



OPINION OF THE EUROPEAN CENTRAL BANK

of 21 October 2008

at the request of the German Ministry of Finance

**on a Law on the implementation of a package of measures to stabilise the financial market and
an order on its implementation**

(CON/2008/57)

Introduction and legal basis

On 17 October 2008, the European Central Bank (ECB) received a request from the German Federal Ministry of Finance for an opinion on a draft law on the implementation of a package of measures to stabilise the financial market (Law on financial market stabilisation, FMStG), adopted on the same day (hereinafter the 'Law'); the original draft law of 13 October 2008 was accompanied by a new Article 1 Section 3a and an amended Article 1 Section 4. Subsequently, also on 17 October 2008, the ECB received a request from the German Federal Ministry of Finance on an Order on the Implementation of the Financial Market Stabilisation Fund Law (Financial Market Stabilisation Fund Order) which was adopted on 20 October 2008 (hereinafter the 'Implementing Order').

The ECB's competence to deliver an opinion is based on Article 105(4) of the Treaty establishing the European Community and the third 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 provisions¹, as the Law and the Implementing Order relate to the Deutsche Bundesbank as well as to rules applicable to financial institutions insofar as they 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 Law and the Implementing Order

1.1 The Law and the Implementing Order are motivated by the current financial market crisis. In order to stabilise the financial market, safeguard the supply of capital for the German economy and protect consumers and investors, the Federal Government will establish the Financial Market Stabilisation Fund² (hereinafter the 'Fund') under the Law, for which it will be liable. The competence to manage the Fund lies with the Ministry of Finance³; however, the Ministry of Finance may delegate this responsibility to the Financial Market Stabilisation Authority (FMSA),

¹ OJ L 189, 3.7.1998, p. 42.

² Article 1 Section 1 of the Law.

³ Article 1 Section 4(1) of the Law.

a body that is organisationally separate from the Deutsche Bundesbank, under the legal and expert supervision of the Ministry of Finance⁴. The Fund has no legal capacity⁵.

- 1.2 The Fund's task is to secure the refinancing of German financial institutions⁶, including safeguarding newly issued refinancing instruments up to 36 months. For this purpose, the Ministry of Finance will be authorised to assume guarantees for the Fund up to an amount of EUR 400 billion for debt securities issued by financial sector entities as from entry into force of the Law until 31 December 2009, as well as for created obligations from deposits of financial sector companies with a maturity of up to 36 months, in order to eliminate liquidity shortages and to support refinancing in the capital market⁷. Furthermore, the Fund can participate in the recapitalisation of financial sector companies, in particular it may purchase shares or dormant equity holdings and acquire other items constituting own funds of these companies, including those created by state law, against the payment of a contribution⁸.
- 1.3 Financing of the Fund will be raised by the Ministry of Finance, which is authorised to borrow up to an amount of EUR 100 billion to cover expenditures under the Fund and measures under Article 1 Sections 6 to 8 of the Law⁹; the Federal Government shall bear the costs related to the management of the Fund¹⁰.
- 1.4 The Law provides that the Fund will expire on 31 December 2009.

2. General observations

- 2.1 The ECB notes that there are ongoing discussions at both the international and European levels with a view to coordinating actions of countries aimed at preserving confidence in and stability of the international financial markets. More specifically, on 12 October 2008 the Heads of State of the euro area issued a 'Declaration on a concerted European action plan of the euro area countries' (hereinafter the 'Declaration')¹¹, in which they confirmed their commitment to act together in a decisive and comprehensive way in order to restore confidence and proper functioning of the financial system, aiming at restoring appropriate and efficient financing conditions for the economy. They agreed on common principles to be followed by the EU and euro area governments, central banks and supervisors to avoid national measures adversely affecting the functioning of the single market and the other Member States. Such coordinated approach includes initiatives aimed at: (i) ensuring appropriate liquidity; (ii) facilitating the funding of banks through various means; (iii) providing additional capital resources to financial institutions; and (iv) recapitalisation of

4 Article 1 Section 3a(2) of the Law.

5 Article 1 Section 3 of the Law.

6 Article 1 Section 7(1) of the draft law (after adoption Article 1 Section 6(1) of the Law).

7 Article 1 Section 7(1) of the draft law (after adoption Article 1 Section 6(1) of the Law).

8 Article 1 Section 6(1) of the draft law (after adoption Article 1 Section 7(1) of the Law).

9 Article 1 Sections 9(1)(4) and (5) of the Law.

10 Article 1 Section 12(1) of the Law.

11 The Declaration is available on the French Presidency's website at www.ue2008.fr.

distressed banks. These principles were also endorsed by the European Council on 16 October 2008 for all Member States. Against this background, the ECB highlights that all the initiatives put in place by national governments to restore confidence in financial markets should be aimed at implementing such common principles, in the spirit of close cooperation with other Member States and EU institutions.

- 2.2 The ECB wishes to draw attention to the recent ECB opinions issued at the request of other Member States, in which the ECB has commented on legislative proposals sharing some of the features of the present arrangements¹². The ECB intends to facilitate coordination of the various national efforts addressing the current financial situation, *inter alia*, through timely adoption and publication of ECB opinions on such draft national legislation.
- 2.3 The ECB understands the application of an accelerated legislative procedure, but would appreciate receiving future consultations with more time allowed for the ECB to prepare its opinion.

3. Specific comments

3.1 *Prohibition of monetary financing and the role of the central bank*

With regard to the role of the central bank, the ECB reminds the German authorities that a number of elements must be observed in order to comply with the monetary financing prohibition laid down in the Treaty.

First, the ECB notes that the Law suggests that the Fund should be considered as a public undertaking within the meaning of Article 101(1) of the Treaty and Council Regulation (EC) 3603/93 of 13 December 1993 specifying definitions for the application of the prohibitions referred to in Articles 104 and 104b(1) of the Treaty¹³. Indeed, the Fund is established under the designation ‘Financial Market Stabilisation Fund – FMS’ as a special fund pursuant to Article 110(1) and Article 115(2) of the German Basic Law and has no legal capacity¹⁴. The ECB understands that the Fund will be managed by the Ministry of Finance with the possibility of

¹² See, e.g. ECB Opinion CON/2008/44 of 3 October 2008 at the request of the Irish Minister for Finance on a draft Credit Institutions (Financial Support) Bill 2008, ECB Opinion CON/2008/46 of 8 October 2008 at the request of the Belgian Ministry of Finance on a preliminary draft law on measures promoting financial stability and in particular establishing a State guarantee for the provision of credit in the context of financial stability, ECB Opinion CON/2008/48 of 15 October 2008 at the request of the Irish Minister for Finance on a draft Credit Institutions (Financial Support) Scheme 2008, ECB Opinion CON/2008/50 of 17 October 2008 at the request of the Belgian Ministry of Finance on a draft royal decree adopted under Article 117bis of the Law of 2 August 2002 on the supervision of the financial sector and on financial services; ECB Opinion CON/2008/52 of 17 October 2008 at the request of the Spanish State Secretary for Economic Affairs on a Royal Decree-Law creating a Fund for the acquisition of financial assets and on a Royal Decree-Law adopting urgent financial and economic measures in relation to the concerted European action plan of the euro area countries, and ECB Opinion CON/2008/56 of 21 October 2008 at the request of the Banque de France on a draft amending finance law for the financing of the economy. The opinions are available on the ECB’s website at www.ecb.europa.eu.

¹³ OJ L 332, 31.12.1993, p. 1. In order to qualify as a ‘public undertaking’ within the meaning of Article 101(1) of the Treaty, the State must exercise dominant influence over the company by controlling its financial resources and governing bodies in accordance with Article 8(1) of Regulation (EC) No 3603/93. A dominant influence on the part of the State or other regional or local authorities is presumed when these authorities, directly or indirectly in relation to an undertaking: (i) hold the major part of the undertaking’s subscribed capital; (ii) control the majority of the votes attaching to shares issued by the undertaking; or (iii) can appoint more than half of the members of the undertaking’s administrative, managerial or supervisory body.

¹⁴ Article 1 Section 3 of the Law.

delegating such management to the FMSA, a public law authority established at the Deutsche Bundesbank that is organisationally separate from the Deutsche Bundesbank. The ECB also understands that the Fund's resources will be financed through public debt issuance and that the Fund will bear its own management costs. The ECB notes that, to ensure compliance with the prohibition of monetary financing, the Fund may not benefit from overdraft facilities or any type of credit facility¹⁵ with the Deutsche Bundesbank (or any other central bank of the European System of Central Banks), while ESCB central banks are also prohibited from purchasing debt instruments directly from the Fund. By contrast, the acquisition by an ESCB central bank of debt instruments issued for the benefit of the Fund in the secondary market is, in principle, allowed. However, such purchases must not be used to circumvent the objectives of Article 101 of the Treaty.

Second, the ECB notes that the involvement of the Deutsche Bundesbank in the context of the Fund must be compatible with the Treaty provisions. As regards the Law, the ECB understands that the Deutsche Bundesbank will not be involved in the actual management of the Fund, but may be used as an agent in the performance of the FMSA's tasks. In this regard, it should be ensured that if the State requests the Deutsche Bundesbank to perform certain activities for the Fund, the arrangement must also comply with the monetary financing prohibition as regards the remuneration for these activities and the Deutsche Bundesbank's institutional and financial independence must be respected.

Third, the arrangement must also safeguard the proper performance of the Deutsche Bundesbank's existing tasks under the Treaty and the Statute of the European System of Central Banks and of the European Central Bank. For this purpose, the ECB recommends that the Fund's tasks be clearly separate from the Deutsche Bundesbank's tasks, and that services of the Deutsche Bundesbank to be provided to the Fund are performed with due regard to the principle of cost-coverage and the avoidance of conflicts of interest.

3.2 *Eligibility for support*

The institutions covered by the Fund under Article 1 Section 2(1) of the Law comprise: (i) institutions established under Section 1(1)(b) of the Law on banking; (ii) insurance corporations and pension funds established under Sections 1(1) (1) and (2) of the Law on insurance supervision; (iii) asset management companies pursuant to the Law on investment; and (iv) operators of stock exchanges and derivatives exchanges; and their respective parent companies, in so far as these are financial holding companies, mixed financial holding companies or supervised financial conglomerate companies and the abovementioned companies have their seat in Germany¹⁶. These institutions qualify as 'financial sector companies' under the Law. Additionally, special purpose vehicles are eligible for support¹⁷. The ECB notes that, in accordance with the Declaration, the

¹⁵ In accordance with Regulation (EC) No 3603/93.

¹⁶ According to the explanatory text presented on the Federal Ministry of Finance's website at www.bundesfinanzministerium.de, this also covers subsidiaries established in Germany of foreign institutions.

¹⁷ See Article 1 Section 7(1) of the draft law (after adoption Article 1 Section 6(1) of the Law) and Article 1 Section 8(1) of the draft law.

Fund will have to operate with the aim of avoiding any distortion in the level playing field as regards both domestic financial institutions and subsidiaries of foreign institutions.

3.3 *Community rules with regard to State aid and financial services*

The ECB notes that it should be ensured that the beneficiary institution(s) will not be unfairly advantaged by making undue use of their guaranteed status¹⁸. In this context, the ECB draws the consulting authority's attention to the Commission's recently adopted guidance on compliance by the financial sector support schemes with EU State aid rules¹⁹, which includes in the specific context of the provision of State guarantees, detailed rules on setting eligibility criteria for the beneficiary institutions²⁰. Further, in line with its previous opinions²¹, the ECB reiterates the importance of ensuring that the regulatory practice under the proposed arrangements will be conducted in full compliance with the relevant Community law provisions, including EU financial services legislation and the single market principles.

3.4 *The relationship with the single monetary policy of the euro area*

The ECB notes that, in line with the Declaration, Member States must act in a coordinated manner to avoid significant differences in national implementation from having a counter-productive effect and creating distortions in global banking markets. The Declaration acknowledges the need to work in cooperation with the ECB to ensure consistency with the Eurosystem's management of liquidity and compatibility with its operational framework. Against this background, the ECB notes that uncoordinated decisions among Member States should be avoided as they may involve a fragmentation of the euro area money market. In this respect, the ECB makes the following observations which are important from a monetary policy perspective, as regards the measures contained in the Law and the Implementing Order.

First, under Article 1 Section 8(1) of the Law, the Fund may acquire assets from financial institutions, to be defined in more detail in subsequent implementing legislation. Although such measures should restore confidence in the German banking system, it is important for the conditions applied by the Fund to its transactions to be determined in a coordinated manner within the euro area and the EU. In particular, the financial conditions of the acquisitions should be determined by market conditions. The ECB notes the importance of price determination of transactions conducted by the Fund and their potential implications for the transmission of the single monetary policy decisions within the euro area. Indeed, uncoordinated price determination between all euro area Member States could lead to segmentation of the euro area money market.

¹⁸ See, e.g., paragraph 3.4 of Opinion CON/2008/48 and paragraph 3.1 of Opinion CON/2008/50.

¹⁹ See the 'Communication from the Commission – The application of State aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis' of 13 October 2008, available on the Commission's website at www.ec.europa.eu (hereinafter the 'Commission's guidance').

²⁰ See paragraph 18 of the Commission's guidance, specifying that 'The eligibility criteria of financial institutions ... must be objective, taking due account of their role in the relevant banking system and the overall economy, and non-discriminatory so as to avoid undue distortive effects on neighbouring markets and the internal market as a whole. In application of the principle of non discrimination on the grounds of nationality, all institutions incorporated in the Member State concerned, including subsidiaries, and with significant activities in that Member State should be covered by the scheme'.

²¹ See paragraph 2.3 of Opinion CON/2008/44 and paragraph 3.5 of Opinion CON/2008/48.

Moreover, the transactions conducted by the Fund should not interfere with the transmission of the single monetary policy.

Second, it is the ECB's view that the extension of the State guarantees to cover interbank deposits should be avoided. It could entail a substantial distortion in the various national segments of the euro area money market by potentially increasing short-term debt issuance activity across Member States and thereby impairing the implementation of the single monetary policy, which is an exclusive competence of the Eurosystem under Article 105(2) of the Treaty. In this context, the ECB notes Article 1 Section 7(1) of the Law, according to which the Federal Minister of Finance is authorised to take over guarantees provided by the Fund with respect to bank obligations related to, *inter alia*, interbank deposits with a maturity of up to 36 months. In this context, it is crucial to ensure the coordination of the price determination of such guarantees within the euro area and the EU, as a level-playing-field is of essence.

Third, the ECB also notes that, under Sections 2(1) and (2) of the Implementing Order, a precise deadline is set for guarantees by the Fund, which will expire on 31 December 2012 at the latest. The ECB notes that this feature meets the principles stated in the Declaration pointing to the temporary feature of such scheme. However, it also notes that harmonisation regarding the end of such scheme across euro area and EU Member States is also crucial. The ECB should be involved in such concertation and coordination, and would welcome the explicit provision for this in subsequent legislation.

3.5 *Conditions for stabilisation measures*

The ECB welcomes the fact that, in accordance with the principle stressed by the Declaration to ensure that financial institutions to which Member States make available additional capital resources should be obliged to accept additional restrictions, notably to preclude possible abuse of such arrangements at the expense of non-beneficiaries, the Law empowers the Federal Government to set in details the conditions to be complied with by the financial sector companies which use stabilisation measures, whereby such conditions have been further specified in the Implementing Order²².

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

Done at Frankfurt am Main, 21 October 2008.

[signed]

The President of the ECB

Jean-Claude TRICHET

²² The Implementing Order requires that financial sector entities benefiting from support will be subject to requirements to ensure a solid and prudent business policy as regards their operations. The companies will be required, *inter alia*, to: (i) examine their business policy and its sustainability; and (ii) grant the Fund appropriate contractual information rights. The beneficiary company will also grant the Fund a right of audit and the Fund should require the beneficiary company to have the fulfilment of the requirements audited by the annual auditor and included in the audit report (see Section 5(1), Section 5(2)(1) and Section 5(7) of the Implementing Order).