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EUROPEAN CENTRAL BANK

OPINION OF THE EUROPEAN CENTRAL BANK

of 25 April 2006

on the Dutch draft law concerning financial sector supervision

(CON/2006/20)

Introduction: background and legal basis

On 6 May 2004 the European Central Bank (ECB) received a request from the Dutch Ministry of Finance for an opinion on the first part of the *Voorstel Van Wet op het financieel toezicht* (draft law on financial sector supervision) (hereinafter the 'draft law'), which contained general provisions of an institutional nature.

On 7 June 2004 the ECB issued an opinion on the first part of the draft law[1] pointing out, *inter alia*, that 'The ECB looks forward to being able to supplement this opinion when it is consulted on the other parts.'

On 1 September 2004 the ECB received part two of the draft law for information purposes only. On 30 September 2004 the President of the ECB sent a letter to the Dutch Minister for Finance requesting that the ECB be consulted on part two of the draft law. The Dutch Minister for Finance clarified in a letter of 5 November 2004 that, in his opinion, it is not necessary to consult the ECB on the parts of the draft law which concern prudential supervision, as well as those concerning the conduct of business by financial institutions. The Minister did undertake to consult the ECB in the future on the part of the draft law which concerns the infrastructure of the financial markets. However, the ECB understands that this part is still under preparation.

The ECB's competence to deliver an opinion on part two of the draft law is based on Article 105(4) of the Treaty establishing the European Community 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[2], as the draft law relates to a national central bank (NCB), namely De Nederlandsche Bank (DNB), payment and settlement systems and rules applicable to financial institutions in so far as they materially influence the stability of financial institutions and markets.

In view of the above, and furthermore considering that the ECB has several comments with respect to the current draft law, the ECB has decided to submit this own-initiative opinion.

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1 ECB Opinion CON/2004/21 of 7 June 2004 at the request of the Ministry of Finance of the Netherlands on a draft Financial Sector Supervision Act.

2 OJ L 189, 3.7.1998, p. 42.

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 establish a legal framework for the introduction of a functional model for supervision.

1.2 The draft law is divided into six parts. Part 'General Provisions'; Part 'Market Access financial companies'; Part 'Prudential Supervision on financial companies'; Part 'Market Conduct Supervision on financial companies'; Part 'Market Conduct Supervision on financial markets'; Part 'Infrastructure financial markets'. The first five parts of the draft law on Financial Sector Supervision are scheduled to enter into force from 1 January 2007. The sixth part 'Infrastructure financial markets' is currently under preparation and is intended that it should enter into force on 1 January 2008. The necessary transitional provisions and amendments of other laws will be covered in a separate law implementing the draft law which will be submitted to Parliament in due course and will enter into force on 1 January 2007.

2. Comments on the proposed institutional framework

2.1 The draft law introduces a new functional model on the basis of which DNB will be responsible for prudential supervision of the entire financial sector, whereas the Authority for Financial Markets (AFM) will be responsible for market conduct supervision and will focus on ensuring orderly and transparent financial market processes, clear relationships between market entities and that consumers are treated with due care.

2.2 As stated above, the ECB has already provided its opinion on an earlier version of part one of the draft law. The ECB is aware that the draft law has since been modified on several occasions through five memorandums of amendments. Currently the sixth memorandum of amendments is under preparation.

2.3 In its earlier opinion, the ECB commented on several aspects of the draft law's institutional part and noted that some draft provisions did not distinguish between DNB's tasks relating to its participation in the European System of Central Banks (ESCB) and its non-ESCB related tasks. As a consequence, some of those provisions were deemed incompatible with the legal framework established by the Treaty concerning NCBs as members of the ESCB. These incompatibilities concerned parts of the draft law dealing with the accountability of DNB and the AFM to the Minister for Finance, the budgetary approval process, the amendment of DNB's statutes and the exchange of information between the Dutch supervisors and the ECB and other central banks. These comments have not been taken into account in the latest version of the draft law.

2.4 As already mentioned in the earlier ECB opinion[3], the draft law allows the Dutch supervisory authorities to exchange confidential information with the ECB, a foreign central bank or other foreign authorities with similar tasks, but only to the extent that this is conducive to fulfilling their 'monetary task' (Article 1:77(1)(a) of the draft law). This limitation to the 'monetary task' is deemed too restrictive as this would not cover the entire set of tasks the Treaty and the Statute of the European System of Central Banks and of the European Central Bank conferred upon the ESCB. Indeed, in addition to its basic task which consists of defining and implementing the single monetary policy, the ESCB's basic tasks also include promoting the smooth operation of payment systems[4] and contributing to the smooth conduct of policies pursued by the competent authorities relating to the prudential supervision of credit institutions and the stability of the financial system[5]. With regard to the latter function, it is noted that the transmission of supervisory information and data, primarily in aggregated form, is necessary for the effectiveness of the central bank's financial stability monitoring and assessment of the conditions of the financial system as a whole as well as of the efficacy of its response when a financial crisis occurs.

2.5 In order to undertake these and other tasks, the ECB, assisted by the NCBs, collect the necessary statistical information either from the competent national authorities or directly from economic agents[6], while limiting the overall reporting burden. Moreover, the ECB anticipates that an exchange of such information can serve to further enhance the statistics needed by the ESCB.

2.6 Therefore, the ECB emphasises the need to insert an explicit provision in the draft law stipulating that the exchange of information under Article 1:77(1)(a) applies to all ESCB-related tasks and not merely to the monetary policy task[7], as well as introducing the other changes suggested in ECB Opinion CON/2004/21.

3. Payment and securities settlement systems

3.1 As has already been noted, the division of tasks under the draft law implies that the AFM will supervise market conduct of financial institutions, including clearing institutions. Market conduct supervision is defined in the draft law as 'promoting orderly and transparent financial market processes' (Article 1:8).

3.2 Payment systems fall under the draft law's definition of financial institutions and might also fall under the scope of the AFM's market conduct supervision. Given the similarity between the concept of market conduct supervision, as defined in the draft law, and the Eurosystem's statutory task of 'promoting the smooth operation of payment systems' (which it performs through its oversight function), considering Article 25.1 of the ESCB Statute on the ECB role in the area of

3 In paragraph 9 of ECB Opinion CON/2004/21, the ECB made a similar recommendation.

4 Article 3.1, fourth indent of the Statute.

5 Article 3.3 of the Statute.

6 See Article 5.1 of the Statute.

7 In paragraph 9 of ECB Opinion CON/2004/21, the ECB made a similar recommendation.

financial stability and knowing that payment systems and securities settlement systems (SSSs) are interlinked, there may be a conflict between the responsibilities of the ESCB and the responsibilities of the AFM, as may be provided for in the future sixth Part 'Infrastructure financial markets' of the draft law.

3.3 At the Community level, the general legal basis for the oversight of payment systems is provided by the Treaty and the Statute[8] with more detailed policies introduced by the Eurosystem's common oversight policy, as defined by the Governing Council.

3.4 In the interest of making responsibilities clear, the ECB recommends that the oversight of payment systems, including market conduct, be explicitly assigned to DNB in the future sixth Part of the draft law, which would be consistent with the participation of DNB in the ESCB.

3.5 As noted in previous ECB opinions, payment systems and SSSs are interlinked, particularly in view of the use of the 'delivery versus payment' mechanism, under which settlements of securities and transfers of funds take place simultaneously. There is therefore a strong argument in favour of the model used in some Member States of integrating the oversight of payment systems and SSSs, and for the NCB to perform this function. Settlement of both legs of such transactions should be subject to similar safeguards in order to avoid asymmetries, possibly with systemic implications.

3.6 In order to safeguard the effectiveness of monetary policy and the overall stability of the financial system, the NCBs' oversight responsibilities mean that they must ensure that SSSs are sufficiently protected against systemic disruptions. The framework for the NCBs' conduct of this function, although informal, has been effective and successful. A growing number of NCBs see a benefit in formalising their oversight role. The majority of NCBs carry out this function on the basis of their statutes without any explicit detailed legal provisions. The ECB therefore also recommends clarifying DNB's role in the oversight of SSSs.

4. Final institution

4.1 Another important issue is that non-public banks (or opting-in banks, i.e. banks that do not longer fall within the scope of the new definition of 'bank' in the draft law, but have opted in for a voluntary bank permit on the basis of Article 2:5 of the draft law) also need to qualify as 'final institutions' within the meaning of Article 212a of the Dutch Law on bankruptcies and Article 2(b) of the Settlement Finality Directive[9] in order to be able to participate in payment systems and SSSs.

4.2 The ECB understands that the definition of final institution in Article 212a of the Law on bankruptcies will only be aligned with the definition of a bank in Article 1:1 of the draft law once the law implementing the draft law – which is now under preparation – is adopted. Furthermore, the ECB would like to observe that, from the point of view of a level playing field, it is considered

8 Article 105(2) of the Treaty and Articles 3.1 and 22 of the Statute.

9 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).

desirable that opting-in banks that hold a voluntary bank permit on the basis of Article 2:5 of the draft law, are brought into line with banks that hold a 'conventional' bank permit. The ECB would also welcome being consulted on this issue.

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

Done at Frankfurt am Main, 25 April 2006.

[signed]

The President of the ECB

Jean-Claude TRICHET