



## **OPINION OF THE EUROPEAN CENTRAL BANK**

**of 26 June 2014**

**on a systemic risk committee**

**(CON/2014/46)**

### **Introduction and legal basis**

On 28 March 2014, the European Central Bank (ECB) received two requests from the Luxembourg Ministry of Finance: one for an opinion on a draft law establishing a systemic risk committee (hereinafter the ‘first draft law’) and another for an opinion on a draft law implementing Directive 2013/36/EU of the European Parliament and of the Council<sup>1</sup> (hereinafter the ‘second draft law’).

The ECB’s competence to deliver an opinion on the first and second draft laws is based on Article 127(4) and 282(5) of the Treaty on the Functioning of the European Union and the third, fourth and sixth indents of Article 2(1) of Council Decision 98/415/EC<sup>2</sup>, since the two draft laws relate to the Banque centrale du Luxembourg (BCL) and to statistics and 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 first draft law**

1.1 In order to implement Recommendations ESRB/2011/3<sup>3</sup> and ESRB/2013/1<sup>4</sup>, the first draft law establishes a systemic risk committee (hereinafter the ‘committee’) with four members: (a) the member of the government responsible for the financial sector, who shall be the chair; (b) the director general of the BCL, who replaces the chair in case of absence; (c) the director general of the Financial Sector Supervisory Commission (‘CSSF’); and (d) the director of the Insurance

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<sup>1</sup> Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (OJ L 176, 27.6.2013, p. 338).

<sup>2</sup> Council Decision 98/415/EC of 29 June 1998 on the consultation of the European Central Bank by national authorities regarding draft legislative provisions (OJ L 189, 3.7.1998, p. 42).

<sup>3</sup> Recommendation ESRB/2011/3 of the European Systemic Risk Board of 22 December 2011 on the macro-prudential mandate of national authorities (OJ C 41, 14.2.2012, p. 1). Available on the European Systemic Risk Board’s website at [www.esrb.europa.eu](http://www.esrb.europa.eu).

<sup>4</sup> Recommendation ESRB 2013/1 of the European Systemic Risk Board of 4 April 2013 on intermediary objectives and instruments of macro-prudential policy (OJ C 170, 15.6.2013, p. 1).

Commission (IC)<sup>5</sup>. The BCL, subject to the authority of its director general, acts as secretary to the committee and is supported in this capacity by one person designated by each of the members of the committee. All decisions of the committee are adopted by unanimous vote<sup>6</sup>.

- 1.2 The first draft law entrusts to the committee the task of coordinating the implementation of macro-prudential policy, with a view to safeguarding the stability of Luxembourg's financial system<sup>7</sup>. By virtue of Article 1(2) of the first draft law, this objective is without prejudice to the powers vested in the ECB and in the BCL as members of the European System of Central Banks (ESCB) and the Eurosystem, and those vested in the BCL pursuant to the Law of 23 December 1998 concerning the monetary status and the Central Bank of Luxembourg<sup>8</sup> (hereinafter 'the Organic Law')<sup>9</sup>. To this end, the committee pursues intermediate objectives and periodically assesses the suitability of these objectives, as well as the effectiveness and efficiency of the macro-prudential instruments chosen<sup>10</sup>.
- 1.3 In order to accomplish its mission, the committee may, inter alia, carry out the following tasks: (a) identify, assess and monitor risks to financial stability; (b) designate systemically important financial institutions and structures in Luxembourg; (c) issue notices, warnings regarding high risks to financial stability, and recommendations addressed to the CSSF, IC, BCL and other players within the financial sector, including credit institutions, insurance and reinsurance companies, investment funds, payment systems, and securities settlement systems, that are capable, either collectively or individually, of having a negative impact on the financial system or one of its components<sup>11</sup>; (d) assess and monitor responses made by recipients referred to under item (c) above in accordance with the 'comply or explain' principle<sup>12</sup>; and (e) support cooperation and information exchange at national and international level, especially with the European Systemic Risk Board (ESRB).
- 1.4 The committee may request the authorities represented on the committee and any other national entities to provide all economic and financial information necessary for it to fulfil its tasks, including macroeconomic data and prudential information regarding individual financial institutions or market infrastructures<sup>13</sup>.

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5 Article 3(1) of the first draft law.

6 Article 3(6) of the first draft law.

7 Article 1(1) of the first draft law.

8 Law of 23 December 1998 concerning the monetary status and the Central Bank of Luxembourg, as modified by the Law of 13 July 2007, the Law of 24 October 2008 and the Law of 10 November 2009.

9 Article 1(2) of the first draft law.

10 Article 1(4) of the first draft law.

11 Article 4 of the first draft law.

12 *Ibid.*

13 Article 5 of the first draft law.

## 2. Purpose of the second draft law

- 2.1 The second draft law implements Directive 2013/36/EU of the European Parliament and of the Council<sup>14</sup> into Luxembourg law. It also designates the CSSF as the competent authority in the context of the Single Supervisory Mechanism (SSM).
- 2.2 The second draft law appoints the CSSF as the ‘designated authority’ within the meaning of Articles 131, 133 and 136 of Directive 2013/36/EU and Article 458 of Regulation (EU) No 575/2013 of the European Parliament and of the Council<sup>15</sup>. When the CSSF acts in this capacity with respect to capital conservation buffers, countercyclical capital buffers, buffers for systemically important institutions, systemic risk buffers and macro-prudential risks identified at national level, it makes its decisions following negotiation with the BCL in order to reach a common position and, depending on the case at hand, after seeking the opinion of the committee or taking into account its recommendations.
- 2.3 The second draft law also amends the Law of 23 December 1998 establishing a financial sector supervisory commission<sup>16</sup>, in order to authorise the exchange of information with the committee.

## 3. General observations

- 3.1 The ECB welcomes that the first draft law establishes the committee, ensures that all the relevant authorities and institutions involved in macro-prudential policy are represented on the committee, and defines its objectives, mission and powers in line with the guiding principles expressed in Recommendation ESRB/2011/3 and Recommendation ESRB/2013/1.
- 3.2 The ECB also welcomes that the second draft law implements Directive 2013/36/EU in Luxembourg law, including its optional provisions. In particular, it provides the CSSF, when acting in its capacity as designated authority, in close coordination with the BCL, on the one hand, and the ECB, on the other hand, with the broadest possible range of macro-prudential tools, including the capital conservation buffer, the countercyclical capital buffer, the global systemically important institution (G-SII) buffer, the other systemically important institution (O-SII) buffer and a systemic risk buffer.
- 3.3 The establishment of the committee and the cooperation arrangement between the CSSF, the BCL and the committee established pursuant to the second draft law are without prejudice to the

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<sup>14</sup> Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (OJ, L 176, 27.6.2013, p. 338).

<sup>15</sup> Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) 648/2012 (OJ L 176, 27.6.2013, p. 1).

<sup>16</sup> Law of 23 December 1998 establishing a financial sector supervisory commission (‘Commission de surveillance du secteur financier’), as amended.

procedures provided for in Article 5 of Council Regulation (EU) No 1024/2013<sup>17</sup> for close cooperation between the CSSF, in continuous close coordination with the BCL, and the ECB in respect of macro-prudential tasks and tools. This national institutional framework is also without prejudice to the ECB's power to act in the CSSF's stead and to apply higher requirements and more stringent measures, in accordance with Articles 5(2) and 9(1) of Council Regulation (EU) No 1024/2013, on the basis of close coordination with the CSSF.

#### **4. Effective macro-prudential policy framework**

An effective macro-prudential policy framework must be designed in such a way as to foster the ability and willingness of the authority entrusted with macro-prudential policy to act. The framework needs to foster, in particular, the authority's ability to act in the face of evolving systemic threats, ensuring the authority has access to information and that the authority has an appropriate range of macro-prudential instruments. It also needs to give assurances that it will act if necessary and offset any biases occurring due to its inaction or insufficiently timely action arising from difficulties in quantifying the benefits of macro-prudential action, and that are often exacerbated by financial industry lobbying, political pressures, and the need for coordination among agencies<sup>18</sup>. The following shortcomings should be addressed with a view to ensure that the institutional framework provided for in the first and second draft laws would entail effective macro-prudential policies in Luxembourg: (a) the limited role of the BCL in the field of macro-prudential policy; (b) the limited powers of the committee, including its power to collect information; (c) the voting arrangements; (d) the lack of clarity as regards the committee's functions; and (e) the committee's disclosure policy. These issues are discussed in the sections below.

#### **5. Leading role of the BCL**

- 5.1 The first draft law provides that the BCL shall act as secretariat to the committee, but shall not receive any other preferential treatment as compared to the other institutions represented on the committee, whether in terms of representation, voting arrangements, the power to put forward proposals or the allocation of specific macro-prudential tasks. The second draft law endows the BCL with an insufficient role as regards countercyclical capital buffers, buffers for systemically important institutions, systemic risk buffers and other macro-prudential measures described under Article 458 of Regulation (EU) No 575/2013.
- 5.2 In principle, the ECB and the national central banks (NCBs) should play a leading role in macro-prudential oversight, given their expertise and existing responsibilities in the area of financial

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<sup>17</sup> Council Regulation (EU) No 1024/2013 of 15 October 2013 conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions (OJ L 287, 29.10.2013, p. 63).

<sup>18</sup> See the International Monetary Fund (IMF)'s 'Key Aspects of Macroprudential Policy' of 10 June 2013, in particular paragraphs 71 and 87; and the IMF's 'Implementing Macroprudential Policy - Selected Legal Issues' of 17 June 2013, in particular paragraph 35. Available on the IMF's website at [www.imf.org](http://www.imf.org).

stability<sup>19</sup>. This is particularly the case for the BCL, which is tasked with the supervision of market liquidity<sup>20</sup> and has a general mandate to contribute to financial stability<sup>21</sup>.

- 5.3 The preparatory work for the first<sup>22</sup> and second<sup>23</sup> draft laws explain that the BCL's leading role would come about as a result of: (a) the BCL acting as chair in the absence of the chairman; (b) the BCL acting as the secretariat of the committee; and (c) the BCL being a party to the cooperative arrangement under the second draft law. However, these arguments are not convincing. First of all, since the committee only meets a few times a year<sup>24</sup>, the likelihood that the chair will be absent is limited. Second, the central bank's leading role in the field of macro-prudential policy may not result from the (ancillary) role played by the NCB in the implementation of some of the provisions of Directive 2013/36/EU of the European Parliament and of the Council<sup>25</sup> and Regulation (EU) No 575/2013 of the European Parliament and of the Council<sup>26</sup>. Third, as echoed in the ECB's previous opinions issued in respect of systemic risk committees chaired by ministers of finance with the NCB acting as secretariat<sup>27</sup>, the allocation of the secretariat function to the BCL does not in itself amount to a leading role on the part of the NCB as recommended by the ESRB. In France, the leading macro-prudential role of the Banque de France results from its additional tasks in this field. These comprise identifying and monitoring systemic risks, contributing to the implementation of the committee's decisions and making proposals to the committee on the use of specific macro-prudential instruments<sup>28</sup>. In Germany, the leading role of the Deutsche Bundesbank results from its tasks in identifying and analysing risks and providing analytical support to the committee. The Deutsche Bundesbank also has a right of veto as regards the adoption and publication of warnings and recommendations and the adoption of the annual report<sup>29</sup>. In the light of the above, the ECB strongly recommends that the Luxembourg legislator revisits the extent of the tasks entrusted to the BCL in order to effectively bolster its leading role in macro-prudential policy.
- 5.4 From an operational and financial point of view, the allocation of new tasks to an NCB should not affect its ability to carry out its existing tasks. It is thus important that the BCL's involvement in the performance of the committee's mandate or the discharge of any additional tasks that may be

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19 See paragraph 2.3 of Opinion CON/2014/21. All ECB opinions are published on the ECB's website at [www.ecb.europa.eu](http://www.ecb.europa.eu).

20 See Article 2(4) of the Organic Law.

21 See Article 2(6) of the Organic Law.

22 See page 8 of the preparatory work for the first draft law.

23 See page 70 of the preparatory work for the second draft law.

24 See Article 3(12) of the first draft law. The committee shall meet every six months, or when required, upon request of its President or two of its members.

25 Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (OJ L 176, 27.6.2013, p. 338).

26 Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (OJ L 176, 27.6.2013, p. 1).

27 See Opinion CON/2012/106 and Opinion CON/2012/55.

28 See paragraph 1.3 and paragraph 5 of Opinion CON/2012/106.

29 See paragraph 1.2.2 of Opinion CON/2012/55.

entrusted to the BCL with regard to macro-prudential policy does not affect the BCL's institutional, functional and financial independence, or that of its governor, or the performance by the ESCB of its tasks under the Treaty and the Statute of the European System of Central Banks and of the European Central Bank. Financial independence, which is an element of the principle of central bank independence referred to in Article 130 of the Treaty, requires that an NCB must have sufficient means to carry out its national tasks as well as its ESCB-related tasks. The ECB has consistently expressed its concern that, when allocating additional tasks to NCBs, it must be ensured that the NCB is able to fulfil its mandate, both operationally, in terms of manpower, and financially, in terms of appropriate financial resources<sup>30</sup>. The ECB welcomes that Article 1(2) of the first draft law provides that the committee's macro-prudential objective is without prejudice to the powers of the BCL and the ECB with respect to this objective. However, for reasons of legal certainty, the abovementioned provision should be accompanied by an explicit provision stating that the committee's recommendations addressed to the BCL are without prejudice to the principle of central bank independence under Article 130 of the Treaty.

## **6. Powers of the committee**

- 6.1 In order to achieve its objectives, the committee only has the right to issue opinions and warnings and address recommendations, either to the authorities represented on the committee or to specific financial players. Accordingly, the committee exclusively relies on the enforcement powers of the authorities represented on it. Such an approach, without any enforcement powers for the committee itself, undermines the committee's ability to influence the scope of regulation or create new macro-prudential instruments in reaction to changing circumstances, thus also restricting its ability to act in the field of macro-prudential policy.
- 6.2 In the same vein, the committee may only obtain information and statistics collected by the institutions represented on the committee and other domestic institutions in accordance with the existing institutional framework, but may not request information from agents falling outside the scope of the reporting requirements. This limits the committee's access to information, which may be of relevance with regard to its policy formulation.
- 6.3 Furthermore, based on the restrictions currently laid down in the laws governing the BCL and the IC<sup>31</sup>, information and statistics may only be collected, used and shared in the context of the BCL's and the IC's respective tasks. It is therefore not entirely clear whether such information and data, in particular those concerning individual entities overseen by the BCL, may be legally passed on only

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<sup>30</sup> See paragraph 2.2 of Opinion CON/2014/27.

<sup>31</sup> See Article 27(3) (on information provided by payment and securities settlement systems as well as issuers of payment instruments to assess their efficiency and safety) and Article 33(2) (organising the exchange of information with the CSSF, the National Institute for Statistic and Economic Studies (STATEC) and the IC 'to the extent necessary for the performance of its tasks') of the Organic Law; and Article 15(4) of the Law of 6 December 1991 on the insurance sector (as amended).

to the committee in the context of the latter's macro-prudential policy mandate<sup>32</sup> or whether it may also be subsequently circulated to other institutions active in this field. The ECB therefore recommends that the Luxembourg legislator should clarify this point in the laws governing the BCL and the IC and ensure that information concerning individual entities overseen by the BCL is shared only with the committee. As noted in paragraph 1.2 above, the requirement for exchange of information stipulated in the first draft law does not prejudice the tasks performed by BCL as an integral part of the Eurosystem.

- 6.4 However, the issue described above does not apply to the CSSF, since the second draft law formally authorises the CSSF to exchange information with the committee<sup>33</sup>.

## **7. Voting arrangements**

The committee's decisions are to be taken unanimously. In practice, this voting arrangement gives each member of the committee a right of veto, which could cause a risk of paralysis in macro-prudential policy. This risk may materialise if the committee, which has exclusive competence in respect of macro-prudential policy, is unable to reach a unanimous decision. In such circumstances, the authorities represented on the committee regain the ability to act individually on the basis of their shared competence with regard to financial stability.

## **8. Lack of clarity as regards the functions of the committee**

In accordance with best practice, the functions necessary to implement macro-prudential policy fall into three broad categories: (a) identification of systemic risks; (b) formulation of a policy response; and (c) mitigation of systemic risk, or implementation of the policy response, through rule-making, supervision and enforcement<sup>34</sup>. However, these functions are contained in various different provisions in the first draft law: the enforcement function is contained in the committee's mission statement in Article 1(1); the formulation of policy response is contained in Article 1(3), which mentions 'the pursuit of intermediary objectives'; and the identification and monitoring of risks is enumerated among the committee's powers in Article 2. For the sake of clarity, the ECB recommends consolidating all aspects of the committee's functions in one provision. Contrary to what the mission statement seems to imply, these functions are not restricted to coordinating the implementation of the macro-prudential policy by the authorities represented on the committee.

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<sup>32</sup> See the IMF's 'Implementing Macroprudential Policy - Selected Legal Issues', of 17 June 2013. See in particular paragraph 36.

<sup>33</sup> See Article 60 of the second draft law.

<sup>34</sup> See the IMF's 'Implementing Macroprudential Policy- Selected Legal Issues' of 17 June 2013. See in particular paragraphs 16 and 17.

## 9. Transparency of macro-prudential policy

- 9.1 Section 1, Recommendation D of Recommendation ESRB/2011/3 stipulates that macro-prudential decisions and the reasons for making them should be made public in a timely manner, unless there are risks to financial stability in doing so. Such transparency, which supports accountability mechanisms, is of the utmost importance since it also ensures that authorities' policies and actions are fully explained to and understood by stakeholders.
- 9.2 Article 3(6) of the first draft law merely stipulates that 'the systemic risk committee shall take decisions on whether to publish notices, alerts and recommendations by unanimous vote'. The ECB recommends that this provision should be amended in order to create greater transparency as regards macro-prudential policy decisions, which should not be left entirely to the discretion of the authorities.

## 10. Strengthening the institutional framework

- 10.1 In view of the shortcomings described above, the ECB urges the Luxembourg legislator to thoroughly review the first draft law in order to strengthen the overall effectiveness of the institutional framework for macro-prudential policy in Luxembourg. For this purpose, the ECB strongly recommends that: (a) the BCL's leading role in macro-prudential policy should be bolstered; (b) either the BCL, in its leading role in respect of the macro-prudential policy or the committee, should be endowed with direct enforcement powers, including those relating to collecting information and statistics; (c) voting and disclosure arrangements should be more flexible; and (d) the overall clarity with regard to the committee's role should be improved. Unless such amendments aim to accommodate the view expressed by the ECB in this opinion, a further consultation with the ECB on the revised first draft law will be required.
- 10.2 It is noteworthy that in its opinion issued on the first draft law<sup>35</sup>, the State Council of Luxembourg also discusses: (a) the overall weakness of the committee, which has no regulatory and enforcement powers of its own; (b) the lack of a clear legal basis for the exchange of aggregated and individual information between the committee and its members; and (c) the ability of the committee to address recommendations to individual institutions, including with regard to shadow banking. In view of these concerns, the State Council of Luxembourg recommends limiting the scope of the committee's action to mere recommendations exclusively addressed to the existing institutions in the context of the sector-specific approach to financial sector oversight. In addition, the ECB considers that the State Council's proposal aiming at removing any mention of the Governor's hierarchical power in relation to the secretariat of the committee is not compatible with the independence of the BCL and its Governor.

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<sup>35</sup> Opinion of the Luxembourg State Council No. 50.541, available on the State Council's website at [www.conseil-état.public.lu](http://www.conseil-état.public.lu). The Luxembourg State Council has not yet issued its opinion on the second draft law.

## ECB-PUBLIC

The ECB advises the Luxembourg legislator to proceed with caution as regards these recommendations, which would unduly weaken the adopted macro-prudential policy framework, resulting, inter alia, in an inappropriate shift towards micro-prudential policy.

- 10.3 This opinion is without prejudice to the conclusions of the ESRB's follow-up assessment, which will be prepared pursuant to Article 17 of Regulation (EU) No 1092/2010 of the European Parliament and of the Council<sup>36</sup>.

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

Done at Frankfurt am Main, 26 June 2014.

[signed]

*The President of the ECB*

Mario DRAGHI

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<sup>36</sup> Regulation (EU) No 1092/2010 of the European Parliament and of the Council of 24 November 2010 on European Union macro-prudential oversight of the financial system and establishing a European Systemic Risk Board (OJ L 331, 15.12.2010, p. 1).