



## PBO Note on Proposed new EU Fiscal Rules (EU Economic Governance Framework)

### Key Messages

- Ireland is required to follow fiscal rules as part of the Stability and Growth Pact, which sets out rules on Government debt and deficits for Member States of the European Union. Member States must maintain a budget deficit of no more than 3% of GDP and have a government debt-to-GDP ratio not exceeding 60%.
- Ireland must also adhere to rules for the Structural Budget Balance; that is, the Government Budget Balance (GBB) adjusted for the impact of cyclical or temporary tax receipts and expenditure and one-off measures. The structural balance is used to capture the Government's underlying fiscal position.
- Member States must also adhere to the Medium-Term Budgetary Objective ('MTO'). The medium-term budgetary objective or 'MTO' is a target level for the structural budget position. It is a country-specific target and seeks to take into account the long-term sustainability of the public finances.<sup>1</sup>
- Under the current rules, Member States with large deficits may also be subject to the Excessive Deficit Procedure (EDP). The Excessive Deficit Procedure or 'EDP' begins when an EU Member State has breached (or is at risk of breaching) the 3% deficit rule or has a debt ratio exceeding 60% of GDP that is not falling at a sufficient pace. The EDP follows a step-by-step procedure to restore fiscal and debt sustainability.
- The fiscal rules have, in effect, been suspended since the beginning of the pandemic in March 2020.<sup>2</sup>
- The European Commission has put forward new proposals, which to some extent, are a simplification of current rules and allow for greater fiscal flexibility for Member States. As part of the common EU framework, the European Commission will propose a 'reference fiscal adjustment path' covering four years to ensure Member States have debt on a downward trajectory and a deficit of no more than 3% of GDP. Member States would then submit their medium-term fiscal plans.
- What are the next steps for the proposed new framework? The European Commission intends to reach an agreement between Member States and the European Commission itself ahead of the 2024 budgetary processes for Member States.
- Ireland is currently in compliance with the fiscal rules, partly due to significant increases in revenue collected for the Irish Exchequer and the GDP impact from a large, foreign-owned, multinationals.

1 Parliamentary Budget Office (PBO), [Briefing Paper 6 of 2018](#).

2 European Commission, [Press Release](#).



## Glossary of Terms

**EU** - European Union.

**EC** - This term refers to the European Commission.

**GDP** - 'GDP' stands for Gross Domestic Product.

**GNI\*** - This term refers to Modified Gross National Income. As noted by the Central Statistics Office, this measure is designed specifically to measure the size of the Irish economy excluding globalisation effects.<sup>3</sup>

**Member State** – the term 'Member State' refers to a Member State of the European Union.

**Fiscal Compact Treaty** – The term 'Fiscal Compact Treaty' refers to the 'Treaty on Stability, Coordination and Governance in the Economic and Monetary Union.'

**SGP** – SGP refers to 'The Stability and Growth Pact.'

**NTMA** – National Treasury Management Agency.

**MTO's** – This term refers to the medium-term budgetary objectives (MTO's) of Member States.

**SDP** – This term refers to the Significant Deviation Procedure.

**EDP** – This refers to the Excessive Deficit Procedure.

**SPU** – The term 'SPU' refers to a Stability Programme Update.

**ECB** – The term 'ECB' refers to the European Central Bank. The European Central Bank sets the monetary policies for euro area members, including Ireland.

**PBO** – This term refers to the Irish Parliamentary Budget Office ('PBO').

**GFC** – This term refers to the 'Global Financial Crisis' of the 2008 period which ultimately triggered a worldwide economic slowdown known as 'the crash' or 'the Great Recession'.

**Eurozone** – The term 'Eurozone' refers to the collective 'Euro area' i.e., the geographical area of European Union Member States which have adopted the euro as their currency.

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<sup>3</sup> Central Statistics Office (CSO), *Modified GNI*.



## What is the Stability and Growth Pact?

The Stability and Growth Pact (SGP) is a set of rules designed to ensure that countries in the European Union pursue sound public finances and coordinate their fiscal policies.<sup>4</sup> The rules are intended to ensure fiscal sustainability across the EU, particularly in the context of the Euro area.<sup>5</sup> As previously noted by the Parliamentary Budget Office (PBO), *'The EU fiscal rules of the Stability and Growth Pact (SGP) constitute the main institutional framework shaping fiscal policy in Ireland.'*

The SGP is comprised of two main arms: the preventive arm and the corrective arm. The preventive arm of the SGP is to ensure sound fiscal policies in good times (i.e., an expansionary macroeconomic environment when the economy is growing), to prepare for bad times (times of economic stress such as recessions, global pandemics, supply chain shocks, times of war, etc.). As noted by the European Commission, the 'corrective arm' of the SGP ensures that EU Member States adopt appropriate policy responses to correct excessive deficits (and debts) by implementing the Excessive Deficit Procedure ('EDP').<sup>6</sup>

## Overview of the Rules

Ireland is currently a member of the European Union ('EU') and is required to follow the fiscal rules of the EU. Further rules were introduced by the Fiscal Compact Treaty but not all EU Member States have signed up to the Treaty.<sup>7</sup> Following the Global Financial Crisis, Member States agreed to strengthen fiscal rules (by building on the economic framework set out by the Stability and Growth Pact)<sup>8</sup> to prevent a repeat of the sovereign debt crisis, which affected several members of the Eurozone and to avoid a collapse of the euro currency.

## Debt Rules

These rules require Member States to reduce government debt to below 60% of GDP. Where a Member State has a debt-to-GDP ratio exceeding 60%, Member States are required to reduce the difference between their debt-to-GDP ratio and the 60% target at an average rate of one twentieth per year (over three years).<sup>9</sup>

## Deficit Rules

There is also the 3% deficit rule whereby Member States cannot run a budget deficit exceeding 3% of GDP. In addition, these rules also require Member States to commit to a mandatory balanced budget rule whereby the annual structural balance does not exceed a deficit of 0.5% of GDP.<sup>10</sup>

The structural balance is the General Government Balance adjusted for the impact of cyclical or temporary tax receipts and expenditure and one-off measures such as bank recapitalisations. It is used to capture the Government's underlying fiscal position and gives a better picture of how healthy the government finances really are.<sup>11</sup>

4 European Commission, [Stability and Growth Pact](#).

5 Members of the Euro Area Agreed to further strengthen the fiscal rules by agreeing to the 'Two Pack.' This only applies to Euro Area members.

6 European Commission, [Stability and Growth Pact](#).

7 The Czech Republic and Croatia have not signed the accord.

8 See below for additional information on the Stability and Growth Pact.

9 European Central Bank ('ECB'), [Main Elements of the Fiscal Compact](#).

10 Ibid.

11 Parliamentary Budget Office (PBO), [Briefing Paper 6 of 2018](#).



The Output Gap is the difference between actual GDP and potential GDP, expressed as a percentage of potential GDP. The Output Gap is used to estimate the cyclical position of an economy. If it is negative, this would indicate that there is slack in the economy. By contrast, the economy is assumed to be at risk of overheating if the Output Gap is positive.

### Suspension of the Fiscal Rules: The Covid-19 pandemic

Due to the Covid-19 pandemic, the fiscal rules were suspended. As noted by the Irish Fiscal Advisory Council, *'The "exceptional circumstances" and general escape clauses of the domestic and EU fiscal rules were activated at the start of the Covid-19 pandemic in 2020 and have remained in place into 2022.'*<sup>12</sup> The European Commission activated the escape clause of the Stability and Growth Pact ('SGP') on 13th March 2020 and proposed to the European Council the temporary suspension of the rules in response to the public health emergency. In 2020, all but two Member states (Denmark and Sweden) had a budget deficit that exceeded 3% of GDP. In 2022, due to the Russian Federation invading Ukraine, the European Commission decided to extend the 'general escape clause' of the SGP and deactivate the escape clause in 2024, assuming that certain economic conditions prevail.<sup>13</sup>

### Criticism of the Fiscal Rules

There have been some criticisms of the current fiscal rules. The Excessive Deficit Procedure never led to fines being imposed on high-debt countries (such as Greece and Italy) for non-compliance with the rules.<sup>14</sup> Another concern is that for the purposes of both the 60% debt and 3% deficit targets, capital investment spending (e.g. investment in infrastructure) is treated the same as current expenditure (spending on day-to-day activities).

As noted by Dullien et. al, *'Currently the fiscal rules mostly do not distinguish between investment purposes and other public spending.'*<sup>15</sup> It should be noted that while there is an investment clause under the current rules, Members can only apply for the investment clause if they record a negative growth forecast or a negative output gap of more than 1.5% of potential GDP, so during a recession when they may not have the resources for the investment.<sup>16</sup> However, so far only two Member States have been granted some flexibility under this clause. In Spring 2014, the European Commission rejected a request by Italy to activate the investment clause because they could not ensure compliance with the debt rule.<sup>17</sup>

Another criticism of the current rules is that they lead to pro-cyclical fiscal policies by not encouraging sufficient surpluses when the macroeconomic environment is favourable (i.e., during economic expansion/a growing economy).<sup>18</sup> The The European Stability Mechanism noted that implementing the Stability and Growth Pact did not initially prevent pro-cyclical fiscal policies, despite the intended focus on stabilisation.<sup>19</sup>

12 Irish Fiscal Advisory Council, *Fiscal Rules - Exceptional circumstances continue*.

13 European Commission, *European Spring Package: Sustaining a green and sustainable recovery in the face of increased uncertainty*.

14 European Journal of Political Economy, *Fiscal Discipline in EMU? Testing the effectiveness of the Excessive Deficit Procedure*.

15 Dullien et. Al, *Between high ambition and pragmatism: Proposals for a reform of fiscal rules without treaty changes*.

16 Ibid.

17 European Stability Mechanism, *EU fiscal rules: reform considerations*.

18 Parliamentary Budget Office (PBO), *Potential Output, the Output Gap and Associated Key Issues for Fiscal Policy-making in Ireland*.

19 European Stability Mechanism, *EU fiscal rules: reform considerations*.



It should also be noted that the output gap can be considered a poor real-time indicator, leading to inappropriate policy decisions. The Parliamentary Budget Office published a paper on this issue<sup>20</sup>, entitled '[\*Potential Output, the Output Gap and Associated Key Issues for Fiscal Policy-making in Ireland\*](#)'. This paper noted several issues around the output gap being poor at identifying issues in real-time and the potential for the rules to reinforce pro-cyclical policies. The PBO paper also noted concerns regarding the Expenditure Benchmark. The Expenditure Benchmark is a spending rule. This rule limits the net growth rate of government spending at or below a country's medium-term potential economic growth rate. As noted in the paper, '*the Expenditure Benchmark might not represent a desirable anchor for counter-cyclical fiscal policy in Ireland, particularly in good economic times.*' The paper also noted '*the risk that cyclical revenues might not be identified and could be used to fund permanent expenditure increases or measures narrowing the tax base.*'

The Parliamentary Budget Office, has in the past, noted concerns that the rules have been poor at identifying various issues in real-time. Calculating the output gap is difficult to estimate, particularly in real-time.<sup>21</sup> In addition, the PBO has previously noted that assessments of the Irish economy in real-time have been misleading (i.e., notably missing the 2004-2007 boom period).

Another concern around the EU's fiscal rules is that they are possibly out-dated, given the significant world events that have occurred in recent times. The submission by Conseil d'Analyse économique (French Council of Economic Analysis) entitled '[\*Reforming the European Fiscal Framework\*](#)', noted that despite changes in the European macroeconomic environment, '*that it [the fiscal framework] appears even more outdated in the post-Covid context of massive increases in public debt, low-interest rates and new joint European debt and recovery plans.*'<sup>22</sup>

Another concern is that due to the complicated nature of the rules, they are not readily understood, and it is difficult to achieve buy-in when the rules are not understood. In addition, and in the case of Ireland, there are specific issues for Ireland as GDP doesn't give a true picture of Ireland's economy, hence why GNI\* is now a more widely used metric to measure Irish economy activity.<sup>23</sup>

## Newly Proposed EU Governance Economic Framework

On the 9th of November 2022, the European Commission adopted a Communication entitled '[\*Building an economic framework fit for the challenges ahead\*](#)', which sets out the path toward a reformed EU economic governance framework.<sup>24</sup> The European Commission proposed these changes in response to a public consultation on the fiscal rules with Member States.

How the new framework works:

- **Step One:** As part of the common EU framework, the European Commission would present a '*reference fiscal adjustment path*', covering four years based on its debt sustainability analysis methodology. The reference fiscal adjustment path should ensure fiscal sustainability. Using a single operational indicator - nationally-financed net primary expenditure (i.e., spending net of discretionary revenue measures which also excludes interest/debt servicing spending as well as

20 Parliamentary Budget Office (PBO), [\*Potential Output, the Output Gap and Associated Key Issues for Fiscal Policy-making in Ireland\*](#).

21 Ibid.

22 Conseil d'Analyse Economique, [\*Reforming the European Fiscal Framework\*](#).

23 Central Bank of Ireland, [\*The Disconnection of GDP from Economic Activity Carried out in Ireland\*](#).

24 European Commission.



cyclical unemployment spending), would serve as the basis for setting the fiscal adjustment path.

It should be noted that the fiscal adjustment path for a Member State (to be agreed with the Commission) will be based on an adjustment in net primary spending, which also helps ensure debt is on a sustainable trajectory. The Debt Sustainability Analysis (DSA) model will be used to determine the 'reference fiscal adjustment' path. A Debt Sustainability Analysis is an economic model/tool used to determine a member state's debt sustainability and trajectory. It studies a country's medium-term to long-term debt situation.<sup>25</sup>

The DSA model shows how a country's current debt and prospective borrowing level affects its present and future ability to meet debt service obligations. It is primarily measured by the debt-to-GDP ratio and its projected trajectory. Please see footnote below as an example of a DSA model.<sup>26</sup> EU Member States will also be ranked according to high, medium, and low risk according to the DSA. The DSA model, which will determine the risk profile of a country's debt trajectory, will therefore be a determinant of the net primary expenditure path, i.e. the spending trajectory.

- **Step Two:** European Member States then submit plans for their medium-term fiscal path and public investment commitments. It should be noted that as part of this step, Member States could propose a longer adjustment period, extending the budgetary adjustment path by up to three years when the path is underpinned by a set of reform and investment commitments that support debt sustainability and respond to common EU priorities and targets. However, while Member States can propose an extension to the adjustment period, this would have to be approved by the European Commission.
- **Step Three:** The Commission would assess the plans, providing a positive assessment if debt is placed on a downward path or stays at prudent levels and the budget deficit remains credibly below the 3% of GDP reference value over the medium term. The European Council would endorse the plans following a positive assessment from the Commission.
- **Step Four:** As a final step, the European Commission would continuously monitor the implementation of the plans. EU Member States would submit annual progress reports on the implementation of the plans to facilitate effective monitoring and ensure transparency.

The Macroeconomic Imbalance Procedure ('MIP') aims to identify potential macroeconomic risks early on and to prevent the emergence of harmful macroeconomic imbalances. The Parliamentary Budget Office has previously published some reports on the Macroeconomic Imbalance Procedure and its impact on the Budgetary Process.<sup>27</sup>

The proposals set out by the European Commission are intended to lead to enhanced dialogue between the Commission and Member States to understand the challenges identified and the policies needed to address them. In turn, Member States would commit to include the reforms and investments needed to prevent or correct imbalances in their national medium-term fiscal plans.<sup>28</sup> The assessment of whether imbalances exist would aim to detect, and address them, early on.

<sup>25</sup> Parliamentary Budget Office, [PBO Debt Sustainability Analysis Calculator Explainer Guide](#).

<sup>26</sup> Parliamentary Budget Office, [PBO Debt Sustainability Analysis Calculator Explainer Guide](#).

<sup>27</sup> Parliamentary Budget Office, [European Semester 2018 - and how it interacts with Ireland's Budget 2019](#).

<sup>28</sup> Ibid.



## Next Steps

It is hoped that the European Commission and Member States will reach a consensus on the proposed economic governance framework ahead of the budgetary process for 2024. This would mean agreement in 2023 as the Budgets for 2024 have to be submitted by 15th October of this year.

## What does this mean in practise?

The proposals put forward by the European Commission could be interpreted as a simplification of the current fiscal rules towards a new framework of rules that allows Member States more time to reduce debt burdens. However, this will depend on the fiscal adjustment path. Under the current rules, Member States can in theory apply for activation of the investment clause however in practise this has only occurred in a few instances.<sup>29</sup>

The slightly less fiscally onerous approach was noted in a recent publication by the Irish Fiscal Advisory Council, which stated, '*The Commission's proposals represent some shift away from a rules-based framework and could represent a relaxation of the existing fiscal rules depending on what fiscal paths are agreed*'.

## Submissions made during the public consultation process

As part of the public consultation process, the European Commission received 225 valid submissions from respondents in 25 different countries, including 21 EU Member States and 4 non-EU countries. Submissions received as part of the consultation on the fiscal rules can be summarised into six different themes<sup>30</sup>:

1. Incentivising public investment;
2. Sustainability of public finances;
3. Macroeconomic stability;
4. Governance: improving compliance, ownership, and enforcement;
5. Preventing macroeconomic imbalances and strengthening economic and social resilience; and
6. EMU deepening: Completing Banking Union and the Capital Markets Union.

Some of the submissions are discussed below.

In a joint submission by Spain and the Netherlands, they noted that while the fiscal rules should focus on the core objectives of debt sustainability and sustainable public finances, any necessary fiscal consolidation measures should be designed in a way to facilitate growth.

<sup>29</sup> European Commission, [Press Release - Commission issues guidance to encourage structural reforms and investments](#).

<sup>30</sup> European Commission, [Commission Staff Working Document: Online public consultation on the review of the EU economic governance framework. Summary of Responses. Final Report](#).



The German Government's submission suggested simplifying the EU's fiscal rules while continuing to apply uniform and comparable parameters. However, the submission also noted that strict compliance with the 1/20th debt reduction rule might require too much fiscal adjustment for certain Member States.

The submission by the German Government also suggested reviewing the possibility of making the European Fiscal Board (EFB) independent from the European Commission. It said this could facilitate more consistent implementation of the rules.<sup>31</sup>

In summary, the submissions by Spain, Germany, and the Netherlands all noted the need for greater flexibility in the fiscal rules and public investment, particularly in the context of climate change and the need to decarbonise economies.

The submission by Bruegel (an economic think tank based in Brussels) noted the need to balance fiscal rules with the need for public investment for the climate<sup>32</sup>. The submission called for a '*green golden rule*', which would mean excluding net green investment from the fiscal indicators used to measure compliance.<sup>33</sup>

The submission by the International Monetary Fund (IMF) stated that the EU rules needed reform.<sup>34</sup> The IMF proposed several changes to the rules, suggesting that independent national fiscal councils would have a more significant role in assessing fiscal risks and macroeconomic projections. The IMF submission also said that strengthening implementation required national ownership of the EU fiscal rules.<sup>35</sup>

The European Economic and Social Committee submission noted that a revision of the EU governance framework was not only necessary for fiscal stability over the short-to medium term but also for providing finance for the green transition and ensuring full employment<sup>36</sup>. The submission also called for the introducing of a '*golden rule*' for public investments in combination with an expenditure rule.<sup>37</sup>

The submission also called for proposals to be put forward by the European Commission for a transition period, during which time the excessive deficit procedure should not be triggered with the possibility of using the "unusual event clause" on a country-specific basis.<sup>38</sup>

The Parliamentary Budget Office notes that several submissions called for an end of the 1/20th debt reduction rule, simplifying the rules, a greater role for national fiscal councils and for public investment (particularly on climate) to be differentiated from current Government spending.

Some submissions also suggested changing the 60% 'reference value' target for public debt levels, i.e., that the Government debt of each EU Member State should not exceed 60% of GDP. The ESM noted that as post-pandemic debt levels were elevated due to the fiscal stimulus provided by Governments during the COVID-19 pandemic, returning to the 60% debt-level target is unrealistic for many Member States. The submission noted that '*requiring all euro area Member States to converge to the current 60% debt-to-GDP reference value appears unrealistic, and risks undermining fiscal framework credibility*'.<sup>39</sup>

31 Ibid.

32 Bruegel, [A green fiscal pact: climate investment in times of budget consolidation](#).

33 Ibid.

34 International Monetary Fund (IMF), [Reforming the EU Fiscal Framework: Strengthening the Fiscal Rules and Institutions](#).

35 Ibid.

36 European Economic and Social Committee, [Reshaping the EU fiscal framework for a sustainable recovery and a just transition](#).

37 Ibid.

38 Ibid.

39 European Stability Mechanism, [EU fiscal rules: reform considerations](#).



The submission called for a new debt-to-GDP target of 100% of GDP but noted that this would require treaty changes.

Another concern in the ESM submission was that after the global financial crisis, efforts to comply with the fiscal rules might have discouraged public investment. The financial crisis and subsequent market pressure led to reductions in government capital spending, particularly for countries subject to an economic adjustment programme.<sup>40</sup> The ESM also noted that a recession should allow for the triggering of the exception clause under the Stability and Growth Pact provided expenditure is for capital/ investment spending rather than current spending.

A lot of the suggestions submitted have been taken on board by the European Commission as per the changes proposed for the new fiscal framework. Some suggestions were not adopted, such as changing the 60% debt-to-GDP target.

## What has changed? What remains the same?

### Changes

- The possibility of greater flexibility (depending on what fiscal paths are agreed)<sup>41</sup> – Member States can now propose a longer adjustment path to the Commission. It is envisaged that plans for reforms and investments will also be submitted.
- 1/20th rule will not apply – The rule which requires that the difference between a government's debt level and the 60% debt-to-GDP target reduce by an average of one twentieth will no longer hold. It was noted in the European Commission's Communication that a rapid adjustment period for Member States with high debt-to-GDP ratios could damage economic growth and could be counterintuitive. In its publication of the proposed new rules, the European Commission noted that *'The current debt reduction benchmark (the so-called 1/20th rule) implies, in the current circumstances of high debt ratios post-COVID, a too demanding frontloaded fiscal effort that risks jeopardising growth and is pro-cyclical.'*
- The Medium-Term Objective (MTO) is being disposed of. The MTO sets out the minimum requirement for the budget balance (adjusted for the business or economic cycle).
- The Expenditure Benchmark is also being discarded. This is being replaced by a net expenditure rule.
- Stronger enforcement regime – With more scope provided to Member States to design their fiscal trajectories, a more stringent EU enforcement regime will underpin multilateral surveillance. Independent fiscal institutions could potentially play a greater role in assessing the assumptions underlying fiscal plans. In Ireland's case, this would mean the Irish Fiscal Advisory Council.
- The new framework also proposed moving away from a structurally adjusted balance to a net expenditure rule.
- The economic sanctions for non-compliance with the framework will be reduced. The fines are being reduced with the expectation that greater national ownership of the rules (due to the increased role of national fiscal councils) will ensure greater buy-in for-into the fiscal rules.

<sup>40</sup> Ibid.

<sup>41</sup> Irish Fiscal Advisory Council, [\*Potential Reforms to the EU Fiscal Rules - Fiscal Assessment Report November\*](#).



## The Same

- The broad fiscal targets remain the same. The 3% deficit-to-GDP ratio remains as does the target for a government debt level not exceeding 60% of GDP.

## What does this mean for Ireland?

Although currently suspended, Ireland complies with the fiscal rules, partly due to surging tax receipts from Corporation Tax resulting in a budget surplus and a large, foreign-owned multinational sector which greatly impacts Irish GDP. As has been well documented in the past, GNI\* is a better measure for the Irish economy than GDP due to the large distortions caused by the large size of the MNC sector. However, the fiscal rules require a deficit of less than 3% of GDP and a debt-to-GDP ratio of no more than 60% (or at least a debt ratio on a downward trajectory where this ratio is above 60%).

For Ireland, the suspension of the MTO and the Expenditure Benchmark removes the complexity of calculating the structural balance. Due to our large multinational sector, the structural balance has long been a problematic indicator for Ireland. Removing this rule should make Ireland's fiscal rules more straightforward to understand and comply with.<sup>42</sup> The complexity of the rules has long been criticised, especially as a country could meet some rules and miss others due to complex calculations.<sup>43</sup>

The Parliamentary Budget Office has previously noted issues regarding the Structural Balance, including the fact that it has been subject to large ex-post revisions over time and is difficult to estimate.

There must be clarity on the expectations for a Member State in advance of the return of the rules. It may be necessary to domestically legislate for these changes (as was the case for the Fiscal Compact Treaty after it had been agreed through a referendum). There must be a clear understanding of how the changes to the SGP, and the existing Fiscal Compact Treaty will coexist. One potential area of concern of the proposed new rules is the potential for disagreement between domestic macroeconomic and fiscal forecasts and those of the Commission. A Member State might build their budget based on more favourable forecasts not reflective of the true underlying situation. For this reason, there is a risk of potential abuse of the rules.

## Conclusion

In conclusion, Ireland is subject to fiscal rules as part of our membership of the European Union. Under the Stability and Growth Pact, Ireland must maintain a budget deficit of less than 3% of GDP and a government debt-to-GDP ratio of less than 60%. These rules have, in effect, been suspended since the beginning of the global pandemic in March 2020. Due to the war in Ukraine and the economic uncertainty this has brought, the suspension of the rules will continue into 2023.

The European Commission has proposed a new Common Framework of fiscal rules. The proposal for a new fiscal framework from the European Commission arises from a public consultation process around the current fiscal rules. In broad terms, the 3% deficit and the 60% debt-to-GDP rule remain

<sup>42</sup> The Irish Fiscal Advisory Council, *Box H: Covid-19, the structural balance, and once-off/temporary measures*.

<sup>43</sup> Trinity College Dublin (Adele Bergin and John Fitzgerald), *The Structural Balance for Ireland*.



unchanged. The proposals set out by the European Commission will allow Member States to request a longer adjustment period, and it is envisaged that independent fiscal councils will have a greater role in assessing assumptions underlying fiscal adjustment paths. In Ireland's case, this would be the Irish Fiscal Advisory Council. It should also be noted that the requirement to reduce the difference between government debt and the 60% debt-to-GDP target at a rate of 1/20th per annum is being removed. The European Commission noted in their recent Communication on the fiscal rules that the activation of the general escape clauses (i.e., the suspension of the fiscal rules) in March 2020 allowed for fiscal stimulus, which helped members during the COVID-19 global pandemic. The new proposed framework is setting out rules that are intended to be more flexible than the current rules .

The new framework is intended to improve surveillance by the European Commission and the European Council, with Member States submitting annual progress reports. Member States also need to set out net expenditure plans over four years. The Commission will provide more details on fiscal policies in the first quarter of 2023. The Commission intends to agree budgetary processes with Member States ahead of their respective 2024 budgetary processes.