



# **The European System of Central Banks and the Eurosystem**

**European Commission  
DG Economic and Financial Affairs**

These slides accompany the explanation of the acquis to Albania and North Macedonia and can only be used for that purpose. Their content is subject to further development of the acquis and interpretation by the Court of Justice of the European Union'

# OUTLINE

- I. EMU and euro as a Union objective**
- II. ESCB, Eurosystem, euro area**
- III. Objectives of the ESCB/Eurosystem**
- IV. Basic tasks of the ESCB/Eurosystem**
- V. Monetary functions and operations**
- VI. Prudential supervision**
- VII. Decision-making in the ESCB/Eurosystem**
- VIII. Financial provisions of the ESCB/Eurosystem**

## I. EMU with a single currency: a Union objective

Article 3 of the Treaty on the European Union:

***"The Union shall establish and **economic and monetary union** whose currency is the euro"***

- Principle of conferral of powers
- Union exclusively in charge for monetary policy (Article 3 TFEU)

## II. ESCB/Eurosystem/euro area

### ESCB (Art. 282 (1) TFEU)

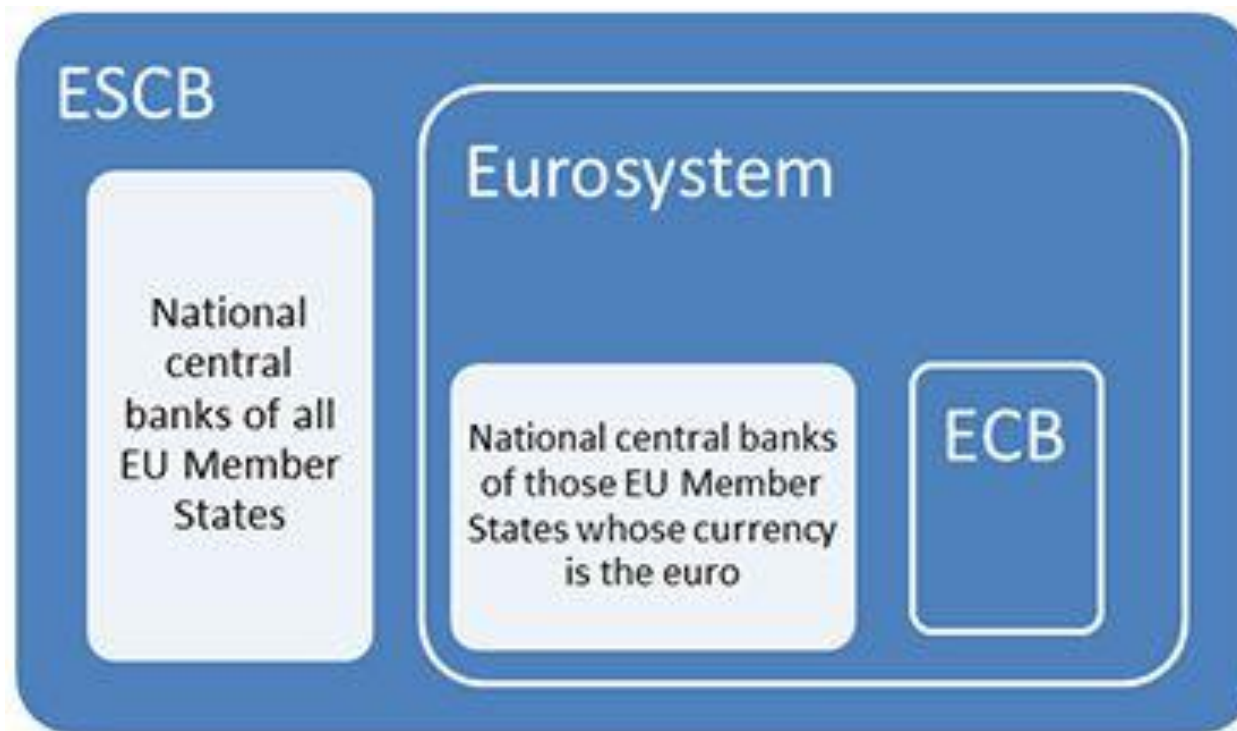
*"The European Central Bank, together with the national central banks, shall constitute the **European System of Central Banks** (ESCB)."*

### Eurosystem (Article 282 (1) TFEU)

*"The European Central Bank, together with the national central banks of the Member States whose currency is the euro, which constitute the **Eurosistem**, shall conduct the monetary policy of the Union."*

### Euro area

Consists of the EU Member States that have adopted the euro (19 out of 28 M





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## The euro area



### III. Objective(s) of the ESCB and Eurosystem

Articles 127 (1) and 282 (2) TFEU:

***"The **primary objective** of the ESCB shall be to maintain price stability"***

*"Without prejudice to that objective, it shall support the general economic policies of the Union in order to contribute to the achievement of the latter's objectives" (**secondary objective**)"*

## III. Objectives of ESCB and Eurosystem

*Governing Council in October 1998:*

***"Price stability shall be defined as a year-on-year increase in the Harmonised Index of Consumer Prices (HICP) for the euro area of below 2%. Price stability is to be maintained over the medium term."***

***The Governing Council aims to maintain inflation rates at levels below, but close to, 2% over the medium term.***



## **IV. Basic tasks of the ESCB/Eurosystem**

**Legal basis: Article 127 (2) TFEU and Article 3 of the ESCB and ECB Statutes**

- **to define and implement the monetary policy of the Union**
- **to conduct foreign-exchange operations consistent with the provisions of Article 219,**
- **to hold and manage the official foreign reserves of the Member States,**
- **to promote the smooth operation of payment systems**

## IV. Other tasks

- **Collection and compilation of statistics (Art. 5 ESCB/ECB Statute)**
- **International cooperation (Art. 6 ESCB/ECB Statute)**
- **Issuing of euro banknotes (Art. 128 TFEU, coins: Member States)**
- **Advisory functions (127 (4) TFEU)**
- **Banking supervision (127 (6) TFEU) + "SSM Regulation"**
- **Role in macroprudential policy (ESRB)**

# V. Monetary functions and operations: policy instruments

## Standing facilities

- **Deposit facility** (rates generally lower than market rates)
- **Marginal lending facility** (rates generally higher than market rates)

## Open market operations

- **Main refinancing operations** (maturity: one week) (MRO)
- **Longer-term refinancing operations** (LTRO)
- **Fine-tuning operations**
- **Structural operations**

## Minimum reserve requirements

## **V. Non standard monetary policy measures**

- **Fixed-rate, full-allotment liquidity provision**
- **Expansion of list of assets eligible as collateral**
- **Longer-term liquidity provision**
- **Liquidity provision in foreign currencies (swaps)**
- **Changes in the required reserve ratio**
- **Outright purchases of specific debt securities**

## VI. Prudential supervision

Article 127 (5) TFEU:

*"The ESCB shall **contribute to** the smooth conduct of policies pursued by the competent authorities relating to **prudential supervision** of credit institutions and the **stability of the financial system**"*

Article 127 (6) TFEU:

*"The Council by means of regulations [...] may confer **specific tasks** upon the European Central Bank concerning policies related to **prudential supervision of credit institutions** [...]"*

# VI. Prudential supervision

## Financial stability

- Overarching objective in EMU (confirmed by ECJ in Pringle)
- Operational definition ECB (Financial Stability Review):

*"Financial stability is a state whereby the build-up of systemic risk is prevented. Systemic risk can best be described as the risk that the provision of necessary financial products and services by the financial system will be impaired to a point where economic growth and welfare may be materially affected"*

# VI. Macroprudential supervision

- **Legal basis:** multiple legal bases (e.g. Council Regulation (EU) No 1024/2013, Capital Requirements Directive, Capital Requirements Regulation, ESRB Regulations, SSM Regulation)
  1. Contribute to financial stability: ECB and NCBs monitor of developments in the banking sectors of the euro area and the EU as a whole, as well as other financial sectors, to identify any vulnerabilities and check the resilience of the financial system.
  2. Facilitating exchanges between supervisors on macroprudential aspects (in European Systemic Risk Board)
  3. Taking targeted measures to address systemic risks (SSM) (e.g. buffers)

## **VI. Macroprudential supervision**

Aim:

- prevent the excessive build-up of risk, resulting from external factors and market failures, to smoothen the financial cycle (time dimension)
- make the financial sector more resilient and limit contagion effects (cross-section dimension)
- encourage a system-wide perspective in financial regulation to create the right set of incentives for market participants (structural dimension)



# VI. Microprudential supervision: SSM

## The single supervisory mechanism ("SSM")

**Composition:** European Central Bank + national competent authorities for banking supervision

**Roles:** ECB central prudential supervisor (Article 127(6) TFEU and Council Regulation (EU) No 1024/2013)

**Geographical scope:** Euro Area Member States + non-euro area Member States that choose to join the SSM via a close cooperation agreement

**Scope on substance:**

- Direct supervision of largest banks ("significant credit institutions")
- national supervisors continue to monitor the remaining smaller banks ("non-significant credit institutions").

## VI. Microprudential supervision

The ECB has the authority to:

- conduct supervisory reviews, on-site inspections and investigations
- grant or withdraw banking licences
- assess banks' acquisition and disposal of qualifying holdings
- ensure compliance with EU prudential rules
- set higher capital requirements ("buffers") in order to counter any financial risks

# Significance?

To qualify as significant, banks must fulfil at least one of these criteria. The ECB can decide at any time to classify a bank as significant to ensure that high supervisory standards are applied consistently.

## Significance criteria

### 1. Size

the total value of its assets exceeds €30 billion

### 2. Economic importance

for the specific country or the EU economy as a whole

### 3. Cross-border activities

the total value of its assets exceeds €5 billion and the ratio of its cross-border assets/liabilities in more than one other participating Member State to its total assets/liabilities is above 20%

### 4. Direct public financial assistance

it has requested or received funding from the European Stability Mechanism or the European Financial Stability Facility

A supervised bank can also be considered significant if it is one of the three most significant banks established in a particular country.

## VII. Decision-making in the Eurosystem/ESCB

### Governing Council

The Governing Council is the main decision-making body of the ECB. It consists of the six members of the Executive Board, plus the governors of the national central banks of the 19 euro area countries.

#### Responsibilities

- to adopt the guidelines and take the decisions necessary to ensure the **performance of the tasks** entrusted to the ECB and the Eurosystem;
- to formulate **monetary policy** for the euro area. This includes decisions relating to monetary objectives, key interest rates, the supply of reserves in the Eurosystem, and the establishment of guidelines for the implementation of those decisions.
- in the context of the ECB's new responsibilities related to **banking supervision**, to adopt decisions relating to the general framework under which supervisory decisions are taken, and to adopt the complete draft decisions proposed by the Supervisory Board under the non-objection procedure.

## VII. Decision-making in the Eurosystem/ESCB

### Meetings and decisions

- Frequency: twice a month (Frankfurt)
- Assessment of economic and monetary developments + monetary policy decisions every six weeks.
  - **The monetary policy decision is explained in detail at a press conference held every six weeks. The President, assisted by the Vice-President, chairs the press conference.**
  - **In addition, the ECB publishes regular accounts of the Governing Council's monetary policy meetings before the date of the next one.**
- At the other meetings, discussion of issues related to other tasks and responsibilities of the ECB and the Eurosystem.
- To ensure the separation of the ECB's monetary policy and other tasks from its supervisory responsibilities, separate meetings of the Governing Council are held.
- Rotation of voting rights

## VII. Decision-making in the Eurosystem/ESCB

### Executive Board

The Executive Board consists of the President, the Vice-President and four other members. All members are appointed by the European Council, acting by a qualified majority.

### Responsibilities

- to prepare Governing Council meetings;
- to implement monetary policy for the euro area in accordance with the guidelines specified and decisions taken by the Governing Council. In so doing, it gives the necessary instructions to the euro area NCBs;
- to manage the day-to-day business of the ECB
- to exercise certain powers delegated to it by the Governing Council. These include some of a regulatory nature.

## VII. Decision-making on macroprudential supervision

**Governing Council** is responsible for taking macro-prudential decisions.

These decisions apply to all countries and banks covered by the Single Supervisory Mechanism (SSM), i.e. the euro area countries and those other EU countries whose national authorities have signed close cooperation agreements with the ECB

## VII. Decision-making on microprudential supervision

**Supervisory Board ("SB"):** internal body of the ECB

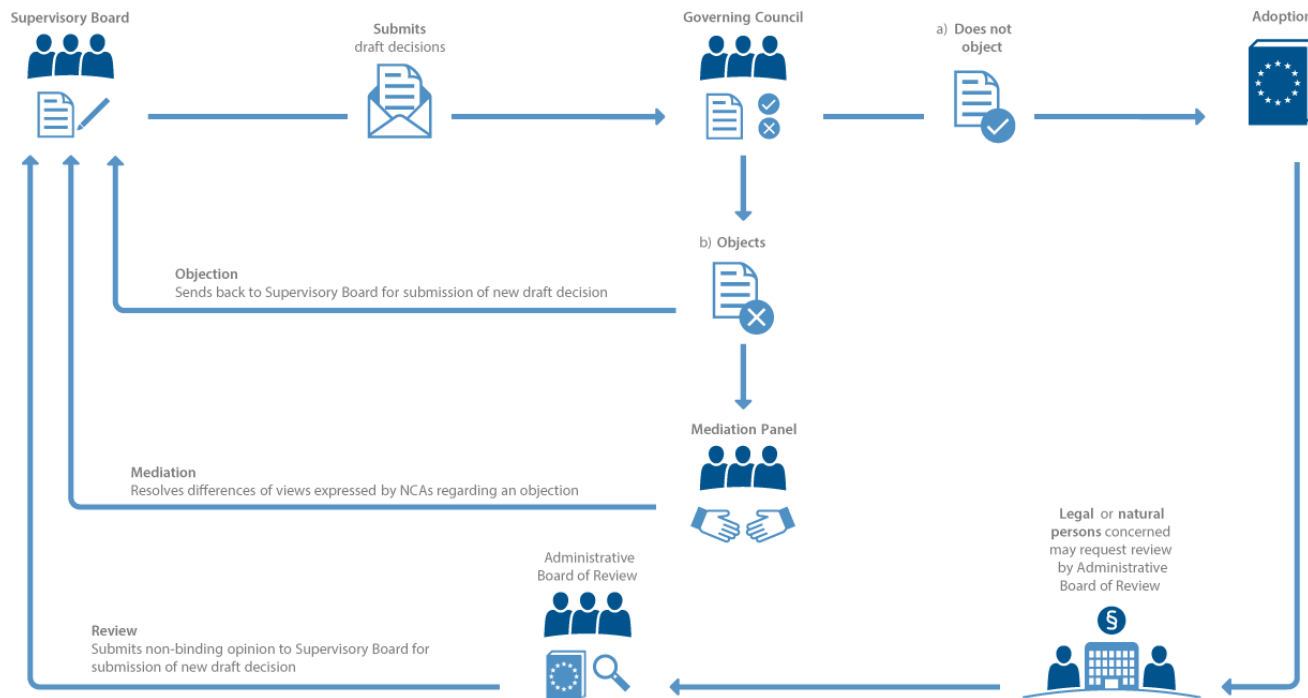
**Task:** prepares the draft decisions on supervisory decisions (e.g. on setting of micro-prudential capital requirements ("buffers"), significance, licensing, acquisition and disposal of qualifying holdings, imposing enforcement measures/sanctions

**Governing Council:** supreme decision making body also in supervisory issues

**Task:** adoption of draft decisions prepared by SB under the non-objection procedure



## VII. Decision-making on microprudential supervision



## **VII. Decision-making in the Eurosystem/ESCB**

### **General Council**

The General Council comprises the President of the ECB; the Vice-President of the ECB; the governors of the national central banks (NCBs) of the 28 EU Member States.

The other members of the ECB's Executive Board, the President of the EU Council and one member of the European Commission may attend the meetings of the General Council but do not have the right to vote.

## VII. Decision-making in the Eurosystem/ESCB

### Responsibilities

contribute to:

- the ECB's advisory functions;
- the collection of statistical information;
- the preparation of the ECB's annual report;
- the establishment of the necessary rules for standardising the accounting and reporting of operations undertaken by the NCBs;
- the taking of measures relating to the establishment of the key for the ECB's capital subscription other than those laid down in the Treaty;
- the laying-down of the conditions of employment of the members of staff of the ECB; and
- the necessary preparations for irrevocably fixing the exchange rates of the currencies of the "EU Member States with a derogation" against the euro.

! Dissolution once all EU Member States have adopted the euro

## VII. Role of National Central Banks ?

- Role in centralised decision-making
- Decentralised implementation of ESCB tasks (Article 12 ESCB/ECB Statute)
- Tasks:
  - **Execution of monetary policy operations**
  - **Management of own and ECB foreign reserves**
  - **Operation of payment systems**
  - **Oversight of financial market infrastructures and payment instruments**
  - **Management and supervision of euro cash operations**
  - **Assistance to the ECB in collecting statistics**
  - **Other national tasks provided they do not interfere with objectives and tasks of the ESCB (Article 14 ESCB and ECB Statutes)**

## VIII. Financial provisions of the Eurosystem/ESCB

### Chapter VI of the ESCB/ECB Statute

- National central banks (NCBs) are the sole subscribers to and holders of the ECB capital. (Non-euro-area NCBs contribute to operational costs (5% of their theoretical contribution)).
- Contribution of NCB to the capital of the ECB calculated pursuant to a key for capital subscription based on population and GDP.
- The initial capital was 5bn Euro but increased based on a decision of the Governing Council to 10bn
- Allocation of profits: Governing Council determines the amount (not exceeding 20% of the net profit) which shall be transferred to the general reserve fund (subject to limit equal to 100% of the capital) + remaining net profit distributed to NCBs



**Thank you for your  
attention !**