

OPINION OF THE EUROPEAN MONETARY INSTITUTE

on a consultation from the Irish Department of Finance under Article 109f (6) of the Treaty establishing the European Community (the “Treaty”) and Article 5.3 of the Statute of the EMI as elaborated in the Council Decision of 22nd November 1993 (93/717/EC) (the “Decision”) on a proposal for legislation entitled the Central Bank Bill (the “Bill”).

CON/96/04

1. The above consultation was initiated on 25th March 1996 by the Irish Department of Finance, which requested an opinion of the EMI within one month of receipt of the consultation, i.e. by 1st May 1996. For this purpose, the Department of Finance submitted the text of the above draft legislation together with explanatory memoranda.
2. The EMI’s competence to deliver an opinion is based on Article 1, section 1 of the Decision, as the Bill relates, inter alia, to the following: the status and powers of the Central Bank of Ireland (second indent of section 1); the collection, compilation, and dissemination of balance of payments, national accounts and other financial statistics (third indent of section 1); approval and supervision of clearing and payment systems (fourth indent of section 1); and, rules which are applicable to the regulation by the Central Bank of Ireland of financial institutions and which may have an impact upon the stability of financial institutions and markets (fifth indent of section 1). In this opinion, the EMI will restrict comments to those parts of the Bill which relate to the above areas of competence. It should also be noted that, in giving this opinion, the EMI has not reviewed all the existing provisions of Irish legislation to which the Bill refers and relates.
3. The EMI welcomes those provisions in the Bill which would enhance the influence of the Central Bank in relation to the oversight of payment systems established in Ireland.

The EMI notes that sections 14 and 15 of the Bill will give the Central Bank wide powers to suspend operations of the system where terms of the original or subsequent approval of the system are breached and to revoke its approval in certain circumstances. However, the exercise of the Bank’s powers to order a payment system to cease activities or to suspend operations on an immediate basis is dependent upon the Bank having first imposed a condition or requirement on the system which has, subsequently not been complied with. To ensure that emergency situations can always be adequately dealt with the EMI recommends consideration of an ability for the Bank, where extreme circumstances exist, to require immediate suspension of operations by a system or by one or more of its members, irrespective of the prior imposition of any condition or requirement. Albeit that such powers would clearly require to be subject to

subsequent review by the courts and would also require to be tied in effectively with all other powers of the Central Bank in this area, including the provisions contained in sections 14 and 15 of the Bill as drafted, so as to ensure a coherent set of powers in this area.

4. The EMI expressly welcomes the provisions contained in sections 21, 22 and 23 of the Bill which are designed to enshrine the following principles in Irish law: finality of payments; the immediate ability of lenders to realise collateral; and, the legal enforceability of bilateral and multilateral netting arrangements.

However, the EMI would suggest consideration of amendments to each of sections 21 and 22.

In the case of section 21 it might prove advisable to include a more detailed provision stating at what point in the process of settlement payments are to be considered final and irrevocable - will this occur upon transmission of instructions to settle or does settlement require to have taken place? In the absence of such additional detail there is a danger that confusion may arise as to when this provision comes into effect. It is also noted that the provision only provides for finality and irrevocability between the credit institutions concerned, thereby implying that this will not be enforceable against third parties. The EMI would encourage consideration of a wider provision expressly stating that finality and irrevocability would also be enforceable against third parties (e.g. a liquidator or third party creditor).

The EMI welcomes the provision in section 22 which would have the effect of ensuring that the Central Bank may realise collateral or securities immediately upon the default of a credit institution in relation to the loan against which such collateral or security is held - thereby presumably overriding any provisions of Irish law which would obstruct such immediate realisation. In view of Stage Three of EMU and the operation of a single monetary policy among participating member states, the EMI would suggest that consideration be given to extension of this provision so that its benefits not only cover the Central Bank but also extend to both the European Central Bank and other EU central banks.

The EMI also welcomes the provision contained in section 50 whereby the Central Bank is to be notified of any application for the winding-up of a licensed bank before the petition is presented and considers that this will be a potentially valuable tool in enabling the Central Bank to protect payment systems, particularly those over which it exercises supervisory powers. However, it is noted that the explanatory memorandum relating to this provision in the Bill states that the reasoning for its introduction is the avoidance of potential damage which might otherwise be caused by the existence of zero hour rules. The explanatory memorandum also notes that there is no precedent under Irish law for a zero hour ruling, but that this is not precluded. The EMI would therefore encourage the Irish authorities to consider a provision

(either within the Bill or within future legislation) which would put this issue beyond doubt by stating that there is no possibility of a zero hour ruling having effect in relation to validly constituted payments and financial contracts. Such a provision would be of great potential benefit in enhancing the stability and security of financial markets where an entity which would be subject to Irish insolvency law participates. This effect could be achieved, for example, by an expanded section 21, as suggested above.

5. The EMI notes the provision, contained in section 28 of the Bill, requiring the Governor of the Central Bank to appear before a relevant Select Committee of the Dail Eireann. Such a provision is not in principle inconsistent with the requirement for independence of central banks, imposed by Article 107 of the Treaty as reflected in Article 7 of the ESCB/ECB Statute.
6. The EMI notes the further extension of the prohibition imposed upon the Governor of the Central Bank from being a director or holding shares in a bank and that this prohibition will now cover all commercial credit institutions and financial institutions and welcomes the additional degree of independence which this will ensure for the office of Governor. However, one NCB has stated that this view should not prejudice further discussions on criteria for central bank statutory requirements to become an integral part of the ESCB.
7. The EMI welcomes the simplification of the tenure of office of the directors of the Central Bank, to a standard period of five years from the date of appointment.
8. In the light of the progress achieved by the EMI, in close co-operation with the Commission, with respect to the preparatory work in the field of statistics, an expansion of section 8, subsection (a) of the Central Bank Act 1942 along the following lines is suggested:

“(a) make provision for the definition, collection and study of data relating to monetary, financial, balance of payments and credit developments and publish related material;”

Subject to this expansion, the EMI welcomes the provision contained within section 30 of the proposal since it embodies the desired level of co-operation between central banks and relevant national statistical institutes within the limits of their respective competences. However, to ensure that, in the future, the Central Bank will be fully able to comply with its obligations under Article 5 of the ESCB/ECB Statute as a member of the ESCB in Stage Three of EMU the EMI also considers that it would be important to insert “without prejudice to subsection (a) above,” at the start of the envisaged, new subsection (d).

9. The EMI notes the additional powers which are proposed for the Central Bank in the field of supervision and regulation of credit institutions and other financial institutions. To the extent

that these changes provide the Central Bank with greater abilities to enhance the stability and security of financial institutions and markets, they are a welcome addition to the Irish regulatory environment.

10. The EMI welcomes the provisions contained in section 52 to 57 having the effect of removing provisions which previously allowed the Central Bank of Ireland to provide financing to the public sector, noting that these changes have been initiated with the intention of compliance with Article 104 of the Treaty.
11. The EMI notes that it is the intention of the Irish authorities to bring forward further legislation to ensure that, by the date of the establishment of the ESCB, Irish legislation is compatible with the Treaty and the ESCB Statute and thereby to comply with the terms of Article 108 of the Treaty and Article 14.1 of the ESCB/ECB Statute. The EMI also notes that adaptations will be required to allow national central banks to function as an integral part of the ESCB, as stated in Article 14.3 of the ESCB/ECB Statute and it may be foreseen that amendments to the legislation relating to the Central Bank are also likely to be required for this purpose.
12. The EMI confirms that it has no objection to this opinion being made public.

28th May 1996