EUROPEAN CENTRAL BANK

OPINION OF THE EUROPEAN CENTRAL BANK

at the request of the Banco de España on a draft Royal Decree on the arrangements for the payment of the Banco de España's profits to the Treasury

(CON/99/16)

1. On 28 September 1999 the European Central Bank (ECB) received a request from the Deputy Governor of the Banco de España to give its opinion on a draft Royal Decree on the arrangements for the payment of the Banco de España's profits to the Treasury (the "Draft"). The Draft was forwarded both in Spanish and English.

2. The Draft is based on the legal authorisation (Second Final Provision of Law 12/1998 of 28 April amending the Act of Autonomy of the Banco de España) to determine, by way of governmental regulation, the regime for the payment of the Banco de España's profits to the Treasury. The said Law of 1998 was subject to consultation with the European Monetary Institute (CON/98/05), and no comments were given to the aspects envisaged by the Draft. The content of the Draft, in summary, consists of laying down the following calendar for payment to the Treasury of profits generated and accounted for by the Banco de España, which does not substantially differ from the practice that existed before the legal reform of 1998:

   – in November each year, 70% of the profits recorded up to the end of September of the same financial year;

   – in February each year, 90% of the profits recorded in the preceding financial year, discounting the instalment paid in November;

   – the remainder, following the formal approval of the accounts for the financial year by the Central Government.

3. The ECB's competence to deliver an opinion is based on Article 105 (4), second indent of the EC Treaty and on Article 2 (1), third indent, of Council Decision (EC) No. 98/415 of 29 June 1998, on the consultation of the European Central Bank by national authorities regarding draft legislative provisions, as the Draft deals with a national central bank. In accordance with Article 17.5 first

sentence of the Rules of Procedure of the European Central Bank, the Governing Council of the ECB has adopted this opinion.

4. The legal possibility for Member States of the European Union to legislate on areas that are not subject to Community provisions or are only partially subject thereto, is extensively recognized in the case law of the Court of Justice, even in areas of exclusive Community competence (joined cases 3,4 & 6/76 *Kramer* [1976] ECR 1279; joined cases 141 to 143/81 *Holdijk & others* [1982] ECR 1299; case C-1/96 *The Queen v MAFF, ex p. Compassion in World Farming Ltd.* [1998] ECR I-1252; etc.). Consequently, there is nothing in theory to prevent the Spanish State from laying down arrangements for allocation of the Banco de España's profits provided that such arrangements are not incompatible with the relevant provisions in Community law or that they do not unduly hinder the achievement of Community objectives. It is relevant to point out that other Member States have similar provisions with regard thereto that have not been deemed to be in conflict with the Community order. It is appropriate here, furthermore, to recall that, since the reform of 1962 (Decree-Law 18/1962 of Nationalization and Reorganization of the Banco de España), the Banco de España is a public entity of the State, and therefore the State has a primary competence to determine the regime for the allocation of the Bank's profits within the perimeters allowed by Community law.

5. The Draft is expressly stated to be provisional in nature, until such time as the ECB adopts decisions on the application of monetary income in the European System of Central Banks (ESCB) under Article 32 of the Statute thereof. Given the primacy of Community law, it would be obvious to state that the application of Article 32 of the Statute of the ECB and the ESCB cannot be conditional on what the provisions of national Law might provide. However, on this point it is necessary to stress that the ECB has exercised Article 32 of its Statute to lay down the arrangements applicable to the monetary income of the ESCB during the transitional period of monetary union, that is to say, for the financial years 1999, 2000 and 2001. These arrangements are laid down in the Decision of 3 November 1998 (ECB/1998/NP12) notified to the national central banks in their capacity as shareholders in the ECB. Consequently, it is suggested that the Draft specifies that the amount of distributable profit is conditioned by the monetary income amounts attributable to the Banco de España after due application of the ESCB's arrangements for monetary income allocation that may be from time to time in force, so as to cover the current situation, and that the Governing Board of the Banco de España is to verify before allowing a pay-out of profits that such payments do not hamper the due application of the ESCB regime adopted under Article 32 of the Statute.

   For the sole purpose of information to the Spanish Treasury, in its capacity as sole final recipient of the distributable profits of the Banco de España, the Decision of 3 November 1998

(ECB/1998/NP12) is annexed hereto; such Decision has neither been subject to official publication nor made public.

6. In this area, the limitations laid down by the Treaty are two-pronged:

(i) The financial independence of the central banks (Article 108 of the Treaty), the safeguard of which would require not leaving to the sole discretion of the political authorities the possibility of requiring advance pay-outs of NCB's profits, and therefore warrants the convenience of pre-established detailed arrangements for such payments; this aspect is sufficiently covered by the Draft, since it regulates in detail the calendar and amount of the advance payments, without affording any ad hoc discretion to the political authorities.

(ii) The prohibition on monetary financing to the public sector (Article 101 of the Treaty), which would require that advance payments of profits to the Treasury be only from profits that are fully realised, accounted for and verified, which in turn would require some kind of formal approval of the profit and loss account for the considered period. Although by setting a ceiling of 70 % of the current profits a prudent criteria is established in this regard, it could theoretically not be sufficient if, for instance, heavy losses at year end would exceed 30 % of the profits realised in the first nine months of the financial year. The Draft would better satisfy this concern by providing for a formal approval by the Governing Council of Banco de España of the profits and loss account which serves as a basis for the calculation of the advance pay outs, and the pay out be conditioned to an assessment by that body that expected economic developments for the final quarter of the year would not give rise to such a risk.

Done at Frankfurt am Main on 28th October 1999.

The Vice-President of the ECB

[signed]

C. Noyer

Annex

EUROPEAN CENTRAL BANK

DECISION OF THE EUROPEAN CENTRAL BANK

of 3 November 1998

ON THE ALLOCATION OF MONETARY INCOME OF THE NATIONAL CENTRAL BANKS OF PARTICIPATING MEMBER STATES AND LOSSES OF THE ECB FOR THE FINANCIAL YEARS 1999 TO 2001

(ECB/1998/NP12)

THE GOVERNING COUNCIL OF THE EUROPEAN CENTRAL BANK,

Having regard to the Statute of the European System of Central Banks and of the European Central Bank (hereinafter referred to as the "Statute") and in particular to Article 32 thereof;

(1) Whereas, according to Article 32.2 of the Statute, the amount of monetary income of each participating national central bank shall be equal to its annual income derived from its assets held against notes in circulation and deposit liabilities to credit institutions; whereas, according to Article 32.3 of the Statute, if the balance sheet structures of participating NCBs after the start of the third stage do not permit the application of the method foreseen in Article 32.2 of the Statute for the allocation of monetary income of participating NCBs, the Governing Council may temporarily adopt an alternative method;

(2) Whereas, according to Article 32.4 of the Statute, the amount of each participating NCB's monetary income shall be reduced by an amount equivalent to any interest paid by that NCB on its deposit liabilities to credit institutions in accordance with Article 19 of the Statute; whereas, according to Article 32.5 of the Statute, the sum of the participating NCBs monetary income shall be allocated to the participating NCBs in proportion to their paid-up shares in the capital of the ECB;

(3) Whereas, according to Article 32.6 and 32.7 of the Statute, it is for the Governing Council of the ECB to arrange for the clearing and settlement at the ECB of the balances arising from the allocation of monetary income and to take all other measures necessary for the application of Article 32 of the Statute;

(4) Whereas Article 10.3 of the Statute stipulates that for any decision taken under Article 32 of the Statute, the votes of the Governing Council of the ECB shall be weighted according to the NCBs' shares in the subscribed capital of the ECB;

(5) Whereas Council Regulation (EC) No. 974/98 of 3 May 1998 on the introduction of the euro, in particular Articles 1, 9 and 10 thereof, has provided for a continuation, during the transition period (i.e. the period between 1 January 1999 and 31 December 2001), of the territorial limits for the legal tender status of banknotes denominated in a national currency unit; whereas such national banknotes are issued by the participating NCBs; whereas banknotes denominated in euro will only be put into circulation as from 1 January 2002; whereas during the transition period the ESCB's monetary policy function is unlikely to have any material impact on banknotes in circulation;

HAS ADOPTED THIS DECISION:

Article 1

Definitions

For the purposes of this Decision:

- "equivalent claims" shall mean the claims of the participating NCBs against the ECB arising from the transfer of foreign reserve assets from the NCBs to the ECB under Article 30 of the Statute;
- "euro area financial sector counterparties" shall mean (i) credit institutions as defined in the first indent of Article 1 of Council Directive 77/780/EEC, other than participating NCBs, the registered or head office of which is located in a participating Member State and (ii) branches of credit institutions, as defined in the first indent of Article 1 of Council Directive 77/780/EEC, in a participating Member State, which have neither their registered nor their head office in a participating Member State;

- "HBS" shall mean the harmonised balance sheet as structured in Annex 4 of the Guideline of the European Central Bank of 1 December 1998 on the legal framework of accounting and reporting in the European System of Central Banks (ECB/1998/NP22);

- "liability base" shall be the amount of qualifying liabilities, within the balance sheet of each participating NCB, specified in accordance with the Annex to this Decision;

- "participating NCB" shall mean a national central bank of a Member State which has adopted the single currency in accordance with the Treaty establishing the European Community;

- "reference rate" shall be the latest available interest rate used by the ESCB in its main refinancing operations under paragraph 3.1.2 of Annex 1 of the Guideline of the European Central Bank of 11 September 1998 on monetary policy instruments and procedures of the ESCB - ECB-GL/1998/02 (ECB/1998/NP16);

- "transition period" shall mean the period between 1 January 1999 and 31 December 2001.

Article 2

Method for measuring monetary income

1. During the transition period the amount of each participating NCB's monetary income shall be determined in accordance with the following formula:

   MI = [LB x RR]

   Where:

   MI is the amount of each participating NCB's monetary income to be pooled;

   LB is the liability base of each participating NCB;

   RR is the reference rate.

2. The amount of each participating NCB's monetary income shall be reduced by an amount equivalent to any interest paid on liabilities included within the liability base.

Article 3

Calculation and allocation of monetary income

1. The calculation of each participating NCB's monetary income shall be effected by the ECB on a daily basis. The calculation shall be based on accounting data reported by participating NCBs to the ECB under the Guideline of the European Central Bank of 1 December 1999 on the legal framework for accounting and reporting in the European System of Central Banks (ECB/1998/NP22).

2. The sum of each participating NCB's monetary income shall be allocated to the participating NCBs in proportion to their paid-up shares in the capital of the ECB. Such allocation of monetary income shall take place at the end of each financial year. The ECB shall inform the NCBs of the cumulative amounts on a quarterly basis.

3. The amount of monetary income to be allocated to each participating NCB shall be adjusted in accordance with any decision by the Governing Council of the ECB made in relation to Article 32.4, second paragraph, of the Statute or to the risk-sharing provisions contained in the Decision of the European Central Bank of 22 December 1998 on the allocation of risks in relation to losses arising in ESCB credit operations (ECB/1998/NP29).

4. The amount of monetary income to be allocated to each participating NCB shall be offset against the amounts due by the same participating NCB as calculated in accordance with Article 2 above. The net balances arising from the allocation of monetary income shall be settled at the ECB.

Article 4

Transitional direct charge on income accruing to participating NCBs from national banknotes in circulation

1. There shall be a charge on income accruing to each participating NCB from assets held against national banknotes in circulation (hereinafter referred to as the NCB's "seigniorage"). Such charge shall give the ECB the right to access an NCB's seigniorage with the exclusive purpose of covering those losses of the ECB that cannot be funded during the financial years 1999, 2000 and 2001 either (i) in the manner outlined under Article 33.2 of the Statute, or (ii) against that portion of the

equivalent claims which can be partially offset against foreign exchange losses under the ECB Guideline (ECB/1998/NP8) of 3 November 1998 on the composition, valuation and modalities for the initial transfer of foreign reserve assets, and the denomination and remuneration of equivalent claims.

2. The Governing Council of the ECB, in addition to approving the annual accounts of the ECB each financial year, will decide the amount of the charge and establish the modalities for settlement of unfunded losses.

3. The amount of the charge shall have a maximum upper limit equivalent to the increase in the total monetary income of the ESCB that would have arisen if banknotes denominated in national currency units had been included in the liability base. The amount of the charge of each participating NCB shall be in proportion to its key for subscription to the capital of the ECB. This limit shall be reduced to the extent necessary to ensure that no participating NCB shall be liable for more than the total of its seigniorage income from national banknotes in circulation for the relevant financial year. For the purposes of this paragraph, national seigniorage shall be calculated by applying the reference rate to the amount of national banknotes in circulation.

Article 5

Final provision

This Decision applies to the financial years of 1999, 2000 and 2001.

Done at Frankfurt am Main on 3 November 1998.

The President of the ECB

[signed]

Willem F. Duisenberg

COMPOSITION OF THE LIABILITY BASE

A The liability base shall include, with the exclusion of any other item:

1. Liabilities to euro area financial sector counterparties denominated in euro, including:

   (a) current accounts (item 2.1 of the HBS);

   (b) reserve requirements under Article 19.1 of the Statute (item 2.1 of the HBS);

   (c) amounts in deposit under the ESCB deposit facility (item 2.2 of the HBS);

   (d) fixed-term deposits (item 2.3 of the HBS);

   (e) deposits related to margin calls arising from ESCB monetary policy operations (item 2.4 of the HBS);

   (f) liabilities arising from liquidity-absorbing repurchase operations (reverse repos) under Chapter 3.1 of Annex 1 of the ECB Guideline of 11 September 1998 on monetary policy instruments and procedures of the ESCB.

2. Liabilities of participating NCBs arising from the issuance to the ECB of promissory notes in connection with the issuance by the ECB of debt certificates under Chapter 3.3 of Annex 1 of the ECB Guideline of 11 September 1998 on monetary policy instruments and procedures of the ESCB (item 10.2 of the HBS).

B The amount of each participating NCB's liability base shall be calculated in accordance with the harmonised accounting principles and rules established in the Guideline of the European Central Bank of 1 December 1998 on the legal framework for accounting and reporting in the European System of Central Banks (ECB/1998/NP22).