Council of the European Union

PRESS

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BACKGROUND[1]
Brussels, 29 November 2018

ECONOMIC AND FINANCIAL AFFAIRS COUNCIL
Tuesday 4 December in Brussels

Ministers will meet at 9:00 for a breakfast meeting on the economic situation, the international role of the euro and the follow-up to the informal ECOFIN lunch of September 2018 on EIB-related issues. The Council is scheduled to start at 10:00.

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The Council will hold an exchange of views on the **digital services tax** with a view to reaching a general approach on the proposed directive.

Ministers will take note of progress on work aimed at reducing risk in the banking industry and on a proposed **European deposit insurance scheme**. In particular, they are expected to endorse the result of the informal trilogue negotiation with the European Parliament on **key risk reduction measures of the so-called "banking package"**. Ministers will also take stock of the implementation of the **action plan to tackle non-performing loans in Europe**.

The Council will take stock of the ongoing **European semester exercise for 2019**, on the basis of a presentation by the Commission of the package presented on 21 November 2018. The Council is expected to adopt new recommendations related to Hungary's and Romania' significant deviation procedures.

Without discussion, the Council is due to adopt Council conclusions setting out an **action plan on anti-money laundering**. On taxation matters, the Council is expected to endorse a **report to the European Council on tax issues**, as well as **a report by the Code of Conduct group on business taxation**, accompanied by Council conclusions, which also addresses cooperation with jurisdictions outside the EU.

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Proceedings will start on Monday 3 December at 13.00 with a meeting of the Eurogroup in regular format. The Eurogroup will then meet in in an "inclusive format" (27 member states) to discuss the reform of the Economic and Monetary Union in view of the 14 December 2018.

Press conferences:

- after the Eurogroup meeting *(Monday evening)*;
- at the end of the Council *(Tuesday lunchtime).*

Eurogroup agenda highlights
Press conferences and public events by video streaming
Video coverage in broadcast quality (MPEG4) and photo gallery

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

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Digital services tax

The Council is expected to take stock of the progress achieved in the negotiations on the digital services tax. Ministers will be invited to reach a general approach on the proposed directive.

Current tax rules were designed for the traditional economy and do not apply to activities that require no physical presence in the country where customers are. As a result, businesses active in the digital sector are perceived not to pay their fair share of taxes in all countries where they are active.

The digital services tax (DST) was proposed by the Commission on 21 March 2018, as part of a "digital taxation package". It is meant as an **interim solution** aimed at addressing the most urgent gaps in the taxation of digital activities, while ensuring a level playing field for all businesses.

Following the political guidance given by ministers at the November ECOFIN, the Council continued discussions at technical level. On this basis, the Presidency concluded that all technical issues had been examined. It put forward a compromise text containing the elements that have gathered the widest support from member states. However, at this stage a number of delegations cannot accept the text for political reasons as a matter of principle, while several others are not satisfied yet with the overall balance of the suggested text.

According to the compromise text, the DST would apply to companies with total annual worldwide revenues of €750 million and annual EU revenues of €50 million. The DST would be applied a rate of 3%.

Three types of services would qualify in the scope of the directive:

- the placing on a digital interface of target advertising;
- the provision of a multi-sided digital interface;
- the sale of data collected about users and generated from users' activities on digital interfaces.

The Presidency's compromise text, as it stands, also provides that the application of the directive would be linked to the progress achieved by the OECD on the revisions to international corporate tax standards to address the challenges arising from digitalisation.

Discussions are also ongoing at international level on how to respond to such challenges. The OECD has taken up work on this issue and has published an interim report in March 2018. Its "Task Force on digital economy" aims at producing a final report by 2020 to the G20.

The challenges of the digital economy were discussed at an EU summit on digital issues held in Tallinn in September 2017. In October, the European Council highlighted the "need for an effective and fair system of taxation for the digital era", while the Council adopted conclusions on "responding to the challenges of taxation of profits of the digital economy" in December.

As a follow up, the Commission put forward a package of measures to better address taxation of the digital economy. In addition to the DST, the Commission published a proposal for a directive and a Commission recommendation on corporate taxation of significant digital presence, as well as a communication on "a modern, fair and efficient taxation standard for the digital economy". In the framework of the May 2018 Presidency digital taxation roadmap, it was agreed to give priority to Council's discussions on the DST.

Banking union - Risk reduction measures and EDIS

The Council is expected to endorse the result of negotiations held with the European Parliament on a package of key risk reduction measures of the so-called "banking package". The endorsement would pave the way to making further progress in the sharing of risk within the EU's banking union.

The Council will also take note of progress achieved on a proposal for a European deposit insurance scheme (EDIS).

Banking package

Presented in November 2016, the proposed package builds on EU banking rules with the aim of reducing risk in the industry.

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).

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 Council achieved an agreement on a general approach in view of negotiations with the European Parliament in May 2018. Following intense trilogue negotiations, the European Parliament and the presidency reached a provisional agreement on key measures of a comprehensive legislative package aimed at reducing risks in the EU banking sector on 22 November 2018.

This agreement is now presented for political endorsement by ministers.

The aim of the risk reduction package is to deliver on three of the key objectives set out by the Council roadmap on **completing the banking union** agreed in June 2016:

- enhancing the **framework for bank resolution**, in particular the necessary level and quality of the subordination of liabilities (MREL) to ensure an effective and orderly "bail-in" process.
- introducing the possibility for resolution authorities to suspend a bank's payments and/or contractual obligations when it is under resolution - the so-called "**moratorium tool**" -, so as to help stabilise the bank's situation.
- strengthening **bank capital requirements** to reduce incentives for excessive risk taking, by including a binding leverage ratio, a binding net stable funding ratio and setting risk sensitive rules for trading in securities and derivatives.

In addition, the banking package contains measures **to improve banks' lending capacity and to facilitate a greater role for banks in the capital markets**, such as:

- reducing the administrative burden for smaller and less complex banks, linked in particular to reporting and disclosure requirements;
- enhancing the capacity of banks to lend to SMEs and to fund infrastructure projects;
- reducing the costs of issuing/holding certain instruments, such as high quality securitisation instruments or covered bonds;

Finally, the banking package contains a framework for the cooperation and information sharing among the various authorities involved in the **supervision and resolution of cross-border banking groups**. The agreed measure preserves the balance achieved by the Council position between the powers of home and host supervisors in order to facilitate cross-border flows of capital and liquidity, while ensuring an adequate level of protection for depositors, creditors and financial stability in all member states. The agreement also introduces amendments to improve cooperation between competent authorities on matters related to the **supervision of anti-money laundering activities**.

Risk sharing and banking union

This agreement paves the way to making further progress in the sharing of risk within the EU's banking union. The Euro-summit is due to review the progress achieved in reducing risk in the EU banking industry in December 2018, and to decide on specific steps to be taken in the framework of a broad reform of the Economic and Monetary Union.

In June 2016, the Council agreed in particular 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.

Council conclusions on a roadmap to complete the banking union, June 2016

European deposit insurance scheme

Presented in November 2015, the EDIS proposal is aimed at establishing an EU-level insurance scheme to strengthen the protection of bank deposits.

A progress report assesses the outcome of work within the Council working group. It is intended to facilitate further work during 2019.

Whereas deposit guarantee schemes provide protection at national level in the event of bank failure, they remain vulnerable to local shocks. In remedying this, EDIS is foreseen as a third 'pillar' of the EU's banking union, alongside the single supervisory mechanism for the banking sector and the single resolution mechanism for unviable banks.

According to the Commission's original proposal, EDIS would be established in three stages.

In June 2016, the Council agreed that negotiations at political level would start as soon as progress has been made on measures to reduce risk in the financial sector (see sub-item above).

To address diverging views, the Commission made some suggestions in a communication issued in October 2017.

It suggested a more gradual introduction of EDIS, with only two phases:

- during a more limited reinsurance phase than in its original proposal, EDIS would provide liquidity coverage to national deposit guarantee schemes (DGSs). It would temporarily provide the means for full pay-outs in the event of bank being in crisis. National DGSs would pay back this support, ensuring that any losses would continue to be covered at national level;
- during a coinsurance phase, EDIS would also progressively cover losses.

Since June 2018, the Council working group has met four times to discuss the proposal. Work was of a technical nature because political discussions were held off pending sufficient progress on reducing risk.

The Austrian Presidency focused the work on exploring thoroughly the technical issues linked to different alternatives for the initial model of EDIS. In particular, the Council working group explored the technical features of a "hybrid model" presented by the Presidency which combined a system of re-insurance based on ideas featured in the October 2017 Commission communication and a mandatory lending scheme.

Moreover, the working party discussed transitional aspects in the context of the introduction of EDIS, the impact of EDIS on non-Banking Union Member States, alternative measures and the calculation of risk-based contributions.

October 2017 Commission communication on completing the banking union

Council page on risk reduction and deposit protection

Non-performing loans

The Commission will report on work to implement the Council's July 2017 action plan on non-performing loans (NPLs) in the banking sector.

Non-performing loans are bank loans that are subject to late repayment or are unlikely to be repaid without requiring the sale of collateral. High NPL levels can drag heavily on investment, and hence on the economy. A legacy of the financial crisis, they remain at historically high levels within the EU.

The report shows overall NPL levels to have dropped from nearly €1 trillion at the end of 2016 to €82 billion according to the latest figures. The ratio of NPLs in proportion to total bank loans has decreased from 5.4% in June 2016 to 3.4%. However, NPL ratios remain uneven across the EU – ranging from 0.6 % to 44.9 % – and slow progress in some Member States remain a source of concern.

In its July 2017 conclusions, the Council highlighted the need for action in order to reduce levels of NPLs and to prevent their build-up in the future, in particular as regards:

- bank supervision;
- the reform of insolvency and debt recovery frameworks;
- the development of secondary markets for NPLs ('distressed assets');
- restructuring of the banking industry.

In response to the Council's call for action, the Commission proposed in March 2018 a package of measures to address the NPLs issues, including a prudential backstop which would make banks set aside funds to cover risks with associated NPLs, measures encouraging the development of secondary markets where banks could sell their NPLs to investors and an efficient mechanism of out-of-court value recovery from secured loans.

On 31 October 2018, EU ambassadors approved the Council's position on the NPL prudential backstop. Negotiations with the European Parliament will start as soon as the Parliament has agreed its stance.

The Commission's proposals on secondary markets and out-of-court enforcement mechanism are still under discussion in the Council working group, with the first issue more advanced than the second. The Austrian Presidency intends to make as much progress possible on secondary markets aspects, in view of reaching a partial general approach by the end of the year.

Press release on 2017 Council action plan on non-performing loans

Commission's third report on the reduction of non-performing loans

Economic governance - 2019 European Semester

The Council will initiate the annual 'European Semester' process for the monitoring of the member states' economic, employment and fiscal policies.

The Commission will present three documents:

- an annual growth survey, highlighting the main conclusions for 2019;
- an 'alert mechanism report', marking the starting point of the annual macroeconomic imbalances procedure;
- a draft Council recommendation on the economic policies of the euro area.

The Council will hold an exchange of views.

It is scheduled to approve the recommendation and conclusions on the two reports at a meeting on 22 January 2018. The 2019 European Semester will conclude in July with the adoption of country-specific recommendations.

Annual growth survey

The Commission's survey is the starting point of the 2019 European Semester. It outlines the most pressing priorities on which the EU and the member states should focus in the economic and social field.

For 2019, the Commission notes a less dynamic economic growth context in Europe. It calls on member states to continue efforts along the lines of the previous annual growth survey:

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

Alert mechanism report

The Commission's report identifies 13 member states that may have a macroeconomic imbalance. For these, it will present in-depth reviews in February 2018.

11 out of the 13 countries were subject to a macroeconomic imbalance procedure last year: Bulgaria, Croatia, Cyprus, France, Germany, Ireland, Italy, the Netherlands, Portugal, Spain and Sweden.

In addition, Romania and Greece, which exited its macroeconomic adjustment programme in August 2018, will also be subject to a review.

The macroeconomic imbalances procedure was introduced in 2011 as an annual process aimed at preventing and correcting such imbalances. Fines can be imposed on eurozone countries if they repeatedly fail to comply with the Council's recommendations.

Recommendation on the economic policies of the euro area

This annual recommendation is a key part of the European Semester. It enables a focus on eurozone priorities when preparing country-specific recommendations in the spring.

In its draft, the Commission recommends in particular:

- to deepen the single market and make reforms that will support productivity, growth and investment;

- to improve the quality and composition of public finances in all countries and rebuild fiscal buffers in countries with high levels of public debt;

- to shift taxes away from labour and strengthen education systems and investment in skills;

- to make progress on the different work-streams related to the reform of the Economic and Monetary Union.

Stability and Growth Pact - Hungary and Romania

The Council is due to take stock of the ongoing significant deviation procedures of Hungary and Romania. Ministers are expected to issue decisions confirming that effective actions have not been taken, as well as new recommendations on measures to take to correct the deviations.

Romania

Romania has been subject to a significant deviation procedure since June 2017.

It is responsible for a significant deviation from the agreed adjustment path towards its medium term budgetary objective.

For the third time, the Council will issue:

- a decision establishing that Romania has failed to take effective action;
- a recommendation on measures to take to correct the significant deviation.

In 2016, Romania’s structural balance deteriorated significantly. But contrary to the 0.5% of GDP structural improvement recommended by the Council in June 2017, the Commission's autumn 2017 economic forecast suggested a further deterioration.

In December 2017 and again in June 2018, the Council established that Romania had not taken effective action. It called for measures to ensure that the nominal growth of net primary government expenditure does not exceed 3.3% in 2018 and 5,1% in 2019, representing an annual structural adjustment of at least 0.8% of GDP.

However, the Commission's autumn 2018 forecast suggest that Romania's structural balance has stabilised in 2018 after reaching -3.4% of GDP in 2017. Its net primary government expenditure was well above the benchmark set by the Council. Both indicators confirm a significant budgetary deviation in 2018.

The failure to act upon earlier recommendations – and the risk of exceeding the EU's 3% of GDP reference value for government deficits – call for urgent action.

The Council is expected to recommend measures to ensure that the nominal growth of net primary government expenditure does not exceed 4,5% in 2019, representing an annual structural adjustment of 1% of GDP.

This will put Romania on an appropriate adjustment path towards its medium-term budgetary objective. Any windfall gains should be used for deficit reduction, and budgetary consolidation measures should secure a lasting improvement.

The Council is expected to set a deadline of 15 April 2019 for Romania to report on action taken.

Hungary

Hungary has been subject to a significant deviation procedure since June 2018.

For the second time, the Council will issue:

- a decision establishing that Hungary has failed to take effective action;
- a recommendation on measures to take to correct the significant deviation.

It is responsible for a significant deviation from the agreed adjustment path towards its medium term budgetary objective.

In June 2018, the Council issued a recommendation for Hungary to take the necessary measures to ensure that the nominal growth rate of net primary government expenditure does not exceed 2,8% in 2018, corresponding to an annual structural adjustment of 1% of GDP.

However, based on the Commission 2018 autumn forecast, Hungary's structural deficit increased by 1,7% of GDP to 3,4 % in 2017 and it is projected to deteriorate further by 0,4 % of GDP to 3,8% in 2018. As a result, the structural deficit is estimated to be 2,3 % of GDP away from the medium-term budgetary objective of 1,5 % in 2018. This confirms a significant budgetary deviation in 2018.

The Council is expected to recommend measures to ensure that the nominal growth of net primary government expenditure does not exceed 3,3% in 2019, representing an annual structural adjustment of 1% of GDP.

This will put Hungary on an appropriate adjustment path towards its medium-term objective. Any windfall gains should be used for deficit reduction, and budgetary consolidation measures should secure a lasting improvement.

The Council is expected to set a deadline of 15 April 2018 for Hungary to report on action taken.

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The decisions and recommendations require a qualified majority amongst 27 of the EU's 28 member states. The member state concerned does not vote.

Action plan on anti-money laundering

The Council is expected to adopt conclusions on an action plan to better tackle money laundering and terrorist financing.

The conclusions set out a number of short-term non-legislative actions to address 8 key objectives:

- identify the factors that contributed to the recent money laundering cases in EU banks, to better inform possible additional actions in the medium and long term;
- map relevant money laundering and terrorist financing risks and the best prudential supervisory practices to address them;
- enhance supervisory convergence and better take into account AML aspects in the prudential supervisory process;
- ensure effective cooperation between prudential and money laundering supervisors;
- clarify aspects related to the withdrawal of a bank's authorisation in case of serious breaches;
- improve supervision and exchange of information between relevant authorities;
- share best practices and find grounds for convergence among national authorities;
- improve the European supervisory authorities' capacity to make better use of existing powers and tools.

Recent money laundering cases in some EU banks have raised concerns that anti money laundering (AML) rules are not always supervised and enforced effectively across the EU, creating risks for the integrity and reputation of the European financial sector, as well as for the financial stability of those banks.

The recent cases of breach or alleged breach of AML rules have prompted calls for action at the highest political level. In its letter of 25 June 2018 to the President of the European Council, the Eurogroup President highlighted the "importance of enhancing the current monitoring of the implementation of anti-money laundering measures". On 12 September 2018, the Commission presented a proposal to further strengthen the supervision of EU financial institutions and to better address money-laundering and terrorist financing threats. The proposal was discussed by ECOFIN ministers in October 2018.

The European rules on anti money laundering and terrorist financing have been considerably strengthened in the past years, with two consecutive reforms being adopted since 2015. The latest revision of the AML directive, the fifth AMLD, was adopted in April 2018 and is due to be transposed at national level by January 2020.

Draft conclusions on AML action plan submitted for adoption

Council page on fight against money laundering and terrorist financing

VAT short-term fixes

The Council will be called on to adopt three short legislative acts aimed at adjusting some of the EU's VAT rules in order to fix four specific issues pending the introduction of a new VAT system.

These relate to:

- call-off stock. The text provides for a simplified and uniform treatment for call-off stock arrangements, where a vendor transfers stock to a warehouse at the disposal of a known acquirer in another member state;
- the VAT identification number. To benefit from a VAT exemption for the intra-EU supply of goods, the identification number of the customer will become an additional condition;
- chain transactions. To enhance legal certainty in determining the VAT treatment of chain transactions, the texts establish uniform criteria;
- proof of intra-EU supply. A common framework is established for the documentary evidence required to claim a VAT exemption for intra-EU supplies.

These adjustments are due to apply from 1 January 2020.

In parallel, discussions are ongoing on a definitive VAT system to replace the current 'transitional' VAT arrangements, applied since 1993. Pending introduction of the new system, four short-term 'quick fixes' are proposed.

November 2018 note submitted to the Council on adoption of the VAT quick-fix

Other items

Financial services legislation

Under 'other business', the Council will be updated regarding work on legislative proposals. The Commission will also report on the implementation of adopted legislation.

Follow-up to Achmea judgment

The Commission will inform ministers on the follow-up to the Achmea judgment of 6 March 2018, relating to the compatibility of arbitration clauses contained in intra-EU bilateral investment treaties with EU law.

Taxation

Without discussion, the Council is expected to approve:

- conclusions on an **action plan to tackle anti-money laundering** (see separate item above);
- short term fixes to the standard **VAT regime.**
- an update to the EU list of non-cooperative jurisdictions for tax purposes suggesting in particular the **removal of Andorra and San Marino from annex II** of the Council conclusions of 5 December 2017**:**
    - November 2018 report on amendments to Annex II of Council conclusions of 5 December 2017.
- conclusions and a six-monthly report on implementation of a code of conduct aimed at eliminating situations of **harmful tax competition,** including an update on the process of monitoring commitments taken by jurisdictions in the context of cooperation with third country jurisdictions;
    - November 2018 report of the code of conduct group on business taxation
    - November 2018 draft conclusions on the code of conduct on business taxation
- a six-monthly report to the European Council on **tax issues**;
    - November 2018 report to the European Council on tax issues