



EUROPEAN CENTRAL BANK

THE PRESIDENT

OPINION OF THE EUROPEAN CENTRAL BANK

**at the request of the Portuguese Ministry of Finance on two draft legislative provisions amending (i) the legal framework of credit institutions and financial companies concerning the Deposit Guarantee Fund and (ii) the executive order governing the activities of the Deposit Guarantee Fund
(CON/99/15)**

1. On 23 September 1999, the European Central Bank (ECB) received a request from the Portuguese Ministry of Finance for an ECB Opinion concerning (i) a draft legislative act which amends the legal framework of credit institutions and financial companies, approved by Decree Law No. 298/92 of 31 December ('Regime Geral das Instituições de Crédito e das Sociedades Financeiras'), concerning the Deposit Guarantee Fund and (ii) a draft executive order that amends the Executive Order No. 285-B/95 (Series II) of 19 September, which lays down detailed rules governing the activities of the Deposit Guarantee Fund.
2. 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 and last indents, 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 legislative act deals with national central banks and with rules applicable to financial institutions which can have a material influence on the stability of financial institutions and financial markets. 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. The draft legislative provisions were submitted to the ECB in its official original version in Portuguese accompanied by a courtesy translation in English.
3. The main purpose of the draft legislative act is, on the one hand, to enlarge the scope of activities of the Deposit Guarantee Fund, allowing for its intervention in situations of financial reorganisation of credit institutions and, on the other hand, to encourage the co-operation between Banco de Portugal and the Deposit Guarantee Fund in the aforementioned situations. This is particularly relevant for the legal framework of credit institutions and financial

companies in Portugal, since the general law relating to preventive bankruptcy measures and to measures of reorganisation of undertakings and protection of creditors does not apply to credit institutions.

4. According to the 'Regime Geral das Instituições de Crédito e das Sociedades Financeiras', Banco de Portugal, as the banking supervision authority, may decide to take exceptional measures whenever the interests of depositors, investors and other creditors or the safeguard of the normal functioning of the money, financial and foreign exchange markets, are threatened. Among these measures, Banco de Portugal may require the institution concerned to prepare a reorganisation plan, whose acceptance by Banco de Portugal may be made conditional upon capital reduction or increase, disposal of shareholdings and other assets or upon any other conditions as deemed appropriate by Banco de Portugal. The draft legislative act allows Banco de Portugal, in the context of its intervention in the institution concerned, to invite the Deposit Guarantee Fund to co-operate in the reorganisation process, particularly by granting monetary or financial support or by participating in possible capital increases. The amendments introduced in Article 142 of the legal framework of credit institutions and financial companies, approved by Decree Law No. 298/92 of 31 December, achieve this objective.
5. The ECB notes that the remaining provisions of the draft legislative have the purpose of adapting the Deposit Guarantee Fund to its new function of co-operating in actions intended to re-establish the solvency and liquidity of credit institutions (see amendments introduced in Articles 155, 158 and 163 of the legal framework of credit institutions and financial companies, approved by Decree Law No. 298/92 of 31 December and the new Article 167-A added to the same Decree Law).
6. The ECB notes that, in relation to the amendments to Article 142, Banco de Portugal will have an extended role over the financial reorganisation of a troubled institution. Namely, Banco de Portugal reserves the right to decide on a capital increase and to further decide that the capital increase is preceded by the absorption of the institution's losses by the relevant 'positive' items of own funds. Banco de Portugal may also invite the Deposit Guarantee Fund or other institutions to co-operate in the reorganisation process, in particular, through the granting of adequate monetary or financial support, or through their participation in the capital increase decided by Banco de Portugal, who shall be also responsible for guiding and defining such co-operation in terms of the timeframe. In this regard, the ECB would like to suggest that some further clarification be given to the possibility of Banco de Portugal to decide on a capital increase of a troubled institution, as foreseen in the proposed paragraph 4 of Article 142. It could be made clearer, in the context of the other provisions of Article 142, that this decision of

Banco de Portugal relates to the appropriateness of a capital increase so that the troubled institution is able to fulfil its commitments. The ECB understands that a decision of Banco de Portugal on a capital increase would not, however, involve the obligation for the shareholders of the institution or for any other investors and institutions, including the Deposit Guarantee Fund, to indeed subscribe the capital increase. These remain free to subscribe or not the capital increase. The ECB would therefore welcome a clarification of this point in order to avoid the impression that Banco de Portugal could enforce a capital increase on unwilling shareholders or other investors and institutions. In this context, the ECB would like to draw the attention of the Portuguese authorities to the jurisprudence of the European Court of Justice in the "Karella and Syndesmos" line of cases (cases C-381/89, C-19/90 and C-20/90, C-134/91 and C-135/91, and C-441/93) on the compatibility with Community law of national rules providing for an increase, by administrative measures, of the capital of a company in financial difficulties.

7. The ECB notes, in relation to the new paragraph 2 of Article 159, that Banco de Portugal will be able, in an urgent situation and under the conditions laid down in its Organic Law, to grant temporarily to the Deposit Guarantee Fund the financial resources required to meet the latter's immediate needs. The ECB would like to note that the financial resources granted by Banco de Portugal to the Fund under this provision are lent without prejudice to its obligations as part of the ESCB and based on adequate collateral (see Articles 24.1 (c) and 25 (b) of the Organic Law of Banco de Portugal) and cannot be used for the special intervention of the Fund in the situations foreseen under the proposed new Article 167-A, which relate to specific cases of financial distress involving member credit institutions. This interpretation results from paragraph 2 of the proposed Article 167-A, which states that the Fund shall confine its financial support operations to situations which, among other criteria, do not involve the recourse of the Fund to loans or to special contributions from member credit institutions. In this context, it should also be mentioned that according to Article 14.4 of the ESCB Statute, national central banks may perform functions other than those specified in the ESCB Statute unless the Governing Council of the ECB finds, by a majority of two-thirds of the votes cast, that these interfere with the objectives and tasks of the ESCB. The ECB does not anticipate that the tasks of Banco de Portugal as described in the draft legislative act under consultation would interfere with the objectives and tasks of the ESCB.
8. The ECB notes, in relation to the new Article 167-A, relating to financial support rules, that the Deposit Guarantee Fund will be able to participate in operations deemed adequate to put an end to situations of financial distress involving member credit institutions. Moreover, it is stipulated that the Fund shall confine its financial support operations to the cases in which financial distress situations are most likely to come to an end within a short period of time, the objectives

are clearly outlined and defined, the way how the Fund's support will end is ensured, and a recourse to loans or to special contributions from member credit institutions is not involved. The ECB notes therefore that the Deposit Guarantee Fund may have, in certain situations, a prominent role in crisis management of credit institutions in Portugal. The ECB welcomes in this regard that the execution of any financial support operation by the Deposit Guarantee Fund is made dependent upon an opinion of Banco de Portugal that the operation is adequate to the resolution of the situation in question. This provision is appropriate taking into account the competencies of Banco de Portugal as overseer of financial stability, in accordance with Article 12 (c) of the Organic Law of Banco de Portugal.

9. The proposed amendments to the Executive Order No. 285-B/95 (Series II) of 19 September, which lays down detailed rules governing the activities of the Deposit Guarantee Fund, are a mere consequence of the new functions of the Deposit Guarantee Fund in the field of financial reorganisation of credit institutions, in particular of the amendments introduced in Articles 142, 155 and 158 of the legal framework of credit institutions and financial companies, approved by Decree Law No. 298/92 of 31 December. The ECB welcomes in this regard that any decision concerning the types of support to a troubled institution should be made in close co-operation with Banco de Portugal.
10. The ECB confirms that it has no objections to this ECB Opinion being made public by the competent national authorities at their discretion.

Done at Frankfurt am Main on 27 October 1999.

The President of the ECB

[signed]

Willem F. Duisenberg