



EUROPEAN CENTRAL BANK

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ECB-PUBLIC

OPINION OF THE EUROPEAN CENTRAL BANK

of 17 February 2017

on conferring new mortgage credit-related tasks on the Central Bank of Cyprus

(CON/2017/3)

Introduction and legal basis

On 27 January 2017 the European Central Bank (ECB) received a request from the Cypriot Ministry of Finance for an opinion on a draft law on credit agreements for consumers relating to residential immovable property (hereinafter the 'draft law').

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 indent of Article 2(1) of Council Decision 98/415/EC¹, 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

- 1.1. The purpose of the draft law is to transpose Directive 2014/17/EU of the European Parliament and of the Council² into Cypriot law, with a view to enhancing consumer protection in respect of consumer loans for the acquisition of real estate or which are secured by residential immovable property. Under the Directive, Member States must designate a national competent authority to ensure the application and enforcement of its provisions. Such competent authorities must either be public authorities or entities recognised by national law or by public authorities expressly empowered for that purpose by national law. Such competent authorities may not be creditors, credit intermediaries or appointed representatives³.
- 1.2. In the draft law, the CBC is designated as a competent authority, together with the Consumer Protection Service of the Republic of Cyprus (hereinafter the 'Service'), responsible for the application and enforcement of certain of the rules that implement Directive 2014/17/EU into national legislation. More specifically, the CBC and the Service are jointly responsible for: (a) the adoption of criteria determining a representative example in relation to certain information to be

¹ 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).

² Directive 2014/17/EU of the European Parliament and the Council of 4 February 2014 on credit agreements for consumers relating to residential immovable property and amending Directives 2008/48/EC and 2013/36/EU and Regulation (EU) No 1093/2010 (OJ L 60, 28.2.2014, p. 34).

³ See Article 5(1) of Directive 2014/17/EU.

included in advertising concerning credit agreements; (b) the provision of general information, including warnings, and adequate explanations to consumers on credit agreements; (c) the use of the terms 'independent advice' and 'independent advisor' in the course of the provision of advisory services by creditors; (d) the use by the parties to a credit agreement of clear, accessible, objective and verifiable indexes or reference rates to calculate the borrowing rate; and (e) cooperation with the competent authorities of other Member States.

While the Service is designated as the competent authority for certain matters (i.e. the financial education of consumers, the requirements to be met in advertising and marketing communications, pre-contractual information, the requirement to inform consumers of the procedure for internal registration of complaints about credit intermediaries and the means of recourse to out-of-court complaint and redress procedures, certain matters related to foreign currency loans, and early repayment), all remaining requirements not specifically attributed to the Service or jointly to the Service and the CBC fall within the exclusive competence of the CBC. These include the monitoring of conduct of business obligations by creditors and credit intermediaries when providing credit to consumers, as well as the knowledge and competence requirements for their staff, ensuring that relevant information is provided free of charge to consumers, the calculation of the annual percentage rate of charge, the assessment of consumers' creditworthiness, ensuring access for all creditors of all Member States to the databases used in Cyprus, the provision of advisory services by creditors and credit intermediaries, certain matters related to foreign currency loans, and certain requirements on the sound execution of credit agreements and related rights including matters related to arrears and foreclosure.

- 1.3. Furthermore, the draft law designates the CBC as the competent authority for the licensing and supervision of credit intermediaries and of non-credit institutions which intend to provide credit under the draft law. In particular, the CBC will be responsible for: (a) licensing credit intermediaries and non-credit institutions; (b) ensuring that all licensed credit intermediaries and non-credit institutions comply with the professional requirements set out in the draft law; (c) refusing or withdrawing the license of credit intermediaries and non-credit institutions; (d) imposing sanctions in case of infringements; (e) carrying out supervisory controls; and (f) carrying out notification procedures which allow licensed credit intermediaries to operate throughout the Union.

2. Observations

2.1. General observations

- 2.1.1. This opinion does not address whether the draft law effectively implements Directive 2014/17/EU into Cypriot law. The ECB will only assess those provisions of the draft law that may impact on the role and tasks of the CBC as a central bank, national supervisory authority and member of the Eurosystem and the European System of Central Banks (ESCB).
- 2.1.2. The draft law broadens the CBC's current supervisory functions by assigning to it responsibility for the supervision and regulation of the market for credit agreements relating to residential immovable property. To this end, the draft law expands the categories of entities over which the CBC exercises prudential supervision to include credit intermediaries which in the course of their trade,

business or profession present or offer credit agreements to consumers, assist consumers by undertaking preparatory work in respect of credit agreements or conclude such agreements on behalf of creditors, as well as non-credit institutions which intend to grant credit pursuant to the draft law.

2.1.3. With respect to the competences entrusted to the Service by the draft law, it is noted that they result in certain powers that parallel those of the CBC. In this regard, the ECB understands that national authorities shall closely cooperate in exercising their powers without adversely affecting their respective supervisory responsibilities⁴.

2.2. *Conferral of new tasks on the CBC*

2.2.1 The ECB underlines that, in the context of a proposed conferral of tasks on a national central bank (NCB) in the ESCB, it is necessary to assess such conferral against the prohibition on monetary financing under Article 123 of the Treaty. For the purposes of that prohibition, Article 1(1)(b)(ii) of Council Regulation (EC) No 3603/93⁵ defines ‘other type of credit facility’, inter alia, as ‘any financing of the public sector’s obligations vis-à-vis third parties’.

As the objective of the monetary financing prohibition of maintaining a sound budgetary policy of Member States may not be circumvented, the task of financing measures which are normally the responsibility of the Member States, and financed from their budgetary sources rather than by the NCBs, must not be entrusted to NCBs by law. In order to decide what constitutes a form of financing of the public sector’s obligations vis-à-vis third parties – which can be translated as the provision of central bank financing outside the scope of the central bank tasks – an assessment of whether the task to be undertaken by an NCB is a central bank task or a government task, i.e. a task within the responsibility of the Member States, needs to be carried out on a case-by-case basis. In other words, sufficient safeguards must be in place to ensure that circumventions of the objective of the monetary financing prohibition of maintaining a sound budgetary policy of Member States do not take place.

2.2.2 As part of its discretion in the exercise of its duty, on the basis of Article 271(d) of the Treaty and Article 35.6 of the Statute of the European System of Central Banks and of the European Central Bank (Statute of the ESCB), to ensure that NCBs honour the obligations laid down by the Treaty, the Governing Council has endorsed safeguards of that kind in the form of criteria for determining what may be seen as falling within the scope of a public sector’s obligation within the meaning of Article 1(1)(b)(ii) of Regulation (EC) No 3603/93 or, in other words, constitute a government task as follows:

First, central bank tasks are in particular those tasks that are related to the tasks that have been conferred upon the ECB and the NCBs by the Treaty and the Statute of the ESCB. These tasks are

⁴ See paragraph 2 of Opinion CON/2016/23. All ECB opinions are published on the ECB’s website at www.ecb.europa.eu.

⁵ Council Regulation (EC) No 3603/93 of 13 December 1993 specifying definitions for the application of the prohibitions referred to in Articles 104 and 104b(1) of the Treaty (OJ L332, 31.12.1993, p. 1).

mainly defined in Article 127(2), (5) and (6) and Article 128(1) of the Treaty, as well as Article 22 and Article 25.1 of the Statute of the ESCB.

Second, as Article 14.4 of the Statute of the ESCB allows NCBs to perform ‘other functions’, new tasks, i.e. tasks that are not related to tasks that have been conferred upon the ECB and the NCBs, are not precluded per se. However, new tasks that are undertaken by an NCB and which are atypical of NCB tasks or which are clearly discharged on behalf of and in the exclusive interest of the government or of other public sector entities should be considered government tasks.

Third, an important criterion for qualifying a new task as atypical of an NCB task or as being clearly discharged on behalf of and in the exclusive interest of the government or other public sector entities is the impact of the task on the institutional, financial and personal independence of that NCB.

In particular, the following aspects should be taken into account:

- (a) Whether the performance of the new task creates conflicts of interest with existing central bank tasks which are not adequately addressed and does not necessarily complement those existing central bank tasks. If a conflict of interest arises between existing and new tasks, sufficient safeguards to mitigate that conflict should be in place. The complementarity between a new task and the existing central bank tasks should not be interpreted broadly, so as to lead to the creation of an indefinite chain of ancillary tasks. Such complementarity should be examined also in relation to the financing of those tasks.
- (b) Whether without new financial resources the performance of the new task is disproportionate to the NCB’s financial or organisational capacity and may negatively impact on the capacity to perform properly the existing central bank tasks.
- (c) Whether the performance of the new task fits into the institutional set-up of the NCB in light of central bank independence and accountability considerations.
- (d) Whether the performance of the new task harbours substantial financial risks.
- (e) Whether the performance of the new task exposes the members of the NCB decision-making bodies to political risks which are disproportionate and may also impact on their personal independence and, in particular, on the guarantee of term of office set out in Article 14.2 of the Statute of the ESCB.

2.3 *Specific observations*

On the basis of the criteria set out above, the following paragraphs assess whether the CBC’s new tasks are in line with the monetary financing prohibition.

2.3.1 *Tasks related to the tasks conferred upon the ECB and the NCBs by the Treaty and the Statute of the ESCB*

The authorisation and supervision of credit intermediaries and non-credit institutions, as well as the oversight and regulation of the market for credit agreements relating to residential immovable

property, can be considered as tasks related to those referred to in Article 127(5) of the Treaty, to the extent that these complement the supervisory tasks exercised by an NCB⁶, particularly where that NCB already exercises tasks of a similar nature⁷. In this respect, it is noted that the CBC already supervises credit institutions and other financing institutions, such as credit acquiring companies⁸ and financial leasing companies⁹.

2.3.2 *Tasks which are atypical of NCB tasks*

A number of Member States have conferred on their NCBs supervisory tasks related to the provision of consumer credit¹⁰. In addition, without prejudice to Article 14.4 of the Statute of the ESCB, the ECB has generally accepted the allocation of consumer protection-related tasks to NCBs based on the understanding that such tasks complement existing supervisory powers (and might be linked to the NCB's overall responsibility for supervision of the financial market¹¹) and thus contribute to the soundness of the financial market and the preservation of confidence in the marketplace¹². It follows that, as regards their nature, the new tasks conferred upon the CBC by the draft law cannot be regarded as atypical of a central bank, nor as being discharged in the exclusive interest of the government.

2.3.3 *Extent to which performance of the new task creates conflicts of interest with existing central bank tasks*

The ECB notes that under the draft law the CBC will be responsible for supervising the conduct of creditors and credit intermediaries towards consumers, including their policies in respect of arrears and foreclosure. While these tasks seem to be broadly of the same nature as the supervisory tasks already performed by the CBC, the ECB notes that conflicts of interest may arise. As the national authority responsible for supervising the financial markets, the CBC will be required to mitigate any potential conflict of interest between its new consumer protection tasks and its supervision and financial stability mandates. The ECB recommends that sufficient mitigation measures are put in place in this respect¹³.

2.3.4 *Extent to which performance of the new task is disproportionate to the CBC's financial or organisational capacity*

The principle of financial independence requires that the Member States may not put their NCBs in a position where they have insufficient financial resources to carry out not only their ESCB-related tasks, but also their national tasks, both from an operational and financial perspective.

6 See paragraph 4.3 of Opinion CON/2016/34.

7 See paragraph 3.3 of Opinion CON/2016/31 and paragraph 3.1.2 of Opinion CON/2015/45.

8 See the Law on the regulation of companies acquiring credit and related matters of 2015 (169(I)/2015) and Opinion CON/2015/45.

9 See the Law on the regulation of financial leasing of 2016 (72(I)/2016) and Opinion CON/2015/37.

10 See paragraph 3.4 of Opinion CON/2015/54.

11 See paragraph 2.3 of Opinion CON/2007/29.

12 See in this regard paragraph 4.4 of Opinion CON/2016/34, paragraph 2.2.2 of Opinion CON/2016/31, paragraphs 2.1 and 2.2 of Opinion CON/2006/47, paragraph 2.3 of Opinion CON/2007/29, and paragraph 2 of Opinion CON/2009/71.

13 See paragraph 4.8 of Opinion CON/2016/34 and paragraph 2.2.2 of Opinion CON/2016/31.

Furthermore, when allocating specific non-ESCB-related tasks to the NCBs, additional personnel and financial resources must also be allocated so that these tasks may be carried out in a manner that will not affect the NCBs' operational or financial capacity to perform their ESCB-related tasks¹⁴. In this regard, notwithstanding a provision that the administrative fines imposed by the CBC in case of infringements of the draft law will be added to its revenue, it is noted that the draft law does not specify how the costs related to the supervision of credit intermediaries and non-credit institutions by the CBC are to be financed. The ECB therefore invites the consulting authority to consider establishing a cost recovery regime, e.g. requiring credit intermediaries and non-credit institutions to pay to the CBC an authorisation fee or an annual fee to cover the actual costs incurred by the CBC in the performance of its new supervisory tasks¹⁵. Once a cost recovery regime is established, the CBC would then need to arrange for the additional necessary staff with the appropriate skills that are considered essential for the supervision of these entities and institutions, in view of the need to ensure that its capacity to perform its ESCB-related tasks and existing supervisory functions would not be affected by the assumption of these new tasks¹⁶.

2.3.5 Extent to which performance of the new task fits into the CBC's institutional set-up, in light of central bank independence and accountability considerations

Given the complementarity of the new tasks with the CBC's existing supervisory powers, in particular in the field of supervision of credit institutions and other financial institutions, the new tasks would fit into the CBC's institutional set-up.

2.3.6 Extent to which the performance of tasks harbours substantial financial risks

The draft law does not contain any specific provisions on liability for the performance of supervisory tasks. The CBC's liability with regard to the supervision of credit institutions, and of any director or officer of the CBC, is excluded, unless it is proven that any act or omission in the discharge of their relevant functions and responsibilities was done in bad faith or was the result of gross negligence¹⁷. Given that liability issues could give rise to substantial financial risks for the CBC, the ECB invites the consulting authority to consider aligning the CBC's liability under the draft law with its liability concerning the supervision of credit institutions.

2.3.7 Extent to which performance of the new task exposes members of the CBC's decision-making bodies to disproportionate political risks and impacts on their personal independence

The performance of the tasks conferred under the draft law does not appear to be exposing the CBC's decision-making bodies to any disproportionate political risk or to impact their personal independence. In this respect, it is noted that the supervisory functions exercised by the CBC already include the supervision of credit institutions and other financing institutions, such as credit acquiring companies and financial leasing companies¹⁸.

14 See paragraph 3.1.6 of Opinion CON/2016/16.

15 See paragraph 4.2 of Opinion CON/2016/34.

16 See paragraph 3.1.6 of Opinion CON/2016/16 and paragraph 3.4 of Opinion CON/2016/31.

17 See Article 32(1) of the Law on the business of credit institutions of 1997 (66(I)/1997) as amended.

18 See paragraph 2.3.1 above.

2.3.8 Conclusion

Considering their nature, the CBC's new tasks of supervising and regulating the market for consumer credit agreements, as well as authorising and supervising credit intermediaries and non-credit institutions, can in principle be regarded as central bank tasks, in the sense that they would complement the CBC's existing supervisory functions. However, in addition to the foregoing, it is essential that the new role assigned to the CBC by the draft law does not have a negative impact on the institutional and financial independence of the CBC and that it does not adversely affect its capacity to carry out its ESCB- or Eurosystem-related tasks or to perform its other functions. To this end, it must be ensured that the supervisory costs incurred by the CBC in relation to its new tasks are adequately covered and that the CBC can avail itself of sufficient resources, including personnel, for the performance of its new tasks. Furthermore, it should be considered to align the CBC's liability under the draft law with its liability concerning its supervision of credit institutions, given that liability issues could give rise to substantial financial risks for the CBC. Finally, it is important to ensure that sufficient mitigation measures are in place to adequately address any potential conflict of interest between the CBC's new consumer protection tasks and its existing supervision and financial stability mandates. Consequently, the ECB invites the Cypriot authorities to consider in more depth the abovementioned aspects before the draft law is adopted.

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

Done at Frankfurt am Main, 17 February 2017.

[signed]

The President of the ECB

Mario DRAGHI