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Houses of the Oireachtas

An Coiste um Fhormhaoirsiú Buiséid

Tuarascáil Réamhbhuiséid 2024

Deireadh Fómhair 2023

Committee on Budgetary Oversight

Pre Budget Report 2024

October 2023

33/CBO/023

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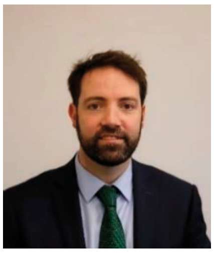
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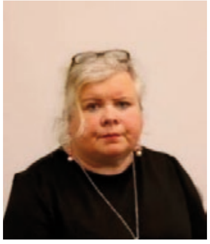
Patricia Ryan
Sinn Féin

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[1] Mairéad Farrell TD was discharged from the Committee on 26 April 2023 and Rose Conway Walsh TD was appointed in her stead
[2] John Lahart TD was discharged from the Committee on 30 May 2023 and Barry Cowen TD was appointed in his stead
[3] Neasa Hourigan TD was discharged from the Committee on 26 April 2023 and Steven Matthews TD was appointed in her stead.
[4] Kieran O'Donnell TD was discharged from the Committee on 21 December 2022 upon appointment as Minister of State. Colm Brophy TD was appointed to the Committee on 7 March 2023.

Cathaoirleach's Foreword

Budget Day has always occupied a significant place in the calendar year, whether through times of economic hardship or economy prosperity. As we approach Budget Day this year, the economic outlook is much more nuanced, but the role of the Budget is no less important or significant than in previous years. Having emerged from the extraordinary effects of the Covid-19 pandemic and the extraordinary measures employed throughout that period, the State yet again faces challenges in an economic environment rarely seen in recent times.

Budget 2023 took place in an environment characterised by rising energy prices, rising inflation, and a cost-of-living crisis. While some of these challenges have begun to slowly subside, they nevertheless pose a serious challenge for our economic and social wellbeing. The economic outlook is still characterised by higher-than-normal inflation, high energy prices, and the impact of rising interest rates can now be felt across the economy, from large businesses to small households.

An additional challenge faced by Government will be to mitigate against these effects during a time where employment is at all-time highs, the economy is near capacity, and where increased spending can result in adding to already problematic inflationary issues. The Government therefore has, as acknowledged, a delicate balance to strike.

Having examined many of these issues during the course of its deliberations, the Committee has produced the following report which we hope will contribute to the consideration of the measures employed in the Budget.

On behalf of the Committee, I would like to thank the witnesses who assisted the Committee in examining potential budgetary decisions and their potential impacts. I would also like to thank the Ministers for their cooperation and facilitation in our discussions.

I would also like to thank the Members of the Committee for their engagement on what is such an important event.

Barry Cowen T.D.,
Cathaoirleach

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Summary of Recommendations & Observations

1. The Committee notes the significance of the capacity issues in the Irish economy and highlights the need to address these challenges in a way that does not further add to inflationary pressures.

2. The Committee recommends that the Budget provide for sufficient resources to adequately resource any changes to the planning system that arise from the Planning and Development Bill.

3. The Committee notes concerns around the potential impact the housing shortage may be contributing to capacity issues in the economy and highlights the need for Budget 2024 to address this issue.

4. The Committee notes the Central Banks concerns that the forecasted housing output is below the level needed for demographic shifts and emphasises the need for Budget 2024 to address this issue.

5. The Committee notes the concerns of the potential increase in expenditure needed to meet the existing commitments in the National Development Plan.

6. The Committee notes the Central Banks concerns that an expansionary budget will lead to an increase in short-run inflation and emphasises the need to exercise caution in this regard when considering budgetary policies

7. The Committee agrees, as has been widely discussed, that the current level of corporation tax should not feed into regular spending or tax cuts.

8. The Committee recognises that the impact of inflation has on those in the lower income deciles and wishes to once again highlight the need for measures in the Budget to specifically target supports at those most in need.

9. The Committee notes the significant spending overruns in certain Departments and recommends that these be fully reflected in the allocations for 2024, unless there is convincing evidence that the expenditure will not be repeated.

10. The Committee notes the significance of the Governments proposed sovereign wealth fund and, in this regard, would like to highlight the

Committee's report on the topic and the recommendations contained therein.

11. The Committee supports the Government decision to spend beyond the 5% spending rule given the current inflationary environment.

12. The Committee notes the concerns regarding the characterisation of core and non-core expenditure. The Committee recommends that strict criteria for the definition of non-core be agreed by the Government and bodies such as the Fiscal Council and Central Bank.

13. The Committee notes concerns regarding the labelling of "windfall capital investment" and recommends that "windfall capital investment" be included in core capital investment figures.

14. The Committee notes the concerns around the use of once-off measures but due to the current inflationary environment supports their limited use for 2024.

15. The Committee recommends that any taxation measure should be limited to ensuring the tax burden on workers does not increase solely due to inflation linked wage increases or be targeted at those most impacted by the inflationary pressures.

16. The Committee notes their recommendations contained in the previous report on indexation and the recommendations in their Pre-Budget Report 2023 and wishes to highlight the importance of providing for measures that will ensure the real incomes of those on lower incomes do not fall due to inflationary pressures.

17. The Committee notes that while once-off measures cushioned the impact of inflation this year, as a result larger increases would be required next year to ensure the standard of living is maintained.

18. The Committee recommends that income thresholds for access to certain public services should be raised in line with changes to social protection payments.

19. The Committee recommends that the Christmas bonus in 2024, and beyond, be included in budgetary projections and Departmental allocations from the Revised Estimates.

Introduction

The Select Committee on Budgetary Oversight ("the Committee") was established during the 32nd Dáil to enhance the role of the Oireachtas in scrutinising the budget and to review the macroeconomic and fiscal issues that form part of the budget considerations. Since its establishment, one of the primary outputs of the Committee has been the publication of the annual pre-budget report, based on the Committee's pre-budget scrutiny.

The Committee held a number of engagements before and after the summer recess (see Appendices 1 and 2), including two meetings with the Minister of Finance and the Minister of Public Expenditure and Reform.

Overview of Previous Reports

The Committee has published four reports since Budget 2023. These reports have covered a range of topics and the Committee believes the recommendations made in the reports should continue to be considered. A fifth report, on the proposal for a Sovereign Wealth Fund, will also be published in advance of Budget 2024.

Post-Budget 2023 Report[5]

The first report published by the Committee following Budget 2023 was on Budget 2023 itself.

The report made the following observations and recommendations relating to the 2023 Budget measures in the report:

- *The Committee notes and recognises the value of programme-level/performance budgeting and recommends that the Department of Finance and the Department of Public Expenditure and Reform introduce such budgetary measures as soon as possible. If necessary, the Committee recommends that a pilot programme of performance budgeting be carried out, with DPER to report back to the Committee when complete.*

5 https://data.oireachtas.ie/ie/oireachtas/committee/dail/33/committee_on_budgetary_oversight/reports/2023/2023-01-31_post-budget-2023-report_en.pdf

- *The Committee notes the additional detail provided for in the Revised Estimates compared to that provided for in the budget expenditure report and recommends that the Department of Public Expenditure and Reform endeavour to include this detail in future budget expenditure reports.*

- *The Committee notes the difficulties in maintaining living standards in the current inflationary environment, particularly for those on low incomes and those reliant on social welfare, and as such recommends that consideration be given to indexing welfare payments to inflation in forthcoming budgets.*

- *The Committee acknowledges the importance of one-off measures used in Budget 2023 but notes that one-off measures for lower-income households should not become a regular feature of the Budget.*

- *The Committee welcomes the inclusion of the "underlying general government balance", or the underlying fiscal balance excluding the Department's estimate of windfall corporation taxes, in the 2023 budget documentation.*

- *The Committee notes the concerns raised by the Fiscal Council with regards the short budgetary forecasting horizon for Budget 2023 and recommends that the Department of Finance return to previous commitments to produce five-year forecasts*.

- *The Committee notes the temporary deviation from the 5% spending rule and acknowledges the rationale for doing so given the challenging budgetary environment. However, the Committee recommends that this rule be reinforced in forthcoming budgets, and that consideration be given to establishing this rule on a legislative basis.*

- *The Committee acknowledges that the decision to pay the Christmas bonus is dependent on the government's fiscal position each year. However, the Committee notes the uncertainty this introduces for households every year and as such recommends that the decision to pay such a bonus be signalled as far in advance as possible.*

Report on Pre-Stability Programme Update Report 2023[6]

As part of its annual work programme the Committee published a report in advance of the Stability Programme Update (SPU). The Committee met with representatives from the ESRI and the Central Bank as part of its Pre-SPU scrutiny.

6 https://data.oireachtas.ie/ie/oireachtas/committee/dail/33/committee_on_budgetary_oversight/reports/2023/2023-04-04_report-on-pre-stability-programme-update-report-2023_en.pdf

The Committee also met with the Minister of Finance and the Minister of Public Expenditure and Reform following publication of the SPU.

The Committee made a number of observations and recommendations in the report, including:

- *The Committee notes that inflation is widely forecast to moderate in 2023 but urges Government to remain vigilant and be ready to react should higher than expected inflation persist.*
- *The Committee reiterates that lower income and rural households are among the most impacted by the current inflationary pressures and that longer term measures may be required to support these households.*
- *The Committee recommends that the SPU include estimates of the impact on the economy of different levels of inflation over 2023 and analyse the impact of inflation on the State's capital expenditure programme.*
- *The Committee recommends that the SPU examine the risks related to the tight labour market and how these can be mitigated.*
- *The Committee notes that housing is a key issue for the Irish economy, as well as society, and has the potential be a significant drag on economic growth and on the public finances.*
- *The Committee recommends that the economic and fiscal risks related to the housing sector be thoroughly examined in the SPU along with the impact of proposed policy responses on the fiscal position.*
- *The Committee notes that the Irish banking sector is more resilient than in the past.*
- *The Committee recommends that the SPU examine the potential risks linked to the international financial system on the Irish economy and on the Irish banking system.*
- *The Committee, as it has done in a previous report, welcomes of the measure of excess corporation tax and the underlying general balance.*
- *The Committee recommends that the Government continue to develop the measure of excess corporation tax in the SPU and set out a framework or set of rules of how the calculation is to be continuously monitored and refined as necessary.*

- *The Committee recommends that the Government provide 5-year economic and fiscal forecasts in its upcoming SPU, to better inform policy decision-making and the context in which it is to take place over the medium-term.*

- *The Committee recommends that the Government clarify the position of expenditure from the National Reserve Fund, and any other such funds, as part of the fiscal rules.*

- *The Committee recommends that the Government set out, in the SPU or otherwise, options for what would be required before funds from the NRF be used and how.*

Report on Section 481 – Film Tax Credit[7]

Following the examination of the Section 481 – Film tax Credit the Committee made a number of observations and recommendations –

- *The Committee recommends that the Department consider altering the claiming process, with a reduced amount of funding to be made available up front based on budgeted expenditure (currently 90%), and the balance claimed on completion, as a means of encouraging compliance with the criteria.*

- *The Committee recommends that consideration be given to extending the 6-month time limit to submit a claim to the Workplace Relations Commission for cases involving the audio-visual sector due to the nature of their operation and structure.*

- *The Committee recommends that DACs established for the purposes of TV, Film and Media production be required to continue in existence for 3 years following the completion of a production, as a requirement for receipt of Section 481.*

- *The Committee recommends that the term 'quality employment and training', in the context of the audio-visual industry, be defined.*

- *The Committee recommends that it is clearly established that producer companies who receive Section 481 on the condition of creating quality*

7 https://data.oireachtas.ie/ie/oireachtas/committee/dail/33/committee_on_budgetary_oversight/reports/2023/2023-05-09_report-on-section-481-film-tax-credit_en.pdf

employment and meeting the industry development test must take responsibility for employees and acknowledge their employment relationship with film crew across different productions and recognise the accumulated service of all such employees as a condition of receiving Section 481.

- *The Committee commits to writing to the EU commission requesting an examination of the use of successive use of Fixed Term Contracts for film crew working across multiple productions, where such crew never acquire Contracts of Indefinite Duration or any acknowledgement of their service, and whether this amounts to a breach EU Directives in terms of both the Fixed Term Workers Directive and EU directives relating to state aid for the Audio-visual sector.*

- *The Committee recommends that under the industry development test, assurance must be given that Irish performers will not be subject to lesser terms and conditions regarding their intellectual property rights than international performers in similar roles when employed on the same project receiving Section 481 funding.*

- *The Committee recommends that compliance with the Copyright and Related Rights Act 2000, as well as the EU Copyright Directive should be a specified requirement in order to avail of the Section 481 credit. In this regard the Committee wishes to highlight the importance of compliance with Articles 18 to 23 of the EU Copyright Directive.*

- *The Committee commits to writing to the EU commission requesting an examination of the use of 'buy-out' contracts in the Irish film production.*

- *The Committee recommends that the Department of Finance engage with the European Commission with a view to retaining the Regional Uplift at a higher rate of 5%, and to increase the 45-kilometre area limit to 75 kilometres or further.*

- *The Committee recommends that the Department of Tourism prioritise and engage with the Department of Education, Screen Guilds Ireland and Screen Ireland and other interested stakeholders to develop an accreditation framework, in line with the National Framework of Qualifications, for recognised skills across the audio-visual sector.*

- *The Committee recommends that the Department of Finance, when providing information on the performance of the Section 481 Film Relief or otherwise, provide data regarding the number of individuals employed on certified projects in addition to FTEs, and to provide data on FTEs excluding extras.*

- *The Committee recommends that consideration be given to removing or increasing the €70 million cap.*

- *The Committee recommends that the Department of Tourism, Culture, Arts, Gaeltacht, Sport and Media and the Department of Finance convene a stakeholder forum as a priority to discuss how to maximise the benefits of the Section 481 credit for all concerned stakeholders, and to facilitate best practice in employment rights, industrial relations, collective bargaining, address Copyright and Intellectual Property issues and any other relevant issues.*

Examination of the Commission on Taxation and Welfare Report[8]

Following the Committee's examination of the report compiled by the Commission on Taxation and Welfare the Committee made a number of observations and recommendations –

- *The Committee broadly agrees with the Commission's proposals to broaden the tax base in order the secure the sustainability of revenues needed to address future challenges and furthermore agree broadly with the Commission's proposals to aimed at improving the effectiveness of the welfare system.*

- *The Committee recommends that prior to the consideration of increasing rates of VAT thorough modelling, research and analysis be carried out on the distributional impact of such measures, and that appropriate welfare supports be put in place for those most affected by such VAT increases, in particular lower-income households.*

- *The Committee recommends that a review of the VAT treatment of goods and services in Ireland be prioritised to ensure they are in line with EU rules.*

- *The Committee recommends that the use of temporary reduced VAT rates should be limited.*

- *The Committee agrees with the Commission that the Group A Capital Acquisitions Threshold should be lowered to help achieve greater fairness via vertical equity. The Committee recommends that when setting a reduced*

8 https://data.oireachtas.ie/ie/oireachtas/committee/dail/33/committee_on_budgetary_oversight/reports/2023/2023-09-20_examination-of-the-commission-on-taxation-and-welfare-report_en.pdf

threshold for CAT, that consideration be given to linking the rate to a multiple of average earnings, to be reviewed and set annually via the Finance Bill.

- *The Committee recommends that as part of the base-broadening measures such as those mentioned in the Commission's report, that the Department of Finance maximise the utilisation of the Automatic Exchange of Information and the Common Reporting System.*

- *The Committee recommends that where proposals to alter the existing capital tax framework are made, thorough analyses are carried out to ensure there are no negative effects on the functioning of the property market.*

- *The Committee notes that the report on the Commission on Taxation and Welfare does not address the tax relief disparity that will exist for those currently making pension contributions and those who will be contributing under the new auto-enrolment pension. The Committee recommends that prior to the autoenrolment scheme coming into effect, that efforts be made to address this inequity. The Committee notes this would be in line with the Commission's recommendation that anomalies in the tax treatment of different retirement arrangements should be eliminated, as far as possible (8.7).*

- *The Committee notes the recent report by the Joint Committee on Social Protection, Community & Rural Development and the Islands, on Pre-Legislative Scrutiny of the General Scheme of the Automatic Enrolment Retirement Savings System Bill 20226, and its recommendation that the "Department carefully consider tax relief in the General Scheme of the Autoenrollment Bill and its impacts on the wider pension system". The Committee reiterates this recommendation.*

- *The Committee strongly supports the Commission's recommendation 8.6 concerning an urgent review of the availability of appropriate and adequate data on the cost and distribution of pension tax expenditures. The Committee recommends that the statutory role of the Office of the Revenue Commissioners be amended to include the collection and provision of policy relevant data on taxes and the taxation system, in particular in relation to tax expenditures.*

- *The Committee welcomes the recommendation by the Commission that enhanced relief measures for the R&D tax credit be introduced which are targeted at small and medium sized enterprises, and that greater guidance and supports should be introduced to facilitate greater uptake by SMEs more generally (9.6).*

- *The Committee would like to reiterate the recommendations previously made by the Committee in its Report on Tax Expenditures: Research & Development Tax Credit and Knowledge Development Box7, aimed at supporting and enhancing the role of the R&D credit for SMEs.*

- *The Committee recommends that greater levels of research into financing barriers faced by small to medium enterprises be carried out to better address such challenges and to allow for the effective implementation of investment incentives.*
- *The Committee notes the Commission's recommendation to continue the use of feedback statements and roadmaps which should be applied to indigenous entities and SMEs and welcomes this point (9.2). The Committee recommends that such roadmaps detail potential tax developments over lengthy time horizons so that SMEs can better plan and navigate potential tax reforms into the future.*

- *The Committee notes the concerns raised with the proposed use of tax expenditures to promote enterprise and recommends that these should only be considered in line with overall reform and reduction of the use of tax expenditures.*
- *The Committee recommends that when considering the Commission's recommendation that those over the State Pension age pay PRSI on all income other than social welfare payments (10.4) and to remove the PRSI exemption on supplementary pension income (10.5), that consideration be given to the effect this may have on older people's financial situations and that a detailed analysis of income replacement rates from all sources of older person's income be carried out. The Committee wishes to highlight the importance that older persons are not adversely affected by these recommendations.*

- *The Committee recommends that when considering the Commission's recommendation that those over the State Pension age pay PRSI on all income other than social welfare payments (10.4) and to remove the PRSI exemption on supplementary pension income (10.5), that consideration be given to the effect these would have on work incentives for older people and the impact on those are not entitled the State pension. The Committee wishes to again highlight the importance that older persons are not adversely affected by these recommendations.*

- *The Committee recommends that any consideration or analysis of the Commission's recommendation to alter the pensions landscape take into* *account the impact of the pensions auto-enrolment system due to be introduced from 2024.*

- *The Committee notes concerns that Commission's analysis of a proposed UBI (10.8) was based on an insufficient number of studies and recommends that further examination of the proposal be undertaken.*

- *The Committee supports the move towards the individualisation of the Standard Rate Cut Off Point but recommends any proposed implementation take into consideration and mitigate against any negative financial consequences for secondary earners in carer roles in single-earner couples. Any proposed move to individualisation should also take into account the position of older persons at present and those currently close to retirement age.*
- *The Committee recognises the need to coordinate and manage the phased introduction of any taxation and welfare reforms and as such supports the Commission's recommendation for the establishment of appropriate coordination mechanisms to monitor the cumulative effect of policy-related labour cost changes on enterprise and the self-employed (11.2).*

- *The Committee welcomes the Commission's recommendation that secondary benefits for people of working-age should be designed on a cross-departmental basis to ensure coherence, with negative work incentives minimised, and benefits targeted appropriately and effectively (11.1). This should also apply to benefits for older persons.*

- *The Committee notes that its Report on Indexation of the Taxation and Social Protection System[9] examined the issue of benchmarking in detail and considers many of the issues raised by the Commission.*

- *The Committee recommends that when considering the Commission's recommendation to undertake a regular benchmarking exercise in respect of all working age income supports, that consideration should also be given to the establishment of a standalone body to carry out periodic, regular evaluations of working age income supports and could be expanded to cover the adequacy of the State Pension also.*

- *The Committee welcomes the government's intention to introduce a greater element of pay-related benefits withing the Social Insurance system and notes*

9 https://data.oireachtas.ie/ie/oireachtas/committee/dail/33/committee_on_budgetary_oversight/reports/2022/2022-07-14_indexation-of-the-taxation-and-social-protection-system_en.pdf

the public consultation on the issues held earlier in 2023. The Committee looks forward to further engagement upon the outcome of this consultation. The Committee also wishes to highlight the possible risks that the "incentive to work" aspects of pay-related benefits may have in excluding those unable to work due to illness, disability, caring duties, migration status and other reasons.

- *The Committee welcomes the Commission's recommendation to progress the individualisation of payments to qualified adults and notes that this system will better reflect the changing nature of families and the equal division of paid work and care.*

- *The Committee notes the Commission's recommendation (13.4) that increases in carbon tax post-2030 should be clearly signalled.*

- *The Committee recommends that the impacts of the projected increase in revenues resulting from the EU Emissions Trading System price on the Irish economy and government revenues be taken into consideration when discussing or proposing the budgetary impacts of moving to a low-carbon economy and the recommendations of the Commission.*

- *The Committee notes the Commission's recommendations to equalise the rate of excise duty on auto-diesel and petrol (13.2) and to reduce fossil fuel subsidies on a phased basis (13.3).*

- *The Committee notes the commission's recommendation to introduce a site value tax but strongly recommends that prior to any such proposal, that a thorough review of such a measure be carried out and that complete, adequate, and appropriate data regarding land values and land holdings be gathered in advance.*

- *With regard to land data the Committee notes the Joint Committee on Housing, Local Government and Heritage's recommendation contained in the Report on Pre-Legislative Scrutiny of the Tailte Éireann Bill 2020[10] that "Tailte Éireann be given, as one of its statutory functions, responsibility for maintaining a publicly accessible, searchable, electronic register of land transactions that would include the price, location, size, zoning, date of sale*

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10 https://data.oireachtas.ie/ie/oireachtas/committee/dail/33/joint_committee_on_housing_local_government_and_heritage/reports/2021/2021-12-06_report-on-pre-legislative-scrutiny-of-the-general-scheme-of-the-tailte-eireann-bill-2020_en.pdf

and ownership details. This new register would operate on a similar basis to the existing Residential Property Price Register".

- *The Committee, in agreement with the Commission, strongly recommends that any proposal to introduce a site value tax includes the condition that differential treatment be applied to agricultural land in active use.*

- *The Committee notes the current introduction of the Residential Zoned Land Tax and notes the Commission's remarks that this tax may be subsumed into a Site Value Tax over time. The Committee is cognisant of the need for a coherent tax policy around land and property and for one that is not unnecessarily administratively burdensome/complex.*

- *The Committee recommends that any proposals to amend the structure or the responsibility for the rate-setting of Local Property Taxes must ensure that the role of local government is not diminished.*

- *The Committee recommends that prior to any proposal to increase Local Property Tax as recommended by the Commission, consideration be given to the retention and augmentation of a payment deferment system for those on low incomes or those in asset-rich and cash-poor situations. The Committee recommends that a distributional impact assessment be carried out in advance of the consideration of such a system.*

- *The Committee recommends that the completion and the publication of the evaluation of the Sugar Sweetened Drinks Tax be prioritised to enable the Department of Finance to effectively consider any proposals to introduce similar measures on health grounds, such as those proposed by the Commission.*

- *The Committee welcomes the views of the Commission regarding the tax expenditure review process and agrees with Commission's recommendations on this topic.*

- *The Committee wishes to highlight and reiterate its recommendations regarding tax expenditures as set out in its previous reports – Interim Pre-Budget Report 2022, and Report on Tax Expenditures: Research & Development Tax Credit and Knowledge Development Box.*

- *The Committee recommends that consideration be given to the inclusion and participation of the Irish Government Economic Evaluation Service in building* *the capacity and expertise in the evaluation or peer-reviewing of tax expenditures, as mentioned in the Commission's recommendation 16.4.*

- *The Committee would like to reiterate its previous recommendation contained in its Report on Tax Expenditures: Research & Development Tax Credit and Knowledge Development Box, that the Department recruit the appropriate staff and resources necessary to review the number of tax expenditures, as required under Department of Finance guidelines.*

Economic Context

Over the last year, the Irish economy has weathered different shocks, from global uncertainty following the pandemic, decades-high inflation rates, and the significant monetary policy response. However, Ireland has withstood these shocks well. The Summer Economic Statement[11] (SES) notes that the level of Modified Domestic Demand (MDD) is well above its pre-pandemic peak with little evidence of any 'scarring' to the economy from these shocks. The Economic and Social Research Institute (ESRI) in their opening statement also noted the current and past macroeconomic context, remarking that that the Irish economy has performed particularly strongly following the impact of the Covid-19 pandemic. However, they advised that it is difficult to understand the underlying pace of growth of the economy due to the significant distortions to headline economic indicators by certain multinational corporations. In this regard the ESRI suggested that the Irish economy has been growing at somewhere between 4% and 4.5% in the period post the financial crash.

The SES notes that official data confirms an expansion in the domestic economy since the beginning of the year, with Modified Domestic Demand, MDD, up 2.7% in the first quarter, supported by stronger than expected growth in consumer spending as well as expansion in construction activity and private sector investments in plant and machinery.

The SES also sets out that rather than any shortfall in demand, the main constraint on the economy is on the supply side. It notes the lack of sufficient housing supply is holding back economic growth, including by reducing labour mobility both from within the country and abroad. Other domestic capacity constraints include the energy infrastructure where demand has come close to the capacity of the system at times.

The ESRI noted that notwithstanding the strength of the recent economic performance, it is more than likely that the Irish economy will experience more moderate growth rates going forward. This is due to the more modest growth rates of

[11] https://www.gov.ie/pdf/?file=https://assets.gov.ie/262563/be1e0616-663e-43e1-98fe-065ff0e49ce9.pdf#page=null

the ICT and pharmaceutical sectors compared to their post-covid growth and this will be reflected in the domestic economy.

The Central Bank also suggested a more moderate pace of growth for the Irish economy, as capacity limits have become more binding and the impulse from external demand wanes. They forecast MDD to grow by 2.9% this year, 2.6% in 2024, and 2.3% in 2025.

The ESRI also noted that the current budget comes at a time when the domestic economy is near its full capacity and transitioning from high to moderate growth. They noted the improved public finances provide an opportunity to address infrastructure deficits in areas like housing, healthcare, and climate change, however higher interest rates make private sector investment in these areas more costly, potentially requiring the government to spend more than initially anticipated.

The Nevin Economic Research Institute (NERI) outlined the importance of understanding the stage of the economic cycle (recession, overheating etc.) the economy before making decisions on the budgetary policy and the fiscal stance. If an economy is downsizing the Government should stimulate the economy and the opposite if the economy is overheating.

NERI's analysis is that the economy is close to overheating, as shown by the record levels (or close to) of employment rates and hours worked, the tight labour market, and there is evidence of labour shortages and capacity constraints in some sectors (e.g., construction and ICT). NERI also noted that consumption and retail sales are growing, and demand has been supported by the winding down of savings built up during the pandemic along with fiscal stimulus.

NERI believes the outlook for the year is mixed. The tightening of monetary policy is impacting on Ireland's trading partners and gradually reducing demand in the domestic economy. Consumer sentiment indicates a broadly negative perception of the future while construction and manufacturing purchase managers indexes (PMIs) imply a broadly stagnant outlook. However, services PMIs are more positive.

The Central Bank, in their opening statement to the Committee, noted that the economy has demonstrated resilience to the shocks of the pandemic and the invasion of Ukraine.

Inflation

The SES states that having peaked at just over 9.5% last summer, headline inflation has fallen by nearly 5 percentage points, reaching 4.8% in June, with the bulk of this decline occurring in the last six months. However, it does note that core inflation is proving to be more persistent than expected and was above headline inflation in May for the first time since the beginning of the current inflation cycle.

The ESRI noted that inflation is still exerting a negative impact on the Irish outlook and while energy prices have been declining, inflation in now being driven by other factors like housing and food costs, with real household income level struggling to register positive growth. They also stated that a challenge currently is the response by monetary authorities to the inflationary period through increases in interest rates, with adverse side effects to investment and economic growth negatively affected. In a domestic context, these higher rates will have negative consequences for the housing market where the cost of finance has increased substantially over the past year. The housing supply deficit might be further affected by the higher cost of construction financing, and affordability challenges also face households looking to secure mortgage finance. However, they advised that Central Bank research may provide some reassurance as it shows that lower income quintiles are much more likely to have a fixed rate mortgage and are therefore less exposed to interest rate rises than middle- and higher-income groups due to the prevalence of tracker and variable rate mortgages among these groups.

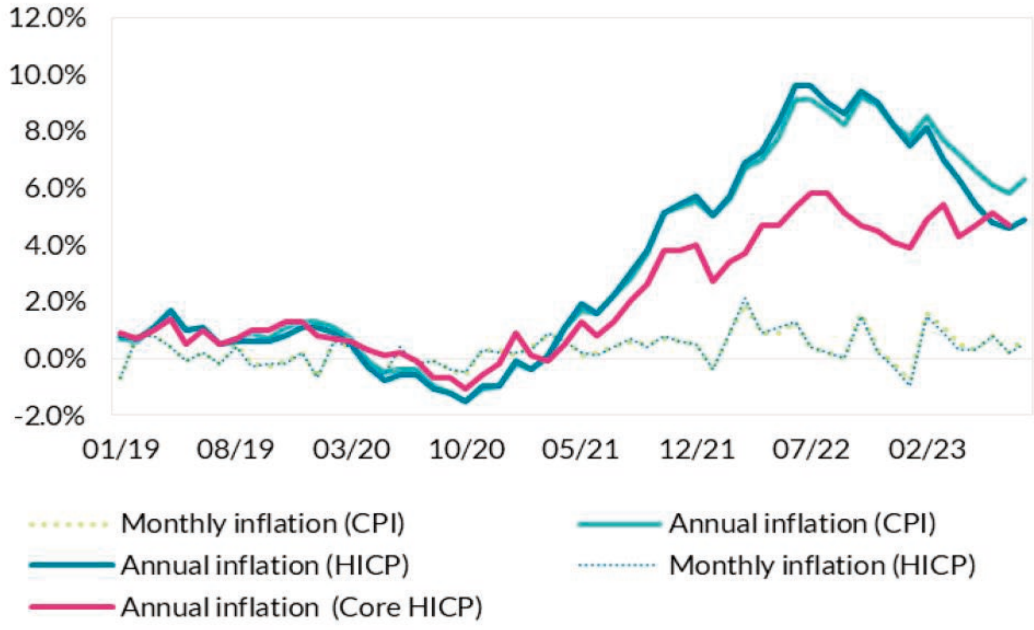

Figure 1 - Consumer Price Inflation. Source: Central Bank

Looking to the short term, the Central Bank noted that the contribution of external factors to headline inflation has declined with domestic factors playing an increasingly important role in influencing inflation dynamics in 2023 and over the forecast horizon. They forecast inflation to moderate to 3.2% and 2.3% in 2024 and 2025 respectively. This is due to energy, food and industrial goods price growth slows, offsetting more persistent upward pressure on inflation from services.

The Central Bank further outlined that the interplay between profit margins and wage pressures will largely determine the persistence of inflation. They noted that scenario analysis based on historical relationships suggests that inflation in Ireland would have been between 2 and 2.5 percentage points higher over the last and next 12 months in the absence of rate increases since July 2022

In discussing the inflationary environment in the energy markets with representatives from the Central Bank, the Committee noted that wholesale electricity prices have seen a sustained decrease in the 12 months to July and there has also been a decrease in wholesale costs, with the same true of gas prices. However, the Committee also noted that while electricity prices across the euro area have fallen substantially since October, there has been no equivalent fall in Irish electricity prices in this period (Figure 2). Responding to this the Central Bank acknowledged that Ireland is out of step with Europe in this regard and advised that typically in this market there is a significant amount of hedging, and such strategies may be slowing down the pass through of lower prices to consumers.

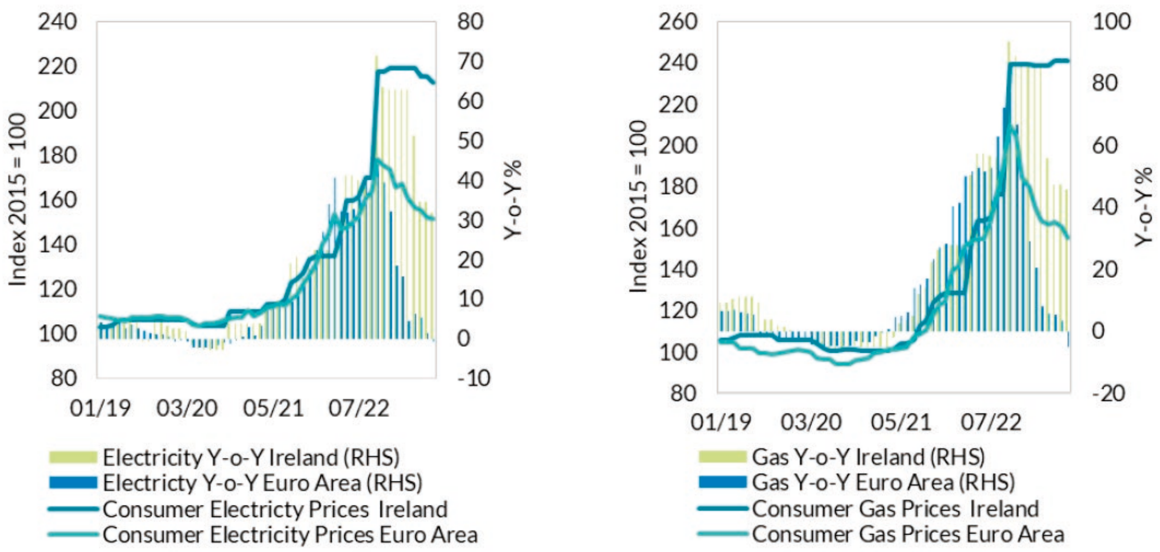

Figure 2 - Consumer Electricity and Gas Prices. Source: Central Bank

In discussing the lagging effects further, the Central Bank further noted that the ECB, having increased interest rates by 450 basis points since last year, considers that rates are now at such levels that if maintained for a long duration, will bring euro area inflation back to target levels.

In this regard, Central Bank analysis shows initial Irish interest rate pass-through is underway but also appears to be slower for new mortgage lending and household deposits relative to historical precedent and euro-area peers. They also advised that the cumulative effect of such increased interest rates will take between 18 and 24 months to feed through to growth and inflation. Elaborating on the impact of these higher interest rates on low- and middle-income households, the Central Bank noted that higher interest rates have a direct effect on loans with a subsequent impact on house prices. They also outlined that there is a consumption effect, whereby if people's mortgage rates increase generally, they have to spend more on their debt leaving them with less to consume. They further noted that, with regard to the distributional effect of such rate increases, the cohort of individuals that that have mortgages in Ireland are not necessarily the lower income households but advised that this was a generalised statement and that there are mortgages across the economy. They did note however that mortgages interest is paid by higher income households in society.

The Central Bank noted that in an analysis they have done they found that the impact on the average mortgage holder is an increase in repayments of 16%, but that this is different across mortgage holders. They further noted that approximately 40% of mortgage holders would not have any increase in their repayment and another 20% would see them increase by 50%. The 20% of mortgages that are seeing a 50% increase would largely be trackers, which would have larger outstanding amounts, longer terms, and larger mortgages overall.

Inflation, NERI agreed, is still a significant issue with the CPI increasing by 6.3% in August, with core inflation at 6.4% raising concerns around the 'stickiness' of inflation. NERI further noted that real wage growth was negative in the second quarter and while it is expected to return to positive growth by the end of the year, this is predicated on no major shocks to inflation.

Employment

The SES outlines that the current economic position is most visible in the labour market where the unemployment rate stood at 3.8% in May, its lowest ever. In the first quarter the level of employment exceeded 2.6 million for the first time, an increase of more than a quarter of a million on its pre-pandemic level, with the employment rate standing as 73.5%, also a record high. While these labour market figures are a positive development, the exceptionally low rate does signal that the demand for labour may well be in excess of supply, potentially triggering 'second-round' effects on inflation.

The Central Bank, in their Quarterly Bulletin, noted that employment growth is forecast to slow in the coming years as capacity constraints in the labour market and broader economy limit the scope for expansion in the labour force. They further stated that the with the unemployment rate forecast to remain approximately 4% out to 2025, tight labour market conditions will result in upward pressure on wages allowing for an increase in real incomes following a 2022 decline.

The Central Bank noted demand for labour has surged with resulting vacancy rates rising substantially and unemployment rates falling to 20-year lows, signalling an economy operating at full capacity.

NERI, in discussing aspects of the labour market with the Committee, advised that there is a good argument that if labour market opportunities in construction were better, or similar to what they were 15 or 20 years ago, it is possible there would be fewer people opting for third level education, and in this regard noted that it is possible there is no need for so many people in third level education and that a rebalancing is required to attract school leavers into construction. Related to this they noted that despite high unemployment, young males are down in terms of their participation rate compared to 15 or 20 years ago.

Expanding on this, NERI advised that one of the public policy goals should be increase the supply of construction workers and to make it an attractive sector. To do this they suggested dealing with issues such as bogus self-employment, making sure wages are strong, and signalling that it is not going to be a volatile or boom-bust sector, and advised a long-term infrastructure plan can be a part of this. They advised that the State needs to signal to people that areas such as retrofitting are going to be the jobs of the future for the next 20 years and that if they skill up in that area they will have a guaranteed job.

Budgetary Parameters

The Summer Economic Statement notes that for Budget 2024, an overall budgetary package of €6.4 billion is being made available. It notes that the overall budget package will be composed of a spending allocation amounting to €5.2 billion in 2024, with core expenditure to grow by 6.1% per cent in 2024. It also notes this deviation from the medium-term framework as set out in the Summer Economic Statement 2021 takes into account the fact inflation is expected to be above trend next year. This framework set 'net' core expenditure growth of 5% annually over 2023-2025 and was designed to ensure sustainable public expenditure growth, with annual increases in spending anchored to the economy's estimated trend growth taking into account an assumed inflation rate of around 2%. In this regard it outlines that while inflation is easing, it is expected to remain above trend next year and on this basis the government had adjusted its fiscal parameters for Budget 2024.

The SES also sets out an overall tax package worth €1.1 billion will be provided, focusing on the need to adjust income tax bands and credits so workers do not fall into the higher levels of taxation by virtue of wage inflation. It also states that €2.25 billion of 'windfall' corporate tax receipts will be made available over the period 2024-2026 to fund what is termed 'windfall capital investment', a form of capital investment "contingent on 'windfall' receipts remaining at elevated levels".

Table 1 - Budgetary Strategy. Source: Summer Economic Statement

	2023	2024	2025	2026
Total budget package (1 = 2 + 3)	*6.9*	*6.4*	*5.7*	*5.9*
Budgetary decisions^ (2)	*2.7*	*3.2*	*3.2*	*3.2*
To be allocated^^ (3 = 4 + 5)	*4.3*	*3.1*	*2.5*	*2.7*
of which: expenditure measures (4)	*3.2*	*2.0*	*1.4*	*1.6*
of which: tax measures^^^ (5)	*1.1*	*1.1*	*1.1*	*1.1*
Voted spending				
Temporary	*5.2*	*4.0*	*0.4*	*0.2*
Windfall capital investment		*0.25*	*0.75*	*1.25*
Permanent ('core')	*85.9*	*91.2*	*95.7*	*100.5*
Growth in core spending	*5.9*	*5.2*	*4.6*	*4.8*
Growth in core spending, per cent	*7.4*	*6.1*	*5.0*	*5.0*
Memo				
*General Government Balance^^^^*	*10.0*	*11.7*	*16.3*	*18.5*

Note: Rounding can affect totals
^ Existing Level of Service in respect of demographics, NDP and public sector pay commitments.
^^ To be announced on Budget day.
^^^ Technical assumption for 2025 and 2026.
^^^^ SPU 2023 GGB after taking into account the SES 2023 fiscal parameters. A full suite of fiscal forecasts will be published alongside *Budget 2024*.
Source: Departments of Finance and Public Expenditure, NDP Delivery and Reform.

Table 2 - Expenditure Strategy. Source: Summer Economic Statement

	2023	2024	2025	2026
Expenditure ceiling	*91.1*	*95.5*	*96.9*	*102.0*
: core spending	*85.9*	*91.2*	*95.7*	*100.5*
: non-core spending	*5.2*	*4.0*	*0.4*	*0.2*
: windfall capital investment		*0.25*	*0.75*	*1.25*
Memo				
Growth in core spending	*5.9*	*5.2*	*4.6*	*4.8*
Growth in core spending, per cent	*7.4*	*6.1*	*5.0*	*5.0*

The Central Bank, in its Quarterly Bulletin, notes that while the baseline fiscal projections for Ireland show promise in the medium term, there are several challenges and risks on the horizon for public finances. A substantial portion of our budget surplus is attributable to substantial corporation tax, receipts, much of which cannot be attributed to underlying economic developments. These "excess" corporation tax inflows, which could potentially see a sudden reversal, mask a less optimistic outlook for the core General Government Balance, GGB. In fact, without these corporation tax windfalls, the GGB would remain in a deficit in 2023, and the projected surpluses for 2024 and 2025 would be considerably smaller.

It also notes that there are other challenges, including ensuring there are adequate resources to address future aging population and climate transition expenses, providing appropriate support for essential public infrastructure investments, and maintaining the right fiscal stance while the economy operates at full capacity. It outlines the need to withdraw the use of temporary measures and notes that although these temporary measures have been vital in aiding households and businesses during the Covid-19 pandemic and periods of high inflation, 2024 will mark the fifth consecutive year in which "non-core" measures have been of significant scale. This prolonged reliance raises the concern that certain planned temporary expenditures may evolve into permanent fixtures.

NERI stated that budgetary policy should be countercyclical. In NERI's view, the budget as currently set out will add modestly to inflation and overheating and the proposed tax cuts will disproportionally benefit the better off.

NERI outlines that there is a tension between addressing the cost-of-living and avoiding adding to inflationary pressures. NERI states that low-income households need to be protected, not through once-off measures but through structural uplifts and that increases to all social protection payments should fully compensate the rise in price inflation. The minimum wage, NERI argues, should also be increased to the living wage.

Fiscal Position

The Central Bank advised that the public finances are in a healthy position with a headline surplus last year after providing a total of €20 billion in temporary support in 2021 and 2022.

They noted that permanently offsetting the real income falls and maintaining current and capital spending in real terms, especially in light of growing demographic, requires significant spending increases. However, increasing such spending in the absence of offsetting revenue raising measures risk creating inflationary pressures and feeding overheating risks.

In discussing this with the Committee, the Central Bank noted that the most acute need in terms of restrained spending is the need not to feed into inflation, with the other element to ensure the public finances are put on a firm foot structurally, which requires that potentially transitory receipts do not feed into expenditure.

The Central Bank also spoke about the challenges in terms of capacity issues in the economy, and they noted that there is potential to increase the capacity of the economy going forward through infrastructure spending for example. However, they further advised that given the size of the shocks that have occurred, to restore people's incomes, avoid fiscal drag through the tax system, and have capital spending, it is too much spending for the economy at present, and thus difficult choices will need to be made. They acknowledged that there is a need to identify and support those households most acutely affected, but stated that there is a balance to be found between doing that and capital spending on infrastructure.

The Fiscal Council, in their Pre-Budget submission, noted that there are capacity constraints, particularly around the tight labour market, which will inhibit capital expansion or reduce value for money. This is due to severe worker shortages in construction and the increased pressure on materials costs. The Fiscal Council also outlined that these capacity constraints are likely one of the reasons the Government has struggled to spend the full capital allocation in recent years.

NERI outlines that in the short-term the fiscal position is healthy, mainly due to the potentially unsustainable performance of corporation tax receipts.

The medium-to-long term fiscal position is, NERI states, extremely challenging. NERI lists age related expenditure, climate action which will reduce revenues and increase expenditure, and the vulnerability of corporation tax as key concerns.

NERI also outlined that Ireland's per capita spending is low compared to other high-income EU countries and that to meet future challenges (e.g., demographics, decarbonisation, digitalisation) there will need to be significant investment across the economy.

Future Costs

Age Action, in their submission to the Committee also noted the Report of the Commission on Taxation and Welfare, noting the total cost of public pensions is projected to increase from 10% of GDP in 2019 to 15% of GDP by 2050, underlying the need for Government to take seriously the revenue raising recommendations of the Commission.

Age Action also noted that the last three budgets were 'emergency' budgets due to Brexit, COVID-19, climate crisis, inflation, and the Ukraine war. Budget 2024 should address medium-term challenges like decarbonisation, digitalisation, and demographic change, and advise that a new all of government ageing strategy is needed, requiring every department and relevant public body to consider how they will adapt to an ageing population. They further advised that all publicly funded services must ensure fair access to people not comfortable with digital technologies for the next 15-20 years. In addition to this they suggested that a cost-of-ageing study be carried out with would clarify demands on the State in terms of pensions, healthcare, long term care and grants mechanisms.

NERI strongly agrees with the Commission on Taxation and Welfare finding that government revenue must increase materially as a percentage of national income.

Budget 2024 – Issues for Consideration

Capital Investment

The Fiscal Council stated that capital spending does attract ongoing spending commitments, for example hospitals and schools require staffing and maintenance, and that many areas of capital spending (such as housing) are likely to be continuous rather than once off.

They highlighted that to make sure capital investment can be maintained in the future it needs to be financed in a sustainable way.

Further elaborating on capacity issues the Committee notes that the Central Bank, in its Quarterly Bulletin, projects housing completions to be 29,000 next year and 30,000 in 2025, and further notes that the Governments housing plan states targets for 33,450, and 34,600 in 2024 and 2025 respectively. In this regard the Committee queried whether these targets are below what is required and whether this may also contribute to capacity issues in the economy. Responding to this the Central Bank advised that the delivery of the number of houses is below the level they would say is needed in terms of the demographic shifts being experienced and advised that there is an interlink between the capacity constraints in the labour market and the availability of accommodation.

The ESRI also noted that the structural demand estimate for housing at present is somewhere between 30,000 and 35,000 unit per annum but noted that the ESRI plans to revise this estimate later in the year and suggested that when that has taken place these figures will be higher due to demographic changes and net migration trends. They advised that this means the existing imbalance between supply and demand is probably greater than what the figures would suggest at present. They further noted that due to the increased cost of finance for private sector developers and home builders from rising interest rates, this will affect their capacity to deliver on the targets set out in Housing For All and as a result funding may need to be increased, as well as more involvement from the public sector, if those targets are to be achieved.

The Minister acknowledged the concerns raised by the central bank with regards to the increasing capital expenditure at a time when the economy is operating at near full capacity.

The Committee in their engagement with both the Central Bank and the ESRI also discussed the infrastructure bottlenecks that might be addressed through non-budgetary measures. In this regard the Committee notes that there are bottlenecks related to the planning process and further noted that there is legislation to be published in the coming weeks in which the Committee hopes will address some of these bottlenecks. The ESRI, in elaborating on infrastructure bottlenecks, noted that they're currently undertaking a project examining housing markets in the UK and Northern Ireland when compared with the Republic of Ireland. They advised that they are looking at differences across planning, zoning and regulatory issues and advised that there is no doubt that there are sizeable issues around bottlenecks and planning issues in Ireland and the UK.

Observations and Recommendations

1. The Committee notes the significance of the capacity issues in the Irish economy and highlights the need to address these challenges in a way that does not further add to inflationary pressures.
2. The Committee recommends that the Budget provide for sufficient resources to adequately resource any changes to the planning system that arise from the Planning and Development Bill.
3. The Committee notes concerns around the potential impact the housing shortage may be contributing to capacity issues in the economy and highlights the need for Budget 2024 to address this issue.
4. The Committee notes the Central Banks concerns that the forecasted housing output is below the level needed for demographic shifts and emphasises the need for Budget 2024 to address this issue.

National Development Plan

In its discussion with the Fiscal Council, the Committee notes that in a previous report the Fiscal Council suggested that to meet its existing ambitions under the current National Development Plan an additional 24% in expenditure would be required. When queried whether this is still the case, representatives from the Fiscal Council noted that it is now probably a little higher than the figure given due to the rise in inflation. They further noted that in an environment such as the current one where inflation suddenly rises rapidly or there are difficulties getting construction workers there will probably be cost overruns and delays to the projects being fulfilled.

Ibec, in its opening statement to the Committee, stated that the current NDP needs to be expanded by at least €20 billion by 2030 just to meet the initial plans and that there is a need to invest heavily to meet the challenges of net zero, digitisation, ageing and technological change.

In discussing aspect of the National Development Plan with the Minister for Public Expenditure, National Development Plan Delivery and Reform, Paschal Donohoe TD, the Minister advised the Committee that he will prioritise making faster progress on the National Development Plan via introducing legislation aimed at bringing more stability to the planning system. Minster Donohoe also advised that he will further resource the planning system so ensure decisions on large applications for important infrastructure projects are made in a timely manner, this will be done by making more resources available to An Bord Pleanála. The third element the Minister detailed to the Committee to progress the NDP is the allocation of €2.25 billion to maintain the real value of the capital plan at a t time when inflation has been high.

The Committee also raised concerns voiced by the Central Bank that the real level of public investment from 2022-2025 is now projected to be 3 billion lower per annum on average than had been expected in 2021. The Committee further noted that even though the nominal figure has increased, real public investment is now lower than envisaged. Responding to this Minister Donohoe remarked that he has noted the Central Banks critique but advised that that is the reason the government has increased capital expenditure in the coming years by 2.25 billion. He further noted that the Central Bank as also cautioned against significantly increasing capital expenditure in an environment of full employment and high inflation and advised that government is attempting to get this this balance right.

Observations and Recommendations

5. The Committee notes the concerns of the potential increase in expenditure needed to meet the existing commitments in the National Development Plan.

Existing Level of Service

The Committee notes that approximately 3% or €2.3 billion of the core current expenditure increase is available to meet existing levels of service, which the minister advised includes the full-year impact of measures carried over from budget 2023, funding for demographic developments, and meeting public service pay commitments. The Committee raised concerns around how a set amount of funding could be set aside which includes funding for a public service pay deal that has not yet been agreed and therefore the funding required is an unknown amount and queried how this will be presented in the budget book.

Minister McGrath, in discussing the ELS requirements with the Committee acknowledged that the inflationary economic environment has had an effect on the real value of ELS. Minister Donohoe noted that they are increasing year-on-year funding the funding set aside for ELS and advised that he is confident that there will be increases in ELS in a number of Government Departments.

Noting the Fiscal Council's estimate that the stand-still cost (or ELS) for core current expenditure will be around €4.6 billion, NERI highlighted that this is above the SES's proposed increase of €4.3 billion. Therefore, there will be some impact on public services.

The Committee also noted the level of ELS required to maintain current economic situation and in their engagement with the Ministers, queried whether the high level of inflation would impact on the ELS and if so, how significant the impact of this is. Responding to this Minister Donohoe advised that the Budgetary documents for Budget 2024 will show an increase in the funding across Departments for ELS going forward and thus will avoid embedding a structural underfunding for ELS due to inflationary pressures. The Minister further noted that the need to increase ELS funding also played a role in the decision to breach the National Spending Rule.

Fiscal and Monetary Policy Cohesion

The Central Bank highlighted the importance of policy cohesion to avoid persistently higher inflation and in this regard advise fiscal policy must avoid at working at cross purposes to monetary policy and providing additional stimulus to an economy currently operating at capacity.

They noted the Summer Economic Statement signals that Budget 2024 will increase core expenditure by €5.5 billion (6.4%), an additional €250 million windfall capital investment spend, €4 billion in non-core current spending and a doubling of the tax cut package, before considering additional measures that may be introduced on Budget Day. This they noted is significantly more expansionary than outlined in April's Stability Programme Update and shifts the stance of fiscal policy in a pro-cyclical direction, with analysis showing the upward revision to permanent core spending adding to short run inflation which can damage Ireland's competitiveness and the gains in living standards.

With regard to the inflationary effect of an expansionary budgetary strategy, the Committee noted the Central Banks forecast inflation rate in 2024 to be 3.2%.

In discussions with the Fiscal Council, they noted the inflationary effects of an expansionary budget and estimated that the effects of the budgetary plans at present would add 0.2% to 0.4% to inflation next year.

The Central Bank also advised that they are concerned about the potential detachment from the inflationary dynamics of Europe and cautioned that if Ireland becomes out of step with Europe, they, as a Central Bank, cannot respond by raising interest rates further to tame demand. In this regard, they advised that if Ireland ends up on a path where inflation is deviating from that happening in Europe due to fiscal expansion, this will create problems for competitiveness.

The Fiscal Council, in their engagement with the Committee, also advised that in aggregate the economy does not require extra stimulus and noted that monetary policy is providing a cooling effect in the economy. Trying to counteract this, they advised, with a stimulatory fiscal policy will simply exacerbate the extent of the price and wage pressures in the near term.

Responding to the concerns raised by the Fiscal Council when queried by the Committee, Minister McGrath advised that it is his belief that the government has struck the right balance in Budget 2024, but acknowledged that it is a difficult balance to achieve when being cautious about adding to inflationary pressures. The Committee queried whether the reported tax and USC cuts might fuel these inflationary pressures and responding to this Minister McGrath noted that the Program for Government includes tax measures but advised that there have not been any final decisions made with regard tax measures for Budget 2024.

Observations and Recommendations

6. The Committee notes the Central Banks concerns that an expansionary budget will lead to an increase in short-run inflation and emphasises the need to exercise caution in this regard when considering budgetary policies.

Corporation Tax Reliance

The SES notes that a key policy goal is a need to avoid building up permanent fiscal commitments on the basis of revenues that may be transitory, and, in this regard, it is noted that although corporation tax receipts have increased significantly over the past decade, they are concentrated in a small sub-set of firms and firm or sector-specific shocks could greatly affect these revenue streams. In addition to this international tax policy will impact on future receipts although it is acknowledged that the timing of this remains unclear. The Government intends to establish a long-term savings vehicle, to be capitalised from budgetary surpluses, which will provide funding for addressing long term structural challenges such as those posed from ageing demographics and the climate transition as well as ensuring the public services are maintained.

It should be noted that the August Fiscal Monitor shows that corporation tax receipts amounted to €1.8 billion in August, down by €1 billion (36 per cent) on the same month last year. While a sharp decline had been expected, and there may be some timing issues, the drop was somewhat higher than anticipated, underlining the exceptional volatility in this tax head. On a cumulative basis, corporate tax receipts for the year stand at €12.7 billion, €0.9 billion (7.3 per cent) higher than in the same period last year.

There was broad agreement during the Committee’s engagement with stakeholders and the Ministers, that the current reliance on corporation tax was vulnerability for the Irish economy and fiscal position.

The Fiscal Council outlined a number of risks to future corporation tax receipts:

- Drop-off in pharmaceutical companies’ profits,
- August returns highlights volatility/unpredictability,
- Concentration of CT receipts,
- Firm or sector socks a key risk to the sustainability of CT revenues,
- Uncertainty around “excess” CT figure.

However, the Fiscal Council also noted that the implementation of the 15% rate as part of BEPS pillar two could lead to a substantial increase in revenue. Over time this could be offset by the BEPS pillar one, which seeks to reallocate profits to where their sales take place.

NERI stated it would be unwise to fund per spending increases or tax cuts from the “windfall” receipts. NERI notes that the risks of relying on corporation tax are well understood, though also highlighted that the move to the 15% rate will likely increase receipts in 2024.

ICTU also stated it would not be prudent to use windfall receipts to fund ongoing current expenditure or tax cuts.

Observations and Recommendations

7. The Committee agrees, as has been widely discussed, that the current level of corporation tax should not feed into regular spending or tax cuts.

Targeted Measures

Minister McGrath acknowledged the impact of the inflationary environment on those in low income deciles, and noted that for many people living standards have decreased as their income has not increased in line with inflation but suggested that the supports over the last year has targeted those most in need of support, and advised that Budget 2024 will once again endeavour to target those groups most affected. In this regard the ESRI also noted that in the most recent budget the cost-of-living measures were progressive and supported the lower end of the income distribution and were well targeted. However, they did note that outside of the one-off measures social welfare rates and tax bands and credits did not rise in line with inflation and generally what you will see as a result is worsening income inequality.

The Fiscal Council also discussed the targeting of measures and noted that a question that should often be asked of policies is how well targeted they are. They noted that if a subset of the population who are in need of extra support are identified, the best use of public funds is one that is targeted rather than imposing a blanket measure where most of the benefit goes to someone else.

The Committee also raised the use of targeted measures during the meeting with the Ministers and in this regard noted that there is a general acceptance and acknowledgement that those on low and middle incomes are disproportionately impacted by the inflationary environment and cost-of-living increases. Minister McGrath acknowledged that inflation has really impacted people but advised that Budget 2023 went some way towards mitigating the impact on lower-income households and remarked that an independent assessment has shown the previous budget to be progressive in this regard. Minister McGrath advised that the government has worked hard to target as many resources as possible to ensure that lower incomes groups were protected, and advised that this will continue to be the approach of the Government.

Observations and Recommendations

8. The Committee recognises that the impact of inflation has on those in the lower income deciles and wishes to once again highlight the need for measures in the Budget to specifically target supports at those most in need.

Spending Overruns

The August Fiscal outlines that current spending is ahead of forecasts by €1.1 billon. Significant overruns are expected in the Department of Health and the Department of Children, Equality, Disability, Integration and Youth (due to the Ukrainian response).

The Committee also discussed the recent overspends emanating from the Department of Health and what impact this will have on the figures as set out in the Summer Economic Statement, and whether such an overspend will have an impact on next year's budget.

The Committee also raised the issue of spending overruns with the Minister during their discussions on the budget, and remarked on the reported overrun in the Department of Health which will require a supplementary estimate this year. The Committee queried how this would be accounted for, and whether a portion of this overrun will need to be factored into the base next year if it is to be a recurring event. The Committee also queried whether it would have to come out of the €2.3 billion or whether this has also accounted for the overspend. Responding to this Minister Donohoe advised that he is in discussion with the Department of Health and is seeking to identify what share of overspend will recur and what impact this may have on policy measures for next year. He noted that this is being treated seriously and advised that he will inform the Committee of the exact figure following discussions with the Department of Health.

Observations and Recommendations

9. The Committee notes the significant spending overruns in certain Departments and recommends that these be fully reflected in the allocations for 2024, unless there is convincing evidence that the expenditure will not be repeated.

Proposal for a Sovereign Wealth Fund

The Committee raised the Report of the Commission on Taxation and Welfare and the recommendations contained therein. Responding to this Minister McGrath acknowledged the body of work undertaken by the Commission and noted that the Governments proposal for a sovereign wealth fund will go some way to address some of the issues raised by the Commission. In this regard the Committee notes that the Autumn Legislative Programme contains a bill entitled the Future Ireland Fund Bill.

The creation of savings vehicle to help pay for future ageing costs has merit in NERI's view, noting that once the fund is large enough the returns will be an additional revenue source for the State. NERI, however, also believe there is scope for additional infrastructure funds to address ongoing challenges such as the green transition and housing. NERI outlined that regardless of how windfall tax receipts are spent, there is still a need for significant structural revenue increases over the medium-term.

In discussing the proposal for a wealth fund, NERI noted that we have an opportunity to sequester away what is thought to be transitory receipts into a number of different funds perhaps. They suggested that one would be a savings fund, invested abroad over the 2030s and 2040s and would generate a dividend that goes towards paying ageing costs. They also noted that an independent fund could also be used to address infrastructure costs and capital spending over the medium to long term, and this could ensure there is a steady supply of housing year on year even during recessionary periods.

Observations and Recommendations

10. The Committee notes the significance of the Governments proposed sovereign wealth fund and, in this regard, would like to highlight the Committee's report on the topic and the recommendations contained therein.

Spending Rule

The Fiscal Council, in its Pre-Budget Statement, is critical of the plans set out in the SES to breach the 5% spending rule every year to 2026. The Fiscal Council outlined that the SES sets out both increased spending and permanent tax cuts compared to the previous plans (in the SPU). Additional tax cuts of €600 million are now planned every year for 2024 to 2026. Spending is also set to increase above that set out in the SPU, with current spending €1.2 billion higher over the three-year period and capital spending €1.1 billion higher.

The Fiscal Council set out three reasons the breach of the spending rule is a "serious cause for concern":

> *Signal a repeat of Ireland's past mistakes of procyclicality*
>
> With the economy performing strongly and the tight labour market the Fiscal Council stated that any fiscal stimulus above the spending rule is "particularly ill-advised". It also notes that approach set out in the SES "echoes Ireland's past mistakes of using windfalls to finance permanent expansions".

Undermines the National Spending Rule

The Fiscal Council outlined that with EU Fiscal rules likely to place less scrutiny on Ireland (as a result of GDP distortions and other factors) the National Spending Rule takes on more importance and that the decision to break the rule repeatedly "casts serious doubts over the integrity of Ireland's own fiscal framework".

Manner of revision weakens the credibility of Government projections

The Fiscal Council stated that the transparency around the change of approach was poor, noting in particular the presentation of additional capital spending as windfall investment and outside of core spending.

The Fiscal Council was also critical of the overall approach, stating that in proceeding with additional tax cuts and increases to capital and current spending "the Government does not appear to have faced up to the hard choices confronting it". For example, the Fiscal Council highlighted that the Government has committed to providing a roadmap for how PRSI would be increased following the decision to abandon the pension age increases but it has yet to be published.

The Central Bank advised that the government's revised spending plans for next year and projections until 2026 violate the Net Spending Rule introduced in 2021 which aims to stabilize expenditure based on a 3% trend growth and a 2% inflation target, supporting counter-cyclical fiscal policy. They highlighted that it's essential to establish credibility in this framework as common fiscal tools like debt-to-GDP and deficit limits are not suitable for Ireland due to GDP distortions and the specific risk posed by windfall corporation tax.

ICTU set out, in its submission to the Committee, that core public expenditure should grow over the next number of years by more than the 5% spending rule, to not only address the cost-of-living pressures and income inadequacy but address the deficits in public spending across multiple areas.

NERI noted that the spending rule allows for any level of increased spending once it is offset by increased taxes.

Observations and Recommendations

11. The Committee supports the Government decision to spend beyond the 5% spending rule given the current inflationary environment.

Non-Core Expenditure

The Fiscal Council questioned the classification of covid spending as non-core, noting the Minister of Health has stated that much of the Covid spending is no longer temporary. If this spending is added to core spending it would bring the increase to almost 7%.

Throughout the Committee's engagements the Fiscal Council, the Central Bank and the ESRI have raised concerns with regards the way in which what could be characterised as non-core expenditure has been presented and accounted for. Responding to this, the Fiscal Council advised that when non-core expenditure first entered budgetary discourse it related to Covid-19 expenditure, and it made sense to do so. They noted that spending does not have to be significantly transient or temporary to qualify as non-core expenditure but advised that if it were decided to treat a certain expenditure as outside the normal realms then this would be appropriate. However, they advised that they take issue with classifying things that are naturally core spending as non-core expenditure on the basis that is expenditure for a year.

The Fiscal Council further advised that the temporal dimension of spending should not be what determines core or non-core expenditure but advised that it is the unique nature of the spending itself. In this regard, the Fiscal Council noted that in the high uncertain circumstances of the last budget, with sudden hikes in energy prices, uncertain gas supplies and electricity prices, demand can be affected in a significant way and particularly that of the most vulnerable. In this scenario, even had Government classified those temporary supports as core spending and breached the spending rule as a result, the Fiscal Council would still have said it made sense at the time. They added that they have issue where such expenditure classification is being used for those type of supports that are disappearing. The Fiscal Council advised that they could justify temporary supports when they are necessary, whether one labels it as core or non-core, but when it is persistent and the argument is made that because it is non-core it does not count, then that is where they take issue with it.

The Fiscal Council also noted that labelling some capital spending as windfall spending rather than including it as core capital spending is not appropriate and remarked that the numbers they will present in their next fiscal assessment report will include windfall capital spending as core capital spending. Elaborating on this, the Fiscal Council noted that we do not refer to transfer payments that are funded from corporation tax as corporation tax funded transfers or characterise capital spending as debt-financed capital spending, as the financing and expenditure are separated and not labelled in such a way.

Observations and Recommendations

12. The Committee notes the concerns regarding the characterisation of core and non-core expenditure. The Committee recommends that strict criteria for the definition of non-core be agreed by the Government and bodies such as the Fiscal Council and Central Bank.
13. The Committee notes concerns regarding the labelling of "windfall capital investment" and recommends that "windfall capital investment" be included in core capital investment figures.

Once-off Measures

In their Pre-Budget Statement, the Fiscal Council noted it appears likely that "the Government will introduce further expansionary measures at Budget time in the form of additional temporary or non-core measures". The Fiscal Council's view is that "there is little to no justification for further one-off measures" beyond the €4 billion included in the SES. It also outlined that while one-offs were appropriate to address the cost-of-living pressures, energy prices are now falling, and uncertainties have reduced.

Minister McGrath acknowledged that the Budget will provide for some temporary one-off measures aimed at alleviating some of the impacts if the inflationary environment, and noted the Fiscal Councils disagreement on this matter.

In relation to once-off measures, NERI stated that they would only make sense if the inflation rate were expected to be negative and that it should not be a feature of Budget 2024. Related to this, NERI outlined the need to move to multi-annual budgeting and a holistic approach incomes policy based on adequacy.

The Committee notes that there is currently legislation passing through the Oireachtas that will establish a cap on market revenues in the electricity market and in this regard the Committee notes that the proceeds from this will be collected by the Commission for the Regulation of Utilities to be redistributed to support consumers of electricity. When discussing this with the Committee, the Minister explained that consumers will be supported through reduced tariffs in their bills and will apply to revenue generated in the seven-month period from December 2022 to June 2023 inclusive. Minister McGrath advised that provisional scenarios suggest that between €80 million and €150 million can be raised as a result of this initiative.

The Minister also noted that there is a temporary solidarity contribution which was operationalised through legislation in July that was commenced in August and at that time it was estimated that exchequer proceeds from this would be in the range of 200 million to 450 million across this year and next but noted that this will be subject to revision in the Budget 2024 fiscal projections.

Observations and Recommendations

14. The Committee notes the concerns around the use of once-off measures but due to the current inflationary environment supports their limited use for 2024.

Taxation Measures

As outlined previously, the SES set out a taxation package of €1.1 billion for Budget 2024.

NERI strongly cautioned against tax cuts in the Budget, outlining that the evidence is clear that cuts to income tax or USC are highly regressive as higher income households will benefit disproportionately. Such cuts would be procyclical and add to the difficulties of meeting current and future challenges. ICTU also stated it would not be prudent to use windfall receipts to fund ongoing current expenditure or tax cuts.

ICTU also outlined its view that plans to cut income taxes are unwise and should be abandoned, as they would be procyclical, inflationary and regressive. It would also impact on revenue which is needed for spending.

ICTU identified increases to employer and self-employed PRSI, increases in capital taxation, increases to green taxes and reform of the tax expenditure system as areas with the most scope to increase revenue.

In its submission to the Committee, the Irish Tax Institute welcomed the €1.1 billion tax package and the Government's intention to adjust income tax bands and credits.

The Committee also raised the concerns of the Central Bank and the Fiscal Council that the proposed Budget is expansionary and may contribute between 0.2% and 0.7% to inflation next year. Responding to this Minister McGrath acknowledged that the Budget will need to provide help to people where it is warranted but also not to push up inflation. He acknowledged that this will be a difficult balance to strike but noted that he believes that the Government has done so.

Observations and Recommendations

15. The Committee recommends that any taxation measure should be limited to ensuring the tax burden on workers does not increase solely due to inflation linked wage increases or be targeted at those most impacted by the inflationary pressures.

Indexation

The ESRI also noted that they have previously spoken to the Committee on the topic of indexation, and in this regard advised that if welfare rates, tax bands, and tax credits are not indexed or increased in line with inflation then people who received wage increases will also experience higher taxation. Indexation would also give people in receipt of social welfare certainty that their income will grow in line with inflation. They note in this regard that in last year's budget the tax and benefits parameters were not increased in line with inflation and therefore if it were not for the one one-off measures there would have been a regressive pattern seen in the impact on the income distribution.

Observations and Recommendations

16. The Committee notes their recommendations contained in the previous report on indexation and the recommendations in their Pre-Budget Report 2023 and wishes to highlight the importance of providing for measures that will ensure the real incomes of those on lower incomes do not fall due to inflationary pressures.
17. The Committee notes that while once-off measures cushioned the impact of inflation this year, as a result larger increases would be required next year to ensure the standard of living is maintained.

Public Services

In their discussions with the Committee, NERI further noted the impact of the cost-of-living crisis and advised that ultimately Ireland has a high-cost economy, which means the long-term strategy should be to bring down the cost of living in order to target the inadequate purchasing power of wages. They advised that the focus should be on the user cost of public services, including education, health, public transport and so on. NERI noted that it is known that lower-income households tend disproportionately to use public services and a lot of these are fixed costs, therefore focusing on these costs is more progressive and will help those households more in need.

Age Action, in its submission to the Committee, advised that eligibility thresholds should be adjusted as many older persons may lose access to medical cards due to small raises in social welfare payments. They advised an all of government approach is needed to the issue of means testing to ensure basic equity and administrative justice.

Observations and Recommendations

18. The Committee recommends that income thresholds for access to certain public services should be raised in line with changes to social protection payments.

Christmas Bonus

The Fiscal Council outlined that the Christmas bonus, which if paid will have been paid for the 10 years in row, is yet to be budgeted for. The Fiscal Council states that the Christmas bonus should be included in budget projections as the precedent for it being paid has been clearly established.

Observations and Recommendations

19. The Committee recommends that the Christmas bonus in 2024, and beyond, be included in budgetary projections and Departmental allocations from the Revised Estimates.

Appendix 1: List of Witnesses

WEDNESDAY 12 JULY 2023

Department of Finance

- Minster Michael McGrath

Department of Public Expenditure, National Development Plan Delivery, and Reform

- Minister Paschal Donohoe

TUESDAY 19 SEPTEMBER 2023

The Central Bank of Ireland

- Dr Robert Kelly
- Dr Martin O’Brien
- Dr Gillian Phelan

The Economic and Social Research Institute

- Dr Claire Keane
- Prof Kieran McQuinn

WEDNESDAY 20 SEPTEMBER 2023

The Irish Fiscal Advisory Council

- Prof Michael McMahon
- Dr Adele Bergin
- Dr Eddie Casey

The Nevin Economic Research Institute

- Dr Tom McDonnell
- Mr Ciarán Nugent

WEDNESDAY 27 SEPTEMBER 2023
Department of Finance • Minster Michael McGrath **Department of Public Expenditure and Reform** • Minister Paschal Donohoe

Appendix 2: Link to Meeting Transcripts

- Wednesday 12 July 2023
- Tuesday 19 September 2023
- Wednesday 20 September 2023
- Wednesday 27 September 2023

Appendix 3: Link to Opening Statements & Submissions

- Paschal Donohoe T.D., Minister for Public Expenditure, National Development Plan Delivery and Reform
- Michael McGrath T.D., Minister for Finance
- Dr. Robert Kelly, Director of Economics and Statistics, Central Bank of Ireland
- Prof. Kieran McQuinn, Economic and Social Research Institute
- Prof. Michael McMahon, The Irish Fiscal Advisory Council
- Dr. Tom McDonnell, Nevin Economic Research Institute
- Michael McGrath T.D., Minister for Finance
- Paschal Donohoe T.D., Minister for Public Expenditure, National Development Plan Delivery and Reform
- Submission from Age Action Ireland
- Submission from Ibec
- Submission from Irish Tax Institute
- Submission from Social Justice Ireland
- Submission from ICTU

Appendix 4: Orders of Reference

219. (1) There shall stand established as soon as may be, following the reassembly of the Dáil subsequent to a General Election, a Standing Committee, to be known as the Committee on Budgetary Oversight, to examine and, where it considers it appropriate, report to the Dáil on—

(a) the overall fiscal position, including—

- (i) the aggregated position on revenue and expenditure and the General Government Balance, including structural targets;
- (ii) medium-term projections for the public finances;
- (iii) macro-economic forecasts and developments;
- (iv) general fiscal governance including the application of fiscal rules and risks to the fiscal position; and
- (v) matters arising from the introduction of a supplementary Estimate or Estimates that, in its opinion, have or may have significant budgetary implications: Provided that the Committee shall advise the appropriate Committee or Committees of any decision on its part to undertake such consideration and the reason or reasons therefore;

(b) public expenditure policy, including—

- (i) the expenditure position having regard to the Government Expenditure Ceiling and the expenditure benchmark under the Stability and Growth Pact;
- (ii) Ministerial Expenditure Ceilings applying to individual Estimates or groups of Estimates for the Public Services where significant variations from the expenditure profile could potentially impact on the overall fiscal position; and

(iii) the adequacy of planned and actual aggregate levels of capital expenditure and the policies and practices in relation to capital expenditure, including public procurement policy and public private partnership policy, intended to ensure the achievement of value for money.

(c) Exchequer receipts policy.

(2) The Committee may consider a matter of public policy with significant impact on the budgetary position or on the overall fiscal position: Provided that prior to the commencement of such consideration, the Cathaoirleach of the Committee shall consult with the relevant sectoral Committee established pursuant to Standing Order 95.

(3) The Committee may also consider the overall framework for parliamentary engagement throughout the course of the budgetary cycle and may make recommendations thereon to the Committee on Standing Orders and Dáil Reform for that Committee's consideration under Standing Order 119(1)(b): Provided that, in so doing, the Committee shall consult with—

(a) the Committees established pursuant to Standing Order 95 on any recommendations which, in the opinion of the Committee, impact on their role or remit; and

(b) the relevant Minister or Ministers on any recommendations which, in the opinion of the Committee, impact on the role or remit of a Department or Departments, and shall notify the results of such consultations to Committee on Standing Orders and Dáil Reform.

(4) The Committee shall have the following powers:

(a) power to send for persons, papers and records as defined in Standing Orders 96(3) and 99;

(b) power to take oral and written evidence and submissions as defined in Standing Order 96(1) and (2);

(c) power to appoint sub-Committees as defined in Standing Order 96(4);

(d) power to engage consultants as defined in Standing Order 96(14);

(e) power to travel as defined in Standing Order 96(15).

(5) Every report which the Committee proposes to make shall, on adoption by the Committee, be laid before the Dáil forthwith, whereupon the Committee shall be empowered to print and publish such report, together with such related documents it thinks fit.

(6) The Committee shall consist of fifteen members, none of whom shall be a member of the Government or a Minister of State, and four of whom shall constitute a quorum: Provided that—

(a) the Committee and any sub-Committees which it may appoint shall be constituted so as to be impartially representative of the Dáil; and

(b) the provisions of Standing Order 106 shall apply to the Committee

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