



Brussels, 5 June 2009

BACKGROUND¹

ECONOMIC and FINANCIAL AFFAIRS COUNCIL

Tuesday 9 June in Luxembourg

*The Council will be preceded as usual by a meeting of the **eurogroup**, on Monday 8 June, starting at 17.00.*

On Tuesday at 9.00, ministers will meet for the annual governors' meeting of the European Investment Bank.

*Starting at 10.30 on Tuesday, the Council is due to prepare a number of dossiers to be referred to the **European Council** (18 and 19 June).*

*In particular, it will discuss the reform of the EU's **supervisory framework** for financial markets, following on from the recommendations of the De Larosière group aimed at strengthening the supervisory system and rebuilding trust in the wake of the global financial crisis.*

*Also to be referred to the European Council: the international financing of **climate change** measures, the assessment of **bank support schemes** and implementation of the **European economic recovery plan**.*

*The Council will moreover discuss the **economic situation** and developments on financial markets, and will hold an exchange of views with two representatives of the IASB on the issue of international **accounting standards**.*

*It is also due to discuss the promotion internationally of **good governance** in tax matters.*

At lunch, ministers are due to discuss preparations for forthcoming G-20 meetings, in particular with regard to reform of the International Monetary Fund and the World Bank.

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://video.consilium.europa.eu/>

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

ECONOMIC AND FINANCIAL SITUATION

- Update on the current situation

The Council is due to hold an exchange of views, on the basis of an update by the Commission and the European Central Bank, on the economic situation and the latest developments on financial markets.

The Commission is also expected to inform the Council of its intentions regarding budgetary surveillance procedures following the latest fiscal notifications by the member states.

- International accounting standards

Ministers will hold an exchange of views on international standards used for the valuation of financial instruments with Sir David Tweedie, chairman of the International Accounting Standards Board (IASB), and Gerrit Zalm, chairman of the trustees of the International Accounting Standards Committee Foundation.

At an informal meeting in Prague on 3 and 4 April, ministers issued a statement calling on standard setters to work urgently with financial market supervisors to achieve clarity and consistency in the application of valuation standards internationally.

They noted that, while financial reporting rules are vital for investor confidence, the current rules could unduly intensify pro-cyclicality – namely the tendency to encourage fluctuations on volatile markets – which should be avoided.

The statement endorsed a G-20 agreement to implement actions to mitigate pro-cyclicality, including a requirement for banks to build buffers of capital resources during economic good times. It highlighted an urgent need to address the issue of the valuation of assets in distressed and inactive markets where market prices cannot be considered as a reliable reference.

The United States have recently amended their accounting rules, which could result in significant divergences in international accounting practices for financial instruments and possible distortions of competition.

In these circumstances, ministers called on the IASB to cooperate closely with the US Financial Accounting Standards Board in order to rapidly address such issues, and the presidency requested the Commission to review the relevant aspects of EU rules on accounting standards.

Under regulation 1606/2002, the Commission can decide on the applicability of international accounting standards within the EU, but cannot independently introduce new standards or modify IASB standards.

In their discussion with Mr Tweedie and Mr Zalm, ministers are expected to make clear their concerns.

PREPARATION OF THE EUROPEAN COUNCIL

The Council will prepare a number of dossiers to be examined by the European Council at its meeting in Brussels on 18 and 19 June, namely:

- **European supervisory framework for financial markets**

The Council is due to adopt conclusions, to be submitted to the European Council, on the reform of the EU's supervisory framework for banking, insurance and securities markets.

The conclusions will set out the Council's position on the recommendations of a high-level reflection group chaired by Jacques de Larosière² aimed at strengthening the supervisory system and rebuilding trust in the wake of the global financial crisis.

At its meeting on 19 and 20 March, the European Council agreed on the need to improve the regulatory and supervisory framework, and that the recommendations of the De Larosière group should be the basis for action. It called on the Council to examine the group's report, as well as proposals from the Commission, with a view to taking first decisions at its meeting on 18 and 19 June. Legislative proposals to give effect to the new framework will follow in the autumn.

In its report, issued in February, the De Larosière group set out its vision for a new system of European financial supervision. Central to this are proposals to strengthen cooperation and coordination between member state supervisors, including through the creation of European supervisory authorities and, for the first time, a European body charged with overseeing risk in the financial system as a whole.

In a communication issued last month (*doc. 10511/09*), the Commission invites the European Council to endorse a reform along the following lines:

- creation of a European Systemic Risk Council (ESRC)³ to continuously assess the stability of the financial system. The ESRC, chaired by the president of the European Central Bank, would have the authority to issue warnings/recommendations for remedial action and to monitor responses;
- establishment of a European system of financial supervisors (ESFS) to develop common approaches to the supervision of individual financial firms, protect consumers and contribute to the development of a single set of harmonised rules. The ESFS, composed of three new European supervisory authorities⁴ working in a network with national supervisory authorities, would draw up technical standards, help ensure the consistent application of EU law and resolve disputes between national supervisors.

Legislative proposals would aim to ensure that the new framework becomes operational during the course of 2010.

The Council is expected to agree with the objectives laid down in the Commission's communication. A number of issues remain to be resolved, however, in particular the legal basis to be used in establishing the two new structures and the powers to be conferred on the three supervisory authorities.

The Economic and Financial Committee will hold an extraordinary session in Luxembourg on Monday 8 June in order to prepare the Council's discussion.

² Former managing director of the International Monetary Fund.

³ Referred to as the European Systemic Risk Board (ESRB) in the draft Council conclusions.

⁴ Responsible, respectively, for the banking, insurance and securities industries.

- **European economic recovery plan**

The Council is due to approve a report to the European Council on implementation of the European economic recovery plan, approved in December in response to the global financial crisis and economic slowdown (*doc. 10349/09*).

The plan, equivalent to around 1.5% of EU gross domestic product (about EUR 200 billion), provides a framework for measures taken by each member state, in response to its specific circumstances, and identifies a number of actions to be undertaken at EU level.

These include an increase in European Investment Bank interventions, especially for SMEs, for renewable energy and clean transport in particular, as well as the simplification of structural fund procedures and the strengthening of investments in the field of energy and infrastructure, including broadband internet.

At its meeting on 19 and 20 March, the European Council noted good progress in implementing the European economic recovery plan. At the same time, it emphasised continued implementation of agreed measures and asked the Commission and the Council to assess and monitor these and to report back in June.

The overall budgetary support provided by member states is estimated at around five percentage points of gross domestic product in 2009-2010. Member states have thereby fully responded to the recovery plan. With the economic and budgetary outlook forecast by the Commission, further budgetary stimulus would not be warranted, the draft report states, and attention should shift towards consolidation.

So far, the report states, recovery measures generally appear to be timely, targeted and designed in a manner consistent with the long-term priorities of the EU's Lisbon strategy for growth and jobs. The challenge now is to ensure that temporary measures are reversed as the economy recovers. And the effectiveness of some measures requires further monitoring.

- **Bank support schemes**

The Council is due to approve a report to the European Council assessing the effectiveness of measures taken, in particular bank support schemes, with the aim of restoring the stability and functioning of financial markets (*doc. 10351/09 + ADD 1*).

In the wake of the global financial crisis, a large majority of member states have taken measures in support of the financial sector involving guarantees and recapitalisation. The measures are defined at national level, in accordance with principles established by the Council at its meeting on 7 October (*see press release 13784/08*). More recently, a limited number of member states have implemented or announced, with a variety of approaches, measures to deal with impaired assets.

As regards the treatment of impaired assets, ministers agreed on the following principles at the Council's meeting on 10 February:

- a correct and consistent approach to valuation is of key importance in avoiding distortions of competition;
- banks benefiting from support schemes should keep a portion of the risk, and some specific conditions related to management may have to be included;
- while there should be some flexibility concerning the choice of assets selected, full transparency should be ensured;
- close monitoring of the implementation of such measures is essential.

The level of public resources that are potentially committed by the support measures varies widely; the overall effort is considerable, amounting to 31.4% of gross domestic product.

At its meeting on 19 and 20 March, the European Council highlighted the need to deal with impaired assets, on the basis of full disclosure to supervisory authorities, suggesting that further measures may be necessary in order to restore the functioning of credit markets and to facilitate the flow of lending in the economy. It called on the member states to act in a coordinated manner, in line with guidelines provided by the Commission in February and in full respect of the EU's competition rules.

The European Council called on the Council to assess the effectiveness of measures taken and to report back in June.

The draft report finds that state guarantees and recapitalisation schemes have been crucial in stopping the downward spiral that was experienced at the height of the financial crisis, and have had a positive impact on access by banks to wholesale funding, thus clearly supporting credit flows. Where appropriate, measures to further reduce uncertainty by dealing with impaired assets and cleaning banks' balance sheets should however be urgently considered.

An EU-wide stress testing exercise conducted by the Committee of European Banking Supervisors, in the context of its regular analysis of risks and vulnerabilities of the EU banking sector, is expected to better assess resilience to future shocks of the financial system as a whole.

- **International financing of climate change measures**

The Council will be called on to adopt conclusions, to be submitted to the European Council, on the international financing of measures taken to combat climate change.

It will also take note of a report prepared by the Economic Policy Committee and the Economic and Financial Committee on international financing mechanisms in support of climate policies.

The conclusions are intended to contribute to the development of the EU's position on post-2012 provisions, in preparation for the 15th conference of the parties of the UN framework convention on climate change, which will convene in Copenhagen in December.

With a view to achieving a 2°C limit to the global average temperature increase above pre-industrial levels, the European Council in March 2007 committed the EU to a 20% reduction in greenhouse gas emissions compared to 1990 levels by 2020, whilst calling on developed countries as a whole to reduce their emissions to 30%. It stated its willingness to sign up to a 30% target in the context of a sufficiently ambitious and comprehensive international agreement that provides for comparable reductions by other developed countries, and appropriate actions by developing countries.

As regards the financial implications of climate change measures, the European Council in June 2008 requested the Commission to present a strategy so as to enable it to agree on an EU position. In December, it reached agreement on a package of measures at EU level to tackle climate change, with the aim of enabling the EU to maintain a leading role in the search for an ambitious and comprehensive agreement at Copenhagen.

The draft Council conclusions reiterate that, in the context of a global and comprehensive agreement, the EU stands ready to contribute its fair share of international support and encourages parties to agree on a global contribution key. Developed countries should take the lead by setting

ambitious medium- and long-term targets for reducing their emissions, whilst developing countries, in particular the most advanced among them, should also undertake substantial own efforts to contain their emissions, with the support of developed countries. The private sector will be the main source of financing for mitigation, which must be driven by appropriate policies and regulation.

The principles to be used as the basis for calculation of the global distribution key remain, however, outstanding.

TAXATION

- Good governance in tax matters

The Council will be called on to adopt conclusions on the promotion of good governance in tax matters as a means of avoiding distortions of competition internationally and combating cross-border tax fraud and tax evasion.

The draft conclusions follow on from a communication published by the Commission, which reviews the issue of good governance in the context of both the economic and financial crisis and recent meetings of the G-20 (*doc. 9281/09*).

The Commission's communication examines, with regard to direct taxation:

- how good governance in tax matters could be improved within the EU;
- the instruments that the Community and member states have at their disposal to promote good governance internationally; and
- the scope for more coordinated action by the member states, so as to support, streamline and complement action taken in international fora such as the OECD and the UN.

The draft conclusions call for work to be accelerated on legislative proposals dealing with the taxation of savings (review of directive 2003/48/EC), administrative cooperation between member states and mutual assistance in the recovery of taxes.

Other issues covered by the draft conclusions include:

- the negotiation of an anti-fraud agreement with Liechtenstein;
- application of the OECD standard on the exchange of information on tax matters between states (article 26 of OECD model convention);
- savings tax measures agreed with Switzerland, Liechtenstein, Andorra, Monaco and San Marino and with the member states' dependant and associated territories.
