



## OPINION OF THE EUROPEAN CENTRAL BANK

of 4 October 2011

on reform of the deposit guarantee scheme

(CON/2011/76)

### **Introduction and legal basis**

On 1 August 2011, the Dutch Ministry of Finance published a draft general administrative regulation (hereinafter ‘the draft regulation’) for public consultation, which intends to transform the Dutch deposit guarantee scheme into an ex-ante funded scheme with risk-based contributions. This public consultation was open for response until 11 September 2011.

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 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 provisions<sup>1</sup>, as the draft regulation relates to De Nederlandsche Bank (DNB) and to rules applicable to financial institutions insofar as they materially influence the stability of financial institutions and markets.

The ECB should be consulted on this draft regulation, particularly because ECB Opinion CON/2011/60 on the Law which the draft regulation will implement<sup>2</sup> advised changes in the Dutch deposit guarantee scheme to ensure compliance with Treaty provisions on the prohibition on monetary financing. Since the ECB was informed that the Dutch Ministry of Finance does not intend consulting the ECB on this matter, the ECB has decided to submit this own-initiative opinion.

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 legislation**

The draft regulation amends the Decree on special prudential measures, investor compensation and deposit guarantees pursuant to the Law on financial supervision and to the Decree on prudential rules pursuant to this Law<sup>3</sup>. Such amendments concern the financing of the Dutch Deposit Guarantee Scheme (Dutch DGS) which is presently operated by DNB. If a credit institution is no longer able to meet its obligations vis-à-vis depositors, the Dutch DGS is activated and the costs are apportioned among other participating credit institutions. The Dutch DGS is funded on an ex-post basis by contributions from the

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

<sup>2</sup> All ECB opinions are available at [www.ecb.europa.eu](http://www.ecb.europa.eu).

<sup>3</sup> *Staatsblad* 2006, 507 and 519.

member credit institutions and DNB advances amounts needed for its operation. The main aim of the draft regulation is to transform the financing of the Dutch DGS from ex-post to ex-ante. Hence, the draft regulation establishes the Foundation for the Deposit Guarantee Fund (hereinafter the ‘Foundation’) which will be financed through contributions imposed on member credit institutions<sup>4</sup> and will reimburse DNB for the Dutch DGS’ operating costs<sup>5</sup> and for advance payouts in respect of guaranteed deposits<sup>6</sup>. The draft regulation regulates such various contributions to be made by member credit institutions of the Dutch DGS, including one-off contributions<sup>7</sup>, basic regular contributions<sup>8</sup> and ex-post contributions if the Dutch DGS has insufficient funds available<sup>9</sup>.

## 2. General observation

The ECB should be consulted on future substantial amendments to the draft regulation. No further consultation will be required if the amendments in essence aim to accommodate the concerns expressed by the ECB in this opinion. Moreover, given the current legislative initiative at Union level for the recast of Directive 94/19/EC of the European Parliament and of the Council of 30 May 1994 on deposit-guarantee schemes (hereinafter ‘draft recast DGS Directive’)<sup>10</sup>, the ECB understands that the relevant national legislation will, as necessary, be aligned with this future Directive<sup>11</sup>.

## 3. Specific observations

### 3.1 Prohibition on monetary financing and operation of the Dutch DGS

3.1.1 The ECB supports the establishment of ex-ante funded deposit guarantee schemes, given their relevance to financial stability, insofar as an exclusive reliance on DGS members’ ex-post contributions may be a source of procyclicality<sup>12</sup>, and credit institutions will participate in deposit protection costs. The ECB points out in this context that the recast DGS Directive will, *inter alia*, harmonise a target level of ex-ante financing, fixed at a certain percentage level of covered deposits. Against this background, the ECB welcomes the Dutch Ministry of Finance’s replacement of the current ex-post funding arrangements for the Dutch DGS with ex-ante funding arrangements. However, at the same time it is important for the national provisions on funding of the deposit guarantee schemes to comply with the monetary financing prohibition under Article 123 of the

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<sup>4</sup> See Sections 23f-23m of the draft regulation.

<sup>5</sup> See Section 23o of the draft regulation.

<sup>6</sup> See Section 23n of the draft regulation.

<sup>7</sup> See Section 23f of the draft regulation.

<sup>8</sup> See Section 23g-h of the draft regulation.

<sup>9</sup> See Section 23r of the draft regulation.

<sup>10</sup> OJ L 135, 31.5.1994, p. 5.

<sup>11</sup> See proposal for a Directive of the European Parliament and of the Council on Deposit Guarantee Schemes [recast] – Council Presidency compromise proposal of 14 June 2011, available on the Council’s website at <http://register.consilium.europa.eu>.

<sup>12</sup> See Commission’s staff working document ‘Summary of the impact assessment. Accompanying document to the proposal for a DIRECTIVE .../.../EU of the European Parliament and of the Council on Deposit Guarantee Schemes [recast]’, p. 5, available on the Commission’s website at [www.ec.europa.eu](http://www.ec.europa.eu).

Treaty. This provision prohibits central banks from providing overdraft facilities or any other type of credit facility to the public sector, including any financing of the public sector's obligations vis-à-vis third parties<sup>13</sup>. Hence, ECB Opinion CON/2011/60 advised the Dutch authorities<sup>14</sup> that advance payments by DNB in the context of the operation of the Dutch DGS are incompatible with the monetary financing prohibition and that consequently relevant Dutch legislation needs to be amended.

3.1.2 Section 22 of the draft regulation provides that DNB will make arrangements for the establishment of the Foundation and that the Foundation will reimburse DNB its costs in connection with the operation of the Dutch DGS. Further, Section 23n of the draft regulation provides that if DNB has paid out amounts related to the operation of the DGS, the Foundation will reimburse DNB as soon as possible for the total of those amounts up to an amount equal to the funds present in the Dutch DGS. Finally, Section 23o of the draft regulation provides that the Foundation reimburses the costs DNB has borne in connection with the DGS. The ECB understands that these provisions imply that DNB will finance, until it is reimbursed by the Foundation: (a) the Dutch DGS' tasks, such as payouts of the guaranteed deposits, and (b) the costs of operating the Dutch DGS. Further, the ECB understands that the limit 'up to an amount equal to the funds present in the deposit guarantee fund' in Section 23n may lead to a situation where DNB has made payments in the context of the operation of the Dutch DGS which will need first to be reimbursed through ex-post contributions from the member credit institutions of the Dutch DGS and can only be reimbursed to DNB subject to the availability of such contributions. The draft legislation does not provide for any backstop financing if ex-post contributions from member credit institutions are unavailable or insufficient<sup>15</sup>.

3.1.3 The above described forms of advance financing of the deposit guarantee scheme by the central bank are incompatible with the monetary financing prohibition. The only compatible forms of central bank financing of deposit guarantee schemes are: (a) intraday credit in line with the general rules on provision of such credit by the central bank, and (b) short-term emergency liquidity financing under strict conditions established in the ECB's Convergence Reports, i.e. if such funding is short term, addresses urgent situations, systemic stability aspects are at stake and decisions are at the NCB's discretion<sup>16</sup>. These conditions need to be listed in national law<sup>17</sup> in the cases where emergency liquidity financing of the DGS is foreseen by the national legal system.

3.1.4 Consequently, the ECB proposes the following amendments:

- (a) clarifying in Section 22 that the Foundation is financed by the dedicated contributions from the member credit institutions of the Dutch DGS and by other listed funding sources, which will not include advance financing by DNB;

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13 See Article 1(b)(ii) 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 104(b)(1) of the Treaty (OJ L 332, 31.12.1993, p. 1).

14 See paragraph 4.2 of ECB Opinion CON/2011/60; see also ECB Annual Report 2010, p. 120 and paragraphs 2.2 to 2.3 of ECB Opinion CON/2007/26.

15 See also paragraphs 3.1.4(d) and 3.2.2 of this opinion.

16 See ECB's Convergence Report, May 2010, p. 25.

17 See paragraphs 2.2 to 2.8 of ECB Opinion CON/2008/5.

- (b) specifying in Section 23n that the Foundation transfers the necessary amounts to DNB before DNB makes payments related to the performance of the Dutch DGS' tasks. Alternatively, it should provide expressly that any advance payments by DNB are only intraday. If in addition short-term emergency liquidity financing of Dutch DGS operations by DNB is foreseen, conditions for such financing referred to in paragraph 3.1.3 of this opinion should be expressly listed in the Dutch law;
- (c) specifying in Section 23o that sufficient funds will be made available to DNB for fulfilling its mandatory task of operating the Dutch DGS, in order to protect DNB's financial independence;
- (d) specifying funding sources available to the Foundation if ex-post contributions by the member credit institutions are insufficient to cover the needs of the Dutch DGS.

## 3.2 Financing of the Dutch DGS by its member credit institutions

### 3.2.1 *One-off contribution*

Section 23f of the draft regulation provides that an entity which becomes a credit institution following entry into force of the Decree will pay a one-off amount to the Foundation. The ECB understands from the explanatory memorandum<sup>18</sup> that existing credit institutions will pay the same contribution under Section III to provide the Foundation with starting capital, both contributions to be laid down by ministerial regulation. The ECB requests further clarification of the determination and size of these contributions, and reassurance that this does not conflict with the principle of a level playing field. The ECB points in this context to the draft recast DGS Directive which aims, *inter alia*, at harmonising the level of contributions paid to the national deposit guarantee schemes with a view to achieving a level playing field<sup>19</sup>.

### 3.2.2 *Ex-post contributions by member credit institutions and backstop financing*

Section 23r of the draft regulation provides for ex-post contributions by member credit institutions of the Dutch DGS if the Foundation does not have sufficient funds to reimburse DNB for incurred costs and advance payments in connection with the DGS. As stated in an earlier ECB opinion<sup>20</sup>, an ex-ante funding scheme should also include the possibility to call on the private sector for additional financial support, as pre-collected funds from the industry may be insufficient in a crisis situation. This principle of ex-post financing from the private sector should promote additional market discipline and address the risk of moral hazard. At the same time, the ECB notes that additional temporary financing going beyond the ex-post contributions by the member credit institutions may be needed in a severe crisis requiring, e.g. activation of deposit guarantees for a major credit institution. The draft regulation does not provide for financing to bridge this financial

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18 See explanatory memorandum, p. 38.

19 See recital 6 of the draft recast DGS Directive.

20 See ECB Opinion CON/2011/12.

gap. As already indicated in paragraph 3.1.4(d) above, the ECB invites the Dutch Ministry of Finance to expressly regulate this issue.

### 3.3. DNB's financial independence

The ECB refers to the principle of financial independence under which an NCB must have sufficient means not only to perform its ESCB-related tasks, but also its national tasks, e.g. financing its administration and own operations<sup>21</sup>. Previous ECB opinions pointed out that allocation to the NCBs of specific non-ESCB related tasks (e.g. tasks in the area of financial supervision or consumer protection) needs to be accompanied by the allocation of adequate human and financial resources allowing for such tasks to be carried out in a manner which will not affect the NCBs' operational capacity to carry out their ESCB-related tasks<sup>22</sup>. In particular, the ECB has advocated a prudent approach in this respect when reimbursement arrangements are proposed in the national legislation as a mode of financing the non-ESCB related tasks<sup>23</sup>. The ECB considers that the draft regulation raises concerns in this respect to the extent that, as developed above, advance financing by the DNB of the Dutch DGS operations is foreseen by the draft regulation other than as intraday or short-term emergency liquidity financing, and in particular in the circumstances where DNB would not be fully reimbursed for such advance financing.

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

Done at Frankfurt am Main, 4 October 2011.

[signed]

*The President of the ECB*

Jean-Claude TRICHET

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<sup>21</sup> See the ECB's Convergence Report, May 2010, p. 21.

<sup>22</sup> See for instance paragraph 3 of ECB Opinion CON/2007/8.

<sup>23</sup> See for instance paragraph 4.2(c) of ECB Opinion CON/2008/16.