AUGUST 2017

PRE BUDGET 2018 SUBMISSION

Construction Industry Federation

CONSTRUCTION INDUSTRY FEDERATION

CONTENTS

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Key Summary Recommendations

1

INFRASTRUCTURE

- Ensure that the capital investment momentum builds firmly from Budget 2018 to 2021. A sustained investment programme in critical infrastructure over the medium-term must be considered the most vital element of Budget 2018.
- Establish a National Infrastructure Commission with responsibility for analysing the long-term infrastructural needs of the Irish economy and society, which will depoliticise infrastructure policy.
- Government should direct all additional fiscal space towards capital investment in infrastructure for the period 2018-2021. While €1.2 billion has been identified in 2018, CIF believes Government has capacity to invest more.
- Legislate to establish multi-annual capital investment targets as a percentage of GDP. Ireland currently spends less than 2% of GDP on infrastructure. Increase the rate of investment to 4% of GDP over the period 2018-2021.
- Commencing in 2019, planned contributions of €500 million per annum to the 'Rainy Day Fund' should be redirected to investment in infrastructure for the period to 2021.
- Government should explore how the existing fiscal rules of the Stability and Growth Pact could be applied more flexibly for Ireland in the current economic cycle; for example by invoking the Structural Reform Clause.
- Progress and finance the forward-planning and preparatory work for essential infrastructure projects, such as transport and water/wastewater infrastructure projects. Sustained investment in transport and water/wastewater infrastructure is an essential catalyst for economic growth.
- Ensure that the quantum of expenditure allocated to capital projects is sufficient to cover depreciation and to tackle backlogs in a number of sectors, for example in critical water and wastewater infrastructure.
- Identify and implement reforms to national infrastructure planning, particularly those necessary for making the broader infrastructure investment environment more open to private participation (e.g. PPPs). Well-targeted policy reforms can increase the quality and quantity of private investment in infrastructure: a significant complement to Exchequer financial investment. Private participation can offer funding support, accelerated project delivery and help to minimise lifecycle costs.
- Identify and reorganise new financing channels for infrastructure investment. As only the largest institutional investors have the capacity to invest directly in infrastructure projects, smaller pension funds in particular require pooled investment vehicles.
- Frame Budget 2018 against the new National Planning Frameworks which, when published later this year, will set a new strategic planning and development context for Ireland and its regions until 2040.
- Ensure project sizes are of appropriate scale to enable local domestic contractors compete for the contracts.
- Continue the good progress being made with regard to the Public Works Contract, so that the contract becomes a fair and equitable document for the industry.
- Review the delivery mechanisms of the Local Infrastructure Housing Activation Fund (LIHAF) to ensure continued investment contains the flexibility for desired impacts. Builders are experiencing difficulty with some of the unfeasible terms and conditions attached to funding.

2

HOUSING

- The Help to Buy (HTB) scheme has been a significant contributor to the growth in residential construction activity. An early withdrawal of this scheme would have a detrimental impact on confidence and the ability of house builders to maintain and increase their residential building programmes. The variation in new house price data between the latter half of 2016 and the early part of 2017 indicates an increase in the number of new houses/units coming to market being purchased at the lower first-time buyer price point.
- Review construction costs: for example, use Local Property Tax to replace Section 48 Development Levies and introduce a temporary VAT rate of 9% for the provision, construction, renovation and alteration of housing for a two-year period.

3

TAXATION

- Amend the 7-Year Capital Gains Tax Exemption as it encourages the retention of property with no incentive to develop the land purchased during the relevant period. This is not compatible with the desire to develop sites and restore construction activity. Provision could be made for a tiered removal of the relief of the capital gains tax liability that would arise for each unexpired year where a relevant asset which benefited from these reliefs is disposed of.
- Consider the introduction of incentives to restore viability to vacant/underutilised town and village centre sites, including commercial rates relief and enhanced capital allowances for a specific quantum of development on a town/ village and regional basis. This could include extending the Living City Initiative.
- The effective tax rate for rental income should be reduced by exempting rental income from PRSI and USC, and by allowing a tax credit in respect of local property tax paid.
- Immediately restore a 100% tax deduction of the interest expense incurred on loans to acquire/ develop residential property for rental purposes.

4

JOBS, EDUCATION & TRAINING

- Maintain the level of employer contribution to the National Training Fund (NTF) at 0.7 % of reckonable earnings. This is in line with a CIF submission to the DPER regarding its recent consultation entitled "Proposed Exchequer – Employer Investment Mechanism for Higher Education and Further Education & Training".
- Redirect the bulk of the NTF to support training for those in employment as current unemployment levels no longer warrant 70% of this allocation.
- Make funding available for a campaign to attract young people to work in the construction sector to ensure talent is available to deliver on the infrastructural requirements of the State.
- Currently, apprentices undertaking construction-related training programmes must pay a levy of €2,750 for tuition in Phases 4 and 6. This does nothing to encourage the much desired intake of apprentices. It is recommended that this apprenticeship levy be abolished for all construction-related training programmes.
- SOLAS is experiencing difficulties recruiting Instructors for certain apprenticeship categories – this is especially so for Electrical Instructors. To achieve the growth expected in the economy and deliver particularly on FDI projects, it is vital that there are sufficient resources to train the required apprentices in this field. Additional funding should be made available to make these positions more attractive to highly skilled Instructors.
- Restore eligibility to partial rebate for statutory redundancy payments having regard for workplace structure. Encouraging employers to directly employ staff is key for the industry. Otherwise with a disjointed industry where training of apprentices and skills are lost to fragmented employment structures and recruitment agencies, ultimately quality is impacted upon.

5

SUPPORTS FOR SMALL AND MEDIUM SIZED ENTERPRISES

- Improve access to finance for construction SMEs through the introduction of a Small Builders Fund. This could be modelled on the Home Building Fund introduced in the UK in 2016. The Home Building Fund in the UK is designed for small builders by supporting them to access the development finance they need to get building and grow their businesses.
- Restore higher levels of R&D support targeting the SME sector using initiatives such as the Small Business Innovation Research fund. The share of innovation expenditure by small firms remains just above 13 percent in Ireland. Promoting innovation in construction through expansion of Government support for SME-driven R&D, including direct funding measures, and non-bank financing will help increase dynamism across the industry and the domestic economy.

> *"Improve access to finance for construction SMEs"*

Economic Context

ECONOMIC CONTEXT

Increasing infrastructure investment is imperative for the sustainable and balanced development of Ireland's economy and society. The Irish population has grown by 30% in one generation and our economy is the fastest-growing in the EU for the last four years.

However, capital investment has reached a long-term average low of around 2 per cent GDP since 2008; down from 5 per cent throughout the early 2000s. Ireland is now the bottom-ranking EU country in terms of capital investment, and successive EU Commission reports have highlighted infrastructural deficiencies as a threat to Ireland's long-term growth.

After nearly a decade of underinvestment, Ireland's infrastructure is increasingly inadequate for its economy and society. A higher proportion of the reduced investment parcel is spent on repairing and renovating our existing infrastructure, rather than on the transformative construction that would underpin Irish economic growth and global competitiveness for the next 30 years. Frustratingly, the Government is curtailed from increasing capital investment by EU fiscal constraints; despite the availability of low-interest funding including the EU's own Juncker Fund.

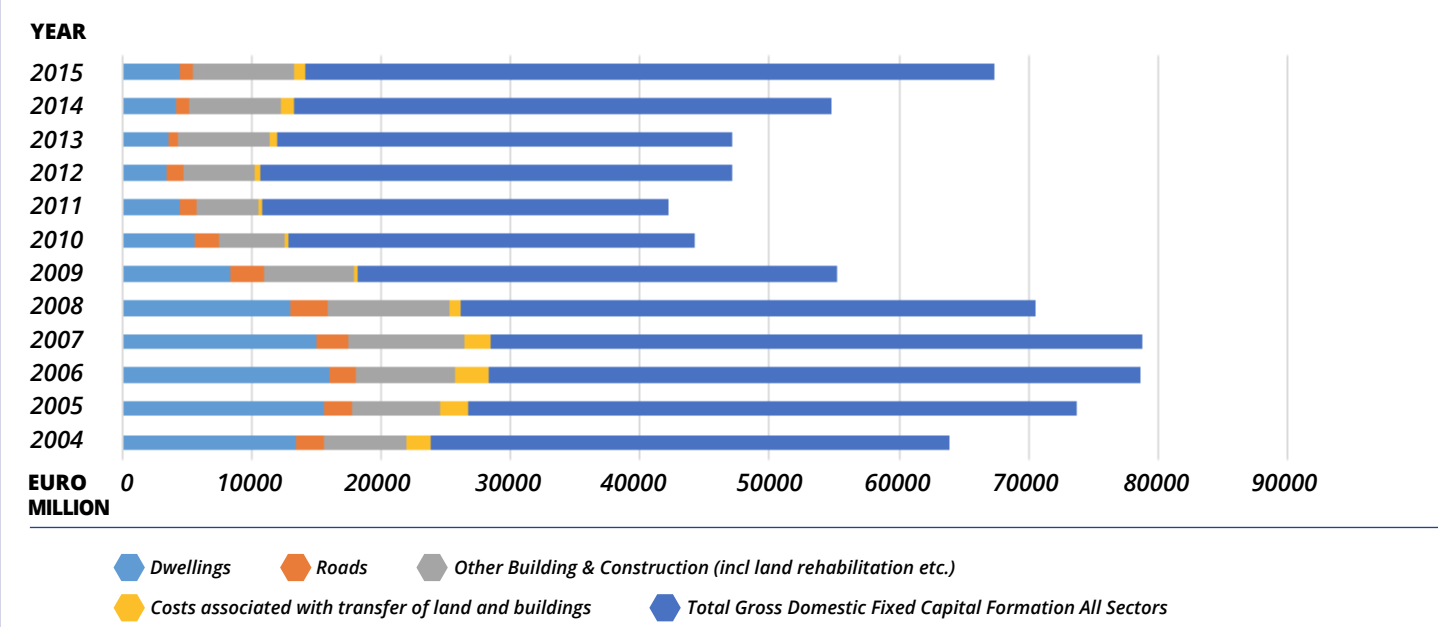
Ireland's economy and population are among the fastest-growing in the EU. The underlying general government deficit has fallen from a peak of 11.5 per cent in 2009, to a projected 0.4 per cent in 2017. GDP growth in 2016 was 5.2 per cent: the highest rate in the European Union. GDP is projected to grow by 4.3 per cent in 2017. However a decade of underinvestment has resulted in shortages of accommodation and inadequate infrastructure.

The economy is projected to grow by a further 3.7 per cent in 2018, driven primarily by the ongoing recovery in the domestic economy. The European Commission is forecasting that the Irish economy will be amongst the fastest-growing economies in the European Union this year and next. Over the medium-term, the economy is assumed to move broadly in line with its potential growth rate of around 3 per cent per annum. As the economy continues to grow, a risk to the downside is that infrastructure bottlenecks and skills shortages will continue to emerge and put Ireland's economic growth capacity in jeopardy.

See Figure 1 below.

Measures taken in Budget 2018 should be focused on building longer-term growth and capacity across all sectors of the economy. The unprecedented need for infrastructure investment, especially in areas such as housing, water and transport, is not subject to debate. Figure 1 illustrates the level of Gross Domestic Physical Capital Formation per annum since 2004. Government is not in a position to fund all of the necessary infrastructure by traditional means, and must therefore examine new options for investment.

Figure 1:
Gross Domestic Physical Capital Formation at Constant Market Prices by Item & Year



Source: CSO

The Nevin Economic and Research Institute (NERI) has recently published new research[1] on public spending in Ireland relative to that of similar EU countries. The Institute states that:
'on a no-policy-change-basis the Republic is scheduled to have one of the lowest spending-to-output ratios in the entire EU by 2021 [...] Most significantly from the perspective of the Republic's long-run productive capacity are the under-spends in education, in infrastructure, and in research and development (R&D).'

The CIF believes that today's lack of investment threatens tomorrow's economy and society. Capital investment is the critical enabler for economic growth and competiveness. It allows infrastructure to expand and industry to innovate. Although the total Exchequer capital provision is projected to reach 2.7 per cent of GNP in 2021, it is still below the average of 3.8 per cent recorded over the 2000-2016 period. Without appropriate and timely investment in critical infrastructure there will be an escalating human cost.

Brexit raises pertinent challenges and issues for the domestic economy. Despite this, the ESRI has called on policymakers to retain their focus on other key issues such as competitiveness, taxation and infrastructure over the short-term. Brexit may impact on the reprioritisation of projects but this will depend on the level of risk Brexit is perceived to post to economic growth over the long-term.

The *Summer Economic Statement* published in July 2017 by the Departments of Finance and Public Expenditure and Reform states that Irish consumption per capita is projected to exceed its pre-crisis peak towards the end of the forecast horizon, while underlying investment as a share of GDP is assumed to revert to more normal levels. In addition, the Capital Plan is now being reviewed to ensure that capital spending remains aligned with national economic and social priorities, consistent with Programme for Partnership Government objectives. This includes examining how available capital funds can best be allocated to underpin sustainable medium-term economic growth and future growth potential. It is within this economic context that this pre-Budget submission is framed.

While a review of the Capital Plan is fully welcomed, the decision to make a public investment in critical infrastructure is typically a decision to direct resources away from current consumption and investment in order to benefit people in the future. In other words, the real cost of the infrastructure is not money that is taken away from the future, but resources not devoted to consumption today. Governments face choices about whether funding for infrastructure should come through borrowing, taxation, or some other source. These are heavy political considerations involving all governments, in all countries, the world over. CIF contends that increased investment in public infrastructure can sustainably lift economic growth. In its empirical analysis, the IMF finds that an exogenous investment shock of 1 per cent of GDP raises output by 0.4% that year and 1.5% four years after the investment.[2] Furthermore, in a study for the OECD, Mourougane et al. estimate the short-term impact on growth of a debt-financed stimulus to be almost twice that of a budget-neutral stimulus.[3]

The IMF[4] reported in June 2017 that Ireland should be maintaining sufficient room for growth-enhancing capital spending within the envisaged deficit-reduction strategy. The IMF welcomed the ongoing expenditure review which is intended to enhance capital planning and expenditure prioritisation. The European Investment Bank (EIB) has also stated that infrastructure is an essential pillar that interconnects internal markets and economies. Infrastructure projects play an important role in economic growth, sustainability and job creation, as well as ensuring competitiveness.

The total remaining unallocated provision for capital formation (i.e. investment in infrastructure) of €1.52 billion over the period 2018-2021 is very modest and will not materially add to the Exchequer public capital framework over the next four years, especially as much of this investment is pre-committed. Worryingly, the reduced level of public capital investment is most acutely felt in the civil engineering sector.

In May 2017 the CIF made a submission on the Mid-Term Review of the Capital Plan 2017 to the Department of Public Expenditure and Reform. The submission contends that funding for infrastructure can be increased by unlocking new funding streams such as increasing user charges, capturing property values, and selling assets and recycling the proceeds for new infrastructure. The fiscal rules that were introduced during the economic crisis in Europe are aimed at ensuring that spending is sustainable over the medium- and long-term. However, these rules restrict the ability of the State to invest for productive purposes. See revised net fiscal space set out in Table 1 as per the *Summer Economic Statement*. Pre-committed expenditure does not include the extension to the Lansdowne Road Agreement.

[1] Public Spending in the Republic of Ireland: A Descriptive Overview and Growth Implications, T. A. McDonnell & P. Goldrick-Kelly, June 2017, NERI WP 2017/No 46 (p. 4).

[2] IMF, 2015. 'Making public investment more efficient', IMF Policy Papers, available at http://www.imf.org/external/np/pp/eng/2015/061115.pdf

[3] A. Mourougane et al., 2016, 'Can an increase in public investment sustainably lift economic growth?', OECD Economics Department Working Papers, no. 1315, p.7 and p.23, available at https://www.oecd.org/eco/Can-an-increase-in-public-investment-sustainably-lift-economic-growth.pdf

[4] IMF, Ireland Staff Report for the 2017 Article IV Consultation, June 2017
http://www.imf.org/en/Publications/CR/Issues/2017/06/26/Ireland-2017-Article-IV-Consultation-Press-Release-and-Staff-Report-45006

Table 1: **Calculation of Fiscal Space**						
		2018 as at Budget 2017	**2018**	**2019**	**2020**	**2021**
a.	Reference Rate %	3.1	3.5	3.6	3.5	3.4
b.	Convergence Margin %	1.7	2.3	0.0	0.0	0.0
c.	Applicable Benchmark % [a-b]	1.5	1.2	3.6	3.5	3.4
d.	GDP Deflator %	1.1	1.3	1.5	1.7	1.7
e.	Permitted Expenditure Growth %	2.6	2.4	5.1	5.2	5.1
f.	Corrected General Government Expenditure Aggregate (year t-1) €bn	69.7	69.7	71.1	73.2	75.6
g.	**Gross Fiscal Space €bn (e*f/100)**	1.8	**1.7**	**3.6**	**3.8**	**3.8**
h.	Discretionary Revenue Measures €bn	0.5	0.5	0.5	0.5	0.5
i.	Adjusted Fiscal Space €bn [g+h]	2.3	2.1	4.1	4.3	4.4
j.	Pre-committed Expenditure €bn	0.8	0.6	0.6	0.6	0.8
k.	Other €bn	0.3	0.2	0.4	0.3	0.2
i.	**Revised Net Fiscal Space €bn [i-j-k]**	**1.2**	**1.3**	**3.2**	**3.4**	**3.4**

Source: Summer Economic Statement 2017

The fiscal rules make no differentiation between capital expenditure and current expenditure with regard to their impacts on the budget deficit: each euro spent on capital and current expenditure is treated equally. The 'Golden Rule' is a fiscal principle according to which deficits are allowed if they have been driven by capital investment. Under this approach, current expenditure should match normal revenue, and capital expenditure would be isolated from consideration with respect to the deficit. The Rule would therefore provide member states with greater leeway to borrow for investment. Applied sensibly, the Rule could result in leeway for countries such as Ireland.

In June 2014, in order to support increased investment levels and to encourage structural reforms, the European Council agreed there was a need to explore how the existing rules of the Stability and Growth Pact (SGP) could be applied more flexibly without changing them. Following the European Council's guidance, the European Commission issued a communication on 'Making the best use of the flexibility within the existing rules of the SGP' in January 2015.[5] The outcome of this was that the Commission emphasised the Structural Reform Clause. This clause allows a state to apply for a temporary deviation of up to 0.5 per cent of GDP from the state's Medium-Term Objective (MTO), provided that the state is not in the Excessive Deficit Procedure (EDP). The state's planned reforms must be major, have a long-term impact on growth and budgetary sustainability, and must be fully implemented. The Structural Reform Clause could be invoked until Ireland reaches its MTO.

Infrastructure will continue to be central to delivering the Government's economic objectives, but it is also key to delivering the country's social and environmental objectives. Lack of infrastructure limits economic opportunities for businesses, but more critically it impacts on the livelihoods of current and future generations of citizens.

Notwithstanding the social and environmental benefits arising from investment in infrastructure, research undertaken by the NERI[6] found that investment in infrastructure has two principal economic effects:

1) *an increase in demand where increased employment in the construction sector leads to increased spending in the wider economy; and* ***2)*** *a long-term supply-side effect where an increase in the stock of infrastructure increases the productivity and output capacity of the economy. The research finds that an investment stimulus of €1bn for one year would create approximately 16,750 short-term jobs and between 675 and 850 long-term, sustainable jobs. Due to greater tax revenues due to higher GDP, the net cost of a €1bn investment is €575 million. This is found to be self-financing,*

[5] Making The Best Use of the Flexibility within the Existing Rules of the Stability and Growth Pact, Communication from the Commission to the European Parliament, the Council, the European Central Bank, the Economic and Social Committee, the Committee of the Regions and the European Investment Bank (December 2015), http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A52015DC0012

as the long term increase in tax revenue more than offsets the interest payments on the initial capital outlay. Overall the case for an increase in public investment is compelling.

Pereira and Pinho[7] investigated the long-term effects of capital investment for twelve countries, including Ireland. In their research they concluded that Irish public investment pays for itself, and leads to an increase in GDP, therefore reducing investment is an ineffective way to close a deficit. They also found that a €1 million investment led to an accumulated job creation total of 84 jobs, equivalent to 2.8 permanent full-time jobs lasting 30 years.

Both the private sector and Government have important roles to play in infrastructure funding. Most public infrastructure does not have adequate commercial opportunities to be fully self-funding. It is then the responsibility of Government to invest in the infrastructure needed, and Government's responsibilities in this respect affect all aspects of its citizens' day-to-day lives.

A report prepared by PWC in 2011 examined new financing models for funding infrastructure in Australia.8 This was in response to the Australian Grattan Institute's report 'Australia's Productivity Challenge' (2011). PWC state:

'With limited infrastructural funds the issue becomes one of prioritisation and innovative structuring to provide the optimal mix of public and private finance to maximise leverage from the State's investment in order to fund more of the project backlog.'

Government could examine other sources of funding for public infrastructure, examples are set out in Table 2 below:

Table 2: **Sources of Funding for Public Infrastructure**

1.	**European Investment Bank:** lending to infrastructure projects is a cornerstone of the EIB's lending objectives. The EIB has provided financing for viable projects in transport, energy, water, health, education and urban sectors. Speaking in 2016, the Vice President of the EIB, Mr. Andrew McDowell said "Ireland is still not yet at the forefront of the EU countries in deploying EIB financial instruments to support investment, particularly under the Investment Plan for Europe. Notwithstanding the evident infrastructure gaps and other pent-up investment requirements, total EIB exposure to Ireland remains, as a percentage of GDP, below the EU average. Our first term report would probably read 'could do better'."[9]
2.	**European Fund for Strategic Investment (EFSI):** Government should aim to secure as much additional funding as possible for infrastructure investment from the EFSI in transport, environment, health, energy, social housing and SME financing.
3.	**Public Private Partnerships:** PPP arrangements provide for long-term strategic planning of infrastructure projects off-balance sheet, while also facilitating social and economic development. The private sector has the expertise to design and build complex infrastructure projects. Effective partnerships with the private sector help to leverage capital, build in greater efficiencies and maximise economic impact. Government has to consider the bankability of each project so that a PPP is successful. Bankability refers to the overall structure of the project being such that lenders are prepared to finance it. A PPP project yields value for money if it results in a net positive gain to society and costs less than the best realistic public sector project alternative. Government could consider a PPP model which identifies an investor(s) (typically providing equity investment and debt finance) for a project and then subsequently novates this finance element to a contractor by traditional procurement, or by design and build.
4.	**Capital Receipts:** The proceeds from the sale of the Government's stake in AIB should be directed towards investment in critical infrastructure.

[6] An Examination of the Effects of an Investment Stimulus, R. O'Farrell, July 2012, NERI WP 2012/No 4.

[7] Pereira, Alfredo Marvao and Maria de Fatima Pinho (2011) 'Public Investment, Economic Performance and Budgetary Consolidation: VAR Evidence for the First 12 Euro Countries,' Journal of Economic Development, 36(1): 1-20.

[8] See PWC Report: https://www.pwc.com/gx/en/psrc/pdf/time-for-a-new-approach.pdf

[9] IEuropean Movement Conference: Investing in Ireland's Infrastructure, Mr. Andrew McDowell, Vice President EIB, 30 September 2016.

Construction: a Pillar for Growth

The overall volume of construction output increased by 12.5 per cent in 2016 to around €15billion (6.9% of GNP), with growth of 8.5 per cent forecast in 2017 and 7.1 per cent for 2018. The average annual growth rate in the period 2016-2020 is projected at 9.1 per cent. The volume of construction output by 2020 is forecast to reach €20.2 billion (in 2015 prices), or just over 10% of GNP, subject to available infrastructure investment.

Ireland needs a sustainable supply of infrastructure to support this growth. The construction industry plays a critical role in delivery of necessary infrastructure. However, the industry is facing a number of direct and indirect impediments which include: uneven distribution of projects in the pipeline; current levels of construction costs and risk; availability of skilled workers; access to development finance; and a delay in the delivery of construction projects on account of planning, regulatory and infrastructure connectivity issues. The Government will unveil a new National Planning Framework by the end of 2017. With a projected population increase of 1 million persons in Ireland by 2040, and an increasing risk to sustainable economic development posed by climate change, it is hoped that this Framework will be a successful driver of plan-led growth, supported by investment, across all Irish regions up to 2040.

The NPF will provide the framework for future development and investment in Ireland, providing a long-term and place-based aspect to public policy and investment It alsoaims to coordinate sectoral areas such as housing, jobs, transport, education, health, environment, energy and communications, into an overall coherent strategy.

The industry hopes that the NPF will be a successful driver of plan-led growth supported by the necessary investment across all regions to 2040. Budget 2018 must identify and put in place the financial framework needed to ensure successful long-term implementation of the NPF from national to regional to local levels.

The global financial and economic crisis which emerged in 2007 caused serious unemployment, but also a significant change to the industrial structure for the construction industry. The implosion in construction caused a 58% fall in construction employment between 2006 and 2011, reaching an unnatural low of 5% of total employment. The spatial distribution of this fall in construction employment has had a devastating effect on some regions in particular.

Today the construction industry accounts for 7% of GNP (2016) and employs 142,500 persons. DKM Economic Consultants have proposed that it would be prudent to plan for an industry that will provide direct employment for around 213,000 persons by 2020.

The construction industry, by its nature, is influenced by the rate of cyclical growth in the economy. This results in sustained periods of growth in the industry followed by periods of retrenchment which may result in job losses. The Redundancy Payments Act 2003 increased construction employers' liability for all redundancy costs, which in turn acts as a deterrent to direct employment periods of greater than two years, and to providing quality longer-term jobs in the construction industry. The construction sector is an entirely different sector compared to other employment sectors where the employment base for employees can be of fixed location whereas the employment base of a construction worker is where the actual construction project is at any one time. The current requirement that employers are 100% responsible for redundancy payments to employees means that construction employers are reluctant to directly hire new employees. This in turn has an adverse effect on quality, training and standards. Disincentives for recruitment of new employees which were introduced during the recession should now be reversed. Construction sector employers' entitlement to redundancy rebates should be restored on a phased basis as a minimum standard for all new employees engaged after a specified date.

The industry is committed to examining how a reduction in both the initial cost of construction and the whole-life cost of assets can be achieved. The industry is also committed to delivering a reduction in the overall time from inception to completion for new-build and refurbished assets, thereby improving efficiency and cost certainty for the client, whether public or private. Industry and Government must align across strategic development and investment plans aimed at training and upskilling the current and future workforce. The

industry has an important role in delivering a reduction in greenhouse gas emissions in the built environment, thereby helping to address the impact of climate change.

The industry calls on Government to assist in developing access to finance, education and skills, and leaner procurement to creating conditions for resilient construction supply chains to thrive. The impact of the economic downturn was particularly felt among the many small businesses that operate in the industry. The industry needs the right conditions for its supply chains to flourish and be confident about investing in new research, innovation, technology and people.

According to a global forecast for the construction industry to 2030 published by Oxford Economics, the global construction market is expected to grow at a faster pace than world GDP over the next decade as Asian economies continue to industrialise and the US recovers. Irish construction companies are well-placed to compete and thrive on the international market and may be better supported once they operate in a growth-focused economy which values and invests in innovation, research and development.

> *"The overall volume of construction output increased by 12.5% in 2016 to around €15billion (6.9% of GNP), with growth of 8.5% forecast in 2017 and 7.1% for 2018."*

The CIF, together with its constituent associations, has continually called on Government to take a lead role in prioritising investment in infrastructure by implementing the actions outlined in *'Construction 2020'* (the National Strategy for the Construction Industry published in 2014) by promoting and controlling policy implementation in complex organisational settings, such as the local government system and across the too numerous central government departments and agencies which relate to the construction industry. Government should establish a National Infrastructure Commission with responsibility for analysing the long-term infrastructural needs of the Irish economy and society, which will in turn depoliticise infrastructure policy.

Finally, to enhance the delivery of critical infrastructure and housing, the Government must reactivate the Construction Sector Group to implement the actions outlined in *'Construction 2020'* (the National Strategy for the Construction Industry published in 2014). This industrial strategy will coordinate the actions of central Government, industry, local government and State Agencies in delivering the essential construction activity Irish society requires over the coming decades. It will also develop a world-class Irish construction industry capable of delivering the needs of the domestic economy and competing for global opportunities. This high-level group should report to the Taoiseach and involve officials from the Departments of Housing, Enterprise and Finance, relevant State Agencies and senior industry leaders.

*"The CIF has continually called on Government to take a lead role in prioritising investment in infrastructure, as outlined in **'Construction 2020'**"*

Key Recommendations for inclusion in Budget 2018

1 INFRASTRUCTURE: FOSTER A SUSTAINED PROGRAMME OF INVESTMENT IN INFRASTRUCTURE

- Infrastructure investment needs to be substantially increased. A sustained investment programme in critical infrastructure must be considered the most vital element of Budget 2018. Investment momentum should progress firmly from Budget 2018 onwards.
- Ireland spent the least on 'general government fixed investment' (capital investment) amongst all EU countries, as a percentage of GDP, at 1.7 per cent in 2015. By comparison, similar European partner countries spent in the order of 3.9% (Denmark), 3.6% (France) and 2.8% (UK) on fixed capital investment in 2015 (source: Eurostat). Government should legislate to establish multi-annual investment targets as a percentage of GDP. These targets would set out the rate of investment Government is obliged to deliver. At a minimum, Government should aim to increase the rate of capital investment to 4% of GDP over the period from 2018 to 2021.
- Increased Public Capital Programme provisions to address infrastructural deficits and support future economic growth are likely to receive careful scrutiny from any domestic or international investor considering investment in Ireland and its regions.
- The quantum of expenditure allocated to capital projects should be sufficient to cover depreciation and tackle the backlog in a number of sectors, for example in water and wastewater infrastructure.
- Implementation of the new National Planning Framework (NPF) must be firmly supported by a long-term, multi-annual capital investment plan for it to succeed. Budget 2018 must be framed against the new NPF, which when published later this year will set a new strategic planning and development context for Ireland and its regions until 2040.
- Explore how the existing fiscal rules of the Stability and Growth Pact could be applied more flexibly; for example by invoking the Structural Reform Clause (which allows a state to apply for a temporary deviation of up to 0.5% of GDP from the state's Medium Term Objective, provided the state is not in the Excessive Deficit Procedure (EDP)) and the Investment Clause.
- Identify and implement reforms around national infrastructure planning needed to make the broader infrastructure investment environment more open to private participation (e.g. PPPs). Well-targeted policy reforms can increase the quality and quantity of private investment ininfrastructure, a significant complement to Exchequer financial investment. Private participation can offer funding support, accelerated project delivery and help to minimise lifecycle costs.
- Use public sector capital investment to leverage private sector investment by tapping into equity capital pools. Leveraging private capital (e.g. through PPPs) creates a larger pool of funding for national and local government to address infrastructural needs, whilst driving economic growth and creating jobs. The instruments and pooling mechanisms selected for investment should depend on the nature of the asset (debt, equity, listed or unlisted), regulatory and tax considerations.
- PPP arrangements provide for long-term strategic planning of infrastructure projects off-balance sheet, whilst also facilitating social and economic development. The private sector has the expertise to design and build complex infrastructure projects. Effective partnerships with the private sector help to leverage capital, build-in greater efficiencies and maximise economic impact. Government has to consider the *bankability* of each project so that a PPP is successful. Bankability refers to the overall structure of the project being such that lenders are prepared to finance it. A PPP project yields value for money if it results in a net positive gain to society and costs less than the best realistic public sector project alternative. Government could consider a PPP model which identifies an investor(s) (typically providing equity investment and debt finance) for a project, and then subsequently novates this finance element to a contractor by traditional procurement or by design and build.
- Progress and finance the forward planning and preparatory work for essential infrastructure projects, for example transport and water/ wastewater infrastructure projects. Sustained investment in transport and water/wastewater infrastructure is an essential catalyst for economic growth.

2 HOUSING: INCREASE THE SUPPLY OF NEW HOMES

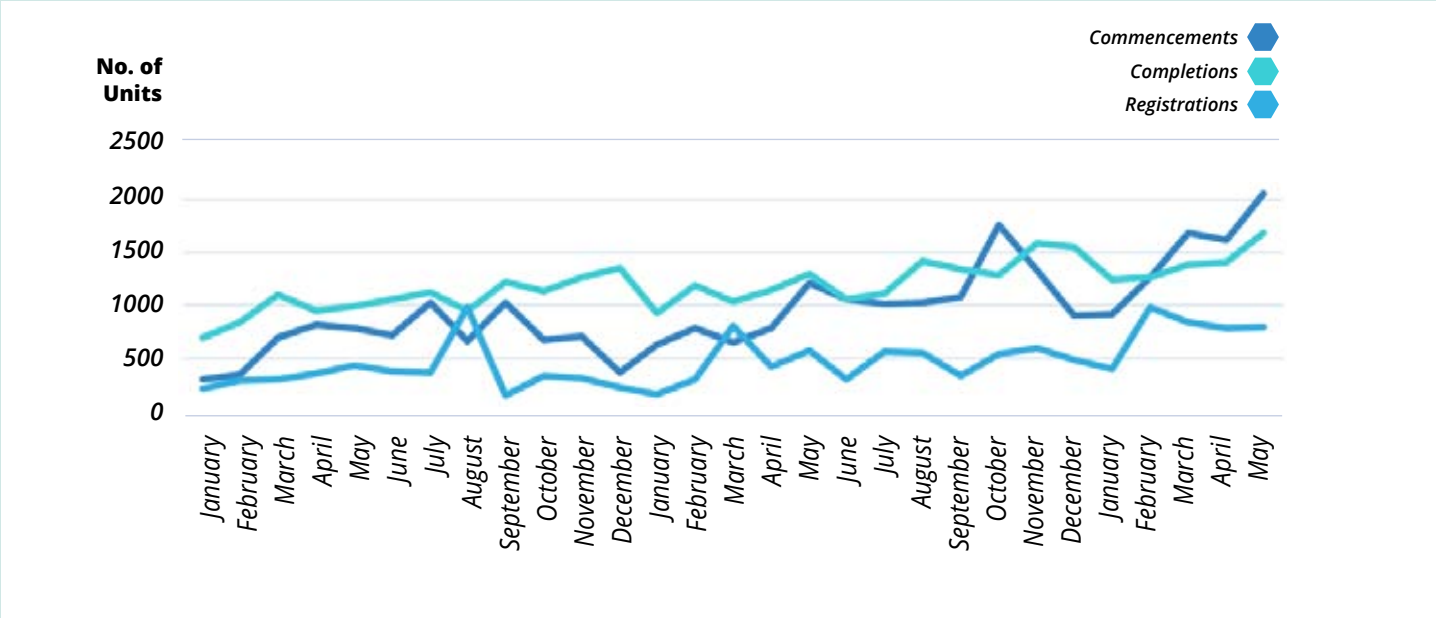
- Establish a *National Infrastructure Commission* with responsibility for analysing the long-term infrastructural needs of the Irish economy and society, which will depoliticise infrastructure policy.
- When renewing investment in water and wastewater services to fund Irish Water's investment programme, Government should ensure investment keeps pace with projected new residential construction.
- Ensure project sizes are of appropriate scale to enable local domestic contractors compete for the contracts.
- Continue the good progress being made with regard to the Public Works Contract, so that the contract becomes a fair and equitable document for the industry.
- LIHAF – the Local Infrastructure Housing Activation Fund - is in need of review so that continued investment contains the flexibility for desired impact. Builders are experiencing difficulty with some of the unfeasible terms and conditions attached to funding requirements.

- The Help to Buy (HTB) scheme has been a significant contributor to the growth in residential construction activity, as confirmed by activity indicators in Figure 2 below. A withdrawal of this scheme would have a detrimental impact on confidence and the ability of house builders to maintain and increase their residential building programmes.

  The benefit of the incentive should be assessed in terms of higher investment and growth in terms of supply of new housing units. The crisis in housing supply in Ireland warranted the temporary introduction of the HTB scheme until late 2019 to assist in: (1) the viability of new residential building, and (2) the ability of first-time buyers to purchase a new home. The variation in new house price data between the latter half of 2016 and the early part of 2017 indicates an increase in the number of new houses/units coming to market being purchased at lower, first-time buyer price points.

  See Figure 2 below.

Figure 2:
Monthly House Building Activity Indicators: Registrations, Commencements & Completions January 2015 – May 2017



Source: Department of Housing, Planning, Community & Local Government

- The ESRI has suggested that long-run housing demand in the Irish economy is now in the region of 30,000 to 35,000 units per annum. Current building activity levels could be as low as 50% of the level of new homes required. Recent Census 2016 data reveals the impact of the housing shortage on household formation and household size. The average household size increased to 2.75 in 2016 (up from 2.73 in 2011) and the rate of new household formation slowed considerably. The principal reason why so few homes are being built is the high cost of construction, and infrastructural deficits.
- The National Competitiveness Council[10] reports that:

  'From a competitiveness perspective, the supply and affordability of residential housing is a component of Ireland's ability to compete internationally [...] The shortage of housing in Ireland remains an impediment both to attracting mobile inward investment and to the expansion of operations by enterprises, and is a critical infrastructure support to job creation in both Dublin and the regions. Despite an increase in construction activity and planning permissions, residential property supply remains constrained. Continued strong demand means that property price inflation is likely to continue in the short term without additional supply becoming available.'
- The market value of new homes in many areas is below the replacement and/or all-in construction cost. For any recovery in building activity to take place the following is required: a combination of rising house prices; enhancement of buyers' ability to secure mortgages and assemble the required deposits; reduction in residential building costs; and funding of essential infrastructure required to open up significant land banks for residential development.

- Review construction costs in line with the recommendations arising from the Department of Housing, Planning, Community and Local Government's *Housing Construction Cost Study* (forthcoming).
- Introduce a temporary reduction in VAT. A temporary VAT rate of 9% should be introduced for the provision, construction, renovation and alteration of housing for a two-year period.
- Use Local Property Tax to Replace S48 Development Levies. As local property tax has been introduced since the current development levy mechanism was provided for in the Planning and Development Act 2000, there is a strong argument that the market value of new residential development upon which the local property tax is based results in a double taxation of newly built homes. Property tax should replace the current development levy contributions for residential development payable under Section 48 of the Planning and Development Act 2000 as amended. This would reduce the overall up-front construction costs of new residential buildings, improve affordability and initiate a real recovery in residential construction activity. Currently, purchasers of newly built residential units are being asked to fund the provision of public services via the development levies paid, and at the same time, pay the local property tax which is assessed on the market value of their new home which is strongly influenced by the services paid for by the S48 development levy. Accordingly, Section 48 development levies pertaining to new residential properties that are subject to local property tax should be abolished.

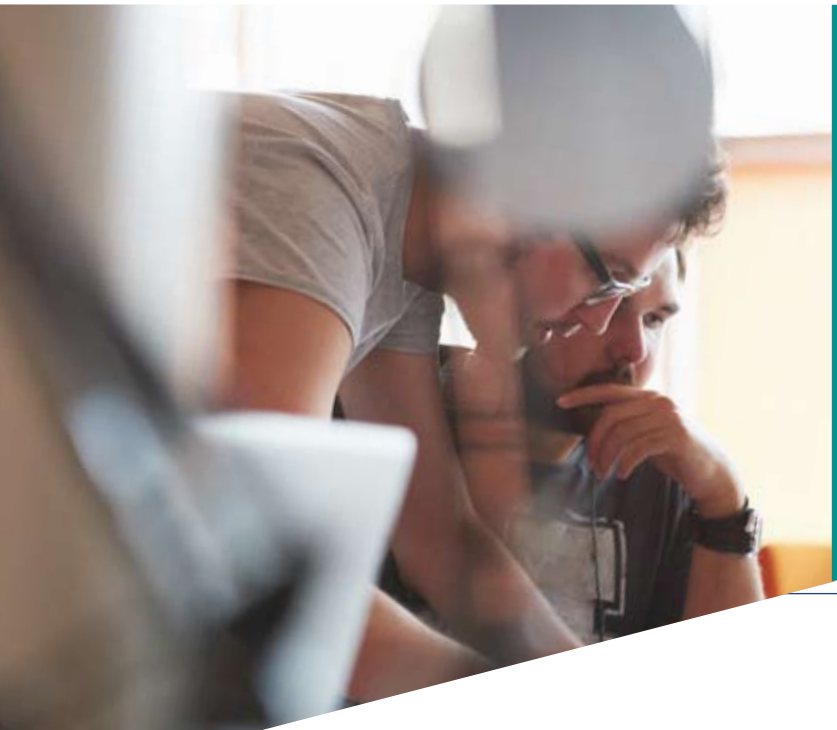
[10] NCC, 'Costs of Doing Business in Ireland 2017', June 2017, pg.6.

3 TAXATION MATTERS

- Amend the 7-Year Capital Gains Tax Exemption: An unintended consequence of a seven year capital gains tax exemption is that it encourages the holding of property – there is no incentive to develop the land purchased during the relevant period. This is not compatible with demand to develop the sites and restore construction activity. To address this anomaly and to encourage disposal of these lands for early development, provision could be made for a tiered removal of the relief of the capital gains tax liability that would arise for each unexpired year where a relevant asset which benefited from these reliefs is disposed of. *See example set out in Appendix 1.*
- Consider the introduction of incentives to restore viability to vacant/ underutilised town and village centre sites, including commercial rates relief and enhanced capital allowances for a specific quantum of development on a town/ village and regional basis.
- The Census 2016 enumerated 198,358 vacant houses that are not being used as holiday homes across the country in both urban and rural areas. Extend the 'Living City Initiative' to target those towns with large numbers of vacant non-holiday homes, this would help to alleviate the housing shortage.
- The effective tax rate for rental income should be reduced by exempting rental income from PRSI and USC and by allowing a tax credit in respect of local property tax paid.
- Immediately restore a 100% tax deduction of the interest expense incurred on loans to acquire/ develop residential property for rental purposes.

4 JOBS, EDUCATION AND TRAINING

- Restore eligibility to partial rebate for statutory redundancy payments having regard for workplace structure. The cost of employing, training and retaining staff is significant. Encouraging employers to directly employ staff is key for the industry. Otherwise with a disjointed industry where training of apprentices and skills are lost to fragmented employment structures and recruitment agencies, ultimately quality is impacted upon.
- The redundancy rebate remains a major issue and a barrier to employment for the industry. If the Government is not in a position to restore the rebate in the current climate, a reduced redundancy payment for all newly hired employees should be considered:
  - Half week per year of service for those under 40
  - One week per year of service for those over 40
  - As it was prior to the 2003 Act
- As the construction recovers, the availability of suitably qualified personnel will be a challenge for the sector. This necessitates significant training programmes and investment by the State to ensure personnel are available to deliver on the needs of the economy. Certain actions are required now to assist / support the construction sector:



> *"Encouraging employers to directly employ staff is key for the industry"*

- The National Training Fund (NTF) is mainly resourced by a levy on employers of 0.7% of reckonable earnings of employees in certain employment classes, which is collected through the PAYE/PRSI system.
  - Government should maintain the level of employer contribution at 0.7 % of reckonable earnings. This is in line with the CIF submission to the DPER regarding its recent consultation entitled "Proposed Exchequer – Employer Investment Mechanism for Higher Education and Further Education & Training"
  - Government should redirect the bulk of the NTF to support training for those in employment, now that unemployment levels no longer warrant 70% allocation.
  - Funding to be made available for a campaign to attract young people to work in the sector to ensure talent is available to deliver on the infrastructural requirements of the State.
  - Currently, apprentices undertaking construction related training programmes must pay a levy of €2,750 for tuition in Phases 4 & 6. This does nothing to encourage the much-needed intake of apprentices. It is recommended that this apprenticeship levy be abolished for all construction-related training programmes.
  - It has come to the attention of CIF that SOLAS is experiencing difficulties recruiting Instructors for certain apprenticeship categories – this is especially so for Electrical Instructors. To achieve the growth expected in the economy and deliver particularly on FDI projects, it is vital that there are sufficient resources to train the required apprentices in this field. Therefore we propose that additional funding be made available to make these positions more attractive to highly skilled Instructors.

5 SUPPORTS FOR SMES: BOOST GROWTH AMONG CONSTRUCTION SMES

- Improve access to finance for construction SMEs through the introduction of a Small Builders Fund. This could be modelled on the Home Building Fund introduced in the UK in 2016, which is directed toward small builders.
  - The Home Building Fund in the UK is designed for small builders by supporting them to access the development finance they need to get building and grow their businesses. The £3bn fund provides government finance to increase the number of new homes being built in England. It combines existing recoverable investment funds, including the Builders Finance Fund, into one fund that provides borrowers with a simple application process to make it easier to borrow from the Homes & Communities Agency (HCA). The HCA has been providing loan finance to the private sector since 2008. During this time, the HCA has made loans and investments available totalling over £4.4 billion to support the private sector to build new homes and bring land forward for development. Finance from the Home Building Fund is available to draw down up to 31 March 2021. The Fund is one of the ways HCA is delivering the British Government's housing ambitions alongside the Shared Ownership and Affordable Homes programme, Starter Homes and the Single Land Programme.
- Restore higher levels of R&D support for the SME sector using initiatives such as the Small Business Innovation Research fund. The share of innovation expenditure by small firms remains just above 13 per cent in Ireland. Promoting innovation in construction through expansion of Government support for SME-driven R&D, including direct funding measures, and non-bank financing will help increase dynamism across the industry and wider domestic economy.

Appendix 1

APPENDIX 1

CAPITAL GAINS TAX EXEMPTION

Amend the 7-Year Capital Gains Tax Exemption:

An unintended consequence of the seven year capital gains tax exemption is that it encourages the holding of property – there is no requirement to develop the land purchased during the relevant period. This is not compatible with the desire to develop the sites and restore construction activity. To address this anomaly and to encourage disposal of these lands for early development, provision could be made for a tiered removal of the relief of the capital gains tax liability that would arise for each unexpired year where a relevant asset which benefited from these reliefs is disposed of.

See example set out below in Table 3.

Table 3: **Proposed Amendment to Capital Gains Tax Exemption**	
Purchase of Asset 2013 7 year period expires 2020	**€100,000**
Sale of Asset 2018 (+5 years)	**€150,000**
CGT Liability calculated as follows:	
CGT @ 33% 2 unexpired years = 2/7 x CGT rate @ 33%	**9.42%**
CGT Payable	**€4,710**
Actual Relief for CGT under the provision	**€11,790**

NOTES

Copy of CIF Submission to Committee on Budgetary Oversight and CIF Submission to the Mid-Term Review of the Capital Plan 2017.

CIF Headquarters

Construction House
Canal Road
Dublin 6

Phone 01 406 6000
Email info@cif.ie

CIF Cork

Construction House
4 Eastgate Avenue
Little Island
Cork

Phone 021 435 1410
Email Cork@cif.ie

CIF Galway

Construction House
8 Montpelier Terrace
The Crescent
Galway

Phone 091 502680
Email Galway@cif.ie

www.cif.ie
@CIF_Ireland