



**COUNCIL OF
THE EUROPEAN UNION**

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NOTE

from: Presidency

to: Council

Subject: Draft regulation of the European Parliament and of the Council on the strengthening of economic and budgetary surveillance of Member States experiencing or threatened with serious difficulties with respect to their financial stability in the euro area

Delegations will find attached draft Regulation on Strengthening the economic and budgetary surveillance of Member States experiencing or threatened with serious difficulties with respect to their financial stability in the euro area reflecting the discussions and agreement reached at the AHWG meeting on 14 February 2012.

Encl.:

Proposal for a

REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

on the strengthening of economic and budgetary surveillance of Member States experiencing or threatened with serious difficulties with respect to their financial stability in the euro area

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 136, in combination with Article 121(6) thereof,

Having regard to the proposal from the European Commission,

Having regard to the opinion of the European Central Bank,

After transmission of the draft legislative act to the national Parliaments,

Acting in accordance with the ordinary legislative procedure,

Whereas:

- (1) The unprecedented global crisis that has hit the world over the last three years has seriously damaged economic growth and financial stability and provoked a strong deterioration in the government deficit and debt position of the Member States, leading a number of them to seek financial assistance.

- (2) The full consistency between the Union multilateral surveillance framework established by the Treaty and the possible policy conditions attached to this financial assistance should be enshrined in Union law. The economic and financial integration of the Member States whose currency is the euro calls for an enhanced surveillance to prevent a contagion from a Member State experiencing difficulties with respect to its financial stability to the rest of the euro area.
- (3) The intensity of the economic and fiscal surveillance should be commensurate to the severity of the financial difficulties encountered and should take due account of the nature of the financial assistance received, which may range from a mere precautionary support based on eligibility conditions up to a full macro-economic adjustment programme involving strict policy conditionality.
- (4) A Member State whose currency is the euro should be subject to enhanced surveillance when it is experiencing - or at risk of experiencing - severe financial disturbance, with a view to ensuring its swift return to a normal situation and to protecting the other euro area Member States against possible negative spill over effects. This enhanced surveillance should include a wider access to the information needed for a close monitoring of the economic, fiscal and financial situation and a regular reporting to the Economic and Financial Committee (EFC) or to any sub-committee the latter may designate for that purpose. The same modalities of surveillance should apply to Member States requesting precautionary assistance from the European Financial Stability Facility (EFSF), the European Stability Mechanism (ESM) the International Monetary Fund (IMF) or another international financial institution.
- (5) The surveillance of the economic and fiscal situation should be strongly reinforced for Member States under macro-economic adjustment programme. Because of the comprehensive nature of the latter, the other processes of economic and fiscal surveillance should be suspended for the duration of the macro-economic adjustment programme, with a view to avoiding a duplication of reporting obligations.

- (6) Rules should be provided in order to enhance the dialogue between the Union institutions, in particular the European Parliament, the Council and the Commission, and to ensure greater transparency and accountability.
- (7) [A decision regarding the non-compliance of a Member State with its adjustment programme would also entail a suspension of payments or commitments of Union funds as provided by Article 21(6) of Regulation (EU) No XXX laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund covered by the common strategic framework and laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund and repealing Regulation (EC) No 1083/2006.]
- (8) The Commission may recommend to reduce or cancel any existing non-interest-bearing deposit or fines decided by the Council in the framework of the preventive or corrective part of the Stability and Growth Pact for a Member State subject to a macro-economic adjustment programme on grounds of exceptional economic circumstances.
- (9) When assessing whether a Member State is threatened with serious difficulties with respect to its financial stability, the Commission should conduct a comprehensive assessment, taking notably into account the borrowing conditions of that Member State, the repayment profile of its debt obligations, the robustness of its budgetary framework, the long term sustainability of its public finances, the importance of the debt burden and the risk of contagion from severe tensions in its financial sector on its fiscal situation or on the financial sector of other Member States.

- (10) References to financial assistance in this Regulation cover also financial supports granted on a precautionary basis, unless otherwise expressly stipulated.
- (11) The decision of the Commission to make a Member State subject to enhanced surveillance under Article 2(1) should be taken in close cooperation with the Economic and Financial Committee (EFC), the European Systemic Risk Board (ESRB) and the relevant European Supervisory Authorities (ESAs). The Commission should also cooperate with the EFC when deciding on whether to prolong the enhanced surveillance.

HAVE ADOPTED THIS REGULATION:

Article 1

Subject matter and scope

1. This Regulation sets out provisions for strengthening the economic and budgetary surveillance of Member States experiencing or threatened with serious difficulties with respect to their financial stability with potential negative spill-over effects on other Member States whose currency is the euro or detrimental impact on the sustainability of public finances and/or of Member States that have requested or receive financial assistance from one or several other States, the European Financial Stability Facility (EFSF), the European Financial Stability Mechanism (EFSM), the European Stability Mechanism (ESM) or other International Financial Institutions (IFI), such as the International Monetary Fund (IMF).
2. This Regulation shall apply to Member States whose currency is the euro.

Article 2

Member States under enhanced surveillance

1. The Commission may decide to make a Member State experiencing severe difficulties with regard to its financial stability likely to have adverse spill-over effects on other Member States of the euro area, subject to enhanced surveillance. The Commission shall decide every six months whether to prolong the enhanced surveillance.
2. The Commission shall decide to make a Member State receiving financial assistance on a precautionary basis from one or several other States, the EFSF, the ESM or any other International Financial Institution, such as the IMF, subject to enhanced surveillance. The Commission shall establish a list of the precautionary financial assistance instruments concerned and keep it updated to take into account possible changes in the financial support policy of the EFSF, ESM or of any other relevant International Financial Institution.
3. Paragraph 2 shall not apply to a Member State receiving a financial assistance on a precautionary basis in the form of a credit line which is not conditioned to the adoption of new policy measures by the concerned Member State, as long as the credit line is not drawn.

Article 3

Enhanced surveillance

1. A Member State under enhanced surveillance shall, in consultation and cooperation with the Commission, acting in liaison with the European Central Bank (ECB), the ESA(s) and the ESRB and where appropriate the IMF, adopt measures aimed at addressing the sources or potential sources of difficulties.
2. The closer monitoring of the fiscal situation laid down in Article 7, paragraphs 2, 3 and 6, of Regulation (EU) No XXX of the European Parliament and of the Council shall apply to a Member State under enhanced surveillance, irrespective of the existence of an excessive deficit. The report in accordance with paragraph 3 of this Article shall be submitted on a quarterly basis.

3. On a request from the Commission, the Member State under enhanced surveillance following a decision under Article 2(1) shall:
- (a) communicate to the relevant ESA(s) and at the requested frequency, disaggregated information on developments in its financial system. On the basis of this information, the relevant ESA(s) shall prepare, in liaison with the ESRB, an assessment of the potential vulnerabilities of the financial system and forward this assessment to the Commission at the frequency indicated by the latter. The ECB shall also receive the assessment. This reporting shall be done in accordance with article 35 of Regulations n°1093/2010, 1094/2010 and 1095/2010 of the European Parliament and of the Council of 24 November 2010;
 - (b) carry out, under the supervision of the relevant ESA(s), stress test exercises or sensitivity analyses as necessary to assess the resilience of the financial sector to various macroeconomic and financial shocks, as specified by the Commission and the ECB in liaison with the relevant European Supervisory Authorities and the ESRB; the reporting mentioned in point (a) shall include an analysis of the results of the stress test exercises and sensitivity analyses mentioned herein;
 - (c) be subject to regular assessments of its supervisory capacities over the banking sector in the framework of a specific peer review carried out by the relevant ESA(s);
 - (d) communicate any information needed for the monitoring of macro-imbalances established by Regulation No 1176/2011 of the European Parliament and of the Council on the prevention and correction of macroeconomic imbalances.

3 (bis) On a request from the Commission, the Member State under enhanced surveillance following a decision under Article 2(2) shall:

- (a) communicate to the Commission, the ECB, and the relevant ESA(s) at the requested frequency disaggregated information on developments in its financial system. The Commission, the ECB, the relevant ESA(s) shall preserve the confidentiality of the disaggregated data received;
- (b) carry out, under the supervision of the relevant ESA(s), stress test exercises or sensitivity analyses as necessary to assess the resilience of the financial sector to various macroeconomic and financial shocks, as specified by the Commission and the ECB in liaison with the relevant European Supervisory Authorities and the ESRB, and share the detailed results with them;
- (c) be subject to regular assessments of its supervisory capacities over the financial sector in the framework of specific peer review carried out by the relevant ESA(s);
- (d) communicate any information needed for the monitoring of macro-imbalances established by Regulation No 1176/2011 of the European Parliament and of the Council on the prevention and correction of macroeconomic imbalances.

4. The Commission shall conduct, in liaison with the ECB and the ESA(s) as needed and when appropriate the IMF, regular review missions in the Member State under surveillance to verify the progresses made in the implementation of the measures mentioned in paragraph 1, 2 and 3. It shall communicate every quarter its findings to the EFC and assess notably whether further measures are needed. These review missions shall replace the onsite monitoring foreseen in Article 10a(2) of Regulation (EC) No 1467/97.

5. Where it is concluded - on the basis of the assessment foreseen in paragraph 4 - that further measures are needed and the financial situation of the Member State concerned has significant adverse effects on the financial stability of the euro area, the Council, acting by a qualified majority on a proposal from the Commission, may recommend to the Member State concerned to take precautionary measures or to prepare a draft macro-economic adjustment programme. The recommendation and the preparatory work done in the run-up to its adoption shall be considered as confidential. The Council may decide to make the recommendation public.
6. Where a recommendation under paragraph 5 is made public:
- (a) the relevant Committee of the European Parliament may offer the opportunity to the Member State concerned to participate to an exchange of views;
 - (b) representatives of the Commission may be invited by the parliament of the Member State concerned to participate to an exchange of views.

Article 4

Information on envisaged financial assistance requests

A Member State intending to request financial assistance from one or several other States, the EFSF, the ESM, the International Monetary Fund (IMF) or another institution outside of the Union framework shall immediately inform the President of the EWG, the Commission and the ECB of its intention. The EWG, shall hold a discussion on this envisaged request, after having received an assessment from the Commission with a view to examine - among other things – the possibilities available under existing Union or euro area financial instruments before the Member State concerned addresses potential lenders.

A Member State intending to request financial assistance from the EFSM shall immediately inform the President of the EFC, the Commission and the ECB of its intention.

Article 5

Evaluation of the sustainability of the government debt

Where financial assistance is sought from the EFSF, the EFSM or the ESM, the Commission shall assess – in liaison with the ECB and wherever possible, the IMF - the sustainability of the government debt and the actual or potential financing needs of the Member State concerned. This assessment shall be forwarded to the EWG if the financial assistance is to be granted under the EFSF or the ESM and to the EFC if the financial assistance is to be granted under the EFSM.

Article 6

Macro-economic adjustment programme

1. A Member State requesting financial assistance from one or several other States, the IMF, the EFSF or the ESM shall prepare in agreement with the Commission - acting in liaison with the ECB and wherever possible the IMF - a draft macro-economic adjustment programme aimed at re-establishing a sound and sustainable economic and financial situation and restoring its capacity to finance itself fully on the financial markets. The draft macro-economic adjustment programme shall take due account of the current recommendations addressed to the Member State concerned under Articles 121, 126, 136 and/or 148 of the Treaty- and its actions to comply with them - while aiming at broadening, strengthening and deepening the required policy measures.
2. The Council, acting by qualified majority on a proposal from the Commission, shall approve the macro-economic adjustment programme.
3. The Commission, in liaison with the ECB and wherever relevant the IMF, shall monitor the progress made in the implementation of the macro-economic adjustment programme. It shall inform every three months the EFC. The Member State concerned shall give the Commission and the ECB its full cooperation. It shall in particular provide to the Commission and the ECB all the information that they deem necessary for the monitoring of the programme. Article 3(3 bis) shall apply.

4. The Commission - in liaison with the ECB and wherever possible the IMF - shall examine with the Member State concerned the changes that may be needed to its macro-economic adjustment programme. The Council, acting by a qualified majority on a proposal from the Commission, shall decide on any change to be made to the programme.
5. If the monitoring referred to in paragraph 3 highlights significant deviations from the macro-economic adjustment programme, the Council, acting by qualified majority on a proposal from the Commission, may decide that the Member State concerned does not comply with the policy requirements contained in the programme.
6. A Member State subject to a macro-economic an adjustment programme experiencing insufficient administrative capacity or significant problems in the implementation of its programme shall seek technical assistance from the Commission which may constitute to this effect groups of experts with Member States and other European and/or relevant international institutions. Technical assistance could include the establishment of a resident representative and supportive staff to advise authorities on the adjustment programme implementation.
7. The relevant Committee of the European Parliament may offer the opportunity to the Member State concerned to participate to an exchange of views on the progress made in the implementation of the adjustment programme.
8. Representatives of the Commission may be invited by the Parliament of the Member State concerned to participate to an exchange of views on the progress made in the implementation of the macro-economic adjustment programme.
9. The provisions of this Article do not apply to financial assistance granted on a precautionary basis and to loans made for recapitalising financial institutions.

Article 7

Consistency with the excessive deficit procedure

1. The macro-economic adjustment programme and the changes thereto provided for by Article 6 of this Regulation shall be deemed to replace the submission of stability programmes provided for by Article 4 of Council Regulation (EC) No 1466/97.

2. If a Member State subject to a macro-economic adjustment programme is the subject of a recommendation under Article 126(7) of the Treaty or a notice under Article 126(9) of the Treaty for the correction of an excessive deficit:
 - (a) The macro-economic adjustment programme provided for by Article 6 of this Regulation shall also be deemed to replace as appropriate the reports provided for by Article 3(4a) and Article 5(1a) of Council Regulation (EC) No 1467/97;

 - (b) The annual budgetary targets in the macro-economic adjustment programme provided for by Article 6(3) of this Regulation shall be deemed to replace as appropriate the annual budgetary targets foreseen in accordance with Article 3(4) and Article 5(1) of Regulation (EC) No 1467/97 in the mentioned recommendation and notice. If the Member State concerned is subject to notice under Article 126(9) of the Treaty, the macro-economic adjustment programme foreseen by Article 6(3) of this Regulation shall also be deemed to replace the indications on measures conducive to those targets foreseen in the notice in accordance with Article 5(1) of Regulation (EC) No 1467/97.

 - (c) The monitoring provided for by Article 6(3) of this Regulation shall be deemed to replace the monitoring provided for by Article 10(1) and Article 10a of Council Regulation (EC) No 1467/97 and the monitoring underlying any decision provided for by Article 4(2) and 6(2) of Regulation (EC) No 1467/97.

Article 8

Consistency with the excessive imbalances procedure

The implementation of Regulation (EU) No 1176/2011 on the prevention and correction of macroeconomic imbalances shall be suspended for the Member States subject to a macro-economic adjustment programme approved by the Council in accordance with Article 6(2) of this Regulation. This suspension shall be applicable for the duration of the macro-economic adjustment programme.

Article 9

Consistency with the European Semester for economic policy coordination

The monitoring provided for by Article 6(3) of this Regulation shall be deemed to replace the monitoring and assessment of the European Semester for economic policy coordination provided for by Article 2a of Regulation (EC) No 1466/97 on the strengthening of the surveillance of budgetary positions and coordination of economic policies. This suspension shall be applicable for the duration of the macro-economic adjustment programme.

Article 10

Consistency with Regulation (EU) No XXX on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area

The implementation of Regulation (EU) No XXX on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area shall be suspended for the Member States subject to a macro-economic adjustment programme approved by the Council in accordance with Article 6(2) of this Regulation, with the exception of Articles 1 to 4 of this Regulation. This suspension shall be applicable for the duration of the macro-economic adjustment programme.

Article 11

Post-programme surveillance

1. A Member State shall be under post-programme surveillance as long as a minimum of 75% of the financial assistance received from one or several other State(s), the EFSM, the EFSF or the ESM has not been repaid. The Council, acting on a qualified majority on a proposal from the Commission, may extend the duration of the post programme surveillance.
2. Article 3(3) shall apply. On a request from the Commission, the Member State shall also provide the information mentioned in Article 7(3) of Regulation (EU) No XXX on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area.
3. The Commission shall conduct, in liaison with the ECB, regular review missions in the Member State under post programme surveillance to assess its economic, fiscal and financial situation. It shall communicate every semester its findings to the EFC and assess notably whether corrective measures are needed.
4. The Council, acting by qualified majority on a proposal from the Commission, may recommend to the Member State under post programme surveillance to adopt corrective measures.

Article 12

Voting within the Council

For the measures referred to in Articles 3(5), 6(2), 6(4), 6(5) and 11(4), only members of the Council representing Member States whose currency is the euro shall vote and the Council shall act without taking into account the vote of the member of the Council representing the Member State concerned.

A qualified majority of the members of the Council referred to in the first paragraph shall be calculated in accordance with Article 238(3)(a) of the Treaty.

Article 13

Transitional provision

Article 11 shall not apply to Member States already under post-programme surveillance at the date of entering into force of this regulation. Instead, post-programme surveillance rules, conditions and procedures adopted in relevant documents related to the granting of financial assistance shall be applied.

Article 14

Entry into force

This Regulation shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

This Regulation shall be binding in its entirety and directly applicable in the Member States in accordance with the Treaties.

Done at Brussels,

For the European Parliament

The President

For the Council

The President