legislation enshrining the fiscal rules in Irish law. Third, they entail an expanded role for national independent fiscal institutions, such as the Fiscal Council.

Crucially, Ireland is likely to face less scrutiny under the new EU fiscal rules. This reflects their focus on GDP-based measures (Casey and Cronin, 2023). However, a more appropriate assessment on a GNI* basis and reflecting excess corporation tax would signal greater risks. The Council assesses that the National Spending Rule should be further developed as a "first line of defence" to ensure sound management of the economy and public finances at home.

Box F: Updated reform proposals to the EU fiscal rules

In April, the European Commission (2023b) published its latest reform proposals for the EU fiscal rules. These proposals build on the Commission's initial set of ideas from November last year (European Commission, 2022), and follow on from discussions among EU Member States. Box E of the *November 2022 Fiscal Assessment Report* discussed the original proposals in greater detail. Here, we take a look at the key elements of the updated proposals.

The November communication introduced the concept of a risk-based economic governance framework based on a country's debt ratio. Under the proposals, the scale and speed of the required fiscal adjustment depended on whether a Member State had a substantial, moderate, or low debt challenge.[54] However, these categories no longer exist. Instead, there are only two categories:

1) Member States with a deficit above 3% of GDP or a debt ratio above 60% of GDP.
2) Member States with a deficit below 3% of GDP and a debt ratio below 60% of GDP.

At the outset, all Member States would be expected to prepare "medium-term fiscal-structural plans". These medium-term plans will map out a Member State's net spending path, as well as its reform and investment commitments. Low debt countries would face little scrutiny. The Commission would only provide them with guidance on the structural primary balance necessary to comply with the 3% deficit limit. This would assume no additional policy measures in the 10 years following the period covered by the four-year plan.

However, high debt countries or those with deficits greater than 3% would come under a much sharper focus. First, the Commission would put forward a reference adjustment path for net spending that would ensure debt is put on a plausibly downward course, and the deficit is brought or kept below 3% of GDP over the medium term. These countries would then consider this reference path when designing their own medium-term plans, which would cap net spending increases at a slower rate than might otherwise be considered sustainable.[55] The plan would cover a minimum adjustment period of four years, which could be extended by up to three years if the Member State commits to certain reforms and investments.[56] The plan will be binding once approved by the ECOFIN.[57]

In addition, the latest proposals also involve an assessment by the Commission as to whether:

- The debt ratio at the end of the path (between 4 and 7 years out) is below its level in the year before the path begins;
- In cases where Member States run deficits greater than 3% of GDP, that this is reduced by 0.5% of GDP each year. The proposals are ambiguous in terms of what this 0.5% refers to;

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[54] A substantial debt challenge was defined as a debt ratio above 90% of GDP. A moderate debt challenge was defined as a debt ratio between 60% and 90% of GDP. Lastly, a low debt challenge was defined as a debt ratio below 60% of GDP (European Commission, 2022).

[55] In this instance, sustainable means in line with usual — or "potential" — economic growth, and, by extension, revenue growth. This is one area where an unobservable measure (potential growth) remains in place in the new framework.

[56] The criteria include whether the reform and investment commitments are: 1) growth-enhancing; 2) support fiscal sustainability; and 3) in line with common EU priorities, such as the European Green Deal (European Commission, 2023).

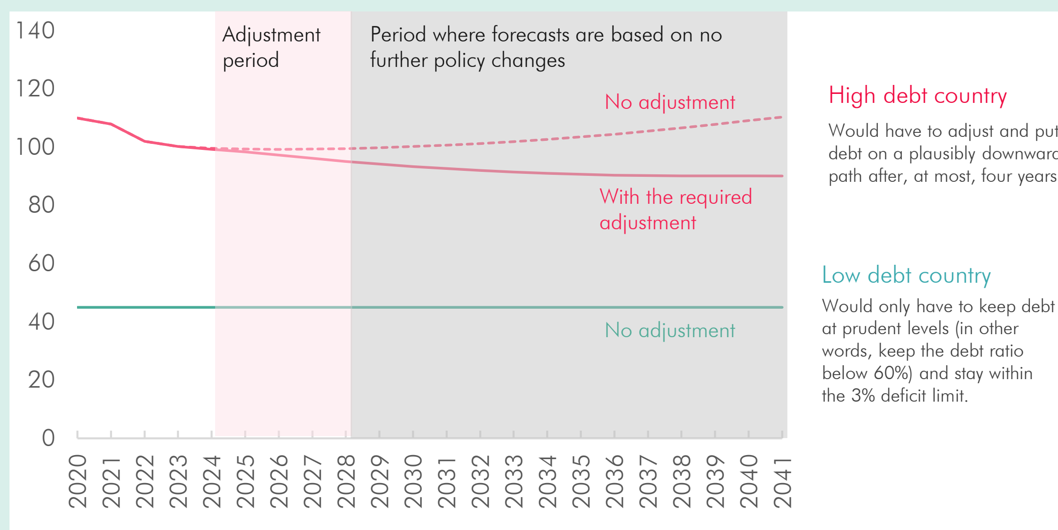
[57] The ECOFIN is the part of the Council of the EU comprising Member States' economics and finance ministers.

- In cases where Member States benefit from an extended fiscal adjustment period, that they deliver most of the adjustment during the first four years covered by the plan;

To illustrate how the new proposals might work, Figure F1 provides an illustrative example. We take two countries, one with a starting debt ratio of around 100% and the other with a starting debt ratio of 45%. For simplicity, we assume neither country is expected to breach the 3% deficit limit such that all that matters is the expected debt path. The low debt country would not come under much scrutiny, provided it complies with the 3% deficit limit. By contrast, the high debt country would have to grow net spending at a slower rate than otherwise planned, thereby ensuring its debt ratio is on a plausibly downward trajectory by the end of the adjustment period (assumed to be four years here).

Figure F1: The path for debt plays a key role in how the rules work

Debt ratio (% GDP)



Source: Casey and Cronin (2023)

Looking ahead, the Commission intends to swiftly agree upon the revised rules with the Member States, with a view to activating them from 2024. However, the proposed legislative changes will need to be agreed by both the European Parliament and the ECOFIN.

What do the latest proposals mean for Ireland?

Ireland is unlikely to come under much scrutiny under the proposed reforms to the EU fiscal rules (Casey and Cronin, 2023). GDP will continue to underpin the Commission's debt ratio assessments despite it being an inappropriate measure of the Irish economy. Ireland's debt ratio is currently below 60% of GDP and is projected to stay below this level. In addition, substantial injections of corporation tax receipts continue to flatter Ireland's budget balance and, as a result, its debt path.

Casey and Cronin (2023) explore how the proposed new framework might look were it better tailored to Ireland. They substitute GNI* for GDP and adjust for excess corporation tax receipts when determining the stress tests. They find a very different, albeit still encouraging, picture for how public debt is likely to evolve. The Commission's approach, if applied on this basis, might involve closer monitoring under the new EU fiscal rules if these aspects were allowed for.

Independent fiscal institutions could take on wider responsibilities

The proposals envisage a stronger role for independent fiscal institutions (IFIs), such as the Irish Fiscal Advisory Council. While traditionally mandated to assess compliance with *national* budgetary rules, the reforms propose IFIs assess compliance with the *EU rules* as well. That is, they would assess whether the budgetary outturns reported in the Government's annual progress reports comply with the agreed net spending path. However, to deliver upon this expanded role, the Commission notes that IFIs would require greater levels of resources and improved access to data.

Moreover, IFIs would be expected to carry out a number of additional tasks. These include:

- producing or endorsing budgetary forecasts underpinning the Government's medium-term plans;
- assessing the Government's debt sustainability analyses;
- assessing the impacts of policies with fiscal sustainability and growth-enhancing implications.