Irish Fiscal Advisory Council

Press Release: Fiscal Assessment Report

Managing corporation tax inflows and capacity constraints

Under embargo until **Wednesday 7 June 2023**

The Government needs to plan to manage windfalls and the keep the economy and public finances on track

The Fiscal Council's latest report assesses the Government’s medium-term plans set out in April’s *Stability Programme Update*.

Following a period of slower growth during the winter, Ireland's economy is recovering as inflation eases. Unemployment rates are at record low levels. Capacity constraints have emerged as a significant challenge. Workers are scarce, particularly in construction, and there are risks that wage and rent pressures persist.

The Government expects the underlying deficit, excluding excess corporation tax receipts, to narrow to 0.6% of GNI* this year. In 2024, the Government projects it will run its first underlying surplus in 17 years on this basis under the National Spending Rule. The net debt-to-GNI* ratio would decline by 23 percentage points between end-2022 and end-2026 (from 69% to 46%) with windfall corporation tax receipts projected to account for about two-thirds of this fall.

Exceptional inflows of corporation tax receipts from foreign multinationals are currently boosting the public finances, but are unreliable. Just three corporate groups accounted for 30% of receipts from 2017 to 2021. There is a risk this could reverse due to firm-specific factors or changes in the international tax environment. Moreover, when these receipts are spent, they inject money into the economy and add to demand as they are based on overseas profits rather than domestic activity.

The Government should stick to the National Spending Rule in 2024 to avoid overheating the economy or increasing reliance on unreliable tax receipts. Choices will need to be made between new tax and spending measures and existing spending as “Stand-Still” costs of maintaining existing policies and investment plans fully use fiscal space under the rule.

If the Government were to go beyond its own spending rule, it risks repeating the mistakes of the 2000s. It would mean using temporary revenues and corporation tax windfalls to finance permanent spending and risks fuelling further inflationary increases. With capacity constraints, scope to raise investment may be limited.

Long-term planning needs to improve, including developing more credible plans to manage ageing pressures in health and pensions and climate-related costs. These are not adequately reflected in the current fiscal projections.

Commenting on the report, Sebastian Barnes, Chairperson of the Fiscal Council, noted:

“The inflow of corporation tax receipts is helping to bring down government debt, but it needs to be carefully managed given that it is unreliable and the economy faces capacity constraints and risks overheating. The Government should follows the National Spending Rule to keep the economy and the public finances on track and to avoid repeating past mistakes. The proposed new Long-Term Savings Fund could play a key role in saving corporation tax windfalls and supporting the sustainability of the pension system in the future”.

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