



EUROPEAN CENTRAL BANK
EUROSYSTEM

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ECB-PUBLIC

OPINION OF THE EUROPEAN CENTRAL BANK
of 29 November 2017
on benchmarks in financial instruments and financial contracts
(CON/2017/52)

Introduction and legal basis

On 6 October 2017 the European Central Bank (ECB) received a request from Българска народна банка (Bulgarian National Bank) (BNB), following correspondence exchanged between BNB and the Minister of Finance, for an opinion on a draft law on payment services and payment systems¹ (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 indent of Article 2(1) of Council Decision 98/415/EC², as the draft law relates to BNB. 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

One of the aims of the draft law that the ECB's previous opinion on the draft law³ did not address is the implementation in Bulgaria of some elements of Regulation (EU) 2016/1011 of the European Parliament and of the Council⁴. In particular, BNB will be designated as the competent authority responsible for carrying out the duties specified under Regulation (EU) 2016/1011 in relation to administrators of interest rate benchmarks and the relevant supervised entities, which are credit institutions within the meaning of Regulation (EU) No 575/2013 of the European Parliament and of the Council⁵, creditors within the meaning of Directive 2008/48/EC of the European Parliament and of the Council⁶, and non-credit institutions within the meaning of Directive 2014/17/EU of the European Parliament and of the Council⁷.

¹ In particular, BNB has reconsulted the ECB on certain provisions of the draft law which were not included in the original draft on which the ECB issued Opinion CON/2017/28. All ECB opinions are available on the ECB's website at www.ecb.europa.eu.

² 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).

³ Opinion CON/2017/28.

⁴ Regulation (EU) 2016/1011 of the European Parliament and of the Council of 8 June 2016 on indices used as benchmarks in financial instruments and financial contracts or to measure the performance of investment funds and amending Directives 2008/48/EC and 2014/17/EU and Regulation (EU) No 596/2014 (OJ L 171, 29.6.2016, p. 1).

⁵ Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (OJ L 176, 27.6.2013, p. 1).

⁶ Directive 2008/48/EC of the European Parliament and of the Council of 23 April 2008 on credit agreements for consumers and repealing Council Directive 87/102/EEC (OJ L 133, 22.5.2008, p. 66).

⁷ Directive 2014/17/EU of the European Parliament and of the Council of 4 February 2014 on credit agreements for consumers relating to residential immovable property and amending Directives 2008/48/EC and 2013/36/EU and Regulation (EU) No 1093/2010 (OJ L 60, 28.2.2014, p. 34).

BNB will therefore have the supervisory powers set out in Article 41 of Regulation (EU) 2016/1011, as well as the power to impose administrative sanctions and other administrative measures in relation to infringements, in accordance with Article 42 thereof. The draft law also amends the Law on Българска народна банка (Bulgarian National Bank)⁸ in order to ensure that the Governing Council of BNB is competent to adopt the related decisions.

2. General observations

- 2.1 The draft law confers upon BNB the new task of supervising compliance of administrators of interest rate benchmarks and the relevant supervised entities with Regulation (EU) 2016/1011. Where a new task is conferred on a national central bank (NCB) in the European System of Central Banks (ESCB) it must be assessed against the prohibition on monetary financing under Article 123 of the Treaty. For the purposes of that prohibition, Article 1(1)(b)(ii) of Council Regulation (EC) No 3603/93⁹ defines 'other type of credit facility' as, inter alia, 'any financing of the public sector's obligations vis-à-vis third parties'.
- 2.2 Ensuring that Member States implement a sound budgetary policy is one of the key objectives of the monetary financing prohibition, which may not be circumvented¹⁰. In view of this, the task of financing measures, which are normally the responsibility of the Member States and funded from their budgetary sources rather than by the NCBs, must not be entrusted to NCBs. To decide what constitutes financing of the public sector's obligations vis-à-vis third parties, which can be translated as the provision of central bank financing outside the scope of central bank tasks, it is necessary to carry out on a case-by-case basis an assessment of whether the task to be undertaken by an NCB is a central bank task or a government task, i.e. a task within the responsibility of the Member States. In other words, adequate safeguards must be in place to ensure that no circumventions of the objective of the monetary financing prohibition of maintaining a sound budgetary policy of Member States take place.
- 2.3 As part of its discretion in the exercise of its duty, on the basis of Article 271(d) of the Treaty and Article 35.6 of the Statute of the European System of Central Banks and of the European Central Bank (hereinafter the 'Statute of the ESCB'), and in order to ensure that NCBs honour the obligations laid down by the Treaty, the Governing Council has endorsed safeguards of that kind in the form of criteria for determining what may be seen as falling within the scope of a public sector's obligation within the meaning of Article 1(1)(b)(ii) of Regulation (EC) No 3603/93 or, in other words, what constitutes a government task as follows:

First, central bank tasks are in particular those tasks that are related to the tasks that have been conferred upon the ECB and the NCBs by the Treaty and the Statute of the ESCB. These tasks are mainly defined in Article 127(2), (5) and (6) and Article 128(1) of the Treaty, as well as Article 22 and Article 25.1 of the Statute of the ESCB.

⁸ Published in *Darjaven Vestnik* No 46, 10 June 1997.

⁹ 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) of the Treaty (OJ L 332, 31.12.1993, p. 1).

¹⁰ Article 123 of the Treaty also serves the objective of maintaining price stability and reinforces central bank independence.

Second, as Article 14.4 of the Statute of the ESCB allows NCBs to perform 'other functions', new tasks, i.e. tasks that are not related to tasks that have been conferred upon the ECB and the NCBs, are not precluded per se. However, new tasks that are undertaken by an NCB and which are atypical of NCB tasks or which are clearly discharged on behalf of, and in the exclusive interest of the government or of other public sector entities, should be considered government tasks.

Third, an important criterion for qualifying a new task as atypical of an NCB task or as being clearly on behalf of, and in the exclusive interest of the government or other public sector entities, is the impact of the task on the institutional, financial and personal independence of that NCB.

In particular, the following aspects should be taken into account:

- (a) whether the performance of the new task creates conflicts of interest with existing central bank tasks which are not adequately addressed, and does not necessarily complement those existing central bank tasks. If a conflict of interest arises between existing and new tasks, sufficient safeguards to mitigate that conflict should be in place. The complementarity between a new task and the existing central bank tasks should not be interpreted broadly, so as to lead to the creation of an indefinite chain of ancillary tasks. Such complementarity should also be examined in relation to the financing of those tasks;
- (b) whether without new financial resources the performance of the new task is disproportionate to the NCB's financial or organisational capacity, and may have a negative impact on the capacity to perform properly the existing central bank tasks;
- (c) whether the performance of the new task fits into the institutional set-up of the NCB in the light of central bank independence and accountability considerations;
- (d) whether the performance of the new task harbours substantial financial risks;
- (e) whether the performance of the new task exposes the members of the NCB decision-making bodies to political risks which are disproportionate and may also have an impact on their personal independence and, in particular, on the guarantee of term of office set out in Article 14.2 of the Statute of the ESCB.

3. Specific observations

Currently BNB carries out activities related to the calculation and publication of interest rate benchmarks, namely the SOFIBID and SOFIBOR reference rates¹¹, the LEONIA Plus reference rate¹², as well as the base interest rate in Bulgaria¹³. While BNB administers these benchmarks, it has no dedicated supervisory function with regard to them. The draft law therefore confers upon BNB a new task.

On the basis of the criteria set out in paragraph 2.3, the following paragraphs assess whether BNB's new task is in line with the monetary financing prohibition.

¹¹ On the basis of a contractual agreement between BNB, the Association of Banks in Bulgaria and the ACI Bulgaria-BDA.

¹² In accordance with the Methodology for calculation of the LEONIA Plus reference rate, adopted by the Governing Council of BNB.

¹³ In accordance with Article 35 of the Law on Българска народна банка (Bulgarian National Bank).

3.1 *New tasks related to the tasks conferred upon the ECB and the NCBs by the Treaty and the Statute of the ESCB*

The supervision of compliance of administrators of interest rate benchmarks and the relevant supervised entities with Regulation (EU) 2016/1011 is not among the central banking tasks listed in Article 127(2) or (5) of the Treaty or otherwise conferred upon the NCBs by the Statute of the ESCB. Although the new task conferred on BNB relates to overseeing compliance with Union law requirements by credit institutions (among others), it does not form part of BNB's prudential supervisory tasks. It follows that the new task conferred on BNB under the draft law is not directly related to the tasks conferred on the ECB and the NCBs by the Treaty and the Statute of the ESCB. Consequently, a careful assessment of the conferral of this task on BNB is required in order to determine whether it constitutes a government task, and whether the related funding gives rise to monetary financing concerns.

3.2 *Tasks which are atypical of NCB tasks*

Designation as a competent authority responsible for carrying out the duties under Regulation (EU) 2016/1011 in relation to administrators of interest rate benchmarks and the relevant supervised entities is a new task for national authorities in the Union.

In this regard, central banks have a particular interest in interest rate benchmarks which are of importance for the monetary policy transmission and financial stability¹⁴. In fact, the ECB itself is also planning the compilation and publication of a new unsecured overnight interest rate benchmark¹⁵.

While the majority of Member States have designated national capital markets supervisors for this task, the ECB has identified a number of Member States, including the Czech Republic¹⁶, Portugal¹⁷ and Slovakia¹⁸, where NCBs have been conferred at least part of the tasks under Regulation (EU) 2016/1011.

The new task conferred on BNB by the draft law does not, therefore, appear to be atypical for an NCB of the ESCB.

3.3 *Impact of the tasks on the independence of BNB*

The potential impact of the new task on the institutional, financial and personal independence of BNB must also be taken into consideration.

3.3.1 *Extent to which the performance of the new task creates conflicts of interest with existing central bank tasks*

¹⁴ See Opinion CON/2014/2 and the European Commission's public consultation on the regulation of indices – Eurosystem's response, November 2012.

¹⁵ See press release, 'ECB to publish new unsecured overnight interest rate', 21 September 2017, available on the ECB's website at www.ecb.europa.eu.

¹⁶ Article 192a(1)(j) of Law No 256/2004 Coll. on capital market undertakings designates Česká národní banka as the competent authority for the purposes of Regulation (EU) 2016/1011 effective as of 3 January 2018.

¹⁷ Article 2, n.º 1, al. b of Regulatory Decree No 8/2017 designates the Banco de Portugal as competent national authority for the supervision of the use of benchmark indices in financial contracts entered into by entities subject to its supervision.

¹⁸ Article 132s of the Law on securities and investment services designates Národná banka Slovenska as the competent authority for implementing authorisations in relation to authorisations in respect of the indices used as benchmarks in financial instruments and financial contracts or to measure the performance of investment funds.

As noted above, BNB is already performing activities related to the calculation and publication of interest rate benchmarks and is consequently administering these benchmarks. Central banks are not subject to Regulation (EU) 2016/1011, as they already meet principles, standards and procedures that ensure that they carry out their activities with integrity and in an independent manner¹⁹. To the extent that BNB has been conferred the tasks of supervising administrators of interest rate benchmarks, potential conflicts of interest may arise and therefore, sufficient safeguards to mitigate such conflicts should be put in place.

3.3.2 *Extent to which the performance of the new task places a disproportionate burden on BNB's financial or organisational capacity*

The principle of financial independence requires that Member States may not put their NCBs in a position where they have insufficient resources to carry out both their ESCB-related tasks and their national tasks, from an operational and financial perspective. Furthermore, when allocating specific new tasks to NCBs, each NCB concerned should have sufficient financial and human resources at its disposal to ensure that the tasks can be carried out without impacting on the NCB's financial or operational capacity to perform its ESCB tasks. In order to ensure that BNB's capacity to perform its ESCB-related tasks is not impacted, BNB must, therefore, be in a position to avail itself of the necessary resources, including personnel, to carry out supervision under the draft law.

3.3.3 *Extent to which performance of the new task fits into BNB's institutional set-up, in the light of the principles of central bank independence and accountability*

The performance of the new tasks does not appear to be problematic from the perspective of BNB's institutional set-up or to raise accountability or personal and institutional independence concerns.

3.3.4 *Extent to which the performance of tasks harbours substantial financial risks*

The draft law does not directly address BNB's potential liability in the event of any legal action, application or other legal proceedings for damages in relation to the exercise of its powers under the draft law or the failure to exercise such powers. In the absence of any provision in the draft law excluding BNB's liability in performing the tasks under the draft law, BNB would ultimately be liable for damages in accordance with the general liability regime under Bulgarian law. Therefore, the new task conferred on BNB under the draft law would entail additional financial risks.

3.3.5 *Extent to which the performance of the new task exposes members of BNB's decision-making bodies to disproportionate political risks and has an impact on their personal independence*

The performance of the new task does not appear to expose the members of BNB's decision-making bodies to any disproportionate political risk or to have an impact on their personal independence.

3.4 *Conclusion regarding the compatibility of the draft law with the prohibition on monetary financing*

The task of carrying out the duties under Regulation (EU) 2016/1011 in relation to administrators of interest rate benchmarks and the relevant supervised entities is not among the central banking tasks listed in the Treaty. The new task conferred on BNB could be regarded as complementing

¹⁹ See recital 14 and Article 2(2)(a) of Regulation (EU) 2016/1011.

BNB's monetary policy and financial stability tasks. Furthermore, this task might be seen as a legitimate task to confer on BNB given that it does not appear to be atypical for NCBs in the ESCB. However, there is uncertainty as regards the size of the additional financial burden imposed on BNB in undertaking this task. The ECB therefore recommends that the consulting authority takes this concern into account when conferring upon BNB the new task of carrying out the duties under Regulation (EU) 2016/1011 in relation to administrators of interest rate benchmarks and the relevant supervised entities.

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

Done at Frankfurt am Main, 29 November 2017.

[signed]

The President of the ECB

Mario DRAGHI