EUROPEAN CENTRAL BANK

OPINION OF THE EUROPEAN CENTRAL BANK

of 3 February 2005

at the request of the Italian Ministry of Economic Affairs and Finance on a draft law amending Law Decree No 7 of 25 January 1999, as converted by Law No 74 of 25 March 1999, concerning urgent provisions on Italian participation in the International Monetary Fund's interventions to confront severe financial crises of its member countries

(CON/2005/1)

1. On 22 October 2004 the European Central Bank (ECB) received a request from the Italian Ministry of Economic Affairs and Finance for an opinion on a draft legislative proposal amending Law Decree No 7 of 25 January 1999, as converted by Law No 74 of 25 March 1999 (hereinafter the 'Law Decree'), concerning urgent provisions on Italian participation in the International Monetary Fund's interventions to confront severe financial crises of its member countries (hereinafter the 'draft law').

2. The ECB's competence to deliver an opinion is based on 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 law contains provisions concerning a national central bank (NCB). In addition, the ECB notes that its role under Article 237(d) of the Treaty of ensuring that NCBs fulfil their obligations thereunder[2], which includes ensuring that they comply with the prohibition on monetary financing laid down in Article 101, makes it necessary to ascertain whether the draft law is compatible with this prohibition. 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.

3. Article 1(1) of the Law Decree currently authorises the Italian Ministry of Economic Affairs and Finance to guarantee the repayment of principal and interest and cover any exchange rate risks on credit lines extended by the Banca d'Italia to the International Monetary Fund (IMF) member countries that respect the conditions of the adjustment programmes approved by the IMF, when

1 OJ L 189, 3.7.1998, p. 42.

2 See also Recital 9 of Council Regulation (EC) No 3603/93 of 13 December 1993 specifying definitions for the application of the prohibitions referred to in Articles 104 and 104b(1) of the Treaty, OJ L 332, 31.12.1993, p. 1, which provides that notwithstanding the role assigned to the Commission pursuant to Article 169 of the Treaty, it is for the ECB, pursuant to Articles 109f(9) (now 117(9)) and 180 (now 237) of the Treaty, to ensure that NCBs honour the obligations laid down by the Treaty.

unforeseen circumstances require financial resources additional to those provided by the latter, up to a cumulative limit of ITL 2 500 billion (approximately EUR 1,29 billion), which is the total amount of the possible interventions under that Article. It should be noted that the Law Decree was not submitted for consultation to the ECB at the time of its adoption. The present consultation refers only to the draft law. The latter would amend the Law Decree to the effect that the Ministry of Economic Affairs and Finance would be authorised, within the abovementioned cumulative limit, to guarantee the repayment of principal and interest and cover any exchange rate risks on credit lines extended by the Banca d'Italia to the Lebanese Republic, in respect of an amount not higher than EUR 200 million.

4. In the explanatory memorandum accompanying the draft law it is explained that on 23 November 2002 an international conference was held in Paris to support Lebanon's economic adjustment programme, which was convened by the President of France and attended by representatives of various EU and non-EU countries, the IMF and the World Bank. On that occasion, the Italian Prime Minister pledged to provide EUR 200 million to support Lebanon's efforts in the context of the stabilisation process of the Middle East.

5. The explanatory memorandum states that the draft law is required since Lebanon does not have a standard financed programme in place with the IMF. It further notes that the draft law is considered to be appropriate since (a) Lebanon is a member of the IMF and has a regular relationship therewith; (b) the IMF welcomed Lebanon's efforts and the support of the international community at the Paris conference; and (c) the IMF confirmed its willingness at the said conference to closely cooperate with the Lebanese authorities. The explanatory memorandum then states that, from a fiscal point of view, the draft law (a) does not have an impact on the Italian national budget since it provides for a contingent liability within pre-approved limits; and (b) would not have any impact on the Italian Government's budget even if the funding was provided by the latter since as a credit it would be a financial item which would not affect Italy's net borrowing according to EU accounting rules. Finally, it states that the Banca d'Italia's balance sheet and profit and loss account 'are completely covered by the full guarantee of the Ministry of Economic Affairs and Finance'.

6. The ECB understands that the draft law concerns a limited financial commitment entered into by Italy to provide support to a country that is emerging from a troubled period in its history. However, the draft law must be examined as to its conformity with the abovementioned prohibition on monetary financing, contained in Article 101 of the Treaty, which prohibits, *inter alia*, overdraft facilities or any other type of credit facility with the NCBs in favour of central governments. Already in 1993 the Committee of Governors of the central banks of the Member States of the European Economic Community noted that this prohibition is of 'essential importance' to ensure that 'monetary policy [is not] hindered in the pursuit of its primary objective of price stability. Furthermore, central bank financing of the public sector lessens the pressure for fiscal discipline'[3].

[3] Letter to Commission President Delors of 20 April 1993.

Therefore, this prohibition must be interpreted in a strict manner, subject only to certain limited exemptions contained in Article 101(2) of the Treaty and Council Regulation (EC) No 3603/93. Article 1(1) of that Regulation provides that 'any financing of the public sector's obligations vis-à-vis third parties' is a 'type of credit facility' which is prohibited by Article 104 (now 101) of the Treaty. The Regulation also contains a number of limited and explicit exemptions from the prohibition on monetary financing. In particular, Article 7 provides that 'The financing by the … national central banks of obligations falling upon the public sector vis-à-vis the International Monetary Fund … shall not be regarded as a credit facility within the meaning of Article 104 of the Treaty'. Recital 14 sets out the rationale behind this exemption, stating that it is appropriate to authorise the financing by the central banks of obligations falling upon the public sector vis-à-vis the IMF as this financing results in foreign claims which have all the characteristics of reserve assets.

7. It is stated in the explanatory memorandum that under the draft law credit lines would be extended by the Banca d'Italia to Lebanon to fulfil the Italian Prime Minister's commitment to provide EUR 200 million to support that country. Therefore, the purpose of the draft law may be considered as authorising the 'financing of the public sector's obligations vis-à-vis third parties' which is prohibited by the abovementioned Article 1(1) of Regulation (EC) No 3603/93. It is therefore crucial to determine whether the draft law falls within the scope of the exemption contained in Article 7. More specifically, the legal question to be clarified is whether the Banca d'Italia's extension of credit to Lebanon can be characterised as its financing of an obligation of the Italian State 'vis-à-vis the IMF'. Although the ECB understands that the IMF takes a favourable view of the international community's support for Lebanon, it notes that Lebanon does not have any financial assistance programme in place with the IMF. The fact that the draft provision constitutes an amendment which will be introduced into an act entitled 'Urgent provisions on Italian participation in the [IMF's] interventions to confront severe financial crises of its member countries' does not affect the nature of the obligations it concerns. The available facts, including the provisions of the draft law itself identifying Lebanon as the direct beneficiary of the financing in question, indicate that the Italian Government's commitment to Lebanon does not derive from any obligation of the Italian State vis-à-vis the IMF, including an IMF-administered mechanism. It is also clear that the extension of a credit line to Lebanon by the Banca d'Italia would not result in any claim on the IMF. Therefore this financing should not be considered as a fulfilment of any obligation towards the IMF and the Article 7 exemption cannot be invoked to allow for Banca d'Italia's proposed financing of Lebanon as set out in the draft law. In addition, it would appear that the credit lines to be extended by the Banca d'Italia to Lebanon would be denominated in euro. Such a euro-denominated loan would not have the characteristics of a reserve asset, as mentioned in Recital 14. In conclusion, the extension of a credit line by the Banca d'Italia to Lebanon under the draft law would thus breach the prohibition on monetary financing contained in Article 101 of the Treaty.

8. This opinion will be published on the ECB’s website upon formal presentation of the draft law to the Parliament by the Italian Government. In any event, this opinion will be published at the latest six months after the date of its adoption.

Done at Frankfurt am Main, 3 February 2005.

[signed]

The President of the ECB

Jean-Claude TRICHET