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EUROPEAN CENTRAL BANK

OPINION OF THE EUROPEAN CENTRAL BANK

of 16 February 2006

at the request of the Finnish Ministry of Justice
on Committee report 2005:2 consisting of a draft Government proposal for a law on emergency powers act and for laws amending certain related Laws

(CON/2006/6)

Background

1. On 5 January 2006 the European Central Bank (ECB) received a request from the Finnish Ministry of Justice for an opinion on a Committee Report (2005:2) 'Proposal for a new law on emergency powers, Report of the Emergency Powers Act Committee'[1] containing a draft Government proposal for a law on emergency powers and other laws amending certain related Laws (hereinafter 'draft law') and their statement of reasons.

2. The ECB's competence to deliver an opinion is based on the first, second, 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 legislative proposal contains provisions concerning rules on currency matters, means of payment, national central banks, payment and settlement systems and 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.

Description of the draft law

3. According to the draft law's statement of reasons its main objective is to bring the Emergency Powers Law (hereinafter 'Law')[3] into conformity with the Finnish Constitution and to modernise the authorities' current emergency powers. In particular, a delegation of regulatory powers in emergency conditions as provided for in the Law is not compatible with the Constitution, as according to the latter, emergency powers affecting basic rights may not be delegated in a loose manner. Instead, a rather detailed legal framework to be applied in emergency situations has to be

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1 Komiteanmietintö 2005:2, Ehdotus uudeksi valmiuslaiksi, Valmiuslakitoimikunnan mietintö, Oikeusministeriö Helsinki 2005.

2 OJ L 189, 3.7.1998, p. 42.

3 Valmiuslaki, 1080/1991 of 22 July 1991.

set out in law. It would also be unconstitutional for the Government to simply assume exceptional powers on an ad hoc basis.

4. The draft law defines a limited number of emergency situations in which a Governmental decree can be issued to provide Finnish authorities with certain emergency powers, for a limited period. These emergency situations are:

- an armed attack on Finland and its immediate aftermath ('armed attack'),
- a substantial armed threat against Finland, the effects of which can only be repelled by immediately introducing the powers under the Emergency Powers Law ('armed threat'),
- a particularly serious event or threat impacting on the population's subsistence or the foundations of the national economy that poses a material hazard to society's functioning ('economic crisis'), and
- a particularly serious major accident and its immediate aftermath as well as widespread dangerous communicable disease having effects comparable to those of a serious major accident ('major accident or communicable disease').

5. In these situations, once the Government has established, in consultation with Finland's President, the existence of emergency conditions, it can adopt a decree activating certain emergency powers. Powers are only authorised that are (i) necessary and proportionate to achieve the purpose of protecting the population and its subsistence and the national economy, maintaining legal order and human rights as well as safeguarding Finland's territorial integrity and independence in emergency conditions; and (ii) proportionate to the goal sought through their use. In addition, the draft law provides that the emergency powers can only be used in situations that cannot be controlled through the authorities' regular powers. The Government Decree must thereafter be submitted to the Finnish Parliament that will decide whether to confirm the Decree, which will then remain in force for the period it foresees, or whether to partially or fully repeal it. The Decree will lapse unless submitted to the Parliament within one week of its issue.

6. The draft law provides for emergency powers in various sectors, such as communications, social security, energy supply and financial markets. In accordance with the ECB's consultative competence, the present opinion only deals with emergency powers concerning the financial markets: These are dealt with in Part II (Sections 13 to 26) of the draft law. In particular:

- Section 14 of the draft law provides that in order to safeguard the nation's exchange reserves and the State's liquidity in the conditions of 'armed attack' and 'armed threat', responsibility is vested in Suomen Pankki for practical measures required for exchange controls, such as granting permission to take actions impacting the currency reserve and deciding on the duty of repatriation of currency, securities and receivables.
- Section 16 of the draft law provides that in order to secure the population's livelihood, the State's liquidity or essential economic activity in the conditions of 'armed attack', 'armed

threat' and 'economic crisis', the Government Decree could e.g. (i) provide for interest rates to be observed by credit institutions, financial institutions and other similar bodies on various types of financial claims so that these would not exceed or fall below the maximum and minimum limits set by the Government Decree; (ii) regulate the issue of loans and restrict withdrawals of deposits and other repayable assets; and (iii) provide for a certain proportion of investments by credit and other institutions to be made in debt instruments issued by the State. Suomen Pankki, the Financial Supervision Authority and the Insurance Supervisory Authority willensure enforcement of these rules in their respective fields of operations.

- Section 18 of the draft law provides that in all the foreseen emergency conditions securities markets could be subject to restriction. The Financial Supervision Authority will be responsible for enforcing these rules regarding securities markets. Moreover, Section 19 provides that in the same cases payment transactions could be restricted. Suomen Pankki and the Financial Supervision Authority will] enforce these rules.

- Section 20 of the draft law provides that in all the foreseen emergency conditions, solvency requirements lower than the those provided for under the law will apply to credit institutions, investment firms and insurance and pension institutions, if meeting the statutory solvency requirement in emergency conditions may materially compromise their operations. In addition, according to Section 22 of the draft law, the Government Decree may provide for exceptions to the ordinary legal requirements concerning bankruptcy, liquidation, accounting and financial statements applicable to credit and financial institutions, management companies, investment firms, the stock exchange, the central securities depository, option corporations, insurance and pension institutions. The Financial Supervision Authority and the Insurance Supervisory Authority will be responsible for enforcement of these rules.

- The draft law also amends Section 13 of the Law on the book-entry system listing the tasks of central securities depository, Arvopaperikeskus ('APK'), which holds all book-entry Finnish securities, providing that APK maintains the central data systems required for the book-entry system with the hardware and software located in Finland.

7. According to Section 26 of the draft law, the Government Decree on the application of certain emergency powers concerning the duties assigned by the Treaty to the European System of Central Banks (ESCB) may only be adopted if the ECB, or Suomen Pankki acting as part of the ESCB, are incapacitated in emergency conditions. Prior to issuing the Decree on emergency powers according to Sections 14, 16 and 19 of the draft law, the Government must request an opinion from the ECB in expedited proceedings.

ECB Opinion

8. By adopting the euro, Finland has transferred irreversibly to the Community monetary policy and other powers enumerated in the Treaty and the Statute with regard to ESCB tasks. In these fields (setting reference rates, injecting or withdrawing liquidity in the market, ensuring efficient and

sound clearing and payment systems, managing foreign reserves, issuing banknotes, contributing to the stability of the financial system) certain policy-making and legislative powers belong exclusively, under Article 8 of the Statute, to the decision-making bodies of the ECB. According to Article 10 of the Treaty, the Member States have a duty to facilitate the achievement of Community's tasks and must abstain from any measure which could jeopardise the attainment of the objectives of the Treaty.

9. Already in 2002, the Finnish authorites consulted the ECB on a draft amendment to the current Law. In its Opinion (CON/2002/27) of 31 October 2002, the ECB concluded that some of the powers granted to the Finnish authorities conflicted with the Treaty as they belonged to Community competencies in the field of monetary union and of the single market for capital. In its opinion, the ECB criticised among others (i) the definition of emergency situations; in particular the emergency conditions enumerated in the Law were broader than those referred to in Article 297 of the Treaty; and (ii) the lack of clarity of the provision on when the Law would apply. In this latter respect, the opinion noted that emergency powers should only apply if both Suomen Pankki and the ECB are deprived by emergency events of their capacity to perform their tasks and that both the ECB and Suomen Pankki should be referred to as authorities that need to be unable to take measures, before the Law can be activated. A different interpretation following which the Law could be applied with regard to the tasks of the ESCB, even if the ECB and Suomen Pankki retained their operational and decision-making capabilities intact, would neither be justifiable under nor consistent with Community law. Finally, the opinion noted that (iii) the ECB should be consulted before the adoption of any draft decree in its field of competence.

10. Having assessed the draft law, the ECB notes that it aims at taking into account the abovementioned concerns raised by the ECB in its previous opinion. The ECB welcomes the fact that Section 26 of the draft law requires the Government to request an opinion from the ECB in expedited proceedings prior to issuing the Decree.

11. Section 26 also provides that the Government Decree on the introduction of the powers provided for in Sections 14, 16 and 19 concerning duties belonging to the ESCB under the Treaty and the Statute may only be issued if the ECB, or Suomen Pankki acting as part of the ESCB, are incapacitated by the emergency conditions. It is clear from the overall assessment set out in the ECB opinion of 2002 that both the ECB (including through the Eurosystem emergency measures) and Suomen Pankki must be incapacitated to take action before national emergency powers affecting the ESCB tasks can be activated. The ECB stresses accordingly that the word 'or' in Section 26 of the draft law should be replaced by the word 'and', in order to avoid the misconception that the Government Decree on emergency powers could be adopted in a situation where Suomen Pankki is incapacitated as part of the Eurosystem e.g. perform its Eurosystem-related duties but the ECB is still functioning. Whereas the draft law's statement of reasons use both expressions 'or' and 'and', they generally provide the impression that the purpose of Section 26 is indeed to ensure the primacy of Community action meaning that also the ECB should

be incapacitated to act before the decree on emergency powers may be adopted. Amending the wording of the Law itself would clarify this issue. In general, the ECB considers Section 26, once clarified, as an important improvement to the current Law.

12. However, there are still some provisions that would need to be brought into line with Community law, as specified in more detail below.

13. According to settled case-law, Member States may derogate from obligations imposed by the Treaty under the conditions laid down in the Treaty itself[4]. Article 297 of the Treaty is one of the few articles allowing derogation from the rules of the Treaty under certain conditions and according to certain procedures[5]. This Article deals with exceptional cases which are clearly defined and are to be interpreted in a restrictive manner[6]; it can therefore be understood only as a 'hedge clause' and not as an expression of any residual Member State competence[7]. The Court of Justice has held in cases where Member States acted due to urgency on matters of exclusive Community competence[8] that 'Member States may act only as trustees of the common interest' and that 'Member States cannot bring into force any interim measure which may be required by the situation except as part of a process of collaboration with the'[Community].

14. Unfortunately, the emergency conditions set out in Section 3 of the draft law still do not correspond with those listed in Article 297 of the Treaty. The emergency conditions 'economic crisis' and 'major accident or communicable disease' in the draft law are clearly not included in the exhaustive list of emergency conditions, although the ECB notes that the emergency condition 'economic crisis', required to trigger the application of the draft law, must concern a particularly serious economic crisis caused by a serious exogenous event or threat, and not merely an economic crisis involving the domestic market. The ECB strongly recommends amending the draft law so that the powers that fall within the ESCB's exclusive competence may not be granted to national authorities in the absence of an emergency condition included in Article 297 of the Treaty.

15. The wording in Article 14 of the draft law 'Finnish currency' could be misinterpreted to mean that Finland would re-introduce an own national currency. Based on the statement of reasons for Section 14, especially concerning the exchange rate used when paying the compensation for repatriated 'Finnish currency'[9], it appears however that reference is made to the euro. The ECB considers that the euro, as a single currency, should be referred to as such and that the wording

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4 Joined Cases 6 and 11/69, *Commission* v *French Republic*, ECR [1969] 523; Case C-285/98, *Tanja Kreil* v *Bundesrepublik Deutschland* [2000] ECR I-69, paragraph 16.

5 Article 297 of the Treaty provides for a consultation obligation for the Member States for the exceptional cases where a Member State may be called upon to take measures to protect its national interests. The proceedings set out in Article 298 of the Treaty aim at guaranteeing that Article 297 is used in a restrictive way.

6 Case C-13/68 *Salgoil* v *Italian Ministry of Foreign Trade* [1968] ECR 453.

7 Gilsdorfer/Brandtner, 'Vorbem. zu den Artikeln 296 bis 298 EG', No 3-5, Bardenhewer-Rating/Grill/Jakob/Woelker, *EG- und EU-Kommentar*, 6th ed. (2004), p. 1534.

8 See e.g., Case 804/79 *Commission* v *UK*, paragraph 30.

9 'The exchange rate for the relevant currency applied by Suomen Pankki when exchanging the relevant currency in euro at the time of transfer would be observed'.

'Finnish currency' should be replaced either by 'euro' or by 'currency being legal tender in Finland'. The ECB also recommends replacing 'the current exchange rate of Suomen Pankki shall be observed' by the wording 'the relevant current exchange rate of euro shall be observed thereby' or by the wording 'the relevant ECB reference rates shall be observed'.

16. Moreover, the ECB considers that the consultation obligation set out in Section 26 of the draft law should cover also Section 18(3) and Section 20 of the draft law. Article 18(3) allows for restrictions on operations of a central securities depository holding securities in book-entry form which is licensed in Finland and may affect the settlement of Finnish collateral held by the Eurosystem and thus the execution of monetary policy operations or the provision of intraday credit for payment system purposes. The provision by Government Decree of a generalised exception to ordinary solvency requirements for credit institutions provided for in Section 20 of the draft law would concern Eurosystem's counterparties and thus imply a derogation from ordinary Eurosystem requirements and possibly cause spill over effects on the financial stability of other Eurosystem members.

17. The draft law introduces a requirement for any central securities depository licensed in Finland to maintain in Finland the book-entry information technology system required for its functioning. The ECB shares the authorities' concerns for the continuity of post-trading facilities located in the euro area. The ECB is of the view, in particular, that it is essential to subject the SSSs used by the Eurosystem for collateral settlement and custody to the law of a euro area country in order to ensure that the perfection and realisation of eligible collateral used for Eurosystem operations are subject to euro area law. In addition, a provision requiring the location of such infrastructure in a specific country and not generally in the euro area warrants careful consideration. Since the treatment of collateral is a collective Eurosystem subject, of which Suomen Pankki is an integral part, it is logical for the collateral infrastructure to be located anywhere in the euro area, as reflected in the Eurosystem's policy line published in 2001[10].

18. The ECB also proposes adjusting the list of definitions in Section 13(1) of the draft law to clarify that when referring to credit and other institutions as addressees of the restrictions, only institutions resident in Finland are concerned. Concerning Section 13(2) of the draft law providing that 'the Nordic Investment Bank, Nordic Project Export Fund and other international financial or other institutions resident in Finland shall be considered parties resident abroad', the ECB assumes that this treatment reflects the 5th edition of the IMF Balance of Payments Manual.

19. Moreover, as it is possible that the ECB and Suomen Pankki, as part of the ESCB, would only temporarily be unable to take normal measures, the ECB recommends also clarifying in Section 26 of the draft law that the Decree it refers to will be applicable only as long as the said entities are incapable of acting. Concerning the ECB's ability to take action, it is noted for the sake of clarity

10 The Eurosystem's policy line with regard to consolidation in central counterparty clearing.

that there are ESCB emergency and contingency plans, according to which the ECB, in general, will act in emergency situations.

20. Article 26 of the draft law provides that the Government Decree affecting the ESCB competences may only be enacted if the ECB, or Suomen Pankki as part of the ESCB, are incapacitated, expressing the principle of the supremacy of Community action. As the draft law provides for procedures for emergency situations based on the principles and procedures set out in Article 297 of the Treaty, the ECB would welcome an additional reference in the draft law, for the sake of clarity, to the obligation to consult the other Member States set out in Article 297 of the Treaty, according to which the Member States are obliged to consult each other to prevent the functioning of the internal market from being affected by the measures a Member State is allowed to take in extraordinary cases enumerated in it. In particular, if 'exceptions to solvency requirements' for financial institutions (for instance by Section 20) in an 'economic crisis' (a particularly serious crisis caused by a relevant exogenous event or threat, with an impact on the stable operations of financial markets) are allowed to be introduced, coordination with other Member States and EU institutions could involve monitoring of spill over effects on financial stability of other Member States with a view to triggering, if necessary, a coordinated Eurosystem or Europe-wide response.

21. In order to avoid any misunderstandings the ECB recommends clarifying in Section 17 of the draft law[11] that the detailed provisions on index clauses will apply for other than statistical purposes.

22. Since the draft law affects some very core principles of Community law, such as the principle of the free movement of capital, the ECB proposes consulting the Commission of the European Communities, as the guardian of the Treaties, on this draft law.

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

Done at Frankfurt am Main, 16 February 2006.

[signed]

The President of the ECB

Jean-Claude TRICHET

11 Section 17 of the draft law provides among others that 'more detailed provisions on index clauses and other links prohibited in emergency conditions alongside the index clauses or engagements prohibited pursuant to the said Law shall be laid down by Government decree'.