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EUROPEAN CENTRAL BANK

EUROSYSTEM

OPINION OF THE EUROPEAN CENTRAL BANK

of 20 October 2008

at the request of the Austrian Ministry of Finance

on draft legal measures to ensure the stability of the Austrian financial market

(CON/2008/55)

Introduction and legal basis

On 15 October 2008, the European Central Bank (ECB) received a request from the Austrian Ministry of Finance (hereinafter the 'Ministry') for an opinion on a draft Federal law adopting a Federal Law on the strengthening of the interbank money market and a Federal Law on measures for ensuring the stability of the financial market, as well as amending the Law on the Austrian Investment and Privatisation Agency (the 'OIAG') 2000, the Law on banking, the Law on the stock exchange, the Law on the Financial Market Supervisory Authority and the Law on the Federal budget 2008 (hereinafter the 'draft law'). The Ministry has informed the ECB that the first chamber of the Austrian Parliament will discuss the draft law in a special session on 20 October 2008 and that the second chamber of Parliament will convene several days later, implying that the Ministry is invoking the exemption under Article 3(2) 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], which allows for a reduction in the minimum time limit for consultation of one month in case of extreme urgency.

The ECB's competence to deliver an opinion is based on Article 105(4) of the Treaty establishing the European Community and on the sixth indent of Article 2(1) of Council Decision 98/415/EC, as the draft law relates to 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 draft law is motivated by the current financial market crisis and comprises a number of different legal measures to ensure the stability of the Austrian financial market. In its letter to the ECB, the Ministry stresses that the draft law is in line with the decisions taken at the summit of the euro-area Member States held on 12 October 2008.

1.2 The main purpose of the first part of the draft law is to revive the interbank money market. It therefore envisages that financial institutions, i.e. banks, insurance companies or their respective

1 OJ L 189, 3.7.1998, p. 42.

interest groups established by law, may set up a company that will operate as a 'clearing house', as it is referred to in the explanatory memorandum to the draft law, between financial institutions, i.e. borrow money from financial institutions and lend money against collateral and at a market rate to financial institutions. According to the submission of the Minister to the Council of Ministers of 14 October 2008, which is not repeated in the draft law or the explanatory memorandum, however, the collateral must not qualify as eligible collateral for receiving central bank liquidity. The clearing house has to provide access to all banks as defined in Section 1(1) of the Law on banking and to all Austrian insurance companies on equal terms. The Minister is empowered to provide a state guarantee to the clearing house for its lending and borrowing operations, which would be effective for a limited period only, and to act as guarantor to credit institutions that issue certain securities for refinancing operations. The beneficiaries of the measures have to pay adequate compensation for such guarantees. The measures may not exceed the amount of EUR 85 billion in total. Finally, the Minister has sole discretion to take any of the measures, although he has to report to the main committee of Parliament on a regular basis regarding any measures taken. The draft law on the strengthening of the interbank money market provides that it will expire on 31 December 2009.

1.3 The main purpose of the second part of the draft law is to support financial institutions in distress. The Minister is empowered to act as guarantor for the liabilities of a financial institution or towards a financial institution, to provide loans or own funds to financial institutions, to acquire shares either by way of a capital increase or by contract and to take over the assets of a financial institution. If this proves insufficient, the Minister may also temporarily take over ownership rights by adoption of a decree, thereby making all other ownership rights null and void, while providing for adequate compensation of the previous owners, i.e. nationalisation. The ownership rights of the State may be held by the Austrian Investment and Privatisation Agency. Once the measures prove successful, the re-privatisation of the nationalised companies will begin. The measures under this part of the draft law may not cost more than EUR 15 billion total, unless the measures to support the interbank money market have not been used up to the maximum amount permitted. Again, the Minister of Finance has to report to Parliament on the measures taken under this part of the draft law.

1.4 Regarding the proposed amendments to the Law on banking, the deposit guarantee for natural persons, which is currently EUR 20 000 per account holder and per bank, will become an unlimited guarantee with retroactive effect from 1 October 2008. This applies to all banks that are members of the Austrian deposit guarantee mechanisms, participation in which is mandatory for all banks with a licence from the Financial Market Supervisory Authority (hereinafter the 'FMA'). As a last resort, if a deposit guarantee mechanism is unable to meet this obligation, it has to take out loans or issue debt certificates, which the State can guarantee. The State has – up to a certain amount - recourse to the deposit guarantee mechanism concerned. Moreover, the FMA's powers to require a bank to have additional capital in specific circumstances, where the bank concerned is subject to an

increased risk that is not adequately covered by the generally applicable capital requirements have been strengthened.

1.5 The proposed amendments to the Law on the stock exchange provide a legal basis for the FMA to prohibit short selling of financial instruments.

1.6 Finally, as regards the proposed amendments to the Law on the FMA, the FMA is required to report to the Minster if it becomes aware that it is possible that measures under the draft law on measures for ensuring the stability of the financial market could be necessary.

2. General observations

2.1 The ECB notes that there is an ongoing discussion at both international and European level with a view to coordinating the actions of countries aimed at preserving confidence in and stability of the international financial markets. More specifically, the ECB notes that on 12 October 2008 the Heads of State of the euro area issued a 'Declaration on a concerted European action plan of the euro area countries'[2] (hereinafter the 'Declaration'), in which they confirmed their commitment to act together in a decisive and comprehensive way in order to restore confidence and proper functioning of the financial system, aiming at restoring appropriate and efficient financing conditions for the economy. They agreed on common principles to be followed by the EU and euro area governments, central banks and supervisors to avoid national measures adversely affecting the functioning of the single market and the other Member States. Such coordinated approach includes initiatives aimed at ensuring appropriate liquidity, facilitating the funding of banks through various means, providing additional capital resources to financial institutions and recapitalisation of distressed banks. These principles were also endorsed for all Member States by the European Council on 16 October 2008. Against this background, the ECB highlights that all the initiatives put in place by national governments to restore the confidence in financial markets should be aimed at implementing such common principles, in the spirit of close cooperation with other Member States and EU institutions.

2.2 The draft law was agreed by the Council of Ministers on 14 October 2008, i.e. two days following the summit of euro area Member States. In line with the Declaration, Member States have to act in coordinated manner to avoid significant differences in national implementation having a counter-productive effect, creating distortions in global banking markets. The euro area Heads of State also acknowledged the need to cooperate with the ECB to ensure consistency with the management of liquidity by the Eurosystem and compatibility with the operational framework of the Eurosystem. The ECB appreciates the fact that the Ministry consulted it on the draft law on 15 October 2008, five days before the discussion in the first chamber of Parliament. It understands that the application of an accelerated procedure during the preparation and adoption of the draft law left insufficient time for the normal consultation process. This does not, however, prejudice the duty under Article 105(4) of the Treaty to consult the ECB on national draft legislative provisions

2 See the Declaration of 12 October 2008, available on the website of the French Presidency, www.ue2008.fr.

falling within its advisory fields of competence, and perhaps the ECB could have been consulted on a previous version of the draft law a few days earlier.

3. Specific observations

Eligibility for support

3.1 The ECB notes that both the draft law on the strengthening of the interbank money market and the draft law on measures for ensuring the stability of the financial market refer to support measures to credit institutions and 'domestic insurance undertakings'. the ECB understands that the institutions potentially addressed by these measures comprise all credit institutions licensed in Austria and all insurance companies having their seat in Austria and being licensed by the Austrian FMA as well. Thereby any distortion in the level playing field as regards the treatment of domestic financial institutions and subsidiaries of foreign institutions should be avoided. The ECB draws the Ministry's attention to the recently adopted Commission guidance on compliance by financial sector support schemes with EU State aid rules[3], which includes in the specific context of provision of State guarantees detailed rules on setting the eligibility criteria for the beneficiary institutions[4].

3.2 Moreover, the ECB would draw attention to the conclusions adopted by the Declaration which highlighted some common principles to guide the action of euro area Member States when providing for recapitalisation of relevant financial institutions, in particular stressing the need to ensure that financial institutions to which Member States make available additional capital resources should be obliged to accept additional restrictions, notably to preclude possible abuse of such arrangements at the expense of non-beneficiaries. The ECB would therefore suggest that the draft law should include specific terms in accordance with the abovementioned principles[5].

Relationship with the central bank

3.3 The ECB understands that the Oesterreichische Nationalbank (OeNB) will not be among the possible shareholders of the 'clearing house' to be established under the draft law on the strengthening of the interbank money market. In line with its previous opinions[6], the ECB considers that, with a view to ensuring the compatibility of the envisaged structure with the financial independence of the European System of Central Banks and the monetary financing prohibition laid down in Article 101 of the Treaty, the OeNB, not being involved in the operation

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3 See 'Communication from the Commission – The application of State aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis' of 13 October 2008, available on the Commission's website, www.ec.europa.eu.

4 See paragraph 18 of the Commission's guidance, specifying that 'The eligibility criteria of financial institutions … must be objective, taking due account of their role in the relevant banking system and the overall economy, and non-discriminatory so as to avoid undue distortive effects on neighbouring markets and the internal market as a whole. In application of the principle of non discrimination on the grounds of nationality, all institutions incorporated in the Member State concerned, including subsidiaries, and with significant activities in that Member State should be covered by the scheme'.

5 On 20 October 2008 the Austrian authorities informed the ECB that it will adjust the draft legislation in order to include this point.

6 See paragraph 5 of ECB Opinion CON/2003/27 of 2 December 2003 at the request of the Austrian Federal Ministry of Finance on a draft Federal law on the National Foundation for Research, Technology and Development.

of the 'clearing house', should be under no obligation to contribute to its finances, either under the draft law or otherwise. The OeNB has confirmed that no OeNB contribution is envisaged or under discussion.

Relationship of the proposals under the draft law to the single monetary policy of the euro area

3.4 The ECB notes that, in line with the Declaration, Member States have to act in a coordinated manner to avoid significant differences in national implementation having a counter-productive effect, creating distortions in global banking markets. The euro area Heads of State also acknowledged the need to work in cooperation with the ECB to ensure consistency with the management of liquidity by the Eurosystem and compatibility with the operational framework of the Eurosystem. The ECB therefore notes that uncoordinated decisions among Member States should be avoided as they may involve a fragmentation of the euro area money market. The Declaration states that the euro area Governments would make available a Government guarantee of new medium-term (up to 5 years) bank senior debt issuance. Against this background, the ECB has a number of observations to make in relation to the draft law.

3.5 Regarding the draft law on measures for ensuring the stability of the financial market, the ECB understands that the Minister of Finance is empowered to act as guarantor for liabilities of a financial institution without limitation in time. Although such measures should have a positive impact to restore confidence in the Austrian banking system, it should also be noted that an open-ended scheme of this nature does not seem to be in line with the Declaration, which pointed to the temporary nature of such schemes. Moreover, it is the ECB's view that the extension of the guarantee to cover all interbank deposits should be avoided. Otherwise there could be a substantial distortion in the various national segments of the euro area money market due to a potential increase in short-term debt issuance activity across Member States, which would impair the implementation of the single monetary policy, which is an exclusive competence of the Eurosystem under Article 105(2) of the Treaty. It also appears crucial to ensure the harmonisation of the price determination of such guarantee within the euro area and the EU, where a level-playing-field is essential. The ECB should be involved in such coordination, and the ECB would welcome that this is explicitly provided for in any subsequent legislation.

3.6 Regarding the draft amendments to the Law on banking, while recognising that the extension of the deposit guarantee for natural persons from EUR 20 000 to an unlimited amount should improve consumer confidence in Austrian financial institutions, the ECB would also remind the Ministry of the need for coordinated measures in this matter, as stated in the Declaration.

4. Information obligations of the FMA

The ECB understands that under the draft amendments to the Law on the FMA, the FMA must report to the Minister if it becomes aware of the possibility that measures under the Law on measures for ensuring

the stability of the financial market could become necessary. As emphasised in previous ECB opinions[7], central bank access to prudential information, and cooperation between financial supervisory authorities and central banks are essential for the conduct of macro-prudential monitoring, the oversight of payment systems and the safeguarding of other market infrastructures, which are in turn essential for the smooth conduct of monetary policy. In particular, from a financial stability perspective, a central bank would inevitably need to be involved in the event of any crisis in financial markets. Even though it is understood that the Austrian system of banking supervision and the safeguarding of financial stability requires close cooperation and information exchange between the FMA and the OeNB, with the OeNB being in charge of all analyses and on-site inspections in the banking area and entrusted with an explicit financial stability monitoring responsibility. However, the draft law could further underline this interaction andprovide for a similar reporting obligation to the OeNB.

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

Done at Frankfurt am Main, 20 October 2008.

[signed]

The President of the ECB

Jean-Claude TRICHET

7 See, e.g. paragraph 2.4 of ECB Opinion CON/2007/33 of 5 November 2007 on the reform of financial supervision in Austria (title shortened).