Council of the European Union

PRESS
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BACKGROUND[1]
Brussels, 23 May 2018

ECONOMIC AND FINANCIAL AFFAIRS COUNCIL
Friday 25 May in Brussels

The presidency will meet at 8.00 with finance ministers from the **Western Balkans and Turkey** to discuss strengthening fiscal frameworks to contribute to economic convergence.

Ministers will hold a breakfast meeting, scheduled for 9.30, to discuss the **economic situation** (in the light of the Commission's spring economic forecast). The Council is due to start at 10.30.

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Ministers will be called on to agree measures aimed at reducing risk in the **banking** industry, strengthening rules on capital requirements and on bank recovery and resolution.

They will assess 'in-depth reviews' of **macroeconomic imbalances**, and discuss projections for **age-related expenditure** in the member states.

The Council is expected to approve measures to boost **administrative cooperation** in the area of VAT. It may be called on to agree on two other VAT proposals: reduced rates for **e-publications** and an optional reversal of liability to **prevent fraud**.

Ministers are expected to make adjustments to the EU's list of **non-cooperative jurisdictions** in taxation matters, and to approve a standard provision on taxation to be included in **agreements with third countries**.

The Council is also expected to adopt a directive on transparency as regards **tax intermediaries**.

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The **Eurogroup** will hold two meetings on Thursday 24 May. At the first, starting at 15.00, it will discuss the fourth review of Greece's macroeconomic adjustment programme, as well as the economic situation (in the light of the Commission's spring forecast). It will also hold a thematic discussion on national spending reviews.

The second Eurogroup meeting is scheduled for 17.30, in an extended format (27 member states), to prepare for the Euro Summit on 28-29 June 2018. Discussions will be devoted to completion of Europe's banking union and reform of the European Stability Mechanism.

Press conferences:

- after the Eurogroup *(Thursday evening)*;
- at the end of the Council *(Friday lunchtime).*

Eurogroup agenda highlights

Press conferences and public events by video streaming

Video coverage in broadcast quality (MPEG4) and photo gallery

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

Banking – Risk reduction measures

The Council will be called on to agree on a package of measures aimed at reducing risk in the banking industry.

If agreement is reached, ministers will ask the presidency to start negotiations with the European Parliament as soon as the Parliament is ready to negotiate.

Preliminary agreement has been reached on a broad range of issues, subject to an overall agreement. The presidency has prepared compromise proposals on all elements that remain unresolved.

Banking package

The proposals set out to implement reforms agreed at international level following the 2007-08 financial crisis. Presented in November 2016, they include elements agreed by the Basel Committee on Banking Supervision and by the Financial Stability Board (FSB).

Strengthening existing EU rules, the aim is to ensure that any outstanding challenges to financial stability are correctly addressed.

The package comprises two regulations and two directives, relating to:

- bank capital requirements (amendments to regulation 575/2013 and directive 2013/36/EU);
- the recovery and resolution of failing banks (amendments to directive 2014/59/EU and regulation 806/2014).

The proposals on bank capital requirements include a binding leverage ratio to prevent banks from excessively increasing leverage, as well as a binding net stable funding ratio.

They strengthen risk-sensitive capital requirements for banks that trade largely in securities and derivatives. And they require global-systemically important institutions ('G-SIIs') to have more loss-absorbing and recapitalisation capacity in case of resolution.

The proposals on bank recovery and resolution implement the FSB's November 2015 standard on 'total loss-absorbing capacity' (TLAC). The TLAC is aimed at bolstering capital and leverage ratios of 30 banks identified as G-SIIs and deemed at risk of being ‘too big to fail’. The aim is to enable them to continue critical functions without endangering financial stability or requiring taxpayer support.

The proposals integrate the TLAC requirement into the EU's 'minimum requirement for own funds and eligible liabilities' (MREL), in order to avoid duplication. Whereas the TLAC standard is limited to G-SIIs, the MREL covers the entire EU banking industry; the proposals address this and other differences between the two.

The Council needs a qualified majority, in agreement with the European Parliament, to adopt the package. (Legal basis: articles 53(1) and 114 of the Treaty on the Functioning of the European Union.)

Outstanding issues

The main outstanding issue relates to the subordination of liabilities that can absorb losses and be used for recapitalisation in the event of a bank having to be resolved.

For non-GSII banks that could pose a systemic risk to financial stability, a new category of 'top tier bank' would be subject to similar minimum subordination requirements as for G-SIIs. A threshold of a €100 billion balance sheet at a resolution group level has been agreed to define that category. National resolution authorities would be able to impose the minimum requirements on banks below this threshold if they might pose a systemic risk.

Views differ however on the amount of subordinated liabilities for G-SIIs and top tier banks in the event of resolution, and on the flexibility that resolution authorities might have to set that amount. Some member states call for a high level of MREL 'pillar 2' subordination (an additional discretionary requirement). Others consider that in some cases this might be economically not viable and impossible for some banks to meet.

The presidency has tabled a compromise relating to both the level of MREL subordination and the discretion provided for resolution authorities to adjust this level.

It has also proposed compromise texts on:

- how to implement the Basel committee's 'fundamental review of the trading book';
- calculation of the G-SII 'score' (the higher the score allocated to a GSII, the higher the capital charges);
- an exemption for 14 promotional banks.

Risk sharing and the banking union

Progress on reducing risk is also necessary if further progress is to be achieved in the sharing of risk within the EU's banking union. The Euro Summit is due to review the situation on 28-29 June 2018 and could decide on specific steps to be taken.

The Council agreed in June 2016 that:

- in line with risk reduction measures, it may be decided to set up a common backstop to the EU's single resolution fund for failing banks ahead of the 2024 agreed start date;
- negotiations on a proposed European deposit insurance scheme for banks would start as soon as sufficient progress has been made on risk reduction.

Member states' experts have been working meanwhile on a possible list of criteria or indicators to measure progress in reducing risk in the banking sector.

The banking union is aimed at placing Europe's banking industry on a sounder footing, whilst ensuring that unviable banks are resolved without using taxpayers' money. Launched in 2012 to address the bank-sovereign nexus in Europe, it involves a transfer of responsibility to the EU level. It currently comprises the 19 countries of the euro area, whilst 7 other member states have also indicated their intention to join.

- Note on May 2018 draft legislative package aimed at reducing risk in the banking industry
- May 2018 draft amendments of regulation 575/2013 on bank capital requirements
- May 2018 draft amendments of directive 2013/36/EU on bank capital requirements
- May 2018 draft amendments of directive 2014/59/EU on bank recovery and resolution
- May 2018 draft amendments of regulation 806/2014 on the single resolution mechanism
- Basel Committee on Banking Supervision
- Financial Stability Board

VAT fraud – Administrative cooperation

The Council will be called on to agree measures aimed at strengthening administrative cooperation in order to better prevent VAT fraud.

Amending regulation 904/2010, the proposal sets out to:

- improve the exchange and analysis of information shared by the member states' tax administrations and with law enforcement bodies;
- strengthen Eurofisc, a network of national tax officials for the exchange of information on VAT fraud, jointly processing and analysing all relevant data;

It also introduces new instruments for administrative cooperation such as joint audits.

An estimated €150-160 billion of tax revenue is lost annually due to shortcomings in the VAT system, including fraud. About €152 billion was lost in 2015.

For cross-border fraud alone, some estimates have put annual losses at €50 billion.

The proposed regulation is aimed at containing fraud in the short term, pending implementation of a definitive VAT system. Proposals aimed at replacing the current 'transitional' VAT arrangements by a definitive system are currently under discussion.

The draft regulation sets out to remedy deficiencies identified in a March 2016 special report of the Court of Auditors.

Specific measures are proposed to address the most widespread forms of cross-border fraud:

- 'missing trader' or 'carousel' fraud, where supplies are purchased and resold without payment of VAT;
- fraud in the trade of used automobiles;
- the fraudulent abuse of a scheme for VAT-free imports of goods.

The Court found VAT fraud prevention to be hampered by a lack of comparable data and indicators. It called for anti-fraud instruments to be strengthened and more consistently applied.

The Council responded to the Court's report in May 2016. It agreed to work to improve the exchange of information between tax administrations.

At an informal meeting in Sofia on 28 April 2018, ministers discussed the capacity of tax administrations to improve implementation of legislation.

The Council needs unanimity to adopt the regulation, after consulting the European Parliament. (Legal basis: article 113 of the Treaty on the Functioning of the European Union.) The Parliament hasn't yet delivered its opinion.

- May 2018 draft regulation on strengthening VAT administrative cooperation (8769/18)
- ECA special report: "Tackling intra-Community VAT fraud: More action needed"
- May 2016 Council conclusions on the VAT action plan and VAT fraud
- April 2018 Sofia informal finance ministers meeting

VAT rates for electronic publications

The Council may be called on to agree a proposal that would allow member states to apply non-standard VAT rates to electronic publications.

The proposed directive is aimed at aligning VAT rules for electronic and physical publications, thereby contributing to the EU's 'digital single market' plan.

Ministers were unable to reach agreement when they discussed the proposal in June 2017.

The text has broad support within the Council. However the Czech Republic has so far been opposed, pending a positive outcome on a proposed generalised 'reverse charge' VAT mechanism (see separate item below).

Under the current VAT rules (directive 2006/112/EC), electronically supplied services are taxed at the standard VAT rate, i.e. minimum 15%, whereas publications on a physical support may benefit from non-standard rates.

For physical publications – books, newspapers and periodicals – member states currently have the option of applying a 'reduced' VAT rate, i.e. minimum 5%. Some have been authorised to apply 'super-reduced' VAT rates (below 5%) or 'zero' rates (which involve VAT deductibility).

The directive would open the possibility member states that so wish to apply reduced VAT rates to electronic publications. Super-reduced and zero rates would only be allowed for member states that currently apply them to 'physical' publications.

The new rules would apply temporarily, pending the introduction of a new, 'definitive' VAT system. The Commission has issued proposals for the new system, which would allow member states more flexibility than at present in setting VAT rates.

The Council needs unanimity to adopt the directive, after consulting the European Parliament. (Legal basis: article 113 of the Treaty on the Functioning of the European Union.) The Parliament delivered its opinion on 1 June 2017.

- May 2018 note on the draft directive on VAT rates applicable to electronic publications (8771/18)
- April 2017 draft directive on VAT rates applicable to electronic publications

VAT fraud – 'Reverse charge' mechanism

The Council may be called on to agree on a proposal allowing member states to temporarily apply a generalised reversal of VAT liability.

The aim of this so-called ‘reverse charge’ mechanism is to better prevent VAT fraud.

It involves shifting liability for VAT payments from the supplier to the customer, thereby derogating from the general principles of the EU's VAT system.

The directive was proposed in December 2016 at the request of member states particularly affected by VAT fraud, though ministers were unable to reach agreement when they discussed it in June 2017.

Most member states are willing to accept a compromise text that was tabled in June 2017. However France has so far been opposed, citing concerns about possible disruptions to the VAT system.

The generalised reverse charge mechanism would apply to all domestic supplies of goods and services above an invoice threshold of €10 000. A member state that wishes to use it would be able do so under certain conditions, once the Council has given its consent. This would apply until a new VAT system is in place or until 30 June 2022, whichever is sooner.

Weaknesses in the VAT system leave member states vulnerable to fraud, sometimes with serious consequences for government treasuries. This is particularly the case with cross-border transactions.

An estimated €150-160 billion of tax revenue is lost annually due to shortcomings in the VAT system, including fraud. About €152 billion was lost in 2015.

A common fraud scheme is 'missing trader' or 'carousel' fraud, where supplies are purchased and resold without payment of VAT.

The reverse charge mechanism can already be applied on a temporary basis, but not in a generalised manner. Under the current rules, it is limited to a pre-determined list of sectors. It may only be used by a member state that has made a specific request and if authorised to do so by the Council.

The directive would offer a short-term solution for containing fraud, pending implementation of a new VAT system where supplies would be taxed in the country of destination. Proposals aimed at replacing the current ‘transitional’ VAT arrangements by a definitive system are currently under discussion.

The Council needs unanimity to adopt the directive, after consulting the European Parliament. (Legal basis: article 113 of the Treaty on the Functioning of the European Union.) The Parliament hasn’t yet delivered its opinion.

- May 2018 note on the draft directive on a generalised VAT reverse charge mechanism (8770/18 REV 1)
- June 2017 draft directive on a generalised VAT reverse charge mechanism

Economic governance – 2018 European Semester

Ministers will assess macroeconomic imbalances and implementation of economic and fiscal policy recommendations.

They are due to adopt conclusions:

- responding to the Commission's 'in-depth reviews' of macroeconomic imbalances in 12 member states;
- reviewing implementation of the Council's country-specific recommendations on the economic and fiscal policies conducted by 27 member states[2].

The in-depth reviews and assessment of implementation are part of the 'European Semester' annual policy monitoring process. The in-depth reviews are also part of the EU's annual 'macroeconomic imbalances procedure'.

The 2018 European Semester will conclude in July.

Macroeconomic imbalances

The in-depth reviews determine whether a macroeconomic imbalance exists and whether it can be considered excessive.

In November 2017, the Commission found that further analysis was needed for 12 member states. Its findings, published on 7 March 2018, are as follows:

- Croatia, Cyprus and Italy are experiencing excessive economic imbalances;
- Bulgaria, France, Germany, Ireland, the Netherlands, Portugal, Spain and Sweden are experiencing economic imbalances that are not considered excessive. (For Bulgaria, France and Portugal, the imbalances had been judged excessive in 2017);
- all 11 of these member states should continue to be subject to specific monitoring;
- Slovenia is no longer experiencing economic imbalances.

Ministers are expected to agree with the Commission's findings.

They will call for strong commitment to structural reforms in all member states, and particularly where macroeconomic imbalances affect the smooth functioning of the euro area. Noting that the current upswing in the economy could mask the build-up of imbalances, ministers will call for these to be addressed in a durable manner.

Implementation of the country-specific recommendations

The 2017 country-specific recommendations were issued last July. They called for policy actions in line with the following three priorities:

- boosting investment;
- pursuing structural reforms;
- pursuing responsible fiscal policies.

The Commission's annual review, also published on 7 March 2018, includes a multiannual assessment of implementation since the European Semester process started in 2011.

This reveals some progress with regard to more than two thirds of the recommendations. However, progress has been uneven across policy areas, across member states and over time.

Ministers will highlight the need for implementation to be stepped up significantly, and to guard against reform fatigue.

The draft conclusions identify the main pending reform challenges.

- May 2018 draft conclusions on in-depth reviews and implementation of the 2017 CSRs
- Press release on country reports and in-depth reviews under the 2018 European Semester

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[2] Greece is not subject to an in-depth review and didn't receive a recommendation in 2017, as it is subject to enhanced surveillance under a macroeconomic adjustment programme.

Public finances – Ageing report

Ministers will discuss challenges for the sustainability of public finances in the light of ageing populations in Europe.

They are due to adopt conclusions, endorsing a report on age-related expenditure projections.

Ageing populations pose a major challenge for public finances. This is exacerbated by the rise in government debt levels since the financial crisis. Ministers will call for growth-friendly fiscal consolidation and further implementation of structural reforms to enhance the sustainability of public finances.

The report analyses age-related public expenditure (pensions, health care, long-term care and education), as well as unemployment benefit expenditure. It sets out projections for the 2016-70 period for the 28 EU member states and Norway. It is based on commonly agreed methodologies and assumptions, and using demographic data from Eurostat, the EU's statistical office.

The report is published every three years, the 2018 projections updating those issued in 2015. It was prepared jointly by the Economic Policy Committee and by the Commission.

The main findings are as follows:

- The expected decline in the working age population will act as a drag on growth over the long term. Labour productivity will be the sole driver of growth. Whilst the EU’s average growth rate is projected to remain broadly stable over the period, there are considerable differences across member states.
- Total age-related public spending is projected to increase by 1.7 percentage points of GDP in the EU over the period, reaching 26.6% of GDP in 2070. Projections feature large differences between member states. Under a more adverse scenario the figure would increase by 2.2 p.p., reaching 27.1% of GDP in 2070.
- Public pension expenditure is projected to increase by 0.8 p.p. of GDP up to 2040, related in part to the post-war baby boom generation reaching retirement age. It is then projected to return to slightly below its starting point by 2070 (11% of GDP). Expenditures would be higher, however, under a more adverse scenario. Diversity across member states is significant, depending on the degree and timing of population ageing, GDP growth prospects, the specific features of national pension systems and, in particular, progress with structural reforms.
- Public expenditure on health care and long-term care is projected to increase by 2 p.p. of GDP, reaching 10.4% of GDP in 2070. This is mainly due to demographic developments. Taking into account possible future developments in non-demographic cost factors in health care and long-term care, the projected increase would be 4 p.p. over the period.

Whilst many member states have undertaken reforms, the draft conclusions call for further policy actions to resolve specific issues.

Ministers will call for the Council’s annual country-specific recommendations to be implemented, and for a three-pronged strategy to be applied:

- addressing the economic and budgetary consequences of ageing by reducing government debt;
- raising employment rates and productivity;
- reforming pension, health care and long-term care systems.

They will highlight the need to avoid measures that result in the reversal of sustainability-enhancing reforms already undertaken.

As concerns pensions, they will call for further steps to raise the effective retirement age.

- 2018 ageing report

Taxation – Non-cooperative jurisdictions

The Council is due to approve, without discussion, a number of amendments to its conclusions of December 2017 on the EU's list of non-cooperative tax jurisdictions.

These include the removal of the Bahamas and Saint Kitts and Nevis from the list, which is contained in annex I of the conclusions.

The two jurisdictions have made commitments at a high political level to remedy EU concerns.

In the light of an expert assessment of those commitments, they will be moved from annex I to annex II, which cites jurisdictions that have undertaken commitments to reform their tax policies.

Implementation of their commitments will be carefully monitored.

Other amendments to the conclusions will include the late addition of Turks and Caicos Islands to annex II of the conclusions.

A screening of its tax system was put on hold after hurricanes struck the Caribbean region in September 2017, and Turks and Caicos Islands has now committed to reform its tax policies.

Like for other jurisdictions on annex II, implementation of the commitments made will be carefully monitored.

The decisions will leave 7 jurisdictions on the list of non-cooperative jurisdictions: American Samoa, Guam, Namibia, Palau, Samoa, Trinidad and Tobago and the US Virgin Islands.

The EU list is intended to contribute to on-going efforts to prevent tax fraud and promote good governance worldwide. It was prepared in 2017 in parallel with work undertaken by the OECD.

First published in December 2017, the list is revised at least once a year. However, the working group responsible for the listing process ('code of conduct group') can recommend an update at any time.

Moves have recently been made to boost transparency in the listing process:

- a specific Council webpage is now online;
- letters seeking commitments from third country jurisdictions have been made public;
- commitment letters received from third country jurisdictions are made public as soon as consent for publication is secured.

- May 2018 note on changes to the EU list of non-cooperative jurisdictions
- Council webpage on the code of conduct group
- December 2017 Council conclusions on the EU list of non-cooperative jurisdictions

Corporate tax avoidance – Tax intermediaries

The Council is expected to adopt, without discussion, a directive aimed at preventing aggressive cross-border tax planning.

The directive is the latest in a series of measures intended to boost tax transparency and better address corporate tax avoidance.

It will require intermediaries such as tax advisors, accountants and lawyers that design and/or promote tax planning schemes to report schemes that are potentially aggressive.

The member states will be required to automatically exchange the information they receive through a centralised database. This will enable new risks of tax avoidance to be determined earlier and measures to be taken to block harmful arrangements.

Member states will be obliged to impose penalties on intermediaries that do not comply with the transparency measures.

The directive broadly reflects action 12 of the OECD's 2013 action plan to prevent tax base erosion and profit shifting. Work is on-going within the OECD on model mandatory disclosure rules to address tax avoidance arrangements.

The Council needs unanimity to adopt the directive, after consulting the European Parliament. (Legal basis: articles 113 and 115 of the Treaty on the Functioning of the European Union.)

The Parliament voted its opinion on 1 March 2018, and the Council reached a political agreement at its meeting on 13 March 2018.

- March 2018 press release on Council agreement on the draft directive on tax intermediaries
- May 2018 draft directive on tax intermediaries

Tax fraud – Agreements with third countries

Ministers are expected to approve, without discussion, an updated standard provision on good tax governance to be included in EU agreements with third countries.

The new provision will reflect developments in international standards in the area in taxation since the original provision was approved in 2008. These include OECD standards aimed at preventing corporate tax base erosion and profit shifting (BEPS).

The focus on good governance is aimed at preventing cross-border tax fraud and tax evasion, as well as money laundering, corruption and the financing of terrorism.

The new provision reads as follows:

"The Parties recognise and commit themselves to implement the principles of good governance in the tax area, including the global standards on transparency and exchange of information, fair taxation, and the minimum standards against Base Erosion and Profit Shifting (BEPS). The Parties will promote good governance in tax matters, improve international cooperation in the tax area and facilitate the collection of tax revenues."

- May 2018 draft conclusions on tax issues in agreements with third countries

Other items

Under 'other business', the presidency will update ministers regarding work on legislative proposals in the field of **financial services**.

- May 2018 progress report on financial services legislative proposals

Without discussion, the Council is expected to:

- remove the Bahamas and Saint Kitts and Nevis from the EU's list of **non-cooperative jurisdictions** in taxation matters (see separate item above);
- adopt a directive aimed at boosting transparency in order to tackle aggressive cross-border **tax planning** (see separate item above);
- approve an updated standard provision on good tax governance to be included in **agreements with third countries** (see separate item above);
- respond to a Court of Auditors special report on the Commission’s intervention in the financial crisis in **Greece**.

- May 2018 draft conclusions on ECA special report on Greece (8665/18)