



OPINION OF THE EUROPEAN CENTRAL BANK
of 5 June 2013
on changes to the governance of the Central Bank of Cyprus
(CON/2013/41)

Introduction and legal basis

On 18 April 2013, the European Central Bank (ECB) received a request from the President of the House of Representatives of the Republic of Cyprus (hereinafter ‘the consulting authority’) for an opinion on a proposed amendment to the Central Bank of Cyprus Laws of 2002 to 2007¹. On 16 May 2013, the ECB received a revised version and, on 31 May 2013, a further revised version of the proposed amendment (hereinafter the ‘draft law’), and it is this last version which forms the basis for this opinion.

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 (hereinafter the ‘Treaty’) and the third 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 provisions², as the draft law relates to the Central Bank of Cyprus (CBC). 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

The draft law provides for the following:

- 1.1 The composition of the CBC’s Board of Directors (hereinafter the ‘Board’) is modified by providing for seven directors instead of five, in addition to the Governor and the Deputy Governor. Two of the directors will be executive directors, while the remaining five will be non-executive directors.
- 1.2 Remuneration and other terms of tenure of the executive directors and the remuneration of the non-executive directors are to be set by the Council of Ministers at the time of the directors’ appointment.
- 1.3 The number of annual mandatory meetings of the Board is increased from six to twelve.
- 1.4 The quorum for meetings of the Board is increased from four to five members.

¹ Law 138(I)/2002 as amended and currently in force.

² OJ L 189, 3.7.1998, p. 42.

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- 1.5 Decisions relating to the CBC's policy, including licensing of banking institutions and amendments to existing banking licences, are to be adopted by the Governor with the approval of the Board.
- 1.6 The Board will assign specific duties to the executive directors who, in turn, will assist the Governor in the management, supervision and control of the CBC's operations. Executive directors will be employed on a full-time basis.
- 1.7 The composition of the CBC's Personnel Committee is augmented by the inclusion of the two executive directors, and the quorum for meetings of the Personnel Committee is increased from three to four members.
- 1.8 An Audit Committee comprised of three members of the Board, appointed by the Board and who will have no executive powers, is to be established and its functions will be to audit compliance with the corporate governance code, supervise the carrying out of internal administrative audits and report to the Board. The Audit Committee may also use the services of an internal auditor.

2. ECB observations on the draft law

- 2.1 The ECB notes the consulting authority's aim to facilitate the smooth functioning of the CBC's decision-making bodies. It nevertheless makes the following observations to the consulting authority, for its consideration.
- 2.2 As a general remark, unless the executive directors and board members of a national central bank (NCB) are subject to the same legal requirements, and enjoy the same independence safeguards as the Governor of the NCB concerned, any provision assigning ESCB-related tasks of the Governor to an executive director, or requiring the approval of that NCB's Board for decisions of the Governor, raises concerns about the Governor's ability to independently carry out the ESCB-related tasks assigned to the Governor. This would not be compatible with Article 130 of the Treaty and Article 7 of the Statute of the European System of Central Banks and of the European Central Bank (hereinafter the 'Statute of the ESCB'). The Governor should not be influenced by an executive director or the members of the Board in the performance of ESCB-related tasks which, under national law, are assigned exclusively to the Governor.
- 2.3 The ECB considers that the draft law is unclear with regard to the nature of the executive directors' powers and the division of competences between the Board and the Governor. In the case of Cyprus, the ECB understands that the competences of the CBC's Governor stem both from primary Union law – in particular the Statute of the ESCB – and from the Constitution of the Republic of Cyprus³. Although the draft law purports to vest two members of the Board with executive powers, in addition to the Governor, it does not specify the corporate governance arrangements applicable to the CBC once the draft law has entered into force. In the ECB's view, the draft law should

³ It follows from Article 119 of the Constitution of the Republic of Cyprus that the Governor and Deputy Governor are independent State officials, with clearly circumscribed powers and tasks. The same provision also provides that the Governor shall be in charge of the management of the CBC and shall exercise all powers and perform all functions and duties within the scope of the CBC's competences.

provide clarity in terms of: (a) the precise scope of the powers and tasks to be assigned to the executive directors, (b) the limits of the competence of the executive directors when assisting the Governor, in particular as regards whether the executive directors will have decision-making powers⁴, and (c) the position of the proposed executive directors in the CBC's organisational structure, for instance, whether or not CBC staff members will report directly to the executive directors. In particular, the independence of the Governor of the CBC should be reinforced by ensuring that the assistance provided by the executive directors to the Governor should be conducted under the supervision of the Governor. Without clarity in these respects, the ECB is concerned that the CBC's decision-making processes will be undermined.

- 2.4 Clarification of the division of competences between the Board and the Governor is also necessary in order to ensure that the draft law does not interfere with central bank independence requirements. The ECB notes that, under Sections 15 and 17 of the Central Bank of Cyprus Law, (a) the Board has no competence in relation to matters which fall within the fields of competence of the European System of Central Banks (ESCB); and (b) the Board, when exercising its duties and tasks, should take due account of the Governor's role as a member of the Governing Council and the General Council of the ECB. Sections 17 and 17A as amended or introduced by the draft law provide that the proposed amendments are without prejudice to the powers of the ESCB and the ECB, and to the Treaty and the Statute of the ESCB. Notwithstanding this, the ECB invites the consulting authority to clarify the interplay between the powers newly granted to two of the members of the Board and the proposed governance structure's compliance with the requirements of central bank independence.
- 2.5 The ECB would like to point to the fact that there are currently a number of vacancies on the Board. Against this background, it is unclear why the number of Board members is being increased, taking into account: (a) the appointment of executive directors; and (b) the requirement for the approval of the Board as regards decision-making in implementing the CBC's policy. Central bank independence needs a stable legal framework for the central bank's functioning. Frequent changes to the legal framework may adversely affect the organisational and governance stability of an NCB and could therefore affect its institutional independence.
- 2.6 The ECB also has concerns about measures which might affect the personal independence of the Board members. To protect the CBC's autonomy in staff matters, which is part of the principle of central bank independence under Article 130 of the Treaty, the Cypriot authorities have an obligation to ensure that any amendment to the legislative provisions on the remuneration of the CBC's Board members is decided in cooperation with the CBC, taking due account of the CBC's views⁵. Furthermore, in order to comply with the Treaty requirements for the personal independence of the members of an NCB's decision-making bodies who are involved in the

⁴ For instance, Article 17, as amended, requires the Board's approval for decisions laying down *and* applying the CBC's policy.

⁵ See, paragraph 3.4 of ECB Opinion CON/2010/56. All ECB opinions are published on the ECB's website at www.ecb.europa.eu.

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performance of ESCB-related tasks, any adjustments to salaries should not affect the terms under which the members concerned were appointed⁶.

- 2.7 In light of the above concerns, the ECB urges the consulting authority to take appropriate steps in order to preserve the independence of the CBC and the members of its decision-making bodies involved in the performance of ESCB-related tasks.

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

Done at Frankfurt am Main, 5 June 2013.

[signed]

The President of the ECB

Mario DRAGHI

⁶ See, for example, paragraph 3.5 of ECB Opinion CON/2010/56.