



## OPINION OF THE EUROPEAN CENTRAL BANK

of 18 January 2010

### on the Magyar Nemzeti Bank's tasks, the structure and legal status of the Hungarian Financial Supervisory Authority and the establishment of the Financial Stability Council

(CON/2010/10)

#### **Introduction and legal basis**

On 23 November 2009, the European Central Bank (ECB) received a request from the Hungarian Ministry of Finance for an opinion on a draft law amending several legal acts, including the Law on the Magyar Nemzeti Bank and the Law on the Financial Supervisory Authority (hereinafter the 'draft law'). On 4 December 2009, the ECB received an additional request from the Hungarian Ministry of Finance for an opinion on further supplementary articles of the draft law. As part of the legislative procedure, on 7 December 2009 the Hungarian Parliament adopted substantive amendments to the draft law, on which the ECB was not consulted. The Parliament enacted the draft law including the amendments on 14 December 2009, before the ECB had adopted its opinion on the draft law. As a consequence, the ECB's views have not been taken into account in the legislative process.

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 and sixth indent 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<sup>1</sup>, as the draft law relates to the Magyar Nemzeti Bank (MNB) and rules applicable to financial institutions in so far 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 draft law**

1.1 The draft law inter alia extends the duties of the MNB. Pursuant to Article 4(7) of Law LVIII of 2001 on the Magyar Nemzeti Bank<sup>2</sup> (hereinafter the 'Law on the MNB') the MNB promotes the stability of the financial system and contributes to the development and smooth conduct of policies related to the prudential supervision of the financial system. The draft law amends this provision so that the MNB will 'support the evaluation and implementation of policies referring to the

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<sup>1</sup> OJ L 189, 3.7.1998, p. 42.

<sup>2</sup> Published in *Magyar Közlöny* 2001/76 (VII. 5.)

prudential supervision of credit institutions and to the stability of the financial intermediary system.’ For this purpose, among other things the draft law specifies that the MNB will identify business and economic risks threatening the financial intermediary system as a whole, promote the prevention of systemic risks and help to ease or eliminate the identified systemic risk.

- 1.2 The draft law authorises the Governor of the MNB to issue decrees prohibiting, restricting or making conditional certain activities, services, deals and the distribution of certain products if they pose a significant threat to the stability of the financial intermediary system. The Governor may also make proposals for legislation to the Government, to a member of the Government or to the President of the Financial Supervisory Authority (FSA) for regulations for the safe and secure operation of the financial intermediary system.
- 1.3 The draft law establishes the Financial Stability Council (FSC) consisting of the Minister of Finance, the President of the FSA and the Governor of the MNB (hereinafter the ‘three represented authorities’), as well as three invited members. The chairmanship of the FSC will rotate annually between the Minister of Finance, the Governor of the MNB and the President of the FSA. The FSC’s tasks are defined in Article 44 of the draft law and include: continuously assessing the stability of the financial market; discussing the FSA’s risk analysis; proposing to the Government, to a member of the Government or to the President of the FSA the adoption of legal acts; discussing the FSA’s annual report; discussing all general measures, orders or decisions of the FSA, other than those applying to individuals; delivering an opinion on draft decrees of the Governor of the MNB issued under the new proposed Article 60/A of the Law on the MNB; and continuously monitoring the FSA’s enforcement activities.
- 1.4 The draft law also changes the FSA’s legal status. Under Article 1(1) of Law CXXXV of 2007 on the Financial Supervisory Authority<sup>3</sup> (hereinafter the ‘Law on the FSA’), the FSA is a Government authority. Under the draft law, the FSA becomes an independent agency. The draft law also amends the purpose of the FSA’s activities.
- 1.5 The draft law establishes a new organisational framework for the FSA. Pursuant to Article 11 of the Law on the FSA, financial supervision is conducted by a Board. Under the draft law, the Board is abolished and most of its functions are transferred to the President of the FSA who will be personally responsible for FSA’s governance. The draft law also regulates in detail the process of appointing the President of the FSA, his conditions of employment and the scope of his duties and authority.

## **2. General observations**

*The appropriate time to consult the ECB*

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<sup>3</sup> Published in *Magyar Közlöny* 2007/162 (XI. 28.)

- 2.1 The ECB points out that, 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. This does not prejudice the consulting authority's duty under Article 127(4) and 282(5) of the Treaty to consult the ECB on national draft legislative provisions falling within its fields of competence in due course of the national legislation process. The second sentence of Article 4 of Decision 98/415/EC states 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. As the draft law was submitted to the Hungarian Parliament a month before the ECB received the first consultation request<sup>4</sup>, the ECB could not take into consideration the consulting authority's request for urgency on the grounds of the advanced stage of the process of legislation.
- 2.2 The opportunity to issue an opinion on a draft law within its competence of consultation allows the ECB to express its views on the substance of the proposed legislation, including considerations such as the importance that the ECB may attach to a particular legislative proposal and its potential impact on the Eurosystem. Therefore, the ECB reiterates its position that even cases of particular urgency do not relieve national authorities from their duty to consult the ECB and to allow sufficient time to take into account its views in accordance with Council 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. Furthermore, with respect to the ongoing consultation, the process of adoption of the draft law should have been suspended. The ECB's comments on the consulted provisions do not eliminate the breach of the obligation to consult the ECB. Even though the provisions have already been enacted, the ECB considers that its comments are important for the application and interpretation of the enacted law and any future amendments. The ECB would appreciate the Ministry of Finance giving due consideration to honouring their obligation to consult the ECB in the future, in accordance with the regulations laid down in Council Decision 98/415/EC.

*New tasks of the MNB in relation to its contribution to financial stability and the prevention of systemic risks*

- 2.3 The ECB understands that, under Articles 4(7) and 60/A of the Law on the MNB, specific new tasks will be assigned to the MNB which are intended to facilitate the MNB's effective

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<sup>4</sup> Draft Law No T/10998 was submitted to the Hungarian Parliament on 22.10.2009, and the consultation request concerning it was received by the ECB on 23.11.2009.

performance of its financial stability role and its contribution to the prevention, identification and elimination of systemic risks. The ECB welcomes and supports the inherent recognition in the proposed institutional framework of the essential role of the central bank in promoting the safety and soundness of financial institutions and the stability of the financial system as a whole<sup>5</sup>. Moreover, the introduction of a reference in the draft law to the ‘support to the evaluation and implementation of supervisory policies’ in the context of the financial stability tasks recognises the importance of taking financial stability considerations into account when developing supervisory policies. In this context, the creation of a financial stability council, with the involvement of the central bank, will allow the central bank to contribute with its systemic risk assessments to the development of the supervisory policies of the FSA.

*Interaction with the monetary policy of the MNB*

- 2.4 The ECB understands that, by setting up the FSC, the draft law does not establish a body responsible for supervision, functioning autonomously within the framework of the FSA. According to Article 44 of the draft law, the FSA will provide the secretariat of the FSC. Although the draft law provides that the FSC will ‘assist’ the FSA, which seems to indicate that the FSC will have a subordinate role in contributing to the fulfilment of the tasks of the FSA, the ECB trusts that the FSC will be a separate body to which the FSA will provide administrative and logistical support. The assignment to the MNB of specific tasks in the context of the establishment of the FSC is welcome, as it enhances the MNB’s contribution to financial stability. These new tasks should contribute to financial stability, without compromising the conduct of the monetary policy by the MNB.
- 2.5 The draft law provides that the FSC will assess the stability of the financial markets, including the money market. It is emphasised that the MNB is a key actor in the money market through the implementation of its monetary policy in order to fulfil its objectives. The implementation of monetary policy decisions is thus the exclusive competence of the central bank and should be preserved in all circumstances. It is therefore expected that the assessment of the stability of the money market will fully respect this exclusive competence of the MNB over monetary policy. Also, any recommendations that may be made by the FSC should not impinge on the MNB’s implementation of monetary policy decisions. For the sake of clarity, it might be advisable to stress that the new tasks conferred on the MNB in the draft law will not affect its conduct of monetary policy.
- 2.6 Given the abovementioned considerations, the FSC’s responsibilities should be formulated precisely so as to ensure that the effectiveness of the coordination process is not affected by any uncertainty regarding the roles, tasks and competences of the FSC and the three represented authorities.

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<sup>5</sup> See, e.g. paragraph 5 of Opinion CON/2004/16.

*Broadening the scope of secondary legislative powers of the MNB, and the MNB's relationship with the FSC*

2.7 Under the new Article 60/A of the MNB Law, the Governor of the MNB is empowered to issue decrees prohibiting, restricting or making conditional certain activities, services, deals and the distribution of certain products if they pose a significant threat to the stability of the financial intermediary system. According to the draft law, the Governor has to inform and seek the opinion of the FSC prior to issuing such decrees. In contrast to other provisions of the draft law, Article 60/A(6) does not set a time limit for the FSC to give an opinion. When issuing a decree, the Governor may also make proposals for legislation to the Government, or to a member of the Government or to the President of the FSA for regulation to provide for the safe and secure operation of the financial intermediary system. The new power of the Governor could be beneficially used to allow the MNB to better carry out its financial stability tasks. This new power of the MNB is underpinned by Article 28(1) of the Law on the MNB which gives the MNB the competence to gather adequate information on activities or persons pursuing activities that could endanger financial stability.

2.8 In its Convergence Reports<sup>6</sup>, most recently in its May 2008 Convergence Report, the ECB has reiterated that: 'An express statutory obligation for an NCB to consult third parties *ex ante* provides the latter with a formal mechanism to influence the final decision and is therefore incompatible with the Treaty and the Statute. However, dialogue between NCBs and third parties, even when based on statutory obligations to provide information and exchange views, is compatible with central bank independence provided that:

- this does not result in interference with the independence of the members of the NCB's decision-making bodies;
- the special status of Governors in their capacity as members of the ECB's General Council is fully respected; and
- confidentiality requirements resulting from the Statute are observed.'

Although the ECB welcomes the fact that the new Article 60/A of the MNB Law reaffirms the independence of the MNB by specifying that an *ex ante* obligation to consult 'may not in any way result in influencing the independence of the members of the decision making bodies of the MNB, or result in influencing or delaying the decision of the MNB', in practice the obligation to consult the FSC in advance without a time limit for the opinion to be given, allows the FSC to influence and delay the MNB's decisions. Therefore, the draft law should establish a regime for cooperation and dialogue based on clear procedural rules, including a time limit for the FSC to give its opinion, ensuring that the MNB's independence is respected and its decisions not delayed.

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<sup>6</sup> Available on the ECB's website at [www.ecb.europa.eu](http://www.ecb.europa.eu)

2.9 As pointed out in ECB Opinion CON/2009/88, it is expected that the MNB's new tasks under Articles 28 and 29, and its activities to support the FSC under Article 44 will fully comply with the Treaty obligations. In particular, it is expected that the MNB's new tasks laid down in the draft law will neither affect the MNB's institutional, functional and financial independence nor the performance by the European System of Central Banks of its tasks under the Treaty and the Statute of the European System of Central Banks and of the European Central Bank. Similarly, it is also expected that it will be ensured that the new tasks of the MNB, such as its contribution to the FSC, will fully comply with the prohibition of monetary financing laid down in Article 123(1) of the Treaty, read in conjunction with Council Regulation 3603/93/EC of 13 December 1993 specifying definitions for the application of the prohibitions referred to in Articles 104 and 104b(1)<sup>7</sup> (now Articles 123 and 125(1) of the Treaty). In this respect, the MNB's new tasks and activities to support the FSC should not give rise, implicitly or explicitly, to any form of overdraft facility or any type of credit facility with the MNB.

*The establishment and role of the FSC*

2.10 In the view of the ECB, the newly established FSC will contribute to fostering cooperation and information sharing between the three represented authorities and contribute to financial market stability, thus creating a forum where the three represented authorities playing a key role in financial regulation can initiate coordinated action in a financial crisis.

2.11 The establishment of national financial stability committees can enhance the ability of national central banks and supervisory authorities to contribute analytical support to the European Systemic Risk Board (ESRB). The tasks performed by these committees should complement the activities performed by the ESRB, therefore it is particularly important to develop appropriate synergies. However, it is necessary to avoid such national committees being entrusted with tasks and powers that potentially conflict with those of the ESRB, and which may undermine the effectiveness of the newly-established European macro-prudential supervisory body. Moreover, the legal frameworks of these committees should appropriately reflect the roles of central banks, should not constrain the independence of the governors of the central banks or unduly affect the quality and impartiality of their contributions as members of the ESRB. Lastly, in view of the importance of ensuring the effectiveness of macro-prudential supervisory arrangements at EU level, it is essential to safeguard the ability of the ESRB to perform its tasks independently and to guarantee an authoritative and effective channel for transmitting the warnings and recommendations issued by the ESRB.

2.12 The ECB also reminds the consulting authority of the Memorandum of Understanding on cooperation between Financial Supervisory Authorities, Central Banks and Finance Ministries of the European Union on cross-border financial stability which entered into force on 1 June 2008. The Memorandum of Understanding provides for the establishment of a domestic standing group in each Member State consisting of the financial supervisory authorities, central banks, finance

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<sup>7</sup> OJ L 332, 31.12.1993, p. 1.

ministries at the national level with the objective of enhancing preparedness in normal times and facilitating the management and resolution of a financial crises.

*Changes to the FSA's institutional framework*

- 2.13 In line with the position taken by the ECB in previous opinions<sup>8</sup>, and in the light of the widespread practice in the European Union on decision-making in supervisory matters, it may be preferable for the FSA's decision-making body to consist of a formal board, acting on the basis of collegiality, rather than a President acting alone.
- 2.14 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 cross-membership between 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 FSA.
- 2.15 Having regard to the above, the ECB would welcome the inclusion in the draft law of provisions establishing a collegiate decision-making body as the FSA's sole organ, including an appropriate number of MNB representatives in such a collegiate body, with the full right to participate in its meetings, to vote and to share in all information available to the FSA. The inclusion of MNB representatives in the FSA's collegiate body would need to give due consideration to safeguards for the independence of the members of the MNB staff and its governing body<sup>9</sup>.
- 2.16 The draft law does not provide for the transfer of the tasks of the current supervisory body, i.e. from the Board to the President of the FSA. The ECB draws the consulting authority's attention to the need to ensure the continuity of the smooth performance of the FSA's tasks by regulating the transfer of the competencies and responsibilities from the Board to the President of the FSA. The operational independence of supervisory bodies from political interference is an essential and internationally recognised standard for the supervision of financial markets. Such standards should be applied in particular to the procedures for the dismissal of the chairman of the Board of the FSA. Article 72(2) of the draft law concerns the status of the current chairman of the Board of the FSA. The ECB welcomes the inclusion in the draft law of a provision for the current chairman of the Board of the FSA to continue in office until the end of his appointed term. Lastly, the ECB stresses the importance of legal certainty. The law governing the tasks and the operational structure of the FSA has been amended several times in recent years, and it is essential for the basic legislation regulating the structure of the FSA to serve as clear and consistent guidance. Overly frequent changes to the structure of the FSA may compromise this function.

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<sup>8</sup> See paragraphs 3.2.3 and 3.2.4 of Opinion CON/2006/15.

<sup>9</sup> See footnote 7.

2.17 The ECB supports the basic principle that, in order to carry out their respective responsibilities effectively, there should be close cooperation between financial regulators. Therefore, the ECB welcomes the reference in the tasks of the FSA to the duty to cooperate with the MNB to prevent systemic risks arising. The Hungarian authorities may also consider further enhancing arrangements for information-sharing between the MNB and the FSA to take into account the duty of the FSA to cooperate with the MNB for the mitigation of systemic risks.

### **3. Specific comments**

#### *Definitions*

According to Article 28 of the draft law, the MNB will play a significant role in the evaluation and implementation of policies concerning the stability of the financial intermediary system. The ECB recommends that the term ‘financial intermediary system’ should be defined for the sake of legal clarity.

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

Done at Frankfurt am Main, 18 January 2010.

[signed]

*The President of the ECB*

Jean-Claude TRICHET