highlighted in Section 1 to materialise, this would provide an upside risk to *SPU 2021* fiscal projections.

Reforms to the global tax environment represent a risk to corporation tax intake

Reforms to the global corporation tax environment also represent a further potential risk to tax revenues in the coming years. Efforts by various international organisations and stakeholders to facilitate both a global minimum corporation tax rate, along with plans to address the digitalisation of profits could see Ireland collect lower levels of corporation tax in the coming years if introduced. Against this uncertain backdrop, *SPU 2021* fiscal projections are based on the assumption that these factors will reduce corporation tax receipts by €500 million per year from 2022. It has been indicated that these losses may be higher. One risk is that a downward adjustment takes place suddenly, rather than gradually as assumed, complicating the budgetary position in specific years more severely.

Box F: Corporate tax reforms could reduce revenues

Ireland has benefited enormously from attracting large foreign-owned multinationals to set up operations on its shores. As well as generating substantial corporation tax receipts for the Government, this policy has attracted significant employment. In turn, this contributes to higher tax receipts being received from employee earnings and from wider economic activity more generally.

However, it has been recognised for some time that the reliance on tax receipts associated with these large multinationals poses risks. Recent efforts to reform the international corporation tax landscape have now gained impetus with the Biden administration's tax proposals. This adds to the concerns around the sustainability of Irish corporation tax receipts.

This box looks at the risks around corporation tax, new reform proposals, and it explores a stylised scenario of what could happen should a number of large multinationals exit Ireland.

Over-relying on corporation tax is a risk to funding spending

The Government's reliance on corporation tax has risen in recent years such that almost 21 per cent of Exchequer taxes come from corporation tax as compared to a long-run average of about 13.5 per cent. There are three risks in particular:

1) **Volatility** — corporation tax receipts are more volatile than other taxes. This also means that forecasts for corporation tax are prone to much larger errors than other taxes. Funding permanent spending on the back of volatile receipts is especially risky. It could entail a widening of deficits or a need to adjust spending downwards at a later stage should receipts fall rather than rise to ensure the public finances are on a sound footing.

2) **Concentration** — corporation tax receipts are heavily concentrated in a handful of companies. In 2019, ten corporate groups accounted for 56 per cent of net receipts. This concentration exposes the Government to risks around firm-specific profitability and various other idiosyncratic risks.

3) **Sudden reversals** — there is a risk that changes in policy regimes and circumstances globally lead to decisions for some firms to relocate. in some cases, companies may be relatively footloose meaning that they have relatively limited physical presence (workers or factories)

and can easily shift activities from one location to another. This could expose the government of the day to a large reversal of corporation tax receipts.

Assessing the risks involved with corporation tax receipts needs to reflect the full range of negative impacts that could occur, including the macroeconomic and labour-market impacts as well as the budgetary effects.

Even just five large multinationals leaving could have big impacts

Building on previous work (Box C of the *June 2018 Fiscal Assessment Report*), this box considers a scenario whereby five stylised large, foreign-owned multinational enterprises exit Ireland.

Revenue produces detailed information on large corporation taxpayers in Ireland by different groupings. Using this information, we can estimate how much tax is paid by a typical large foreign-owned multinational: about €99 million in 2019 for the top 99, rising to €456 million for the top 10 payers. Table F1 estimates a stylised large foreign-owned multinational firm based on the available Revenue data.

For the purposes of illustrating a potential shock associated with five major foreign firms exiting Ireland, we build on the stylised firm in Table F1 and assume:

- direct corporation tax losses of €3 billion (about a quarter of all corporation tax and 3.5 per cent of total government revenue);
- a shock to real GNI* of 1 per cent. As noted in FitzGerald (2015), in terms of their impact on the real economy, most of the output of foreign firms in Ireland is confined to the wage bill and the corporation tax paid on the profits; the rest of the profits are repatriated. We therefore calibrate the shock based on estimates of (1) the direct wage bill losses arising from the firm exits and (2) the indirect wage bill losses from local jobs supported. This analysis would suggest that the real economy effects would be relatively small even though the impact on tax receipts would be substantial.[49]

Table F1: Large multinationals account for significant jobs and taxes

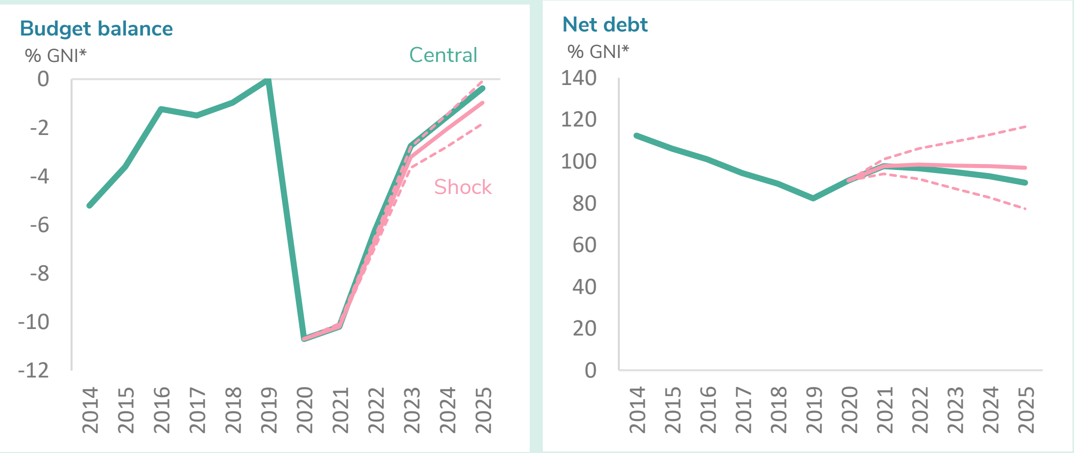
	All	Top 10	A stylised firm (estimated)
No. of Companies	99	10	1
Employments	103,822		1,049
Total staff earnings	€4,203,000,000		€42,454,545
Average wage	€40,483		€40,483
Corporation tax liability	€6,813,000,000	€6,072,000,000	€607,200,000

Source: Revenue (2021); and Fiscal Council workings.
Notes: This table looks at the larger foreign-owned multinational enterprises contained in Revenue data.

The results (Figure F1) suggest that the deficit could be wider by 0.6 to 1.4 per cent of GNI* by 2025, with the result that the net debt ratio would be on a flatter path in later years (2023–2025), falling by just 0.5 percentage points per annum as compared to 2.3 percentage points in the central scenario.

[49] Specifically, we assume 5,000 direct job losses and 15,000 indirect job losses based on Brady (2019) multiplier estimates for local jobs created. Of the direct job losses, we considered between 10–25 per cent translate to higher unemployment, 20–50 per cent to higher emigration, and the remainder re-employed at the median wage. This would suggest that a 1 per cent shock to domestic income is a reasonably conservative estimate.

Figure F1: Exits of foreign firms would widen deficits and slow debt reduction



Sources: CSO; Department of Finance; and Fiscal Council workings.

Biden and BEPS proposals are expected to reduce future FDI and taxes

Discussions on reforms of international tax rules have been ongoing under the OECD/G20 Inclusive framework on Base Erosion and Profit shifting (BEPS). As part of the BEPS 2.0 proposals, there are two 'pillar' reforms that change the global corporation tax environment. Pillar one relates to changing a share of tax collection from where firms have physical presence to where the firm's market or user is located. Pillar two relates to the establishment and enforcement of a global minimum corporation tax rate.

The Biden administration has given renewed impetus to the implementation of these reforms through recent corporate tax proposals of its own.[50] Aligning most closely with Pillar two, the Biden proposals include raising the current US Global Intangible Low-Taxed Income (GILTI) tax to a minimum of 21 per cent on profits of US corporations on a country-by-country basis and removing certain key exemptions, namely the exemption for Qualified Business Asset Investment (QBAI). The current GILTI system includes a global minimum corporate tax rate of 10.5 per cent and also allows for the higher profits paid in one jurisdiction to offset the lower profits paid in another jurisdiction, so that globally the 10.5 per cent rate is met. In addition, the proposals signal a shift from digitally-targeted tax reforms to ones that focus primarily on the largest companies.

However, the proposals will ultimately have to be passed by US congress, so their final form is uncertain. Similarly, the final form of the OECD BEPS reforms are also uncertain. As a result, it is difficult to gauge their impacts on both the macroeconomy and the public finances.

There are a number of channels through which revenues may be reduced. The location of profit booking is an important consideration for Ireland, with the shifting of profits from Irish domiciled firms naturally reducing corporation tax primarily. If firms have incentives to relocate these profits elsewhere, corporation taxes may be lower going forward.

There are also risks around the location of 'real' multinational activity in the event of changes to the global corporation tax environment. Reduced inflows of such activity in Ireland would have clear spillovers into other sectors of the economy and would impact Exchequer revenues more broadly and to a more significant extent. However, it may not have a significant impact on the current level of investment by multinational firms who already have a presence here.

The Department has estimated that some €2 billion in revenue will be lost over 2022-2025 as a result of the BEPS reforms. While tax rates are one of a number of factors multinational firms would consider when deciding where to invest, any reduction still has important implications for

[50] See the White House fact sheet on the American Jobs Plan for further details of the Biden administration's proposals: https://www.whitehouse.gov/briefing-room/statements-releases/2021/03/31/fact-sheet-the-american-jobs-plan/.

the provision of public services and the implementation of policy priorities in the coming years. Ultimately, both pillars of the OECD's framework would reduce the relative attractiveness of Ireland as a place for new US FDI, and potentially reduce direct profitability. With corporation taxes largely representing an exogenous inflow into the Irish economy, their use to fund current spending in recent years requires careful consideration in the context of a changing global taxation environment.

In addition to risks posed by the OECD and US proposals, the EU is also exploring other avenues for corporate taxation reforms. These are contained in its May 2021 communication on "Business Taxation for the 21st century" (European Commission, 2021). The proposals include new approaches to allocating taxable profits between Member States. The European Commission is also expected to set out proposals for a digital levy this summer.