EUROPEAN CENTRAL BANK

EUROSYSTEM

OPINION OF THE EUROPEAN CENTRAL BANK

of 26 October 2006

at the request of the Cypriot Ministry of Finance on a draft provision amending the draft law amending the Central Bank of Cyprus Laws of 2002 and 2003

(CON/2006/50)

Introduction and legal basis

On 13 October 2006 the European Central Bank (ECB) received a request from the Cypriot Ministry of Finance for an opinion on a draft provision (hereinafter the 'draft provision') amending the draft law amending the Central Bank of Cyprus Laws of 2002 and 2003 (hereinafter the 'CBC Law') in respect of the appointment of independent external auditors for the Central Bank of Cyprus (CBC).

The ECB's competence to deliver an opinion is based on Article 105(4) of the Treaty establishing the European Community 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 a national central bank. 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 Subject matter and background

1.1 The subject matter of this opinion is a draft provision amending Section 60 of the CBC Law on the audit of the annual financial statements of the CBC in line with Article 27.1 of the Statute of the European System of Central Banks and of the European Central Bank[2]. The ECB has been consulted in the past on two earlier versions of draft provisions amending Section 60 of the CBC Law and refers to its previous opinions on these provisions[3].

1 OJ L 189, 3.7.1998, p. 42.

2 The inconsistencies of Section 60 of the CBC Law with the Statute are identified on p. 222 of the 2004 ECB Convergence Report.

3 ECB Opinion CON/2006/4 of 27 January 2006 at the request of the Central Bank of Cyprus on a draft law amending the Central Bank of Cyprus Laws of 2002 and 2003; ECB Opinion CON/2006/33 of 28 June 2006 at the request of the Cypriot Ministry of Finance on a draft provision amending the draft law amending the Central Bank of Cyprus Laws of 2002 and 2003.

1.2 In Opinion CON/2006/4, the ECB concluded that, notwithstanding the Auditor General's independence[4] as enshrined in the Cypriot Constitution[5], the Audit Office (of which the Auditor General is the Head) is not an external auditor within the meaning of Article 27.1 of the Statute and cannot, for that reason, be appointed as the CBC's independent external auditor[6]. Reaffirming its view on this matter[7], the ECB also concluded that the appointment of an independent external auditor, in accordance with Article 27.1 of the Statute, to audit the CBC's annual financial statements once Cyprus has adopted the single currency, 'will not prevent the Audit Office from continuing to perform a control function, provided that its auditing activities: (i) do not interfere with the review of European System of Central Banks (ESCB) related tasks of the CBC to be undertaken by the CBC's independent external auditors to be approved by the Council of the European Union in accordance with Article 27 of the Statute; and (ii) do not jeopardise the CBC's independence'[8].

1.3 In Opinion CON/2006/33, the ECB reiterated the conclusions reached in Opinion CON/2006/4, also drawing attention to its May 2006 Convergence Report, according to which the powers of auditors, other than those appointed under Article 27.1 of the Statute, are compatible with central bank independence only when the necessary safeguards are in place[9].

2 Assessment of the draft provision

2.1 Subsection 1(a) of the draft provision now under consideration provides that the financial statements of the CBC shall be audited in accordance with Article 27 of the Statute and that the CBC shall provide the auditors appointed in accordance with Article 27 with full information, books and other records that are necessary for the exercise of their duties. The ECB welcomes this subsection.

2.2 Subsection 1(b) of the draft provision provides that the Auditor General may carry out financial and management audits of those activities of the CBC that are not related to its ESCB tasks and competences, provided that his reports and audit activities do not impinge on the CBC's

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4 The personal independence of the Auditor General is guaranteed under Article 115.3 of the Cypriot Constitution, according to which he or she is not to retire or to be removed from office except on the same grounds and in the same manner as a judge of the Supreme Court.

5 Under Article 116(1) of the Cypriot Constitution, 'The Auditor General assisted by the Deputy Auditor-General shall, on behalf of the Republic, control all disbursements and receipts and audit and inspect all accounts of moneys and other assets administered, and of liabilities incurred, by or under the authority of the Republic and for this purpose he shall have the right of access to all books, records and returns relating to such accounts and to places where such assets are kept'.

6 Paragraphs 2.1 and 2.2 of Opinion CON/2006/4.

7 As expressed in paragraphs 5 to 7 of ECB Opinion CON/2002/22 of 2 September 2002 at the request of the Swedish Ministry of Finance on a draft legislative proposal establishing the National Audit, including proposed amendments to the Sveriges Riksbank Act (1988:1385).

8 Paragraph 2.3 of Opinion CON/2006/4.

9 See, generally, ECB Convergence Report, May 2006, page 66, available at: http://www.ecb.int/pub/pdf/conrep/cr2006en.pdf. For specific examples of such safeguards, see page 74 of the ECB Convergence Report of May 2006 (Appointment of Independent External Auditors), *ibid.*

independence. The ECB also welcomes subsection 1(b) and the draft provision's definition of management audit, which preclude any interference with the audit to be carried out by the CBC's independent external auditors.

2.3 The ECB thus considers the draft provision to be consistent with its earlier opinions in this matter and recommends (as an alternative to the initial wording on which the ECB was consulted by the CBC[10]) its incorporation in the draft law amending the CBC Law as the appropriate means of adapting, in this particular case, national audit arrangements to the requirements of Article 27 of the Statute and, in particular, to the principle of central bank independence.

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

Done at Frankfurt am Main, 26 October 2006.

[signed]

The President of the ECB

Jean-Claude TRICHET

10 Opinion CON/2006/4.