Brussels, 29 February 2008

BACKGROUND[1]

ECONOMIC and FINANCIAL AFFAIRS COUNCIL

Tuesday 4 March in Brussels

*The Council will be preceded as usual by a meeting of the **eurogroup**, on Monday, 3 March, starting at 17.00, which, in particular, will examine the economic situation, as well as a second series of annual updates of euro area member states' stability programmes, and economic and employment policy guidelines for the euro area member states.*

Ministers will hold a breakfast meeting on Tuesday at 9.30 to discuss the economic situation, on the basis of the Commission's interim forecasts, and developments on financial markets. The president of the eurogroup will report on deliberations of the previous evening.

*Starting at 10.00, the Council is due to adopt opinions on a number of annual updates of the member states' **stability and convergence programmes**. It will prepare a number of dossiers to be referred to the spring European Council, namely this year's update of the EU's **broad economic policy guidelines** and **country-specific recommendations**, as well as a report on **financial stability**.*

*The Council will discuss **sovereign wealth funds** and adopt conclusions establishing priorities for the EU's general **budget for 2009**. It will also adopt conclusions on **VAT fraud** and will be briefed by the Commission on the promotion of **savings tax** measures with certain third countries such as Singapore, Hong Kong and Macao.*

At lunch, ministers will discuss issues related to the European Bank for Reconstruction and Development and the World Customs Organisation.

Press conferences:

- after the eurogroup meeting *(Monday, as from 20.00)*;
- at the end of the Council, before lunch (*Tuesday, as from 13.00*).

Press conferences and public events can be followed by video streaming:
http://www.consilium.europa.eu/videostreaming

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[1] This note has been drawn up under the responsibility of the press office

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Stability and convergence programmes

The Council is due to adopt opinions on a number of annual updates of the member states' stability and convergence programmes, namely:

- updated stability programmes presented by Austria, Cyprus, Greece, Ireland, Malta, Portugal, Slovenia and Spain;
- updated convergence programmes presented by Bulgaria, the Czech Republic, Denmark, Estonia, Latvia and Lithuania.

This follows adoption of opinions on a first series of programmes at the Council's meeting on 12 February.

Under the EU’s stability and growth pact, member states having the euro as their currency are required to present stability programmes, and those not participating in the single currency to present convergence programmes.

The programmes are required to set out the member states’ medium-term budgetary objectives (MTOs), the main assumptions about expected economic developments and important economic variables, a description of budgetary and other economic policy measures, and an analysis of how changes in assumptions will affect their budgetary and debt position.

The aim is to ensure sound government finances as a means of strengthening the conditions for price stability and for sustainable growth, conducive to employment creation.

Based on article 99(5) of the European Community treaty, the opinions require a simple majority within the Council for adoption.

Preparation of the spring meeting of the European Council

- **Broad economic policy guidelines**
- **Country-specific recommendations**

The Council is due to approve reports, to be submitted to the spring meeting of the European Council (13 and 14 March), on:

- the EU's broad economic policy guidelines (BEPGs) for the 2008-2010/2011 period, to be included in integrated guidelines for growth and jobs (*doc. 6728/08*);
- the 2008 update of country-specific integrated recommendations on economic and employment policies (*doc. 6775/08*).

The BEPGs, which contain economic policy recommendations for implementation at national level, as well as specific recommendations for the euro area, are part of a single set of guidelines for both economic and employment policies. The employment recommendations are due for approval by the Employment, Social Policy, Health and Consumer Affairs Council at its meeting on 29 February.

Once endorsed by the European Council, the guidelines and recommendations will be adopted by the Council without further discussion.

Both texts are based on article 99(2) of the European Community treaty, requiring a qualified majority within the Council for a decision.

- **Financial stability**

The Council will hold an exchange of views on the situation on financial markets and on progress with financial stability issues, with a view to further discussion by the European Council at its spring meeting (13 and 14 March). It is due to approve an interim report on the subject, to be submitted to the European Council, in the light of a communication from the Commission.

The draft Council report examines ongoing work on financial market stability, in the light of the sustained period of volatility on global financial markets experienced since last August.

At its meeting on 9 October, the Council adopted conclusions on a series of initiatives to be followed in response to weaknesses identified in the financial system. These combine actions of both a regulatory and non-regulatory nature around four main objectives:

- improving transparency in the market, notably as concerns banks' exposures relating to securitisation and off-balance sheet items;
- upgrading valuation standards to respond in particular to problems arising from the valuation of illiquid assets;
- strengthening the EU's prudential framework for the banking sector, e.g. with respect to the treatment of large exposures, banks' exposures to securitisation as well as liquidity risk management; and
- investigating issues such as the role played by credit rating agencies.

The Commission's communication suggests that the European Council confirms principles to guide the EU, both internally and in international fora, as well as a series of actions for endorsement.

The draft Council report notes that growth in the EU economy is expected to moderate this year, although the extent of the slowdown should remain limited in Europe because of strong fundamentals and the absence of significant macroeconomic and financial imbalances. The Commission has issued an interim forecast for GDP growth for 2008 of 1.8% for the euro area and 2% for the EU as a whole, many of the downside risks identified in its autumn forecast having materialised, including a significant rise in oil prices and a strengthening in the euro exchange ratio.

In the current context, the draft states, EU economic and financial policies should be geared towards ensuring macroeconomic stability and pursuing structural reforms.

- **Sovereign wealth funds**

The Council will hold an exchange of views on issues relating to sovereign wealth funds, on the basis of a communication from the Commission and with a view to further discussion by the European Council at its spring meeting (13 and 14 March).

Sovereign wealth funds are state-owned investment vehicles funded by foreign-exchange assets. More than thirty countries have established sovereign wealth funds since the early 1950s, most of those in the last eight years; the biggest funds are sponsored by China, Kuwait, Norway, Saudi Arabia, Singapore and the United Arab Emirates.

Sovereign wealth funds are estimated to control assets of between EUR 1.5 and 2.5 trillion – more than all the world's hedge funds together – up from merely hundreds of billions a few years ago.

In its communication the Commission suggests promoting the definition at international level of a code of conduct to ensure greater transparency, predictability and accountability in sovereign wealth funds; a code that would involve countries that invest in such funds.

EU budget

- **Council priorities for the 2009 budget**

The Council is due to adopt conclusions setting its priorities for the EU's general budget for 2009 (*doc. 6704/08*). It may hold a brief exchange of views.

The Council conclusions will be used by the presidency as a broad mandate for negotiations with the Parliament and the Commission later this year.

The 2009 budgetary procedure will be the third to be followed under the EU's financial framework for the period 2007-13. The draft conclusions emphasise that the May 2006 inter-institutional agreement on budgetary discipline and sound financial management must be applied to the full, and that the annual limits set by the financial framework itself must be strictly respected.

The conclusions also emphasise:

- the growing role of common foreign and security policy and the need for it to continue to be adequately funded,
- the continued need to monitor and improve the effectiveness of the EU's institutions with a view to improving administrative efficiency and reducing bureaucracy;
- the need to keep firm control on the funding of the EU's decentralised agencies.

Combating tax fraud

The Council is due to adopt conclusions on the issue of combating value-added tax (VAT) fraud, on the basis of a communication from the Commission (*doc. 6859/08 + ADD 1*).

Although few estimates are available of the volume of taxes not collected in the EU due to tax fraud, it is estimated to account for 2 to 2.5% of GDP. Free circulation of goods within the internal market since 1993 has resulted in member states being less capable of fighting tax fraud on their own.

In May 2006, the Commission issued a communication highlighting issues to be addressed in order to tackle tax fraud. VAT, in particular, is vulnerable to a practice known as “carousel” fraud, where goods are traded so as to enable fraudulent businesses to deduct input VAT whilst the supplier deliberately does not pay the VAT that is due.

In November 2006, the Council adopted conclusions setting out the following priorities:

- an action plan to ensure more efficient use of administrative cooperation;
- exploration of ways for member states to protect other member states’ VAT revenues;
- possibilities for more rapid and detailed exchange of information between member states;
- the examination of potential changes to the VAT system with a view to enhancing the legal possibilities for combating VAT fraud.

In June 2007, the Council adopted conclusions requesting the Commission to present legislative proposals for conventional measures to tackle tax fraud by reinforcing the existing VAT system, and to analyse the effects of possible more far-reaching measures to modify the system. As regards the latter, it called on the Commission to report on both the possible taxation of intra-Community transactions and the possible optional use of a generalised reversal of tax liability (the so-called reverse-charge system). In December 2007, it adopted further conclusions urging the Commission to present its findings.

In its communication, approved in February, the Commission examines the potential for both types of measures for tackling fraud: the taxation of intra-Community transactions and the generalised reverse-charge system.

Under a reverse-charge system, which is already used in specific limited cases in some member states, the VAT liability for transactions between companies is shifted from the company providing the supply to the company receiving the supply. The Commission also examines the possibility of running a reverse-charge system pilot project in one member state.

The majority of member states consider that fundamental changes to the VAT system should only be examined if conventional measures failed to be efficient in tackling fraud. And although two delegations want the Commission to rapidly present a proposal for a pilot project, many have reservations on the idea of a generalised reverse-charge system.

The draft conclusions accordingly give priority to work on legislative proposals for conventional measures, and state the Council's intention to revisit the question of more far-reaching measures by the end of 2011, including the possibility of a pilot project.

Taxation of savings - Contacts with third countries

The Commission will brief the Council on progress made in its contacts with certain third countries and territories as regards the promotion of savings tax measures that are equivalent to those applied in the Community.

Savings tax measures are currently applied in the EU under directive 2003/48/EC, in five third countries (Andorra, Liechtenstein, Monaco, San Marino and Switzerland) and ten member states' associated and dependent territories (Anguilla, British Virgin Islands, Cayman Islands, Montserrat, Turks and Caicos, Aruba, Netherlands Antilles, Guernsey, Jersey and the Isle of Man under savings tax agreements).

In conclusions adopted in October 2006, the Council asked the Commission to start exploratory talks with Singapore, Hong Kong and Macao, and to report back. This will be the first time that the Commission reports on its contacts.