## Box G: Exchequer has benefited from some €22 billion "excess" corporation tax

This box presents new analysis showing how the Exchequer has benefited from some €22 billion in corporation tax receipts in recent years, which could be considered "excess". That is, beyond what is explained by the performance of the domestic economy.

Over the past seven years, corporation tax receipts have continued to surge and become even more concentrated among a handful of firms. Receipts represent nearly one-in-every four euro raised by the Exchequer, and the top-ten paying companies account for more than half of those receipts: up from a quarter in 2008.

Corporation tax receipts could still be subject to sharp reversals. They are more volatile than other major taxes; prone to larger forecast errors; concentrated in a handful of companies; and they are exposed to changes in the global tax environment.

At the same time, the Government has increased its reliance on these receipts to fund day-to-day public services and supports. By funding current spending with corporation tax receipts, the Government risks having to adjust current spending down to set the public finances on a sound footing should receipts fall.

Unfortunately, the Government has no explicit strategy to reduce this over-reliance. This box sets out the Council's assessment that (1) the Government should clearly show the impact of excess corporation tax receipts on the budget balance and (2) the Government should take measures, including potential use of the Rainy Day Fund or faster reductions in debt, to save rather than spend these excess receipts.

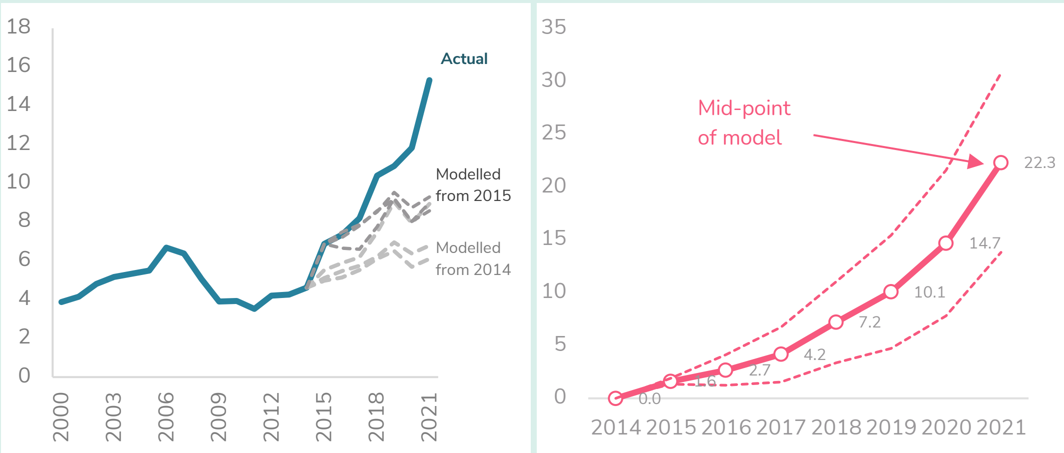
### How much corporation tax receipts are potentially at risk?

The Council's analysis suggests that some €6 to 9 billion (40–60 per cent) of the total €15.3 billion of annual corporation taxes collected in 2021 are not explained by the performance of the domestic economy (Figure G1A).[65] In other words, these appear to be "excess" to what might be driven by the expansion in domestic economic activity.

### Figure G1: A substantial amount of corporation tax can be considered "excess"

**A. Modelled vs actual receipts**
€ billions

**B. Cumulative "excess" receipts collected**
€ billions, cumulative gap for model vs actual




Sources: Revenue data; and Fiscal Council workings. Get the data.
Notes: The suite of models estimates use Domestic GVA and GNI* to predict receipts from 2014 and 2015.

[65] Estimating receipts potentially at risk of sudden reversals is complicated. One way to get at this applied by the Council is to adapt similar modelling approaches to the Department's for forecasting. However, instead of applying these approaches to the overall economy, we apply it to CSO measures of the domestic economy. This helps ascertain the exceptional performance in corporation tax receipts driven by foreign-owned multinationals.

Looking at the cumulative excess of receipts received since 2015, the analysis suggests that some €22 billion of corporation taxes have been collected over and above what can be explained by the performance of the domestic economy (Figure G1B). The uncertainty range around this is very large, with estimates ranging from €14 to 31 billion depending on the modelling approach used.

In line with this approach, two years ago, the Department of Finance (2020) recommended assessing the potential "froth" in corporation tax receipts. Its approach was intended to identify what was "potentially 'windfall' in nature". The approach involved comparing corporation tax's share of total taxes to its historical average of 14 per cent. Anything above 14 per cent could, in the Department's approach, then be considered froth.

If the Department's approach was applied to the same period as the analysis above, it would suggest that a cumulative €15 billion of froth in corporation tax has been collected in recent years.

The analysis above suggests that (1) there is a large exposure to annual corporation tax receipts that is *not* explained by the performance of the domestic economy; and (2) this has resulted in a substantial gain to the Exchequer in recent years.

As shown in the Council's recent report on the health budget (Casey and Carroll, 2021), a substantial portion of the excess receipts has been absorbed into ongoing spending. For instance, corporation taxes have come in on average €1.2 billion higher than forecast at the start of the year each year since 2014. Over the same period, health spending has averaged overruns of €0.8 billion each year, with most of this permanent in nature, including for permanent staff increases or current spending increases elsewhere.

### Ireland's own form of oil wealth

A useful analogy for these exceptional levels of receipts is the oil wealth from which countries such as Norway have benefited. In much the same way, Ireland's remarkable levels of corporation tax receipts are volatile, difficult to forecast, somewhat removed from other activities, and subject to potential reversals in future.

In 1990, Norway decided to start sending its oil and gas revenues to a special oil fund. Various goals included saving wealth for future generations; cushioning fiscal sustainability in case commodity prices reversed; and avoiding the temptation to spend revenues in full. A concern was that spending receipts as they came in would have had procyclical consequences: domestic inflation, appreciation of the domestic currency, and lost competitiveness. Instead, the Norwegian Government opted to use only the returns generated by the oil fund to serve current generations, while preserving its overall value for future generations (Yukhov, 2021; Bhopal, 2021).

### What can be done to reduce the risks?

Ireland's dependency on exceptional corporation tax receipts is now regularly baked into the annual budgetary arithmetic. That is, the Government does not currently have a plan to reduce its dependency on corporation tax receipts. Instead, the tax base is for the most part assumed to grow broadly in line with wider economic activity and there are no plans to actively manage down the associated risks.

Forecasting slightly lower corporation tax receipts and planning for reducing the Government's reliance on these receipts are two different things. Reducing the risks should entail a clear strategy being set. This should include ways to reduce the dependency already built up and plans for how these receipts might be replaced in future, should they reverse.

The Commission on Taxation and Welfare is likely to focus on potential areas for replacing any lost corporation tax receipts when it submits its report to the Minister for Finance (by 1 July 2022). But, as it stands, the Government does not have a credible strategy to address the over-reliance on corporation tax receipts built up in recent years.

The Council's assessment is that risks could be mitigated with two actions.

First, the Government could report on its budget balance, excluding a measure of "excess" receipts in order to better communicate what the underlying fiscal position is likely to be. Figure 3.15

shows what this would look like when applied to the structural budget balance. The Department of Finance (2019) proposed defining a budget balance figure excluding some element of the corporation tax "froth" three years ago, given its view that the headline balance was "being flattered by very strong [Corporate Tax] receipts".

Second, the Government should establish a mechanism to reduce its reliance on excess corporation tax receipts. This would involve two steps:

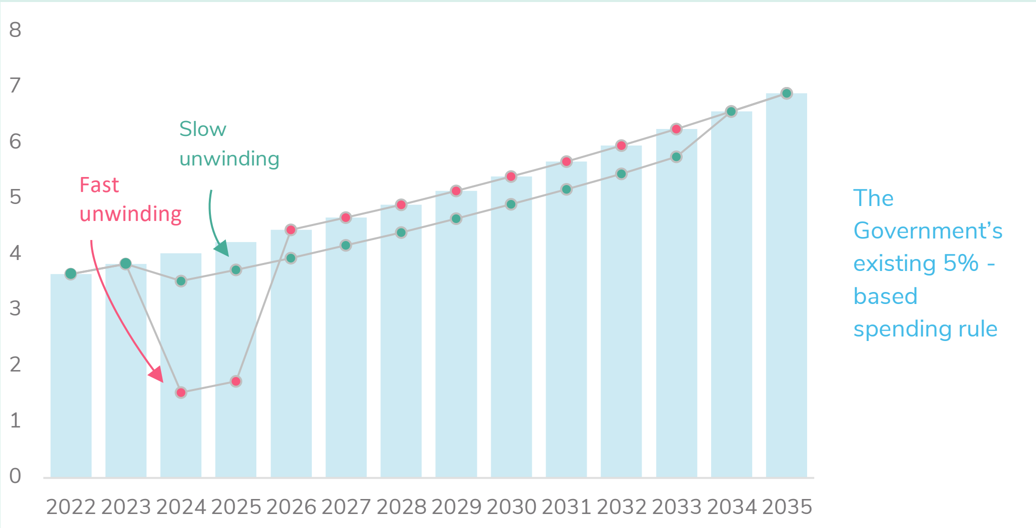
a) the Government should identify the amount of corporation tax currently raised annually that it considers to be excess.

b) the Government should develop a plan to gradually reduce the reliance on this excess over a defined period of time.

As an example of how the dependence could be reduced, consider an illustrative scenario in which the excess corporation tax receipts were identified as being €5 billion with a plan set to reduce the reliance on this either urgently (say, over two years) as might happen if these receipts were to disappear rapidly, or gradually (say, over ten years) which could happen if the Government took pre-emptive action to reduce dependence on excess corporation tax revenues. This could entail reducing planned core spending increases by €2.5 billion in both 2023 and 2024 or by €0.5 billion annually over the next ten years (Figure G2). Alternatively, revenue-raising measures equivalent to the same amounts could be introduced to offset the overreliance on corporation tax and return spending to the higher level consistent with the 5% Spending Rule.

**Figure G2: Excess can be unwound with slower spending rises or new revenues**

€ billions, core spending increases




Source: Fiscal Council workings.

These approaches give an illustration of how excess corporation tax receipts built up to date could be unwound. If followed, along with the 5% Spending Rule, the Government would also ensure that potential future overperformances unexplained by domestic economic activity could be saved rather than spent. At a minimum, the Government should cap its exposure to the surge in corporation tax receipts. This would entail ensuring that further outperformances in corporation tax — beyond reasonable projections for growth in the domestic economy — be set aside.

By using excess receipts to fund ongoing expenditure, the Government has potentially opted not to set aside some €22 billion in a Rainy Day Fund or to reduce net debt by a substantial amount. Using these resources, which could be considered an injection of funds from overseas, will have boosted economic activity and tax receipts to some extent in the meantime, meaning that the full €22 billion is not the ultimate opportunity cost to reducing net debt. though the risks to fiscal sustainability from these decisions remain sizeable.