



Brussels, 8 March 2006

BACKGROUND¹

ECONOMIC and FINANCIAL AFFAIRS COUNCIL

Tuesday 14 March in Brussels

*The Council will be preceded as usual by a meeting of the **eurogroup**, on Monday 13 March starting at 19.00 hrs, which will examine the economic situation in the euro area and budgetary developments in the member states.*

The president of the eurogroup will hold a press conference after the meeting.

Also on Monday, there will be a dialogue with the social partners on macroeconomic policy at 14.30 hrs and a troika meeting with the European Parliament, by video-conference at 16.00, on the EU's broad economic policy guidelines.

A ministerial breakfast meeting on Tuesday at 9.00 will focus on the economic policy challenges of the Lisbon strategy for jobs and growth.

*Meeting at 10.00, the Council will deal with excessive deficit procedures with regard to **Germany** and **Italy**. It is expected to proceed to the next step in the procedure for Germany, giving it notice to take measures to bring its deficit below 3% of GDP by 2007 at the latest, and to take note of a communication from the Commission on Italy's deficit, which concludes that no further action is necessary at this stage.*

*The Council will prepare a number of dossiers to be referred to the spring **European Council**, regarding the Lisbon reform strategy, the European Investment Bank's contribution to growth and employment measures, the "better regulation" initiative and social inclusion and social protection in areas such as pensions and healthcare.*

*Amongst the other points on its agenda, the Council will give its opinion on a number of updated **stability and convergence programmes** presented by the member states.*

At lunch, ministers will discuss issues related to energy markets.

The president of the Council will hold a press conference at the end of the meeting.

*
* *
*

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

Preparation of the spring European Council

- **Lisbon strategy for growth and jobs**
- **Key issues paper**

The Council is due to approve a contribution to the European Council meeting on 23 and 24 March on implementation of the strategy for growth and jobs laid down at Lisbon in 2000, on the basis of a key issues paper prepared by the presidency and following discussion at the Council's meeting on 14 February. The key issues paper follows on from an annual progress report by the Commission.

In a mid-term review last March, the European Council agreed changes to the Lisbon strategy's governance provisions, with the aim of strengthening its contribution to growth and employment in the EU. Accordingly, the Commission's report is aimed at strengthening momentum and forcing the pace of delivery of public policy.

The report assesses national reform programmes (NRPs) drawn up by the member states in response to economic policy and employment guidelines laid down by the Council. It identifies the strengths of the NRPs, highlights areas where there are shortcomings and proposes action at EU and national level to deal with them.

The key issues paper identifies the following priorities:

- Using the opportunity of the evolving recovery to pursue fiscal consolidation, in line with the EU's stability and growth pact;
- Improving the sustainability and quality of public finances;
- Increasing employment in Europe as one of the top priorities for reform;
- Providing the right incentives for innovation;
- Creating a favourable business environment for small and medium-sized enterprises;
- Ensuring a coherent EU energy policy in a global context.

- **EIB contribution to promoting growth and jobs**

The Council is due to adopt a report, to be submitted to the European Council on 23 and 24 March, on proposals by the European Investment Bank on a strengthened contribution by the EIB and the European Investment Fund to promoting growth and employment in the EU.

The EIB proposes to reinforce its contribution in four areas:

- research and development, innovation and competitiveness;
- energy efficiency, security and diversification of energy supply;
- support to small and medium-sized enterprises;
- investment in large-scale infrastructure.

At its meeting on 14 February, the Council approved the priorities identified by the EIB. It highlighted the need to identify clearly the economic rationale for the bank's intervention, as concerns both the added value that it can provide in areas where the market cannot provide the required funding and the catalytic effect that it can have in leveraging private investment.

The Council agreed that all interventions must respect the existing framework for the EIB's capital, namely that its next capital increase should not occur before 2010 and that it should be self-financing.

- **Better regulation**

The Commission will report on how the measurement of administrative burdens on businesses is being integrated into its work programme on regulatory simplification.

The Council will take stock of progress more generally on the "better regulation" initiative, in the light of a document from the presidency referring to experiences at national level.

- **Social protection and social inclusion**

The Council will take note of the expected adoption, by the Employment, Social Policy, Health and Consumer Affairs Council on 10 March, of a joint Council and Commission report on social inclusion and social protection in pensions, healthcare and long-term care, which will be submitted to the European Council on 23 and 24 March.

Stability and convergence programmes

- **Germany, Greece, Spain, France, Italy, Ireland, the Netherlands and Portugal**
- **Cyprus, Lithuania, Malta, Poland and the United Kingdom**

The Council will adopt opinions on a third and final series of annual updates of the member states' stability and convergence programmes, namely:

- updated stability programmes presented by Germany, Greece, Spain, France, Italy, Ireland, the Netherlands and Portugal;
- updated convergence programmes presented by Cyprus, Lithuania, Malta, Poland and the United Kingdom.

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

The pact requires programmes that set out the medium-term objective of the member state's budgetary position, 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 Council adopted opinions on the other member states' updated programmes at its meetings on 24 January and 14 February.

Excessive deficit procedure

- **Germany**
- **Italy**

The Council is expected to proceed to the next step in the EU's excessive deficit procedure with regard to Germany. It is due to adopt a decision, under article 104(9) of the treaty, giving notice to Germany to take measures in order to bring its government deficit below 3% of gross domestic product (GDP), the reference value provided for by the EU treaty.

As regards Italy, the Council will take note of a communication from the Commission which concludes that no further action is currently necessary under the excessive deficit procedure.

Germany

The draft Council decision gives notice to Germany to correct its excessive deficit as rapidly as possible and by 2007 at the latest, requiring it to report to the Commission by 14 July on measures taken to this end, and to ensure an annual reduction in its structural deficit of at least 0.5% of GDP after the excessive deficit has been corrected.

Based on article 104, paragraph 9 of the treaty, the draft decision requires for adoption a two-thirds majority of weighted votes of members of the euro area except Germany.

Germany's government deficit has been above the 3% reference value since 2002. It amounted to 3.3% of GDP in 2005, according to Eurostat on the basis of provisional data provided by Germany on 24 February, down from the 3.9% projected by the Commission in its 2005 autumn forecast thanks to better-than-expected budget revenues towards the end of the year.

The new German government has started implementing a budget consolidation strategy. It adopted on 22 February a draft federal budget for 2006 and a draft law aimed at raising the standard VAT rate from 16% to 19% as from 1 January 2007. In the light of this, the Commission expects the German deficit to stay slightly above 3% of GDP in 2006 and to drop clearly below the reference value in 2007.

The German deficit was last examined by the Council in January 2005 when no additional action was considered necessary under the excessive deficit procedure. The Council at that time considered action taken by Germany broadly consistent with the objective of bringing its deficit below the 3% reference value in 2005.

The procedure with regard to Germany was opened in January 2003, when the Council adopted a decision under article 104(6) on the existence of an excessive deficit and a recommendation under article 104(7) on measures to correct it.

Italy

The Council will take note of a communication from the Commission assessing the action taken by Italy in response to a recommendation issued by the Council last July, under article 104(7) of the treaty, on measures to be taken in order to bring its government deficit below the 3% reference value by 2007 at the latest.

The Council is expected to share the Commission's view that Italy's measures would, provided that they are fully and effectively implemented, ensure adequate progress in 2006 towards correction of the excessive deficit in 2007, in accordance with the time limit set in the Council's recommendation.

It is expected to consider, however, that correction of the deficit will require both execution of the 2006 budget and substantial measures for 2007.

After two downward revisions of growth projections for 2005, the Italian government targeted a deficit of 4.3% of GDP last year. The budget law for 2006, approved by the Italian parliament on 22 December, aims for a 3.5% deficit this year. According to the December update of its stability programme, Italy aims to reduce its deficit below 3% by 2007 and to pursue further fiscal consolidation in subsequent years, whilst restoring the debt ratio to a declining path as from 2006 and taking measures to reduce statistical discrepancies.

The Commission considers that the 2006 budget law is consistent with the minimum 0.8% of GDP structural adjustment between 2005 and 2006 recommended by the Council, provided that a 1.5% GDP growth rate is recorded this year and that implemented correction measures are effective. As regards correction of the excessive deficit in 2007 and the reduction in the debt ratio, the Commission considers there to be significant uncertainties that will require it to closely monitor budgetary developments.

The excessive deficit procedure was opened with regard to Italy in July 2005, when the Council adopted a decision under article 104(6) on the existence of an excessive deficit and a recommendation under article 104(7) on measures to correct it.

EU budget - Discharge for 2004, priorities for 2007

The Council is expected to approve a recommendation on the discharge to be given to the Commission for implementation of the EU's general budget for 2004 and to adopt conclusions on the Council's budgetary priorities for 2007. And the Commission will present an action plan aimed at establishing an improved control framework for implementation of the EU budget.

The draft recommendation, which will be forwarded to the European Parliament, is based on article 276 of the treaty, requiring a qualified majority within the Council for adoption.

Most delegations can agree on the recommendation, although some oppose the text, considering that it puts insufficient emphasis on the need to remedy a situation where, for more than ten years running, the Court of Auditors has refused a positive statement of assurance on the reliability of the accounts and the legality and regularity of the underlying transactions.

The conclusions will be used by the presidency as the basis for an exchange of views with the Parliament and the Commission on preparation of the EU budget for 2007. The significance of this item is heightened by the fact that negotiations are still underway with Parliament and Commission on the renewal of an agreement on budgetary discipline and on the EU's budgetary framework for the 2007-13 period.

In addition, the Council will adopt, without discussion, conclusions on the follow-up to the discharge for the 2003 budget and recommendations on the discharge to be given for Community agencies for 2004.