



OPINION OF THE EUROPEAN CENTRAL BANK

of 12 July 2016

**on the exclusion of set-off rights with respect to claims mobilised as collateral with a central bank
of the European System of Central Banks**

(CON/2016/37)

Introduction and legal basis

On 10 June 2016 the European Central Bank (ECB) received a request from the French Ministry of Finance and Public Accounts for an opinion on a draft legal provision excluding the exercise of any contractual or statutory right to set-off with respect to credit claims mobilised as collateral with a central bank of the European System of Central Banks (ESCB) (hereinafter the 'draft law').

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/EC¹, as the draft law relates to national central banks, payment and settlement systems, and the rules applicable to financial institutions insofar as they materially influence the stability of financial institutions and markets. 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. Purpose of the draft law

- 1.1 The purpose of the draft law is to introduce in French law a specific provision to eliminate set-off risks resulting from the acceptance by the Banque de France and other ESCB central banks of credit claims as eligible collateral in ESCB monetary policy, intraday credit and other credit operations.
- 1.2 Set-off rights arise in situations where a debtor has a legal right to set-off or net its obligations towards a creditor by the amount of outstanding claims the debtor has against the creditor, e.g. bank deposits. A set-off risk is the risk of loss for the ESCB which arises when an ESCB central bank enforces a credit claim presented as collateral by a defaulting counterparty where the credit claim mobilised as collateral would have lost part of its value as a result of set-off.
- 1.3 In order to eliminate set-off risk the draft law provides that, notwithstanding any provision or stipulation to the contrary, no right to set-off may give rise to the extinction, in full or in part, of credit claims submitted as collateral to a central bank that forms part of the ESCB.

¹ Council Decision 98/415/EC of 29 June 1998 on the consultation of the European Central Bank by national authorities regarding draft legislative provisions (OJ L 189, 3.7.1998, p. 42).

2. General observations

- 2.1 Credit claims have been accepted as eligible collateral for Eurosystem monetary policy and intraday credit operations since 1 January 2007². The scope for accepting eligible credit claims has been extended by the additional credit claims (ACC) framework that was implemented in December 2011 as a temporary measure. Under the ACC framework other types of credit claims, such as residential mortgages or pools of credit claims, provided they meet certain additional specific criteria, qualify as eligible collateral in certain euro area jurisdictions, including France.
- 2.2 The ECB considers the draft law's aim of excluding set-off risks associated with the acceptance of credit claims as collateral in Eurosystem credit operations as legitimate and fully in line with the Statute of the European System of Central Banks and of the European Central Bank (hereinafter the 'Statute of the ESCB'). Protecting the ESCB against any potential loss arising from the acceptance of such collateral is closely linked to the requirement laid down in the second indent of Article 18.1 of the Statute of the ESCB, pursuant to which lending by the ESCB central banks must be based on adequate collateral. In addition, adequately addressing set-off risks also facilitates the continued eligibility of credit claims as eligible collateral in Eurosystem credit operations³, and thereby contributes to the efficiency of the transmission of monetary policy to the real economy.
- 2.3 The ECB notes that, in line with the draft law, several other euro area Member States have enacted statutory provisions which exclude set-off risks when credit claims are mobilised as collateral for central bank operations. The approach adopted by these Member States differs as to the scope of the parties benefitting from the exclusion. In certain Member States statutory provisions only exclude set-off rights for credit claims mobilised as collateral for operations with the particular Member State's central bank. Some Member States also have statutory provisions that provide protection for the ECB and other ESCB central banks. In one Member State, the exclusion of set-off rights applies to operations with all Union central banks and any third party to whom a credit claim may subsequently be transferred by a central bank⁴.
- 2.4 Against this background, the draft law excludes all rights to set-off credit claims mobilised as collateral with an ESCB central bank⁵. This exclusion is not subject to any additional formalities and applies regardless of any other provisions or stipulations, whether laid down in other legal acts or by way of contract. The ECB welcomes the initiative of the French authorities to exclude such

² See 'Decisions taken by the Governing Council of the ECB (in addition to decisions setting interest rates)' for July 2005 and the related ECB press release of 22 July 2005 entitled 'Eurosystem collateral framework: Inclusion of non-marketable assets in the Single List', available on the ECB's website at www.ecb.europa.eu.

³ In 2008 the European Commission noted that the possible exercise of set-off rights by the debtor of the credit claim provided as collateral could discourage the use of credit claims as collateral. This is because 'the collateral can as such disappear if the debtor exercises set-off right vis-à-vis the creditors of the credit claim and vis-à-vis persons to which the creditors assigned, pledged or otherwise mobilised the credit claim as collateral.' See 'Commission staff working document accompanying the Proposal for a Directive of the European Parliament and of the Council amending the Settlement Finality Directive and the Financial Collateral Directive – Impact Assessment', April 2008, available on Eur-lex website at www.eur-lex.europa.eu.

⁴ See the Law on the Autonomy of Banco de España, sixth additional provision, paragraph (4)(e) introduced by the Royal Decree-Law 2/2012 on the reorganisation of the financial sector.

⁵ The ECB notes that the legal technique used for the mobilisation of credit claims with the Banque de France is the title transfer financial collateral arrangement under Article L.211-38 of the French monetary and financial code (COMOFI). Under Article L.211-38 of the COMOFI the constitution and opposability of such title transfers are not subject to any particular formality.

set-off risks⁶. In particular, the ECB welcomes the broad scope of application of the draft law and the fact that its provisions will apply to credit claims mobilised as collateral in operations with all ESCB central banks.

- 2.5 However, the ECB considers that in order to increase the effectiveness of the protection against set-off rights, the draft law should also apply to any third party purchasing credit claims from an ESCB central bank. In fact, in the event of a default of a central bank's counterparty, the collateral represented by the credit claims, would have to be enforced. The central bank enforcing the collateral as the legal owner of the credit claims, might decide to hold the credit claims in its portfolio or sell them to a third party. If the credit claims are sold to a third party, the ESCB central banks would only be fully protected against the set-off risk if the protection afforded to ESCB central banks was transferred together with the credit claims to the third-party purchaser. Otherwise the applicable set-off rights might continue to affect the value at which the ESCB central banks could sell the credit claims. In this respect, the ECB suggests that in order to ensure full effectiveness of the draft law when a central bank wants to sell its credit claims to a third party, the draft law should explicitly extend the protection against set-off rights to third-party purchasers.

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

Done at Frankfurt am Main, 12 July 2016.

[signed]

The President of the ECB

Mario DRAGHI

⁶ The ECB already noted in its response to the Commission's Green Paper on establishing a capital market union (CMU), that while set-off rights can currently be validly waived by debtors pursuant to the Financial Collateral Directive (FCD), the divergence in the transposition and interpretation of the FCD greatly undermines the underlying rationale of protecting collateral takers of this provision, which could be mitigated if set-off were fully excluded with respect to credit claims mobilised as collateral with central banks. See 'Building a Capital Markets Union – Eurosystem contribution to the European Commission's Green Paper', p. 24, available on the ECB's website at www.ecb.europa.eu.