Brussels, 3 December 2010

BACKGROUND

ECONOMIC and FINANCIAL AFFAIRS COUNCIL
Tuesday 7 December in Brussels

Proceedings will start on Monday 6 December with an informal dialogue between Council representatives and a delegation from the European Parliament, focusing on economic governance.

The Euro Group will meet, also on Monday, as from 17.00.

On Tuesday at 9.00, ministers will hold a breakfast meeting to discuss the economic situation.

Starting at 10.00, the Council will be called on to approve a draft directive aimed at strengthening administrative cooperation between the member states in the field of taxation, one of a number of savings taxation and tax governance measures aimed at preventing tax evasion and tax fraud.

The Council is due to take a formal decision on financial assistance to Ireland, as agreed at the Informal meeting on 28 November, setting out the conditions for granting that assistance.

Other items on the agenda include bank levy schemes and the accounting of pension reforms, for which the Council is expected to approve reports for submission to the European Council. It will also take note of progress on legislative proposals on economic governance and adopt conclusions on public healthcare, financial crisis management and on the code of conduct on business taxation.

At lunch, the French delegation will present the programme for its country's presidency of the G-20 and ministers will discuss EU representation at the G-20.

Press conferences:
- after the Euro Group meeting (Monday evening);
- at the end of the Council (Tuesday, before lunch).

Press conferences and public events by video streaming: http://video.consilium.europa.eu/

Video coverage for preview and download in broadcast quality (MPEG4): http://tvnewsroom.consilium.europa.eu

For reasons of security with regard to the EU-Russia summit being held on the same day, it is necessary for media representatives who are not in possession of an EU inter-institutional press card to request accreditation for access to the building. For last-minute accreditation: www.european-council.europa.eu/summitswiththirdcountries/media-accreditation

1 This note has been drawn up under the responsibility of the press office
COMBATING TAX FRAUD: ADMINISTRATIVE COOPERATION

- Public deliberation

The Council will be called on to reach political agreement, on the basis of a compromise proposed by the presidency, on a draft directive aimed at strengthening administrative cooperation in the field of direct taxation.

The draft directive is intended to enable the member states to better combat tax evasion and tax fraud. In the light of greater taxpayer mobility and a growing volume of cross-border transactions, it sets out to fulfil their growing need for mutual assistance – especially via the exchange of information – so as to enable them to better assess taxes due.

One of a number of measures implementing the EU's strategy against tax fraud, launched in 2006, it provides for an overhaul of directive 77/799/EEC, on which administrative cooperation in the field of taxation has been based since 1977.

The Council reached broad agreement on the draft directive in November 2009, whilst noting political reservations by the Luxembourg and Austrian delegations. The text was again discussed in January as part of a package of measures related to the taxation of savings interest and governance in tax matters.

With a view to enabling a compromise to be reached, the text has now been split from the package and key provisions have been redrafted. The Council examined the draft at its meeting on 19 October, focusing on provisions regarding the automatic exchange of information. It asked the Permanent Representatives Committee to oversee further technical work with a view to reaching political agreement.

Two issues have yet to be resolved, in relation to:

- automatic exchange of information. The text would require the automatic provision of information on certain categories of income and capital held by non-residents that are residents of the recipient member state. The positions of member states diverge, however, in relation to the information they have and are willing to send. The presidency compromise provides for a step-by-step approach aimed at eventually reaching unconditional exchange for eight categories of information;

- exchange of information on request. Certain delegations, concerned about the risk of member states making imprecise requests aimed at detecting irregularities ("fishing expeditions"), ask for details to be specified in the directive regarding the format for requests, in accordance with an OECD standard. The presidency compromise on this issue offers two alternatives: the first would involve specifying certain details regarding the format for requests; the second would provide for a transition during which two member states that have signed a bilateral tax information exchange agreement could require each other to respect a specified format when making requests for information (thereafter, the format to be used for requests would be as established by an implementing regulation to be adopted by the Commission).

The draft directive sets out to implement an OECD model tax convention on income and capital as regards the exchange of information on request, thus eliminating bank secrecy in cross-border situations. It would prevent a member state from refusing to supply information concerning a taxpayer of another member state on the sole grounds that the information is held by a bank or other financial institution.
In addition, the directive would:
- extend cooperation between member states to cover taxes of any kind;
- establish time limits for the provision of information on request and other administrative enquiries;
- introduce provisions on the automatic exchange of information;
- allow officials of one member state to participate in administrative enquiries on the territory of another member state;
- provide for feedback on the exchange of information;
- provide that information exchange be made using standardized forms, formats and channels of communication.

Based on articles 113 and 115 of the Treaty on the Functioning of the European Union, the draft directive requires unanimity for adoption by the Council, after consulting the European Parliament.

**ECONOMIC GOVERNANCE**

- **Follow-up to the October European Council**

The Council will be briefed by the chairman of the Economic and Financial Committee regarding work in progress on legislative proposals from the Commission aimed at strengthening the EU's economic governance provisions.

On 29 September, the Commission approved six legislative proposals on economic governance, dealing in particular with budgetary discipline in the member states and the coordination of economic policies.

On 28 and 29 October, the European Council endorsed the final report from a task force established in March to devise proposals to provide for better budgetary discipline in the member states and a budgetary crisis resolution framework at EU level. Further to this:
- as regards budgetary discipline and the coordination of economic policies, it called on the Council and the European Parliament to reach agreement on the ensuing legislation by the summer of 2011, on the basis the Commission's proposals, so as to enable a rapid and effective implementation of the group's recommendations;
- on budgetary crisis resolution, further to the work of the task force, it asked its President to undertake consultations on a limited change to the EU treaties in order to establish a permanent mechanism to safeguard the financial stability of the euro area. It will revert to this at its meeting on 16 and 17 December with a view to taking a final decision both on the outline of a crisis mechanism and on a limited treaty amendment.

On 28 November, the Euro Group agreed on the outlines of a crisis mechanism, to be called the European Stability Mechanism:


The agreement builds on discussions held in the framework of the mandate given to the President of the European Council, Herman Van Rompuy.

The proposals on economic governance are based on articles 121, 126 and 136 of the Treaty on the Functioning of the European Union, allowing for adoption by the Council by qualified majority.
FINANCIAL SUPPORT FOR IRELAND

The Council, in accordance with the agreement reached at an informal meeting on 28 November, is expected to adopt:

- a decision providing financial assistance to Ireland, on the basis of regulation 407/2010 on the European Financial Stability Mechanism (EFSM);
- a recommendation setting out the conditions for that financial assistance, in the framework of the EU's excessive deficit procedure.

On 28 November, ministers approved an EUR 85 billion package of financial assistance to Ireland in response to a request submitted by the Irish authorities on 22 November.

The package includes:

- EUR 10 billion to be used immediately to recapitalise Irish banks, with a EUR 25 billion contingency reserve;
- EUR 50 billion to cover the financing needs of the Irish government's budget.

Half of the banking support measures (EUR 17.5 billion) will be financed by an Irish contribution through its treasury cash buffer and investments in Ireland's National Pension Reserve Fund. The remainder of the overall package (i.e. EUR 22.5 billion each) will be shared equally amongst: (i) the EFSM, (ii) the European Financial Stability Facility, together with bilateral loans from the United Kingdom, Denmark and Sweden, and (iii) the International Monetary Fund.

The loans will be provided on the basis of a programme negotiated with the Irish authorities by the Commission and the IMF, in liaison with the European Central Bank. The programme will involve an overhaul of Ireland's banking system, growth-enhancing reforms, and the correction of Ireland's excessive deficit by 2015, extending a previous 2014 deadline.

Ireland has been the subject of an excessive deficit procedure since April 2009, when the Council set out measures to reduce the deficit to below 3 % of gross domestic product by 2013. But in response to a worsening of the economy, whilst acknowledging Ireland's compliance with its recommendations, the Council in December 2009 agreed to extend the deadline to 2014.

The draft decision is based on regulation 407/2010, allowing for adoption by the Council by qualified majority. The draft recommendation, based on article 126(7) of the Treaty on the Functioning of the European Union, requires a qualified majority of euro area member states, excluding Ireland, for adoption by the Council.

PREPARATION OF THE DECEMBER EUROPEAN COUNCIL

- Impact of pension reforms on implementation of the stability and growth pact

The Council will be called on to approve a report, to be submitted to the European Council meeting on 16 and 17 December, examining how the impact of pension reforms should be accounted for in implementation of the EU's stability and growth pact.

The report was requested by the European Council meeting in October. In the context of the current reform of EU economic governance provisions (see above), in particular plans to impose stricter sanctions on member states that violate the pact's debt and deficit criteria, the European Council asked the Council to speed up work to establish how the impact of pension reforms is accounted for in implementation of the stability and growth pact.
Nine member states, led by Poland and Hungary, which have introduced or are introducing reforms in order to establish a so-called multi-pillar pension system (both public and private), have asked for a review of the way in which the costs generated by such reforms are accounted for. The group consider that the reforms increase their budget deficits in the shorter term despite creating benefits for the sustainability of public finances in the longer term. Poland and Hungary advocate that the cost of pension reform programmes be therefore excluded from public debt and deficit figures.

The draft report acknowledges that discounting the costs of pension reforms when taking decisions under the excessive deficit procedure for a defined period of time is one way to take into account the impact of pension reforms. However, it excludes any modification to the EU treaty protocol on the excessive deficit procedure or to rules applied by the EU's statistical office, Eurostat, in its assessment of public accounts.

In 2005, rules on implementation of the stability and growth pact were amended, allowing for the costs of pension reforms (establishing mandatory funded defined contribution schemes) to be deducted at diminishing rates over a period of five years from the moment at which a member state enacts its pension reform. This notably applies when an excessive deficit procedure is opened and when a decision is taken to close the procedure.

A multi-pillar pension framework consists of a public pillar without a specific fund allocation (often referred to as "pay-as-you-go"), a fully-funded second pillar, and possibly individual private funds that constitute a third pillar. In a mandatory fully-funded or "second pillar" scheme, a government may receive funds from households or employers that are then invested in the market. If it is a "defined contribution" scheme, individual pension benefits will depend on the accumulated assets, leaving no risk for the government. Therefore, Eurostat decided in 2004 that even if such a scheme is managed by the government, it cannot be treated in national accounts as a social security scheme. As a consequence, the flows of contributions and benefits under such schemes are not recorded as government revenue or expenditure. The introduction of such schemes may therefore lead to higher deficit and debt statistics.

- **Levies on banks**

The Council is expected to approve a report on bank levy schemes, to be submitted to the European Council meeting on 16 and 17 December, examining how different schemes in place should be coordinated so as to avoid the multiple charging of banks that operate in several member states.

Bank levies are amongst the measures being examined as part of a new crisis resolution framework for the financial industry. They could also help ensure that the industry makes a fair contribution to the consolidation of public finances, thus relieving the pressure on taxpayers.

Governments in the EU provided public support to financial institutions in 2008 and 2009 amounting to 16.5% of EU gross domestic product. In order to relieve national budgets and shift part of the burden back to banks, a number of member states have imposed levies on banks or are in the process of doing so.

The draft report comes in response to a request by the European Council in October, which noted the need for further work – both at the international level and within the EU – on both bank levies and the introduction of taxes on financial institutions.
The report notes that it is unlikely that all member states will introduce levies or taxes in the short term, given that ten member states are considering introducing a levy at a late stage. However, national systems, with different parameters, are likely to co-exist in the short term, although the risk of the multiple charging of financial institutions is currently limited to only some member states.

The report states that multiple charging mainly occurs when a country either introduces a levy that also covers subsidiaries of its financial institutions in other member states or when a country imposes a levy on the branches of banks based in other member states. However, few member states have introduced such a levy – for instance, France and the United Kingdom, which have addressed the issue by concluding a double charging agreement. The report warns nevertheless that the problem could become more significant if other member states were to introduce a levies with such a scope. In such an event, the Central and Eastern European member states could be particularly affected due to the significant share of foreign ownership of their banking institutions.

The report also warns that differences in national levies can lead to distortions of competition and relocation of businesses, although these risks are likely to be limited in the short term.

In a communication presented in May\(^2\), the Commission suggested that general principles be agreed on so as to enable a coordinated approach. And it recommended that \textit{ex ante} resolution funds be established – to be financed by a levy on banks – in order to facilitate the resolution of ailing banks as part of a new EU crisis resolution framework for the financial industry.

In a report to the October European Council, the Council noted a growing consensus regarding the base and scope of bank levies, though not so as concerns the precise objective pursued and the question of whether the proceeds should go to member states' general budgets or be channelled into specific crisis resolution funds.

Progress on the issue at international level has so far proven difficult. At a summit in Toronto on 27 June, the G-20 agreed that the financial industry should contribute towards the costs of resolution. However, whilst acknowledging that some countries are pursuing the option of a financial levy, it noted that other countries are using other approaches.

HEALTHCARE

The Council is expected to adopt conclusions on public healthcare services, welcoming the findings of a joint report on the subject by the Commission and the Economic Policy Committee (\textit{doc. 16940/10}).

The draft conclusions (\textit{doc. 16939/10}) emphasise the need for health system reforms in the member states for the more effective use of public resources and the provision high quality services. To this end, the text defines policy challenges that will need to be addressed.

The text reaffirms the Council's commitment to its long-term strategy for meeting the economic and budgetary consequences of ageing populations, which involves:
- reducing levels of public debt at a fast pace;
- raising employment rates and productivity rates;
- reforming pension, healthcare and long-term care systems.

\(^2\) Doc. 10394/10
In the EU as a whole, public spending on health accounted for 14.7% of total government expenditure and 7.4% of gross domestic product (GDP) in 2008 (up from 12% and 6.6%, respectively, in 1998). According to a 2009 joint report by the Commission and the Economic Policy Committee on the impact of ageing populations, public spending on health is projected to further increase within a range of 0.7 to 2.2% of GDP on account of demographic factors and technological developments. Health expenditure has often risen at a faster rate than GDP growth.

CRISIS MANAGEMENT IN THE FINANCIAL SECTOR

The Council is expected to adopt conclusions on crisis prevention, management and resolution in the banking sector, on the basis of a communication from the Commission (doc. 15375/10).

The Commission is currently preparing a crisis management framework comprising three types of measures, namely preparatory and preventative measures, early intervention by supervisory authorities and instruments and powers for crisis resolution. The draft conclusions (doc. 17006/10) welcome the broad thrust of the Commission's programme, as well as its intention to present legislative proposals in spring 2011. The Council is also expected to agree that exceptional crisis rules on state aid for banks should be extended until the end of 2011.

The draft conclusions also examine issues such as fair burden-sharing by financial institutions, the principal elements of the future regulatory framework and of preparatory and preventative measures, principles on early intervention, as well as crisis resolution and the medium-term financing of resolution measures.

HARMFUL TAX COMPETITION - CODE OF CONDUCT

The Council will receive of a six-monthly report from a working group on implementation of a code of conduct aimed at eliminating situations of harmful tax competition in the EU with regard to business taxation. It will be called on to adopt conclusions.

The working group is responsible for assessing:
- the "rollback" of tax measures deemed as harmful (i.e. where favourable tax treatment in one member state attracts businesses from other member states);
- the monitoring of a "standstill" commitment by member states not to introduce new measures that are harmful.

The report summarises the group's work during the Belgian presidency.

OTHER ITEMS

The Council, without discussion, will take note of progress reports regarding work:
- on the VAT (value-added tax) treatment of postal services;
- on a draft regulation on the short selling of securities and on credit default swaps (doc. 17039/10).