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EUROPEAN CENTRAL BANK

EUROSYSTEM

OPINION OF THE EUROPEAN CENTRAL BANK

of 11 January 2010

on recovery measures that apply to undertakings in the banking and financial sector, on the supervision of the financial sector and financial services and on the statutes of the Nationale Bank van België/Banque Nationale de Belgique

(CON/2010/7)

Introduction and legal basis

On 23 November 2009 the European Central Bank (ECB) received a request from the Belgian Ministry of Finance for an opinion on three draft laws: (a) a draft law supplementing the recovery measures that apply to undertakings in the banking and financial sector (hereinafter the 'first draft law'), (b) a draft law providing remedies supplementing the first draft law (hereinafter the 'second draft law'), and (c) a draft law amending the law of 2 August 2002 on the supervision of the financial sector and financial services, as well as the Law of 22 February 1998 establishing the Organic Statute of the Nationale Bank van België/Banque Nationale de Belgique (hereinafter the 'third draft law'). Given the current turmoil in the financial markets and the need for firm intervention by the authorities involved, the consulting authority has requested the ECB to provide its opinion as a matter of urgency to allow for the swift adoption of the draft laws.

The ECB's competence to deliver an opinion is based on Articles 127(4) and 282(5) of the Treaty on the Functioning of the European Union, and the third, fifth and sixth indents of Article 2(1) of Council Decision 98/415/EC of 29 June 1998 on the consultation of the European Central Bank by national authorities regarding draft legislative provisions[1], as the draft laws relate to the Nationale Bank van België/Banque Nationale de Belgique (NBB), payment and settlement systems and rules applicable to financial institutions insofar as they materially influence the stability of financial institutions and markets. In addition, the Eurosystem shall contribute to the smooth conduct of policies relating to the prudential supervision of credit institutions and the stability of the financial system under Article 127(5) of the Treaty. In accordance with the first sentence of Article 17.5 of the Rules of Procedure of the European Central Bank, the Governing Council has adopted this opinion.

1 OJ L 189, 3.7.1998, p. 42.

1. Purpose of the draft laws

1.1 The first draft law extends the scope of the measures that the Banking, Finance and Insurance Commission (BFIC) and the King may take as part of the general rescue package put in place by the Belgian authorities in response to the current turmoil in the financial markets. Under the first draft law, the BFIC may suspend the execution of contracts of insurance undertakings and credit institutions that are subject to its supervision[2]. In addition, if an insurance undertaking, credit institution, securities settlement institution[3] or assimilated institution is not operated in compliance with applicable laws and if such non-compliance is likely to affect the stability of the Belgian or international financial system, the King may adopt any measure in favour of the State or any other person or entity, whether Belgian or foreign, and whether subject to public or private law. Such measure may provide for the transfer, sale or contributions relating to: (a) assets, liabilities or one or more fields of activity or all or part of the rights and obligations of an insurance undertaking or credit institution, as well as (b) securities or shares issued by all such institutions and undertakings, whether capital or not, and whether or not they entail voting rights[4].

1.2 The ECB understands from the explanatory memorandum that the purpose of such transfer, sale or contribution is to enable the underlying assets of the non-compliant undertakings and institutions to be transferred to 'bad banks', 'good banks' or 'bridge banks'. This legal framework is significantly inspired by the Law of 26 July 1962 on emergency proceedings for expropriations for public purposes, the constitutionality of which has been confirmed several times by the Belgian Constitutional Court[5]. If the Belgian State decides to carry out a transfer, sale or contribution, it must file a request with the Court of First Instance of Brussels. The Court will verify the legality of the transfer, sale or contribution and the fairness of the compensation. The transfer, sale or contribution will only take effect once the Court confirms that these two conditions are met. The owners of the assets subject to transfer, sale or contribution are only entitled to request that the Court review the issue of compensation, without prejudice to the transfer, sale or contribution being executed. When assessing the fairness of the compensation, the Court takes particular account of the credit institution's actual situation prior to the transfer, including its financial situation, or the financial situation it would have been in if the public aid, from which it has benefited directly or indirectly, had not been granted. For the purposes of this provision, advances of emergency liquidity and guarantees given by legal entities governed by public law are treated as public aid.

1.3 In addition, the first draft law amends the loss-sharing arrangements applicable to the owners of securities whose financial instruments are held by financial intermediaries involved in the issuance

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2 Articles 2(1) and 4(1) of the first draft law.

3 The 'securities settlement institution' is generally defined under Article 2(17) of the Law of 2 August 2002 on the supervision of the financial sector and financial services as 'an institution performing the settlement of transfer orders of financial instruments, of the entitlements relating to such financial instruments or forward exchange transactions, with or without cash settlement'. The securities settlement institution that may be subject to the new measure should also be licensed as central depository under Royal Decree No 62 on the deposit of fungible financial instruments and the settlement of operations concerning those instruments, coordinated by the Royal Decree of 27 January 2004.

4 Articles 2(2), 4(2) and 6(2) of the first draft law.

5 Second draft law, explanatory memorandum, p. 2.

or holding of book-entry securities[6]. Under the current provisions[7], in the event of the insolvency or administration of a financial intermediary that issues or holds book-entry securities, if the remaining value of securities of a given category is insufficient to discharge the obligation of that financial intermediary towards all owners of these securities, the loss is borne by all owners of the same category of instrument in proportion to their holdings. If the financial intermediary holds securities of the same category in its own name and for its own account, these securities will be shared between all other owners of the same category of security, thereby mitigating the loss incurred by the owners of those securities. Under the first draft law, if the owners of securities authorise a financial intermediary to dispose of their securities, and if the securities are disposed of as authorised, in the event of the insolvency or administration of the financial intermediary, the owners of the securities may not recover all the securities of the same category. The owners of these securities continue to have a claim against the financial intermediary, which will be satisfied after the claims of those owners of securities who have not authorised the re-use of their securities.

1.4 The third draft law sets up the 'Committee for systemic risks and system-relevant financial institutions' (CSRSFI)[8] as an autonomous institution with legal personality, with the task of contributing to maintaining the stability of the financial system and, in particular:

(a) monitoring the financial system in order to intervene if it identifies any threats to the stability of the system;

(b) advising the Federal Government and the Federal Parliament on measures that are necessary to contribute towards stability, and the proper functioning and efficiency of the country's financial system;

(c) coordinating crisis management;

(d) supervising financial institutions that are important to the financial system and in particular monitoring and evaluating the strategic developments and risk profiles of these institutions[9];

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6 Articles 32, 33 and 34 of the first draft law. These financial intermediaries include:
- all possible participants of securities settlement institutions (namely those authorised under Directive 98/26/EC of the European Parliament and of the Council of 19 May 1998 on settlement finality in payment and securities settlement systems (OJ L 166, 11.6.1998, p. 45), to become participants of a 'system', including the credit institutions, investment undertakings, public authorities, central counterparties, settlement agents, clearing houses, securities settlement systems and system operators),
- all licensed account holders (*teneurs de compte agréés*) under the Law on Companies and the Royal Decree of 12 January 2006, namely all credit institutions incorporated under Belgian law, stock exchange brokers incorporated under Belgian law, all branches of the aforementioned institutions when authorised in their home state to carry out similar activities, the NBB, as well as all securities settlement institutions incorporated under Belgian law, and
- the entities authorised to hold government bonds under the Law of 2 January 1991, namely credit institutions incorporated under Belgian law, investment undertakings incorporated under Belgian law, branches of the aforementioned institutions incorporated under the laws of an EU Member State, as well as securities settlement institutions.

7 Law of 2 January 1991 on the market in public debt securities and monetary policy instruments, and Royal Decree No 62 on the deposit of fungible financial instruments and the settlement of operations concerning such instruments, coordinated by the Royal Decree of 27 January 2004 as well as the Law on Companies.

8 Article 22 of the third draft law, inserting Chapter IV in the Law of 2 August 2002 on the supervision of the financial sector and financial services.

(e) ensuring the exchange of information and the coordination of policies between the NBB and the BFIC;

(f) contributing to the performance of these tasks on an international and European level, in so far as this concerns cooperation with the European Systemic Risk Board (ESRB).

1.4.1 The CSRSFI is exclusively authorised to take administrative decisions pertaining to the prudential supervision of financial institutions that are important to the financial system, including taking extraordinary recovery measures and imposing penalty payments. In exercising these powers, the CSRSFI will support the BFIC and the NBB, in accordance with their respective powers. The BFIC and the NBB are responsible for implementing the decisions within the areas of their responsibility.

The CSRSFI may oppose the strategic decisions of a financial institution that is important to the financial system, if its decisions would be contrary to the prudent management of the financial institution or if this would have a significant adverse effect on the stability of the financial system.

1.4.2 In the performance of its tasks, the CSRSFI is supported by the BFIC and the NBB, which provide information for the proper discharge of its tasks. The operating costs of the CSRSFI are to be borne by the budgets of the BFIC and the NBB, in accordance with the decision of the King on the recommendation of the CSRSFI.

1.4.3 The CSRSFI is composed of the members of the BFIC's Executive Committee and of the NBB's Board of Directors with an observer from the Federal Public Service Finance appointed by the Minister for Finance. The CSRSFI is chaired by the NBB's Governor. Decisions are taken on the basis of a majority of the votes cast. The Chair has a casting vote.

1.4.4 The CSRSFI staff members and governing body members, as well as the persons previously fulfilling the functions referred to above, are bound by obligations of confidentiality and may not disclose confidential information concerning the CSRSFI's activities or policies to any unauthorised person or authority.

1.4.5 By 30 September 2010, the King will adopt royal decrees that will allow for the structures related to supervision of the financial sector to be developed[10]. Under the royal decrees, NBB will be entrusted with (a) the powers and tasks of the CSRSFI, insofar as they concern the prudential supervision of financial institutions that are important to the financial system, and (b) with the powers and tasks of the BFIC, insofar as they concern the prudential supervision of credit institutions, insurance companies, investment firms, management companies of undertakings for collective investment, reinsurance companies and institutions for corporate pension schemes, with the exception of the supervision of codes of conduct that apply to the savings, investments,

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9 Financial institution that are important to the financial system are defined by reference to a combination of institutional criteria (it may be a credit institution or an insurance undertaking) and economic criteria (the amount of the balance sheet of the consolidated annual accounts, market share of the savings market or the supply of credit in Belgium, or its deciding role with regard to custodian or payment activities, or transactions relating to Belgian securities on Belgian territory). See Article 2 of the third draft law.

10 Article 26 of the third draft law.

pensions and insurance markets. Under the royal decrees NBB will have the power to establish one or more legal entities (hereinafter the 'entities') to exercise all or some of the powers referred to above and some of the tasks assigned to the NBB by the Law of 22 February 1998 establishing the Organic Statute of the NBB. The NBB, on behalf of those entities, will be responsible for establishing their tasks, bodies and methods of funding, providing personnel, and using any other means necessary to ensure their effectiveness. Furthermore, the royal decrees will regulate the transfer of NBB staff members to the entities and the transfer of BFIC staff members to the NBB or to the entities; the legal entity to which the staff members are transferred will assume all existing rights and obligations as regards such staff members.

2. General observations

2.1 *Reorganisation of the supervisory structure of the Belgian authorities*

2.1.1 The ECB supports the Belgian supervisory reform, which is aimed at enhancing the Government's ability to identify and monitor systemic risks. The establishment of the CSRSFI, which will be followed next year with NBB being assigned responsibility for the prudential supervision of all financial institutions (thereby adopting a 'twin-peaks' supervisory model) is welcome and is in line with the ECB's consistent position regarding the need for the close involvement of central banks in prudential supervision[11]. The ECB understands that the supervisory reform that is the subject of the third draft law will be accomplished by way of separate legislation, yet to be adopted by the King. This separate legislation should be the subject of a separate consultation based on Articles 127(4) and 282(5) of the Treaty; the general comments that follow are without prejudice to a more detailed analysis of the supervisory reform, based on the royal decrees to be adopted by the King.

2.1.2 In order to avoid any legal risks associated with the independent discharge of the NBB's European System of Central Banks (ESCB)-related tasks, any new legal entity established by the NBB to carry out existing or new tasks of the NBB under the supervisory reform could be placed under the control of the NBB's decision-making body responsible for the discharge of its ESCB-related tasks. However, as specified by the ECB in its Convergence Reports[12], 'if the law provides for separate decision-making by such supervisory authorities, it is important to ensure that decisions adopted by them do not endanger the finances of the NCB [national central bank] as a whole. In those cases, the national legislation should enable the NCBs to have ultimate control over any decision by the supervisory authorities that could affect an NCB's independence, in particular its financial independence.' The exposure of the NBB to liabilities resulting from the funding and budgetary decisions of such entities that are outside the control of the NBB's decision-making body responsible for the discharge of its ESCB-related tasks, but that are at the same time a constituent part of the NBB, could be seen as a threat to the NBB's financial independence[13]. The new entities

11 Opinion CON/2007/33, paragraph 2.1. All ECB opinions are available on the ECB's website www.ecb.europa.eu.

12 ECB's Convergence Report 2008, p. 21 and 22.

13 ECB's Convergence Report 2008, p. 21 to 23. See also footnote 15.

should not seek to influence the NBB's decision-making body in the performance of its ESCB-related tasks, and the NBB should in particular preserve its institutional independence[14].

2.2 *Establishment of the CSRSFI*

2.2.1 The ECB understands that the CSRSFI, an autonomous institution with a legal personality, decision-making competences, and regulatory as well as sanctioning powers, will have the task of contributing to maintaining the stability of the financial system. As the ESRB has similar responsibilities, and as the task of contributing, at national level, to the stability of the financial system is shared with the NBB[15], the ECB makes the following observations regarding the establishment of this committee.

2.2.2 First, the establishment of national financial stability committees can enhance the ability of national central banks and supervisory authorities to contribute analytical support to the ESRB. The tasks performed by these committees should complement the activities performed by the ESRB, therefore it is particularly important to develop appropriate synergies. However, it is necessary to avoid such national committees being entrusted with tasks and powers that potentially conflict with those of the ESRB, and which may undermine the effectiveness of the newly-established European macro-prudential supervisory body. Moreover, the legal frameworks of these committees should appropriately reflect the roles of central banks, should not constrain the independence of the governors of the central banks or unduly affect the quality and impartiality of their contributions as members of the ESRB. Lastly, in view of the importance of ensuring the effectiveness of macro-prudential supervisory arrangements at the EU level, it is essential to safeguard the ability of the ESRB to perform its tasks independently and to guarantee an authoritative and effective channel for transmitting the warnings and recommendations issued by the ESRB.

2.2.3 Second, the Memorandum of Understanding on cooperation between Financial Supervisory Authorities, Central banks and Finance Ministries of the European Union on cross-border financial stability (MoU) that entered into force on 1 June 2008, provides for the establishment in each Member State of a domestic standing group, i.e. a national level group consisting of the financial supervisory authorities, central banks and finance ministries, with the objective of enhancing preparedness under normal market conditions and facilitating the management and resolution of financial crises. Following the conclusion of the MoU, the Belgian authorities designated the Belgian Financial Stability Committee as the national domestic standing group. For the purposes of legal certainty, the related tasks, i.e. enhancing preparedness under normal market conditions and facilitating the management and resolution of a financial crisis, could be listed in the third draft law among the tasks entrusted to the CSRSFI.

2.2.4 Third, it is necessary to ensure that the tasks assigned to the CSRSFI, i.e. to supervise the financial institutions that are important to the financial system and in particular to guarantee the monitoring

14 Opinion CON/2002/16, paragraph 6.

15 Article 12 of the Law of 22 February 1998 establishing the Organic Statute of the NBB.

and evaluation of the strategic developments and risk profiles of these institutions, do not prejudice nor overlap with the exclusive responsibility of the NBB to ensure the proper, efficient and sound operation of clearing systems[16], as such securities settlement systems qualify as financial institutions that are important to the financial system under the third draft law[17], as well as the responsibilities of NBB as an integral part of the Eurosystem based on Article 127(2) of the Treaty and Article 22 of the Statute of the European System of Central Banks and of the European Central Bank (hereinafter the 'Statute of the ESCB').

2.2.5 Fourth, as regards the financing of the CSRSFI by the NBB[18], the ECB refers to the principle of financial independence according to which an NCB must have sufficient means not only to perform its ESCB-related tasks, but also its own national tasks[19]. Also, the supervisory tasks should be carried out while complying with the prohibition of monetary financing laid down in Article 123(1) of the Treaty, read in conjunction with Council Regulation (EC) No 3603/93 of 13 December 1993 specifying definitions for the application of the prohibitions referred to in Articles 104 and 104b(1) [now Articles 123 and 125(1)] of the Treaty[20]. Thus, the assignment to the NBB of the tasks and powers of the BFIC must be accompanied by measures that insulate the NBB from financial obligations resulting from the prior activities of the BFIC[21].

2.2.6 Fifth, one of the CSRSFI's tasks will be to ensure the exchange of information between the NBB and the BFIC. Such information is protected by the rules on confidentiality applicable to the members of the CSRSFI's governing body and its staff members. The ECB recommends that these rules on confidentiality should be complemented with appropriate information disclosure standards that are consistent with Union law provisions that regulate the exchange of supervisory and statistical information between supervisory authorities[22].

16 Opinion CON/2002/13, paragraph 11.

17 See the definition of 'system-relevant financial institution' in Article 2 of the third draft law; see also the explanatory memorandum to the third law, p. 4 and 5.

18 In accordance with a Royal Decree to be adopted by the King.

19 Opinion CON/2009/93, paragraph 3.1.5.

20 OJ L 332, 31.12.1993, p. 1.

21 ECB's Convergence Report May 2008, p. 23 and 24; see Opinion CON/2005/24, paragraph 12, and Opinion CON/2005/39, paragraph 9.

22 See, e.g., Article 12 of Directive 2002/87/EC of the European Parliament and of the Council of 16 December 2002 on the supplementary supervision of credit institutions, insurance undertakings and investment firms in a financial conglomerate and amending Council Directives 73/239/EEC, 79/267/EEC, 92/49/EEC, 92/96/EEC, 93/6/EEC and 93/22/EEC, and Directives 98/78/EC and 2000/12/EC of the European Parliament and of the Council (OJ L 35, 11.2.2003, p. 1), Article 58(5) of Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments amending Council Directives 85/611/EEC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and repealing Council Directive 93/22/EEC (OJ L 145, 30.4.2004, p. 1), Article 49 of Directive 2006/48/EC relating to the taking up and pursuit of the business of credit institutions (recast) (OJ L 177, 30.6.2006 p. 1), and Article 70 of the Directive of the European Parliament and of the Council on the taking-up and pursuit of the business of insurance and reinsurance (Solvency II) (recast), 19 October 2009 (not yet published in the *Official Journal of the European Union*).

3. Specific remarks

3.1 *Transfer, sale or contribution of assets, liability, branches of activities, securities or shares*

3.1.1 The draft laws provide a new legal framework for the transfer, sale or contribution of assets, liabilities or shares of credit institutions, insurance undertakings, securities settlement institutions and assimilated institutions, to enhance the tools for managing crises of financial institutions and in particular to enable the transfer of underlying assets to 'bridge banks'. Such a development is welcome and is in line with current policies both at European and international levels for establishing a sound crisis resolution framework to intervene when financial institutions have a systemic impact on the financial system.

3.1.2 The ECB notes that the first draft law provides that the King, either at the BFIC's request or on his own initiative, after receiving an opinion from the BFIC and the CSRSFI, has the power to initiate the sale, transfer or contribution by an insurance undertaking, a credit institution, a securities settlement institution or assimilated institution, of assets in favour of the State or any other person or entity (whether Belgian or foreign, and whether subject to public or private law). This procedure does not sufficiently recognise the important role of the NBB when evaluating the consequences of such measures on overall financial stability, as the first draft law envisages a role for the NBB limited to providing opinions at the request of the BFIC.

3.1.3 The ECB understands that the Belgian legislator has framed the proceedings leading to such measures in the light of the decisions of the European Court for Human Rights[23] as well as of the Belgian Constitutional Court, and so to comply with the principle that no one may be deprived of their possessions except in the public interest and in accordance with the law. The second draft law establishes a detailed legal framework, with the involvement of a court to verify that the conditions of the law are complied with, and that the compensation paid to the owners of the underlying assets is fair[24]. The ECB assumes that such measures will be taken in exceptional circumstances where, in compliance with the principle of proportionality, the seriousness of the measure is commensurate to the threat to the financial stability that the measure seeks to remedy. As already mentioned in its opinion on rescue measures adopted by the Belgian legislator[25], it is important that national authorities seek to coordinate their responses to the current financial situation with their Union partners, in line with applicable Union law and the arrangements in place, such as the MoU[26].

3.1.4 As for paragraph 6 of the second draft law, in line with its previous opinions[27], the ECB emphasises that emergency liquidity assistance should consist of temporary liquidity provision to illiquid but solvent institutions. In this respect, the provision of emergency liquidity assistance is a normal central bank task and cannot be considered as State aid. Therefore, the sentence referring to

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23 7 November 2002, *Olczak* v *Poland*, No 30417/96 and 1 April 2004, *Camberrow MMS AD* v *Bulgaria*, No 50357/99.

24 Articles 2, 4 and 6 of the second draft law.

25 Opinion CON/2008/46, in particular paragraph 2.2.

26 Available on the ECB's website at www.ecb.europa.eu.

27 In particular, see Opinion CON/2008/46, paragraph 3.1.

emergency liquidity assistance as a form of State aid[28] could be misleading. For the sake of clarity, it is suggested that the word '*publiques*' should be deleted from this sentence of the draft law and the explanatory memorandum.

3.1.5 The above measures are without prejudice to the NBB's oversight function on the basis of Article 127(2) of the Treaty and Article 22 of the Statute of the ESCB. Securities settlement institutions and assimilated institutions, to the extent that they are subject to the abovementioned exceptional measures upon the occurrence of exceptional circumstances, should continue to employ all necessary accounting practices and safekeeping procedures, as well as internal and external controls to comply with ESCB/Committee of European Securities Regulators' 'Recommendations for Central Counterparties' (CESR), in particular Recommendations 7 and 14, and provide participants with sufficient information for them to identify and evaluate accurately the risks associated with using these services. Custodians entrusted with financial instruments by a Central Counterparty should continue to comply with ESCB/CESR Recommendations for Security Settlement Systems, including Recommendations 12 and 18.

3.2 *Amendment of the loss-sharing arrangements upon insolvency of a financial intermediary*

Notwithstanding the loss-sharing arrangement proposed under the first draft law and without prejudice to the NBB's oversight functions in accordance with Articles 127(2) of the Treaty and Article 22 of the Statute of the ESCB, there must always be a number of procedures, controls and remedies in place to reflect ESCB/CESR Recommendations for securities settlement systems, in particular Recommendations 6 and 12, making the materialisation of such a loss actually highly unlikely. Moreover, the records maintained by financial intermediaries must include details of the clients and financial instruments that may be used to enable the correct calculation in any loss allocation mechanism that might be applicable. Finally, financial intermediaries should provide securities owners with sufficient information for them to accurately evaluate the risks and costs associated with any applicable loss sharing arrangements.

28 See Article 2 of the second draft law, inserting an Article 26ter in the Law of 9 July 1975 concerning the regulation of insurance undertakings, §6 in fine, which reads as follows: 'The Court shall in particular take into the insurance undertaking's practical situation before the transfer, especially the financial situation it was in, or the financial situation it would have been in if public aid, from which the insurance undertaking directly or indirectly benefited, had not been granted. For the purposes of the current provision, the following shall be treated as public aid: advances of emergency liquidity and guarantees given by a legal entites governed by public law'. See the similar provisions in Article 3, inserting an Article 57ter §6 in the Law of 22 March 1993 concerning the status and supervision of credit institutions and Article 4 inserting an Article 23/2 in the Law of 2 August 2002 on prudential supervision of the financial sector and financial services.

This opinion will be published on the ECB's website.

Done at Frankfurt am Main, 11 January 2010.

[signed]

The President of the ECB

Jean-Claude TRICHET