

Box 5: Proposed reforms to the European fiscal rules

Following a pandemic-related pause, the European Commission relaunched its review of the EU's Economic Governance Framework (EGF) in October 2021. The review revolves around *inter alia* potential reform of the Union's fiscal rules, which constitute the framework within which Member States make budgetary decisions.

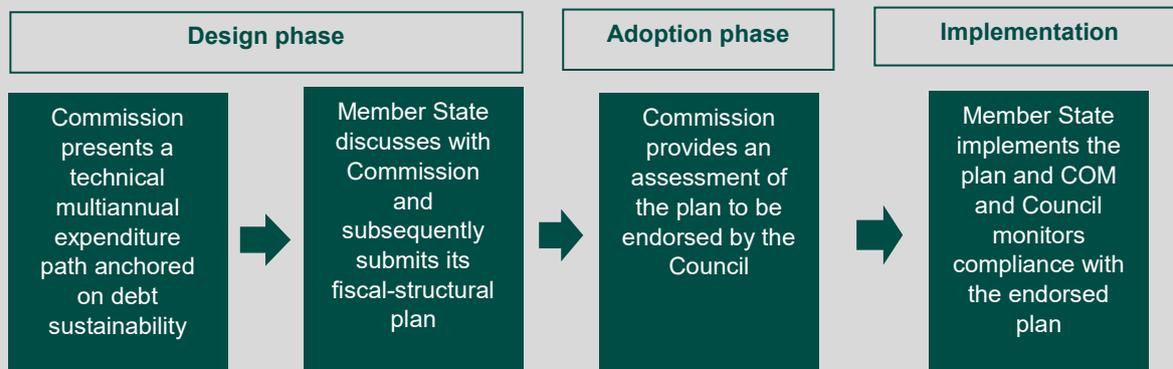
The current set of fiscal rules, known as the *Stability and Growth Pact* (SGP), first came into effect in 1999. They have subsequently been revised twice, most recently following the Global Financial Crisis. Notwithstanding these revisions, changes in the macroeconomic environment (not least due to increasingly frequent economic shocks), elevated levels of public debt in some Member States, and excessive complexity have raised fundamental questions as to whether the rules remain fit-for-purpose.

In November 2022, the European Commission set out an overview of its proposals for a reformed set of rules.[^] The Commission's proposals incorporate a greater focus on the medium-term, with new 'fiscal-structural plans', set over a four-year horizon, forming the cornerstone of the proposals. These national plans, combining the current Stability Programme Update and National Reform Programme, are intended to allow for greater country-specific differentiation, while still being assessed and agreed within a common rules-based framework. The basis of this common framework would be the Commission's existing debt sustainability analysis (DSA) methodology, which would allow for an assessment of debt trajectories over the medium term..^{^^}

Under the proposals, the Treaty reference values of a 3 per cent budget deficit and 60 per cent debt-to-GDP ratio would remain unchanged. Member States would be categorised according to the extent of their public debt challenges, based on the Commission's DSA. This categorisation would determine the length of the adjustment period for putting debt on a sustainably declining path. The adjustment period could be extended if a Member State commits to reforms and investments which could help put debt on a more sustainable path.

Assessment of the national fiscal plans would be based on a single operational indicator – net primary expenditure^{^^^} – anchored on a debt target. As a first step, the Commission would put forward multi-annual fiscal trajectories for Member States, based on results from the DSA – with the trajectory corresponding to the minimum fiscal effort required to put debt on a sustainably declining path over the medium-term. Following a bilateral dialogue with the Commission, Member States would then submit a medium-term fiscal-structural plan for assessment by the Commission and endorsement by the Council (**figure 16**).

Figure 16: Summary of the reform proposals



Source: European Commission

The Commission's proposals have formed the basis for discussion of a new framework among Member States over recent months. Member States agreed Council Conclusions^{^^^} on the Economic Governance Review at the European Union's monthly Finance Minister's meeting (ECOFIN) on 14th March. The Council Conclusions highlight a number of areas of convergence that have emerged in the discussions so far, as well as identifying areas where additional work is needed.

The next step in the process is for the Commission to bring forth legislative proposals.

[^] *Communication on Orientations*, European Commission (2022), available at: https://economy-finance.ec.europa.eu/system/files/2022-11/com_2022_583_1_en.pdf

^{^^} See *Fiscal Sustainability Report 2021*, European Commission (2022), available at: https://economy-finance.ec.europa.eu/publications/fiscal-sustainability-report-2021_en

^{^^^} The expenditure indicator is net of discretionary revenue measures, as well as interest expenditure, EU-funded expenditure and the cyclical element of unemployment spending.

^{^^^} *Orientations for a reform of the EU economic governance framework - Council Conclusions*, European Commission (2023), available at: <https://data.consilium.europa.eu/doc/document/ST-6995-2023-REV-1/en/pdf>