



EUROPEAN CENTRAL BANK

OPINION OF THE EUROPEAN CENTRAL BANK

of 20 January 2004

at the request of the Economic Committee of the Finnish Parliament
on the government proposal to amend the Suomen Pankki Act and other related acts

(CON/2004/1)

Introduction

1. On 22 December 2003 the European Central Bank (ECB) received a request from the Economic Committee of the Finnish Parliament for an opinion on a government proposal (HE 134/2003) to amend the Suomen Pankki Act (*Laki Suomen Pankista (214/1998)*) of 27 March 1998, the Suomen Pankki Officials Act (*Laki Suomen Pankin virkamiehistä (1166/1998)*) of 30 December 1998, and the Financial Supervision Act (*Laki Rahoitustarkastuksesta (587/2003)*) of 27 June 2003 (hereinafter the ‘final legislative proposal’). The consultation request concerns the same subject matter as that addressed in ECB Opinion CON/2003/22 of 15 October 2003 which related to the draft government proposal (hereinafter the ‘draft legislative proposal’). The present opinion concerns the final government proposal that was submitted subsequent to the ECB’s first opinion. Like the first opinion also this opinion focuses on proposed measures affecting Suomen Pankki’s financial position and provisions relating to its power to issue norms.
2. The ECB’s competence to deliver an opinion is based on the second indent of 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 ECB by national authorities regarding draft legislative provisions¹, as the final legislative proposal relates to the national central bank (NCB) of Finland (Suomen Pankki). In accordance with the first sentence of Article 17.5 of the Rules of Procedure of the European Central Bank, the Governing Council of the ECB has adopted this opinion.

Summary of the most important differences between the draft and the final legislative proposal

3. The draft legislative proposal suggested reducing the primary capital of Suomen Pankki. This reduction would have forced Suomen Pankki *de facto* to sell part of its foreign reserve assets. As stated in CON/2003/22 the ECB considered that reducing the capital combined with other proposed measures

¹ OJ L 189, 3.7.1998, p. 42.

affecting Suomen Pankki's financial position and with a lack of statutory safeguards ensuring Suomen Pankki's ability to perform its ESCB-related and other tasks would have endangered Suomen Pankki's independence. The ECB welcomes the fact that the final legislative proposal does not reduce the capital. The ECB also welcomes the fact that the final legislative proposal contains a clause aiming to ensure that Suomen Pankki is able to perform its ESCB-related tasks, although this clause does not fully satisfy the requirements of financial independence as discussed below.

General assessment of the proposed measures affecting Suomen Pankki's independence

4. Article 109 of the Treaty provides that the Member States must ensure that their national legislation, including the NCBs' Statutes, is compatible with the Treaty and the Statute of the European System of Central Banks and of the European Central Bank. Article 108 of the Treaty, reinforced by Article 7 of the Statute, requires an NCB that forms part of the European System of Central Banks (ESCB) to be independent.
5. The principle of financial independence of central banks embedded in Article 108 of the Treaty requires that 'the NCBs be in a position to avail themselves of the appropriate means to ensure that their ESCB-related tasks can be properly fulfilled'². The concept of financial independence also requires that an NCB must, at all times, have sufficient financial means to carry out its other functions, i.e. to perform its national tasks, to meet its international obligations, and to cover properly its administrative and operational expenses. It should also be taken into account that the NCBs have commitments also regarding their foreign reserve assets and own funds, such as IMF-related commitments. Suomen Pankki's national tasks include those related to financial stability and crisis prevention and management. Although systemic crises tend to be rare events that are largely unpredictable, they can have great impact on the economy and should therefore receive appropriate attention from central banks. In such cases, an NCB's ability to act swiftly may prove to be particularly valuable. In particular, sufficient financial resources will assure public confidence as to the NCB's ability to intervene independently to tackle the crisis. This would also strengthen the credibility of its public statements aimed at restoring confidence in the viability of the financial system as a whole.
6. The final legislative proposal contains, *inter alia*, two measures, (i) an obligation to transfer 100% of Suomen Pankki's profits to the State, as a rule, and (ii) a strict limitation on Suomen Pankki's right to create financial provisions. Without proper statutory safeguards ensuring Suomen Pankki's ability to perform its ESCB-related tasks, the combined effect of these measures will weaken Suomen Pankki's financial position over time, increasing the risk that it may not have sufficient resources in the future to carry out its ESCB-related and other tasks and making it dependent on the decisions of third parties in such situations. In view of the uncertainty about future financial demands on Suomen Pankki, it is vital to have adequate margins and to safeguard the real value of the bank's resources in relation to its tasks.

² European Monetary Institute, Convergence Report, March 1998.

In its present form, the final legislative proposal infringes the principle of financial independence with regard to Suomen Pankki. Therefore, the ECB concludes that the final legislative proposal is still incompatible with the Treaty and its intentions. Moreover, as the weakening of the financial position of an NCB forming part of the ESCB/Eurosystem cannot be seen in isolation from the system as a whole, the final legislative proposal will have an adverse effect on the credibility and financial standing of the Eurosystem as a whole.

Distribution of Suomen Pankki's profit

7. According to the final legislative proposal the rules on the allocation of Suomen Pankki's profit would be amended. The current Suomen Pankki Act states that half of the profit is credited as income to the State and the other half is transferred to the reserve fund, unless the Parliamentary Supervisory Council decides to allocate the profits differently. The final legislative proposal will change this rule and establish the compulsory transfer of the entire annual profit of Suomen Pankki to the State. A decision by the Parliamentary Supervisory Council to use the profit differently would require special justification.
8. The ECB is seriously concerned with regard to the consequences of a legislative arrangement under which not even a share of Suomen Pankki's profits is allocated to the reserve fund either automatically or based on the independent and professional judgement of the Board of Suomen Pankki after taking into account any possible future risks. The wording of the final legislative proposal places the use of possible profits for such purpose at the sole discretion of the Parliamentary Supervisory Council. Financial independence in Member States where Government or Parliament can directly or indirectly exercise influence on the distribution of an NCB's profit requires that statutory provisions guarantee that the proper performance of the NCBs' ESCB-related tasks is not hindered⁴.
9. Section 21.2 of the final legislative proposal acknowledges that the Parliamentary Supervisory Council can decide to alter the profit allocation in order to safeguard the performance of ESCB-related tasks. However, the wording of the clause, especially the use of the word 'can' instead of 'must', leaves the discretion of opting for or against the main rule (100% to the State) entirely with the Parliamentary Supervisory Council. Even though the justification for Section 21.2 in the explanatory memorandum states that 'the allocation of profit may not jeopardise the performance of Suomen Pankki's ESCB-related tasks', the ECB considers that the actual drafting of the statutory clause does not ensure the financial independence of Suomen Pankki required by Article 108 of the Treaty. For the sake of clarity the ECB would point out that even if it were not proposed to transfer the whole profit to the State as a rule but only a part of it, the final legislative proposal would still infringe the requirement of central bank independence set out in the Treaty if it allowed the Parliamentary Supervisory Council to refrain from allocating profits to Suomen Pankki where the performance of ESCB-related tasks would require

⁴ European Monetary Institute, Convergence Report, March 1998.

such an allocation.

10. In its report to the Economic Committee of the Finnish Parliament of 27 November 2003 the Finnish Parliament's Constitutional Committee considered that since Article 108 of the Treaty may in certain circumstances oblige the Parliamentary Supervisory Council to detract from the main rule for profit allocation, the statutory law should not imply that the Parliamentary Supervisory Council has any kind of discretion in such situations. The ECB fully supports this view.

Suomen Pankki's right to make financial provisions

11. The final legislative proposal would abolish Suomen Pankki's right independently to create financial provisions to safeguard the maintenance of the real value of its capital and reserves. The ECB stresses that future financial and economic developments cannot be foreseen with any degree of certainty, and therefore does not consider it justified for an NCB to be deprived of the opportunity of protecting itself against the erosion of the real value of its capital in the longer term.
12. The final legislative proposal allows exchange rate risk and the risk of variation in the market value of securities to be covered by making financial provisions. However, such provisions may only equal the amounts of annual realised net profits resulting from these sources. Where such net realised gains do not exist or are insufficient to cover future exposures, the final legislative proposal leaves the decision of allocating regular profits to the general reserve fund to the discretion of the Parliamentary Supervisory Council. This arrangement is not compatible with the requirement for an NCB to be financially independent, as the professional assessment of the Board of Suomen Pankki regarding coverage of future exposures would, under the final legislative proposal, not be decisive and there is still no adequate safeguard that the rules concerning the allocation of regular profits would sufficiently guarantee Suomen Pankki's ability to take care of its current or future tasks.

Suomen Pankki's power to issue norms regarding oversight

13. The final legislative proposal grants Suomen Pankki certain limited powers to issue norms in order to carry out its duties as part of the Eurosystem. According to the final legislative proposal, the norms would only be addressed to those institutions that maintain or participate in such payment and clearing systems as the Finnish Ministry of Finance has designated under the Finnish law implementing the Settlement Finality Directive⁵. As the final legislative proposal remained, to some extent, unchanged on this matter, the ECB would like to reiterate the views expressed in CON/2003/22.
14. Article 105(2) of the Treaty and Article 3.1 of the Statute include as a basic Eurosystem central bank task the promotion of the smooth operation of payment systems. For the NCBs of the participating Member States, these Articles provide a legal basis for the oversight of payment systems functionally

⁵ Directive 98/26/EC of the European Parliament and the Council of 19 May 1998 on settlement finality in payment and securities settlement systems, OJ L 166, 11.6.1998, p. 45.

directly linked with settlement systems. Within the Eurosystem, oversight activities are generally performed at NCB level, in line with the common oversight policy defined for the Eurosystem by the ECB's Governing Council. The ECB understands that in line with the NCBs' oversight function⁶, Section 3 of the Suomen Pankki Act provides the legal basis for Suomen Pankki's oversight function by stipulating that it will both participate in maintaining the reliability and efficiency of the payment system and the overall financial system and assist in their development.

15. The ECB supports the proposed measure, which makes it easier for Suomen Pankki to fulfil its oversight function in a sufficiently transparent way. The ECB notes, however, that the wording of the final legislative proposal appears relatively restrictive and could prove to be impracticable. Firstly, Suomen Pankki is responsible for overseeing the reliability and efficiency of the overall infrastructure of the financial system, which includes securities settlement systems. Therefore, an explicit reference in the Suomen Pankki Act to Suomen Pankki's oversight function regarding securities clearing and settlement systems might be helpful for the sake of clarification. Secondly, given the broad oversight function of Suomen Pankki, as described in the explanatory memorandum, it would be reasonable for all payment and securities clearing and settlement systems to be brought under the regulatory powers of Suomen Pankki, regardless of whether they are protected by the Settlement Finality Directive. Thirdly, ECB legal acts other than guidelines, instructions and regulations, such as decisions, as well as ESCB-wide agreements, are excluded from the explicit wording of the final legislative proposal. ECB decisions that bind the NCBs are, however, referred to in the explanatory memorandum. The ECB notes that when adopting the Treaty Finland undertook to act in a manner enabling its central bank to abide by the legal instruments of the ECB with binding effect on it. For the sake of greater clarity and legal certainty the ECB would like to invite the Finnish Government and Parliament to extend the explicit wording of the final legislative proposal to cover ECB legal instruments binding on NCBs. This could be done for example by linking Suomen Pankki's power to issue norms to its obligation to carry out its tasks as part of the ESCB, as is acknowledged in the explanatory memorandum. In this context, the ECB would point out that the NCBs are always bound by the content and parameters laid down in ECB legal acts, which do not allow discretionary powers to be used when implementing them.

⁶ The oversight function of NCBs has been described in detail in previous ECB opinions published on its website <http://www.ecb.int>. For example see ECB Opinion CON/2003/14 of 7 August 2003 at the request of the Banca d'Italia on a draft regulation on payment systems, payment infrastructures and payment instruments and ECB Opinion CON/2003/15 of 8 August 2003 at the request of Sveriges Riksbank on a draft law amending the Sveriges Riksbank Act (not yet published).

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

Done at Frankfurt am Main on 20 January 2004.

[signed]

The President of the ECB

Jean-Claude TRICHET