WHO IS PAYING FOR REGIONAL BALANCE IN IRELAND?

Edgar Morgenroth[*]

Economic and Social Research Institute, Dublin, Ireland

During good times and bad times, there has been ongoing debate about the extent of regional disparities in income and appropriate policy responses. In a recently published paper Edgar Morgenroth analysed the extent to which resources are redistributed across regions in Ireland through taxes and public expenditure and how this has affected regional disparities. Morgenroth's analysis shows that the operation of the fiscal system reduces income disparities across counties. The gap between the counties with the highest and lowest incomes before taxes and subsidies is significantly reduced once subsidies and taxes are taken into account. The difference between the 'poorest' and 'richest' counties increased over the period 1995 to 2002, suggesting that there was income divergence during the 'Celtic Tiger' era.

Since taxes on personal income and personal subsidies are not the only fiscal transfers that take place the paper also considers a wider range of government expenditure and taxes including all taxes and all direct expenditure by the public service. While there are no officially published data on regional government accounts the data which are published, when combined with reasonable assumptions as to the distribution of expenditure items for which regional information is not published, allow a broad picture of regional government accounts to be constructed for the first time.

This data shows that real resource transfers per head of population (i.e., the per capita excess of expenditure over revenue), have increased over time. In other words, redistribution across regions has increased over time. These transfers tend to flow from richer to poorer areas – a large negative correlation between the implied transfer of resources and real per capita gross value added. Thus the Irish fiscal system acts to reduce regional disparities, even though there are no explicit equalisation rules. Expenditure is positively correlated with real per capita output (Gross Value Added), but tax revenue is even more strongly correlated with real per capita output, implying that the fiscal system operates to transfer resources from richer to poor regions.

Overall, Dublin and the South-West region are substantial net contributors. For example, in 2004 both Dublin and the South-West contributed just over €2,000 per person while in the same year the Midlands region received a transfer of just over €3,000 per person. In

[*] Edgar.Morgenroth@esri.ie

absolute terms the level of transfers is also substantial. In 2004 just over €3 billion were transferred from the 'net surplus regions' Dublin, South-West and Mid-West to the other regions. Overall the tax burden (including social contributions) averages at €11,000 per person in 2004 with a high for Dublin of almost €14,000 per person and a low of €8,500 per person in the Midlands.

While Dublin and the South-West regions have a higher per capita expenditure than other regions, they have an even larger per capita revenue. For example, over the period 1995 to 2004 Dublin accounted for 28.9 per cent of the population, 35 per cent of revenue and 31.4 per cent of expenditure. The Midlands, which accounted for just 5.7 per cent of the population and 4.6 per cent of revenue accounted for 5.5 per cent of public expenditure. Thus while being redistributive the fiscal system does not appear to unduly disadvantage the better off regions.

Given that the debate has been concentrating on expenditures and particularly investment it is particularly interesting to consider trends in real per capita public investment. In real terms the level of investment has increased substantially in all regions. While the Dublin region received a large share of total investment, it also accounts for a large share of the total population. In per capita terms, therefore, Dublin is not favoured when it comes to capital expenditure. Indeed no clear pattern of 'excess' per capita capital expenditure can be detected in the data.

The debate about regional expenditure is implicitly a debate about the trade off between equity and efficiency. In as much as the analysis can address this debate, the results suggest that the Irish fiscal system does provide a mechanism to achieve more equity, while at the same time preserving a higher level of expenditure in the wealth generating regions. The finding that the system provides a significant degree of regional equity is largely the result of the centralised nature of revenue collection in conjunction with the aim to provide similar levels of service across the full range of government activities in all regions. In order to achieve a similar level of equity with a less centralised system would require a more sophisticated system of fiscal equalisation payments across regions. Thus, while many have argued that the Irish system is too centralised this centrality turns out to be an asset in terms of achieving regional equity.

Whether the levels of transfers provide an optimal balance between equity and efficiency cannot be determined with the analysis provided here. However, since there is no clear pattern of 'excess' capital expenditure in the less developed regions, it appears that the bulk of the re-distribution does not tackle any structural deficiencies in those less developed regions, and thus will do little to generate sustained convergence in living standards.

*"Regional Dimension of Taxes and Public Expenditure in Ireland", *Regional Studies*, forthcoming, and currently available on the journal's website under the reference **DOI:** 10.1080/00343400802093839.