



EUROPEAN CENTRAL BANK
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Mario DRAGHI
President

Mr Sven Giegold
Member of the European Parliament
European Parliament
60, rue Wiertz
B-1047 Brussels

Frankfurt, 13 July 2015

L/MD/15/418

Re: Your letters (QZ-74, QZ-77 and QZ-79)

Honourable Member of the European Parliament, dear Mr Giegold,

Thank you for your letters, which were passed on to me by Mr Roberto Gualtieri, Chairman of the Committee on Economic and Monetary Affairs, accompanied by a cover letter dated 5 May 2015.

The negotiations between the government of the Republic of Cyprus and the programme partners (namely the European Commission, in liaison with the ECB, and the International Monetary Fund) started in June 2012 and, despite several staff-level visits to Cyprus, remained without a result until April 2013.¹

The resolution and restructuring of the Cypriot credit institutions

At that time, a disorderly default of the two largest Cypriot banks, which already faced large capital needs, would have been highly probable², unless actions were taken by the Cypriot authorities to restructure the Cypriot banking sector and obtain financial assistance.

All measures taken by the Cypriot authorities with regard to the resolution and restructuring of credit institutions were national measures that fell outside the decision-making competence of the ECB. The above

¹ The memorandum of understanding between the Cypriot authorities and the Vice-President of the European Commission, acting on behalf of the European Stability Mechanism, was signed on 26 April 2013, while a staff-level agreement was reached on 3 April 2013.

² European Commission, "The Economic Adjustment Programme for Cyprus", *European Economy – Occasional Papers*, Vol. 149, May 2013, Brussels, p. 34

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was confirmed by the General Court, a constituent court of the Court of Justice of the European Union, which held³ that any alleged damages were the consequence of the adoption and implementation of Cypriot resolution and restructuring measures. These unilateral and sovereign measures were taken by the Cypriot Parliament, the Cypriot Government and/or the Central Bank of Cyprus, the latter acting in its capacity as national resolution authority. Consequently, such national measures – and any loss allegedly linked to them – cannot be attributed to the ECB, and can be challenged solely in national courts.

As I also had the possibility to explain in detail in a recent letter of reply which I sent to your colleagues Messrs De Masi and Sylikiotis⁴, providing all required capital to the two largest Cypriot banks from public resources would have critically endangered the sustainability of Cyprus' public debt. A rapid and substantial downsizing of the banking sector, including the disposal of foreign operations of the Cypriot banks, was therefore supported by the EU/IMF programme.

The sale of the Greek operations of Laiki Bank and the Bank of Cyprus

Please note that the sale of the Greek operations of the two largest Cypriot banks (Laiki Bank and the Bank of Cyprus) did not force them into bankruptcy. Prior to the transaction, the Central Bank of Cyprus, acting as the Cypriot Resolution Authority, placed these two banks into resolution.⁵ This implies that the Central Bank of Cyprus considered the two banks to be no longer viable, or likely to be no longer viable, and that no other measures would have been sufficient to ensure compliance with minimum capital requirements.⁶ As part of the resolution plans, the sale of the Greek operations of Laiki Bank and the Bank of Cyprus was mandated by the Central Bank of Cyprus, in its capacity as the Cypriot Resolution Authority.⁷

In this context, the sale was the result of a bilateral agreement between Cyprus and Greece, the aim of which was to protect the stability of both the Greek and Cypriot banking systems.⁸ In implementing that agreement, the Bank of Greece called for expressions of interest among Greek banks to acquire the operations of Cypriot banks in Greece. On 22 March 2013, the Hellenic Financial Stability Fund approved the bid by Piraeus Bank.⁹

³ See, for example, *Ledra Advertising v. Commission and ECB*, T-289/13, ECLI:EU:T:2014:981 (under appeal).

⁴ This letter was published on 21 April 2015 and is available at http://www.ecb.europa.eu/pub/pdf/other/150420letter_de_masi_sylikiotis.en.pdf

⁵ Decree No 93 (Sales of Operations of [BoC]), *Official Gazette of the Republic of Cyprus*, 3rd Annex, Part I, No 4638, 25 March 2013, p. 739; Decree No 94 (Sales of Operations of [Laiki]), *Official Gazette of the Republic of Cyprus*, 3rd Annex, Part I, No 4638, 25 March 2013, p. 741.

⁶ Article 6(1)(a) and 6(1)(b) of the Resolution of Credit and Other Institutions Law of 2013, *Official Gazette of the Republic of Cyprus*, 22 March 2013.

⁷ Decree No 96 (Sale of Greek branches of Bank of Cyprus), *Official Gazette of the Republic of Cyprus*, 3rd Annex, Part I, No 4640, 26 March 2013, p. 745; Decree No 97 (Sale of Greek branches of Laiki Bank), *Official Gazette of the Republic of Cyprus*, 3rd Annex, Part I, No 4640, 26 March 2013, p. 749

⁸ See the Eurogroup statement on Cyprus dated 16 March 2013, p.1 and the Eurogroup statement on Cyprus dated 25 March 2013, p.1.

⁹ See Hellenic Financial Stability Fund press release dated 22 March 2013.

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As I explained in the aforementioned letter of reply to your MEP colleagues, the ECB was at no point in time party to the negotiation of the sale price, and it is not for the ECB to justify the business case and the detailed conditions, including the price, underlying the sale of the Cypriot banks' Greek operations.

Regarding your question on the accounting treatment of the transaction, it is important to note that International Financial Reporting Standards do not permit the recognition of projected future losses against which a bank would be required to hold capital upon the acquisition of assets.¹⁰ The difference between the purchase price and the current value of acquired assets and liabilities was therefore recognised as a one-off accounting profit, in the form of negative goodwill, for the acquiring bank. However, these accounting profits were only temporary and were gradually offset by losses over time. In other words, at that point in time the accounting value of the assets was significantly above their long-term economic value, as projected under the adverse scenario of the stress test exercise that constituted an important piece of information for this transaction.

Related to your assertion that this accounting profit helped Piraeus Bank escape insolvency, it is important to note that, at the time of the transaction, Piraeus Bank was compliant with the minimum capital requirements according to the publicly available data, having been recapitalised by the Hellenic Financial Stability Fund according to the asset quality review and stress test exercise carried out by the Bank of Greece.

Finally, with respect to the points you made concerning the alleged benefits that the chairman of Piraeus Bank may have received from the transaction, I would like to refer you to the competent national authorities.

Yours sincerely,

[signed]

Mario Draghi

¹⁰ For a detailed description of the accounting requirements, see IFRS 3, paragraphs 32 to 36.

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