 2011.

Source: Source: ECB (2012) Euro area and national MFI interest rates (MIR)

7.3 Policy Focus on Credit Costs

Given the complexity surrounding the market for funding and the policy solutions being advanced, a wide range of measures are required to support an improved lending environment.

Considerable uncertainty remains over the impact of the banking crisis on banks' ability to raise funds and support lending. The banking system is currently undergoing comprehensive change in terms of recapitalisation, deleveraging and restructuring.

Recommendation: There is a need to ensure that the efficacy of measures put in place to improve credit flows is assessed and action taken as required.

Responsibility: Central Bank of Ireland / Credit Review Office / Department of Finance / SME Credit Consultation Committee

The collapse of the domestic banks and the withdrawal of many foreign banks (e.g. Bank of Scotland Ireland) raise concerns over the levels of competition in the banking sector. Central Bank data (Herfindahl Indices using Central Bank Business Credit and Deposits Data) highlights that bank concentration in the business (NFC) lending market is rising¹³¹. Concentration is particularly high for SMEs. Three banks dominate lending in the SME market, with 78 per cent of those applying for credit in the Mazars SME Lending Study, November 2011 seeking credit from the two 'pillar' banks.

131 McCann, F., McIndoe-Calder, T., Bank Competition Through the Credit Cycle: Implications for SME Financing, Central Bank of Ireland, Economic Letters Series, Volume 2012, No. 4, April 2012

Recommendation: Efforts to encourage existing foreign banks to retain lending operations in Ireland and to attract new entrants in the medium term, while challenging, are important. In terms of new entrants, potential may exist to attract new entrants offering innovative business models. The sale of State banking assets could also be used to boost competition in the banking sector.

Responsibility: Central Bank of Ireland / Department of Public Expenditure and Reform

In 2010, the UK Office for Fair Trading (OFT) undertook a review¹³² of the barriers to entry, expansion and exit in retail banking, including both personal and SME banking. The review looked at the regulatory requirements, access to essential inputs such as IT infrastructure and payment systems, and barriers to achieving scale such as switching and the role of brands and branch networks. The Competition Authority should consider the merits of undertaking a similar study here.

Recommendation: The Competition Authority should consider the merits of undertaking a review of the barriers to entry, expansion and exit in retail banking, with a view to encouraging greater competition.

Responsibility: Competition Authority

Finally, the IMF has highlighted that the “banks remain burdened by cost structures that are too high; plans to reduce operational expenses will need to be fully implemented”¹³³.

132 http://www.offt.gov.uk/shared_offt/personal-current-accounts/oft1282

133 IMF, 2012 Article IV Consultation with Ireland - Concluding Statement of the IMF Mission

8. Business Services Costs

8.1 Summary

This chapter looks at the cost of key professional services to business such as computer programming and consultancy, accountancy and legal services. In general business and professional services account for a relatively low proportion of the enterprise cost base – certainly compared with labour costs and property costs¹³⁴. Nevertheless as an input to almost every enterprise in the country, the cost competitiveness of professional and business services has a direct impact on the competitiveness of the entire Irish economy. This has been recognised in the EU/IMF Programme of Financial Support for Ireland, which accords significant attention to the promotion of competition in the professional services sector¹³⁵.

There are limited data sources available for professional and business service prices. The most relevant source is the CSO's experimental Services Producer Price Index (SPPI) which measures changes in the average prices charged by domestic service producers to other businesses for a selected range of services¹³⁶.

Figure 8.1 examines the change in price levels for a number of business and professional services subsectors. In 2011, the cost of most services had fallen to, or below, 2006 levels. The largest decrease in services costs since 2006 has been in the Architecture, Engineering and Technical testing category, where prices have fallen by nearly 12 per cent. The exception to this trend is the Legal, Accounting, PR and Business Management category, where prices remained 1.5 per cent above 2006 levels.

Looking in greater detail and accountancy and legal costs, Figure 8.2 shows that while the cost of accountancy services have continued on a downward trajectory over the course of the last number of years and are now significantly below their 2006 level, legal service costs remain approximately 12 per cent above 2006 price levels.

Looking internationally, Figure 8.3 decomposes the cost of enforcing a business contract into three categories. According to the World Bank, Ireland remains one of the most expensive locations among those benchmarked. Attorney fees account for the 70 per cent of the cost of enforcing a business contract in Ireland.

The final indicator in this section examines non-life insurance density (i.e. premiums) in a range of countries (Figure 8.4). High insurance density can be a function of both high insurance costs and the requirement for high coverage levels. Non-life insurance relates to motor property, employer's liability, public liability, travel and other business insurance. The density of non-life insurance in Ireland is marginally below that of the OECD average and has decreased by 15 per cent since 2008. Despite this, the business sector remains concerned

134 This reflects experiences elsewhere – for instance, the Italian Antitrust Authority has estimated that in Italy an average of 6 per cent of exporting firms' total costs are accounted for by professional services. See European Commission, Communication from the Commission: Report on Competition in Professional Services, COM (2004) 83 final, 2004.

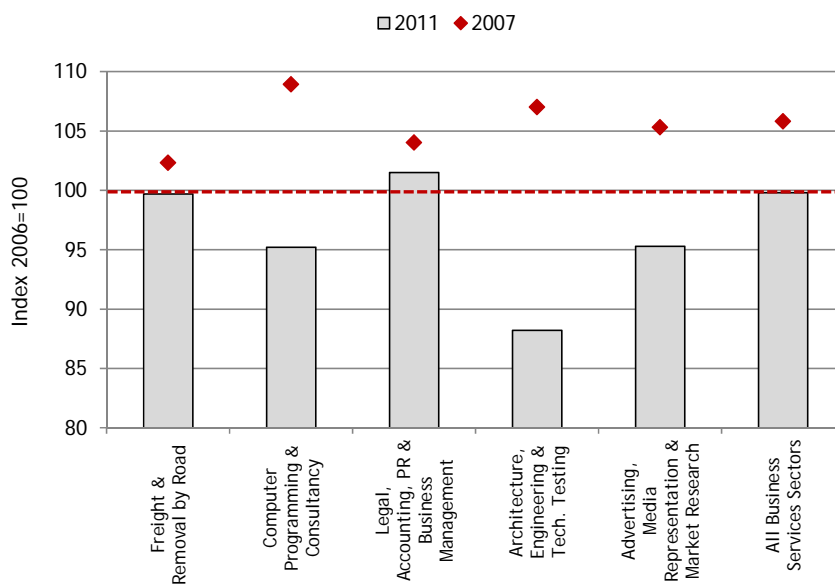
135 EU Commission/IMF, EU/IMF Programme for Financial Support for Ireland, December 2010.

136 The SPPI is an experimental survey by the CSO which measures changes in the average prices charged by domestic service producers to other businesses for a selected range of services. In most cases, the index covers transaction costs from business to business and excludes consumers who are covered in the Consumer Price Index (CPI). The individual price indices are aggregated together to create a "service industry" index that is limited in coverage. The indices are still under development and may be subject to methodological improvement. Figures should therefore be treated as provisional and subject to revision. These indices are being published to engage users in the on-going development of the SPPI methodology.

over insurance costs. The AXA Small Business Report 2011 examined a wide range of issues affect SME across countries. Having interviewed 650 small and medium-sized enterprises across 10 countries in Europe, North America and Asia, insurance and its cost as a significant business risk, was mentioned by only 1 per cent of respondents globally. However, the cost of insurance as a business risk was most recognised in Ireland (10%)¹³⁷.

8.2 Business Service Indicators

Figure 8.1: Services Producer Price Index, 2011

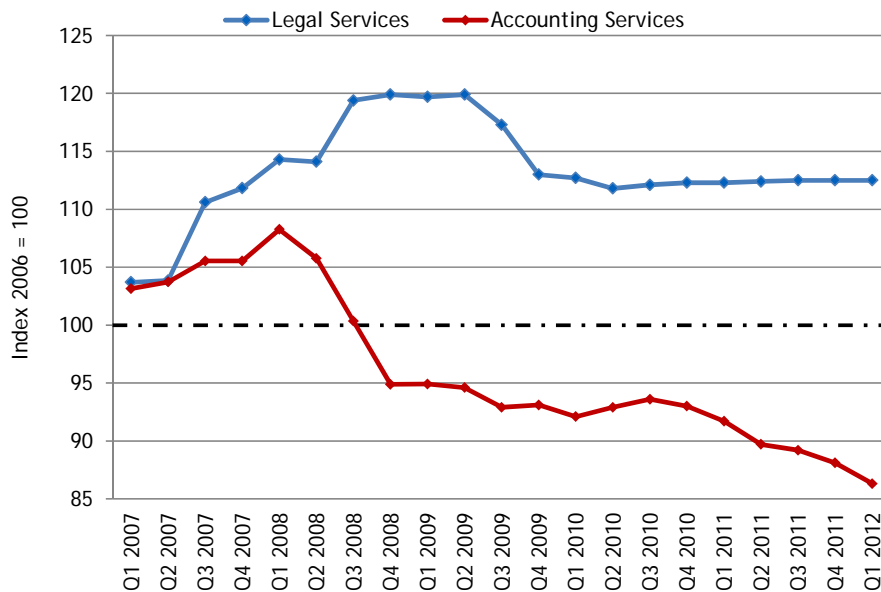


In 2011, the cost of most business services had fallen to, or below, 2006 levels. The exception to this was the Legal, Accounting, PR and Business Management category, where prices remained 1.5% above 2006 levels. The largest decrease in services costs since 2006 has been in the Architecture, Engineering and Technical testing category, where prices have fallen by nearly 12%.

Source: CSO, Services Producer Price Index

137 AXA International, Small Business Report 2011

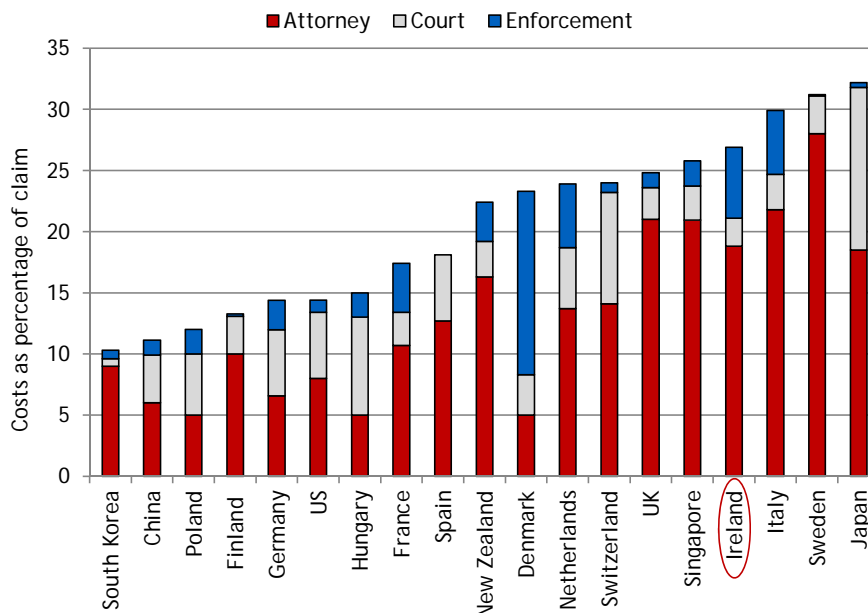
Figure 8.2: Accountancy and Legal Costs¹³⁸, Q1 2007- Q1 2012



This indicator examines the evolution of accountancy and legal costs in greater detail. While the cost of accountancy services have been on a continual downward trajectory over recent years, legal service costs have remained approximately 12% above 2006 price levels.

Source: CSO, Services Producer Price Index

Figure 8.3: Legal Fees, Cost of Enforcing a Business Contract, 2011

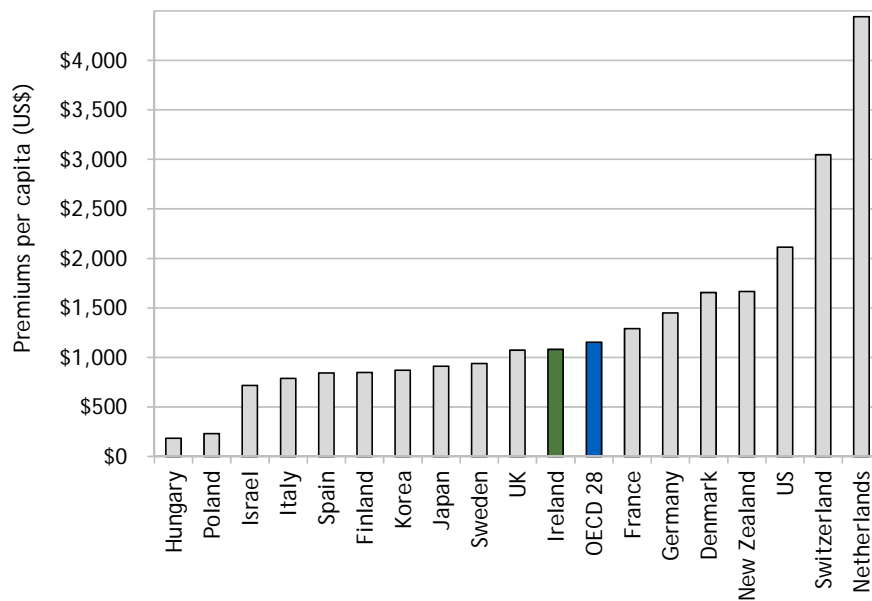


This indicator decomposes the cost of enforcing a business contract into three areas. Ireland remains one of the most expensive locations among those benchmarked for the total cost of enforcing a business contract. Attorney fees account for 70% of the cost of enforcing a business contract in Ireland.

Source: World Bank, Doing Business 2012

138 Data on legal services is based on responses received from 18 companies (and 112 price observations), the majority of whom employ between 10 and 49 employees. The survey does not include data on prices for barrister services. Given the small sample size, caution should be used when interpreting the results.

Figure 8.4: Non-Life Insurance Density, Premiums per Capita in US\$, 2010



High insurance density (insurance expenditure per capita) can be a function of both high insurance costs and the requirement for high coverage levels. Non-life insurance relates to motor, property, employer's liability, public liability, travel and other business insurance. The density of non-life insurance in Ireland is marginally below that of the OECD average and has decreased by 15% since 2008.

Source: Swiss Re, Sigma No.2, 2010

8.3 Policy Focus on the Legal Profession and Procedural Reform

The legal profession has repeatedly been subject to a range of investigative studies, all of which recommended reform¹³⁹. Despite several positive recent developments (such as the Bar Council reforming the restrictions it imposes on newly qualified barristers), the profession remains characterised by a range of restrictions on competition. Relative to the other professions examined, prices for legal services have proven extremely sticky and have not adjusted downwards to the degree that might have been expected given current economic circumstances.

The Legal Services Bill (currently progressing through the Oireachtas), once enacted, will deliver many welcome reforms. However, a number of amendments would be beneficial¹⁴⁰. For example, while the Bill facilitates the establishment of multi-disciplinary partnerships offering legal services, it does not allow the establishment of a limited liability partnership (LLP). An LLP is a partnership in which some or all of the partners have limited liability - an LLP, therefore, is more akin to a company in that one partner is not responsible or liable for

139 For example, Trade Commission, The Report of Study into Restrictive Practices in the Legal Profession by the Trade Commission (1990); Legal Cost Working Group, Report of the Legal Cost Working Group, 2005; Competition Authority, Competition in Professional Services- Solicitors and Barristers by the Competition Authority, 2006; Committee of Public Accounts, Third Interim Report on the Procurement of Legal Services by Public Bodies, Dáil Éireann, January 2011

140 At present, if a party's barrister makes an argument in written form and sends a legal submission to the judge and the opposing barrister, the public and other legal professionals do not get to see that document. In the interests of both transparency and competition (the current procedure limits access to specialised legal knowledge, bidding up the price of specialised legal advice), there is merit in considering the introduction of an amendment which would direct the superior courts of Ireland to maintain copies of a party's legal submissions as part of the official case records.

another partners' misconduct or negligence. At present, law firms outside of Ireland can benefit from such a structure when servicing the Irish market and this may put Irish based firms at a disadvantage.

Recommendation: Consideration should be given to amending the Legal Services Bill to facilitate the establishment of Limited Liability Partnerships.

Responsibility: Department of Justice and Equality

Other Structural Reforms are Required

At present, the Irish legal system comprises a two-tier structure made up of junior and senior counsel. Such a structure allows for higher fees to be charged but does not offer a definitive guide as to the quality of the barrister in question. This is an obvious additional cost which must be borne by enterprise and individual consumers alike.

The National Competitiveness Council has previously recommended (along with others) that the present manner in which Senior Counsel are appointed be reformed so that the title becomes a useful quality signal facilitating competition in legal services. Further, consideration should be given to the creation of a single tier counsel system - the removal of the distinction would promote meritocracy and would, for example, lessen the requirement for the State and other clients to engage senior counsels for High Court and Supreme Court cases where the complexity does not necessarily require a senior.

There are other possible paths that reform might take. At present, solicitors are prohibited from being the lead advocate where a legal team of both barristers and solicitors is representing a client. This restriction should be removed and solicitors be permitted to act as lead counsel when advocating in court with a barrister in order to promote enhanced competition in legal services.

Although a less urgent issue than at the height of the property boom, the role of the legal profession in the property market (specifically through their conveyancing role) should not be overlooked. Previous studies have found that the cost of conveyancing in Ireland is significantly higher than other countries with similar legal systems. Suitably qualified professionals, in addition to solicitors, should be allowed to provide conveyancing services. As suggested previously by the Competition Authority, the development of a specialist conveyancer profession in Ireland, with appropriate regulations and standards would enhance competition. This has already occurred in the UK (in 1987) with the creation of licensed conveyancers, allowing conveyancing to be done by non-solicitors. Subsequent evaluations have found that the creation of this profession had a positive effect on price competition¹⁴¹.

Recommendation: Consideration should be given to the creation of a single tier counsel system.

Responsibility: Department of Justice and Equality

141 Zerp et al, Summary of the Comparative Legal and Economic Study into the EU Conveyancing Services Market, COMP/2006/D3/003, 2007, available at: http://ec.europa.eu/competition/sectors/professional_services/studies/csm_standalone_en.pdf

Recommendation: Suitably qualified professionals, in addition to solicitors, should be allowed to provide conveyancing services.

Responsibility: Department of Justice and Equality

Significant Cost Savings could arise through Procedural Reform

In establishing independent regulation, improving access and competition, making legal costs more transparent and ensuring that adequate procedures are in place to address consumer complaints, the Bill will address many of the concerns expressed in the plethora of reports previously referenced¹⁴².

The high cost of legal services in Ireland is not entirely a result of regulatory factors and so regulatory reform is not the sole response required if costs are to be reduced. While protecting the independence and quality of the judicial system (an important competitive strength in Ireland), there is a need to widen the scope of reform to include reform of court procedures - improved case management, whereby time delays in scheduling and hearing cases is minimised, for instance, offers potentially significant cost savings.

Previously, the Legal Cost Working Group recommended a number of procedural measures to the operation of the legal system¹⁴³. For instance, the group recommended that the rules of the court should include a specific order facilitating supervision by the court of the pace of litigation and this should also contain measures to sanction unnecessary delays.

Recommendation: The procedural reforms recommended by the Legal Cost Working Group are designed to make the operation of the courts more efficient and to reduce cost, and so should be implemented.

Responsibility: Department of Justice and Equality

142 The Bill currently proposes the establishment of three new bodies – a regulatory authority (the Legal Services Regulatory Authority), an Office of the Legal Cost Adjudicator, and a Legal Profession Disciplinary Tribunal.

143 Legal Cost Working Group, Report of the Legal Cost Working Group, 2005

9. Broader Cost Environment

9.1 Summary

The previous chapters examined direct enterprise costs. Enterprise, however, does not operate in a vacuum, separate from the rest of the economy. The price of all goods and services contributes to the overall price level in the economy and ultimately impacts upon a country's international competitiveness.

Consumer prices, measured by the Consumer Price Index (CPI), can be viewed as indirect costs for business. They are a reflection of the overall cost environment. Outside of work, employees purchase goods and services. Movements in these prices impact upon wage demands, and so the impact of price changes in consumer markets spill over into the cost base of the enterprise sector. For instance, the correlation between rapidly escalating house prices and increases in average wage levels is widely recognised.

This chapter, therefore, focuses on the overall cost environment for consumers and changes in the price levels for goods and service. The analysis draws primarily from the CSO's Consumer Price Index, as well as the European Harmonised Index of Consumer Prices.

While consumer prices in Ireland have adjusted downward in recent years, Figure 9.1 shows that prices remain high relative to most other euro area countries. In 2011 Ireland was the 3rd most expensive location in the euro area for consumer goods and services and Irish prices were 12 per cent above the euro area average.

An alternative method of comparing prices is used in Figure 9.2. This indicator shows the relative cost of a weighted basket of 122 goods and services (excluding rent) compared to the cost in New York. In 2008 there was an approximate 20 per cent premium on the costs of these goods and services in Dublin compared to New York. As a result of cost reductions, Dublin was ranked the 26th most expensive city surveyed (24 per cent cheaper than New York), down from a high of 4th in 2008.

The consumer price index (CPI) increased in Ireland in 2011 following declines in each of the two previous years (Figure 9.3). As seen in Figure 9.4, health and education consumer costs have increased at a significantly faster rate than overall consumer costs since 2000. In 2011, education costs were 93 per cent above what they were in 2000 while health costs were approximately 76 per cent above 2000 prices.

Figure 9.5 looks at inflation in a European context using the Harmonised Index of Consumer Prices (HICP) and finds that prices in Ireland increased at a significantly slower rate than in most of the euro area in 2011. The price of food and non-alcoholic beverages in Ireland have increased at a slower rate than the other countries included in Figure 9.6, representing a competitiveness gain. However these changes must be viewed in the context of overall price level for food and non-alcoholic beverages. Data from Eurostat has shown that in 2009 Ireland was the fourth most expensive country among the EU27 for food and non-alcoholic beverages.

Housing costs - both to buy and to rent - are significant determinants of wage demands. Since the bursting of the construction and property bubble, house prices have adjusted downwards and consequently have become more affordable when expressed as a ratio of average earnings (Figure 9.7). In terms of the rental market, rental values declined sharply between 2007 and the end of 2009. Since then rent prices have stabilised nationally, at approximately 25 per cent below 2007 levels (Figure 9.8).

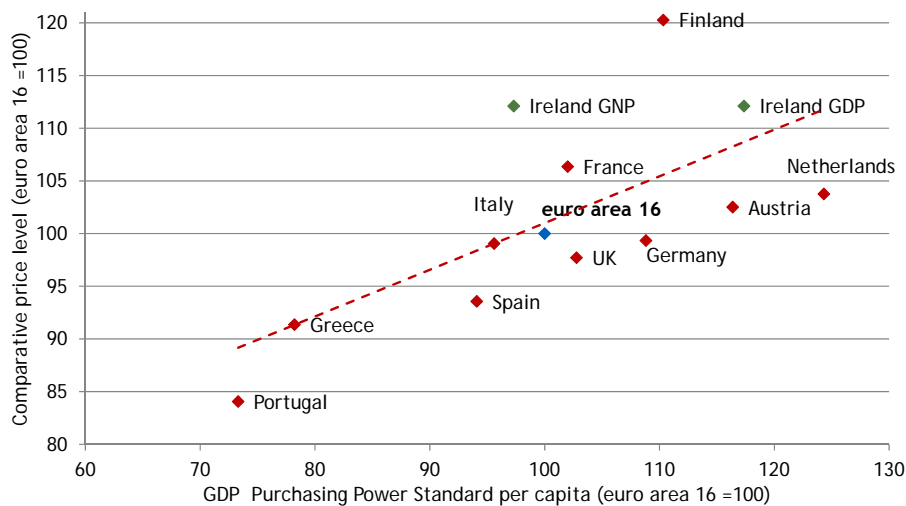
Returning to the theme of wages, the remaining charts in this chapter examine wage rates for a range of (largely public sector) employees. Figure 9.9 examines primary school teachers' salaries. The starting salary of a primary school teacher in Ireland in 2010 was more than 20

per cent higher than the OECD and euro area averages. At the top of the scale the differential is greater - salaries in Ireland are 48 per cent higher than OECD average and 40 per cent higher than euro area average¹⁴⁴.

Figure 9.10 illustrates gross salary data for nurses in both dollar terms and adjusted for the cost of living (i.e. PPPs). Irish salaries are amongst the highest in the OECD. Data for all countries is provided on a gross basis, and does not take into account differences in tax regimes across countries that affect the take home pay of these individuals. As noted in Chapter 3, Irish workers are likely to benefit from a relatively low tax wedge at average wage levels, but the tax wedge increases as wage levels increase. Figure 9.11 examines data on gross annual remuneration of health specialists for a number of OECD countries. Based on this data, health specialists in Ireland are the highest paid in the OECD (for countries where data is available) in both dollar terms and adjusted for cost of living.

9.2 Cost Environment Indicators

Figure 9.1 Price Levels and GDP per Capita¹⁴⁵, 2011



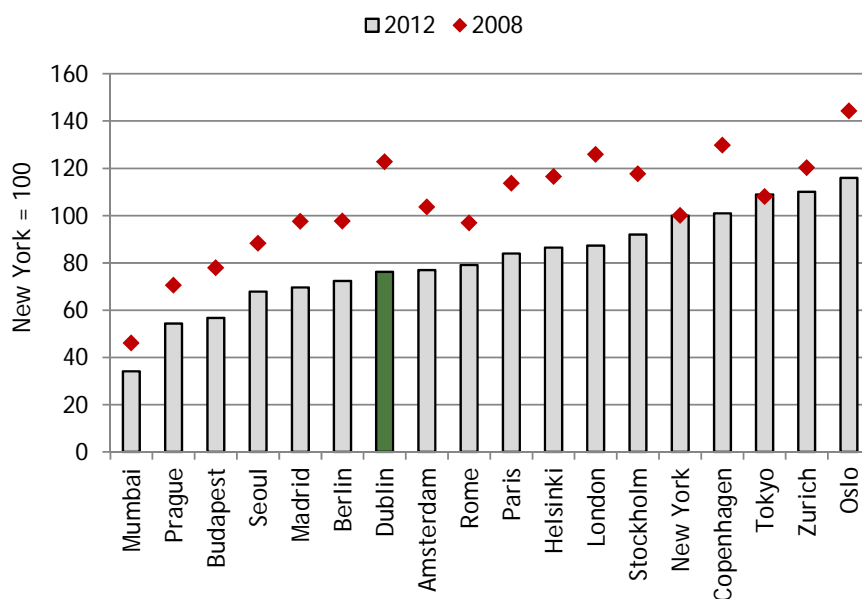
While consumer prices in Ireland have adjusted downward in recent years, this chart shows that prices remain elevated relative to most other euro area countries. In 2011 Ireland was the 3rd most expensive location in the euro area for consumer goods and services. Irish prices were 12% above the euro area average. Costs relative to national income (in GNP terms) remain particularly high when compared to the euro area average.

Source: Eurostat, Forfás calculations

144 This data is expressed in US\$ and is not adjusted using purchasing power parities. The OECD's Education at a Glance also publishes salary data in terms of US\$ converted using PPPs. Based on this data, starting salaries for Irish primary teachers are 18.5 per cent above the OECD 29 average and 37.9 per cent above the OECD average at the top of the scale. It should be noted that since this data was collected, salaries and allowances for teachers in Ireland have been reduced. Following a decision announced in January 2012 to suspend various allowances, it is estimated that new entrants to the teaching profession will earn up to 30 per cent less than those who began teaching two years ago – see Irish Times, Pay for new teachers down 30% since 2010, 28th August 2012.

145 GDP per capita PPS refers to 2010 for Germany and Ireland – 2011 data is not yet available for these countries.

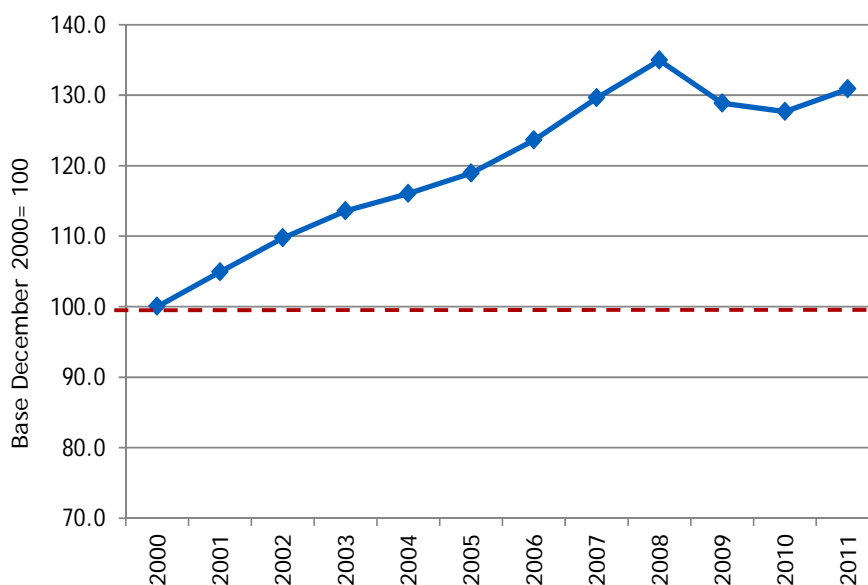
Figure 9.2 Consumer Price Level Comparison 2008 - 2012, (New York = 100)



This indicator shows the relative cost of a weighted basket of 122 goods and services (excluding rent) in 72 cities compared to the cost in New York. In 2008 there was an approximate 20% premium on the costs of these goods and services in Dublin compared to New York. By 2012, the costs of these goods and services in Dublin had fallen significantly - as a result Dublin is now the 26th most expensive city surveyed, down from a high of 4th most expensive in 2008.

Source: UBS, Prices and Earnings

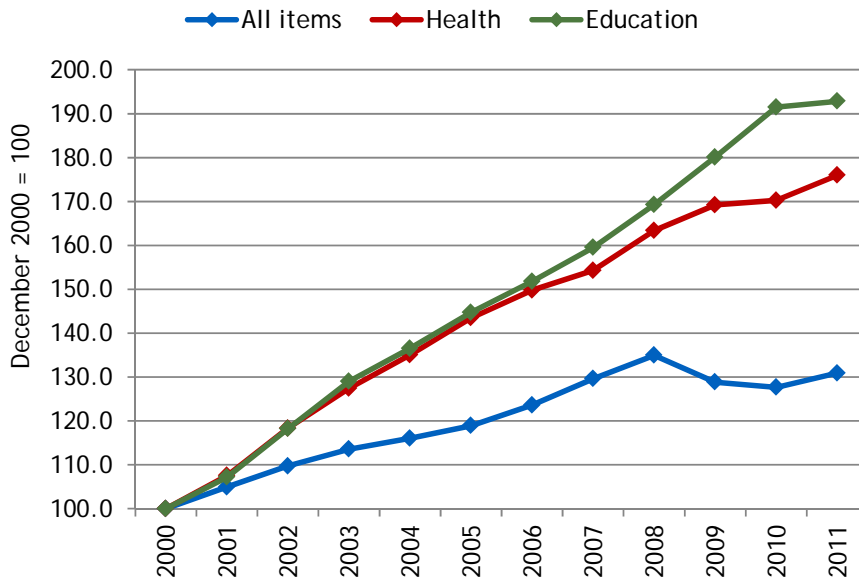
Figure 9.3 Consumer Price Index, Base December 2000=100



The consumer price index - which provides data on changes in the cost of living - has increased in 2011 following two years of decline in 2009 and 2010. The chart shows that the cost of living in Ireland has increased substantially since 2000. In 2011, consumer prices were 31% above what they were in 2000, and 6% above 2006 levels.

Source: CSO, Consumer Price Index, Forfás calculations

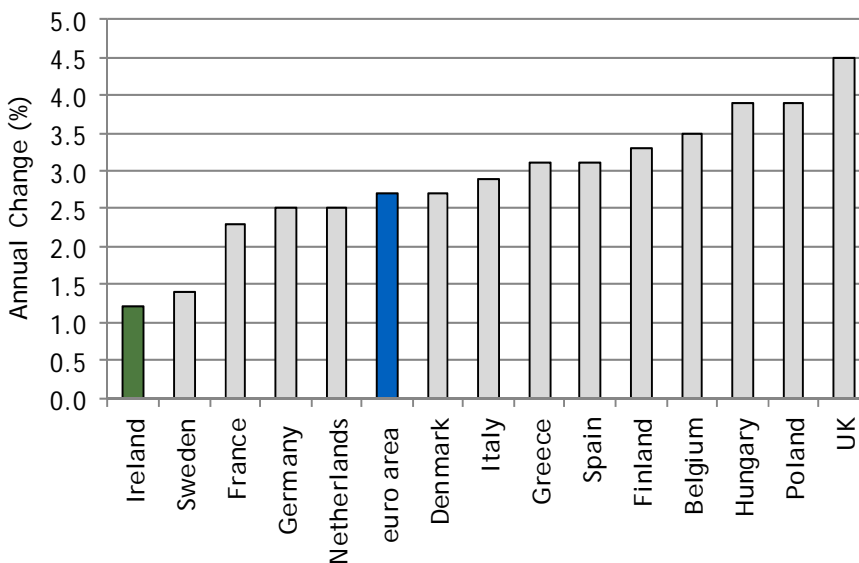
Figure 9.4 Health and Education, 2000-2011, (December 2000=100)



As seen in Figure 9.4, health and education consumer costs have increased at a significantly faster rate than overall consumer costs since 2000. In 2011, education costs were 93% above what they were in 2000 while health costs were approximately 76% above 2000 prices.

Source: CSO, Consumer Price Index, Forfás calculations

Figure 9.5 Harmonised Index of Consumer Prices¹⁴⁶, Annual Percentage Change, 2011

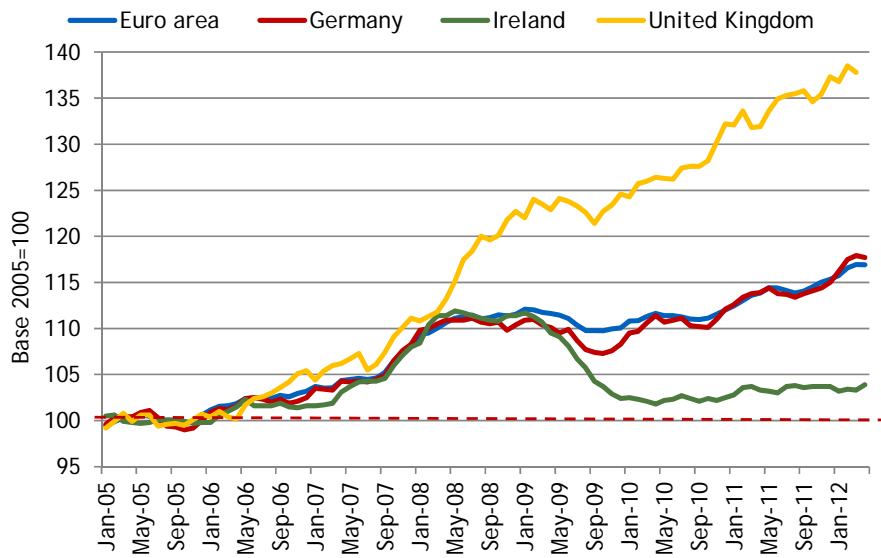


Consumer price inflation in the euro area is measured by the Harmonised Index of Consumer Prices (HICP). According to the HICP, prices in Ireland increased at a significantly slower rate than in most of the euro area in 2011.

Source: CSO, Consumer Price Index

146 Certain items are excluded from the coverage of the HICP, which in essence makes the HICP a subset of the main CPI. The HICP expenditure covers just under 90 per cent of the total CPI expenditure and excludes mortgage interest, building materials, union subscriptions, motor taxation, house insurance (dwelling), and the non-service elements of motor and house insurance (contents). In addition, the weight of health insurance is lower in the HICP, where net rather than gross household expenditure on health insurance is used.

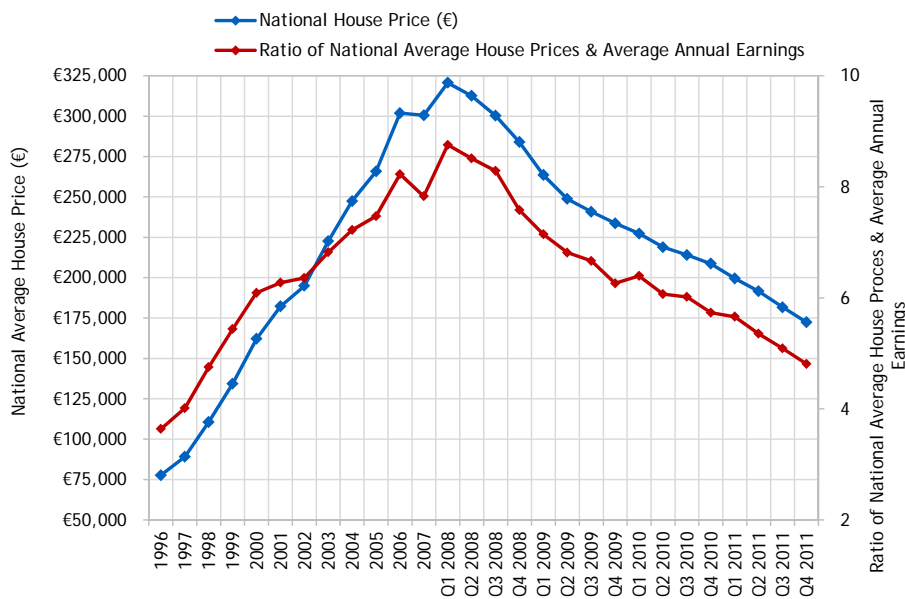
Figure 9.6 Food and Non-Alcoholic Beverages, 2005=100



The price of food and non-alcoholic beverages in Ireland have increased at a slower rate than the other benchmarked countries, representing a competitiveness gain. These changes, however, must be viewed in the context of overall price level for food and non-alcoholic beverages. Data from Eurostat has shown that in 2009 Ireland was the fourth most expensive country among the EU27 for food and non-alcoholic beverages¹⁴⁷.

Source: Eurostat, Harmonised Index of Consumer Prices

Figure 9.7 Affordability of Irish House Prices, 1996-Q4 2011

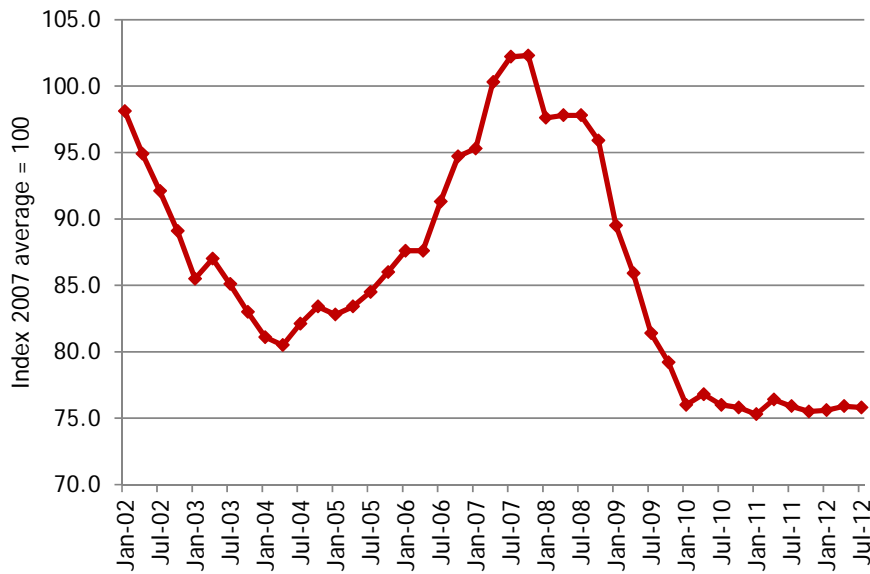


Since the bursting of the construction and property bubble, house prices have adjusted downwards and consequently have become more affordable when expressed as a ratio of average earnings. It is estimated that house prices are now five times the average annual earnings.

Source: Bank of Ireland Irish Residential Property Review, CSO EHECS Survey

147 Eurostat, Statistics in Focus, 30/2010. Available at URL: http://epp.eurostat.ec.europa.eu/portal/page/portal/product_details/publication?p_product_code=KS-SF-10-030

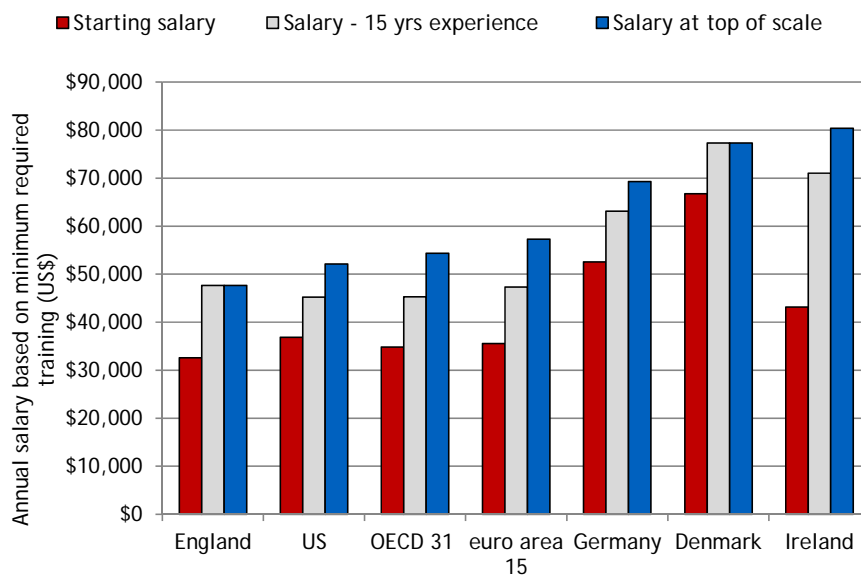
Figure 9.8 National Rental Index, April 2012 (2007= 100)



Rental values declined sharply between 2007 and the end of 2009. Since then rent prices have stabilised nationally, at approximately 25% below peak 2007 levels. Average monthly rent in Cork and Dublin are increasing on an annual basis, while outside the main cities, average monthly rents are declining. The total number of rental properties on the market fell for the third consecutive year¹⁴⁸.

Source: Daft.ie, Rental Report, Q2 2012

Figure 9.9 Primary School Teachers' Salary, US\$, 2010¹⁴⁹



This indicator details primary school teachers' salaries for a range of comparators. In 2010, the starting salary of a primary school teacher in Ireland was more than 20% higher than the OECD and euro area averages. At the top of the scale the differential is greater- where salaries in Ireland are 48% higher than OECD average and 40% higher than euro area average.

Source: OECD, Education at a Glance 2012, Forfás calculations

148 The rental index is based on asking rents for properties advertised to let on Daft.ie. Figures are calculated from econometric regressions, which calculate changes in price that are independent of changes in observable measures of quality, such as location, or bedroom number. For further details, see Daft.ie, Rental Report, Q2 2012

149 Data is based on OECD, Education at a Glance, Table X2.3a (Teachers' salaries in national currency, minimum training) and OECD.StatExtracts exchange rate data for 2010. This methodology does not apply purchasing power parity to national data. Euro area 15 excludes Cyprus and Malta. OECD 31 excludes Israel, Mexico and Turkey.

Figure 9.10 Remuneration¹⁵⁰ of Hospital Nurses, US\$/US\$ PPP, 2009 and 2010

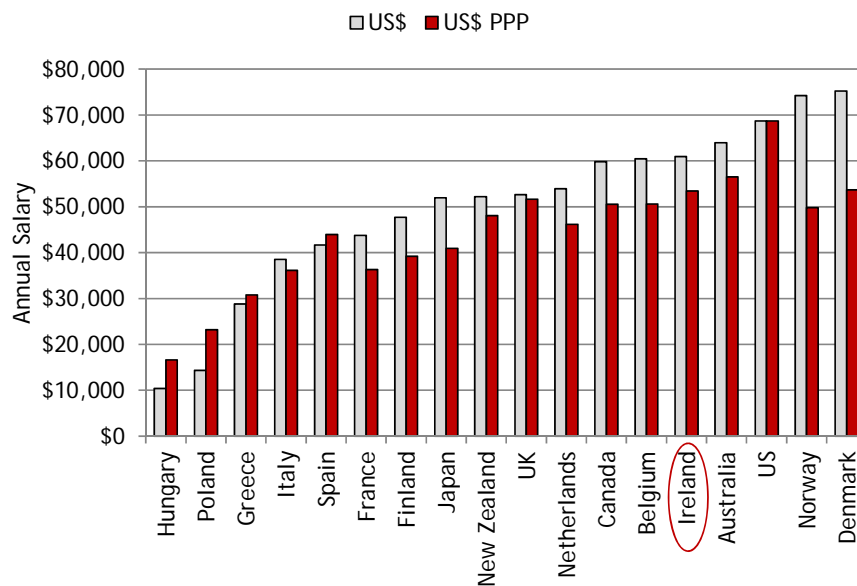
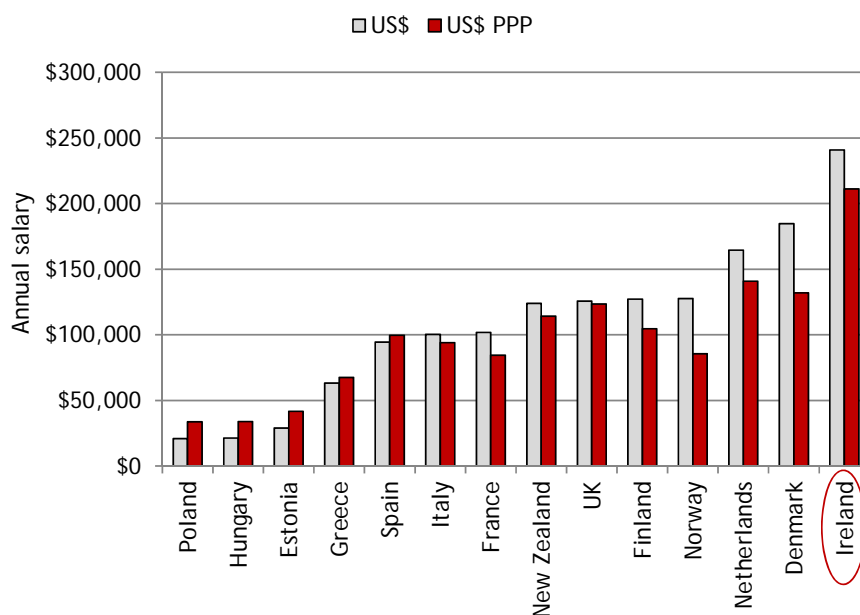


Figure 9.10 illustrates gross salary data for nurses in both dollar terms and adjusted for the cost of living (i.e. PPPs). Irish salaries are amongst the highest in the OECD. Figures for Ireland relate to 2010. As data for all countries is provided on a gross basis, and does not take into account differences in tax regimes across countries that affect the take home pay of these individuals, or variations in hours worked.

Source: OECD, Health Data 2011

Figure 9.11 Remuneration of Health Specialists¹⁵¹, US\$/US\$ PPP, 2009 and 2010



This indicator examines gross annual remuneration for health specialists for a number of OECD countries. Based on this data, health specialists in Ireland are the highest paid in the OECD (for countries where data is available) in both dollar terms and adjusted for cost of living.

Source: OECD, Health Data 2011

150 Remuneration is defined as the average gross annual income, including social security contributions and income taxes payable by the employee. Data relates to certified/registered nurses actively practising in public and private hospitals and who receive most of their income via a salary.

151 Remuneration is defined as the average gross annual income, including social security contributions and income taxes payable by the employee. Data relates to fully-qualified physicians who have specialised and work primarily in areas other than general practice. The data does not take account of variations in hours worked.

9.3 Policy Focus on Broader Cost Environment

Ireland remains an expensive location in which to live and trade. We cannot just focus on tackling those costs of direct consequence to enterprise if we wish to enhance cost competitiveness and to protect living standards. Ultimately all costs, direct and indirect, have an impact upon our ability to compete internationally, and so we must relentlessly address those areas of the economy where costs are out of line with costs in our key competitors.

The public sector has a substantial impact on costs across the economy. Ultimately, every citizen and business pays for and uses the services provided by the public sector. There is, therefore, a need to maximise value for money, ensuring that public services are delivered as efficiently and productively as possible.

Measuring productivity in the non-market economy is particularly difficult. The Dutch Institute for Social Research has undertaken a detailed comparison¹⁵² of four public services (education, health care, social safety and housing) in 28 developed countries over the period 1995-2009. Looking at health, the report compares health outcomes (combined measures of life expectancy, healthy life years and infant mortality), health outputs (the number of consultations per person, the number of discharges from hospital, and the number of older persons who use some form of formal long-term care) and health expenditure (public and private.) While correlations between all three metrics appear relatively weak across countries, it is notable that while Ireland spends approximately 10% of GDP on health, a range of other countries, including other English speaking countries with similar systems, spend around the same (despite having older populations) but get much better outcomes. It is also notable that while Irish expenditure on health is close to the average, Ireland produces significantly less health outputs (e.g., number of consultations per person, etc.).

An OECD study measures the potential impact of a range of structural reforms that can impact directly upon productivity and can directly improve national fiscal positions while maintaining services to the public. This analysis focused on the healthcare and education sectors, and suggests that Ireland could save up to 0.25 per cent of GDP through educational reform, and more significantly, 4.8 per cent of GDP through reform of the health care system. The OECD is not prescriptive, however, in determining how such savings are to be achieved.

In September 2012, the Government published a report on public sector reform. The reform agenda consists of five main commitments to change, namely¹⁵³:

- Placing customer service at the core of everything that the public service does;
- Maximising new and innovative service delivery channels;
- Radically reducing costs to drive better value for money;
- Leading, organising and working in new ways; and
- A strong focus on implementation and delivery.

It is important now that the objectives and actions outlined in the Government's Public Service Reform plan are delivered in a timely fashion¹⁵⁴. The issue of the size and cost of the

152 The Dutch Institute for Social Research, Countries Compared on Public Performance, May 2012

153 Department of Public Expenditure and Reform, Progress on the Implementation of the Government's Public Service Reform Plan, September 2012

public sector is particularly important. To date, much of the debate on public sector reform in Ireland has focused on reducing the cost of running the public sector through reductions in numbers employed. There is a need, however, to move beyond relying almost exclusively on downsizing or contraction as a vehicle to drive reform to ensure that the public sector allocates its' human resources efficiently and effectively¹⁵⁵. It is essential that Departments and Agencies have access to the necessary skill sets as well as sufficient numbers of staff to undertake their functions.

Recommendation: In order to help reduce the public sector pay bill and maximise reform, government departments and agencies should be provided with pay budgets within which they must manage headcount, rather than the current assigned headcount target approach. Such an approach would optimise the deployment of resources.

Responsibility: Department of Public Expenditure and Reform

While the progress achieved to date in implementing the programme of public service reform is welcome, alternative approaches may be required to deliver a more cost effective public service. Given the cost of the public sector wage bill, the issue of pay cannot be ignored. The data in Figures 9.9-9.11 provide some information on public sector pay levels in Ireland vis-à-vis equivalent levels in our key competitors. At present, however, the available data is limited - it does not capture the full scale of pay and pension-related developments nor is sufficient data available for many areas of the public sector. It is important that policymakers have access to comprehensive comparative, up-to-date data on public sector pay, which allows Irish public sector wage rates to be compared against international norms and against other sectors of the domestic economy. Given the need to achieve further reductions in exchequer spending, and the tough choices confronting policy makers in terms of where adjustments can be made, the appropriateness of current public sector pay rates, allowances and increments must be continually reviewed relative to productivity achieved.

9.4 Conclusion

While Ireland has already regained some cost competitiveness, further progress is required if Ireland is to return to strong economic and employment growth. To achieve a greater restoration in cost competitiveness, further price adjustment is required relative to our main competitors. It is, however, relative prices that matter from a competitiveness perspective. So long as Irish prices grow at a slower rate than prices in our competitor economies, Ireland will continue to achieve competitiveness gains.

There are risks, however. The period of deflation in Ireland appears to have come to an end and prices are rising again. A combination of domestic price increases allied to external factors such as oil prices threaten to undermine recent competitiveness gains.

154 The National Competitiveness Council previously made a number of recommendations designed to enhance public sector productivity through: the adoption of a stronger output and outcomes focus across the public sector; improving the manner in which public sector resources are allocated; and incentivising good behaviour. For more detail see National Competitiveness Council, Ireland's Competitiveness Challenge 2011, Forfás, January 2012.

155 Public Service numbers (currently 292,000) will be reduced to 282,500 by the end of 2015 from a peak of 320,000 in 2008.

It is difficult for small open economies, particularly those that share a currency with larger regions, to control their rate of price inflation, as this is, to a significant degree, determined by events outside domestic control. Nonetheless, as noted throughout this report, there are a number of policy levers available to Government which can be used to restore Ireland's cost competitiveness. Continued reductions in costs for labour, property, transport, utilities, credit, professional services and public services would exert downward pressure on overall costs and prices across the economy. Implementation of these recommendations, combined with the broader agenda to enhance productivity, would represent a major step in ensuring Ireland's future competitiveness and prosperity.

Appendix 1: Labour Market Reform Case Study

OECD research highlights that ‘Germany stands out among OECD countries as having implemented a large number of labour market reforms in the years preceding the current crisis. These reforms have profoundly changed the institutional environment of the labour market and thus help explaining the differences in labour market outcomes relative to past recessions. The reforms are likely to have reduced structural unemployment, an adjustment that is still going on, and to have offset some of the cyclical increase that would otherwise have occurred. While most commentators focus on the Hartz reforms in the period 2002-05, notably their impact on the level of benefits and on eligibility (mainly Hartz IV), reforms were much more wide-ranging, covering improvements in job placement, a general cut in unemployment benefit duration and, importantly, the phasing out of early retirement options’¹⁵⁶.

Table 2. A timeframe of labour market reforms in Germany during the last decade

Reform	Implementation Date	Main Measures	Likely Effect
Job-AQTIV	2002	Introduction of qualitative profiling of jobseekers	Improved job search efficiency
		More efficient use of ALMP	
Hartz I	Jan-03	Enlisted private firms to help workers search for jobs	Improved job search efficiency
		Tightened conditions for acceptability of jobs and introduced sanctions for unemployment benefit recipients	Raising incentives for taking up employment
		Liberalisation of temporary agency work	
Hartz II	Jan-03	Reform of small jobs, e.g. mini- and midi-jobs with limited social security contributions	Raising incentives for taking up employment
		Subsidies for unemployed who become self-employed	
Hartz III	Jan-04	Reorganisation of the Federal Employment Agency towards a more efficient service provider	Improved job search efficiency
		Simplification of active and passive policy measures	
Hartz IV	Jan-05	Merging of unemployment assistance and social assistance into the means-tested unemployment benefit II	Raising work incentives for welfare recipients (reduction in reservation wages)

¹⁵⁶ For further details, see Hübner, F. and C. Klein, The German Labour Market: Preparing for the Future, OECD Economics Department Working Papers, No. 983, 2012.

Shortening unemployment benefit duration	Feb-06	Benefit duration was cut to a maximum of 12 months for recipients up to 54 years (from a maximum of 26 months before) and to 18 months for recipients aged 55-64 years (from up to 32 months before)	Increase work incentives, notably for older workers
Phasing out of early retirement options	2006-10	Increase in age threshold for the early pension for unemployed (Altersrente wegen Arbeitslosigkeit) from age 60 to 63 from 2006 to 2008	for older workers
		Phasing out of the regulation that unemployed persons aged 58 can receive benefits without actively searching for jobs (58er Regelung) in January 2008	
		Subsidised part-time employment scheme for older employees (Altersteilzeit) closed for new entrants from January 2010	

Source: Wunsch, C. (2005), "Labour Market Policy in Germany: Institutions, Instruments and Reforms since Unification", University of St. Gallen Discussion Papers 2005-06; OECD (2008a), Economic Surveys: Germany, OECD, Paris, www.hartz-iv-iii-ii-i.de.

Appendix 2 Forfás Board Members

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Martin D. Shanahan

Chief Executive, Forfás

Mark Ferguson

Director General, Science Foundation Ireland

John Murphy

Secretary General, Department of Jobs, Enterprise and Innovation

Barry O’Leary

Chief Executive, IDA Ireland

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Chief Executive Officer, Enterprise Ireland

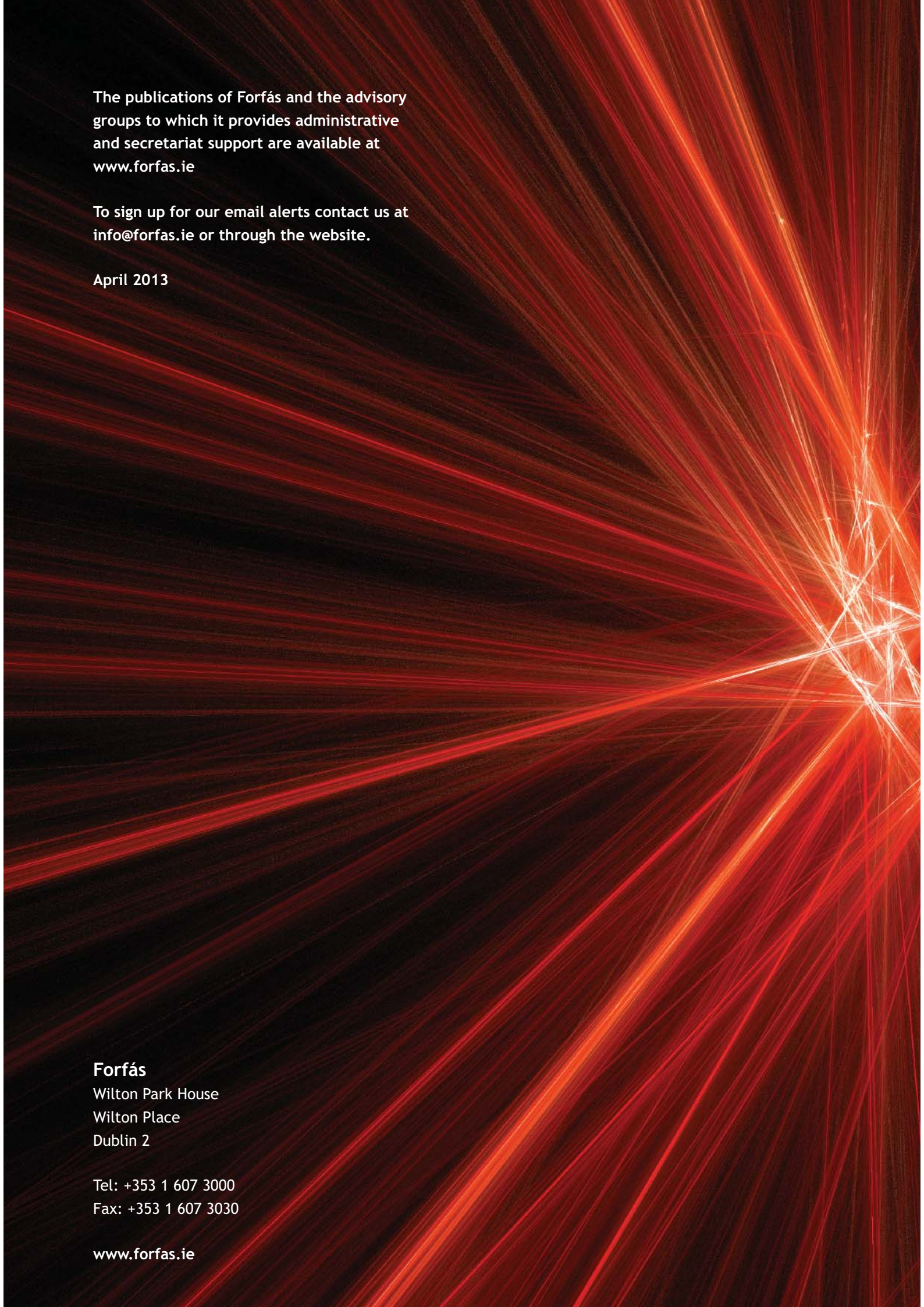
Michael O’Leary

Secretary to the Board, Forfás

Appendix 3 Recent Forfás Publications

Vacancy Overview 2012 EGFSN	February 2013
A Review of the Equity Investment Landscape in Ireland Forfás	January 2013
Regional Labour Markets Bulletin EGFSN	January 2013
A Review and Audit of Licences across Key Sectors of the Economy Forfás	December 2012
Global Entrepreneurship Monitor (GEM) 2011 Global Entrepreneurship Monitor	September 2012
Annual Employment Survey 2011 Forfás	August 2012
National Skills Bulletin 2012 NCC	July 2012
Monitoring Ireland's Skills Supply - Trends in Education and Training Outputs 2012 EGFSN	July 2012
Ireland's Competitiveness Scorecard 2012 NCC	July 2012
Forfás Annual Report 2011 Forfás	July 2012
Key Skills for Enterprise to Trade Internationally EGFSN	June 2010
Sustainability of Research Centres Advisory Science Council	June 2012
The Science Budget 2010-2011 Forfás	June 2012
Annual Business Survey of Economic Impact 2010 Forfás	June 2012

Overview of the Main Infrastructure Issues for Enterprise Forfás	May 2012
Ireland's Productivity Performance, 1980 - 2011 NCC	May 2012
Community Innovation Survey 2008-2010 Forfás, CSO	April 2012
The Irish Enterprise Funding Environment Forfás	April 2012
The Expert Group on Future Skills Needs Statement of Activity 2011 EGFSN	April 2012
Playing our Part: Statement on Horizon 2020 ACSTI	March 2012
Report of the Research Prioritisation Steering Group Research Prioritisation Steering Group, DJEI, Forfás	March 2012
Vacancy Overview 2011 EGFSN	February 2012
Guidance for Higher Education Providers on Current and Future Skills Needs of Enterprise Forfás	February 2012
Ireland's Competitiveness Challenge 2011 NCC	January 2012
Strategy for Science, Technology and Innovation Indicators Forfás	December 2011
Review of Energy Competitiveness Issues and Priorities for Enterprise Forfás	December 2011
South East Region Employment Action Plan Forfás	December 2011
Statistics at a Glance 2011 Forfás	December 2011
Report of the Advisory Group for Small Business Advisory Group for Small Business	November 2011



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