EUROPEAN CENTRAL BANK

EUROSYSTEM

OPINION OF THE EUROPEAN CENTRAL BANK

of 7 December 2011

on the revised amendments to Lietuvos bankas' profit distribution rules

(CON/2011/99)

Introduction and legal basis

On 30 November 2011, the European Central Bank (ECB) received a request from Lietuvos bankas for an opinion on a revised draft law amending and supplementing Article 23 of the Law on Lietuvos bankas as regards the rules on the distribution of Lietuvos bankas' profit (hereinafter the 'revised 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/EC of 29 June 1998 on the consultation of the European Central Bank by national authorities regarding draft legislative provisions[1], as the draft law relates to Lietuvos bankas. 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 revised draft law

1.1 Pursuant to Article 23(3) of the Law on Lietuvos bankas, the profit for a financial year is allocated in the following order:

(a) first, to cover losses carried forward from previous financial years;

(b) second, 70 % is distributed to the State budget, after deducting losses carried forward from the previous financial years;

(c) third, any remaining profit is allocated equally between authorised and reserve capital, until the authorised capital reaches LTL 200 million;

(d) fourth, any residual profit is allocated to reserve capital.

1.2 The revised draft law establishes a new framework for the distribution of Lietuvos bankas' profits.

1.2.1 It provides for improved arrangements relating to the sequence in which the net distributable profit will be allocated. First, the net distributable profit will cover uncovered losses and will be allocated to authorised capital up to a determined amount. Second, it will be used to maintain an adequate reserve capital level; the Board of Lietuvos bankas will establish the adequate reserve capital level independently, based on its assessment of potential risks faced by Lietuvos bankas. The reserve capital may not be less than five times the amount of the authorised capital. Third, any excess will

1 OJ L 189, 3.7.1998, p. 42.

be contributed to the State budget; this contribution may not exceed the amount corresponding to 70 % of the calculated average of Lietuvos bankas' profit (loss) of the last three financial years.

1.2.2 Furthermore, the revised draft law provides for the possibility to carry forward the part of the profit, which remains after the allocation of the net distributable profit according to the established sequence, and by doing so to create retained earnings. The net distributable profit for a given financial year therefore consists in the profit for the financial year and any undistributed profit carried over from the previous financial years. Similarly, the revised draft law provides that the loss for a given financial year and any undistributed profit carried over from the previous financial years will be attributed to the net distributable loss and that, furthermore, the net distributable loss will be covered by Lietuvos bankas' reserve capital, and where this is insufficient, by the distributable profit of the succeeding financial years.

1.3 The revised draft law also sets out the conditions under which the part of Lietuvos bankas' profit contribution to the State budget for the financial year 2011, which is to be calculated according to the rules currently in force, may be used to compensate Lietuvos bankas at market value for the transfer of some assets of Lietuvos bankas to the State authorities.

2. General observations

2.1 On 10 November 2011, the ECB adopted Opinion CON/2011/91 on the amendments to Lietuvos bankas' profit distribution rules[2] in response to a request for an opinion on a previous version of the revised draft law (hereinafter the 'draft law'). The draft law amended the reference period for calculating Lietuvos bankas' profit to be distributed to the State budget: instead of basing the calculation on the preceding financial year, as provided for in the Law on Lietuvos bankas, it was to be based on the average profit of the preceding three financial years. Where the calculated amount, based on the average profit of the preceding three years, was to be greater than the profit of the preceding financial year, the remaining part of Lietuvos bankas' distribution was to be paid to the State budget from Lietuvos bankas' reserve capital. In addition, the following were to be deducted before distribution to the State budget: (a) 30 % of the market value of Lietuvos bankas' real property transferred to the State Property Fund during the preceding financial year; and (b) if Lietuvos bankas' reserve capital was lower than five times the authorised capital, an amount equal to this difference.

2.2 In Opinion CON/2011/91 the ECB noted that several aspects of the draft law raised concerns regarding its compatibility with central bank financial independence and with the monetary financing prohibition. The ECB notes that its remarks were taken into account.

2.3 In any event, the proposed revised profit distribution scheme needs to comply with the requirement that any transfer of national central bank (NCB) resources to a Member State, either in the form of a profit distribution scheme or any equivalent form, complies with the limitations imposed in this respect by the Treaty, in particular with the principle of central bank independence pursuant to

2 All ECB opinions are available on the ECB's website at www.ecb.europa.eu.

Article 130 of the Treaty, and with the prohibition on monetary financing laid down in Article 123(1).

3. Specific observations

3.1 *Treatment of losses*

The revised draft law addresses the ECB concerns as regards the treatment of losses[3] and stipulates that any uncovered loss carried forward from previous financial years has to be covered before allocating the net distributable profit[4].

3.2 *Creation of financial provisions*

The ECB welcomes the provision of the revised draft law stipulating that the Board of Lietuvos bankas can take an independent decision to allocate necessary amounts to the reserve capital, taking into account the potential impact of risks faced by Lietuvos bankas[5]; this addresses the ECB's comment that NCBs must be free to independently create financial provisions or buffers to safeguard the real value of their capital and assets[6]. In this context, the ECB reiterates[7] that NCBs need to maintain adequate net equity to be covered against potential risks arising from the nature of their activities.

3.3 *Three-years average rule*

3.3.1 The revised draft law changes the concept of the three-years average rule, which is now considered as a calculation method and a cap for the Lietuvos bankas' profit distribution to the State budget[8]; Lietuvos bankas' net distributable profit includes the last financial year profit plus undistributed profit carried over from the previous financial years. These changes introduced in the revised draft law address the ECB's concerns as regards the compliance with the monetary financing prohibition[9].

3.3.2 The ECB welcomes in particular that the revised draft law leaves unaffected Lietuvos bankas' reserve capital and ensures that the actual contribution to the State budget cannot exceed the amount of the net distributable profit. The ECB understands that should the net distributable profit be insufficient to fully cover the calculated profit contribution according to the revised draft law, i.e. the amount corresponding to 70 % of the calculated average of Lietuvos bankas' profit (loss) of the last three financial years, the part of the calculated profit contribution which cannot be paid to the State in the given financial year cannot result in a claim of the State for the allocation of profit in the future.

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3 Paragraph 3.6 of Opinion CON/2011/91.

4 Proposed Article 23(1) and (2) and Article 23(3)(1) of the revised draft law.

5 Proposed Article 23(3)(3) of the revised draft law.

6 ECB's Convergence Report May 2010, p. 23. Paragraph 3.7.1 of Opinion CON/2011/91.

7 Paragraph 3.7.3 of Opinion CON/2011/91.

8 Proposed Article 23(3)(4) of the revised draft law.

9 Paragraph 4.2 of Opinion CON/2011/91.

3.4 *Transfer of Lietuvos bankas' real property*

3.4.1 The revised draft law amends the compensation rule for the remuneration of transferred property. It addresses the ECB concern that in order to be compatible with the monetary financing prohibition, the transfer to the State of NCB assets, e.g. real property, must be remunerated at the market value of the real property transferred to it and the transfer of the real property to the State should occur at the same time as the remuneration[10]. The ECB understands that if the compensation rule could not be applied due to an insufficient profit contribution by Lietuvos bankas to the State, as provided for in the revised draft law, the transfer of Lietuvos bankas' real property would either not take place or an alternative appropriate means of remuneration would have to be agreed with the State authorities.

3.4.2 The ECB's comment on the unclear legal status of Lietuvos bankas' assets and its consequences remains valid[11], since the revised draft law treats the transfer of some real property of Lietuvos bankas as a one-off measure.

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

Done at Frankfurt am Main, 7 December 2011.

[signed]

The President of the ECB

Mario DRAGHI

10 Paragraphs 4.3.1 and 4.3.2 of Opinion CON/2011/91.

11 Paragraph 4.3.1 of Opinion CON/2011/91.