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EUROPEAN CENTRAL BANK

EUROSYSTEM

OPINION OF THE EUROPEAN CENTRAL BANK

of 21 December 2010

on the Hungarian Financial Supervisory Authority and on its President's legislative powers

(CON/2010/94)

Introduction and legal basis

On 9 November 2010, the European Central Bank (ECB) received a request from the Hungarian Ministry of Public Administration and Justice for an opinion on (i) a draft law on legislation and (ii) a draft law amending Law XX of 1949 on the Constitution of the Hungarian Republic (hereinafter the 'draft law amending the Constitution') with regard to the legislative powers of the President of the Pénzügyi Szervezetek Állami Felügyelete (the Financial Supervisory Authority, hereinafter the 'PSZÁF'). On 17 November 2010, the ECB received a request from the Ministry of the National Economy on a draft law on the PSZÁF (the draft law on legislation, the draft law amending the Constitution and the draft law on the PSZÁF, hereinafter collectively referred to as 'the draft laws'). Since the subject matter of the draft laws is closely related, the ECB has merged these consultations.

The ECB's competence to deliver an opinion is based on Articles 127(4) and 282(5) of the Treaty on the Functioning of the European Union and the third, fourth, 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[1], as the draft laws contain provisions concerning the Magyar Nemzeti Bank (MNB), the collection of statistical data, payment and settlement systems and rules applicable to financial institutions that may 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 laws

1.1 *Amendments to the Constitution and to the draft law on legislation conferring legislative powers on the PSZÁF's President*

The draft law on legislation will replace the Law on legislation annulled by the Hungarian Constitutional Court[2], and will thus re-establish the legislative framework in Hungary. The reason

1 OJ L 189, 3.7.1998, p. 42.

2 Decision 121/2009 (XII.17.)

for the annulment was that most provisions of the Law on legislation did not comply with constitutional developments that had taken place since its adoption. Since the remaining provisions were insufficient to constitute a legal act, the Constitutional Court annulled the Law on legislation in its entirety with effect for the future. The Constitutional Court requested the legislator to adopt a new law on the same subject matter by 31 December 2010 and obliged the legislator to regulate certain issues in the Constitution rather than in the Law on legislation. In reaction to this judgment, the Hungarian legislator had already drawn up a draft law amending the Constitution and a draft law on legislation on which the ECB had been consulted with regard to the legislative powers of the MNB[3]. The legal provisions concerning the legislative powers of the PSZÁF's President now submitted for consultation will be inserted in these draft laws.

According to the new amendments, the Constitution lays down the PSZÁF's main tasks[4] and provides that its President is appointed by Hungary's President for a term of six years[5]. Furthermore, the draft Constitution sets out that decrees issued by the PSZÁF's President qualify as legislation[6] and that they may not contradict laws, or government or MNB Governor decrees[7]. The legislator explains that these changes are intended to ensure the PSZÁF's independence.

1.2 *The draft law on the PSZÁF*

The draft law on the PSZÁF will repeal and replace Law CXXXV of 2007 on the Financial Supervisory Authority and is expected to enter into force on 1 January 2011.

In general, the draft law on the PSZÁF maintains the current legislative framework currently applicable to it. According to the explanatory memorandum, the PSZÁF's status is strengthened as it will be subordinated only to laws[8]. The draft law on the PSZÁF will establish a financial arbitration board to protect consumers, modify its organisation mainly on labour law related issues, provide for new sources of income and modify its supervisory procedures.

In addition, the draft law on the PSZÁF restricts the rights of the Pénzügyi Stabilitási Tanács (the Financial Stability Council, hereinafter the 'PST'). The PST consists of the Minister for Finance, the PSZÁF's President and the MNB's Governor and has the mandate to assist the FSA and, *inter alia*, to assess the stability of the financial markets. It can also submit legislative proposals to the Government or to one of its members or to the PST's Chair and has the right to be informed about how the addressee is going to proceed with this proposal[9]. The new draft no longer provides for this duty to 'comply or explain' in reaction to legislative proposals by the PST[10].

3 Opinion CON/2010/76. All ECB opinions are available on the ECB's website at www.ecb.europa.eu.
4 Article 40/D(1) of the draft Constitution.
5 Articles 30/A(1) and 40/D(2) of the draft Constitution.
6 Article 7/A(2) of the draft Constitution.
7 Article 40/D(4) draft Constitution.
8 Article 1 of the draft law on the PSZÁF.
9 'comply or explain'.
10 See Section 33 of the new draft law on the FSA.

2. General observations

2.1 *The appropriate time to consult the ECB*

The draft law amending the Constitution and the Law on legislation were adopted on 22 November 2010 while the Law on the PSZÁF was adopted on 13 December 2010 shortly after the ECB had been consulted and before it could adopt the present opinion. As a consequence, there was no possibility for the Hungarian legislator to take the ECB's views into account before adopting the draft laws.

The ECB reiterates that even cases of particular urgency do not relieve national authorities from their duty under Articles 127(4) and 282(5) of the Treaty to consult the ECB and to allow sufficient time to take into account its views, in accordance with Decision 98/415/EC. Any substantive amendments to the draft law – as in the case of the provisions subject to this consultation – have to be submitted to the ECB in order to allow it to issue its opinion based on the most recent text. In cases of particular urgency which do not allow for a normal consultation period, the consulting authority may indicate urgency in the consultation request and ask for a shorter deadline for the ECB's opinion to be adopted, thereby indicating the estimated course of the legislative process. The second sentence of Article 4 of Decision 98/415/EC provides that the ECB must be consulted 'at an appropriate stage' in the legislative process. This implies that the consultation should take place at a point in the legislative process which affords the ECB sufficient time to examine the draft legislative provisions and to adopt its opinion in all required language versions, and which also enables the relevant national authorities to take the ECB's opinion into consideration before the provisions are adopted. Article 3(4) of Decision 98/415/EC also obliges Member States to suspend the adoption process for draft legislative provisions, pending receipt of the ECB's opinion.

With respect to this ongoing consultation, this duty to consult the ECB has not been respected by the Hungarian authorities. This present Opinion in no way eliminates this breach of duty, as it is important for the application and interpretation of the enacted laws and any future amendments. The ECB would appreciate it if the Hungarian authorities would honour their obligation under the Treaty to consult the ECB, in accordance with Decision 98/415/EC.

2.2 *Legal certainty*

The ECB stresses the importance of legal certainty. The Law governing the tasks and the operational structure of the PSZÁF has been amended several times in recent years, and it is essential for the basic legislation regulating the PSZÁF's structure to serve as clear and consistent guidance. Frequent changes to the PSZÁF's structure would compromise this function.

2.3 *Observations made in ECB Opinion CON/2010/10*

With regard to the latest amendment to Law CXXXV of 2007, the Hungarian Ministry of Finance consulted the ECB at a very late stage in the legislative process. The observations made in Opinion CON/2010/10 could not be taken into account, as the Law was enacted before the ECB adopted its

opinion. Opinion CON/2010/10 is of particular relevance to the present consultation and the ECB invites the Hungarian authorities to take note of it.

Already this earlier amendment changed the PSZÁF's legal status from government agency into a 'self-regulatory administrative body[11], 'operated and managed independently'[12]. Furthermore the PSZÁF's organisational framework has been changed by abolishing the Board as a decision-making body and transferring these powers to its Chair[13]. A Financial Stability Council (PST) was also created[14].

3. Specific observations

3.1 *Competence of the PSZÁF's President to adopt legislative decrees*

According to the draft Constitution, the PSZÁF oversees, monitors and regulates Hungary's financial intermediation system. The PSZÁF is responsible for the smooth operation of the financial intermediation system in the manners specified by law. The PSZÁF's President may adopt decrees within the scope of the PSZÁF's authority concerning a wide range of financial matters, including on the collection of statistical data, payment and settlement systems, and rules applicable to financial institutions that may materially influence the stability of financial institutions and markets.

Article 40/D(4) of the draft Constitution provides that decrees issued by the PSZÁF's President may not contradict laws, or government or MNB Governor decrees. In this respect, it should be made clear how this rule will be applied in order to be compatible with the PSZÁF's independence which is indispensable for the exercise of its supervisory function[15].

3.2 *The obligation to consult the ECB*

The ECB welcomes the stress in Article 20 of the Law on legislation specifically on the duty to comply with notification and consultation obligations in the legislative process, as foreseen in Union legislation and that the draft law on legislation includes new decrees drafted by the PSZÁF's President. The duty to consult the ECB applies to generally applicable acts of supervisory authorities where these bodies have regulatory powers. However, this does not mean that the ECB should be consulted on all secondary legislation implementing primary legislation falling within the ECB's fields of competence. Given the objectives of Decision 98/415/EC, it is clear that an opinion should only be sought from the ECB on draft secondary legislation where its subject-matter is closely related to the ECB's tasks and if the impact on areas within the ECB's fields of competence differs from that resulting from the primary legislation itself.

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11 Section 1(1) of Law CXXXV 2007.

12 Section 1(3) of Law CXXXV 2007.

13 Section 11 of Law CXXXV 2007.

14 Section 14 to 16 of the Law CXXXV 2007.

15 The need for independence is also reflected in Principle 1(2) of the Core Principles Methodology, Basel Committee on Banking Supervision, October 2006 available on the BIS' website at www.bis.org.

3.3 *Supervisory college*

The ECB welcomes Article 12 of the draft law on the PSZÁF that introduces the concept of the supervisory college. The ECB is of the opinion that this will ensure smooth cross-border cooperation among the relevant supervisory authorities.

3.4 *Respect of MNB's independence*

As already indicated in ECB Opinion CON/2010/10, the PST will contribute to fostering cooperation and information sharing between the three represented authorities and contribute to financial market stability. The ECB expects that the PST will be a separate body for which the PSZÁF and the MNB will provide administrative and logistical support. Also, the ECB expects that the exercise of the PST's powers will fully respect the MNB's exclusive competence over monetary policy and any legislative proposals and recommendations that may be made by the PST should not impinge on the MNB's implementation of monetary policy decisions.

3.5 *PSZÁF's institutional framework*

Concerning the PSZÁF's institutional framework, the ECB refers to paragraphs 2.13 and 2.16 of Opinion CON/2010/10 in line with the position taken by the ECB in previous opinions[16], and in the light of the widespread practice in the Union on decision-making in supervisory matters. The ECB would prefer if the PSZÁF's decision-making body consisted of a formal board, acting on the basis of collegiality, rather than a President acting alone. In many Member States that have adopted supervisory models based on an independent financial supervisory authority, the central bank either provides members of the decision-making body of the supervisory authority or plays an institutional role in the appointment and dismissal of its members. In some cases there is joint membership of the decision-making bodies of the central bank and of the supervisory authority. Such an approach would retain some of the advantages of the existing institutional framework for the supervision of credit institutions in Hungary, and provide a practical means for exchanging information between the MNB and the PSZÁF. The ECB would, furthermore, welcome the inclusion in the draft law of provisions establishing a collegiate decision-making body with an appropriate number of MNB representatives having the full right to participate in its meetings, to vote and to share in all information available to the PSZÁF. The inclusion of MNB representatives in the PSZÁF's collegiate body would need to give due consideration to safeguards for the independence of the MNB's staff and its governing body[17].

3.6 *Determination of the salary for the PSZÁF's staff by its President*

The ECB notes the discretionary powers conferred on the PSZÁF's President with respect to the salary of the PSZÁF's staff who have civil servant status[18]. The President may reduce the civil servants' basic salary by up to 35% or increase it by up to 50%. He has also the power to grant a

16 See paragraphs 3.2.3 and 3.2.4 of Opinion CON/2006/15.

17 See footnote 7.

18 Article 25 of the draft law on the PSZÁF.

personal salary for civil servants achieving outstanding performance, which amounts to 150% of the basic salary and which is revocable without explanation. These discretionary powers are not in line with sound governance; they disrespect the need for transparency and legal certainty in the decision-making process.

3.7 *Limiting the PST's powers*

The PST's powers were originally tailored to the financial crisis, enabling it to efficiently assess and evaluate the implementation of prudential supervision policies. The ECB considers that under the draft law on the PSZÁF, the PST should still be entitled to be informed of how the addressee is going to proceed with its legislative proposals. Due to its composition, the PST has the knowledge and expertise to ensure a proper reaction to any financial stability issues. The proposed limitation on its powers will considerably weaken the impact of its legislative proposals. Moreover, limiting the PST's supervisory powers without entrusting these powers to another competent body or institution raises concerns.

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

Done at Frankfurt am Main, 21 December 2010.

[signed]

The President of the ECB

Jean-Claude TRICHET