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COVER NOTE

from:	Jean-Claude TRICHET, President of the European Central Bank
date of receipt:	18 March 2011
to:	Mr Herman Van Rompuy, President of the European Council
Subject:	Opinion of the European Central Bank (ECB) on 17 March 2011 a draft European Council Decision amending Article 136 of the Treaty on the Functioning of the European Union with regard to a stability mechanism for Member States whose currency is the euro (CON/2011/24)

EUROPEAN CENTRAL BANK

EUROSYSTEM

Jean-Claude TRICHET
President

Mr Herman Van Rompuy
President
European Council
Rue de la Loi, 175
1048 Brussels

17 March 2011

Your reference: SG10 15920 – 2010/0821 (NLE)

ECB Opinion on a draft European Council Decision amending Article 136 of the Treaty on the Functioning of the European Union with regard to a stability mechanism for Member States whose currency is the euro (CON/2011/24)

Dear Mr Van Rompuy,

Further to your letter of 20 December 2010, please find enclosed the English version of the requested Opinion on a draft European Council Decision amending Article 136 of the Treaty on the Functioning of the European Union with regard to a stability mechanism for Member States whose currency is the euro, which was adopted by the ECB's Governing Council at its meeting on 17 March 2011. Copies of the Opinion in 21 other official languages of the European Union will follow.

The Opinion has been transmitted to the European Commission and European Parliament and will be published on the ECB's website and in the *Official Journal of the European Union*.

Yours sincerely,

Encl.

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EN

EUROPEAN CENTRAL BANK

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OPINION OF THE EUROPEAN CENTRAL BANK

of 17 March 2011

on a draft European Council Decision amending Article 136 of the Treaty on the Functioning of the European Union with regard to a stability mechanism for Member States whose currency is the euro

(CON/2011/24)

Introduction and legal basis

On 10 January 2011 the European Central Bank (ECB) received a request from the President of the European Council of the European Union for an opinion on a draft European Council Decision amending Article 136 of Treaty on the Functioning of the European Union (TFEU) with regard to a stability mechanism for Member States whose currency is the euro[1] (hereinafter the 'draft decision').

The ECB's competence to deliver an opinion is based on Article 48(6) of the Treaty on European Union. 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.

General observations

1. In a monetary union, strengthened fiscal and macroeconomic surveillance is the appropriate instrument to minimise risks of sovereign debt crises of the magnitude and severity that the European Union has experienced in the recent past. To this end, the ECB has called for a 'quantum leap' in the economic governance of economic and monetary union (EMU), which should lead towards a deeper economic union that is commensurate with the degree of economic integration and interdependency already achieved by the Member States whose currency is the euro. The ECB put forward its proposals for such 'quantum leap' in its communication 'Reinforcing economic governance in the euro area' of 10 June 2010 and has made concrete legal suggestions to this effect in ECB Opinion CON/2011/13 of 17 February 2011 on economic governance reform in the European Union[2].

1 See the conclusions of the European Council of 16 to 17 December 2010.

2 Not yet published in the Official Journal. See also the introductory statement of the ECB's President following the Governing Council's meeting of 4 November 2010.

2. To the extent that the risk of sovereign debt crises still remains relevant even under such strengthened fiscal and macroeconomic surveillance, and with the purpose of safeguarding the stability of the euro area as a whole, it is desirable to establish a permanent crisis management framework which can, as *ultima ratio*, provide temporary financial support to Member States whose currency is the euro experiencing impaired access to market financing. Such framework should be designed in a way that minimises moral hazard and reinforces incentives for pre-emptive fiscal and macroeconomic adjustment.

3. In the recent past, Member States whose currency is the euro have underlined their determination to take action to safeguard the stability of the euro area, and, for that purpose, they put together a package of bilateral loans to the Hellenic Republic and have established the European Financial Stability Facility (EFSF) as an intergovernmental euro area temporary facility to provide assistance to Member States in difficulty. The EFSF exists alongside the European Financial Stabilisation Mechanism (EFSM) of the European Union and, also like the loan package to the Hellenic Republic, its financing is subject to strict conditions negotiated between the Member State requiring assistance and the European Commission acting on behalf of the Member States whose currency is the euro, in liaison with the ECB, and the International Monetary Fund, and must be approved by the Member States whose currency is the euro providing assistance.

4. Against this background, and reiterating its call for the further strengthening of fiscal and macroeconomic surveillance in line with Opinion CON/2011/13, the ECB welcomes the draft decision. Following approval by all Member States of the draft decision a new Article 136(3) will feature in the TFEU. In accordance with it, Member States whose currency is the euro are expected to establish a permanent mechanism, known as European Stability Mechanism (ESM)[3]. The ESM is to be activated if it is indispensable to safeguard the stability of the euro area as a whole and temporary financial assistance may be granted under it only subject to strict conditions. The ESM will replace the current temporary arrangements of the EFSM and the EFSF, which will remain in force until June 2013 or until a date by which its activities have ended.

5. In addition, and even before its entry into force, the text of the new Article 136(3) TFEU helps to explain, and thereby confirms, the scope of Article 125 TFEU with respect to safeguarding the financial stability of the euro area as a whole, i.e. the activation of temporary financial assistance is in principle compatible with Article 125 TFEU provided that it is indispensable for such safeguarding and subject to strict conditions. Also, the new Article 136(3) TFEU does not increase the competences of the Union.

6. With respect to the exact design of the ESM, the necessary preparations are under way. There are four features that would enhance the effectiveness and facilitate the functioning of the ESM: (a) it should be established by means of a Treaty subject to international public law approved by the Member States whose currency is the euro so that national laws have to be made compatible with

3 See the Eurogroup Statement of 28 November 2010.

the provisions of the Treaty; (b) the rules for decision-making in the ESM should favour efficiency, for instance by providing for the activation of the ESM by mutual agreement of the Member States whose currency is the euro; (c) in full compliance with the Treaties, the ESM should be granted the capacity to employ an appropriate range of instruments in order to be able to effectively fight against contagion in situations of acute market instability; and (d) the ESM has to observe the principles of cautious and sound financial management and be subject to auditing by external and internal auditors.

7. In addition to these four features, there is a fundamental need for the ESM to be safeguarded against the moral hazard inherent in any crisis management mechanism. Safeguards such as IMF involvement in debt sustainability analysis, programme negotiations and financing, non-concessional terms consistent with IMF practice and regular and strict surveillance on compliance by the assisted Member States with the programme of fiscal and macroeconomic adjustment on which financial assistance is conditional, are indispensable for providing strong and lasting incentives for sound fiscal and economic policies in the Member States whose currency is the euro. Furthermore, such safeguards support the effectiveness of the abovementioned strengthened fiscal and macroeconomic surveillance framework of the Union.

8. A key element of the draft decision is that it provides for an intergovernmental mechanism instead of a Union mechanism. The ECB supports recourse to the Union method and would welcome that, with the benefit of the experience gained, the ESM would become a Union mechanism at an appropriate point in time. In the meantime, the ECB encourages that regarding the assessment of circumstances leading to the activation of the ESM and regarding conditions on financial assistance, Union institutions are granted a prominent role given their expertise and their focus on the collective Union interest.

9. With respect to the role of the ECB and the Eurosystem, while the ECB may act as fiscal agent for the ESM pursuant to Article 21.2 of the Statute of the European System of Central Banks and of the European Central Bank (hereinafter the 'Statute of the ESCB'), in the same way as under the Union's Medium-Term Financial Assistance Facility[4], the EFSM and the EFSF, Article 123 TFEU would not allow the ESM to become a counterparty of the Eurosystem under Article 18 of the Statute of the ESCB. On this latter element, the ECB recalls that the monetary financing prohibition in Article 123 TFEU is one of the basic pillars of the legal architecture of EMU[5] both for reasons of fiscal discipline of the Member States and in order to preserve the integrity of the single monetary policy as well as the independence of the ECB and the Eurosystem.

10. The ECB encourages Member States to approve the draft decision promptly in order for it to enter into force at the date provided in it, which is 1 January 2013.

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4 See the second sub-paragraph of point 1 of ECB Opinion CON/2009/37 of 20 April 2009 on a proposal for a Council Regulation amending Regulation (EC) No 332/2002 establishing a facility providing medium-term financial assistance for Member States' balances of payments (OJ C 106, 8.5.2009, p. 1).

5 See ECB Convergence Report, May 2010, p. 24.

11. The ECB recommends that the draft decision is amended on a legal technical point. A specific drafting proposal is set out in the Annex accompanied by explanatory text to this effect.

Done at Frankfurt am Main, 17 March 2011.

The President of the ECB

Jean-Claude TRICHET

Annex

Drafting proposal

Text proposed by the European Council	Amendment proposed by the ECB[6]
Amendment Article 2, second paragraph	
‘This Decision shall enter into force on 1 January 2013, provided that all the notifications …’.	‘**Article 1 of** this Decision shall enter into force on 1 January 2013, provided that all the notifications…’.
<u>*Explanation*</u> It is only Article 1 of the draft decision that will enter into force on 1 January 2013, in accordance with Article 48(6) of the EU Treaty, provided that the national approval process has been completed by that date, or on a later date following the completion of the national approval process. Article 2, which deals with the Member States’ obligation to notify completion of the respective national approval process, will enter into force, like the draft decision itself, in accordance with the second sub-paragraph of Article 297(2) TFEU (i.e. on the twentieth day following that of the publication of the Decision in the *Official Journal of the European Union* unless a date is specified in the draft decision), in the absence of a reference in Article 48(6) of the EU Treaty to the entry into force of this specific notification obligation.	

6 Bold in the body of the text indicates where the ECB proposes inserting new text.